



Operations Evaluation

The Loan Guarantee Instrument
for TEN-T Projects (LGTT)

An Evaluation Focusing on the Role of the EIB
in the Implementation of the Instrument

Synthesis Report

April 2014

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Operations Evaluation

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EVALUATION REPORT

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NOTICE

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GLOSSARY OF TERMS AND ABBREVIATIONS

AFS	Appraisal Fact Sheet
BAFO	Best-And-Final-Offer
Borrower	The legal persona with whom the Bank signs a Loan Agreement
CA	EIB Board of Directors
CBA	Cost-benefit analysis
COP	The Bank's Corporate Operational Plan (COP)
CRD	Credit Risk Department (EIB)
CRPG	Credit Risk Policy Guidelines
DAC	Development Assistance Committee
DG MOVE	EC's Directorate General for Mobility and Transport
EC	European Commission
ECG	Evaluation Cooperation Group
EFS	Eligibility Fact Sheet
EIB	European Investment Bank
EIRR	Economic Internal Rate of Return
EL	Expected Loss
EP	European Parliament
EPEC	European PPP Expertise Centre
EPC	Engineering, procurement and construction
EU	European Union
EV	Operations Evaluation (EIB)
FIIR	Financial Internal Rate of Return
FSA	Fact Sheet A
FSB	Fact Sheet B
FVA	Financial Value Added
JASPERS	Joint Assistance to Support Projects in European Regions
JESSICA	Joint European Support for Sustainable Investment in City Areas
JU	Legal Department
LGTT	Loan Guarantee Instrument for TEN-T Projects
LLCR	Loan life cover ratio
MC	EIB's Management Committee (q.v.) Internal EIB committee, comprising the Bank's President and Vice-Presidents
MS	Member States
NER	New Entrance Reserve
NPC	New Product Committee
NPST	New Products and Special Transactions
OPSA	Directorate for Operations in the European Union and Candidate Countries (EIB)
PBA	Planning, Budget and Analytics
PBI	Project Bonds Initiative
PCM	Project Cycle Management
PCR	Project Completion Report
PFLP	Portfolio First Loss Piece
PJ	Projects Directorate (EIB)
PPP	Public Private Partnership
RSFF	Risk Sharing Finance Facility
SBF	Stand-by liquidity facility
SDG	Steer Davies Gleave
SFF	Structured Finance Facility
RM	Risk Management Directorate
TA	Technical Assistance
UL	Unexpected Loss
TEN-T	Trans-European Transport Network
VA	Value Added

EXECUTIVE SUMMARY

This section summarises the results from the evaluation on the role of the EIB in setting up and implementing the Loan Guarantee Instrument for TEN-T Projects (LGTT).

In the early 2000s the Trans-European Network Transport infrastructure (TEN-T) programme appeared to be constrained in its speed and scale of development by the financial limitations of EU and member state public budgets.

The LGTT is an innovative financial instrument for supporting TEN-T projects. The instrument was developed by EC/EIB in the period from 2004 to 2007, based on a market testing exercise. Initially, about 35 TEN-T projects were thought to be able to benefit from the instrument. The LGTT was designed to (1) cover the traffic risk during the ramp-up period of TEN-T projects, (2) involve and increase private sector participation in the financing of the projects and (3) accelerate the implementation of the projects.

This evaluation was based on a review of relevant EU and EIB policies, regulation and programmes, a sector review and a market survey amongst key market players. At instrument level it involved an evaluation and rating of the use of the LGTT at instrument level, a detailed review of its design and a lending portfolio review in the TEN-T sector in the EU Member States (MS). In parallel there was an evaluation and rating of a sample of five LGTT projects out of a total of seven, plus two TEN-T projects which were eligible for the LGTT but did not use it.

In respect of LGTT's three key objectives noted above, the evaluation found that

- (i) Traffic risk was appropriately covered during the ramp-up period in the limited number of projects which benefitted from its use.
- (ii) Its use has 'locked-in' involvement of the private sector in projects rather than increasing their participation. This should be seen as a positive outcome in the context of a market in crisis.
- (iii) No evidence was found that the use of the LGTT has contributed to the acceleration of the overall implementation of the TEN-T network programme by accelerating projects. It did, however, prevent a major delay on project #22 in Germany.

The evaluation carries a mixed message of success. Its use at project level has brought benefits, but to a much smaller number of projects than initially envisaged. At instrument level the LGTT has largely failed to meet the objectives of increasing private sector participation and acceleration of projects. However, it has shown how the EIB can flexibly tailor a product to changing market needs and has shown the EC/EIB how they can jointly work on complex financial instruments.

Thus, there remains potential for its future use, provided some changes occur and the market retains an interest in the instrument. The reasons behind this mixed message are described in the key findings below, and the recommendations are outlined in a table following the findings.

The Key Findings

There was some market testing but no instrument level ex-ante assessment as to how likely the LGTT was to achieve its objectives. Without this assessment the emphasis quickly moved on to the practicalities of using the funds efficiently, and quantified targets were obscured in the development process.

LGTT took four years to be brought to the market after the market testing. This time period proved too long since the markets deteriorated substantially in the four years, a result of Europe's financial crisis. It led to much reduced market volumes, reducing the potential pipeline for the LGTT. The initial suggestion of 35 projects became a potential 14 eligible deals, and resulted in 7 signed deals. The current pipeline has 3 potential projects.

All sample projects have experienced reduced traffic volumes and, in one case within the sample, traffic is 30% down on initial forecasts. The evaluation notes difficulties with traffic forecasting in a period of financial crisis, and with the greater potential of correlated risks between projects in such severe economic conditions.

