June 2013

Operations Evaluation

Ex post evaluation of EIB Intermediated lending to SMEs in the EU, 2005-2011

"The evolution of a key operational priority"

Synthesis Report

Prepared by

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EVALUATION REPORT

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Edited March 2019

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NOTICE

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GLOSSARY OF TERMS AND ABBREVIATIONS

Absorption capacity	The ability to use approved funds in the timescale and manner envisaged
Allocation	The attribution of a share of a loan to a specific sub-project or beneficiary (of a Multi-Beneficiary Intermediated Loan)
Borrower	The legal persona with whom the Bank signs a Loan Agreement
Bp(s)	basis point(s) (one hundredth of one per cent interest)
CA	EIB's Board, The EIB Board of Directors
CD	EIB's Management Committee
CEE	Central and Eastern Europe
CEB	Council of Europe Development Bank
COP	Corporate Operational Plan
DAC (OECD)	Development Aid Committee (Organisation for Economic Co-operation and Development)
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECG	Evaluation Cooperation Group
EIA	Environmental Impact Assessment
EIB	European Investment Bank
EIRR	Economic Internal Rate of Return
ERDF	European Regional Development Fund
EU	European Union
EU12	The 12 New EU Member States since 2004
EU15	The 15 EU Member States before enlargement as of 2004
EU27	The 27 EU Member States
EV	EIB Operations Evaluation (Ex-Post)
FI	Financial Intermediary
FL	Framework Loan
FVA	Financial Value Added
GDP	Gross Domestic Product
GED	Gestion Électronique de Documents (Electronic Documents Management System)
GL	Global Loan
IL	Investment Loan
L4SME	Loan for SMEs
MBIL	Multi-Beneficiary Intermediated Loan
MLT	Medium to Long Term (referring to loan duration)
NMS	New Member States (EU12)
NPL	Non Performing Loan
OP	Operational Programme (EU)
Ops-A	EIB Directorate for Lending Operations – EU Members, Acceding, Accession and Candidate States
PCR	Project completion report
PJ	EIB Projects Directorate – responsible for ex-ante project techno-economic analyses, preparation of Technical Description, physical monitoring of implementation and completion
PPP	Public Private Partnership
PPR	Project Progress Report
Project	A clearly defined investment, typically in physical assets, e.g. a specific section of road, a bridge, etc.
Project Pipeline	Those projects which have been signalled to the Bank, but have either not yet been approved by the Management Committee, or have been approved but not yet signed. These include projects under active appraisal and those in the process of contract negotiation prior to signature.
Promoter	Normally the *body* responsible for identifying and developing a project. The promoter may also be responsible for operating and/or implementing the project.
RM	EIB Risk Management Directorate, responsible for credit appraisal / portfolio management
SERAPIS	The Bank's internal project IT system
SME	Small or Medium Sized enterprise (having up to 250 employees)
Sub-loan	Loan (here: to SMEs) extended by an FI under a loan (co-)financed by the EIB
TFEU	Treaty of the Functioning of the European Union
ToFA	Transfer of Financial Advantage
TA	Technical Assistance
VA(F)	Value Added (Framework)

EXECUTIVE SUMMARY

Introduction

SMEs are considered the backbone of the European Union's economy. According to the European Commission (EC), 99.8% of firms in the euro area are SMEs. Altogether, they account for 70% of employment in the private sector, making a significant contribution in terms of skills and job creation. SMEs are also considered a driving force of Europe's growth, accounting for 60% of its turnover, generating innovation and enhancing competitiveness. In addition, they are seen as a key factor of local and social integration.

This evaluation follows an explicit request by the EIB's Board of Directors in February 2010 for Operations Evaluation in due course to carry out an ex-post evaluation of the Bank's intermediated SME[1] lending that would (i) reflect on the implementation of the EIB's new strategies with regard to SME financing and (ii) provide insights into the benefits accruing to SMEs.

EIB Intermediated SME Lending 2005-2012

In this area, over 2005-2012, the EIB signed EUR 64bn in loans to around 370 FIs within the EU27. By end 2012, EUR 53bn of this was disbursed to those FIs, which in turn had on-lent nearly EUR 48 billion to SMEs through around 300 000 sub-loans (allocations).

Consequently, this evaluation was designed to capture the time frame from when SME support formally became a stand-alone key operational priority (2005) until end 2011. It thus includes the pivotal point in time, when in the context of the crisis response the EIB was requested at the Ecofin meeting in Nice (09/2008) to step up substantially its support to SMEs by mobilising a total of EUR 30bn to support European SMEs by 2011.

The Bank's response to the crisis that started in 2008 coincided with the introduction of a new product, the EIB's Loan for SMEs (L4SMEs). This evaluation therefore reflects on the strengths and weaknesses of this new tool to reach SMEs as much as it assesses the Bank's response to the evolving policy context.

Importantly, this evaluation concentrates on what amounts to more than 95% of the Bank's SME support, i.e. intermediated lending to SMEs through Financial Intermediaries (FIs). The evaluation does not consider smaller, less volume driven SME activities, where at times some SME related risk is assumed by the Bank (e.g. Risk-Sharing Initiative for SMEs). The activities of the European Investment Fund (EIF) are also outside the scope of the evaluation. EIF activity mostly focuses on SME support in the EU and amounts to slightly over EUR 2.5bn per annum, for equity and guarantee finance.

A sample of 20 individual operations in 11 Member States was selected, reviewed and were part of this evaluation. Through these operations, at the time of evaluation, some 15000 SMEs had been reached. Of these, 19 operations were evaluated in-depth. For one operation in Northern Italy, initially chosen for an in-depth evaluation, EV decided to cancel the on-site mission to the Financial Intermediary as well as the SME site visits, following the May 2012 earthquake that resulted in tragic losses of life and property in this region.

Responding to the explicit Board request, this evaluation also sheds a light on the beneficiary SMEs by two means, through 74 independently chosen SME site visits, and through a large scale survey executed by Gallup Europe across a statistically representative sample which was derived from the 15000 beneficiary SMEs of the sample.

1003 interviews were successfully completed through this SME Survey, which was designed i.a. to highlight the SMEs' characteristics, awareness of EIB funding and funding conditions. The SME Survey also attempted to illustrate the financings' contribution to the SMEs' growth and employment creation. The results are referenced throughout this synthesis report and need to be read in light of the entire evidence base of this evaluation, which includes *inter alia* the SME site visits and missions to the Financial Intermediaries.

This SME Survey is "a first" in the history of the EIB's lending support for SMEs. While EV maintained its independence all throughout its execution, this survey exercise is also an example of good cooperation with the Bank's services. Specifically, EV wishes to thank the Economics and the Operations Support

[1] For the EIB eligible entities are autonomous SMEs with less than full-time equivalent 250 employees prior to the investment.

Departments as well as the Central Allocation Unit and all the respective loan officers for their valuable contributions and the excellent co-operative spirit that made this survey possible in a time of financial turmoil across Europe.

Overall conclusion

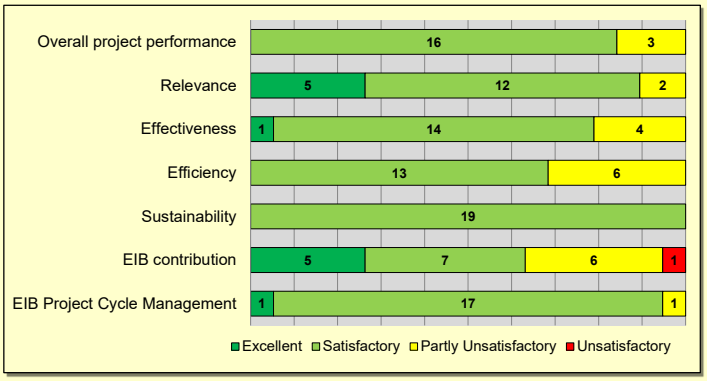
The evaluation shows EIB SME intermediated lending to be highly consistent with EU and EIB objectives and their evolution over time. The broad scope of the L4SME product made it relevant and increasingly so when access to finance for SMEs deteriorated across Europe as from 2008. Yet, the operations' relevance can still be improved if fine-tuned to national SMEs' funding needs. The complementarity of the EIB product within national policy mixes should be better assessed. This is especially important as the SME Survey showed country context to be the strongest predictor of the loans' impact on SMEs' competitiveness, growth and employment.

The L4SME product replaced the Global Loan product for SMEs. It was introduced when – by coincidence – the financial crisis started. The L4SMEs is effective: it says what it does, and does what it says. It allows the Bank, through contractual and reporting requirements and the definition of specific eligibility criteria, to better understand and control – and potentially better target or steer – the advantages transferred to SMEs and the types of SMEs financed. The L4SME is a major improvement in comparison to the former Global Loan approach for which it was unclear how much of the EIB advantage ultimately benefited SMEs and how much remained on the FIs' balance sheets. The contractual Transfer of Financial Advantage (ToFA) and more stringent transparency obligations have, as assessed by EV ex post, clearly contributed to providing a higher level of comfort that a financial advantage is indeed passed on to SMEs. Transparency is enhanced most notably by the detailed reporting on allocations to SMEs, by the publicity on the FIs' websites and the reference to the EIB in contracts with the SMEs. Such advantages were mainly interest rate rebates and, to a lesser extent, increased tenor – though a few FIs substantially increased tenor compared to their overall SME portfolio.

All Financial Intermediaries adhered to the principles and requirements of the new L4SME product. Most made, sometimes substantial, efforts to create e.g. a special EIB product, set up IT systems to track the SMEs benefiting from EIB funds, train front office staff and make publicity. In some cases the publicity for EIB funds was only 2 or 3 "clicks" away from an FI's homepage. In such cases the information on the EIB funding possibility is highly accessible for entrepreneurs. Also, SMEs have an "EIB" mention on their loan contracts. Over 40% of surveyed L4SME final beneficiaries were indeed aware that funding originates from the EIB – more than twice as many as for the GLs. The evaluation found clear evidence that visibility and transparency make a difference. The more extensive a FI's responsiveness to the EIB's visibility and transparency requirements, the higher the ex post level of comfort that ToFA is measurable and real.

FIs generally tend to choose comparatively larger and less risky SMEs to be financed under the EIB loan in comparison to their overall eligible SME portfolios. This effect is most pronounced in EU15 (old member states). The proportion of smaller and younger firms in the EIB portfolios financed by the FIs decreased over time. The proportion of SMEs surveyed for this evaluation stating that they received the full amount asked for remained relatively stable over time. Other SME access-to-finance surveys show that, with the crisis, SMEs generally obtain lower loan amounts than what they ask for. EIB's intermediated SME lending has a broad scope and, apart from a series of exclusion criteria, does generally not focus on specific types of SMEs in terms of size, sector or risk profile.

Overall ratings



The majority of the 19 operations evaluated in-depth were satisfactory. "Partly unsatisfactory" overall ratings were due in two cases to limited effectiveness and efficiency; in the third case it was due to partly unsatisfactory relevance and efficiency. For the latter operation time to disbursement and allocation time were extremely long due to initially low interest for the loan by the borrower and subsequently a very low absorption capacity. This was also the operation for which the EIB Contribution was low. EIB PCM was overall satisfactory.

Moreover, in these operations the EIB does not share SME risk, it promotes on-lending at relatively longer tenors and ToFA is settled in markets which are highly volatile. Finally, FIs prefer to have little or no losses on the EIB portfolio for reasons of reputational risk. Under such conditions, FIs prefer to choose comparatively larger and less risky SMEs. These can be either existing clients or come from other banks. The EIB loan thus induces competition between banks, which is viewed as positive. Ultimately, the different pieces of evidence converge to the conclusion that for a majority of operations SMEs were often also those that would have most likely obtained funding anyway, although probably on less favourable terms. EIB funding is thus in most cases not "gap funding" but rather used to support SME "champions".

During the period under review, the EIB loans had some impact on growth and employment, though great variations exist across countries. About half of the SMEs declared that turnover had grown after receiving the EIB funds, of which one-third attributed this entirely or partly to the funding. Also, half of the SMEs reported that the loan or lease had positive effects on productivity, market share or general economic health of their business. Yet, according to the SME Survey, on average about one job per financed SME was created. Furthermore, there is only limited evidence that the EIB loans helped maintaining employment – although for some operations, especially in countries where the crisis hit SMEs hardest, there is anecdotal evidence that the EIB loans helped keeping companies afloat. The relative impact on growth and employment was found to be higher in the New Member States. The economic impact of EIB lending was also found to be higher for small (10 to 49 employees), but not micro firms, and for relatively young (2 to 5 years), but not the youngest firms. Likewise, firms having introduced innovations or those that used the funds for research and development show a relatively higher impact. As the strongest predictor of the loans' impact on SMEs' growth and employment is the country context, it should be taken better into account in the design of new operations.

In sum, EIB intermediated SME lending does not primarily improve access to finance for those SMEs which are un- or underserved by banks due to their risk profile, except if operations are carried out within the framework of national programmes, implemented by, for instance, promotional banks. The L4SME is first of all a volume driven instrument with a broad scope and a wide reach, leaving to the FIs the types of SMEs to be targeted. It is standardised, working well and well under control. The Bank definitely needs such an instrument in order to be able to fulfil its increased SME lending targets over the coming years. Yet, the Bank should recognise that whereas this tool is fit to maximise lending volumes it does not necessarily maximise impact. Possibilities offered by the eligibility criteria to influence the targeting of final beneficiaries open opportunities for reflecting, in a longer term perspective, on how the L4SME product could also be mobilised to fill specific gaps instead of funding a broad spectrum of SMEs. This could then lead to optimising the EIB's contribution to growth and employment.

MANAGEMENT RESPONSE

1 Introduction and general context

The Bank's Management welcomes the Operational Evaluation (EV) report on EIB's intermediated lending to SMEs in the European Union (EU)[2], and in particular the core conclusion – that the Loan for SMEs 'says what it does, and does what it says'. The use of a survey of more than 1,000 SMEs that had received allocations of EIB funds represents an important element underpinning the report, and the results provide the EIB with a very insightful view on the actual impact of the EIB's SME lending through GL/L4SME.

The EV report covers the critical period 2005–2011 when the EU economies were hit by a severe financial crisis – that we are still experiencing – and when the EIB's main intermediated lending product serving SMEs was overhauled and streamlined from the Global Loan (GL) to the Loan for SMEs (L4SME)[3].

Following the call by the September 2008 ECOFIN summit for EIB to step up its SME activity in response to the unfolding financial crisis, the EIB Group followed a two-pronged strategy to support European SMEs:

- An immediate large-scale increase in funding available for on-lending to SMEs by financial intermediaries (FIs) over three years to provide EUR 30 billion between 2008 and the end of 2011; and
- Development of more targeted structures to address specific SME needs and market gaps.

The EV report recognises that the EIB deliberately chose an anti-crisis strategy between 2008 and 2011, focussing on quickly ensuring availability of SME finance at attractive conditions and long tenors through expanded L4SME activity. Such volume-driven support was only possible thanks to standardised rules across the EU that created widespread understanding of the product across the branch network of EIB's FIs and without which the EIB's funds would not have reached a comparable number of SMEs. In the meantime, the EIB Group developed and rolled out other, more specific products, targeting well defined SME and MidCap groups (e.g.: extended Risk Capital Mandate, Mezzanine Facility for Growth), also with the support of the EU (e.g. Risk Sharing Initiative for SMEs, European Progress Microfinance Facility).

The results presented in the EV report should be interpreted, and the EV proposed recommendations assessed, against the context outlined above. In particular:

(i) Recession period: The performance of the EIB intermediated lending activity as assessed by EV took place against the backdrop of a very difficult economic and financial environment, with falling employment and contracting bank lending to SMEs, significantly affecting the second half of the period considered.

(ii) Tightening of credit standards for SMEs by banks: Europe-wide surveys show that finance providers systematically tightened credit standards over the latter years of the evaluation period. The shift towards less risky borrowers is further reinforced by emerging tighter regulatory conditions. Evidence of a high proportion of EIB lending being allocated to more established SMEs by financial intermediaries should be seen in the context of this general trend across the market.

(iii) Structural change from GL to L4SME: Within the evaluation, a largely discontinued product for SMEs is compared with its successor. Average results recorded over the long period considered should therefore be carefully interpreted, as data related to L4SME in certain cases differ materially from the corresponding data for the GL.

(iv) Broader product offering for SMEs at Group level: The report focuses on the L4SMEs on a stand-alone basis. In reality, the L4SME is only one element of a wider and articulated

[2] The Evaluation Report examines all EIB intermediated lending operations with a full or partial SME eligibility in the European Union in the period 2005-2011, focusing on Global Loan and Loan for SME activity. The review also took account of activity in 2012.

[3] The EIB Board of Directors approved the modernised Loan for SMEs on 23rd September 2008. Lehman Brothers filed for bankruptcy on 15th September 2008.

product offering for SMEs at Group level, comprising a more volume-driven funding product (GL/L4SME) and more targeted guarantee, risk-sharing (blending with EU budget and Structural Funds) or risk-taking (equity/hybrid debt/equity) products. The L4SME product has not been designed "to do it all", i.e. to incorporate approaches tailored to specific market segments; on the contrary, it critically builds on a standardised framework that allows for maximum possible outreach and spread of the funding it provides.

2 Important role of the EIB Loan for SMEs in the context of its overall activities

The EV report identifies the role of the GL/L4SME as a high volume product serving the entire SME market. Signatures of EUR 12.1 billion in the EU and Candidate Countries in 2012 represented some 24% of EIB's EU signatures in 2012 and are a core EIB activity in the SME domain. The SME policy objective has been reinforced again in the current Corporate Operational Plan (COP), with sustained and increased levels of lending for SMEs targeted over the next three years (EUR 42 billion of signatures in EU and Candidate Countries in 2013-2015). The objective has also been endorsed by the EIB Board of Directors under the "Access to Finance" priority as central to the EIB's efforts to support European growth and employment following the capital increase. At the same time, intermediated SME lending has wider ramifications for the EIB: not least, it helps cement close links to the wide network of FIs with which EIB cooperates on other projects.

3 Continuous product improvement: From Global Loan to Loan for SMEs

The L4SME was developed with a broad scope, notably to make most SMEs and most categories of investment made by SMEs eligible for support. Ease of use by FIs, transparency and impact on SMEs, were also prime considerations[4]. The EV report charts the progressive evolution of EIB Group's offer between 2005 and 2011, for example through:

- The change from the 'project' focus of the GL to the wider L4SME approach that treats the SME as an economic entity;
- The enhancement of eligibility, incorporating the eligibility of working capital, enterprise transmission and purchase of second-hand assets;
- Improved communication of the role of EIB by FIs to SMEs;
- An improved, and more systematic, transfer of a part of the financial advantage (FVA) generated by EIB's involvement (ToFA) to SMEs.

These improvements are reflected in the reported increases in the value of SME loans signed, the number of allocations to SMEs, the level of SME awareness of EIB's role and of receiving a financial advantage, amongst other indicators.
The EIB has continued to improve the L4SME since the end of 2011 to maintain its relevance, also in line with some of the EV recommendations. In particular:

- Definition of an harmonised approach to setting the minimum ToFA introduced in January 2012, resulting in a more consistent proportion of FVA being transferred to SMEs;
- Updating the conditions covering re-use of funds repaid by SMEs, making the requirement that FIs re-use repaid funds more clear and consistent;
- Progressive harmonisation of contractual terms towards a 'final beneficiary' approach, ensuring that SMEs receive the same terms, regardless of the FI providing the sub-loan.

4 EIB intermediated lending to SMEs achieves the intended impact on the target group

<u>Support to growth and employment achieved in time of crisis.</u>
The Bank's Management takes note of the conclusion that the L4SME '[…] *had overall some impact on growth and employment* […]'. The Bank's Management considers however that the achievement of positive effects on annual turnover, productivity, market share development or general health of a business, as reported by approximately half of the SMEs, and increased employment, even marginally, in the SMEs supported - during a period of generalised recession and contracting employment, heavily affecting many SMEs - is in itself a significant accomplishment.

[4] Comments from FIs frequently identify that the Loan for SMEs is easier to administer than joint instruments incorporating EC funding, and this is borne out by the EV report which included one such instrument.

Support to the long term stability of companies.
According to the EV report, FIs have tended to apply a relatively large proportion of EIB SME finance to longer term sub-loans reaching more established SMEs[5]. EV finds that about 70% of surveyed SMEs benefited from tenors longer than 3 years[6]. This is consistent with internal analysis performed by the Bank. The Bank's Management considers this a very positive demonstration of the value of the L4SME product to SME at a time where risk aversion of FIs for SME lending has materially increased and propensity to longer-term lending decreased. While provision of longer tenors is an EIB requirement for FIs, the preference for more established SMEs reflects sound banking practice: since FIs retain the credit risk of the SME, they are more likely to use long term EIB funding for credit worthier clients. In addition, EIB security policy (requiring in some cases assignment of rights on the final beneficiaries) and the presence of transaction costs (mainly fixed costs) related to screening and monitoring activities would encourage FIs to favour more established and relatively larger clients.

The Bank's Management also questions the conclusion that EIB intermediated SME lending has limited impacts on overall access to finance of SMEs which are un- or underserved by banks: In reality, such riskier SMEs are served by the EIB Group through dedicated products, which (have to) incorporate risk-taking or risk-sharing elements (making recourse to EU funds) in order to provide adequate incentives to FIs to address such higher risk groups. In addition, it should also be noted that banks, as well as SMEs, are facing difficulties in raising finance, while higher credit losses, tighter capital adequacy regulations and liquidity rules are leading to an overall shrinking of SME lending portfolios of many FIs. The availability of EIB loans to dedicated SME lenders contributes to expanding the overall pool of financing; the funding stability associated to longer EIB tenors may help to maintain a significant number of enterprises and jobs in a context of difficult wholesale financing conditions. The Loan for SMEs is thus a vital counterweight to many of the broad market trends affecting SMEs. Given the generally acknowledged importance of SMEs for economic growth and employment (SME account for 70% of private sector employment in Europe), the funding provided by the L4SME – in addition to the dedicated EIB group products mentioned above - can certainly be seen, directly or indirectly, as contributor and stabilising element to maintain the going concern and stable growth of this important layer in the EU economy.

5 Smaller SMEs are appropriately served by the GL/L4SMEs

The EIB SME Objective includes all SMEs within the prevailing SME definition, i.e. up to 250 employees. However because of the large numbers of smaller SMEs, and the particular difficulties that they face in obtaining finance, smaller SMEs are an area of effort for the EIB. In this sense, with "*[…] over 80% of beneficiaries [being] firms with less than 50 employees*"[7], the GL/L4SME clearly reaches out in majority to the smaller segment of companies within the prevailing SME definition.

This is supported by available data: The 2012 average and median allocation to SMEs in the EU was EUR 124 000 and EUR 35 000 respectively. 2012 levels also indicate substantial reductions compared to 2011. In 2012 Operational Services made enhanced efforts with FIs working with smaller SMEs, and a higher proportion of funding was channelled through FIs providing leasing, which is often used by smaller SMEs. Operational Services continue to engage with FIs serving smaller SMEs, and in particular with smaller cooperative and regional banks, with a view to increasing the levels of EIB Loans for SMEs deployed through them. They also deepened relationships with national and regional development institutions.

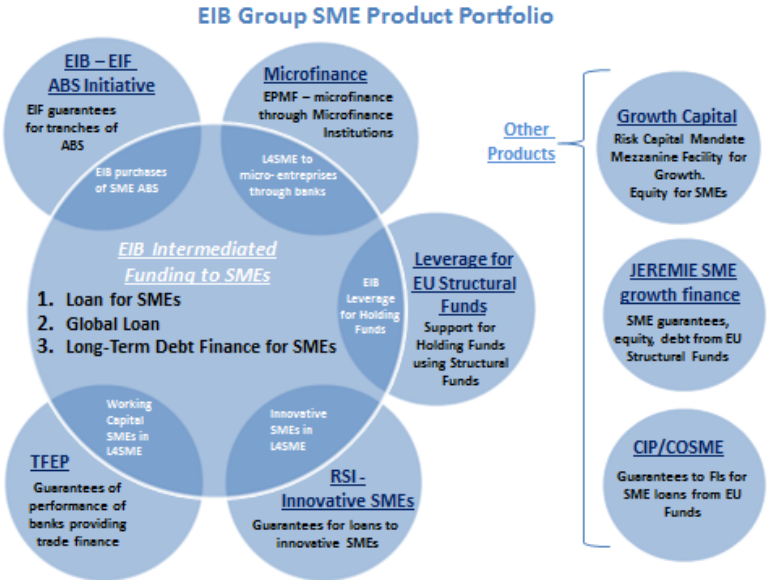
[5] EV recognises a possible survivor bias issue in such a survey (weaker SMEs may not have survived to be surveyed ex post).
[6] EV report, pg. 17
[7] EV report, pg. 15

6 EIB Group Portfolio of complementary products targeting SMEs

In parallel to the improvement of its main intermediated lending product, EIB - frequently in close cooperation with EIF - has developed products targeting specific niches since 2008. The EV report focuses on the GL and L4SME only. The comments on the detailed recommendations, and in particular those on 'smart targeting', should be read in the light of a much wider SME product portfolio of the EIB Group. In contrast to 2008, the EIB Group now deploys a wide range of products that address specific segments of the SME market through a wide range of intermediaries, including banks, guarantee institutions, investment funds and public promotional institutions. Thus, for example, innovative SMEs are addressed both by increased availability of private equity provided through RCM, and also through guarantees for debt under RSI. In the same way SME start-ups and micro entrepreneurs may be able to obtain conventional bank finance under L4SME, or if they are unable to do so, through microfinance institutions funded through EPMF.

In particular, the EIB group has stepped up its product development efforts in support of SMEs and currently offers the following additional products (shown schematically in the chart below, further details in the Annex):

- The extended Risk Capital Mandate (RCM) and Mezzanine Facility for Growth (MFG);
- JEREMIE instruments using Structural Funds to target specific categories of SMEs;
- The CIP/COSME guarantee schemes for SME lending;
- The L4SME used as complement to Structural Funds for SME growth;
- The European PROGRESS Microfinance Facility (EPMF);
- The Risk-Sharing Initiative for SMEs (RSI);
- The joint EIB – EIF initiative to support SME-backed ABS;
- The Trade Finance Enhancement programme (TFEP);
- The SME Guarantee Fund for Greece.



These products target different segments of SMEs, with different products (guarantees, risk sharing, equity, hybrid instruments) to a diverse range of intermediaries (VC and mezzanine funds, banks, promotional institutions, guarantee institutions, leasing companies, microfinance institutions, specialised micro banks etc.).

In contrast to the GL/L4SME, many of these products require an element of external public support to provide FIs with elements of risk sharing, balance sheet/profit and loss protection and compensation for higher costs of implementation (related to new product design, new internal procedures, tailored reporting and compliance requirements that go along with heightened accountability to public fund providers). For these same reasons, development of such structured activities is also most efficient when they can be adapted to serve more than one market or provide for portfolio diversification effects at European level, albeit tailored to national market needs.

7 Promoting the development of EU SMEs in line with national/local priorities

Given the continued situation of financing shortages for SMEs, the EIB will continue to focus on anti-crisis measures, while developing further targeted initiatives required to sustain long term growth and innovation and create employment. In particular, the EIB remains ready to develop specific SME support initiatives in collaboration with local players in agreement with national authorities. This has been the case in Greece, where two new SME-dedicated products have been recently launched (Trade Finance and SME Guarantee Fund).

While the EV report suggests to work more through national promotional banks, the possible use of the L4SME product may be limited in those cases where EIB's intervention may be perceived as competing to the local offer and/or where risk sharing schemes would be more attractive than a funded product providing a marginal or no financial advantage compared to other funding sources. Operational Services have recently embarked on a general country-related policy research and operational planning exercise that has allowed for better identification of gaps and tailored responses. Operational Services intend to lead this exercise into the future (also considering the SME-specific market research already conducted by the EIF), allowing for a synergetic product portfolio and adapted choice of product for each intermediary.

8 Conclusions and comments on recommendations

The EIB welcomes many of the conclusions of the EV report (see detailed comments), and in particular:

- The role of the L4SME in fulfilling increased SME lending targets;
- Improvement in the outreach and attractiveness of the L4SME compared to the GL;
- Recognition that the L4SME, and EIB's SME financing in general, must balance broad provision of finance to SMEs against access to finance for particular SME types;
- Increased awareness of the role of EIB amongst final beneficiaries, a major impact of the L4SME;
- More effective transfer of benefit to SMEs through the L4SME.

The EIB equally welcomes the following EV recommendations:

- Regular reviews of the benefits passed on to SMEs;
- Further increasing the transparency of EIB's role through enhanced transfer of information;
- Further evolving the role of the Central Allocation Unit to support Loan Officers and ensure a good understanding of the product by the FIs;
- The replacement of the term "additionality" by a more appropriate term;
- The usefulness of country needs assessments for product development.

