

Evaluation of EBRD operations

Project evaluation involves the assessment of operations once investment has been completed. This normally occurs one to two years after full disbursement has taken place. Performance ratings are assigned according to how the project has fulfilled the EBRD's mandate. The ratings focus on impact on the transition process and the application of sound banking principles. They also assess "additionality" and environmental performance. In addition, technical cooperation operations are evaluated, applying the same means of assessment that are used for EBRD investments.

Operational lessons are identified and disseminated in various ways. The Bank's Project Evaluation Department (PED) produces three types of evaluation reports:

- Operation Performance Evaluation Reviews (OPERs), which build on field work, interviews and additional analysis that is often supported by external expertise;
- PED assessments of self-evaluation reports, which are prepared by operation teams in the Banking Department;
- thematic and sector-oriented evaluation reports, which seek to identify patterns of experience.

The PED seeks to establish how well the EBRD's operations meet their objectives, thereby assessing the Bank's transition effectiveness. The lessons learned from the EBRD's operations and from the experience of other international financial institutions are used to improve the selection and design of future operations. The EBRD makes use of relevant lessons in formulating strategy papers and is also keen to learn from the evaluation of ongoing operations. The independent status of the PED ensures objectivity, transparency and accountability.

Evaluating projects

By early 2001, PED had evaluated 239 of the 308 projects where full disbursement had taken place. The results are therefore fairly representative. A total of 75 per cent of the projects were given medium to high ratings for transition impact (44 per cent medium and 31 per cent high). Transition impact ratings were higher for public sector operations (where infrastructure dominates) than for private sector projects. There was little variation according to the size of the investment or to its status as loan or equity.¹ These results confirm that the EBRD continues to operate according to its mandate to advance the transition process in its countries of operations.

Of the 239 projects evaluated, 115 were covered by OPER reports and 124 by PED assessments of Banking's self-evaluation reports. The remaining 23 per cent were covered by self-evaluation reports prepared by Operation Leaders, which have not been independently validated by PED. Performance ratings for these projects are not included in the tables below.

¹ The overall transition impact ratings are slightly better on average for loans compared with equity, reflecting a slightly greater percentage of loans in infrastructure.

Transition impact and the EBRD's overall transition effectiveness

In evaluating the transition impact of projects, the EBRD looks in particular at their wider impact in the sector and on the economy as a whole. At project evaluation, PED assesses transition impact using the same criteria applied by the EBRD during the selection and approval of projects. Some of the key indicators are promotion of privatisation, the development of skills, the encouragement of competition and support for market expansion. Other key aspects are institution-building to improve the functioning of markets, positive demonstration effects, and the setting of new standards in business conduct and governance. These criteria are constantly being developed by the PED and the Bank's Office of the Chief Economist. Of the 212 operations evaluated in 1996-2000,² 43 per cent achieved a transition impact rating of "medium" and 33 per cent were assessed as "high".

Transition impact ratings of evaluated EBRD projects 1996-2000

	Negative		Low-Negative		Medium		Medium-High		Number of evaluated projects
	%	%	Low %	Negative %	Medium %	High %	High %		
1996	0	0	17	17	66	17	83	35	
1997	0	6	25	31	42	28	70	36	
1998	6	6	14	26	41	33	74	49	
1999	6	12	8	26	50	24	74	50	
2000	2	12	5	19	19	62	81	42	
1996-97	0	3	21	24	54	23	77	71	
1996-98	3	5	18	26	48	27	75	120	
1996-99	4	6	15	25	49	26	75	170	
1996-2000	3	8	13	24	43	33	76	212	

A total of 24 per cent of evaluated projects were given transition impact ratings in the low-negative range, which is similar to previous years. This apparent lack of progress may be due to the difficulties experienced as a result of the Russian financial crisis in 1998. This put the sustainability of some private sector operations at risk and therefore affected their transition impact potential. A stable share of medium-high transition impact ratings can therefore be regarded as positive, although it is too early to draw any firm conclusions. The economic crisis in 1998 highlighted the systemic institutional weaknesses in the region, as indicated in recent evaluation reports, but the signs of resumed growth should enhance the transition impact potential of new private sector operations.