Despite this, the stated objectives at project level, to cover traffic risk during ramp-up and to improve ability of borrowers to service senior debt, were largely met. LGTT clearly facilitated financial close in a difficult market in all deals which used it. However, the availability period of the guarantee was often linked to refinancing dates rather than ramp-

up period per se. The funds guaranteed were more clearly linked to refinancing requirements and credit ratios rather than scale of traffic revenue losses.

There was strong marketing in the early years. However, the detailed development work on LGTT offers has been late in the project cycle (typically at tendering or at Best and Final Offer (BAFO) stage). This is too late to influence the instrument objectives of increased private sector participation or accelerated implementation of TEN-T projects, although it brought greater assurance that projects were ready for implementation and allowed stronger focus on project or operational objectives.

A market survey was conducted as part of the evaluation leading to the following observations on the instrument's attractiveness to the market

- Traffic risk during ramp-up is a small element of traffic risk and often related to medium to long-term traffic growth risks, which is the current main concern of private investors. The narrow initial definition of the risk coverage impeded the relevance of LGTT initially.
- The mechanism of indirect funding through Standby Liquidity Facility (SBF) providers was seen as an unnecessary complication of the instrument to the market. Currently, the funding is used to back a guarantee in favour of commercial banks which then provide a contingent SBF. The SBF can then be drawn by the project company in the case of unexpected reductions in traffic income of the project during the initial ramp-up period to assure senior debt service.

- A comprehensive and readily understandable product guideline was lacking.

Finally, there was consensus that the EIB was the right choice of partner for the EC providing the expertise and resource to develop, market and manage the early growth of LGTT. The experience with the instrument has helped in the development/shaping of further partnerships with the EC, although there is a view within the EC that some additional reporting would bring further comfort.

In summary, an ex-ante assessment at instrument level would have enhanced the understanding of the initial objectives and contributed to their prioritisation. The LGTT is an instrument that was designed before the global economic and financial crisis when it appeared that the coverage of a narrow portion of traffic risk would facilitate the private financing of at least 35 TEN-T projects. The fact that only seven projects have used the LGTT, when compared against, for example, the EIB TEN-T portfolio of 188 projects, suggests that LGTT has *de facto* become a niche product with limited potential reach. Furthermore, with only one project in the sample where the LGTT influenced the timeline, it would appear worthwhile to consider revising the LGTT design and marketing approach with a view to enhance its relevance and effectiveness.

Whilst the project cycle was generally well managed, this evaluation recommends a number of housekeeping improvements.

Against this general background, this evaluation has developed a set of specific conclusions and recommendations in key areas, which are presented in the table overleaf.

	Assessment		
	Project level (5 projects)		Instrument level
Relevance	4		1
Effectiveness	5		
Efficiency	1	4	
Sustainability	1	3	1
EIB Contribution*	3		2
EIB Management	5		

- Excellent
- Satisfactory
- Partly unsatisfactory
- Unsatisfactory
- High
- Significant
- Moderate
- Unsatisfactory

MANAGEMENT RESPONSE

The Bank's Management welcomes the results of the LGTT evaluation. These confirm the conclusions drawn in the evaluation carried out on behalf of the European Commission in accordance with the LGTT Cooperation Agreement.

The LGTT clearly provided significant value in all deals which used it, notably the flagship projects #26 and #24. However, as a result of Europe's financial crisis, the potential pipeline of projects with traffic based demand risk for the LGTT instrument has significantly reduced and the LGTT has now become a specialist application. In this context, it will be paramount that the CEF Financial Instruments are designed in a flexible way so that they could be adapted to changing market needs.

The LGTT has enabled the EIB, and the European Commission, to develop experience within the project finance market as a credit enhancement provider, paving the way for the development of future credit enhancement instruments such as the pilot phase of the Project Bond Initiative introduced in November 2012 and which has already seen an early take-up by the market. The operational and institutional experience gained to date in the implementation of LGTT will guide both the Bank and the European Commission in the joint objective to develop efficient products and instruments addressing continuing financing gap for European infrastructure.

In particular, the Bank's Management will, to the extent possible, seek to implement the recommendations of both the present and the Commission's own evaluations in the design of successor instruments to the LGTT under the Connecting Europe Facility (CEF).

The CEF is the Commission's 'flagship' programme designed to support infrastructure investments necessary to meet the EU's 2020 objectives in the areas of transport, energy networks and telecommunications (notably superfast broadband). The CEF includes provision for the development by the Bank of a range of debt and equity financial instruments. The Project Bond Initiative (designed to promote capital market financing of infrastructure) has been the first instrument developed by the Bank under the CEF. A number of the lessons from the LGTT experience have already been taken on board when launching the Project Bond Credit Enhancement instrument ("PBCE") in 2012.

The Bank and European Commission are currently working on a number of options to extend the range of debt instruments under the CEF. Amongst these is a direct successor to LGTT which will focus leveraging additional bank finance for European infrastructure projects. This will complement the Project Bond Initiative. The precise design of the successor instrument to LGTT remains subject to the conclusions of the European Commission's *ex ante* assessment (required for all new financial instruments). However, it can be anticipated that, relative to LGTT, this will extend both the range of eligible sectors and risk coverage. This is in line with the recommendations of the current evaluation report.

As a first stage, the Bank is currently negotiating with the European Commission provisions for the merger of the existing LGTT and Project Bond portfolios. Provision for this merger has been made explicitly in the CEF Regulation. The effect of the merger of the portfolios will be to increase significantly the leverage effect which can be achieved from European funds in infrastructure investment.