With respect to the EV recommendations to start pilot projects, the Bank Management sees only limited room in the current circumstances to develop pilot schemes under the L4SME product, given the need to maintain highly standardized features. In parallel, other pilots outside L4SME are regularly being developed.

The EIB agrees to EV's recommendation that the EIB Group's support to SMEs has to be constantly evaluated against its impact on growth and employment for SMEs as a whole and its impact on specific sub-segments. This balance determines the relative importance that EIB will be able to give to anti-crisis (volume driven) and long-term growth (impact driven) measures, within the overall SME objective. It is proposed that this balance is continued to be reviewed over time, according to macroeconomic and COP developments.

Annex to Management Response

Summary of EIB Group targeted products serving SMEs

- The ***Risk Capital Mandate (RCM)*** and ***Mezzanine Facility for Growth (MFG),*** managed by EIF, for investment in private equity funds targeting SMEs across all stages from technology transfer and start-up to later stage growth. EIB recognises that long term equity may be essential in securing growth for some SMEs, and deploys EUR 7 billion through RCM/MFG.
- A range of ***JEREMIE instruments*** supporting SMEs, deployed by EIF on behalf of the EC, that use Structural Funds to target specific categories of SMEs such as recent start-ups and smaller SMEs through loans and guarantees. JEREMIE also supports SME development through investment in SME equity funds. JEREMIE investments draw on extensive country by country 'gap analyses' to ensure that they primarily serve activities unserved, or underserved, by the market;
- The ***CIP/COSME*** guarantee schemes for SME lending, supported by EC funds, aim to increase FI appetite for SME funding by absorbing a part of the associated risk;
- The ***L4SME used to increase the impact of Structural Funds for SME growth*** by investing into Holding Fund structures that use the EC funds as a junior (first loss) investment and the EIB funds to enhance their impact. The associated Holding Funds made a wide range of equity, debt and quasi-equity investments;
- The ***European PROGRESS Microfinance Facility (EPMF)***[8]***,*** financed by EIB and the EC to specifically target microfinance for micro entrepreneurs facing exclusion from the conventional banking system [9]. EPMF therefore directly compliments the smaller allocations to more 'bankable' small SMEs made by FIs under the L4SME;
- *The* ***Risk-Sharing Initiative for SMEs (RSI),*** that guarantees part of the risk of sub-loans made by FIs to innovative SMEs, and so actively encourages banks to lend more to innovative enterprises. RSI is financed by the European Commission (EC). EIB and EIF work closely to combine RSI with allocations of L4SME to SMEs that meet RSI's specific innovation criteria;
- The ***joint EIB – EIF initiative to support SME-backed ABS*** combines long term liquidity provided by EIB and EIF`s longstanding market experience of providing guarantees for portfolios of SME lending, as part of wider EIB Group initiatives to help restart the SME-backed ABS market. EIB would purchase senior tranches of SME-backed ABS, while EIF would guarantee other tranches of the same ABS, making them more attractive to market purchasers.
- *The* ***Trade Finance Enhancement programme (TFEP)*** for selected crisis countries, responding to a specific market failure in the provision of trade finance for SMEs (in addition to working capital financing under the L4SME);
- The ***SME Guarantee Fund for Greece*** created a dedicated guarantee fund supporting lending to SMEs in Greece in 2012. EUR 500 million from unabsorbed Structural Funds earmarked for Greece were made available by the Hellenic Republic and the European Commission to guarantee EIB loans for SMEs totalling up to EUR 1 billion.

[8] EPMF comprises a joint EIB-EC investment fund providing funding to Microfinance Institutions (MFIs) for on-lending as microloans, and an EC-funded microloan guarantee scheme.
[9] Microfinance comprises microloans of less than EUR 25 000 to microenterprises with fewer than 10 employees.

TABLE OF RECOMMENDATIONS AND REPLIES

The following recommendations are made against the background that presently EIB intermediated SME lending, on the basis of the L4SME product, **is overall effective**. This is viewed positively, especially given the strongly increased SME lending target over the coming three years. The evaluation findings provide guidance on how the lessons learnt from the experience with the L4SMEs can be used to optimise the Bank's contribution to economic growth and employment objectives.

The table below contains recommendation summaries. These are an abridged version of the more comprehensive version found in Section 12.2 ("Recommendations") of this report.

STRATEGY

R1 Clarify the objectives of intermediated SME lending

By extending finance to eligible SMEs the Bank aims at providing finance at improved conditions as well as improving access to finance. Eventually, the goal is to enhance the competitiveness of SMEs and ultimately generate a positive impact on economic growth and employment. The evaluation found that the Bank – through its intermediated SME lending – is indeed providing finance at improved conditions to eligible SMEs. However, it contributes less to providing access to finance for SMEs that would otherwise not have obtained such finance. Depending on how those objectives and their relation to the ultimate objectives are interpreted, they may not necessarily be consistent with each other, or difficult to pursue in parallel. Moreover, although overall EIB SME intermediated lending did certainly contribute to growth and employment, the evaluation found that the comparatively larger and less risky SMEs most served by the loans were not necessarily those contributing *most* to the growth and employment objective. Furthermore, it is not clear that aiming at providing access to finance to un- or underserved SMEs would necessarily maximise the Bank's impact on growth and employment.

In order for the Bank to clarify *how* its action contributes to the global EU objectives of growth and employment, it is recommended to define more precisely the objectives for intermediated SME lending and how they relate to each other. A narrative should also be made more explicit on how the objectives of improving funding conditions and/or improving access to finance are expected to contribute to the ultimate objectives of economic growth and employment.

Management Response

There is consensus that the objective of EIB SME financing as a whole is to encourage SME growth and employment, and that one of the mechanisms to achieve this objective is to enhance the competitiveness of SMEs by ensuring wide access to finance. The EV study concludes that the L4SME is a valuable instrument to make this mechanism work. EV's view is, however, that the volume-driven L4SME with its current, broad eligibility and application, might have lower levels of impact than more targeted schemes could have.

The Services note that, in order to clarify the objectives of SME intermediated lending, it is important to take a wider perspective than just the L4SME product: in fact, the EIB Group provides a large and diversified range of products to finance SMEs:

a) on the one hand it provides broadly applicable and volume driven products in the form of L4SME (funding the SME lending activities of FI) and EIF portfolio guarantees (providing risk relief for FIs to foster additional SME lending); on the other hand, the EIB Group offers tailored, smaller scale and often higher risk schemes for specific needs (such as RSI for innovative SMEs, EPMF for microenterprises reaching out to vulnerable groups and national schemes focusing on growth stimulation in a particular country context - such as the SME Guarantee Fund and the Trade Finance Enhancement Programme ("TFEP") in Greece).

Particularly in the last few years, EIB deliberately used the L4SME product to respond to explicit calls from its stakeholders to provide significant additional volumes of finance for SMEs, while in parallel improving the benefits for SMEs. The priorities set with the recent capital increase (and approved by the Board of Directors) entailed yet another rise in SME lending targets for 2013-15, to EUR 14 bn p.a., as well as those for more targeted instruments such as RSI. Opportunities to develop further targeted products complementing the L4SME are actively pursued, including jointly

with the EIF (see R2, R3). The L4SME should thus not be seen in isolation, but in the context of the whole product offering of the EIB Group.

The Services agree that the product mix and relevant objectives should regularly be validated against evolving market needs and the Bank's Operational Plan as endorsed by the EU Member States (EIB Shareholders). They however consider that the overall product mix offered by EIB Group is viable, and adequate to achieve the highest possible impact on growth and employment in the current context.

b) With regard to EV´s estimate (through the SME Survey) of a relatively low impact of L4SMEs on growth and employment, Services believe that the result has been affected by the crisis period surveyed. The relatively modest new job creation estimated by Gallup should be evaluated in such context of generally falling employment levels. In this context, it should also be noted that methodologies to ascertain employment effects are generally fraught with uncertainties as to causality, secondary effects and relevant benchmarks. Additional evidence of positive growth and employment impact can be seen in the fact that "*Roughly half of the SMEs surveyed reported that their annual turnover had increased* […]"[10] and "*Nearly half of the SMEs reported […] positive effects on productivity, market share development or the general economic health of their business*", which should increase their competitiveness and therefore growth prospects.

c) With regard to EV´s finding that the L4SME has reached "larger" and "less risky" companies, Services note that:

- In line with good banking and risk management practice, FIs tend to extend loans at the longer tenors requested by the Bank to SMEs considered creditworthy for such tenors. These are naturally more mature and stable companies.
- Nonetheless, as reported by EV, more than 80% of SMEs reached were companies with less than 50 employees. Given that the SME definition includes enterprises with up to 250 employees, the L4SME demonstrably reaches out to the smaller segment of the SME universe. This is further supported by the low average and median allocation sizes of EIB L4SME in the EU (approx. EUR 124,000/EUR 206,000 and EUR 35,000/EUR 40,000, respectively in 2012/2011).

R2 Adjust EIB Group product offering better to national needs and policy mixes

The evaluation identified a fairly consistent lack of *ex ante* SME needs assessments at the national level. Where such assessments did exist, both effectiveness and efficiency of the operations were noticeably better. Moreover, in the SME Survey country context appears the strongest predictor of impact.

The EIB should optimise its intermediated SME lending by adjusting better to local circumstances at Member State level. In the future, beyond the volume driven targets, this could allow the Bank to optimise its impact in view of its objectives.

The Bank should therefore engage in:

(a) a periodic SME country needs assessment to determine how EIB intermediated SME lending can best achieve its objectives. The competent services across EIB departments (ECON, PJ, Ops) could be involved in those assessments;

(b) launching the follow-up of the SME Consultation (as initially foreseen) with all relevant stakeholders, including, beyond the FIs, other DFIs/IFIs, SME associations, etc.;

(c) reflecting in the appraisal process how a proposed L4SME operation responds to the SME country needs assessment, how it addresses identified SME needs and how it is complementary to other SME products available in the country or offered by the EIB Group.

Management Response

The L4SME product is built on the recognition of a general and persisting gap in access to finance for SMEs. EV confirms that this generic market failure is a continuing political priority, both at EU and national levels. EV also recognises that the crisis has further strengthened the general intervention logic to generally support access to finance to SME. The L4SME serves this purpose based on its wide eligibility and its availability across all European countries. The standardised features of the L4SME allow for very limited tailoring to fit particular country-related situations or narrow target groups. Such tailoring is achieved, instead, by specific products, occasionally borrowing certain features of the L4SME product. A recent example of such a country-specific solution is the TFEP for Greece.

Ad (a)

The Services agree that country-focused product development benefits from in-depth periodic assessment of national markets, in particular at times of diverging European economies. For this reason, EIB Group services have recently embarked on more systematic policy and country research and operational planning for lending to allow for a better informed match of operational solutions with national priorities. Operations Directorate supports the further evolution of this useful exercise in cooperation with other relevant EIB services, and in particular with EIF Research & Market Analysis (RMA), that has been conducting SME-specific market research over many years[11].

Ad (b)

In addition to the above, Operational Services maintain a continuing close dialogue with stakeholder organisations representing FIs and SMEs. Against this backdrop, it is not clear that a formal, repeat 'SME Consultation' would produce net positive impacts – particularly when taking into consideration that such an exercise would imply a significant resource commitment by the Bank at a time where ambitious lending targets have to be fulfilled. Operational Services consider that at this stage recommendation 2(b) is better met by the range of continuing internal and external activities and dialogues, rather than another formal consultation. A repeat of the 'SME Consultation' may possibly be considered again in a few years' time, following the capital increase business plan cycle.

Ad (c)

The newly introduced 3 Pillar framework includes the assessment of the "economic interest" of an MBIL, that considers the strategic intent of the operation and its response to market needs. The landscape of SME products available in a given market and possible fit of EIB Group products will continue to be analysed in the context of future regular country needs assessment, operational planning and product development activities.

R3 Prepare for smart targeting

The L4SMEs is an effective volume instrument which currently does not aim at more precise targeting in view of e.g. countries' specific SME finance needs or achieving higher relative growth and employment results.

Given the Bank's recent capital increase and the corresponding increase in SME lending targets it is expected that intermediated SME lending should continue to be volume driven in the short term. Yet, the Bank could also with the L4SME be able to increase its added value through the use of more focussed eligibility criteria. In order to gain experience with such "smart targeting" in view of the needs of specific SME groups, it is recommended that the Bank set up a pilot for a small volume to be determined. This envelope should allow the Bank to experiment to target specific SME groups in view of the Bank's objectives of growth and employment, following the exercise of an SME country needs assessment.
The pilot should result in an assessment of the feasibility and conditions of more targeted intermediated SME lending, and an action plan in case feasibility is proven. It should be set up in conjunction with the recommendations R1 and R2.

[11] Inter alia a regular publication "European Small Business Finance Outlook" and thematic analyses e.g. on microfinance, leasing, securitisation, business angel financing etc.

Management Response

A wide range of targeted instruments have been developed by EIB Group in parallel to the L4SME since 2009 (see Management Response for an overview). These complement the 'volume'-driven L4SME by addressing specific market gaps identified in the SME market where policy benefits can be maximised through 'smart targeting'. Operations Directorate will maintain this dual approach, strengthening cooperation with EIF wherever possible (e.g. through joint RSI and ABS transactions).

The scope for variation and diversification of the L4SME product is limited. Frequent changes to or greater diversification of the product framework through specific ´targeting´ to more restrictive and riskier sub-categories of SMEs would have adverse effects:

- The Bank would not be able to continue to reach a broad range of SMEs, reducing the potential global volume impact under its SME access to finance objective;
- It would lead to a less clear positioning of the L4SME product, and create confusion and possible disruptions at FI level;
- It could increase the administrative burden on FIs and skew the incentive balance on which the product is currently built;
- It may require financial or other incentives to FIs well beyond the portion of FVA currently left with them. This would be difficult, particularly in areas where EIB's competitiveness is already under pressure ;
- Developing targeted instruments is generally much more resource-intensive than the L4SME, making wide replicability or portfolio effects (prerequisites for efficiency and impact) difficult to achieve;
- It would make reporting on the impact achieved by L4SME even more complex (see also R9).

In light of the above, setting up proposed pilot schemes under the L4SME - in addition to the current development of more targeted non-L4SME products - does not appear appropriate in the current high lending volume context. The Services would like to re-state that pilots are being regularly developed at the level of the EIB Group (see list of examples annexed to the Management Response), drawing also from the experience and the approach of the L4SME product, where appropriate.

R4 Additionality: in order to avoid confusion, choose a more appropriate term

As an economic concept, "additionality" generally refers to the assessment of whether an investment would have taken place without a given (public) intervention. It assesses the effect of the intervention compared to a baseline or a situation "without" it. If an intervention does not substitute for existing activities (in the present case, for existing finance) it is considered "additional".

For L4SMEs, the Bank asks the FI for a formal confirmation that the volume of its SME financing - in line with EIB eligibilities and with a term of more than 2 years - signed during the Allocation Period of the EIB loan and financed with *non*-EIB resources has been at least as much as that of the EIB Loan for SMEs. This is referred to as the "additionality" requirement. This requirement is an interpretation of the Bank's statute (Art. 16 (2)), which states that, as far as possible, loans shall be granted only on condition that other sources of finance are also used. In the case of Investment Loans, Framework Loans and Global Loans, the Bank therefore generally does not finance more than 50% of total project cost. In the case of the L4SME product, where financing of up to 100% of the loan granted by the intermediary to the SME is allowed, the "two times EIB lending rule" was introduced to mimic the statutory requirement while simplifying the administration of the L4SME over the Global Loan.

This "additionality" requirement, as per the Bank's terminology, is in fact a matching requirement. It controls for whether the FI can show the same volume of similar SME lending and ultimately for whether the FI's SME portfolio is not financed by the EIB only. It is therefore a relevant requirement to respond to the EIB Statute and in line with good banking practice more generally. However, it

provides no assurance that EIB lending led to additional lending compared to the FI's normal lending pattern.

In order to avoid confusion it is recommended to replace "additionality" in the contractual documentation by a more appropriate term, e.g. "complementarity" or "matching".

Management Response

The recommendation to replace the term "additionality" in the contractual documentation by a more appropriate term (e.g. "complementarity") is accepted and will be taken into account in the next update of templates used, reflecting the common approach for other EIB lending products.

Concerning the assurance that EIB lending leads to additional lending compared to the FI's normal lending pattern, the Operational Services:

- Recall that the estimation of catalysis (additional induced lending) is a complex and academic exercise and causalities are difficult to ascertain.
- Also recall that a loan product (like the L4SMEs) generally provides for limited leverage potential. This can be better achieved through higher risk products (such as equity fund investments), or guarantee/risk sharing products (with higher risk and capital consumption).
- Highlight that in order to seek such assurance additional obligations and reporting requirements for FIs would have to be established, with corresponding higher costs for the counterparts. This would not be compatible with the need to maintain a streamlined L4SME product.

R5 Optimise the benefits passed on to SMEs

The underlying conditions between 'lending' and 'on-lending' define the critical nexus of how the Bank ultimately reaches out to SMEs. In particular in the current crisis context and its high market volatility, it is of great relevance how much of the overall EIB benefits should reasonably reside with the FIs (Financial Value Added - FVA) and how much of it and in what form should be passed on to SMEs using the L4SME vehicle (Transfer of Funding Advantage – ToFA). EV's ex post assessment of this critical nexus identified the following recommendations:

a) It is recommended that the Bank undertake a regular internal review of the actual benefits passed on to SMEs in order to optimise and possibly maximise them. Beyond elements of price this should also include other financial benefits, especially tenor. This review should be performed at least on an annual basis and should be informed *inter alia* by an analysis that takes into account contractual ToFA relative to the actual (reported) ToFA. Such analysis should be performed for *a representative sample* of operations. It should inform the future decisions about the level of FVA and ToFA, in view of optimising and possibly maximising the benefits passed on to SMEs.

b) It is recommended that the Bank undertake a review of the underlying principles on the topics of reuse of funds and maturity mismatch, and following that a clarification of the related contractual clauses and a better enforcement of such clauses.

Together, these recommendations would more clearly delineate the critical inputs in the relationship between 'lending' and 'on-lending' and further enhance transparency of the EIB-FI-SME relationship for the Bank's services.

Management Response

Ad (a)

In September 2011, following a review and consultation with representatives of EIB's FIs, the Management Committee put in place a harmonised approach to setting minimum ToFA (to be transferred by FIs). Following such development, the Operational Services have analysed the benefits passed on to SMEs and recorded an increase in the average level of ToFA committed at contract signature stage. The EV recommendation to review, at the Operational Services level, the benefits passed to SME beneficiaries by taking into account the contractual ToFA and the actual ToFA transferred to SMEs as reported by FIs on a representative sample is considered appropriate. Such analysis can be repeated on a regular basis, in order to assess the ongoing effects of the 2011

harmonisation and decide on possible adjustments to optimise the benefits passed on to SMEs, if needed.

The EV Report recognises that ToFA is a significant outcome of the L4SMEs, although it is not the only one: availability of loan financing as such and longer tenors are also important advantages for SMEs. In parallel, the EIB would therefore continue efforts to monitor and optimise other value-adding elements, such as longer tenors as per the revised value added methodology (3 Pillar Assessment).

Ad (b)

The recommendation has been addressed through a revision of the contractual provisions for Multi-Beneficiary Intermediated Loans which will be implemented shortly.

OPERATIONAL

R6 Promote visibility and transparency even more

The evaluation found clear evidence that visibility and transparency make a difference. The more extensive an FI's responsiveness to the EIB's transparency and visibility requirements, the higher the *ex post* level of comfort that ToFA was measurable and real.

It is recommended that the Bank

(a) require from FIs to use, *simultaneously*, multiple ways of communicating to SMEs the EIB involvement, rather than giving FIs the choice. Development of a dedicated EIB product should in all cases be encouraged in discussing a new operation with an FI;

(b) in its due diligence of FIs present a comprehensive review of how a proposed FI undertakes to pass on the advantages to SMEs. This should include highlighting the FIs internal links between their treasury and their operational (front office) side (e.g. pricing policy / pricing models);

(c) through COM reach out directly to SMEs with publicity on the possibilities offered with EIB funding.

Management Response

Operations Directorate agrees with the importance that SMEs become aware of the role of EIB in SME lending, and welcomes the improvement recorded in the SME Survey results. It will endeavour to further enhance visibility and transparency, along the lines of the recommendations made, in cooperation with the relevant Services.

R7 Assess clients' adherence to environmental and social regulations

With respect to national and EU environmental and social regulations, no specific checks are carried out by the Bank at the SME level, other than a presumption of reliance on the ultimate borrowers' compliance with a clause in the sub-loan agreements.

During the appraisal the EIB should review and document the FIs processes and procedures with respect to assessing their clients' adherence to national and EU environmental and social regulations and assess whether such reliance is sufficient for the Bank.

Management Response

The EV study covers EIB lending for SMEs within the European Union. All EU Member States have transposed the EIA Directive and adhere to the most advanced social standards. EIB's standard Finance Contract for GLs and L4SMEs requires FIs to ensure that SME final beneficiaries certify their compliance with all EU and national laws and regulations, and not only those covering environmental and social issues. A reference to EIB's Statement of Environmental and Social Principles and Standards will also be included in the Side Letter, which forms part of the contractual documentation. The eligibility of individual allocations to SMEs is assessed against a sector list (NACE Code) which excludes activities which are sensitive according to Annex 1 or Annex 2 of the EIA Directive.

There is no evidence of repeated non-compliance with national or EU environmental and social regulations by L4SME beneficiaries. The appraisal process already includes a review of all FI processes and procedures, particularly for new counterparts. Operational Services consider that the current approach provides an appropriate assurance and balance between the need to avoid inappropriate on-lending and minimising the cost and burden of reporting born by FIs and Final Beneficiaries.

R8 Reinforce CAU's role

The establishment of the Central Allocation Unit (CAU) at the EIB is viewed as an appropriate and pro-active response to the policy demands directed at the Bank. The CAU can provide a valuable contribution to the *timeliness* of the Bank's outreach to SMEs through an efficient handling of the allocation process. In many instances the efficiency of this process could have been enhanced by an *earlier* involvement of CAU (and where applicable PJ), in the operational process.

The role of CAU should be reinforced. Because loan officers are increasingly de-coupled from the allocation process *per se* (now handled by CAU), CAU (and where necessary PJ), with their detailed knowledge of the application of the EIB's eligibility criteria should be involved *in situ* at the inception of an operation to explain better the Bank's eligibility modalities.

Management Response

Operations Directorate agrees that the role of CAU can be reinforced.

CAU was created in 2010 to centralise and increase consistency and efficiency of processing of allocation requests from FIs. It has since evolved into a dual role, as it is now also responsible for an increasing number of monitoring functions (ensuring that commitments on transparency and transfer of benefit are met, producing End of Allocation Reports, etc.). Very close client contact is necessary to perform both functions, and occasional accompanying operational staff on client visits during the appraisal process, where useful, has indeed proven to be beneficial to the overall success of the relevant transactions. Strengthened CAU involvement in "front office" aspects of the operational process, together with new monitoring tasks potentially arising from the implementation of recommendations made herein, would have to be assessed in light of available resources.

R9 Improve internal and external SME reporting

The *ex post* data collection for this evaluation's portfolio review highlighted a number of issues regarding the aggregation and reporting on the Bank's SME intervention. In particular, the aggregation of individual SME related data to a portfolio of SMEs is cumbersome, if not at times misleading. One example: the published number of individual SMEs the Bank reaches out to corresponds in reality to the number of SME *allocations*. As one SME can have several allocations, the number systematically overestimates the number of individual SMEs reached.

The EIB should review how individual SME related data is captured and then aggregated in its IT systems to report on the Bank's SME activities. Based on internal and external reporting needs the Bank should then improve on the currently available tools.

Management Response

One objective of the L4SME was to minimise the reporting burden placed on FIs. EIB has made significant progress since introduction of the L4SME in the volume and quality of data recorded by the Bank, and in the internal performance tools used to monitor activities.

Operations Directorate takes note that the recording of numbers of allocations reaching SMEs may at times overstate the number of individual entities reached. This would affect the implied breadth, although not the depth, of the impact of EIB's L4SME support. Further refinement of statistics on SME lending is challenging due to the high number of allocations involved (almost 80,000 in 2012) and the complexity of the Bank's reporting systems. Nonetheless, Operations Directorate will seek to further develop its reporting tools, in order ensure that reporting is relevant for different external and internal audiences, while continuing to keep the reporting obligations on FIs and SMEs at acceptable levels.

1 INTRODUCTION

1.1 Background

SMEs are considered the backbone of the European Union's economy. According to the European Commission (EC), 99.8% of firms in the euro area are SMEs. Altogether, they account for 70% of employment in the private sector, making a significant contribution in terms of skills and job creation. SMEs are also considered a driving force of Europe's growth, accounting for 60% of its turnover, generating innovation and enhancing competitiveness. In addition, they are seen as a key factor of local and social integration.

SMEs have specific access to finance needs. A recent Eurostat survey confirmed that loans remain the most important type of finance sought by SMEs – a trend that is expected to continue. Meeting SMEs' funding needs by providing and/or improving their access to finance contributes to support their competitiveness and growth potential. According to a broad counterfactual study recently finalised by DG REGIO, loans would be more effective in this regard than grant funding. Ensuring access to finance for SMEs is even more important during a financial crisis, when the liquidity squeeze makes it harder to obtain loans. Again according to Eurostat, between 2007 and 2010 there was a steep overall 19% *decrease* in the success rate of SMEs to obtain loan finance, however with substantial variations across the EU27.

It is against this background that the European Investment Bank finances SMEs, mostly through Financial Intermediaries (FIs). Over the period 2005-2012, the EIB in this area has signed a total volume of EUR 64bn with 367 different FIs. More than EUR 53bn of this amount was disbursed to FIs, which had, at end 2012, in turn disbursed nearly EUR 48bn to an estimated 284 thousand SMEs through nearly 355 thousand allocations. The Bank has especially stepped up its action directed to SMEs with the crisis that hit Europe as from 2008.

EIB SME Intermediated lending 2005-2012	
Volume signed for SMEs	EUR 64.0 bn
Number of operations	560
Number of contracts	759
Disbursements-FIs	EUR 53.3 bn
# FIs	367
Disbursements to SMEs	EUR 47.6 bn
# allocations to SMEs	354 958
Source: EV Analysis of EIB data	

The present evaluation focuses on the Bank's intermediated lending to SMEs through Financial Intermediaries (FIs). It has been carried out in response to an explicit request by the EIB Board of Directors ("CA") in February 2010. It assesses the implementation of the new strategies of the Bank with respect to SMEs and sheds light on the benefits accruing to those Final Beneficiaries (FBs).

The evaluation is primarily intended to assist the EIB's governing bodies in the formulation of Bank policy and strategies, and to enhance accountability and transparency of the Bank's operations. It should also offer practical support with regard to the implementation of operations to the Lending Directorate and the Projects Directorate of the Bank. Outside the EIB, the evaluation may be of interest to the general public, to public authorities and private promoters in relevant sectors.