² Transition ratings before this period were not sufficiently refined, and the checklist of transition indicators had not been fully developed.

The overall success of the EBRD's operations is illustrated in the table below, which presents overall "transition effectiveness" ratings. "Transition effectiveness" gives a high weighting to transition impact but also includes other performance ratings, such as the fulfilment of project objectives, financial performance, environmental performance and additionality. In 1996-2000, 54 per cent of evaluated projects achieved a rating of successful or highly successful.

Overall transition effectiveness of evaluated EBRD projects 1996-2000

	Unsuccessful %	Partly successful		Successful/ Highly successful		Number of evaluated projects
		%	%	%	%	
1996	14	31	43	11	54	35
1997	11	42	36	11	47	36
1998	22	20	53	4	57	49
1999	22	24	46	8	54	50
2000	17	24	45	14	59	42
1996-97	13	37	39	11	50	98
1997-98	17	30	45	8	53	120
1998-99	18	28	45	8	53	170
1996-2000	18	27	45	9	54	212

The transition effectiveness ratings are lower than those for transition impact. This is primarily due to the impact of lower financial performance ratings, which was caused by a high-risk investment environment hampering the financial sustainability of many EBRD projects. In several project evaluations it was concluded that the Bank could have mitigated the industry-specific risk more effectively and that specialist knowledge of the industry must be used in the appraisal and structuring of projects. The EBRD was generally more successful in identifying industry risk when it made use of specialist knowledge of specific sectors.

Dissemination of lessons

Apart from performance ratings to meet the accountability needs of a public institution, a key evaluation role is to ensure that past experience is applied to new projects. This begins with intensive consultation with operation teams on the lessons in draft evaluation reports. Regular feedback is also offered at every stage of the approval process to provide bankers with relevant past experience. Case-based workshops are held and tailored to the specific needs of Banking teams. Other activities include presentations to management and the maintenance of a lessons-learned database for internal and external use.

Investment operations – some thematic lessons from evaluations

The following lessons are taken from key examples of successful and less successful EBRD operations since the Bank was established. They are presented in line with the Bank's Public Information Policy and selected for their potential to influence future strategy.

Infrastructure projects with a high potential for transition impact and low risk. Both public and private infrastructure projects can involve relatively low risk when linked to and conditional on institutional and enterprise reform. This supports continuing emphasis on infrastructure in the Bank's future operations.

Institutional and regulatory reform in support of markets. Direct investment in carefully selected private sector projects can have a significant impact on the transition when institutional and regulatory reform has been undertaken in support of markets. Conversely, slow reform efforts may hamper the sustainability of private sector investments. The risk to wider transition impact and to the Bank's investment can therefore be very high. Excessive systemic risk can limit the level of direct private sector intervention in some areas, justifying investment by other institutions in conjunction with policy dialogue.

Risk mitigation for investments in "brownfield" industry complexes. Risks to investments in large conglomerates can generally be mitigated satisfactorily only if full owner control is yielded to new sponsors. These need to be strong parties in the industry with a clear strategic reason for entry reflected in material investments and managerial support. A proven record in complex enterprise turnaround in the industry under emerging-market conditions is desirable. In addition, measures may need to be in place to mitigate adverse social effects caused by redundancies, in particular in "one-company towns". These lessons are currently applied in the Bank's cautious selection of large enterprises in need of support for post-privatisation reform.

Weighting the risk of government securities. In the event of a country's supervisory authorities failing to insist on risk-weighting of the government's securities, the EBRD should recalculate capital adequacy ratios to assess whether a more prudent approach would make a material difference to the Bank's position.