The Bank intends to conclude with the European Commission a Delegation Agreement for the development of CEF Financial Instruments in the final quarter of 2014. The new CEF financial instruments, including the potential LGTT successor, will be introduced in 2015 and 2016, benefitting not only from the current evaluation but also the evaluation to be carried out on the Project Bond Initiative in 2015.

In the interim, LGTT in its current form will continue to be available for suitable projects approved by the Bank until end-2014 as a complement to the Bank's PBCE and 'traditional' senior debt instruments

TABLE OF RECOMMENDATIONS AND REPLIES

The table below contains the recommendations made by this evaluation in summary form, as outlined in Section 6 of the report on Conclusions and Recommendations.

	DESIGN OF THE LGTT
R1	<p>A stronger upstream marketing effort</p> <p>Projects are only considered for assessment when they already have the characteristics that the LGTT essentially tried to promote. Emphasis should be on initial screening at an early stage when they still have the potential to be turned into projects with utilisation-based income and private participation. The LGTT should be promoted vis-à-vis the public authorities taking decisions regarding the procurement strategy for such TEN-T projects, so that these authorities can consider the possibility of using LGTT when making their decision. This would allow the instrument to have an impact on improved levels of private participation and implementation, and improve the impact on the overall TEN-T programme. Special efforts should be allocated to those countries where there is no PPP culture, perhaps in partnership with EPEC.</p> <p>A more comprehensive and readily understandable product guidelines document/website for customers should be produced, since there is now greater knowledge within EIB about the specificities of the LGTT and the various ways of using it. This would be linked to recommendations in R1.</p>
	<p>Management Response</p> <p>OPS agree on the importance of effective marketing of financial instruments, and promoting better understanding of these instruments amongst Procuring Authorities. For this reason, we welcome the provision for an advisory component under the Connecting Europe Facility (“CEF”), albeit that this may be under-resourced by the EC for the task at hand.</p> <p>In respect of LGTT, OPS devoted considerable time in meeting with Procuring Authorities to present the key features of the LGTT instrument and describe the value it could bring to demand-risk projects. OPS built on this experience on the introduction of the Project Bond Initiative, and has made still further efforts at outreach to the procuring and financing community, including commissioning marketing materials. Going forward, it is envisaged to prepare professional presentation materials for all CEF instruments (including potentially a revised LGTT instrument), in a similar format to the one prepared for the Pilot Phase of the Project Bond Initiative. It should nevertheless be recognised that Procuring Authorities themselves are solely responsible for defining their policy stance with respect to most appropriate way of procuring TEN-T projects (Design & Build, availability based/demand risk structures...).</p>
R2	<p>Shorter lead time for new instruments</p> <p>When LGTT was finally offered four years after the initial market testing, the financial and economic crisis had already eroded the number of LGTT candidate projects. It is essential that the lead time needed by EC/EIB to set up new financial instruments and take them to the market is kept short (say not more than one year). Once set up, there should be emphasis on retaining the instrument’s relevance and sustainability through, for example, revision of the instrument design based on an independent mid-term evaluation reflecting any changes to the market needs.</p>
	<p>Management Response</p> <p>OPS acknowledges the need to minimise the lead time to take new financial instruments to the market, and for retention of post-launch flexibility to ensure continuing adaptation and relevance to market needs. There may, however, be a trade-off between robust design and testing, and early introduction. In general piloting is to be welcomed – it is clear, for example, that there will be important lessons to be learned from the Pilot Phase of the Project Bond</p>

	<p>Initiative.</p> <p>All new financial instruments under the MFF will require the EC to prepare an ex-ante assessment (see R3). Whilst this is strongly to be welcomed to ensure robust analysis of market gaps/needs, this has the disadvantage of making the actual timing for the launch of an instrument to some extent outside the Bank's control.</p> <p>It is also to be welcomed that under the CEF regulations there is explicit scope for developing, modifying and fine tuning instruments during the 2014-20 period.</p>
R3	<p>Ex-ante assessment as to whether global objectives can be met</p> <p>There was no assessment as to whether the LGTT was likely to achieve the objective to accelerate implementation for the TEN-T programme overall or at project level. For any revised or new instrument, EC/EIB should include an ex-ante test in the market and feasibility assessment to assess the likelihood of the instrument achieving its overall objectives. For each potential project, EIB should carry out and present an explanation of how a potential project will contribute to the implementation of the TEN-T programme.</p>
	<p>Management Response</p> <p>An ex-ante assessment is now required under the CEF to launch a Financial Instrument; a detailed analysis of the markets needs will therefore be carried out before the instruments are implemented.</p> <p>All projects eligible for the LGTT instrument are on the TEN-T network and therefore contribute to the implementation of the TEN-T programme. Eligibility is explicitly checked and confirmed by the EC.</p>
R4	<p>The provider of Standby Liquidity Facility</p> <p>Market participants perceived the instrument to be complex, and specifically that indirect funding through Standby Liquidity Facility providers seemed an unnecessary additional complication of the instrument. There should be further discussion with the EC about mandating the EIB to directly provide liquidity to projects rather than through third-party Standby Liquidity Providers.</p>
	<p>Management Response</p> <p>At the time the LGTT was launched, there was considerable appetite from commercial banks to act as Standby Liquidity Facility providers. However, it is clear that, with hindsight in the aftermath of the financial crisis, such a requirement appeared to add only little value and to complicate significantly the use of the instrument.</p> <p>The Bank, and EC, have taken on board the lessons from the LGTT experience when launching the Project Bond Credit Enhancement instrument ("PBCE") in 2012; the PBCE is indeed directly provided by the EIB.</p>
	<p>MANAGEMENT BY EIB</p>
R5	<p>Clearer updated guidance and management of documents is needed for EIB Officers involved in the use of LGTT</p> <p>Documents related to LGTT at instrument level and at project level are sometimes difficult to trace. EIB should enhance its document management systems and discipline by, for example, creating a central platform, where all relevant documents are stored or hyperlinked.</p> <p>EIB should also develop written guidance for officers dealing with the LGTT, in particular in support functions who are not using the instrument on a daily basis (e.g. guidelines for traffic and revenue risk analysis in the context of LGTT operations). The analysis of the sample of projects suggests that the European economic crisis of recent years has had a significant effect</p>