1.2 Structure of this report

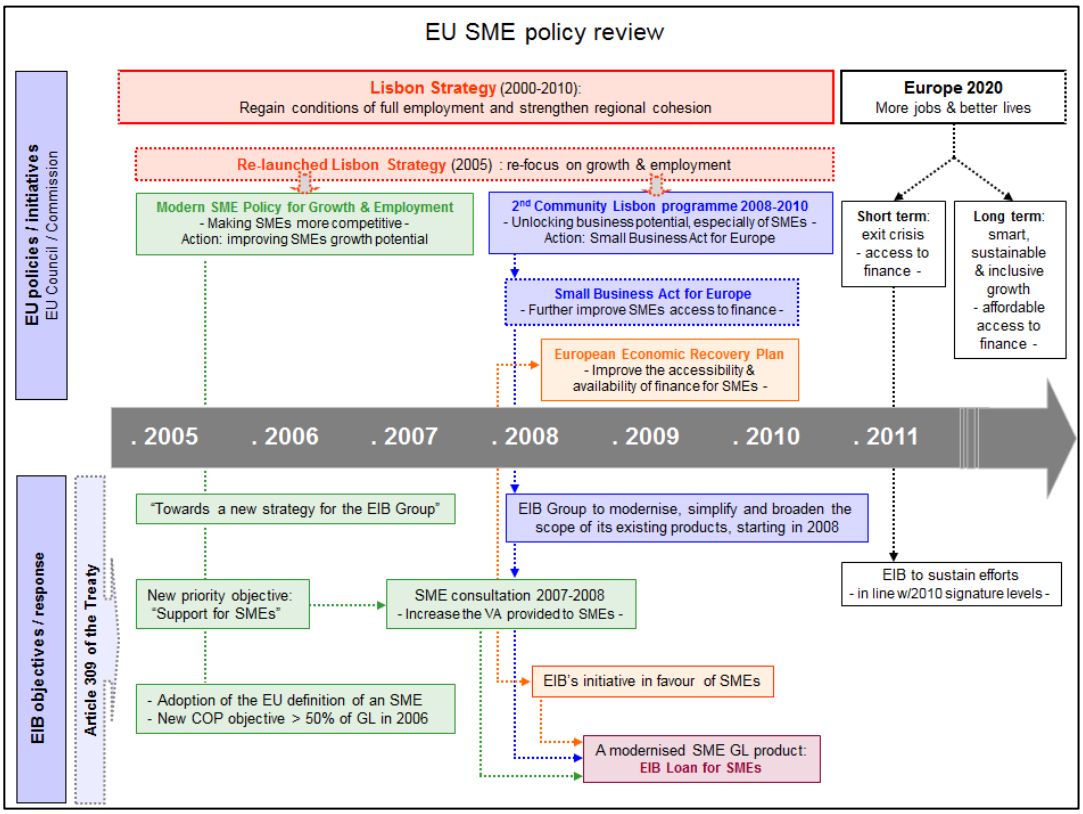
This report is structured as follows. After the present introduction, Chapter 2 analyses the evolution of EU and EIB policies. Chapter 3 describes the methodology for this evaluation. Chapter 4 contains the portfolio analysis and describes the sample. Chapter 5 discusses the relevance of the projects, whilst Chapters 6, 7 and 8 discuss Effectiveness, Efficiency and Sustainability, respectively. Chapter 9 summarises the findings and provides the overall ratings for the projects.

The subsequent two chapters relate more specifically to the Bank. Chapter 10 assesses the EIB contribution to the operations. Chapter 11 assesses the management, by the EIB of the operations (Project Cycle Management, PCM).

Chapter 12 summarises the overall conclusions of the evaluation and proposes recommendations.

2 EVOLUTION OF EU AND EIB SME POLICY – 2005-2011

Since 2005 EU and EIB SME policies have evolved, not least due to the crisis. The graph below provides a schematic overview. The policies will be further described in two subsequent paragraphs.



2.1 The evolving EU level policy context

The EU priority objectives related to SMEs for the 2000-2010 period are embedded in the Lisbon Strategy. Initially, in 2000, the EU's strategic goal was "[…] *to become the most competitive and knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs, and greater social cohesion*" by 2010.

In 2005, the Council reoriented its priorities towards growth and employment. With respect to SMEs this meant a focus on "*unlocking the business potential*." In the years that followed, the Council and the Commission, reaffirming the priority areas of the renewed Lisbon Strategy, launched the Second Community Lisbon Programme (2008-2010) and a "Modern SME Policy for Growth and Employment". Initiatives of immediate importance for SMEs included the Small Business Act for Europe of 2008, which identified *inter alia* the "*further facilitation of access to finance, including through existing EU financial instruments*". Eventually the aim was to improve the growth potential and competitiveness of SMEs. Although the ultimate focus remained on growth and employment, from late 2008 onwards Europe started to put all efforts on exiting the financial crisis with a series of immediate crisis-response actions focusing on availability and accessibility of finance for SMEs.

In 2009 the Europe 2020 Strategy followed up on the Lisbon strategy. It has an objective of "more jobs and better lives". Against the crisis context the 2020 Strategy mentions "[…] *access to finance support should continue until there are clear signs that financing conditions for business have broadly returned to normal*." As underlined by studies on SME's access to finance, in recent years it has become increasingly difficult for SMEs to access banking credit. In light of this information and of more subdued economic growth perspectives, end 2011 when the present evaluation was launched, supporting access to finance remained a priority.

2.2 EIB: from "Global Loans" to "Loans for SMEs"

In line with the re-launched Lisbon Strategy and the initiatives tabled by the Council and the European Commission, in 2005 the EIB endorsed new strategic orientations. "Support for SMEs" became one of the Bank's five key operational priorities within the EU. In practice, this meant *inter alia* that as from 2006 – well before the crisis – more resources were to be made available for SMEs. Global loans were viewed as an important instrument to achieve this. Also, EIB added value was given further attention through the Bank's added value framework.

The new strategy for the EIB group stated SME support was to be channelled through the combined strengths and actions of the EIB and the European Investment Fund (EIF). Further synergies were to be sought, with the EIB concentrating on financing operations through the EU banking sector.

In order to help the Bank determine how to provide support to SMEs in this context, a comprehensive SME consultation involving stakeholders such as financial intermediaries, the EC, and other European/national institutions and associations was carried out from June 2007 to January 2008. This SME Consultation marked the start of a renewal of the Group's SME products, simplifying their use and broadening their scope.

The EIB Global Loan product was to be adapted further to FI and SME needs. Only a few months later, the financial crisis started to severely affect European economies. For the EIB Group, the European Economic Recovery Plan[12] endorsed by the European Council and its crisis-responses required reinforced interventions both quantitatively and qualitatively.[13] Consequently, the Bank was to urgently step up its activity notably through a substantial increase of its global loan activity to SMEs and by promoting the availability of such funding. This would complement other EIB Group products and the types of finance available, i.e. coming from the national and regional level ("subsidiarity").

The EIB Group had been asked before to modernise and streamline its products, and to develop the quality of its global loans, ensuring that the benefits provided through EIB funding reach the eligible SMEs, improving their financing terms. Hence, a modernised SME global loan product, the EIB *Loan for SMEs* (L4SMEs) was introduced. The smooth and swift implementation of the L4SMEs implied a series of organisational changes. A temporary *SME unit* within the Operations Directorate's support structure was created (2009-2011) to accompany product development, monitor policies and support the administration. Additionally, within the Directorate for Operations in the European Union and Candidate Countries (Ops A), a *Central Allocation Unit* (CAU) focusing on post-signature monitoring was established and started operating as of September 2010.

3 EVALUATION METHODOLOGY

In accordance with EV's Terms of Reference and internationally adopted (DAC and ECG) evaluation criteria, this evaluation assesses the relevance of EIB operations, the performance of the operation, the EIB contribution (including financial value added) and the management by EIB of the project cycle. The evaluation was carried out by EV staff with the assistance of consultants.

Evaluation criteria

The evaluation criteria applied are "relevance", "effectiveness", "efficiency", "sustainability", "EIB contribution" and "EIB Project Cycle Management". Whenever available and possible, criteria were compared to relevant benchmarks. In accordance with the Bank's evaluation procedures, individual projects are rated according to four categories: "Excellent", "Satisfactory", "Partly Unsatisfactory" and "Unsatisfactory" ("High", "Significant", "Moderate" and "Low" for EIB contribution).

3.1 Key steps

The evaluation approach consisted of the following steps:

1. *Policy review*. A review of the evolving policy context of SME lending for the EIB during the chosen time frame, and an understanding of the GL and L4SME products as financing instruments used in the Bank. This review formed the basis for the Intervention Logic used in the evaluation and presented below.

[12] Council of the European Union, 11-12 December 2008 and European Economic Recovery Plan (COM/2008/0800 final).
[13] Council of the European Union, press release, 7 October 2008 (13784/08) and 15-16 October 2008 (14368/08).

2. *Portfolio analysis*. Elaboration of the portfolio and subsequent portfolio review of 477[14] operations for GLs with an SME component and L4SMEs signed between 01/01/2005 and 31/10/2011, that is, when the evaluation started (at the end of the evaluation process this portfolio was updated until 31 Dec 2012 and re-analysed, below).
3. *Sampling*. A representative sample of 20 operations was selected amongst the 477 operations present in the portfolio at evaluation start. The sample reflects the variety of the portfolio in terms of geographical distribution but it also considers additional elements to increase potential lessons learnt for this evaluation (see below). It included 8 GLs of which 5 were converted to a L4SME prior to the end of allocation and 12 L4SMEs.
4. *In-depth evaluation*. In-depth evaluation of 19 individual operations as one operation was withdrawn from the sample for in-depth evaluation due to a natural disaster which affected the headquarters of the FI and prevented site visits to be conducted; this operation was included in the SME Survey (see below) however.
5. *Workshop*. A workshop where initial findings were discussed with relevant EIB services.
6. *Synthesis*. Analysis of the outcomes of all preceding elements and drafting of this synthesis report.
7. *Consultation*. Consultation with services on two subsequent drafts of the present report.

The relevant operational departments were also consulted through the various stages of the evaluation and for each of the 20 in-depth evaluations of individual operations.

3.2 Evidence base

The evaluation has the following evidence base.

Internal and external documentary evidence. For each of the operations evaluated in-depth, a review of the project documentation internally available was made, interviews with relevant EIB services were held, documents in the public domain regarding the wider policy context consulted, and FI reporting data analysed. During each mission, further documentary evidence was sought and provided by the FIs and additional qualitative evidence was gathered during the various interviews with representatives of the FI.

Interviews with EIB services. Open interviews were held with representatives of EIB, especially those related to the operations that were evaluated in-depth as well as with internal stakeholders across the EIB hierarchy. The workshop on emerging findings and recommendations, held towards the end of the evaluation process, provided further input from relevant EIB services.

Interviews with FIs. Semi-structured interviews were held with representatives of EIBs counterparts (front office, back office, treasury, risk management), also including, if applicable, relevant subsidiaries (e.g. in the case of leasing). This included interviews with approximately 60 SME retail bankers on the ground.

Visits to SMEs. Following a standardised selection process designed by EV, 3 to 4 SMEs per operation were visited and interviewed for each operation. In a few exceptional cases, last minute complications for some scheduled appointments with SMEs resulted in conducting a phone interview instead. In total 74 SMEs, for 19 operations in 11 different EU countries were visited.

SME Survey. Under supervision of and in close consultation with EV, a survey was conducted by a specialised firm with longstanding experience in EU-wide surveys focusing on SMEs (Gallup Europe). The selected sample of 20 intermediated SME operations across 18 different FIs had, at the start of the evaluation, allocations to over 15 000 SMEs over the 2005-2011 time frame. A statistically representative number of these SMEs were identified in collaboration

Topics addressed by the survey (following evaluation criteria)

- characterisation of company (size, sector, growth path, credit history)
- characterisation of loan/lease: tenor and cost; reason and purpose; fit with company strategy and realisation of goals (e.g. investment made)
- alternative sources of finance; rationale behind EIB intermediated loan
- effects of loan on company in terms of turnover, production efficiency gains, access to new markets, competitive position, job retention or creation, selection of suppliers, environmental quality, access to other sources of finance
- relationship with FI (first time/repeat loan; credit terms/conditions; procedures/paperwork; credit process)
- future development of the company and future finance needs

[14] Corresponding to 658 finance contracts.

with the polling firm, targeting 1 000 successfully completed interviews. These were subsequently contacted to participate in the survey and ultimately 1 003 were interviewed. The survey was based on a Computer Assisted Telephone Interview (CATI) approach with a structured questionnaire. Its results fed directly into the individual evaluation reports and are reflected in the relevant parts of this synthesis report.

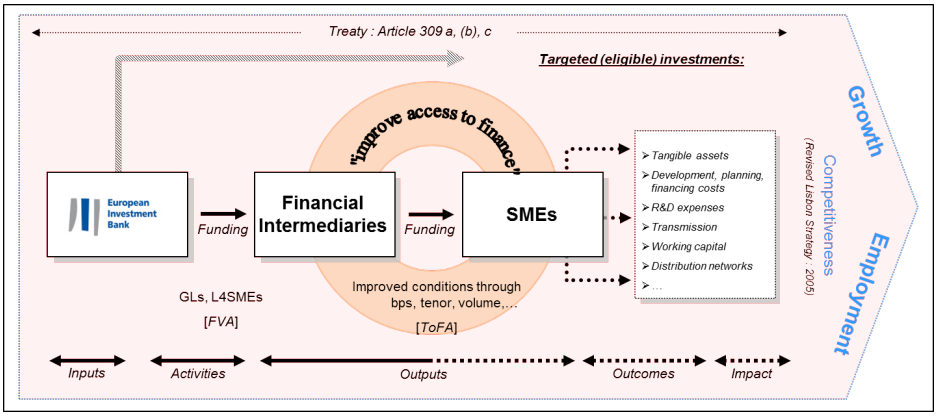
3.3 Objectives and Intervention Logic

Within an operation, Operations Evaluation (EV) distinguishes between three levels of objectives: operational, intermediate and global objectives. Operational objectives relate to what is expected to be directly delivered by the implementation of the project or programme ("outputs"). Outputs are under the control of those who implement the intervention. Intermediate objectives correspond to the effects of the intervention on the direct beneficiaries ("results" or "outcomes"). Global objectives correspond to the direct and indirect effects following on from the outcomes, corresponding to often longer-term impacts. The more remote the effects are from the intervention's outputs, the more difficult it is to attribute them to that particular operation.

Based on the policy review, the distinction between those three levels allowed EV to reconstruct the Intervention Logic of the Bank's SME intermediated lending operations, confirmed by the services during the inception meeting. On the basis of the EIB internal project documentation and the policy context the overall Intervention Logic for the EIB's SME operations (GL and L4SME) was identified, corresponding to the three levels of objectives and confirmed by the services. The systematic comparison of ex-post results with this Intervention Logic was the main basis for the evaluation of the effectiveness of the operations. The three levels of objectives that can be identified within SME intermediated operations are as in the above table.

Level	Objective
Operational	to extend finance to eligible SMEs (sign, disburse, "allocate")
Intermediate	to provide such finance at improved conditions to improve access to finance
Global	to enhance the competitiveness of SMEs, ultimately, generating a positive impact on economic growth and employment

The Bank aims to achieve these objectives mainly by providing Financial Value Added (FVA) to FIs, which in turn are expected to transform part of this into benefits to SMEs (in terms of Transfer of Financial Advantage (ToFA), tenor and volume). This will be discussed in detail in Sections 6.1.3 and 10.1.1. On this basis, the Intervention Logic can be graphically represented as follows.



4 PORTFOLIO REVIEW AND SAMPLE

This chapter considers the scope and evolution of the SME Intermediated Lending portfolio, and its sector and geographical reach, and concludes with the sample selected for this evaluation.

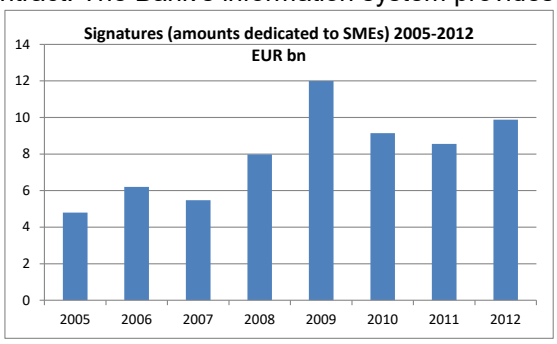
4.1 Portfolio review

At first, the portfolio review identified all EIB operations with an SME component, or "eligibility", over the period 2005-2011, within the EU27. This was reduced to take into account multi-beneficiary intermediated lending operations only. Accordingly, this led to focusing the portfolio review on the Bank's GL and L4SMEs activity. At the end of the evaluation period this portfolio was updated to take into account the year 2012.

The preparatory work for the portfolio review highlighted a number of issues regarding the collection of the required data. It was observed, for example, that for a given operation the intended proportion (%) of SME funding upon approval, signature, disbursement, and later the actual share of funding allocated to SMEs by a FI can all, to a certain extent, differ.

Also, EIB reporting uses the number of allocations as a proxy for the number of SMEs financed, but this is clearly an overestimation. As one SME can receive several allocations, the number of SMEs actually reached is lower than the number of allocations. Calculations on the sample used for the SME Survey suggests that the number of SMEs reached corresponds to about 80% of the number of allocations, for some operations this percentage even being much lower.

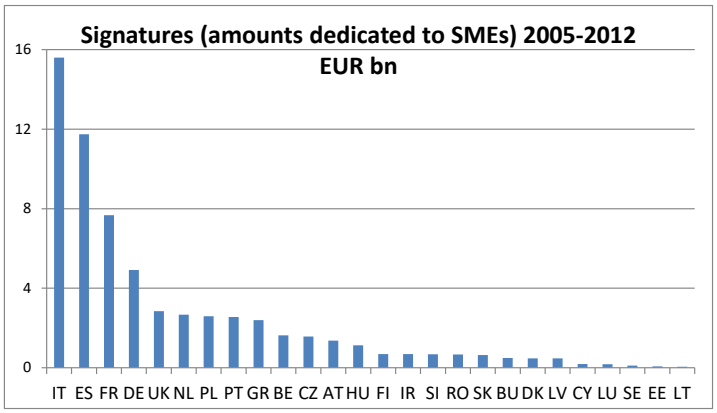
Of the four levels mentioned (approval, signature, disbursement, allocation), two parameters were especially important for the determination of the portfolio and subsequent sampling. First, the intended proportion (%) of SME funding at signature, as this would constitute the relevant portfolio as such. Second, the actual allocations to SMEs under each contract. The Bank's information system provides for each operation signed the proportion intended to be directed to SMEs. However, subsequently linking the "portfolio of signatures" to actual allocations is a very complex task. Therefore allocations were extracted manually from the system for each operation by EV.



With these reservations in mind, the portfolio of GLs with an SME component and L4SMEs was as follows:

- Between 1 Jan 2005 and 31 Dec 2012, the Bank signed EUR 64.0 bn dedicated to SMEs under 560 operations, corresponding to 759 finance contracts.
- EUR 53.3 bn of this was subsequently disbursed to intermediaries and EUR 47.6 bn allocated to an estimated 284 000 SMEs (on the basis of 355 000 allocations up to 31.12.2012).

Between 2005 and 2007 annual amounts oscillated around EUR 5 bn. In 2008, signatures increased and reached a peak in 2009, decreasing thereafter.



Three quarters of the signed EUR 64.0 bn volume were to the benefit of 7 Member States (see insert), with Italy, Spain and France constituting the "top three" beneficiary countries, together accounting for 55% of the portfolio.

As the crisis emerged the demand for the new L4SME product increased. Whereas intermediaries in countries like Italy, Spain, France and Germany had drawn on GLs in the first half of the period under scrutiny, the UK, Greece, the Benelux countries as well as most of the New Member States had the vast majority of signatures as from 2009 only. Malta was the only Member States without signatures throughout the period.

The increased demand after the start of the crisis correlates with the results of the previously mentioned Eurostat survey. This survey shows that some countries were affected more severely by the decrease in the success rate of obtaining loan finance by SMEs. These same countries started, as the crisis unfolded, to increasingly use EIB funding for SMEs.

4.2 Sample selection

For the purpose of in-depth evaluations, a representative sample of 20 operations was selected amongst the 477 operations in the portfolio when the present evaluation started (Oct 2011). The sample reflects the variety of the portfolio in terms of numbers of SMEs reached; loan size; disbursement and allocation levels; loans vs. leasing; public vs. private intermediaries; repeat vs. single operations; and geographical distribution. However, the proportion for Italy, Spain and France in the

sample, resulting from their high shares in the portfolio (60%) was intentionally reduced in order to increase potential lessons learnt for this evaluation by allowing for a wider geographic spread. This was achieved by applying additional factors, including the number of SMEs reached by EIB funding, the sizes of the loans, the level of disbursement and allocation, loans vs. leasing operations, public vs. private financial intermediaries, and repeat vs. single operations.

The list of selected projects for in-depth evaluation is as follows.

No.	Country	Year of signature	Signed Amount (mEUR)**	GL or L4SMEs
1	Bulgaria	2008	< 100	GL*
2	Czech Republic	2007	< 100	GL
3	Czech Republic	2008	100-250	GL*
4	France	2007	>250	GL
5	France	2010	>250	L4SMEs
6	France	2008	100-250	L4SMEs
7	Germany	2008	100-250	GL*
8	Germany	2009	100-250	L4SMEs
9	Ireland	2009	100-250	L4SMEs
10	Italy	2008	100-250	GL*
11	Italy	2010	>250	L4SMEs
12	Italy	2010	>250	L4SMEs
13	Poland	2007	< 100	GL*
14	Poland	2010	100-250	L4SMEs
15	Slovakia	2009	< 100	L4SMEs
16	Slovenia	2009	100-250	L4SMEs
17	Spain	2006	100-250	GL
18	Spain	2010	100-250	L4SMEs
19	Spain	2009	100-250	L4SMEs
20	United Kingdom	2008	100-250	L4SMEs

*is a GL converted to a L4SME; ** for reasons of confidentiality ranges are given

One project [#10] has not been subject of in-depth evaluation because of an earthquake in the region where this FI was located (northern Italy), after which EV decided to cancel the mission. It was taken into account in the SME Survey however. Another operation [#4] has been subject to in-depth evaluation but was not taken into account in the survey because the underlying SMEs could not be identified, as this was not a contractual requirement at the time the operation was signed (GL).

5 RELEVANCE

Relevance is the extent to which project objectives are consistent with EU policies, the decisions of the EIB Governors, as well as with country policies and national, regional or local needs. This section also assesses the internal consistency of objectives and relevance of design of operations.

5.1 Evaluation results

Overall the operations were relevant, with relevance being *partly unsatisfactory* for only two.

The relevance of operations in view of EU policies was strongly determined by the evolving context. That is, during the crisis EIB operations became increasingly relevant in light of the priorities stated at the EU level in terms of access to finance. However, also the type of product used

appeared as an important factor in explaining relevance, the L4SME by design being more relevant than GLs. Relevance in relation to EIB policies and strategies was generally high; this is not surprising as operations are all selected to be compliant with those. Though to a lesser extent than for EU and EIB objectives, operations were generally also found relevant in view of national needs and, again, due to the crisis, became more so over time. Finally, the type of FI is an important factor: though representing only a small number in the sample, operations with promotional banks appeared relatively more relevant to EU and national policies than those with commercial banks. These elements are explained in detail in the following paragraphs.

5.1.1 Relevance in relation to EU policies

The evolution of EU policies with regard to SMEs and SME finance was discussed in Section 2.1. It is against this background that the operations were evaluated for this sub-criterion.

The evaluated operations' objectives at different levels (operational, intermediate, global) were all well aligned with the evolving EU objectives of improving and subsequently supporting SMEs access to finance. Access to finance is expected to increase SMEs productivity and competitiveness and ultimately enhance their capacity to generate employment and economic growth. With 2 exceptions, alignment with the evolving EU SME policy objectives was overall satisfactory, and in 6 cases judged excellent [#3, #5, #9, #15, #16, #18].

More recent operations appear to be more relevant in view of EU SME policy objectives; alignment with EU policies increased with the start of the crisis. Out of the 19 evaluated operations, four were signed before the outbreak of the crisis and 15 after. The 6 operations with the highest alignment were all signed after Nov 2008, i.e., after the outbreak of the financial crisis in Europe (1 in Dec 2008, 4 in 2009 and 1 in 2010). Correspondingly, the 6 highly aligned projects were all L4SMEs. L4SMEs are more often fully aligned with EU SME policies than the previous GLs with partial or full SME dedication. This reflects the fact that the product was to answer the concerns and tackle the priorities voiced by the Council and the EC, i.e. modernised, streamlined, measurable benefits passed on to SMEs.

Two out of those 6 highly aligned operations were with promotional banks. In response to the crisis, most of the promotional banks' activities were stepped up to support the Governments' efforts.

Finally, relevance in relation to EU policies does not seem to depend on the loan volume or size of an operation.

5.1.2 Relevance in relation to EIB policies, strategies and objectives

All operations evaluated refer to the fact that SMEs are a key operational priority of the EIB. A great number of those operations concomitantly targeted other objectives such as convergence, i2i or energy efficiency. For more than half, the contribution to especially the convergence objective is very clear [#1, #2, #3, #9, #13, #14, #15, #16, #17, #18, #19]. Reflecting the focus of the present evaluation, relevance was not evaluated against those additional objectives.

The evolution of EIB policies, strategies and objectives with regard to SME finance was discussed in Section 2.2. It is against this background that the operations were evaluated for this sub-criterion.

Overall alignment with EIB policies was good
In 2005 the EIB Group implemented a new strategy with four major strategic guidelines as regards SMEs: (1) adding SMEs to the Bank's key operational priorities, (2) a renewed partnership with the banking sector, (3) controlled increase in tolerance of risk; new financial instruments and (4) enhanced cooperation with the European Commission and with other IFIs.

In 2007 the EIB launched a broad-based consultation process (the "SME Consultation") on the modernisation of the Bank's product offer to SMEs in EU27, with the aim to increase its added value for the final beneficiaries. The conclusions underlined the need to progress further on actions to support the four major strategic guidelines identified in 2005. Next, in response to the EU's crisis response measures end 2008, the EIB committed to an increase in the volume of funds available for SMEs. Overall the evaluated operations were aligned with the evolving EIB SME policy objectives and strategies. Four out of the 19 operations were even judged excellent in this regard [#9, #15, #16, #18].

An analysis of the stated operational, intermediate and global objectives of all individual operations evaluated clearly shows their intention to improve access to finance for eligible SMEs, both quantitatively and qualitatively. Quantitatively, as, in view of the overall portfolio, at aggregate level they helped stepping up EIB lending to SMEs significantly. Qualitatively, as the objective of providing added value to SMEs by extending favourable financing conditions was systematically stated in all Board reports. When, end 2008, the EIB launched the L4SME product to enhance transparency on the actual Transfer of Funding Advantage (ToFA) to SMEs, on-going GL operations were "converted" to L4SMEs. This meant that new contracts under those operations were signed with L4SME characteristics rather than leaving them as GLs. This responded well to evolving EIB objectives and strategies. Only three operations in the sample, signed in 2006 and 2007 i.e. before the introduction of the L4SME, were entirely carried out as GLs.

As regards EIB's support to the EU crisis response, half of the 12 operations signed as L4SMEs included references to the 2008 Nice ECOFIN Council, where the EIB committed to earmark an additional EUR 15bn (+50%) for 2008-2009 for loans to SMEs across Europe. The new L4SME product addressed the conclusions of the SME Consultation exercise. Though initially not on purpose as it was not put in place for that, it also addressed the EU crisis response, as it aimed to improve funding conditions to SMEs.

Eligibility under Article 309: from "convergence" to projects "of common interest"
In terms of eligibility, SME-related operations are generally justified under Article 309 of the Treaty of the Functioning of the European Union (TFEU). Prior to 1973 this was linked to the predecessor of Article 309a underlining the contribution of SMEs to developing *convergence regions*. After this date, a generic eligibility of SME projects under Article 309 was taken on board, including under 309c. The latter article aims at projects presenting a *common interest* to SMEs of several Member States of such a nature that they cannot be entirely financed by the various means available in the individual Member States.

For SME support this implies that the EIB would have to determine whether funding for SME projects was readily available in a Member State, or not. A recent brochure published by the EIB Group[15] confirms this: "In keeping with the task set out in Article 309 of the TFEU, the EIB provides funding […] for economic activities that do not have ready access to finance (e.g. in less developed regions, SMEs) in the territories of Member States […]". The assessment of SMEs' "ready access to finance in the territories of the MS" would therefore normally have to be part of the appraisal process, but this was often not the case. More thorough SME country needs assessments would support this. More generally, the Bank is currently starting to consider more country specific assessments.

5.1.3 Relevance in relation to national, regional, local and beneficiary needs

Since the 1990s EU Member States identify market failures in SME access to funding which provided the rationale for the continuation of stronger government intervention and support in this area. For the Member States acceding in 2004 and 2007, pre-accession criteria triggered similar phenomena. There is an increased collaboration and alignment on SME policy between the EU and the Member States, with the EU Small Business Act ("SBA") initiative as relevant policy guidance. Therefore, overall, the increased focus that the Bank has given to SMEs in the past was generally in line with the policy evolutions in EU Member States, which themselves to a great extent also reflect EU priorities.

Some national specificities

Poland: creditors enjoy high degree of protection through collateral/bankruptcy laws.
Bulgaria: SMEs are perceived as high risk with interest rates for loans below EUR 1m granted in 2010 at an average interest rate twice the EU average, according to ECB data.
France: high potential, fast growing SMEs ("gazelles") have more difficulties in emerging than in other major economies.
Slovenia: accessing other financing instruments (e.g. equity, participation loans, etc.) is difficult.

For the period covered by the operations evaluated, the focus across the EU Member States was on growth and innovation, in alignment with EU policy. The "SBA factsheets" for the different Member States suggest that although the issues for SMEs are similar across the EU their relative importance varies. National governments adapt their policies to national SME needs and specific national market gaps. New Member States, relatively more dependent on EU grants and instruments than EU15 countries, align more strongly with EU policy.