Ownership investigation in newly formed or restructured banks. It is essential to carry out a thorough study of the ownership of banks to establish the motivation of owners as well as the extent of their financial resources. Since ownership is frequently hidden behind front companies, it is often necessary to establish who owns these companies and whether there is a common ownership. In the case of individual shareholders, it is important to find

Examples of evaluated EBRD projects

Projects assessed as successful

Staged financing supports the privatisation of a national telecoms operator

A number of years ago the EBRD lent the equivalent of over €100 million with a sovereign guarantee to a national telecoms operator to modernise and extend its network. The state-owned monopoly in central Europe was subsequently converted into a joint-stock company. The Government undertook gradual privatisation after network congestion had been reduced and investments had been completed for long-distance and international services. The achievement of financial self-sufficiency through new tariff policies and improved financial planning paved the way for the second stage of privatisation. To encourage this and to attract a strategic investor to assume management responsibility for the corporatised company until the expiry of its monopoly, the EBRD extended a new corporate loan similar in size to the original loan. As a result, the Government was successful in selling a significant stake in the company to a foreign strategic investor. The new investor currently holds a significant minority stake in the company with control over its management. PED's evaluation verified that the Bank was instrumental in bringing about the privatisation process. New telecommunications legislation and regulation were introduced, especially to introduce competition in mobile services. Substantial infrastructure investments benefited domestic suppliers while international suppliers helped to develop skills in the telecoms sector. The process facilitated growth in mobile services in particular.

EBRD helps local bank to develop new services

The EBRD lent comparatively large sums to a leading bank in a country at the intermediate stage of transition for on-lending to small and medium-sized enterprises (SMEs) and to home owners for mortgage financing. Long-term financing, as provided by the EBRD, was not available via commercial channels and allowed the client bank to gain gradual access to international capital markets. Moreover, the relative stability of the

recipient bank allowed the EBRD to lend to a bank on a direct basis without a sovereign guarantee for the first time in this country. EBRD support helped the bank to develop a new focus on small business and retail banking. Evaluation confirmed that the EBRD's financing was successful in meeting the needs of the new market economy. The financing helped to promote new banking products and encouraged similar activities by foreign banks and newly privatised banks. This project was well-designed and implemented. It helped to set a positive example for other domestic banks and had a significant impact on the transition process.

Turnaround success in Russian manufacturing company achieved with strategic investor support

Following the privatisation in the early 1990s of a producer of building materials and components for the engineering industry in Russia, a strategic investor was sought to support reforms. The EBRD contributed equity financing via a controlling consortium in parallel with another multinational financier. Investments helped to improve product quality and energy efficiency as well as reduce risks concerning health and safety and the environment. Evaluation of the project confirmed that a long-term development strategy by a strong sponsor was key to the success of the project. The financing had a significant impact on the transition process, and good management helped to withstand a market downturn after the economic crisis in 1998. The project demonstrated how a company can successfully adapt its sales, production, quality control and accounting. The reform of the manufacturing firm was achieved because of the intervention of a competent and motivated strategic investor, which was able to gain full control of the company. As a minority investor, the EBRD remains on the supervisory board and is ready to intervene if necessary. PED's evaluation confirmed that further cuts in the workforce are needed to approach international productivity levels. Recent discussions have focused on possible international and domestic support to mitigate the social impact of further redundancies.

out whether they can be expected to act in their own interests or whether they are under obligation to other parties.

Alternative strategies for local investment support in absence of banking reforms. The decision to stop supporting a strong non-reformist regional bank should be taken only after careful consideration of the alternatives, taking account of the EBRD's country and sector strategies. Attempts to change a bank's

behaviour from within or through policy dialogue should be considered if there is no obvious competitor to support. If the regional banking market is unlikely to offer efficient assistance to investment activity for some time, the EBRD should focus its attention on supporting the corporate sector, either directly or through regional funds.