	<p>across all projects.</p> <p>Management Response</p> <p>Accepted. A more efficient use of the GED tool is proposed for all Financial Instruments in the future. All relevant documents will be centralised in GED and specific folders will be created with limited access for confidential information (provided by consortiums during the tender phases of the LGTT projects).</p> <p>Training sessions will be organised with the relevant Services of the Bank to present the key features and likely impact of the Financial Instruments developed in the context of the CEF.</p>
R6	<p>Monitoring at instrument level going forward</p> <p>EIB should clarify and formalise responsibilities for the monitoring of LGTT and its transactions, with a view to facilitate sufficient focus and avoid conflict of interest issues. EIB should set up the capacity to monitor LGTT at instrument level, such that assessment can be quickly made of, for example, amounts signed, amounts at risk to be drawn or lost, headroom etc. EIB should also consider the option of dedicated monitoring of LGTT project transactions by a separate officer. This may require grouping with the monitoring of other joint instruments with similar potential conflict of interest issues.</p>
	<p>Management Response</p> <p>Mitigation of conflict of interest is anticipated in line with the conflict of interest guidelines recently issued by the Bank. Rules have been agreed between the services, foreseeing that responsibility for the origination stage (where instruments are negotiated and presented) rests with OpsA geographical divisions for senior debt and LGTT team for the LGTT instrument, whereas the responsibility for post-signature monitoring phase rests with TMR who keeps Ops informed. Within TMR, the monitoring of the senior instrument is performed by the Project Finance Monitoring team whereas the junior instrument/equity is monitored by the Equity Monitoring Team.</p> <p>In case a PF operation enters into a restructuring/distress phase, the TMR restructuring team takes over and proposes an appropriate restructuring strategy (case-by-case consideration) that aims to address Conflicts of Interest while ensuring a unified restructuring and / or recovery approach.</p>
R7	<p>Availability and quality of cost recovery information at instrument level.</p> <p>Operational services should work with SG/IS/PBA (and other Bank’s services as appropriate) to ensure separation of costs/revenues related specifically to such instruments from those linked to other elements of corresponding lending projects (e.g. senior debt in the case of LGTT). This recommendation should in particular be considered in the context of the Horizon 2020 implementation of the Horizon 2020, the Connecting Europe Facility and other new joint instruments, and in support of recommendations arising from the Joint Actions Working Group.</p> <p>In addition, the operational services should ensure the quality of instruments-related time records. In particular, specific attention should be paid to (i) timely creation of relevant product codes, which will enable proper tracking of pre- and post- signature costs, and (ii) ensuring the completeness and accuracy of time records of relevant staff working on such activities.</p>
	<p>Management Response</p> <p>OPS understands the importance of ensuring that costs and revenues are correctly recognised and can be accounted for and reported on accordingly. Ops will continue to work with SG to ensure that costs and revenues for different components of related activities can be separately identified in line with reporting and other requirements. This includes the timely notification of relevant product codes to enable the tracking of costs incurred at various stages in the</p>

	<p>lifecycle of an instrument. Product codes for the Connecting Europe Facility and Horizon 2020 instruments which have already been implemented in the time reporting systems will be further reviewed by OPS to ensure that the different components of instruments are separately identifiable.</p>
<p>R8</p>	<p>Further development of partnership with EC</p> <p>Whilst most of the reporting to the EC is performed as required, there were areas for improvement. In order to further promote the development of the partnership between EIB and EC it is recommended that</p> <ul style="list-style-type: none"> - At project level, EIB should enhance reporting to EC on financial risks for signed LGTT deals e.g. where risk profiles for individual projects are deteriorating significantly. - At an instrument level, EC/EIB should hold LGTT Steering Committee meetings more regularly or record why they are not held. - EC/EIB should confirm whether the development of further coverage of traffic risk beyond the ramp-up period is a workable option to enhance the relevance of design of the instrument to market participants and increase its likelihood of being effective.
	<p>Management Response</p> <p>OPS acknowledges that, whilst reporting obligations have been met, information sharing with the EC could be further improved, and welcome the suggestions made by EV.</p> <p>In addition, OPS notes that in the context of the CEF it will be even more important to implement robust reporting procedures; the reporting requirements under the CEF Delegation Agreement and Financial Regulation are indeed expected to be much more stringent while taking account of the delegated nature of the mandates. This will apply to all the so-called ‘centralised’ financial instruments developed jointly with the EC.</p> <p>OPS intends to bring forward plans to centralise certain reporting activities under the new Financial Instruments in order to ensure synergies and capitalise on best practices.</p>

INTRODUCTION

1.1 Background to the Evaluation

The Loan Guarantee Instrument for Trans-European Networks for Transport (TEN-T) Projects (LGTT) is a new financial instrument developed and funded jointly by the EC and the EIB. It is targeted at traffic risk during the ramp-up period in TEN-T projects, whose financial viability depends on utilisation-based income. The instrument was developed in the period from 2004 to 2007, based on a market testing exercise by the EC and the Bank which suggested a need for an instrument like the LGTT. The LGTT aims at facilitating a larger participation of the private sector in the financing of TEN-T projects with a view to accelerating the implementation of projects.