[15] The Governance of the European Investment Bank (03.09.2012)

The financial and economic crisis has not increased the importance of SME policy *per se*, as the role of SMEs for the economy was already commonly recognised, but reemphasised the need for public support. This came after an upswing, in the early 2000s, of private banking support to SMEs which culminated in markets becoming highly liquid, and, eventually, fragile. Supporting the provision of credit to SMEs was deemed necessary by many EU Member States for economic recovery, accompanied by additional programmes and instruments to support SMEs in various areas (e.g. credit lines provided by the Spanish Government through the Instituto de Credito Oficial (ICO)). Hence, whereas prior to the crisis government programmes and initiatives tended to be more focused on specific market failures (i.e. targeting SMEs experiencing more difficulties, e.g. start-ups), following the crisis, SME access to finance was viewed as a market failure *as such* and the range of SMEs to be supported broadened, if not generalised.

Eurostat statistics on access to finance for SMEs in the EU comparing data for 2007 and 2010 portray a significant deterioration of access to finance for SMEs across all the EU MS. Whereas prior to the crisis banks had access to various funding sources at competitive prices and could easily on-lend to SMEs, as the crisis developed access to finance for SMEs became a more pressing issue for the different countries of the operations evaluated. Hence, different governments in the EU stepped up their support to the banking sector as a condition of encouraging the financing of SMEs.

Governments in at least five countries covered by the sample strongly encouraged the financial sector to increase or at least maintain their SME lending in the crisis [FR, IR, SK, ES, UK]. In those MS, SME lending targets were formally agreed between the governments and financial institutions. Such explicit targets were absent prior to the crisis [#4, #17].

For two cases relevance in view of national needs was low [#4, #7]. These were both GLs in EU15 with FIs which had routinely obtained EIB funding in the past, and which were appraised before the crisis, in countries where access to finance for SMEs was (and in one case remained to a certain extent) not a pressing issue. In one case in particular [#7] an ex ante review of the EIB's product complementarity (or lack thereof) would have allowed for better targeting and hence would have improved relevance.

Finally, national development agencies or promotional banks [#2, #15, #16] can play an important role in supporting government programmes and in channelling funds to SMEs, sometimes through on-lending to private banks [#15]. Operations where the FI were promotional banks – like EIB, policy rather than commercially driven – show better alignment with national and EU SME policy.

5.1.4 Internal consistency of objectives and relevance of design

This section examines the internal consistency of operational, intermediate and global objectives. It also examines if, *ex ante*, the design of the operation was conducive to reaching the objectives of the operations.

To what degree are EIB objectives consistent?
The objectives of EIB intermediated lending to SMEs trigger two observations. First, by extending finance to eligible SMEs the Bank aims at providing finance at improved conditions *as well as* improving access to finance in order ultimately to foster growth and employment. Depending on how those objectives and their relation to the ultimate objectives are interpreted, they may not necessarily be consistent with each other, or difficult to pursue in parallel. Does the Bank mean that it would provide access to un- or underserved SMEs or would EIB loans just improve finance conditions for SMEs that can obtain funding anyway, though at (slightly) worse conditions. This question merits clarification. Second, eventually the goal is to enhance the competitiveness of SMEs and ultimately generate a positive impact on economic growth and employment. Here, it is not clear that aiming at providing access to finance to un- or underserved SMEs would necessarily maximise the Bank's impact on growth and employment.

Little analysis of complementarity with other stakeholders
There is little to no evidence of an analysis of complementarity between EIB objectives and those of other stakeholders for the implementation of the initiatives and instruments in support of SMEs. That is, in order to support the SMEs in the different Member States the EIB Group could have considered using other instruments. The lack of an EIB Group general SME country needs assessment makes it difficult to assess whether the GL or L4SME was the best product choice to meet the global objectives of the operations.

Related to the previous point, EIF activity with a FI – which could be used to justify the Bank's intervention in a specific national context (e.g. complement to equity finance) – is not normally mentioned or assessed in EIB internal documents. Only in one operation [#16] an EIF SME needs assessment was used as input to the design of the operation.

Factors affecting the design of operations

- Weak assessment of absorption capacity [#2, #14, #15,#17]
- Weak assessment of complementarity with other SME market players [#7]
- Strong regional focus [#6, #19]
- Good outreach across sectors and types of SMEs (at all phases of the development cycle)
- Expertise to allocate to different sectors of the economy
- Ability to satisfy fully EIB's reporting criteria
- Solid financial ratios and/or strong backing from parent group or government
- Experience of the FI
- Part of a financial group with previous EIB relations
- Role in supporting government's measures (i.e. for promotional and development banks)

Relevance of design increases from GL to L4SMEs
GLs or converted operations generally suffered from a weaker design than L4SMEs. The L4SME was a new product designed, *inter alia*, to ascertain better than before that funding and part of the advantageous conditions were actually passed on to SMEs. It therefore incorporated a set of features that the earlier GLs did not have, i.e. quantitative requirements to pass on advantageous conditions to SMEs, streamlining the product, enhancing visibility by requiring FIs to make certain types of publicity, broadening eligibilities intended to allow a more flexible use and consequently broaden the reach of EIB products. Global loans on the other hand were often not structured to address some of the stated objectives of the operations; requirements were such that the passing on of a funding advantage to SMEs could not be checked *ex post* [#4, #17].

Aspects considered by the EIB for selecting FIs

- Solid financial ratios and/or strong backing from parent group or government
- Part of longstanding relationship with EIB, guaranteeing a periodic flow of funding targeting SMEs
- Important player in the country as regards SME activity
- Main focus of activity on SMEs
- Large SME pipeline and the ability to absorb the funding
- Wide geographical coverage
- Previous relationship with EIB in supporting other priorities different to SMEs
- Specialized in leasing
- Regional focus
- Good outreach both across sectors and typologies of SMEs
- Expertise to allocate to different sectors of the economy
- Able to satisfy fully EIB's reporting criteria
- Part of a financial group with previous EIB relations
- Role in supporting government's measures

The choice of FI is not done in view of optimising achievement of global objectives
Another element affecting the design of operations is that the selection of intermediaries is not done in order to optimise the achievement of global objectives. The Bank naturally has strict risk guidelines to select its borrowers and these are correctly followed. It also assesses to what extent a FI will be able to implement the operation timely and allocate the loan in compliance with EIB criteria, making sure that funding (under the L4SME) would be passed on to SMEs. However, there is no consistent approach to select them *in view of the national context or needs*. FI selection is bottom-up, demand driven, often influenced by existing relationships (especially for the bigger FIs in EU15 countries), rather than also being done in view of the optimal achievement of global objectives. Hence, from the viewpoint of the individual operation the selection of an FI will generally be justified, however from a *portfolio perspective*, it is unclear whether the mix of FI in a given country is well thought through in view of the needs of that country.

5.2 Conclusion

Operations overall show a high consistency with EU as well as EIB objectives and their evolution over time. The increased focus that the Bank has given to SMEs in the past was generally in line with the policy evolutions in EU member states, which to a great extent reflect EU priorities themselves. Whereas prior to the crisis government programmes and initiatives tended to be more focused on

specific market failures (i.e. targeting SMEs experiencing more difficulties, e.g. start-ups), following the crisis, SME access to finance was viewed as a market failure *as such* and the range of SMEs to be supported broadened if not generalised. Governments in several Member States encouraged the financial sector to increase or at least maintain their SME lending during the crisis. Operations with promotional banks show better alignment with both national and EU SME policy.

From a dynamic perspective, more recent operations appear to be more relevant in view of EU SME policy objectives; L4SMEs are more often fully aligned with EU policies, reflecting the fact that the product was to answer the concerns and tackle the priorities voiced by the Council and the EC. The crisis made SME lending and the L4SME product even more relevant as access to finance for SMEs deteriorated. Converting GLs into L4SMEs when the latter product was launched is therefore deemed to have been the right choice.

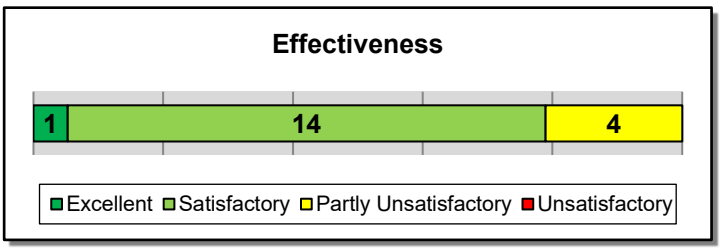
In terms of eligibility, SME-related operations are generally justified under Article 309a and c (or predecessors). The latter article implies that the EIB would determine whether funding for SME projects was readily available in a Member State or not. However, such assessments were not systematically made. This is partly reflected in the finding that EIB loans could be more complementary with national SME policies and instruments, and be explicitly offered in conjunction with other EIB Group products. The lack of country needs assessments makes it difficult to assess whether the GL or L4SME was the best product choice to meet the *global* objectives of the operations. Related to this, the choice of the FI is generally not made in view of optimising the achievement of global objectives. From a *portfolio perspective*, it is unclear whether the FI mix in a country and the EIB Group products range proposed is optimally tailored to a country's SMEs' financing needs. There is evidence from some operations however that if such assessments would have been made, EIB intervention would have been even more relevant. In order to make such assessments however, the relationship between both intermediate objectives (improving finance conditions and/or improving access to finance) as well as their expected contribution to the global EU objective of growth and employment should be made more explicit.

6 EFFECTIVENESS

Effectiveness refers to the extent to which operational, intermediate, and global objectives have been achieved, or are expected to be achieved, taking into account their relative importance, while recognising any change introduced over time (see intervention logic, Section 3.3).

6.1 Evaluation results

Out of the 19 operations evaluated in-depth, 14 scored satisfactory on effectiveness, 4 were partly unsatisfactory and 1 was judged excellent.



L4SMEs were overall more effective than the GLs, linked to the design of the product but also to the time of their introduction, i.e. at the advent of the crisis. All converted loans (from GLs to L4SMEs) obtained a satisfactory rating, which suggests this was a good decision also for effectiveness.

On average, operations with promotional banks score better than the others. This can be explained by the mandate and focus of such banks which are more conducive to meeting the intermediate and global objectives, notably by reaching out to those SMEs un- or underserved by the market. The number of promotional banks in the sample being low, this finding should be treated with caution, however.

There is a learning effect in terms of effectiveness as FIs that have previous experience with SME intermediated lending in partnership with the EIB generally score better. This notwithstanding, one new FI nevertheless obtained an excellent rating for effectiveness.

The following sections will discuss these results more in detail. While operational objectives are nearly always achieved across all types of products and FIs, the results are more moderate when it comes to achieving intermediate and global objectives.

6.1.1 Operational objectives

Extending finance to FIs and SMEs
For this thematic evaluation, reaching operational objectives is measured by the degree to which the amounts signed with FI were fully disbursed and subsequently on-lent, that is, allocated directly or via sub-intermediaries to eligible SMEs[16].

For nearly all operations rated, the amounts authorised and subsequently signed were fully disbursed to FIs. For two operations, the disbursement targets were not met mainly linked to, respectively, (1) a substantial overestimation of the absorption capacity of a FI new to the Bank [#14]; and (2) a volatile economic context, generating an unforeseen (and unforeseeable) banking consolidation move [#19]. In both cases, half of the amounts authorised were not disbursed.

Regarding allocations to SMEs, at the time in-depth evaluations were carried out, nearly one-third of the operations (6 out of 19) had not yet fully allocated the funding to SMEs. For 5 operations the allocation process was still on-going, of which for 4 *ex post* it can be reasonably expected to be fully allocated to eligible SMEs, either within the negotiated deadlines [#1, #15, #16], or shortly after [#8]. In one case, there are doubts as to whether the amount signed would be fully allocated to eligible SMEs [#14]. The capacity of the new FI and the time taken to implement the operation raise concerns. For the 6th operation the amount signed only accounted for half of the amount approved, with the remaining half being cancelled [#19]. The initial (*ex-ante*) SME outreach potential of the operation was therefore not fully achieved.

On the basis of this evidence operations (1) with FIs having already carried out SME intermediated lending operations with the EIB and (2) in EU15 countries overall tend to perform better than those in EU12 countries. Yet several EU12 operations [#1, #15] were also highly effective in allocating funding to SMEs.

Reaching out to eligible SMEs with non-excluded investments/sectors
With some minor exceptions, funding was extended to eligible SMEs, for non-excluded investments. For one operation out of the 19 rated, one-third of the allocations although eligible did not correspond to the stated SME objective. Those allocations enabled the installation of photovoltaic capacity within SMEs – sometimes intentionally established to benefit from the EIB loan – rather than contributing to those SMEs' production process *per se* [#2]. For a couple of SMEs visited across the sample, the autonomy of the SMEs was questioned (i.e. whether the SME was part of a larger group). FIs sometimes had difficulties verifying this.

The L4SME broadened the eligibilities for SMEs with the aim to enlarge the product's scope, to cover anticipated SME needs not covered before and make implementation easier for FIs. Broadened eligibilities included, for example, a wider definition of eligible working capital (WC) as well as the possibility to finance more intangible assets such as the transmission of enterprises. Eligibilities were even further broadened after the inception of the L4SME, notably to provide more flexibility in a period of "credit squeeze", including by relaxing the rules pertaining to the use and justification of WC.

Ex post, the consequences of those broadened eligibilities were as follows. For converted operations, side letters were introduced, specifically referring to general WC needs. For one operation, shorter maturities were even foreseen in specific cases for the financing of WC [#7]. However, overall, these operations focused on the financing of tangible investments and did not make much use of the WC option.

Type of funding received and use/purpose of the funding

The SME Survey revealed that 65% of the SMEs opted for a lease agreement versus a loan. The proportion of loan agreements was higher in the second part of the evaluation period (2010-2011). Several factors (e.g. tax and/or accounting treatments, etc.) can explain such dominance of lease agreement.
A large majority of lease agreements had been used to buy equipment or vehicles. SMEs' reasons to apply for a loan were more varied. Focusing solely on SMEs that had signed a loan agreement, 56% reported that they had used the loan to buy equipment/vehicles or land/buildings. A quarter of FBs had used the funding as working capital; a figure lower than the one observed in other "access to finance" surveys. A quarter of SMEs had used the loan – among other purposes – to finance innovation or to enhance competitiveness and growth.

Source: SME Survey

[16] The sample selection to increase potential lessons learnt for this thematic evaluation introduced a favourable bias in terms of level of disbursement and allocations (see Section 4.2).

For L4SMEs, observations are more nuanced. Some FIs fully endorsed the broadened eligibilities [#6, #11, #14, #15, #19], sometimes explicitly capping the WC share [#18]. Some FIs did *not* offer it or restricted it to the earlier eligibility of permanent increases in working capital required for expanding business activities. *Ex post*, not (fully) using this option was explained by the EIB definition of WC not always being aligned with the context or with the FIs' strategy and needs. This included, for example, the use of overdrafts rather than WC loans [#9], or WC being considered too risky in a crisis context. In such cases, the two year minimum duration was considered too long [#9, #16, #20].

On the SME side, according to the SME Survey, only a quarter of all SMEs used the EIB loan for working capital purposes. This percentage is, in all likelihood, inflated. Indeed, the understanding of the "working capital" concept does not seem to have been fully understood, with a number of SMEs surveyed considering the purchase of equipment as working capital. The findings of the SME Survey thus tends to confirm the observations collected during the on-site visits and interviews with FIs, revealing – in spite of the identified need and of the crisis context – a very limited use by the FIs, and ultimately SMEs, of this financing possibility. Moreover, it took the EIB some time to stabilise the wording of the working capital eligibility – e.g. reflected in the evolving wording of the Operations procedure manual, which may have dissuaded loan officers to insist on this option with their FI counterparts.

6.1.2 Characteristics of the beneficiary SMEs

To what type of companies and projects was EIB funding allocated? Most operations covered the entire spectrum of SMEs, from very small to larger SMEs both in terms of number of employees and turnover. However, each operation is unique in the type of SMEs reached, some operations focusing more on the low end of the spectrum (SMEs with less than 10 employees), others targeting the high end (50 to 249 employees). This depends very much on the FI specialisation (e.g. a large multinational banking group versus a small regional bank or promotional bank).

Broad sector coverage
Sector coverage also varies from one operation to the other. However, overall, sector coverage was broad, reflecting the broad EIB eligibilities. Across all operations sampled, SMEs involved in the construction, transport and ICT sector were the main beneficiaries, followed by SMEs involved in trade, accommodations and food services, and SMEs with activities in the industrial sector. SMEs involved in the agricultural sector were only covered by a few operations, in such cases reflecting the importance of this sector in the national or regional context.

Innovative SMEs
With the reservation that the concept may have been broadly interpreted by respondents, 65% of SMEs surveyed claim they had introduced some form of *innovation* in the past five years. The introduction of a new or significantly improved product or service to the market being the most likely innovative activity among the ones listed in the SME Survey. Large SMEs (with 50 employees or more), as well as those involved in the industry sector were the most likely to have introduced some form of innovation. Some FIs dedicated part of the EIB loan to innovative projects (see insert).

An innovative use of the EIB loan: targeting innovative projects [#11]

At the time the operation was appraised and implemented, Government policies were centered on promoting innovation, particularly for SMEs. The FI, taking on board governmental priorities decided to rely on one of its entities to direct a portion of EIB funding to projects with a specific innovation component. The FI therefore channelled a portion of the funding through one of its standard products dedicated to enterprises financing research, investments in information technology and to the purchase of equipment linked to an innovation project (the only one of its kind available at the national level). Such projects are appraised by a team of engineers based in the headquarters of the FI. Funding may reach up to 100% of the investment with a repayment period of 5 years (up to 7 years for Research), including a grace period of up to 18 months, extendable to 24 months and even 30 months in some cases involving longer research activities.

The proportion of smaller and younger firms served decreased over time
The operations extended financing to businesses with a variety of ownership structures: owned by one person, multiple entrepreneurs, a family, or by other firms or business associates. Only very few were listed on the stock market. Virtually all SMEs visited and interviewed were autonomous profit-oriented companies at the time they signed the financing agreement, however it was not always obvious for FIs

to establish this and some firms during the visits turned out to be part of bigger groups – these were exceptions however.

Although several operations extended a considerable proportion of loans and leases to relatively "young" businesses (i.e. those that had been active for less than 10 years), the majority of FBs surveyed had existed for more than 10 years when they received the financing (62% of all FBs).

The majority of SMEs reached were firms with less than 50 employees, accounting for over 80% of beneficiaries. Although most operations provided financing to a considerable number of micro-firms (below 10 employees) their proportion in the overall FI portfolios decreased during the period 2010-2011. Fewer micro and young firms were reached *after* the crisis started. Finance constraints are reportedly (as per ECB surveys for instance) more important for very small and young firms than for larger more mature firms. The present survey also confirms this general finding.

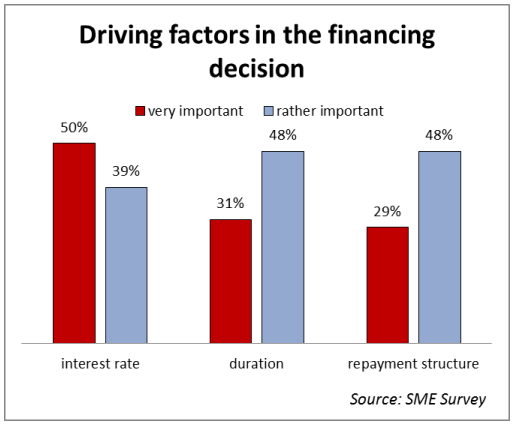
Most FIs direct the EIB loan towards comparatively larger and less risky firms of their SME portfolio
Upon benchmarking with external SME surveys, EV's SME Survey suggests that the loans and leases funded by the EIB were generally larger than SME loans and leases extended during the same period in the target countries. Given that loan size increases with firm size, it is expected that EIB funding was more frequently directed to relatively larger SMEs.

Upon benchmarking with the FIs' overall SME portfolios responding to the same eligibility criteria, the evaluation furthermore provides strong evidence that the beneficiary SMEs are on average larger and less risky than those of the FI SME portfolios overall (See also 8.1.2, 8.2). Interviewed and surveyed SMEs indeed often claim that they would have obtained funding anyway, although probably on less favourable terms. Only two operations, both with promotional banks, were directed to "gap funding", i.e. to SMEs that would not or with great difficulties have obtained funding otherwise. For [#15], the FI even acted as a lender of last resort.

6.1.3 Intermediate objectives: access to finance at improved conditions

In view of the intervention logic for intermediated SME lending (see Section 3.3), this section addresses the extent to which finance was provided to SMEs at improved conditions as a result of the operation. The section takes into account a number of elements that have been considered ex-post as improving SMEs financing conditions, namely, the attractiveness of the EIB funded lending conditions, the availability and volume of funding when needed by SMEs and the impact of the operations on the overall eligible SME lending activity of FIs, which can be used as a proxy for improved access to finance.

Attractiveness of lending conditions
According to the SME Survey, interest rate was the most important factor in the SMEs' financing decision at the time they took out the EIB loan/lease and increasingly so over the period under scrutiny, and more so for larger companies.



Comfort that the transfer of an actual pricing advantage took place increases with the shift from the GL to the L4SME product. For the GL operations in the sample [#2, #4, #17] and for one of the converted operations [#7] this transfer is more difficult to establish. By moving from GLs to L4SMEs, the EIB has structured its operations in such a way as to encourage FIs to pass on a pricing advantage to eligible and *identifiable* SMEs, contributing to improving lending conditions to SMEs in a more transparent manner. Two elements have contributed to such an improvement, the introduction of (1) a contractual transfer of benefit to SMEs and (2) more stringent and harmonised transparency requirements.

Transfer of benefit. A major innovation introduced with the Loans for SMEs compared to the Global Loans is the quantification of the contractual Transfer of Financial Advantage (ToFA), which is contractually binding. That is, the FI agrees to a ToFA of a determined number of basis points. Before,

in GL contracts, the ToFA was expressed in qualitative terms or not at all [#2, #4, #17]. Converted Global Loans introduced minimum levels for ToFA. For all but one converted operation, at least the contractual ToFA was passed on to the SMEs. Only for [#7] *ex post* it was not possible to obtain information on the SME loan pricing models applied for EIB funded sub-loans and on the pricing discretion left to the front office.

For a number of L4SME operations, the FIs went *beyond* the agreed ToFA (see also EIB contribution, Section 10.1.1 especially). Interviews with FI representatives illustrated that pricing is determined by the market and the FI's pricing strategy – which differ between FIs and which the EIB has no influence on – from which the ToFA (which is contractually fixed between EIB and FI) is subsequently deducted. In cases where banks, as verified *ex post*, incorporated EIB pricing into their pricing models the EIB advantage is easier to ascertain [e.g. #6, #15, #16].

Interviews with around 60 account managers in the front office as well as with SMEs confirmed those findings, with SMEs identifying an actual pricing advantage linked to the EIB loan/lease, which, moreover, for L4SMEs is explicitly mentioned in their contracts.

The survey findings partly qualify these positive observations. Overall, 35% of SMEs interviewed reported that they had received a reduction in the interest rate of the loan or lease. Although the survey found, for each operation, at least some evidence that the funding advantage was being passed on to some FBs, large differences were observed in the proportion of respondents which answered that the loan/lease had specifically advantageous conditions linked to lower interest rates [ranging from 9 out of 10 (87%) respondent SMEs for #16, to close to 60% for #2 and #8 to 18% for #9 and 14% for #20]. There is often no systematic correlation between the SME Survey result in terms of the perception of SMEs interviewed and the degree of comfort acquired at the level of the FI itself (*ex post* analysis of portfolio and contractual terms showing that funding advantages had been passed on). Given their size (relatively larger companies) and risk profile (lower) one would expect many companies to have such negotiation power as to obtain a good price, as confirmed by several companies visited, especially in EU15; also, more than half of the SMEs surveyed considered several offers in their financing decision. In those cases ToFA was often used by FIs to maintain or gain new clients from competitors.

Over a quarter of the surveyed SMEs explicitly stated that the funding received was advantageous compared to other sources of financing and this was more often the case for larger businesses. More generally, 80% of the respondents answered that they had asked for more than one quote, which would suggest that the EIB loan that they finally chose was amongst the most advantageous, if not the most advantageous one.

Transparency. To increase the likelihood of financial benefits being passed on to SMEs, for the L4SME product a number of elements, including transparency conditions, were introduced in the side letter with the FI. *Ex post*, most FIs complied with these requirements through a specific EIB product label and internal or external documentation on the origin of the funding and the discount to be applied (brochures, side letters or special mention within contracts, mention on the FI website).

Overall, the SME site visits and review of the contractual documentations between FIs and FBs suggest that those obligations were fulfilled by FIs. This notwithstanding, the SME Survey found that a considerable number of FBs were still not aware that the financing received originated from the EIB (even in cases where this must have been written into the FI-FB contract). EIB visibility has improved over time, though: an increase was observed in the proportion of SMEs that were aware of the EIB loan origination from 16% for financing agreements signed between 2006 and 2008 to 41% for those signed in 2011. For the L4SME product awareness of EIB involvement was twice as high as for GLs, for which a mention of the EIB origin was not an obligation. Yet, no statistically significant improvement was observed in the perception of the final beneficiaries for the L4SMEs product in terms of transfer of financial benefit or increase in tenor.

Importantly, the transparency and communication requirements attached to the L4SME instilled, in most FIs interviewed, a certain change of behaviour going beyond a mere compliance check to EIB requirements and to the creation of an EIB *product*. For L4SME operations the evaluation suggests that the comfort level for the transfer of an actual pricing advantage equivalent to at least the ToFA was higher for those operations that had the highest level of marketing and transparency. One lesson learnt from the in-depth evaluations [#6, #7, #9, #14, #15, #16, #18, #20] is that the EIB could improve

the performance of its intermediated funding even more through stronger communication, targeting not only the FIs but also the SMEs.

Tenor

Irrespective of the type of loan (GL, L4SME, converted), according to most finance contracts the term of the SME sub loan agreements should correspond to the economic and technical life of the SMEs' investments, with a minimum of two years (for L4SMEs) and of three years (for GL operations). The longest tenor of EIB loans extended to FIs in the sample was 12 years while sub loans generally have shorter maturities.

Information on tenors of comparable SME loans extended by the FIs was difficult to obtain, as such information was not a contractual requirement. When such information could be provided to the evaluators, average tenor of the EIB portfolio was equal or slightly longer. Only in two cases [#16, #19] the FIs used the EIB operation to increase the sub-loan tenors *substantially*, to act counter-cyclically in a crisis context, where financial institutions generally had a high reluctance to provide long term funding to SMEs.

SMEs encountered were satisfied with the tenors extended. According to the survey, around 80% of the SMEs financed answered that they signed loan or lease agreements with a tenor below 8 years. Only 10% of the respondents benefited from longer tenors, yet generally remaining below the tenor provided to the FI by the EIB. 32% of respondents had tenors below 3 years. A number of FIs on their own initiative offered grace periods to their clients (12% of the SMEs surveyed), ranging from less than 3 months to most frequently one year or more (40% of respondents).

Operations differ in terms of their focus on loan or lease agreements. Three groups can be distinguished, "loan", "lease" and "mixed" operations. Extrapolating to the total population of SMEs reached by the operations, the SME Survey showed that a majority of SMEs had signed a leasing agreement (65% vs 31% loan agreements); with a higher proportion of loan agreements in the second part of the evaluation period (2010-2011) than in the first period (2005-2009). The importance of leasing goes to a certain extent against the idea that longer tenors for loans are better for SMEs as, usually, leasing contracts are of shorter maturities. The higher share of shorter leasing contracts suggests that ideal maturities do not imply longer tenor in absolute terms. It depends on the underlying investments and on the finance product used.

Availability of funds to SMEs

Expected loan amount. Across most operations, about 85% of SMEs surveyed reported that they had received all the financing requested. The SME Survey shows that, in accordance with the findings of other surveys on SMEs' access to finance, smaller companies were more likely to have received only part of the financing requested. The proportion of partially successful applications ranges from 7% for companies with more than 50 employees to 18% for those with less than 10 employees. There is a direct relationship between the amount of funding requested and the size of the SME, micro businesses typically applying for smaller loans/leases.

SMEs' most pressing problems, as per the SME Survey

When asked for their most pressing problem, 16% of SMEs financed with EIB loans declared access to finance. It ranked as their second most pressing problem, after finding customers (20%) but before competition (15%), the costs of production or labour (14%), bureaucracy (11%) and the availability of skilled staff or experienced managers (10%).

However, SMEs financed with EIB loans do not show the same pattern as shown by SMEs in general which since the beginning of the crisis suffered severe deterioration in access to finance, as suggested by various sources (e.g. ECB). For European SMEs both the success rate of loan requests fell over the past period (from 84% in 2007 to 65% in 2010) and SMEs obtained generally lower loan amounts than requested. In sharp contrast, the share of SMEs interviewed in the SME Survey that received all the financing requested did not drop between 2006 and 2011.