Examples of evaluated EBRD projects

Projects with a less successful outcome

A significant minority stake in a manufacturing company under domestic manager-owners fails to produce good results

The EBRD took a significant minority stake in a central European producer of technical equipment for buildings. The company had been privatised, leaving its top managers as the main shareholders. The EBRD's investment was based on a favourable evaluation of the company and its management. The capital investments resulted in the production of state-of-the-art products, which met the highest industry standards. However, sales were significantly lower than projected. An increase in sales to Western markets proved more difficult than expected and would have required major investments in the development of sales and distribution. Moreover, most of western Europe was already oversupplied. EBRD representatives on the company's supervisory board sought to encourage cost-cutting in response to the sluggish markets. They also put forward proposals to reschedule commercial bank loans and mobilised some turnaround management support. The management/owner majority, however, rejected any radical measures. A Bank-led search for a new strategic investor proved unsuccessful.

Evaluation by PED concluded that the operation had largely failed to support the transition process. The domestic managers/owners had failed to adopt reforms, placing the EBRD's equity investment in jeopardy. A more comprehensive appraisal could have helped to identify and mitigate some of the risks. Adequate structuring could have insisted that investment by the Bank was conditional on prior debt restructuring. The EBRD's minority stake was not sufficient for the Bank to play a key role in support of reform. The key lessons are that investments in corporate restructuring can experience difficulties in the absence of strong external strategic sponsors. Another lesson is that incumbent management in complex manufacturing companies are prone to asset accumulation rather than streamlining and cost-cutting in response to adverse markets.

Equity investment leads to slow reform of a large agribusiness group at its post-privatisation stage

The EBRD made an equity investment, with an optional follow-on loan, to a major partly privatised agribusiness group, which focused on foreign and domestic trading as well as the collection, storage and processing of some key domestic crops and agri-products. The Government retained an ownership stake alongside management and workers. EBRD representation on the corporate supervisory board, a programme of investments and reform led by the incumbent management were expected to pave the way for final privatisation in the medium term with the possible entry of strategic sponsors into some of the main business lines. The company's shares were widely held before the Bank's participation. Progress in reform was expected to be greeted favourably on the domestic market for equities, providing a potential exit route for the Bank. However, the reform process was hampered by management responding to signals from the Government rather than the markets. Another constraint was the difficulty in monitoring the performance of a multitude of subsidiaries.

Evaluation a few years after the equity investment recognised that the EBRD and its nominees on the Board had made considerable efforts to intensify reforms and to promote privatisation. The structure of manager and worker shareholders alongside a government stake limited the influence of the Bank and other minority shareholders. Privatisation of some of the main business lines met with political opposition in view of the links with the rest of the agriculture sector. Despite the potential for a high transition impact, the company's structure could not mitigate some of the key risks. The Bank's equity stake emerged as a poor investment, and the company never qualified for the intended reform loans. One of the key lessons is that restructuring of major former state monopolies is prone to excessive risk unless control is yielded at an early stage to competent strategic investors. As a minority investor, the EBRD cannot normally expect to form stable owner alliances in support of radical reform when the Government retains a significant stake alongside incumbent managers and workers. Large agribusiness groups with significant links to domestic primary agriculture can lead to additional political and regulatory risk, which may be mitigated only if the Government gives a binding commitment to firm privatisation timetables.

Cooperation with other MDBS and donor institutions

The EBRD collaborates extensively with other multilateral development banks (MDBs). In 2000 the Bank chaired the Evaluation Co-operation Group (ECG) and participated in its working groups on private and public sector evaluation. New joint studies were commissioned by the EBRD during the year with technical cooperation support from Sweden and the United States. These

included studies on the evaluation of institutional development and on harmonising the evaluation of public sector operations. The EBRD will continue to participate in joint ECG work on evaluation methods and harmonisation, contributing to and benefiting from the experience of other MDBs. PED also participates regularly in the Development Assistance Committee Working Party on Aid Evaluation of the OECD. These consultations have resulted in mutually beneficial cooperation on project evaluation.