Following the development phase, the LGTT Cooperation Agreement (in the following the "LGTT Agreement") between the Bank and the EC was signed in January 2008. The risk sharing described in this agreement relies on four principles: (i) the risks are shared on a project-by-project basis; (ii) the capital provisioning is shared 50/50 between the EC and the EIB; (iii) the EC risk is capped at the amount of its budgetary commitment; while (iv) the residual risk is borne in full by the EIB. Initially, the LGTT was funded with a capital contribution of EUR 1 billion (EUR 500 million each from the EC and the EIB). The key roles and responsibilities of the EIB with respect to LGTT are outlined below.

The key elements of the LGTT Agreement, related to the management of the LGTT by the EIB.

- Article 2, Articles 7 and 8 provide details on the EC Contribution and Closing and Treasury Management Fees. According to Article 9, a review of the cost recovery mechanism can be requested by either party by end of 2009.
- Article 3 obliges the EIB to manage the LGTT Operations in accordance with the terms of this Agreement and its own rules, principles and procedures, good banking practice and appropriate monitoring and control measures. Furthermore, it assigns to EIB the tasks to (i) carry out product development and awareness raising for the LGTT, (ii) reporting as per Article 16, (iii) open, maintain and manage the LGTT account, and (iv) be responsible for treasury management of the funds on the LGTT Account in accordance with the Treasury Guidelines for Asset Management.
- Article 5 stipulates that LGTT credit risk shall be assessed by EIB in line with the rules for the SFF under the EIB's CRPG. It also sets the principles of risk and revenue sharing between the EIB and the EC, where the expected loss provision and capital allocation will be shared on a 50:50 basis, whilst the residual risk is borne by the EIB.
- According to Article 6, EIB shall maintain the LGTT Account related to the EC Contribution.
- Article 11 sets the procedural framework for LGTT operations. It stipulates that LGTT applications, appraisal and due diligence follow EIB's usual rules and criteria, pertaining to SFF. It requires that EIB obtains from the EC confirmation whether the operation concerns a TEN-T, and that EIB explains the financial structure of each LGTT operation.
- Article 15 requires a Steering Committee of four members (Director level) each from the EC and EIB and chaired by the EC shall supervise the implementation of the LGTT and meet at least annually or upon request by EIB or EC.
- Article 16 includes EIB's reporting obligations which are further detailed in Annex III regarding operational reporting and Annex IV regarding Financial Reporting.
- Article 19 requires all publicity material and events to mention the EC LGTT contribution.

Following the signing of the LGTT Agreement in 2008, a first project making use of the instrument was signed in 2008. Two other projects followed in 2009, one in 2010 and three more in 2011.

Some changes to the instrument are currently under preparation as detailed by regulation (EU) 670/2012¹. The first change would involve risk sharing arrangements, upon agreement of a Portfolio First Loss Piece (PFLP) approach². This change was incorporated into the LGTT Agreement in December 2013. The second change is to the capital available, given that only a proportion of the

¹ Regulation (EU) No 670/2012 of the European Parliament and of the Council of 11 July 2012, amending decision No 1639/2006/EC establishing a Competitiveness and Innovation Framework Programme (2007-2013) and Regulation (EC) No 680/2007 laying down general rules for the granting of Community financial aid in the field of trans-European transport and energy networks.

² Under the PFLP risk sharing approach, sharing of the First Loss Piece is 95% EC, 5% EIB for a portfolio of projects, up to a defined percentage of losses ("first-loss" cushion). Only if potential losses were to exceed the EC contribution, the EIB contribution would be used to cover such further losses on an agreed basis.

original capital allocated had been utilised. It was decided that EUR 200 million from the EC contribution to the LGTT would be re-allocated to the Project Bonds Initiative (PBI) in a pilot phase from 2012 to 2013 and a further EUR 50 million has been re-allocated to grant funding elsewhere.

The current LGTT Agreement stipulates that the “EC will carry out an evaluation by 2012 and that the EIB shall provide the necessary information”. EV has met with the relevant EC counterparts for the purpose of initial coordination as part of the early consultation exercise.

1.2 Approach and Sources of Information

This evaluation of the LGTT focuses on the EIB’s role in setting-up and implementing the LGTT instrument. It is based on an assessment at instrument and project level. The evaluation was carried out based on internationally adopted (DAC and ECG) evaluation criteria and in accordance with EV’s terms of reference. These criteria include Relevance, Effectiveness, Efficiency and Sustainability. In addition, EIB’s contribution and management of the instrument and its use in projects is assessed.

The approach to this thematic evaluation is based on the following steps and sources of information:

- A review of EU policies, regulation and programmes at the general level and with a particular focus on the TEN-T programme, new financial instruments and specifically the LGTT.
- A review of EIB policies, strategies and procedures with regard to TEN-Ts, financial and risk management.
- A sector and market review including an enquiry amongst key market players regarding market needs, design of the LGTT and the perceived role of the EIB.
- A detailed review of the LGTT design and its relevance in relation to the objectives pursued.
- A comprehensive review of the EIB lending portfolio in the TEN-T sector for the EU Member States (MS), analysing country distributions, sub-sectors, financing trends, as well as eligibility for LGTT and actual use of the instrument. This review includes an assessment of the coverage of the TEN-T portfolio by the LGTT and the circumstances supporting / limiting the use of the LGTT.
- An evaluation of a sample of five out of seven TEN-T projects in which LGTT was used, and two TEN-T projects which were eligible for the LGTT but where the project company did not make use of the instrument. The evaluations focused on the use (or not) of the LGTT in the projects rather than on the project performance and were undertaken in accordance with the EV standard method for in-depth project evaluation suitably modified to take account of the stage of development of the projects. They were based on desk study, interviews with EIB staff involved in the project, as well as meetings with the organisations responsible for project implementation and operation. Where relevant, site visits included meetings with representatives from national, local or regional authorities or other organisations.
- The evaluation of the LGTT at instrument level focused on the role of the EIB in setting up and implementing the instrument. This assessment is based on the review of instrument-level documentation concerning the LGTT (e.g. the LGTT Agreement, Steering Committee meeting minutes, credit risk guidelines), as well as on interviews with key staff from EIB and from the EC. The results of the above-mentioned market enquiry amongst market participants further informed this instrument-level evaluation of the LGTT.