Timeliness. The SMEs surveyed declared the funding had been obtained when needed. Across all operations, more than 80% of SMEs reported that the financing was obtained at the right time. The proportion of FBs that answered the funding had been received later than expected, needed or hoped for remained below 10% for nearly all operations. This will be further discussed in the Efficiency section (7.1.1).

Leverage. The impact of EIB operations on the volume of funding extended by the FIs to SMEs attempts to measure the extent to which access to funding has increased for SMEs overall. For this evaluation this element is assessed by observations on the leverage the operation likely had, and by the fulfilment of the "additionality" requirement.

For about half the operations evaluated, the amounts extended by the EIB were marginal when compared to the overall volume of Medium-Long Term (MLT) funding extended by FIs to eligible SMEs [#4, #5, #7, #9, #11, #18, #19, #20]. For the other half, the amounts were substantial [#2, #3, #6, #8, #12, #13, #14, #15, #16], accounting for 10% to up to one-third of MLT annual SME funding. In these cases, without the EIB funding, the same volume of MLT SME funding would not have been extended but only a (sometimes much) smaller amount. In a crisis context, when banks were oftentimes reluctant to provide MLT funding to SMEs, this can be considered as a positive achievement. All the operations carried out with promotional banks positively influenced the flow of MLT funding directed at eligible SMEs. The majority of operations for which the funding was considered substantial were located in the EU12 (New Member States), impacting the FIs ability to extend further loans/leases to SMEs [7: #1, #2, #3, #13, #14, #15, #16]. For nearly half of the operations the presence of EIB funding induced the FIs to do more. In such cases, EIB funding is considered to have leveraged SME funding, at least to a certain extent.

Whilst the majority of the FBs were already clients of the FIs, the operations helped them reach out to new clients. According to the SME Survey, over a quarter (28%) of SMEs were new clients of the FIs and for an additional 14% of SMEs it was the first time they signed an agreement for financing with the FI. There are important differences from one operation to the other, with the percentage of new clients/first financing agreement ranging from 15% to 71%. Across the portfolio, micro firms (with less than 10 employees) and younger ones were most likely to be new clients. Even in cases were the amount of the EIB funding was not considered material, it enabled FIs to remain competitive, retain clients and close additional deals.

For L4SME operations FIs have to confirm that the volume of MLT SME financing (with a term of more than 2 years) outside excluded sectors, signed during the Allocation Period and financed with non-EIB resources has been at least as much as that of the EIB Loan for SMEs. The "additionality" requirement allows the EIB to comply with the general rule that EIB financing should not exceed 50% of project cost.

The additionality requirement appears, in fact, to be more of a compliance check than an incentive for FIs to increase MLT lending to SMEs. It is *not* equivalent to the additionality concept normally used in the economic literature. That is, the additionality indicator as used by the Bank is not measuring the induced extra lending by the FI on top of a baseline, i.e. lending it would have otherwise not extended. It just controls for whether the FI can show a same volume of similar SME lending regardless of whether this was additional to its normal lending pattern. The term additionality therefore seems misleading.

Whilst a number of additionality comfort letters had not yet been received as allocations were still on-going (see Section 11), meeting the additionality requirement was not an issue but for 2 FIs [#15, #14]. The additionality requirement penalises FIs with smaller SME portfolios; more recently however, within the crisis context, the Bank has allowed for some flexibility in this regard.

6.1.4 Global objectives: competitiveness, growth and employment

According to the Bank's policy objectives, operations were eventually to support the competitiveness/productivity of SMEs, their growth and their employment levels. Additionally, in a crisis context, such operations were to stimulate economic growth and support the efforts undertaken at national level to exit the economic crisis.

Mainly based on the survey results, several operations appear to have had a visible impact on growth and employment [#1, #9, #13, #14, #16]. These were all but one [#9-IR] in NMS. A vast majority of the SMEs encountered and surveyed (on average, 93%) stated the funding had contributed to the successful implementation of the project pursued. However, importantly there is no correlation between the successful implementation of the projects pursued, and growth and job creation. Indeed, some of the operations where successfully completed investment projects were frequent, have generated the most limited impact on competitiveness, growth and jobs [#3, #5]. Conversely, the two operations with the lowest percentage of positive answers on the successful implementation of the projects pursued

[#14, #16] generated some of the strongest impact. Successful implementation of investments is not the only condition for impact.

Roughly half of the SMEs surveyed reported that their annual turnover had increased after having received the EIB funded loan or lease. SMEs that declared this increase was partly or solely due to the financing outnumbered those for which it was unrelated (30% vs. 22%). Nearly half of the SMEs reported the financing had triggered positive effects on productivity, market share development or the general economic health of their business.

For about a quarter of the SMEs surveyed, the EIB funded loan or lease led to an expansion of workforce. On average, about one job was created per sub-loan per SME that acquired financing through any of the 19 operations surveyed.

Achieving global objectives

SMEs financed by EIB loans tend to show lower risk than SMEs receiving funding from other sources. This situation can be explained by the design of the Loans for SMEs. Although it might appear disappointing that weaker SMEs do not seem to see their access to finance improve with EIB's intermediated lending, such result is counterbalanced by an increased ability to achieve the global objective of enhancing the competitiveness of SMEs, thus ultimately generating a positive impact on economic growth and employment.

The performance of the EIB loan in terms of its global objectives does not seem to be related to the economic situation of a county *per se*. For example, four of the countries struck harder by the crisis and with relatively low scores in satisfying loan requests performed very differently with respect to global objectives. Two countries counted amongst the lowest performing operations in this respect [#10, #11, #12 (IT) and #17, #18, #19 (ES)], whilst the two others [#9 IR, #16 SI] were amongst the ones with the highest relative levels of growth and job creation.

No significant differences were found in terms of impact between operations within a country, nor between loans and leases. The survey results suggest that EIB lending is likely to generate more impact on growth, jobs and competitiveness when targeted at SMEs having introduced innovations and used the funding to finance research and development. The economic impact of EIB lending is also likely to be higher for small (but not the smallest) firms with 10-49 employees rather than for micro firms (0-9 employees), and for relatively young (but not the youngest) firms (2-5 years of activity).

Impact is enhanced by a solid knowledge and alignment of an operation with the country specificities in terms of local SMEs' financial needs, FIs' funding needs and national and local promotional activities. When the products complement national policies and are adapted to market demand, the impact is likely to increase. Operations that showed a good achievement of global objectives [#1, #9, #13, #14, #16] also showed a high internal consistency of objectives, three of them score high on overall relevance [#9, #13, #16] and 4 had a good relevance of design [#1, #9, #13, #16]. Other examples had high impact as they showed good alignment with policy initiatives, e.g. [#18, #19] and blended government credit lines with EIB funds.

6.2 Conclusions

6.2.1 The L4SME says what it does and does what it says

The Bank has come a long way in structuring its interventions with regard to SME intermediated lending. The introduction of the L4SME and the experience acquired has led to a situation where intermediated SME lending is to a great extent harmonised in contractual terms, in terms of the definition of the benefits passed on to SMEs (ToFA) and in the way in which this is tracked in order to be able to identify a set of SMEs that would have benefited from EIB advantageous lending conditions.

In other words, unlike the earlier GL, **the L4SME "says what it does and does what it says".** It says what it does namely, that the Bank aims to transfer an identified minimum amount of financial advantage to a set of identifiable final beneficiary SMEs. It does what it says, namely it identifies the sets of SMEs to which, as evidenced by the evaluation results, advantages are actually passed on and this is largely confirmed by the evaluation results.

This approach stands in sharp contrast with the GL approach where practices, procedures and reporting requirements were heterogeneous across the Bank. Especially, for most GLs it was unclear

how much of the EIB advantage ultimately benefited SMEs and how much remained on the FIs' balance sheets.

6.2.2 Operational objectives achieved, but for intermediate and global objectives more difficult to ascertain

The evaluation shows that the operational objectives of the loans were generally achieved. That is, for the majority of operations under scrutiny the authorised amounts were signed, disbursed and allocated to eligible SMEs (with the reservation that some allocation processes had not formally ended by the time the evaluation was carried out).

The contractual ToFA and more stringent transparency conditions of the L4SME product have clearly contributed to providing a higher level of comfort that a measurable financial advantage was indeed passed on to SMEs. Under those EIB loans FIs provide loans at improved conditions (mainly bps, often also tenor) as compared to their overall SME loan book. The L4SMEs and with it the heightened interest of the EIB regarding on-lending conditions to SMEs, has for some FIs triggered a change of behaviour leading them to adopt more transparent pricing models that allow for a clearer appreciation of ToFA. Still, only a quarter of SMEs surveyed explicitly stated that the interest rate was more advantageous as compared to competitors. More importantly, however, about 80% of SMEs had asked for several quotes before preferring the EIB funded offer, which suggests that the EIB loan increased competition.

SMEs overall appeared satisfied with the provided tenor, volume and timeliness. Tenor appeared equal to or only slightly higher than FIs SME portfolios' tenors overall or compared to what survey respondents tended to get. Only very few operations explicitly used the EIB funds to on-lend at substantially longer tenors than they normally do for this target group.

As concerns global objectives, several operations had a visible impact on growth and employment – all but one in the New Member States. According to the survey results, on average about one job per financed SME was created. About half of the SMEs declared that turnover had grown after receiving the EIB funds, of which one-third attributed this entirely or partly to the funding. Also half of the SMEs reported that the loan or lease had positive effects on productivity, market share or general economic health of their business. The economic impact of EIB lending is likely to be higher for small (but not micro) firms and for relatively young (but not the youngest) firms. Firms having introduced innovations or that used the funds for research and development show a relatively higher impact. Finally, impact is also enhanced by a solid knowledge and alignment of an operation with the country specificities in terms of local SMEs' financial needs, FIs' funding needs and national and local promotional activities.

"Improved access to finance"

In general terms, at least three situations can be described as "improved access to finance":

- From a microeconomic perspective:
  - SMEs underserved by commercial banks can see their projects financed through the funding provided via the operation. This could notably happen for SMEs showing a higher risk than their peers.
  - the financial terms are more advantageous than the ones of other sources of funding. This would impact the type of projects undertaken by SMEs and/or leave the SMEs with more financial resources available. By the same token, the improved conditions could also materialize in longer tenors for loans funded by the operation compared to other products available in the market.
- From a macroeconomic perspective, improved access to finance can mean the ability to find funding while there is an overall contraction of the volume of available loans. This happens during periods of economic stress when the perceived risk profile of investment projects deteriorates and lenders' balance sheets show signs of weaknesses.

6.2.3 EIB intermediated SME loans generally serve larger and less risky firms in FI SME portfolios

EIB's intermediated SME lending has a broad scope and, apart from a series of exclusion criteria, does generally not focus on specific types of SMEs in terms of size, sector or risk profile. Moreover, the EIB does not share SME credit risk, promotes on-lending at generally long tenors and ToFA is settled in markets which are highly volatile. Finally, FIs prefer to have little or no losses on the EIB portfolio for reasons of reputational risk. The evaluation shows that, under such conditions, the FIs generally tend

to choose larger and less risky SMEs to be financed under the EIB loan in comparison to their overall eligible SME portfolios. Moreover, the proportion of smaller and younger firms in the EIB portfolios financed by the FIs decreased over time.

In most cases, EIB operations contributed to fund SMEs at (measurably) better conditions. However, because of their risk profile, it is expected that those SMEs were often also those most likely to obtain funding anyway. This is confirmed by interviews with account managers in branch offices who in several cases used the loan to attract or retain SMEs from competing banks; and by the site visits and survey results which suggest that a great proportion of SMEs have some power to negotiate loan conditions.

As a consequence, EIB intermediate SME loans do not primarily seem to enable access to finance for SMEs which are underserved by banks, except if operations are carried out within the framework of national programmes/policies, implemented by, for instance, promotional banks [#2, #16].

6.2.4 FIs do not fully use the range of options provided under the L4SMEs

Eligibility criteria do not only concern the types of SMEs that are financed. They also refer to the types of products that FIs are allowed to offer to SMEs under the EIB loan. The L4SME product broadened those in comparison to the earlier GL, allowing more than only capital investment to be financed, especially working capital for a minimum duration of 2 years. The evaluation suggests that FIs use these possibilities only very marginally. A variety of reasons account for the very limited use of these broadened eligibilities, such as not being adapted to the regional context, national programmes covering the need for working capital funding especially during the crisis and a tenor of 2 years being considered too long for working capital. Also, FIs that were used to working with the EIB hesitated to broaden the scope, not being fully confident about the eligibility. This reluctance may have been reinforced by the fact that contractual definitions on EIB's side took some time to stabilise.

6.2.5 Visibility and transparency make a difference

Visibility requirements (mention of product and conditions on website; brochure; communication by account managers; contractual clauses) make a difference, as the SME is made aware of the possibilities of obtaining better funding. The evaluation gathered solid evidence that contractual advantages were generally passed on, and contractual ToFA was often even exceeded by FIs. In fact, the more extensive an FI's responsiveness to the EIB's transparency and visibility requirements, the higher the *ex post* level of comfort that ToFA was measurable and real.

However, a considerable number of FBs were still not aware that the financing originated from the EIB, even if EIB visibility has improved over time. Awareness of EIB involvement was for the L4SME product twice as high as for the GLs. Yet, in the perception of the final beneficiaries no statistically significant improvement was observed for the L4SMEs product in terms of transfer of financial benefit or increase in duration. Hence, awareness of EIB presence *per se* is not a sufficient factor (or not the only factor) for SMEs to acknowledge benefits linked to EIB lending. Despite the already increased awareness due to the new contractual clauses of the loans for SMEs covering EIB visibility, there is still room for improvement on this point, e.g. by improving the flow of information between stakeholders at large, and with FIs and SMEs.

6.2.6 FIs with smaller SME portfolios have more difficulties complying with the additionality requirement

For L4SME operations FIs have to confirm that the volume of MLT SME financing with a term of more than 2 years outside excluded sectors, signed during the allocation period and financed with non-EIB resources has been at least as much as that of the EIB Loan for SMEs. This obligation is inspired by the fact that normally the EIB would only finance up to 50% of an investment which was the case under GLs. Allowing for a 100% finance of an FI-SME contract streamlined the administration of L4SMEs as no longer a distinction needs to be made between EIB and other funds; the "additionality" of the EIB loan was elevated from the individual investment to the FI portfolio level which has strongly facilitated the administration of the L4SME product as compared to the previous GL.

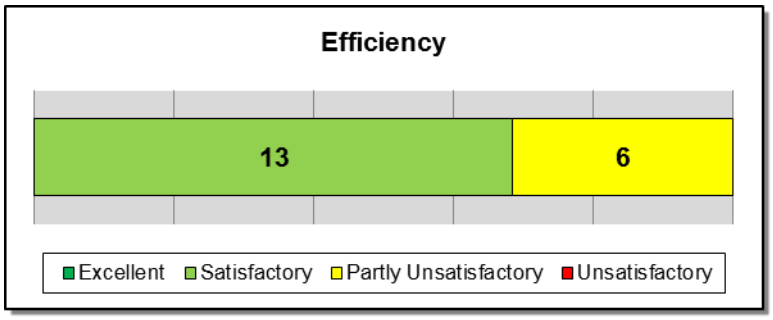
Although the additionality requirement, as set out in the additionality clause, was respected across the sample, it was more difficult to fulfil for FIs with smaller SME portfolios – meaning probably that in such cases their absorption capacity initially was overestimated. For larger FIs on the other hand, which

form the majority of the sample, fulfilling the requirement was easy as the EIB funding is marginal on their overall eligible portfolio; the requirement in such cases becomes a formality and is not a meaningful measurement of additionality. In order to prevent confusion, the Bank could consider changing the term.

7 EFFICIENCY

Efficiency considers the extent to which project benefits/outputs are commensurate with resources/inputs. This is approached by assessing the following sub-criteria: timeliness and absorption capacity; maturity (mis)matches and possible reutilisation of funds; cost-effectiveness at FI and FB level; and management efficiency.

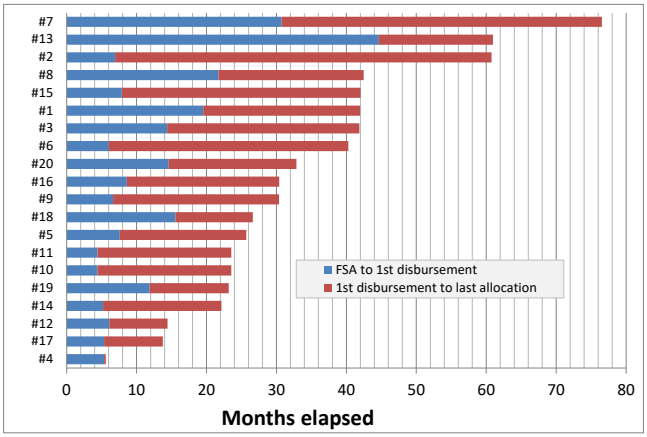
7.1 Evaluation results



The efficiency of 13 out of the 19 operations evaluated was deemed satisfactory; for the remainder this was partly unsatisfactory. The timeliness of operations showed great variations. Observed delays before disbursement had a variety of explanations especially, e.g. the complexity of an operation or borrowers which would wait until FVA would become more attractive. Delays after disbursement were explained by lower absorption capacity of the FI, the market, or both, in some cases exacerbated by the crisis. Delays in absorption often led to allocation extensions. At the level of SMEs, timeliness – an important factor for the surveyed SMEs – was overall good. This implies that efficient delivery mechanisms exist on the FIs side. About half of the operations had maturity mismatches. For two of those, action was undertaken by the FIs to address them. Maturity mismatches can have an impact on the efficiency of an operation.

Finally, FIs overall found operations cost-effective for them despite, in several cases, additional costs incurred in setting up internal procedures for handling the EIB loan and corresponding IT solutions. Reporting to EIB was overall compliant, yet of variable quality.

7.1.1 Timeliness and absorption capacity



Timeliness and absorption capacity are important features to look at from an efficiency point of view. Timeliness is important not only because it was a formal objective for the EIB since the start of the crisis. It is also a proxy for the efficiency of the process underlying the transfer of funds, from the EIB, *via* the FI, to the SME. Funds should not sit unnecessarily in the FI's treasury.

The adjacent graph shows, for the 20 operations of the sample, the time elapsed (months) between "Fact Sheet A" (FSA) and the final allocation to SMEs as sent by the FI to the EIB. The FSA can be interpreted as the first formalisation of a need for SME-funding expressed by a FI. The graph also shows the moment of first disbursement, i.e. when the funding becomes available to the FI to finance SMEs.

The duration of this process varied highly: from about 6 months for the shortest to more than 6 years for the longest. Reasons for this divergence are mostly operation and context specific, as follows.

The three operations quickest to be processed overall, both on EIB and FI side were two GLs [#4, #17] and a L4SME. Those were high volume tickets (EUR 300m, 200m and 350m respectively) to big banking groups (among top national rank) in France, Spain and Italy respectively that all had a long

track record with the EIB. The three lengthiest project cycles (in excess of 5 years), were for three GLs, in Germany, Poland and the Czech Republic respectively (the first two of which were converted to L4SMEs during the operation). Two were with first-time clients [#13, #2]; one [#7] was with a long-standing client but the first GL to focus strongly on SMEs, coupled with little to no *ex ante* analysis of SME needs. In between those extremes one finds a variety of operations, in a variety of EU countries with no clear pattern overall as regards the reasons for timeliness.

Analysing the different stages of the operations more in detail, reasons for observed lengthiness and, especially, delays, turn out to be varied.

For the period before first disbursement:

- Being a *first time operation* with the intermediary [#13] required considerable time for due diligence and negotiations (this is not a general rule – several other cases were found where first time clients of the Bank went rapidly through this process). Once signed, another delay was caused by the need to set up a dedicated leasing product linked to the EIB funding as well as by the conversion from GL to L4SME. In total more than 2.5 years elapsed from FSA to signature and another year before a first disbursement was made. After disbursement, implementation proceeded swiftly however.
- A *lack of borrower's willingness to take out the loan* after signature, because loan conditions were not to the satisfaction for the intermediary [#7]. The EIB loan became attractive only when the financial and economic climate deteriorated, triggering disbursement requests.
- The *complexity of the operation* [#1], with three different contracts for three different purposes (energy efficiency, municipal finance, SME finance), which moreover would be co-funded by EU funds (which finally did not work out). Adding to the complexity was the establishment of an additional contract with a leasing subsidiary. This meant that signature took a long time. Subsequently, disbursement was delayed because of lack of demand: initially no *ex ante* assessments were made, and for the energy efficiency and municipal components very little interest turned out to exist.
- Negotiation and signature of a *guarantee* by a parent company [#8].

The timeline after disbursement seems to be influenced by two major, partly interrelated, factors: (1) the absorption capacity of the FI itself (translating mainly into the size of the SME loan book and additionality of the loan: the more marginal (in volume terms) the EIB loan on the overall loan book, the higher the absorption rate) and (2) the absorption capacity of the market for SME loans. The following examples can be cited:

- Of the 12 "fastest absorbers" *10 were EU15, the other two were Polish operations*. Interestingly, the Polish FIs were first-time partners for EIB (of which one had had a very long period up to disbursement (see above), the other a relatively short one).
- The remaining 8 operations – "slow(er) absorbers" – were in NMS, in Ireland [#9], France (regional bank [#6]), and Germany [#7]:
    - The German operation [#7] was confronted with *competition in the SME loans* market by the national promotional bank, which slowed down absorption. This was also the operation for which the borrower had delayed the disbursement request (see above). Here, after a long delay Operations conducted an additional analysis and suggested to include a leasing subsidiary as an additional intermediary to speed up the process, and this worked.
    - In NMS, market developments and the *deterioration of the economic and financial climate* slowed down absorption more markedly than in EU15. This turned out to be particularly true in NMS, where on average the borrowers were new, smaller, and more often first-timers than in the EU 15 (e.g. [#1, #2, #3, #15, #16]).
    - The time needed to design a dedicated product with the EIB funds [#6]. Partly related to this, setting up the internal systems to administer the EIB loan in the case of a L4SME (see Section 7.1.4 below).
    - Finally one, relatively *singular*, case [#2] had two main reasons for delay. First, the borrower had assumed it could retro-finance an existing portfolio but was in fact required to generate a new one. Second, EIB funds were used to co-fund a national programme which was funded with EU funds. Implementation of the latter funds was delayed hence the allocation of the EIB funds was also strongly delayed. On top of this the deterioration of the economic climate did not improve absorption.

Slow implementation of the loan triggered allocation extensions in 11 out of the 19 cases studied in-depth. Operations with actual allocation periods within the set limits or shorter were for the bigger loans, mostly disbursed at once, with the bigger banks in EU15 countries having a longstanding track record with the EIB.

Finally, being a GL or a L4SME does not seem to be a distinguishing factor overall (possibly because the sample shows a bias against L4SME). This notwithstanding, several cases were found, also for the "rapid absorbers" [e.g. #5], where the new loan did require more time and effort, especially for setting up internal procedures (see below).

SME level
Through the SME Survey and SME site visits more information was gathered on the timeliness of the loans from the FI to the FBs. The main observations to be drawn from the survey are:

- Timeliness appears "quite important" to "very important" for SMEs, and increasingly so for micro-enterprises (across all operations, roughly three-quarters – or more – of respondents answered that the time span between the funding request and the transfer of funds had been *at least* "rather important" in their decision to sign for financing with the bank or financial institution discussed in the interview. Micro companies (<10 employees) were somewhat more likely than larger SMEs to say that the time span between the funding request and the transfer of funds had been *very important* in their financing decision (43% of "very important" responses for micro companies vs. 36% for SMEs with at least 10 employees).
- Funding was obtained when needed, which implies efficient delivery mechanisms by the FIs. The SMEs surveyed declared that funding had been obtained when needed; across all operations, more than 80% of SMEs reported that the financing was obtained at the right time. The proportion of FBs that answered that the funding had been received later than expected, needed or hoped for remained below 10% for almost all operations. Across most operations, a majority of SMEs reported that the time span between the funding request and the actual transfer of funds was less than one month; the operations that scored best in this area were [#2] and [#15], both promotional banks.
- Longer lead times correlate with larger loans to SMEs, which is no surprise.

7.1.2 Maturity (mis-)match / reutilisation of funds

Maturity matches are an important element to consider from an *ex post* evaluation perspective. First, the relatively higher tenor provided by the Bank is meant to allow FIs to on-lend with higher tenors to SMEs. The previous chapter, discussing effectiveness, shows that tenors have only been marginally increased. Second, the match between the maturity of the EIB loan compared to those of the loans to the SMEs is also an efficiency issue. If the EIB/FI maturity is longer than those of the underlying sub-loans, *and* the funds are used again for the same purpose (i.e. funding of eligible SMEs), the loan can generate *more* effects and becomes *more* efficient than without this re-use. Inversely, when the loan is not reutilised, part of the funds may not serve the purpose the Bank initially intended to pursue. The funds therewith become less efficiently used in view of the Bank's objectives.

Out of the 19 operations 4 had no contractual obligation to reuse funds when underlying loan tenors would be shorter than the EIB loan's tenor.[17] However, in 3 out of those 4 operations there appeared to be no or only a marginal mismatch.

On the remaining 15 operations, which all had such an obligation, for one case, a global loan, the underlying loans' tenors were unknown [#4], and 6 operations had no or only a marginal "maturity mismatch" – even though one FI had anticipated a possible mismatch and had explicitly over-allocated the loan for this purpose [#9]. Of the 8 operations that showed a significant mismatch only 2 had taken steps to reuse the funds. The first [#18] had contacted the EIB in order to discuss how to solve the issue; these discussions were on-going at the time of evaluation. The second [#5], where lending and on-lending tenors differed by a factor 2 (respectively 12 and 6 years on average) had proposed a direct reuse of the loan up to the same amount as the original loan. The advantage for this FI was administrative (i.e. not having to come back to this operation in 6 years' time) whereas it also reduces credit risk. For the EIB, the importance is that this loan will be fully rolled over and has therefore the

[17] In three out of those four cases, however, funds from prepaid (not *re*paid) loans, i.e. before their initial end term, would have to be used with the same eligibility criteria.

potential to be twice as effective and twice as efficient. Alternatively, and depending on *local SME needs*, the Bank could encourage longer on-lending tenors *per se* rather than reuse, or make sure that tenors better reflect the expected lifetime of underlying assets.

For the operations in the sample, the contractual clauses relative to reuse of funds appeared not standardised and a variety of formulations were encountered. These formulations also were not always fully transparent or understandable for the Borrower – the difficulty some had in distinguishing prepaid (i.e. before the term) from repaid (at the term) is an example. More generally, the importance of reuse appeared only weakly acknowledged on the side of the Borrowers, given the low number that had given it a thought. Even though in many of those cases loans had not been repaid yet, this is an issue that should be tackled early on, as shown by the example of the direct reuse proposed, and accepted by the Bank, under operation [#5]. The Banks' services have informed EV that during the course of the evaluation an effort to harmonise the L4SME practises in this field, and related contractual wording was launched between the operational and legal services of the Bank.

7.1.3 Cost-effectiveness

Cost-effectiveness for FI

Out of the 19 operations, 15 FIs found the operation cost-effective. The four remaining operations were only found moderately cost-effective by the respective FIs. Two of those were with promotional banks [#2, #16], one of which on-lent to a second layer of intermediary banks, which then made allocations to SMEs; funding benefits were passed on directly to those on-lending banks. One operation was partly cancelled, therewith lowering its efficiency. The fourth operation was the one referred to above, with a very long timeline both before and after disbursement.

As effectiveness was discussed in the previous chapter, below some more emphasis on the different *cost* elements for the FIs will be provided.

In terms of human resources dedicated to the implementation of the loan, in several cases an initial effort was made. This was especially so when it was the first time the FI worked with the Bank; when it was the first time a L4SME was implemented; or when a new product was designed and implemented with the EIB SME funds. The exact amounts of staff involved are generally not tracked by FIs and, during the interviews, appeared not always easy to estimate. Such estimates ranged from 100 person-days of preparatory input (one-off) to "marginal" efforts. Several FIs expect this initial investment to be amortised over time, when they would obtain new L4SMEs from the EIB. In one case [#19] the FI expected that the loan would not be followed up thereby making the current loan (which furthermore was not going to be fully disbursed) less cost-effective for this FI given the initial efforts put in.