Evaluating technical cooperation operations

Evaluation of technical cooperation (TC) includes in-depth OPERs of large TC operations, thematic studies and independent assessments of completion reports on TC operations by banking teams.

Since 1993, 30 OPERs have been prepared and nine special studies/mid-term reviews have been undertaken on projects and on areas where technical cooperation has played an important role. In addition, three studies on the quality and cost-effectiveness of Project Completion Reports have been completed since 1998. These studies have covered over 180 TC-funded consultant assignments, involving about €52 million of funding from some 30 donors under the EBRD's Technical Cooperation Funds Programme (representing about 8 per cent of total TC grants to the Bank). The evaluations concern TC-funded services in support of EBRD investments as well as "stand-alone" TC operations. The table below provides a general picture of the overall success of these TC operations, with the proviso that it includes too few examples to be considered as a representative sample of all TC operations.

The results are regarded by PED as largely satisfactory, although it is notable that, in contrast with reports on investment operations, no TC reports have yet achieved a "highly successful" rating. A common finding from these evaluations is that client commitment and "ownership" is a key condition for success. Another recurrent lesson is that monitoring by the EBRD can improve the outcome. A special study in 1999 indicated that investment operations with TC support generally obtained higher transition impact ratings than investment projects without TC assistance. Out of the 239 evaluated investment operations evaluated since 1993, 142 had received some form of TC support.

Performance ratings of TC projects 1993-2000

	Unsuccessful %	Partly successful %	Successful %	Highly successful %	Number of projects evaluated through OPERs	TC funding € million
1993	0	3	97	0	5	7.3
1993-94	0	18	82	0	8	8.6
1993-95	0	22	78	0	11	9.8
1993-96	0	23	77	0	14	11.9
1993-97	3	20	76	0	17	17.7
1993-98	2	30	68	0	22	29.7
1993-99	4	32	65	0	26	32.6
1993-2000	4	33	63	0	30	35.0

Examples of evaluated technical cooperation operations

Successful advisory services linked to small business loans

The EBRD lent €10.7 million to SMEs via commercial banks in Kyrgyzstan, a country with little SME credit on offer and still at an early stage of transition. The loan was channelled through the National Bank of Kyrgyzstan. The financing was accompanied by about €2.2 million of TC funding from various donors to assist the banks and their clients. SME lending consultants helped the banks to develop their credit systems and provided on-the-job training for staff. TC funding was also used to set up local business advisory service centres supported by SME consultants. The centres assisted entrepreneurs in preparing business plans and in improving management techniques. Evaluation conducted in 2000 found that the TC support had been a success. The loan was disbursed in spite of the country's adverse macroeconomic conditions, and the sub-loans were repaid and the funds on-lent to new SME borrowers. SME lending skills were developed effectively, with potential for extending this know-how into the banking sector as a whole. Several advisory centres were well-established. The project was seen as a model for SME support in the region, combining EBRD finance with TC-funded advice for both the intermediary banks and the SMEs.

Mixed results from TC support for Russian railway

To assist the Russian Ministry of Railways (MPS) in its plans to modernise the country's railway systems, the EBRD launched 13 TC operations totalling about €3.8 million. The studies and advisory components were intended to prepare the way for major capital investments and to support new strategies. Following completion of the TC operations, PED rated the transition impact as satisfactory. The TC operations had helped, for example, in the restructuring of MPS's auxiliary activities. The evaluation also confirmed that four in-depth TC-funded studies had clearly facilitated investments, including an EBRD loan of €97 million. Several other studies proved less successful in boosting investments, which were down-scaled to about a third of the originally envisaged amount. A recommended maintenance and improvement strategy was being successfully implemented but support for the signalling systems needed further refinement. Overall, the series of TC operations was rated as "partly successful".