The evaluation was carried out by internal EV staff with the assistance of consultants. The relevant operational directorates were consulted at the various stages of the evaluation, including an issues meeting in December 2012, a consultation process for the 7 in-depth reports, a workshop to discuss emerging findings and recommendations on 6 June 2013, as well as a consultation process for the present synthesis report. This synthesis report has also been consulted with the EC.

This synthesis report summarises the findings of individual LGTT project evaluations, and of an assessment carried out at LGTT instrument level. After presentation to the EIB’s Board of Directors, a shortened version of the report is posted on the Bank’s website and enters the public domain.

1.3 Structure of this Report

This report is structured as follows. After this introduction, section 2 provides the EU policy context as it evolved during the period when the LGTT was conceived and applied. Section 3 contains a

description of the LGTT, including its history, design and objectives. Section 4 presents background trends for the TEN-Ts (i.e. programme, implementation, time line), presents a portfolio review of TEN-T projects considered for financing by the Bank and of projects in which the LGTT was utilised, and explains the selection of the sample of projects which have been evaluated. Section 5 synthesises the results of the evaluation at project and instrument level of the LGTT according to the standard criteria for performance (i.e. relevance, effectiveness, efficiency and sustainability), the Bank's contribution as well as for management by EIB. Finally, section 6 summarises key conclusions of this evaluation and recommendations.

2. EU POLICY CONTEXT

Transport infrastructure is considered fundamental for the smooth operation of the internal market, for the mobility of persons and goods and for the economic, social and territorial cohesion of the EU, although most of the EU's transport infrastructure has been developed under national policy implementation.

In order to establish a single, multimodal network that integrates land, sea and air transport networks throughout the EU, the European policymakers decided to establish the TEN-T. The ultimate intention was to allow goods and people to circulate quickly and easily between EU MS and enable international connections. Establishing an efficient TEN-T has constituted a key element of the Lisbon Strategy for competitiveness and employment in Europe and is considered to play a central role in the implementation of the Europe 2020 Strategy, which aims at delivering high levels of employment, productivity and social cohesion.³

The TEN-T programme was initiated in 1990 and has been constantly evolving as shown below⁴:

- 1990: The EC adopts a first action plan on the TENs.
- 1993: The Maastricht Treaty gives the TENs a legal basis.
- 1994: The Essen European Council endorses 14 TEN-T projects to be completed by 2010.
- 1996: The European Parliament (EP) and the Council adopt the TEN-T Guidelines (Decision No 1692/96/EC).
- 2001: The EP and the Council adopt the amendment of the TEN-T Guidelines with respect to ports and intermodal terminals (Decision No 1346/2001/EC).
- 2003: A group chaired by Van Miert proposes new priority projects.
- 2004: Revised TEN-T guidelines and financial regulation are adopted, including a list of 30 Priority Projects to be completed by 2020.
- 2007: Regulation EC 680/2007 of the EP and the Council laying down the general rules for the granting of Community financial aid in the field of trans-national transport and energy networks
- 2010: Recast Union guidelines for the development of the TEN-T (decision No 661/2010/EU of the European Parliament and of the Council of 7 July 2010).
- 2011: Proposal for a Regulation establishing the Connecting Europe Facility.
- 2013: New TEN-T guidelines under discussion.

An emphasis has been put on cross-border connections, which are vital to the network but face major difficulties in being implemented since they receive less priority at the national level and require greater coordination efforts.⁴

By the beginning of the new millennium it was found that the pace of implementation of the TEN-T had not met expectations.⁴ In 2003, barely one third of the network had been built and only three of the 14 projects endorsed by the Essen Council were completed. The Van Miert High Level Group concluded that the TEN-T's implementation was constrained by financial limitations of the EU MS.

³ http://ec.europa.eu/transport/themes/infrastructure/index_en.htm.

⁴ European Parliament (2007): New Financial Instruments for European Transport Infrastructure and Services. Brussels.

As a consequence, ways were sought to involve private funding in the financing of the TEN-T and the concept of public-private partnerships (PPP) for TEN-T projects was promoted. PPPs were seen as a way to both accelerate infrastructure provision and facilitate faster implementation.⁵

The policy objective to promote PPPs⁶ in transport to accelerate TEN-T implementation was in principle complementary with the policy to apply the “user pays” principle through infrastructure charging e.g. in the form of tolls.⁷ However, it had also become apparent that excessive risk transfer can be a barrier for private investors.⁸

In 2003, the European Council endorsed the Growth Initiative which sought to mobilise investment in transport, energy and telecommunications infrastructure networks with a view to stimulating growth and creating jobs. A key element of the Growth Initiative was the deployment of innovative financial instruments with the aim of leveraging private finance. The two key instruments developed subsequently were Risk Sharing Finance Facility (RSFF) and the LGTT.