Adaptation of IT by FIs

10 FIs [#5 #6 #8 #9 #11 #13 #14 #15 #19 #20] adapted their IT or developed dedicated IT solutions to administer the EIB loan for which specific training on the EIB loan was systematically provided to their staff. In the cases where there was an IT solution the collection of allocations at the level of the SMEs was performed automatically whereas in the other cases this was still done manually, HQ-centralised. Those cases were not the ones that claimed that the administrative burden was too high – however it might be that the efforts were simply less visible than in the case when an identifiable and separately costed IT project was set up to implement the EIB loan.

The resources required at "cruising speed", i.e. to implement the loan after initial preparation, were also difficult to estimate for the FIs. Such efforts were mainly linked to the allocation process (most often carried out by FI HQ and/or automatically through an IT solution) and to client managers to explain the EIB loan (including its benefits and the additional contractual clauses in the case of L4SME) to SME clients. Based on headcounts, this ranged from 30 person-days per year, to, again, "marginal additional efforts" when no or only few changes had been made to FIs' internal procedures and routines.

Whereas the majority acknowledged that implementing the EIB loan represented an additional administrative burden, only in 5 out of the 19 cases evaluated this was deemed to be substantial by the FI. Four of these ([#5, #6, #14, #19]) had put in place new procedures or products, implemented dedicated IT solutions and had provided training to their staff about the EIB loan implementation. The fifth FI [#2] found the administration of the loan cumbersome, because it recorded allocations manually in EIB spread-sheets, which were themselves judged as "cumbersome".

In several cases there was a direct financial cost involved for the FIs, linked to the establishment of guarantees, collateral, assignment-of-rights issues or setting up of an Asset Backed Securities (ABS) structure. It appeared difficult to estimate the precise costs of those.

As part of the efficiency assessment, the overall efficiency of the intermediaries was assessed and for each case compared to a peer group. Most of the FI's were similar to their peers, slightly below or slightly above. In the case of the promotional banks, moreover, this was difficult to assess due to their specific mission. The result of this assessment is that there does not seem to be a direct link between the overall efficiency of the FI as measured by indicators (such as cost-to-income ratios) and the cost-effectiveness of the operation, in terms of the efforts made by the FI. Rather the opposite: the more efficient intermediaries overall seem to have taken the opportunity to make a greater initial investment to implement, notably, the L4SME, in view of an expected more efficient implementation of future loans. This rests on the assumption that EIB requirements remain relatively stable in the future and do not radically alter.

Cost-effectiveness for FB
Across all operations, the SMEs replied generally that no specific efforts had to be made to apply for "EIB loans" in comparison to other loans.

However, a large variation was observed across operations in the proportion of SMEs that had paid closing, contract or legal fees to receive the financing (from 15% [#11] to 100% for [#15]). The payment of fees was more common for EIB funded loan agreements than for lease agreements (57% *vs*. 25%). However, in the majority of the cases such fees were found reasonable in comparison to other (but similar) loans or leases even though almost a quarter answered that the fees had been higher. Virtually none of the SMEs surveyed stated that the fees to receive the EIB funded loan or lease had been lower than those for other loans/leases.

Overall however, in view of the benefits that came with the loan (in terms of availability of funding, timeliness and interest rate – the most important factor in their financing decision), the majority of SMEs found the loan to be cost-effective.

7.1.4 Management structures and reporting

In only 5 cases [#5, #7, #13, #19, #20] it can be said that dedicated procedures and structures existed or were put in place beyond the FIs' standard procedures (this excludes the adaptations of the loan contract to account for the EIB funding which was compulsory for all L4SMEs and converted operations and which necessarily had an impact on the FIs internal procedures as contracts were adapted and needed to be explained to clients). In two of those cases [#7, #13] there was a specific unit within the FI to deal with EIB and similar sources of funding. For operation [#20], a specific unit was established to administer the available pool for the cash-back. In the two remaining cases specific responsibilities and routines were put in place to administer the EIB loan internally, often with additional IT applications discussed above. There does not seem to be a link between the performance of an operation and the establishment of dedicated management structures at FI level.

Finally, at face value, all reporting was compliant with EIB requirements. This is not surprising as reporting is contractual and EIB exerts control to make sure that reports are complete and delivered on time. However, in some cases, upon closer inspection, the data provided by FIs appeared to be incorrect or only approximate. This was especially so in relation to employee figures [#11, #12], loan characteristics such as tenor and ToFA [#19, #20] or sector information [#20]. Conversely, for some operations the FIs provided *more* information than necessary when they did not use the L4SME *simplified* reporting procedure for enterprises below 10 employees and amounts below 40k [#6, #15, #16]. Interviews with CAU staff suggest that often FIs send much more information than required (e.g. on job creation) which is not used and therefore leads to inefficiencies on the side of the FI (for having collected it) and the Bank (for having to sort the data). In the case of converted loans (GL => L4SME) or the longer lasting operations [#7 in particular] reporting requirements changed over time and FIs had to adapt.

As indicated above, several FIs found reporting and data-communication in its present form cumbersome and suggested the EIB develop a more automated, perhaps web-based, system for this.

Overall, and maybe because these were the first series of L4SMEs, reporting simplification had not yet led to the desired result. This will be further discussed under Section 11 (EIB Project Cycle Management).

7.2 Conclusions

7.2.1 Timeliness is variable and absorption capacity of the market *and the FI* are important factors

The timeliness of operations varies greatly and observed delays had a variety of explanations. Before disbursement, this could be linked to being a first time client (though this is not a general rule); to a low initial FVA (see EIB contribution) meaning that drawdown was delayed until conditions improved for the FI; to the complexity of an operation; or the negotiation of a guarantee. Timelines after disbursement are influenced by two main factors, namely the FI's absorption capacity and the absorption capacity of the market. Whereas especially in times of crisis absorption capacity may not always have been straightforward to estimate, based on the FIs track record, absorption capacity in several cases could have been better anticipated. Slow implementation of the loan triggered allocation extensions in 11 out of the 19 operations evaluated. At the level of the FBs, timeliness was said to be an important factor by SME respondents. In the perception of SMEs, funding was generally obtained rapidly, at the right time, with only short time periods between request and disbursement. This implies that efficient delivery mechanisms existed on the FI side.

7.2.2 Maturity mismatches existed, sometimes significant

Maturity mismatches can become an efficiency issue when EIB tenors are much longer than FIs' tenors in their loans to SMEs, without funds flowing back being used again for the same purpose.

Three quarters of the operations in the sample had a contractual obligation to reuse funds if underlying loan tenors would be shorter than the EIB loan's tenor. Of these, out of the 8 FIs with operations that showed a significant mismatch only 2 had taken steps to remediate this when the evaluation was carried out (2012). One of those two FIs had, at its own initiative, proposed a mechanism for *entirely* reusing the loan, therewith doubling at least its volume effect. For the operations that had not yet reflected on reuse, it turned out that contractual clauses were not always fully clear. These clauses visibly deserve more clarity and explicit language, better explanation from the side of EIB services and enforcement. The Banks' services have informed EV that during the course of the evaluation an effort to harmonise the L4SME practises in this field, and related contractual wording was launched between the operational and legal services of the Bank.

7.2.3 Operational costs for some FIs significant, but not more than for any other new product

Out of the 19 operations, 15 FIs found the operation cost-effective for them. Of the moderately cost-effective operations, two were with promotional banks [#2, #16], one of which had an on-lending structure to a second layer of intermediary banks. For 10 operations in the sample, FIs adapted their IT and sometimes developed dedicated IT solutions. FIs appeared to invest additional efforts in the operation especially when it was the first time they worked with the Bank; when it was the first time they implemented a L4SME; or when a new product was designed and implemented with the EIB SME funds. The exact amounts of FTE involved are difficult to establish but seem to vary widely between FIs. At "cruising speed", i.e. to implement the loan after initial preparation, additional efforts were mainly linked to the allocation process (most often handled by FI HQ and/or automatically through an IT solution) and to client managers to explain the EIB loan. Whereas the majority acknowledged that implementing the EIB loan represented an administrative effort, only in 5 out of the 19 cases evaluated this was deemed to be substantial, yet comparable to the launch of a new product more generally.

FBs generally reported that they made no extra (e.g. admin) efforts for the implementation of the loan. A large variation was observed in the proportion of SMEs per operation that had paid some sort of fees. Overall, however, these were deemed reasonable.

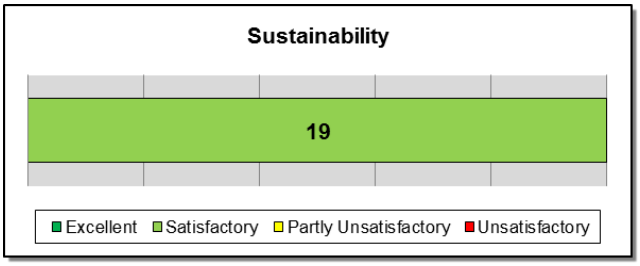
7.2.4 In a quarter of the cases dedicated management structures were put in place

For only a quarter of operations dedicated procedures were established to implement the loan that went beyond the FI's standard procedures, in three cases even leading to a small unit administering the EIB loan (in one case the cash-back). Reporting was overall compliant yet variable, as certain types of data were at times approximate or inaccurate, e.g. on SME employee figures and sector, and tenor and ToFA (for which systematically the same value is often provided whereas in reality more variety exists).

8 SUSTAINABILITY

The sustainability criterion considers the probability that resources will be sufficient to maintain the outcome achieved by the operation. It is assessed at the level of the financial intermediary (both technical/institutional and financial) and of the final beneficiary SMEs. Economic, environmental and social sustainability are discussed in a separate subsection.

8.1 Evaluation results



All operations in the sample obtained a *satisfactory* rating for sustainability. Given the difficult economic and financial context for financial intermediaries and final beneficiaries, this is a remarkably positive result. It can be explained by the careful selection of intermediaries by the Bank. The FIs in the sample all have, to different degrees, systems, operational targets and sometimes longer term plans in place to continue or increase SME lending. At final beneficiary level, the relatively good sustainability is explained by the fact that for the majority of operations the EIB SME Portfolios financed by the FIs are generally of better credit quality than the FIs' comparable overall SME portfolios. Correspondingly, the level of NPLs among the beneficiary SMEs is virtually nil, whereas for many FIs NPLs in general rather increased over the past years.

Although some FIs seem to have had their "worst" moments, the financial and economic context in most EU27 countries is still weak and supply and demand for SME lending have stagnated if not deteriorated. For a majority of operations, FIs were rated downward by rating agencies over the period of concern. This notwithstanding, the majority continues to have acceptable financials as compared to their peers and good market positions. In some cases SME lending may be curtailed in the future due to shortages on the funding side. Moreover, Basel III is expected to have a negative impact on lending to smaller, riskier SMEs, which are already not well served by EIB loans.

8.1.1 Financial Intermediaries

Operational and institutional sustainability
Without exception, for all FIs in the sample, SMEs are a clear and explicit priority. On the one hand, SMEs have gained increasing interest as a client group since the mid-1990s and SMEs having become a priority as part of a broader trend. However, with the crisis, the deterioration of SME finance has been commonly acknowledged and several FIs [e.g. #4, #5, #6, #9, #11, #14, #15, #20] have publicly engaged in maintaining or increasing SME funding through agreements with their respective governments. This includes setting concrete targets for SME lending (e.g. France, Ireland) or participating in government programmes (e.g. Spain).

This SME priority was translated into strategic plans and orientations [#6, #7, #17/18, #20]; specific SME products [#13]; internal procedures, training and assigned responsibilities (see Section 7.1.3); specific subsidiaries with a strong or exclusive focus on SME lending or, more often, leasing [#3, #8, #12, #11]; or significant recent increases in SME lending *per se* [#9, #14]. For the three promotional banks in the sample SME lending is a government priority. In one of those three cases it is expected that the increasing EU emphasis on financial engineering (with initiatives such as JEREMIE and JESSICA) would contribute to this institution's operational sustainability [#2].

An interesting example of indirect institutional sustainability of EIB lending was cited under [#8], where the national promotional bank (itself not funded by the EIB) is reflecting on setting up credit lines along structures and principles (intermediated lending) similar to those of the EIB. This may further decrease the need for EIB funding in this country, where EIB is already not very active in SME lending, precisely due to the existence of this promotional bank. However, the EIB setting an example which finds a follow-up would typically be a sustained effect of EIB activity.

Financial sustainability
Making reliable forecasts is in itself a difficult task. For the present evaluation making sound statements on the financial sustainability of the operations was moreover complicated given the current financial and economic situation within the EU27. The majority of FIs in the sample have been rated downward by rating agencies in recent years, sometimes several times and several notches, sometimes as the evaluation was on-going. Some seem to have started to recover [#8, #9, #20], regaining a positive outlook recently or increasing again SME lending. The crisis hit on both sides of the balance sheet: on the one hand loan books have worsened, with an increasing amount of NPLs in general and an uncertain evolution of demand for SME finance on the short term. As a result, generally FIs have become stricter on credit risk in general and for SMEs in particular. On the other hand medium and long term funding has become tighter, making, in turn, EIB MLT financing more relevant, as discussed above.

Most FIs have seen their SME lending markets shrink in recent times in absolute terms. In spite of this evolution about one-third maintained high market shares in SME lending or even increased their market share [#3, #9, #14, #15, #16]. A minority of FIs in the sample recently saw a decrease in market share of their SME lending. For only two countries covered by the sample (Germany and Poland) the FIs considered the demand for SME finance relatively stable in the future, whereas the remainder expected slowdowns or at least deemed it uncertain.

Several FIs pointed out that Basel III capital requirements, gradually implemented as from 2014, will impact their SME lending. This is a finding generally acknowledged by the literature.[18] SMEs are perceived as higher risk and less attractive in terms of income. Depending on the behaviour of lenders, Basel III is expected to lead to credit pricing, credit rationing or both, especially with regard to SMEs.

Finally, SME lending through blending, albeit very marginal as compared to total SME lending volumes, may see an increase in the coming EU programming period (2014-2020). This change has possibly been reinforced by the insight that loans seem to have a higher impact than grants, for which initial evidence has recently been found in a large counterfactual study published by EC DG REGIO.[19]

8.1.2 Final Beneficiaries (SMEs)

Sustainability of the final beneficiaries was approached in four ways: (1) through the information obtained from the FIs on the risk profile of the financed SMEs, (2) through the performance and prospects of the visited SMEs, (3) through the propensity of financed SMEs to seek and, as per their own saying, obtain more finance in the near future and (4) by combining different impacts, as measured by the survey, which would improve the sustainability of individual companies.

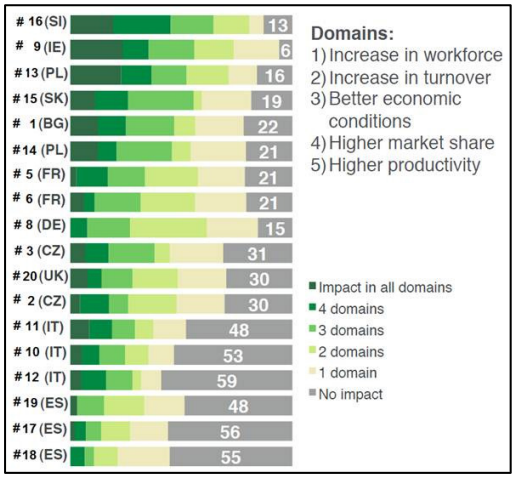
Information obtained from FIs already cited in the Effectiveness chapter suggests that SMEs financed under the EIB loan generally had a better risk profile than the comparable SME portfolios overall, which can be explained by the characteristics of the EIB loans (Section 6.1.2). Most importantly, the profile of the EIB portfolio remained in most cases stable over time or even improved, whereas the overall risk profile of the FIs' SME portfolios deteriorated in recent years. The EIB loan typically leads to risk-averse selection, meaning that the underlying companies can be expected to be more sustainable than the average. This is an important evaluation finding which should be taken into consideration as and when the Bank designs new policies and tools.

[18] E.g. Association of Chartered Certified Accountants (ACCA), 2011, Framing the debate: Basel III and SMEs, London; ACCA.
[19] Daniel Mouqué, 2012, What are counterfactual impact evaluations teaching us about enterprise and innovation support? Brussels: DG REGIO.

This is confirmed by the site visits and interviews (of companies, it is recalled, which were not selected by the FIs but randomly by EV), which generally showed healthy companies with sustained past growth patterns and good prospects – even though there were differences between countries.

The survey shows that more than one-third of all companies interviewed planned to apply for external finance (mainly loans or leases) in the six months following the interview; for companies above 50 employees this was even one out of two, showing a great short-term need for financing. Moreover, roughly 4 in 10 SMEs deemed they would actually obtain requested finance in the future and again the larger companies score higher in this regard. This can be taken as a proxy for the expectation on sustained activity of those companies. One in five SMEs identified the tightening of credit supply from banks as the main factor that would limit their ability to attract financing, while 17% cited interest rates that could be seen as being too high and therewith possibly slowing down investments. SMEs in Ireland, the UK, Spain, Slovakia and Slovenia were the most likely to state that the tightening of the credit supply from banks would be the most important obstacle to receive financing in the near future.

Finally, a way in which sustainability was approached was by analysing the frequency by which certain impacts on the company would occur *simultaneously* in the survey. Those were increase in workforce, increase in turnover, better economic conditions, higher market share and higher productivity. As these elements impact the way a business operates on a daily basis, they are expected to contribute positively to an SME's sustainability. The higher the number of impacts occurring together, the higher the expected sustainability of the underlying companies. The result for the different operations is given on the right.



This analysis shows that the 6 operations scoring lowest on combined impact – and which are therefore also deemed to be the least sustainable – all are situated in Italy and Spain. This would correspond quite well with the general economic situation in those countries. Additional analysis shows that the country factor is statistically indeed the most important predictor in this analysis. Another way to interpret those results is that, rather than leading to additional impacts on those companies, the loan was used to keep companies afloat which might not have resisted the present crisis circumstances in those countries. However, for the latter point there is only limited evidence through the SME Survey. The 7th operation from the bottom is with a promotional bank which provides subordinated loans to companies which otherwise would not have obtained funding at all, and therefore can be deemed non-sustainable without EIB intervention.

On the basis of the available evidence, the SMEs financed under EIB loans are generally deemed sustainable, however, major differences between countries exist, and the country factor is statistically the most important predictor for impact. Those effects are presently exacerbated by the economic and financial crisis.

8.1.3 Economic, environmental and social sustainability

Economic sustainability

It is outside the scope of the evaluation to make a full-fledged analysis of the economic impact of the sample operations beyond the impact on the SMEs *per se* (e.g. effects on suppliers or clients of those SMEs). However, in the case of, especially, the high volume operations which had a positive effect on growth and employment or on the maintenance thereof, and given that the SMEs in the "EIB portfolios" financed by the FIs were often of better quality than the FIs portfolios overall, one would expect those operations to have yielded sustainable economic effects. This is indeed the picture that emerges from both the visits to individual SMEs and the SME Survey.

Environmental and social sustainability
FIs were contractually bound to comply with EU and national environmental legislation. Side letters covered a series of standard restrictions in this regard as well as an obligation for the borrower to see to it that final beneficiaries would respect national and EU environmental regulation, especially with regard to nature zones. However, no specific controls on this were carried out by the Bank and often also not by the FIs' front office staff – notable exceptions being for instance [#6, #7]. The general hypothesis is that, operating within a EU environment, companies benefiting from the loan would generally comply with environmental legislation. Only one FI however assessed SMEs' environmental and social sustainability [#7].

FIs themselves increasingly implement environmental and social responsibility policies, including some form of rating or accreditation such as the FTSE4 Good and ASPI indexes, EU Eco-Management and Audit Scheme guidelines (EMAS), SAM (Sustainability Asset Management), a Dow Jones index for sustainable development, etc. This testifies of a growing concern for environmental, social and sustainable development issues.

Whereas there does not seem to be explicit control by FIs on whether the investments made by SMEs through loans are compliant, for leasing there is an incentive to consider this more closely, for two reasons. On the one hand, the equipment from the vendors is generally expected to respond to the latest technical standards and therefore also respond to high environmental quality standards. This is generally confirmed by the SME visits. On the other hand, leasing companies appeared to pay close attention to the evolution of environmental legislation because changes in regulation may impact on resale prices at the end of the lease term, when environmental regulation becomes more stringent and therefore be a factor in choosing the moment of replacement of the old equipment. The incentive to incorporate environmental sustainability considerations seems to be naturally higher for leasing than for lending.

Despite some site visits during which it was felt that the environmental and social (health especially) standing of companies could be improved, some comfort exists that the beneficiary SMEs and the investments they have made are overall environmentally and socially sustainable. In light of the fact that but for one exception FIs do not review or assess the environmental and social dimension of their SME client, some exposure, including for reputational risk, exists for the EIB.

8.2 Conclusions

Assessing sustainability of the operations, in terms of the sustainability of the FIs and of the impacts of the operations on the SMEs and beyond is generally difficult, but even harder for this evaluation which was carried out in a period of crisis of which it is unclear how and when the EU will recover.

On the basis of the evidence gathered during this evaluation the institutional and technical sustainability of the FIs' SME lending is deemed satisfactory. The FIs in the sample all have, to different degrees, systems, operational targets and sometimes longer term plans in place to continue or increase SME lending.

Making sound statements on the financial sustainability of the operations is more complicated given the current financial and economic situation within the EU27. The majority of FIs in the sample have been down-rated in recent years, often several times and by several notches. Even during the drafting of the present synthesis report this process continued, with several FIs of the sample experiencing reduced financial performance for 2012 and implementing major cost cutting plans. Although some start to recover, most FIs in the sample have seen their SME lending markets shrink in recent times in absolute terms – even if about one-third maintained high market shares and some even increased it. The evolution of the SME lending market is highly volatile. On the longer term, Basel III capital requirements, gradually implemented as from 2014, may also impact negatively on SME lending as SMEs are perceived as higher risk and less attractive in terms of income.

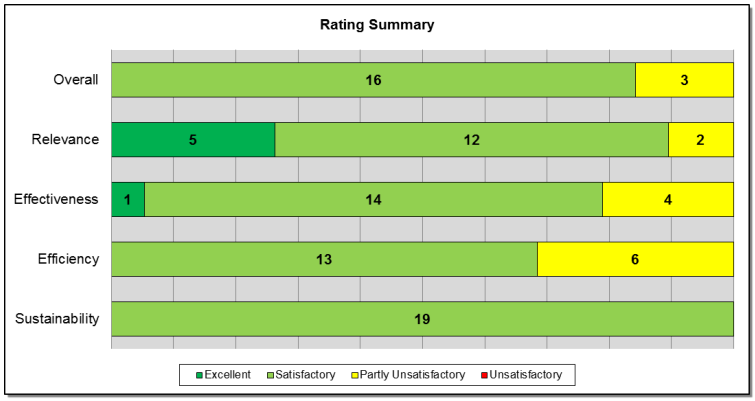
On the other hand, the final beneficiaries that were served by the EIB loans appear to be relatively sustainable. This is explained by the fact that for the majority of operations the EIB SME Portfolios financed by the FIs are generally of better credit quality than the FIs' comparable overall SME portfolios. Correspondingly, the level of NPLs among the beneficiary SMEs is virtually nil, in stark contrast with the increase of SME NPLs in general in the portfolios of the intermediary banks. This is

an important evaluation finding which should be taken into consideration as and when the Bank designs new policies and tools.

Although it is difficult to provide hard evidence, based on the SME profiles and the impact on growth and employment of the operations, investments made with the support of EIB funding are expected to be economically sustainable. Great differences between countries continue to exist however.

While difficult to ascertain ex post given the sheer size of some of the operations, it is expected that some yielded sustainable economic effects. This is indeed the picture that emerges from both the site visits and the SME Survey. Finally, some comfort exists that the beneficiary SMEs and the investments they have made are overall environmentally and socially sustainable; however, some exposure, including for reputational risk, still exists for the EIB.

9 RATING SUMMARY AND OVERALL RATINGS



The overall ratings for the 19 operations evaluated in-depth were satisfactory for 16 operations and partly unsatisfactory for 3 operations. The "partly unsatisfactory" overall ratings were due in two cases to partly unsatisfactory effectiveness and efficiency of operations; in the third case it was due to partly unsatisfactory relevance and efficiency. The latter concerned an operation in Germany for which time to disbursement and allocation were extremely long due to initially low interest for the loan by the borrower and subsequently a very low absorption capacity. EIB's intervention toward SMEs in this country is generally less relevant due to the presence of KfW which traditionally guarantees a good and attractive supply of SME finance.

Relevance

Operations showed a high consistency with EU and EIB objectives and their evolution over time – taking due account of the EU crisis response and the EIB's subsequent increase in lending volumes. The increased focus that the Bank has given to SMEs in the past was also in line with policy evolutions in EU Member States, which in fact to a great extent reflect EU priorities.

Even if the L4SME product was designed before the crisis, its broad scope made it more relevant even when access to finance for SMEs deteriorated. Converting existing GLs into L4SMEs was the right choice.

However, the Bank's intermediate objectives ("providing finance at improved conditions" and "improving access to finance") as well as their relation to the global objectives of growth and employment need further clarification. Moreover, in order to increase relevance, the assessment of whether or not a given Member State has ready access to finance for SMEs should have been a systematic ingredient in the rationale for an EIB intervention and therefore normally be part of the appraisal process. This was often not the case. In the few cases where ex ante assessments of SMEs funding needs and the potential complementarity of the EIB product level were undertaken, the effectiveness and efficiency of the operations were already noticeably better. Country context appeared by far the strongest predictor of SME impact (competitiveness, growth, and employment), highlighting how critical it is for SME interventions to reflect the needs of the national SME markets.

Effectiveness

The L4SME says what it does and does what it says
In sharp contrast with the former GL where often it was unclear how much of the EIB advantage ultimately benefited SMEs (and how much went to FIs' balance sheets), the contractual ToFA and

stringent transparency conditions of the L4SME product have clearly contributed to providing a higher level of comfort that a financial advantage was indeed passed on to SMEs. Under the EIB loan, FIs provide loans at improved conditions (mainly bps, often also tenor) as compared to their overall SME loan book. Contractual advantages are generally passed on and contractual ToFA is often even exceeded. Tenor appeared equal or only slightly higher as compared to FIs SME portfolios' tenors overall or compared to what the survey respondents tended to obtain. Only a few operations used the EIB funds to on-lend at *substantially* longer tenors than they normally do for this target group.

A quarter of SMEs surveyed explicitly stated that interest rate was more advantageous as compared to competitors. More importantly, about 80% of SMEs had asked for several quotes before preferring the EIB funded offer, which suggests that the EIB loan increased competition. SMEs overall appear satisfied with the provided tenor, volume and timeliness.

Several operations had a visible impact on growth and employment – all but one in EU12 (NMS). Nearly half of the SMEs reported the financing had triggered positive effects on productivity, market share development or the general economic health of their business. The survey results suggest that on average about one job per financed SME per operation was created. The economic impact of EIB lending is likely to be higher for small (10 to 49 employees) but not micro firms and for relatively young (2 to 5 years) but not the youngest firms. Firms having introduced innovations or that used the funds for research and development show a relatively higher impact.

EIB intermediated SME loans generally serve larger and less risky firms as compared to FI SME portfolios
For a variety of reasons (broad scope of EIB SME lending, EIB not sharing risk, long tenors, volatile markets, FI reputational risk), the FIs generally tend to choose larger and less risky SMEs to be financed under the EIB loan in comparison to their overall eligible SME portfolios. Whereas EIB operations contributed to fund SMEs at (measurably) better conditions, there is strong evidence that those SMEs were often also those most likely to obtain funding anyway. Overall, the proportion of smaller and younger firms in the EIB portfolios financed by the FIs decreased over time. As a consequence, EIB intermediated SME loans do not primarily seem to improve access to finance for SMEs which are underserved by banks due to their inadequate risk profile. The exceptions are operations carried out within the framework of national programmes, implemented by, for instance, promotional banks.

FIs do not fully use the range of options provided under the L4SMEs
The L4SME product broadened eligibility criteria in comparison to the earlier GL, including especially working capital for a minimum duration of 2 years. FIs seem to use these possibilities only marginally, for a variety of reasons: not being adapted to the regional context, existence of national programmes for working capital funding especially during the crisis and the 2 year tenor being considered too long for working capital. Some FIs that were used to working with the EIB hesitated to broaden the scope, not being fully confident about the eligibility; this reluctance may have been reinforced by the fact that contractual definitions at EIB side took some time to stabilise.

Visibility and transparency make a difference
Visibility requirements make SMEs aware of the possibilities of obtaining better funding. Even if EIB visibility has improved over time – awareness of EIB involvement doubling from L4SME to GL – a considerable number of FBs were not aware that the financing originated from the EIB. There is still room for improvement on this point, e.g. by improving the flow of information between stakeholders at large, and with FIs and SMEs.

FIs with smaller SME portfolios have more difficulties complying with the additionality requirement
Although the additionality requirement (which, in short, states that the FI's MLT SME financing has been at least as much as that of the EIB Loan for SMEs) was respected across the sample, it is more difficult to fulfil for FIs with smaller SME portfolios – meaning probably that in such cases their absorption capacity was initially overestimated. For larger FIs on the other hand, which form the majority of the sample, fulfilling the requirement is easy as the EIB funding is marginal on their overall eligible portfolio; the requirement in such cases becomes a formality and is not a meaningful measurement of additionality.

Therefore, in order to avoid confusion with generally accepted definitions, the term "additionality" used in the contractual documentation could be replaced by a more appropriate term.

Efficiency

Timeliness is variable; absorption capacity of the market and the FI are important factors
The timeliness of operations showed great variation and observed delays had a variety of explanations. Before disbursement, this could be linked to being a first time client (though this is not a general rule); to a low initial FVA (see EIB contribution) meaning that drawdown was delayed until conditions improved for the FI; to the complexity of an operation; or the negotiation of a guarantee. Timelines after disbursement are influenced by two main factors, namely the FI's absorption capacity and the absorption capacity of the market. Whereas especially in times of crisis absorption capacity may not always have been straightforward to estimate, based on the FIs track record, absorption capacity in several cases could have been better anticipated. Slow implementation of the loan triggered allocation extensions in 11 out of the 19 operations evaluated.

Maturity mismatches existed, sometimes significant
Three quarters of operations in the sample had a contractual obligation to reuse funds if underlying loan tenors would be shorter than the EIB loan's tenor. Of these, out of the 8 FIs with operations that showed a significant mismatch only 2 had taken steps to remediate this. One of those two FIs had, at its own initiative, proposed a mechanism for *entirely* reusing the loan, therewith doubling at least its volume effect. For several operations that had not yet reflected on reuse, it turned out that contractual clauses were not fully clear. These clauses visibly deserve more clarity and explicit language, better explanation from the side of EIB services and enforcement. The Banks' services have informed EV that during the course of the evaluation an effort to harmonise the L4SME practises in this field, and related contractual wording was launched between the operational and legal services of the Bank.

Operational costs for some FIs considerable, but not more than for any other new product
The large majority of FIs found the operation cost-effective for them. On the moderately cost-effective operations, one was with a promotional bank having an on-lending structure to a second layer of intermediary banks which decreased overall efficiency. For more than half of the operations, FIs adapted their IT or developed dedicated IT solutions. In a few cases dedicated management structures were put in place such as a special unit to administer the EIB loan. Such additional efforts were made when it was the first time they worked with the Bank; when it was the first time they implemented a L4SME; or when a new product was designed and implemented on the basis of the EIB SME funds. Whereas the majority acknowledged that implementing the EIB loan represented an additional administrative burden, only one quarter deemed this to be substantial, yet comparable to the launch of a new product more generally.

SMEs deemed cost and administrative efforts associated with their loans reasonable.

Sustainability

Assessing sustainability of the operations, in terms of the sustainability of the FIs and of the impacts of the operations on the SMEs and beyond is generally difficult to assess, but even harder for this evaluation which was carried out in a period of crisis.

Institutional and technical sustainability of the FIs' SME lending is deemed satisfactory. The FIs in the sample all have, to different degrees, systems, operational targets and sometimes longer term plans in place to continue or increase SME lending.

Making sound statements on the financial sustainability of the operations is more complicated given the current financial and economic situation within the EU27. The majority of FIs in the sample have been rated downward in recent years, often several times and several notches in total; during the drafting of the present synthesis report this process went on. Several sample FIs saw strongly reduced benefits for 2012 and implementing major cost cutting plans in order to survive. Although some FIs start to recover, SME lending markets shrunk even if about one-third of FIs maintained high market shares and some even increased it. In the longer term, Basel III capital requirements, gradually implemented as from 2014, may also impact negatively on SME lending as SMEs are perceived as higher risk and less attractive in terms of income. The evolution of the SME lending market is by most seen as still uncertain.

The final beneficiaries served by the loan appear to be relatively sustainable. This is explained by the fact that for the majority of operations the EIB SME Portfolios financed by the FIs are generally of better quality than the FIs' comparable overall portfolios. Correspondingly, the level of NPLs among the beneficiary SMEs is virtually nil, in stark contrast with the increase of SME NPLs in general in the portfolios of the intermediary banks.

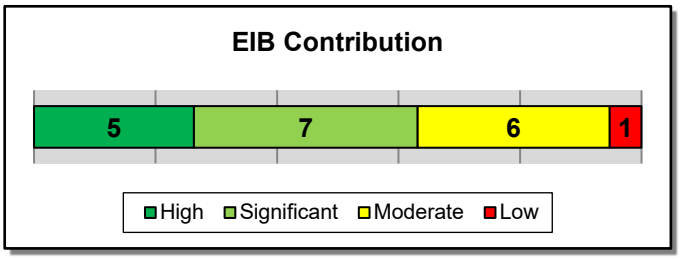
Although it is difficult to provide hard evidence, it is, again on the basis of the SME profiles and the impact of growth and employment of the operations, expected that investments made with the help of EIB funding are economically sustainable. Great differences between countries exist however.
While difficult to ascertain ex post given the sheer size of some of the operations, it is expected that some yielded sustainable economic effects. This is indeed the picture that emerges from both the site visits and the SME Survey. Finally, some comfort exists that the beneficiary SMEs and the investments they have made are overall environmentally and socially sustainable; however, some reputational risk still exists for the EIB.

10 EIB CONTRIBUTION

The EIB contribution section identifies the financial and non-financial value added (including financial facilitation) provided in relation to the alternatives available, including improvements on financial aspects. To evaluate EIB contribution, EV started out from the third pillar of the value added methodology applied to the operations sampled at the time of their appraisal. This analysis was enriched with complementary elements as explained whenever relevant throughout this section.

10.1 Evaluation results

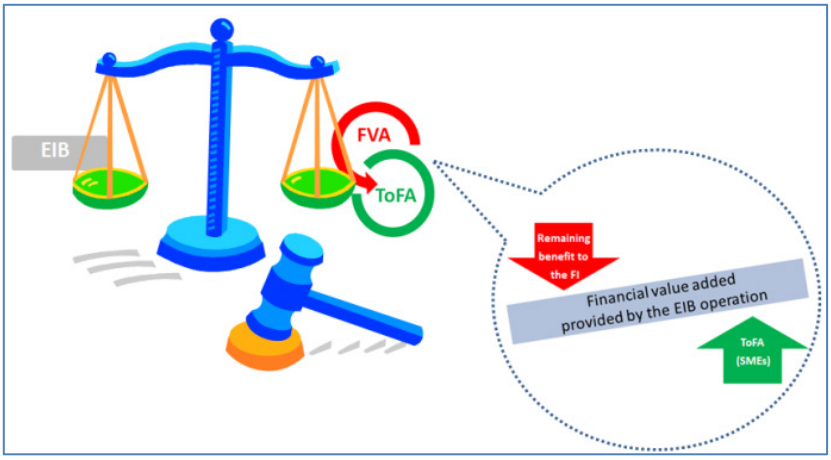
The assigned *ex post* ratings for EIB Contribution span the available spectrum from "High" to "Low". Overall ratings for EIB contribution were arrived at by combining the findings for financial contribution and non-financial contribution.



The 5 operations with a high EIB contribution [#8, #14, #15, #16, and #18] are all L4SME operations implemented after 2008. All operations are the first L4SMEs ever implemented by the FIs, of which only two had prior experience of EIB SME intermediated lending operations. On the three promotional banks, two obtained the highest ratings. All GL operations have an overall moderate EIB contribution [#2, #4, #17]. The operation ranking low [#7] was a converted operation.

Differences in the ratings for EIB contribution are driven largely by differences in the Bank's financial contribution, and not by non-financial value added. Only for one operation in the sample it was deemed that the Bank had a high non-financial contribution [#16].

10.1.1 Financial contribution



The Bank's AAA credit rating enables it to raise funding at advantageous conditions. This funding advantage is passed on to FIs (Financial Value Added, FVA) with the aim, ultimately, to partly or totally transfer it to SMEs (Transfer of Financial Advantage, ToFA). However, to preserve its strong credit rating, the Bank must adequately price its operations and keep a share of the potential financing advantage. Finding the right balance between the three elements is a constant concern. The share of FVA and ToFA are interrelated: for a given FVA, the higher the ToFA, the lower the remaining benefit

to the FI. The ToFA is not the only benefit provided by the Bank. The volume extended by the EIB, and the advantageous tenors are also valued by FIs and SMEs.

As a complement to the Bank's VA methodology, the present evaluation took into account, insofar as possible, not only the *ex-ante* expected FVA (as assessed by the Bank), but also the actual FVA at signature and disbursements. The evaluation furthermore considered, in the case of contractually committed ToFA (L4SMEs), the evolution during implementation, including at disbursement and at the time of evaluation. While available data quality varied across the 19 operations, this dynamic aspect gave some insights into the FIs pricing behavior to SMEs in light of market volatility. It also illustrated how aspects of the operational cycle, including during the appraisal process, can have an immediate impact on the EIB's outreach capacity and ultimately contribution to SMEs.

In view of the objectives of EIB intermediated lending to SMEs, operations with relatively higher ToFA obtained better assessments for EIB contribution in the present evaluation.

Overall, the financial contribution of the EIB is assessed as positive, generating, in most cases, a positive FVA for the FIs, a transfer of ToFA to SMEs, positive outcomes in view of the long tenors extended and, occasionally, of the volume extended.

Being a historical partner of the EIB for SME funding is no explanatory factor for the importance of the EIB contribution. The size of an operation is not a determining factor either. The discriminating factor is the *type of product: L4SMEs show higher EIB Contribution than GLs*. The operations with the lowest financial contributions are all GL or converted operations signed in or before 2008 [#2, #4, #7, #17, #20]. All but one of these [#2] were located in EU15 countries. The operations with high financial contribution are all L4SMEs [#8, #14, #15, #16, #18], two of which were with promotional banks, underlining their willingness to voluntarily pass on as much ToFA as possible to SMEs, which is implicit in their "development" mandate.

The remainder of this section provides more detail concerning the financial contribution at the two levels, i.e. the intermediary and the final beneficiaries.

Financial contribution to the FI: FVA and other elements

FVA. The lowest FVA is found for GL operations signed before 2008 (pre-crisis), at a time when the competitive advantage of EIB conditions was lower. FVA increased with, respectively, converted loans and L4SMEs, signed during the financial crisis (see insert).

Differences between estimates at appraisal and actual FVA are mainly linked to methodological issues and evolving market conditions.

FVA – evaluation results

- For GL operations the actual FVA was estimated to be lower [#17] or not quantifiable by the FIs [#2, #4].
- For converted and L4SME operations, results are more nuanced, with nearly half of the actual FVA estimates being lower than ex ante expectations (defined at appraisal), and the other half with higher actual estimates. In at least three cases, the actual estimates varied during the course of the implementation of the operation, shifting/evolving from lower/similar to higher, mainly linked to the financial turmoil, and the growing difficulty of raising LT funding on the markets [#7,#12,#16].
- For four operations FIs might have only marginally benefited from the FVA identified at appraisal given the ToFA actually transferred during the course of the operation might have been equal or slightly beneath the FVA estimated at appraisal or actually transferred [#5, #14, #18, #20].
- For one operation FVA was negative [#7].

According to the SME Consultation *"[t]he advantage offered by EIB's funds may be measured as the differential between the interest rate to be paid on the EIB loan and the rate to be paid on the alternative source of funding, at the time of disbursement and for the lifetime of the loan*". However, for a number of operations, the variety of funding sources and benchmarks included by the Bank for the calculation of the FVA is not the same as the one used by the FIs. This concerns deposits, other short term to medium term retail savings products, lending from cooperative banks and other governmental resources [#3, #7, #11, #12, #14, #15], or evolving benchmarks [#18, #20]. Thus, the EIB considers FI's marginal cost of funding, whereas FIs would consider their average cost of funding (including deposits, etc.)

Furthermore, market conditions change with time. FVA conditions at disbursement therefore differed from those calculated at appraisal. The influence of market volatility on FVA is particularly well illustrated by one operation the disbursement of which was delayed by the promoter as FVA was to be non-existent. Also for other operations it was noted that FVA would have been different at signature or disbursement which could have influenced commitments on the magnitude of the contractual ToFA to be transferred to SMEs [#5, #6, #9, #12, #13, #14, #15, #16].

The one operation with an overall *low* rating for EIB contribution

One operation stands out as an overall low for EIB contribution. The absence of any real FVA in a highly liquid national market since appraisal and approval in 2005 led to no (or no identifiable ex post) benefit to SMEs. Only, when the market moved to generating some FVA for the intermediary, when the operation was converted to a L4SME, and when a more suitable distribution channel was identified in the intermediary's network (leasing), did it commit to a quantified benefit transferred to SME. Even that, however, unlike with other operations in the sample, remained somewhat opaque as the elements of comfort with respect to ToFA remained limited. In this case, the Bank's failure to assess adequately the complementarity of its product in the national context during the appraisal phase and identify suitable distribution channels early, led ex post to an overall low EIB contribution both for the intermediary as well as at the SME level.

Tenor. the financial value added generated from the EIB loan is also derived from the loan's maturity structure. For 12 operations the tenor of the EIB loan was perceived as a very attractive feature contributing to diversify the FIs senior debt funding sources and, at times, constituting their only or one of few sources of LT funding [#1, #6, #8, #9, #11, #12, #13, #14, #15, #16, #17, #19].

Volume. For at least 9 operations, the volume was not marginal and in some cases even significant, representing 10% to up to one-third of MLT [#2, #3, #6, #8, #12, #13, #14, #15, #16]. The number of operations for which the volume can be considered significant increases when one takes into account the operations that are repeated on a regular basis with historic EIB clients [for example, #4, #5]. Although this makes the EIB Contribution important, in some cases it also implied a risk of too great dependence on EIB funding [#3].

Financial contribution to the final beneficiary SMEs: ToFA and other elements

> *"The crucial element against which EIB's action should be evaluated is the value added its intervention provides to the final beneficiaries, in terms of improving SME's access to the appropriate financial product at attractive conditions."*
> (SME Consultation, 2008)

As underlined in the effectiveness section (Section 6.1.3), a major innovation introduced with the L4SME is the quantification of the ToFA, which has become contractually binding (for GLs this could not be tracked). This means that the FI agrees to a ToFA of a determined number of basis points. The ToFA is calculated on the basis of an assessment of the FVA estimated at the appraisal stage of the project. Prior to this innovation, the financial benefit to SMEs was expressed in qualitative terms in the Global Loans [#2, #4, #16]. For converted Global Loans, ToFA quantitative minima were introduced upon their conversion to L4SMEs.

ToFA generally was passed on to SMEs via interest rate reductions applied either during the entire duration of the sub-loan to the SME or, in one case, for the duration of the EIB loan to the FI [#9]. For one operation ToFA was passed on as a "cash back" [#20]. Here, after it was discounted, the FVA calculated by the FI became a cash back of a percentile of the nominal amount that would be applied to those SMEs receiving an allocation of EIB funds. This ToFA was applied evenly to all loans independently of their tenor and loan structure. Although for the FI this approach is simpler it tends to reward shorter term loans better than longer term loans.

Other positive aspects for SMEs such as availability of funding, volume and long tenor were already assessed in the effectiveness section and are not factored in into the rating of the EIB contribution (Section 6.1.3).

ToFA – evaluation results

- For the GL operations, transfer of ToFA cannot be ascertained. In at least two cases, EIB funding may have contributed to offer (marginally) better conditions to FI SME clients overall.
- For converted operations, in two cases FIs went beyond contractual requirements, voluntarily transferring more ToFA. Three of the four operations would be aligned with the current minimum transfer of FVA into ToFA, illustrating this threshold as an interesting reference point.
- For L4SME operations, whilst all FIs transferred at least the required ToFA, some voluntarily went beyond transferring up to 3 times the ToFA. For 7 L4SMEs out of 12, FIs voluntarily increased the actual ToFA to SMEs. 8 operations would be aligned with the current minimum transfer of FVA as estimated at appraisal or actually transferred. The remaining 4 L4SME operations either did not reach this threshold at appraisal or dropped below the minimum requirement when assessed/benchmarked against actual ToFA and actual FVA calculated ex post by EV. For one operation, the entire FVA was to be transferred as ToFA, but this could not be verified ex post. In three other cases it is expected that FVA to the FI was almost entirely passed on to the SMEs.

10.1.2 Non-financial contribution

In most cases no technical or institutional contribution was witnessed and L4SMEs show no difference with GLs in this respect. This is not surprising given the SME lending expertise of most of the sample FIs. In the 3 cases [#13, #16, #20] where EIB provided technical or institutional support, this related to the structuring of the technical or legal set-up of operations. The respective FIs perceived the latter as an opportunity to build capacity in terms of loan approval processes and procedures, documentation and monitoring. Some FIs considered that discussions with EIB staff introduced positive improvements, notably to reporting systems [#8, #14].

Limited financial facilitation, which for the operations evaluated could have included the leveraging of third party funds, was provided by the EIB. In 5 cases the operations were either provided in conjunction with national/regional financing schemes or other EIB Group products [#1, #3, #16, #17, #19, all but one in NMS]. Only one operation was carried out in conjunction with the EIF, increasing the attractiveness of the loans [#17]. None of the operations led the FIs to carry out similar operations with other potential financial partners although some were preceded, paralleled or followed up by loans of institutions such as KfW or the CEB.

10.2 Conclusions

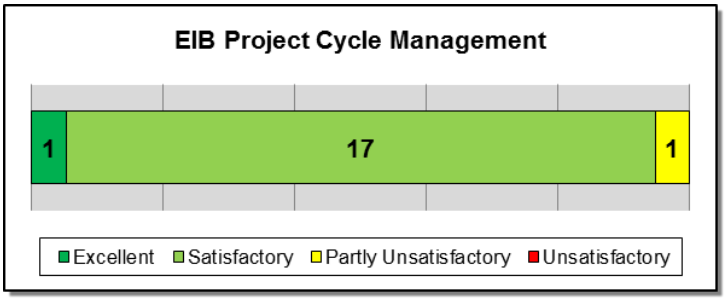
Overall, the financial contribution of the EIB is assessed as positive, generating, in most cases, an attractive FVA for the FIs, a transfer of ToFA to SMEs – however with strong variations between operations – and loans provided to SMEs at tenors that were as long as or slightly exceeding tenors extended by EIB to the FIs. For about half of the operations the volume was not marginal and was sometimes even a significant share of their overall MLT lending. L4SMEs appeared to lead to a higher financial contribution than GLs or converted loans but this is partly linked to the latter being implemented under increasingly constrained market conditions.

FVA calculations only use a limited number of benchmarks. Also, they are not updated whereas in volatile markets, the actual FVA can fluctuate significantly, and especially over the long periods that normally elapse between the moment the FVA is calculated at appraisal and the disbursement (when the FVA materialises). Therefore, from an economic viewpoint it could be relevant to reassess FVA at disbursement following an agreed upon methodology.

Non-financial contribution was provided in only three cases. This low number is not surprising in view of the expertise in SME lending of most of the FIs in the sample. There was one clear case of financial facilitation (operation in conjunction with EIF) and for a few operations funding occurred in conjunction with regional, national or EU programmes.

11 EIB PROJECT CYCLE MANAGEMENT

This criterion examines the way in which the EIB followed the operations through the project cycle from initial identification to completion (Project Cycle Management, PCM). It examines firstly whether the Bank's procedures were correctly followed and, wherever possible, the appropriateness of those.



Since procedures relate to the type of loan (GL or L4SME), it is recalled that out of the 19 operations evaluated in-depth, 3 were GLs, 4 were GLs converted into L4SMEs prior to the end of allocations and 12 were L4SMEs.

11.1 Evaluation results

Although PCM was rated satisfactory for most operations there is still potential for improvement going beyond compliance with procedures.

EIB PCM was in all but one case found "satisfactory" or better. This reflects that it was overall in line with the procedures and requirements valid and applied at the time. However, this rating does not provide an opinion on the intrinsic quality of these procedures and requirements.

From an organisational viewpoint, the Bank responded well to the elevation of SMEs to a "key operational priority". The SME Consultation (see 2.2), the establishment of a temporary SME unit, and centralised allocation handling through the Central Allocation Unit (CAU) are all viewed as appropriate, positive and pro-active responses to the policy demands directed at the Bank – a movement set in train before the crisis started. Currently therefore, the actual project cycle for intermediated lending to SMEs at the EIB is a well-oiled machine. Long-standing relationships with FIs often trigger annual repeat operations, with minimal reflections on changes in the SME market, and deliberations about how the EIB can best design and address its intervention to meet these demands (see also Section 5.1.3).

In one case an "excellent" rating was awarded [#9], as the Bank's services considered in greater depth the needs and specificities of the national SME market and how the EIB intervention could address these. This in turn had positive effects on the performance of the operation. In one case [#14] a "partly unsatisfactory" rating was awarded since missing important aspects of the operation during appraisal and misunderstandings as to the application of EIB's eligibility criteria affected negatively the allocation of EIB funds to the SMEs.

11.1.1 Identification, appraisal, negotiations and signature

4 of the 19 rated operations were signed before the outbreak of the crisis and 15 after. Of the 16 rated operations that were either L4SMEs from the start or which were converted, 13 were the first L4SME signed with the FI. For three operations, it was the second L4SME.

The adjacent table shows that the majority of operations of the sample were with repeat borrowers with which the EIB had a longstanding relationship directly and/or with the banking group of the FIs. The EIB tends to maintain a working relationship with the majority of the FIs with which it interacts. All but one [#19] of the FIs for the operations evaluated, had or have additional operations with the EIB covering SMEs or other EIB priorities; another intermediary acts as intermediary within the JEREMIE initiative. The long term relationship was by many of the FIs highlighted as one of the reasons for a smoother identification, pre-appraisal and appraisal. There were also clear synergies identified for the EIB, the FIs and the SMEs in allocating EIB funds through "repeat borrowers". Over the whole portfolio however, the Bank has opened up increasingly to new clients over time.

				Relationship with intermediary							
#	Product Type			Overall			As GL product			L4SME	
	GL	Conv	L4SME	Repeat	Group	New	Repeat	New	SMEs now	1st	2nd
1		√		√			√			√	
2	√			√					√		
3		√		√			√			√	
4	√			√			√				
5			√	√			-				√
6			√	√			-			√	
7		√		√					√	√	
8			√		√		-			√	
9			√	√			-			√	
11			√	√			-				√
12			√	√			-				√
13		√			√			√		√	
14			√			√	-			√	
15			√	√			-			√	
16			√			√	-			√	
17	√			√					√		
18			√	√			-			√	
19			√			√	-			√	
20			√	√			-			√	
Total:	3	4	12	14	2	3	3	1	3	13	3

As required under the characteristics of the modernised L4SME product, all operations created as L4SMEs had additional information on the relevant SME market and the Bank's lending activity in the respective country in the past.

However with two exceptions, no analysis of the complementarity between the interventions of the EIB and the other stakeholders (i.e. mainly the FIs and the governments of the MS) were found. There were no mechanisms to assess whether the FI's allocation of funds to SMEs covered specific market gaps or "business as usual" deals. There was no "customization" of EIB's offer to the specific operational context of the operations beyond the improvements resulting from the change from GL to L4SME. This was also discussed under the Relevance section (Section 5.1.3).

The partly unsatisfactory rating for operation [#14] was mainly due to a weak appraisal and misunderstandings as to the application of EIB's eligibility criteria by the FI, leading to significant deficiencies during allocation. On the other side of the spectrum, the excellent rating for operation [#9] was clearly linked to more comprehensive upstream work carried out at appraisal which had a more positive impact on the on-lending to SMEs.

Operations [#13] and [#19] required signature extensions and although there were significant changes in the context the appraisal was not updated. The lack of an appraisal reflecting the new context affected negatively the smooth implementation of both operations.

Several aspects complicated PCM up to and including signature. They can be grouped in three main categories (see insert), namely related to risk and legal issues; related to the design of the operation; and related to cooperation from the onset with the EC.

Issues complicating PCM grouped by categories	
Type	***Examples***
Risk and legal	Negotiation of a "master contract" covering all operations with the counterpart [#5]
	Formalisation of first demand guarantee agreement from parent company for first time operation [#8]
	Attempt to obtain government guarantee [#15].
	First operation in the MS with assignment or pledge of claims as security [#13].
	Down grading of rating for some of the FIs triggered contractual clauses requiring closer monitoring or additional guarantees/collateral provided to the EIB [most FIs to different degrees during crisis].
Design	Operations instrumented via a loan substitute rather than through a traditional loan structure [#17, #19].
	Operation originally conceived as loan substitute but redesigned as plain vanilla loan [#18].
	Conversion from GL to L4SMEs and corresponding contractual changes [#1, #3, #7, #13].
Cooperation w/ EC	Delays related to negotiations linked to use of energy efficiency grant complementing EIB funds [#1].
	Mixing of EIB funds with SME FF facility [#3, #13].

11.1.2 Implementation, disbursement, and allocations

As an anti-crisis measure, the EIB was asked to speed up its disbursements. With the crisis EIB's conditions often became comparatively more attractive for the FI and the demand for the EIB product by the SMEs increased while overall SME demand dwindled. Overall disbursements were carried out in a timely manner following signature of the contracts by the FIs. Operations instrumented as loan substitutes [#17 and #19] are disbursed a few days after signature once the necessary obligations for this type of structure are complied with by the FI. Timeliness was discussed in Section 7.1.1.

Some operation specific issues affecting speed of allocations

- Operations with EC grants [#1, #3, #13]
- Setting up separate EIB product, with corresponding procedures, IT systems and FI's staff training or awareness raising, especially for new FIs [#8, #13, #14, #16 and #17]
- Double intermediation introduced by the FI to further on-lent EIB funds through sub-intermediaries [#16].

No concerns were transmitted as regards the assessment of eligibility for the GL operations (as generally this did not have to be checked in great detail). However, for L4SME and converted operations, assessing whether SMEs were eligible was one of the most time-consuming issues for FIs. Operations [#6, #9, #14, #15, #16, #19, #20] would have appreciated more time spent between the EIB and the FI to discuss/explain eligibilities and/or monitoring/reporting. Some eligibility guidelines

were found to be restrictive or unclear. The latter FIs made proposals to review the eligibilities and the flexibility of EIB's criteria. Beyond the contract or side letter, no additional EIB document directed to the FI regarding eligibility was found.

11.1.3 Monitoring and completion

Monitoring greatly improved with the creation of the CAU
The smooth and swift implementation of the new L4SMEs implied, at the operational level, making organisational changes. A temporary SME unit within Ops-A was created (2009-2011) to accompany product development, monitor policies and support the administration. Additionally, a Central Allocation Unit (CAU) focusing on post-signature monitoring was established in Ops A and started operating in September 2010.

Regarding monitoring, CAU performed random checks looking at the completeness of mandatory information fields, eligibilities etc. Requests formulated by CAU were generally followed up by the FIs.

An "End of Allocation Report" (EAR) has to be produced at the end of the allocation period of each operation. This EAR provides basic information on the operation and on the allocations, and an assessment of the contribution of the operation to the 3 pillars of EIB Value Added. The four EARs produced by the time of this evaluation contained this information.

Establishment of the EAR is conditional to the CAU having received the additionality letter. However, no contractual deadline to provide the additionality letter was found in the operations evaluated. Although in some cases a few months had passed since end of allocation, some of the additionality letters had not been received [#6, #9, #13, #16].

EARs do not contain information on the number of SMEs served by each operation. In the Bank's statistics the number of SMEs is taken to be the number of allocations. However in reality there is no such equivalence. One allocation can cover several SMEs (the possibility of grouping several contracts under one allocation exists). Conversely, several allocations can represent a series of contracts with the same SME.

As regards the L4SME operations the stated objective on information requirements for this product was complied with by the EIB i.e. streamlining reporting requirements and reducing the burden on the FIs. Nonetheless EIB's reporting requirements were too basic to have a good ex-post understanding of the operation. Although those operations with EARs had additional information, more had to be requested from the FIs during the evaluation to have a complete overview of the operation. Most of this information was already produced internally by the FIs and could have been requested by the services to complement the EAR.