In 2006, the EC created the “Trans-European Transport Network Executive Agency”⁹ (TEN-T EA) to manage the TEN-T programme on behalf of the European Commission until 31 December 2015. Whilst the role of the European Commission’s Directorate-General for Mobility and Transport (DG MOVE) is to define the policy, the TEN-T EA implements and oversees the programme (see Annex 5b). The role of the TEN-T EA with regard to the LGTT is to advise DG MOVE on the eligibility of projects for the instrument and to verify and process transfer requests sent by EIB.

3. DESCRIPTION OF THE LGTT INSTRUMENT

3.1 Short History

The original idea to develop an EU loan guarantee instrument for TEN-T projects dates back to the early 2000s, when the project finance markets in the EU benefitted from an abundance of liquidity. However, whilst credit margins were at a historical low, user-based PPPs were unable to fully benefit from these conditions as funders were wary of traffic risk.

The EC identified possible areas of action within the framework of the Growth Initiative in its Communication of 11 November 2003. This included the possible creation of a new financial instrument, in the format of a guarantee to support TEN-T projects which could attract higher private sector participation. This Commission proposal was supported by the EIB.

The ECOFIN Council of 25 November 2003 adopted the final report on the European Action for Growth¹⁰ highlighting that issues to be resolved before any commitment concerning an EU guarantee instrument can be made. They include *“the funding of the instrument, appropriate risk diversification and budgetary risk management and its administration”*.

The European Council of 12 December 2003 invited the EC *“to further examine the necessity of developing a specific EU guarantee instrument for certain post-construction risks in TEN transport projects, to report on the results of that examination and, if appropriate, to present a proposal in this regard.”*

Following this request, the Commission services, in collaboration with the EIB, carried out a market testing exercise in 2005 to examine the feasibility of a loan guarantee instrument for transport projects. Based on this market testing exercise, the EC concluded that it would be appropriate to put in place a new EU loan guarantee instrument to support TEN-T projects. A proposal for the design of the guarantee instrument was presented in a Commission Communication to the Council¹¹.

On 20 June 2007, Regulation (EC) No 680/2007 of the European Parliament and of the Council laying down general rules for the granting of Community financial aid in the field of the trans-

⁵ EC (2003): Guidelines for successful public-private partnerships. http://ec.europa.eu/regional_policy/sources/docgener/guides/ppp_en.pdf.

⁶ Mobilising private and public investment for recovery and long term structural change: developing PPPs. COM (2009) 615.

⁷ EC (2001): White paper – European transport policy for 2010: time to decide. Brussels.

⁸ European Parliament (2007): New Financial Instruments for European Transport Infrastructure and Services. Brussels.

⁹ (2007/60/EC) Commission Decision of 26 October 2006 establishing the Trans-European Transport Network Executive Agency pursuant to Council Regulation (EC) No 58/2003.

¹⁰ ECOFIN of 25 November 2003, 15352/03.

¹¹ COM(2005)76.

European transport and energy networks was adopted, which forms the legal basis for Community financial aid in the form of the LGTT. According to Regulation (EC) No 680/2007 the EIB manages the EC Contribution to the LGTT on behalf of the Community.

On 7 June 2006, the EIB's Board of Governors approved a gradual increase of the SFF Reserve by an overall amount of EUR 3 000 m to a maximum ceiling of EUR 3 750 m and an immediate increase by EUR 500 m to EUR 1 200 m. Inter alia, this increase was designed to enable EIB to develop the LGTT with the EC. On 3 June 2008 the Board of Governors approved a further increase in the SFF through a transfer of EUR 1 500 m from the Additional Reserves of the Bank.

This paved the way for the signing of the LGTT Agreement between the EIB and the EC on 11 January 2008. This stipulated that the credit risk pertaining to LGTT Operations should be assessed and quantified by the EIB, in accordance with the rules applicable to the SFF, and in particular in accordance with the EIB's Credit Risk Policy Guidelines (CRPG).

No pilot transactions were implemented prior to the signature of the agreement as the set-up of the LGTT instrument was only finalised in 2008, after the current budgetary period 2007-2013 had commenced. In this period seven projects have benefited from use of LGTT.

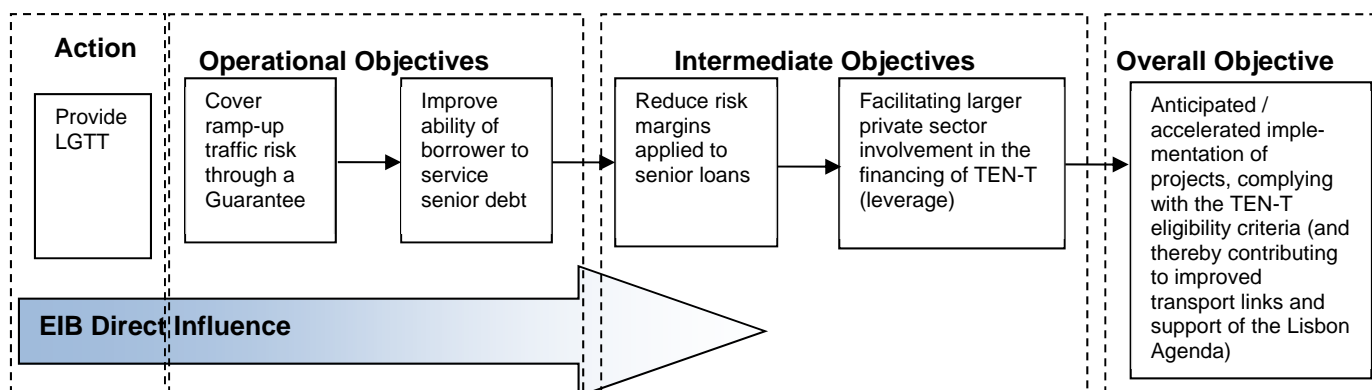
On 11 July 2012, Regulation (EC) No 670/2012 of the European Parliament and of the Council amending Regulation (EC) No 680/2007 and laying down general rules for the granting of Community financial aid in the field of the trans-European transport and energy networks was adopted, which introduced the concept of a Portfolio First Loss Piece (PFLP) approach. Negotiations with the EC are still on going to incorporate this change into the LGTT Cooperation Agreement. Further, given that the capital available had only been partly utilised, it was decided that EUR 200 million from the EC contribution to the LGTT would be re-allocated to the Project Bond Initiative in a pilot phase from 2012 to 2013 and EUR 50m re-allocated to grant funding.