No formal completion missions
EIB's follow-up is limited to: (i) verifying that each subproject allocated complied with the selection criteria and (ii) monitoring the financial performance of the FIs and the evolution of their risk profile. The crisis and the down grade in the ratings of most of the counterparts have intensified the second monitoring aspect for all FIs. It should be noted that in the past PJ was involved in GLs and completion missions were carried out. No evidence of completion missions was found but there is anecdotal evidence that some loan officers used the missions for new contracts as an opportunity to discuss older operations. This process is not structured or formalised and depends mainly on individual loan officers. As per procedures at the time, follow up and monitoring took place via electronic and paper correspondence with no physical visits to SMEs. For all operations evaluated though there was very limited correspondence found in the Bank's Electronic Documents Management System (GED Knowledge Centre) , providing little visibility to the evaluators as to this monitoring.

GL reporting for the FIs was non-problematic, L4SMEs show some issues however
No issues were highlighted as regards the reporting for the GLs, however several issues where found for the L4SMEs.

Examples of reporting issues for FIs on L4SME operations

- Difficulties identifying the "autonomous SME" eligibility both for the FI and the EIB [#3].
- Difficulty monitoring NACE codes and number of employees as these criteria were not used by the FI [#11].
- The NACE codes provided to the FI were an older version whereas the FI always used the latest version [#19].
- Additional follow up requested by OCCO not found [#14].
- FI used double intermediation without contractually requiring any information on the sub-intermediaries, leading to lack of visibility on final beneficiaries [#16].
- An FI felt that the EIB misunderstood the difference between "committed" (i.e. proposal for funding made by the FI) and "realised" allocations. It was noted that the list of "committed" SMEs and/or amounts could vary as compared to the "realised" as some SMEs might eventually not draw the funds (e.g. refuse the offer) or change the initial amounts requested. Reporting on "realised" allocations obviously required a longer time lag than reporting on "committed" allocations [#20].
- Many FIs identified the need for a better method/tool of collecting and reporting back to the EIB; with several proposing an on-line platform (i.e. web based reporting).

The thresholds of financing SMEs up to a maximum of EUR 25 million project costs appear to have been complied with for all operations. However since the information provided to the EIB refers to the amount funded by the FI it is not possible to ascertain whether the SMEs funded larger projects using several sources of funds or whether the FI provides several loans to the same SME to fund the same project when the costs of these are larger.

Evidence of allocations rejected by the EIB was only found for two GL operations under the list approach allocation method [#2, #4]. However, for both operations the number of rejections was insignificant in absolute terms.

Most of the allocation requests for operation #8 were initially rejected but this was linked to a reporting deficiency of the FI which when corrected led to the approval of the previously rejected requests.

Many of the FIs interviewed praised the EIB services for clearly addressing their eligibility questions but not much documentation or emails were available in the internal documents to understand the dialogue taking place between the FI and the EIB. However, there are indications that in some cases refusals by the EIB are not recorded but rather new SMEs meeting the criteria are proposed by the FI and added to the "official" lists of allocations recorded.

11.1.4 Coordination and cooperation

For *all* operations, the regular authorisations were asked and obtained from the EC and MS. Except for three operations [#1, #3, #13], the operations did not involve any cooperation and coordination with the EC and the MS. None of the operations involved other IFIs as part of a joint initiative.

11.2 Conclusions

Operations generally followed pre-appraisal and appraisal procedures correctly. Having a historical relationship with a promoter generally smoothened this process. Aspects affecting the length of this process are related to risk and legal issues, to the design of the operation, and for the very few cases where this was applicable, early cooperation with the EC.

From an organisational viewpoint, the Bank responded well to the elevation of SMEs to a "key operational priority". The SME consultation, the establishment of a temporary SME unit, and centralised allocation handling through the Central Allocation Unit (CAU) are all viewed as appropriate, positive and pro-active responses to the policy demands directed at the Bank – a movement set in train before the crisis started. The current project cycle for intermediated lending to SMEs at the EIB is a very well-oiled machine and probably amongst the most homogeneous and streamlined processes at the Bank.

The EIB overall disbursed faster during the crisis, allowing the Bank to achieve the targeted volumes and allowing FIs to make the funding available to SMEs more rapidly. Issues affecting the subsequent allocation appear very much operation and context specific. However, in some cases there was lack of clarity on eligibility criteria – which with the L4SMEs were broadened – leaving some options unused by FIs. Leaving such options open in itself is deemed to be a positive development as it leads to more flexibility for the FIs.

Monitoring the progress of operations, especially by checking allocation requests, has greatly improved with the L4SMEs and with the creation of the Central Allocation Unit. End of Allocation Reports are of good quality and provide the relevant material to ascertain compliance. They could incorporate more information for the Bank to make more strategic use of the information that can be provided by FIs – especially at the level of the effects that are generated by each operation. This has, of course, administrative resource implications.

EIB reporting tools for SME intermediated lending have greatly improved over the past few years. Whereas most FIs have no difficulties complying, especially some smaller, less well-equipped FIs which cannot make the necessary investments to benefit from economies of scale, find the tools cumbersome and may need some extra support from the Bank.

Finally, for *all* operations, the regular authorisations were asked and obtained from the EC and MS. Except for three operations, the operations did not involve any explicit cooperation and coordination with the EC and the MS. None of the operations involved other IFIs as part of a joint initiative.

12 CONCLUSIONS AND RECOMMENDATIONS

12.1 Conclusions

The evaluation shows EIB SME intermediated lending to be highly consistent with EU and EIB objectives and their evolution over time. The broad scope of the L4SME product made it relevant and increasingly so when access to finance for SMEs deteriorated across Europe. Yet, the operations' relevance can still be substantially improved if fine-tuned to national SMEs funding needs. The complementarity of the EIB product within national policy mixes should be better assessed. This is especially important as the SME Survey showed country context to be the strongest predictor of the loans' impact on SMEs' competitiveness, growth and employment.

The L4SME product replaced the Global Loan product for SMEs. It was introduced when – by coincidence – the financial crisis started. The L4SMEs is effective: *it says what it does, and does what it says*. It allows the Bank, through contractual and reporting requirements and the definition of specific eligibility criteria, to understand better and control – and potentially better target or steer – the advantages transferred to SMEs and the types of SMEs financed. The L4SME is a major improvement in comparison to the former Global Loan approach for which it was unclear how much of the EIB advantage ultimately benefited SMEs and how much remained on the FIs' balance sheets. The contractual Transfer of Financial Advantage (ToFA) and more stringent transparency obligations have, as assessed by EV *ex post*, clearly contributed to providing a higher level of comfort that a financial advantage is indeed passed on to SMEs. Transparency is enhanced most notably by the detailed reporting on allocations to SMEs, by the publicity on the FIs' websites and the reference to the EIB in contracts with the SMEs. Such advantages were mainly interest rate rebates and, to a lesser extent, increased tenor – though a few FIs substantially increased tenor compared to their overall SME portfolio.

All Financial Intermediaries adhered to the principles and requirements of the new L4SME product. Most made, sometimes substantial, efforts to create e.g. a special EIB product, set up IT systems to track the SMEs benefiting from EIB funds, train front office staff and make publicity. In some cases the publicity for EIB funds was only 2 or 3 "clicks" away from an FI's homepage. In such cases the information on the EIB funding possibility is highly accessible for entrepreneurs. Also, SMEs have an EIB mention on their loan contracts. Over 40% of surveyed L4SME final beneficiaries were indeed aware that funding originates from the EIB – more than twice as many as for the GLs. The evaluation found clear evidence that visibility and transparency make a difference. The more extensive a FI's involvement in the EIB's transparency requirements, the higher the *ex post* level of comfort that ToFA is measurable and real.

FIs generally tend to choose larger and less risky SMEs to be financed under the EIB loan in comparison to their overall eligible SME portfolios. This effect is most pronounced in EU15 (old member states). The proportion of smaller and younger firms in the EIB portfolios financed by the FIs decreased over time. The proportion of SMEs surveyed for this evaluation stating that they received the full

amount asked for remained relatively stable over time. Other SME access-to-finance surveys show that, with the crisis, SMEs generally obtain lower loan amounts than what they ask for.

EIB's intermediated SME lending has a broad scope and, apart from a series of exclusion criteria, does generally not focus on specific types of SMEs in terms of size, sector or risk profile. Moreover, in these operations the EIB does not share risk, it promotes on-lending at relatively longer tenors and ToFA is settled in markets which are highly volatile. Finally, FIs prefer to have little or no losses on the EIB portfolio for reasons of reputational risk. Under such conditions, FIs prefer to choose comparatively larger and less risky SMEs. These can be either existing clients or come from other banks. In the latter case the EIB loan induces competition between banks, which is viewed as positive. The different pieces of evidence converge to the conclusion that for a majority of operations SMEs were often also those that would have most likely obtained funding anyway. EIB funding is thus in most cases not "gap funding" but rather used to support SME "champions".

During the period studied, the EIB loans had some impact on growth and employment, though great variations exist across countries. About half of the SMEs declared that turnover had grown after receiving the EIB funds, of which one-third attributed this entirely or partly to the funding. Also half of the SMEs reported that the loan or lease had positive effects on productivity, market share or general economic health of their business. Yet, according to the SME Survey, on average about one job per financed SME was created. And there is only limited evidence that the EIB loans helped maintaining employment – although for some operations, especially in countries where the crisis hit SMEs hardest, there is anecdotal evidence that the EIB loans helped keeping companies afloat. The relative impact on growth and employment is likely to be higher in the New Member States. The economic impact of EIB lending is also likely to be higher for small (10 to 49 employees) but not micro firms and for relatively young (2 to 5 years) but not the youngest firms. Firms having introduced innovations or that used the funds for research and development show a relatively higher impact. Overall, the country context should be taken better into account if the Bank wants to optimise its impact on growth and employment.

In sum, EIB intermediated SME lending does not primarily improve access to finance for SMEs which are un- or underserved by banks due to their risk profile, except if operations are carried out within the framework of national programmes, implemented by, for instance, promotional banks. The L4SME is first of all a volume instrument with a broad scope and a wide reach, leaving to the FIs the types of SMEs to be targeted. It is standardised, working well and well under control. The Bank definitely needs such an instrument in order to be able to fulfil its increased SME lending targets over the coming years. Yet, the Bank should recognise that whereas this tool is fit to maximise lending volumes it does not necessarily maximise impact. Possibilities offered by the eligibility criteria to influence the targeting of final beneficiaries open opportunities for reflecting, *in a longer term perspective*, on how the L4SME product could also be mobilised to fill specific gaps instead of funding a broad spectrum of SMEs. This could then lead to optimising the EIB's contribution to growth and employment.

12.2 Recommendations

The following recommendations are made against the background that presently EIB intermediated SME lending, on the basis of the L4SME product, is overall effective. This is viewed positively, especially given the strongly increased SME lending target over the coming three years. The evaluation findings provide guidance on how the lessons learnt from the experience with the L4SMEs can be used to optimise the Bank's contribution to economic growth and employment objectives.

12.2.1 Strategic recommendations

R1. Clarify the objectives of intermediated SME lending

Level	Objective
Operational	to extend finance to eligible SMEs (sign, disburse, "allocate")
Intermediate	to provide such finance at improved conditions to improve access to finance
Global	to enhance the competitiveness of SMEs, ultimately, generating a positive impact on economic growth and employment

On the basis of the policy review the "Intervention Logic" of the Bank for intermediated SME lending could be established. By extending finance to eligible SMEs (operational objective) the Bank aims at providing finance at improved conditions as well as improving access to finance (intermediate objectives). The achievement of those intermediary objectives should in turn enhance

the competitiveness of SMEs and ultimately generate a positive impact on economic growth and employment (global objective).

The evaluation found that the Bank – through its intermediated SME lending – is indeed providing finance at improved conditions to eligible SMEs. However it contributes less to providing access to finance for SMEs that would otherwise not have obtained such finance. It was also noted that depending on how those objectives and their relation to the ultimate objective of growth and employment are interpreted (e.g. does "improve access to finance" only cover SMEs having no access at all?), the intermediary objectives may not necessarily be consistent with each other. They may also be difficult to be pursued in parallel as different types of SME target groups may be concerned, which the evaluation results tend to show.

Moreover, although overall EIB SME intermediated lending did certainly contribute to growth and employment, the evaluation found that the larger and less risky SMEs most served by the loans were not necessarily those contributing *most* to the growth and employment objective. Furthermore, it is not clear that aiming at providing access to finance to un- or underserved SMEs would necessarily maximise the Bank's impact on growth and employment.

Therefore, in order for the Bank to clarify how its action contributes to the global EU objectives of growth and employment, it is recommended to define more precisely the objectives for intermediated SME lending and how they relate to each other. A narrative should also be made more explicit on how the objectives of improving funding conditions and/or improving access to finance are expected to contribute to the ultimate objectives of economic growth and employment.

R2. Adjust EIB Group product offering better to national needs and policy mixes

In line with the EIB's interpretation of Article 309 (c) of the Treaty of the Functioning of the European Union (TFEU), "the EIB provides funding for […] economic activities that do not have ready access to finance (e.g. […] SMEs) in the territories of Member States"[20]. The assessment of whether or not a given Member State has *ready access to finance for SMEs* should therefore be a fundamental ingredient in the rationale for an EIB intervention:

The evaluation identified a fairly consistent lack of *ex ante* SME needs assessments at the national level. In the few cases where such (even limited) assessments of SMEs funding needs and the potential complementarity of the EIB product were undertaken, both the effectiveness and efficiency of the operations were already noticeably better. Moreover, the SME Survey found strong evidence that across its statistically representative sample of 1003 SMEs interviewed, by far the strongest predictor of SME impact (competitiveness, growth, and employment) was the country context, highlighting how critical it is for SME interventions to reflect on the needs of national SME markets.

The EIB should optimise its intermediated SME lending by adjusting better to local circumstances at Member State level. In the future, beyond the volume driven targets, this could allow the Bank to optimise its impact on the global objectives of growth and employment. The Bank should therefore *already now* engage in:

(a) a periodic SME country needs assessment to determine how the EIB's intermediated SME lending can best achieve its global policy objectives of growth and employment. The competent services across EIB departments (ECON, PJ, Ops) could be involved in those assessments;
(b) launching the follow-up SME Consultation (as initially foreseen) with all relevant stakeholders, including, beyond the FIs, other DFIs/IFIs, SME associations, etc.;
(c) reflecting in the appraisal process how a proposed operation responds to the SME country needs assessment, how it addresses identified SME needs and how it is complementary to other available SME products, and how it addresses identified SME needs.

R3. Prepare for "smart targeting"

The broad scope of SME lending can have both positive (e.g. on SMEs' sustainability – likely higher in the case of less risky SMEs) and negative implications (not optimising growth and employment). However, the L4SMEs is an effective volume instrument which currently does not aim at more precise

[20] See recent EIB publication: "The Governance of the European Investment Bank", September 2012, p.4.

targeting in view of e.g. countries' specific SME finance needs or achieving higher relative growth and employment results.

Given the Bank's recent capital increase and the corresponding increase in SME lending targets it is expected that intermediated SME lending should continue to be volume driven in the short term. However, the Bank should also with the L4SME be able to increase its added value through the use of more focussed eligibility criteria. In order to gain experience with such "smart targeting" in view of the needs of specific SME groups, it is recommended that the Bank set up a pilot for a small volume to be determined. This envelope should allow the Bank to experiment to target specific SME groups in view of the Bank's policy objectives of growth and employment, following an exercise of an SME country needs assessment. The eligibility criteria being the knobs with which to define and fine-tune the final beneficiary group, such an experiment will allow the Bank to learn more about the relationship between eligibility criteria and outcomes of its lending. It will also help the Bank to assess the resource (capital, human, operational, etc.) implications of "smart targeting". This pilot should be set up in conjunction with the recommendations on the clarification of the objectives (R1) and on the adjustment to national needs (R2). The pilot should result in an assessment of the feasibility and conditions of more targeted intermediated SME lending, and an action plan in case feasibility is proven.

R4. Additionality: in order to avoid confusion, choose a more appropriate term

Under normal circumstances, in order to comply with EIB's statutory requirements (art. 16(2)) as reflected in the relevant decisions of the Bank's governing bodies, EIB financing is generally limited to 50% of the "project cost" of its investments. This was also the case for SME GLs in the past where in principle EIB funds could be used to finance only up to half of each SME's investment. For L4SMEs a new rule was introduced where a loan to an SME can be entirely financed by the EIB loan, i.e. 100%. This makes administration of such loans much easier for the Bank, the FI and even the SME than if the 50% rule would have been maintained. In order to nevertheless comply with this rule, for L4SME operations FIs have to confirm that the volume of MLT SME financing with a term of more than 2 years outside excluded sectors signed during the allocation period and financed with non-EIB resources has been at least as much as that of the EIB Loan for SMEs. This is called the "additionality" requirement.

The "additionality" requirement was respected across the sample. It was, however, more difficult to fulfil for FIs with smaller SME portfolios – meaning probably that in such cases their absorption capacity initially was overestimated. For larger FIs on the other hand, which form the majority of the sample, fulfilling the requirement is easy as the EIB funding is marginal compared to their overall eligible portfolio; the requirement in such cases becomes a formality.

> As an economic concept, "additionality" generally refers to the assessment of whether an investment would have taken place without a given (public) intervention. It assesses the effect of the intervention compared to a baseline or a situation "without" it. If an intervention does not substitute for existing activities (in the present case, for existing finance) it is considered "additional".

The "additionality" requirement is in fact a matching requirement. It is more a compliance check than an incentive for FIs to increase MLT lending to SMEs. It controls for whether the FI can show the same volume of similar SME lending and ultimately for whether the FI's SME portfolio is not financed by the EIB only. It is therefore a relevant requirement to respond to the EIB Statute and in line with good banking practice more generally. However, it is *not* equivalent to the additionality concept normally used in the literature (see insert). That is, the additionality indicator used by the Bank is not measuring the *induced* extra lending by the FI on top of a baseline, i.e. lending it would have otherwise not extended. It just controls for whether the FI can show a same volume of similar SME lending regardless of whether this was truly additional to its normal lending pattern. The use of the term additionality is therefore misleading.

In order to avoid confusion it is recommended to replace "additionality" in the contractual documentation by a more appropriate term.

R5. Optimise the benefits passed on to SMEs

The relationship between the EIB providing funding to FIs ("lending") and FIs providing such funding to SMEs ("on-lending") is at the heart of this evaluation. The underlying conditions between 'lending' and 'on-lending' define the critical nexus of how the Bank ultimately reaches out to SMEs. In particular in the current crisis context and its high market volatility, it is of great relevance how this nexus is determined, how much of the overall EIB benefits should reasonably reside with the FIs (as a result of

the EIB's Financial Value Added - FVA) and how much of it and in what form benefits should be passed on to SMEs using the L4SME vehicle (as Transfer of Funding Advantage – ToFA). EV's ex post assessment of this critical nexus identified the following recommendations:

(a) It is recommended that the Bank undertake a regular internal review of the actual benefits passed on to SMEs in order to optimise and possibly maximise them. Beyond elements of price this should also include other financial benefits, especially tenor. This review should be performed at least on an annual basis and should be informed *inter alia* by an analysis that takes into account contractual ToFA relative to the actual (reported) ToFA. Such analysis should be performed for *a representative sample* of operations. It should inform the future decisions about the level of FVA and ToFA, in view of optimising and possibly maximising the benefits passed on to SMEs.
(b) It is recommended that the Bank undertake a review of the underlying principles on the topics of reuse of funds and maturity mismatch, and following that a clarification of the related contractual clauses and a better enforcement of such clauses.

Together, these recommendations would more clearly delineate the critical inputs in the relationship between 'lending' and 'on-lending' and further enhance transparency of the EIB-FI-SME relationship for the Bank's services.

12.2.2 Operational recommendations

R6. Promote visibility and transparency even more

The evaluation found clear evidence that visibility and transparency make a difference. The more extensive an FI's involvement in the EIB's transparency and visibility requirements, the higher the *ex post* level of comfort that ToFA was measurable and real.

It is recommended that the Bank
(a) require from FIs to use *simultaneously* multiple ways of communicating to SMEs the EIB involvement, rather than giving them the choice (i.e. have a webpage *plus* mention of the funding advantage *plus* a brochure, etc.). The most effective option is when FIs develop a dedicated EIB product, which should in all cases be encouraged in discussing a new operation with an FI;
(b) in its due diligence of FIs present a comprehensive review of how a proposed FI undertakes to pass on the advantages to SMEs. This review should include highlighting the FIs internal links between their treasury and their operational (front office) side (e.g. pricing policy / pricing models);
(c) through COM reach out directly to SMEs with publicity on the possibilities offered with EIB funding;

R7. Assess clients' adherence to environmental and social regulations

With respect to national and EU environmental (and social) regulations, no specific checks are carried out by the Bank at the SME level, other than a presumption of reliance on the ultimate borrowers' compliance with a clause in the sub-loan agreements. Only *one* FI from its own accord performed specific checks at the SME level during its loan approval process. The general hypothesis for the others was that, operating within an EU environment, companies benefiting from the loan would generally comply with applicable legislation.

During the appraisal the EIB should review and document the FIs processes and procedures with respect to assessing their clients' adherence to national and EU environmental and social regulations and assess whether such reliance is sufficient for the Bank.

R8. Reinforce CAU's role

The establishment of the Central Allocation Unit (CAU) at the EIB is viewed as an appropriate and pro-active response to the policy demands directed at the Bank. The CAU can provide a valuable contribution to the *timeliness* of the Bank's outreach to SMEs through an efficient handling of the allocation process. In many instances the efficiency of this process could have been enhanced by an *earlier* involvement of CAU (and where applicable PJ), in the operational process.

The role of CAU should be reinforced. Because loan officers are increasingly de-coupled from the allocation process *per se* (now handled by CAU), CAU, (and where necessary PJ), with their detailed knowledge of the application of the EIB's eligibility criteria should be involved *in situ* at the inception of an operation to explain better the Bank's eligibility modalities.

R9. Improve internal and external SME reporting

The *ex post* data collection for this evaluation's portfolio review highlighted a number of issues regarding the aggregation and reporting on the Bank's SME intervention. In particular, the aggregation of individual SME related data to a portfolio of SMEs is cumbersome, if not at times misleading. One example: the published number of individual SMEs the Bank reaches out to corresponds in reality to the number of SME *allocations*. As one SME can have several allocations, the number systematically overestimates the number of individual SMEs reached.

The EIB should review how individual SME related data is captured and then aggregated in its IT systems to report on the Bank's SME activities. Based on internal and external reporting needs the Bank should then improve on the currently available tools.

APPENDIX 1 – EVALUATION PROCESS AND CRITERIA

In accordance with EV's Terms of Reference, the objectives of evaluation are:

- To assess the quality of the operations financed, which is assessed using generally accepted evaluation criteria, in particular those developed by the Evaluation Cooperation Group, which brings together the evaluation offices of the multilateral development banks. The criteria are:

  a) Relevance corresponding to the first pillar of value added*:* is the extent to which the objectives of a project are consistent with EU policies, as defined by the Treaty, Directives, Council Decisions, Mandates, etc., the decisions of the EIB Governors, as well as the beneficiaries' requirements, country needs, global priorities and partners' policies. In the EU, reference is made to the relevant EU and EIB policies and specifically to the EU Treaty that defines the mission of the Bank. Outside the Union, the main references are the policy objectives considered in the relevant mandates.

  b) Project performance, measured through **Effectiveness (efficacy), Efficiency** and **Sustainability** and second pillar of value added.

  Effectiveness relates to the extent to which the objectives of the project have been achieved, or are expected to be achieved, taking into account their relative importance, while recognising any change introduced in the project since loan approval.

  Efficiency concerns the extent to which project benefits/outputs are commensurate with resources/inputs. At ex-ante appraisal, project efficiency is normally measured through the economic and financial rates of return. In public sector projects a financial rate of return is often not calculated ex-ante, in which case the efficiency of the project is estimated by a cost effectiveness analysis.

  Sustainability is the likelihood of continued long-term benefits and the resilience to risk over the intended life of the project. The assessment of project sustainability varies substantially from case to case depending on circumstances, and takes into account the issues identified in the ex-ante due-diligence carried out by the Bank.

  Environmental and Social Impact of the projects evaluated and specifically considers two categories: (a) compliance with guidelines, including EU and/or national as well as Bank guidelines, and (b) environmental performance, including the relationship between ex ante expectations and ex post findings, and the extent to which residual impacts are broadly similar, worse or even better than anticipated.

  Evaluations take due account of the analytical criteria used in the ex-ante project appraisal and the strategy, policies and procedures that relate to the operations evaluated. Changes in EIB policies or procedures following project appraisal, which are relevant to the assessment of the project, will also be taken into account.

- To assess the EIB contribution *(Third Pillar)* and management of the project cycle:

  EIB Financial contribution identifies the financial contribution provided in relation to the alternatives available, including improvements on financial aspects as facilitating co-financing from other sources (catalytic effect).

  Other EIB contribution (optional) relates to any significant non-financial contribution to the operation provided by the EIB; it may take the form of improvements of the technical, economic or other aspects of the project.

  EIB Management of the project cycle rates the Bank's handling of the operation, from project identification and selection to post completion monitoring.

EUROPEAN INVESTMENT BANK
OPERATIONS EVALUATION (EV)

In 1995, Operations Evaluation (EV) was established with the aim of undertaking ex-post evaluations both inside and outside the Union.

Within EV, evaluation is carried out according to established international practice, and takes account of the generally accepted criteria of relevance, efficacy, efficiency and sustainability. EV makes recommendations based on its findings from ex-post evaluation. The lessons learned should improve operational performance, accountability and transparency.

Each evaluation involves an in-depth evaluation of selected investments, the findings of which are then summarized in a synthesis report.

The following thematic ex-post evaluations are published on the EIB Website:

1. Performance of a Sample of Nine Sewage Treatment Plants in European Union Member Countries (1996 - available in English, French and German)
2. Evaluation of 10 Operations in the Telecommunications Sector in EU Member States (1998 - available in English, French and German)
3. Contribution of Large Rail and Road Infrastructure to Regional Development (1998 - available in English, French and German)
4. Evaluation of Industrial Projects Financed by the European Investment Bank under the Objective of Regional Development (1998 - available in English, French and German)
5. An Evaluation Study of 17 Water Projects located around the Mediterranean (1999 - available in English, French, German, Italian and Spanish).
6. The impact of EIB Borrowing Operations on the Integration of New Capital Markets. (1999 – available in English, French and German).
7. EIB Contribution to Regional Development A synthesis report on the regional development impact of EIB funding on 17 projects in Portugal and Italy (2001 – available in English (original version), French, German, Italian and Portuguese (translations from the original version)).
8. Evaluation of the risk capital operations carried out by the EIB in four ACP countries 1989-1999 (2001 - available in English (original version), French and German (translations from the original version)).
9. EIB financing of energy projects in the European Union and Central and Eastern Europe (2001- available in English (original version), French and German (translations from the original version))
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11. EIB Financing of Solid Waste Management Projects (2002 – available in English (original version), French and German (translations from the original version)).
12. Evaluation of the impact of EIB financing on Regional Development in Greece (2003 – available in English (original version) and French (translation from the original version)).
13. Evaluation of Transport Projects in Central and Eastern Europe (2003 – available in English (original version).
14. EIB Financing of Urban Development Projects in the EU (2003 – available in English (original version), French and German (translations from the original version)).
15. Evaluation of the Projects Financed by the EIB under the Asia and Latin America Mandates (2004 – available in English (original version), French, German and Spanish).
16. Evaluation of EIB Financing of Airlines (2004 – available in English (original version) French and German)
17. Evaluation of EIB Financing of Air Infrastructure (2005 - available in English (original version) German and French)
18. EIB financing with own resources through global loans under Mediterranean mandates (2005 - available in English (original version) German and French.)
19. Evaluation of EIB Financing of Railway Projects in the European Union (2005 - available in English (original version) German and French.)
20. Evaluation of PPP projects financed by the EIB (2005 - available in English (original version) German and French).
21. Evaluation of SME Global Loans in the Enlarged Union (2005 - available in English (original version) and German and French.)
22. EIB financing with own resources through individual loans under Mediterranean mandates (2005 - available in English (original version) and German and French.)

23. Evaluation of EIB financing through individual loans under the Lomé IV Convention (2006 - available in English (original version) German and French.)
24. Evaluation of EIB financing through global loans under the Lomé IV Convention (2006 - available in English (original version) German and French.)
25. Evaluation of EIB Investments in Education and Training (2006 - available in English (original version) German and French.)
26. Evaluation of Cross-border TEN projects (2006 - available in English (original version) German and French).
27. FEMIP Trust Fund (2006 - available in English.)
28. Evaluation of Borrowing and Lending in Rand (2007 - available in English (original version) German and French).
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30. Economic and Social Cohesion - EIB financing of operations in Objective 1 and Objective 2 areas in Germany, Ireland and Spain (2007 - available in English. (original version) German and French)
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40. Evaluation of EIB Financing in Candidate and Potential Candidate Countries between 2000 and 2008 (2009 – available in English (original version) and French).
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