3.2 Objectives

A review of relevant documents revealed the following objectives of the LGTT:

- Providing guarantee coverage for traffic risk during ramp-up in TEN-T projects;
- Significantly improve the ability of borrower to service senior debt during ramp up and to enhance the credit quality of the senior credit facilities;
- Reduce risk margins applied to senior loans to the project - savings in risk margins should be higher than cost of the guarantee;
- Facilitating larger participation of the private sector (leverage effect) in financing the TEN-T;
- Accelerated implementation of TEN-T projects; and thereby leading to improved transport connections and enhanced conditions for mobility;
- Thereby contributing to the Lisbon Agenda / Europe 2020.

On that basis, EV reconstructed the LGTT intervention logic, which is depicted hereunder.



3.3 Design

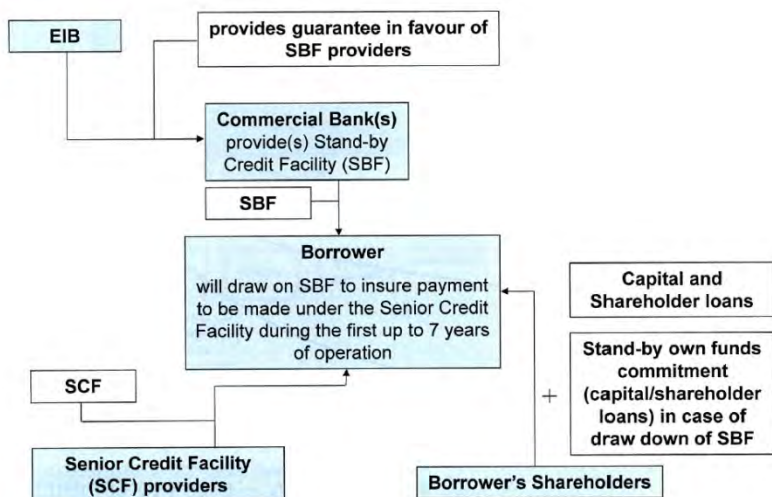
The LGTT¹² is a joint financial instrument by the EC and the EIB to cover traffic revenue shortfalls during the initial operating period (ramp-up) of eligible TEN-T projects. Ramp-up risk in the core sense is the risk of users slowly discovering the infrastructure and volumes of traffic being low for an initial period only. However, risks in the ramp-up period can also include the uncertainty of the level at which *long-term* traffic flow stabilises.

To be eligible for the LGTT, projects must be TEN-T compliant, derive utilisation based income (e.g. user tolls), benefit from the support of national authorities and demonstrate an appropriate level of private sector financial participation. TEN-T Priority Projects are to be preferred should the funds available for LGTT prove insufficient.

For each project, the risk capital for the LGTT is jointly provided by EIB and the EC as a guarantee provided to commercial banks which are contracted to provide a stand-by liquidity facility (SBF) that can be drawn by the project company in case of unexpected traffic income reductions during the initial ramp-up period to guarantee senior debt service. The SBF can be drawn down only in the initial ramp-up period, but after construction completion. Availability period can be up to seven years with a size limit for LGTT per transaction of 20% of senior debt and a ceiling of EUR 200 million.

All repayments on the outstanding amounts of the SBF are made on a cash sweep basis. These are subordinated to the senior loans underpinned by it, subject to specific needs of a given financial structure. If at the end of the availability period there are still amounts outstanding under the SBF (interest, interest accrued and principal), the LGTT guarantee can be called upon by the SBF providers, and the EIB would pay out to the SBF providers and then become a subordinated creditor to the project. Once EIB becomes a creditor to the project, amounts due under the LGTT will still rank junior to the debt service of the senior credit facility and would be repaid either on a cash sweep basis based on the cash available after senior debt service (default solution) or on a fixed reimbursement profile of the LGTT debt, *but before* equity dividends are made.

The parties involved in a project finance operation making use of the LGTT and the relationship between them are depicted in the figure hereunder.



However, while this is the general case there are exceptions, as explained in later sections. The Bank's Credit Risk Policy Guidelines note that the pricing for financial instruments to reflect risk comprises three elements: (i) an incremental margin required to cover the Expected Loss of the operation, calculated in accordance with an Expected Loss Methodology (ii) the incremental margin required to deliver the returns on the capital allocation, and (iii) a mark-up (which includes allowance for residual risk). Risk and revenue sharing between EIB and EC is, to date, 50:50 with regard to the expected loss and the capital allocation, whilst EIB is solely responsible for the residual risk, which it prices for.

¹² <http://www.eib.org/about/documents/lgtt-fact-sheet.htm>

4. TEN-T / LGTT PORTFOLIO REVIEW AND SAMPLE SELECTION

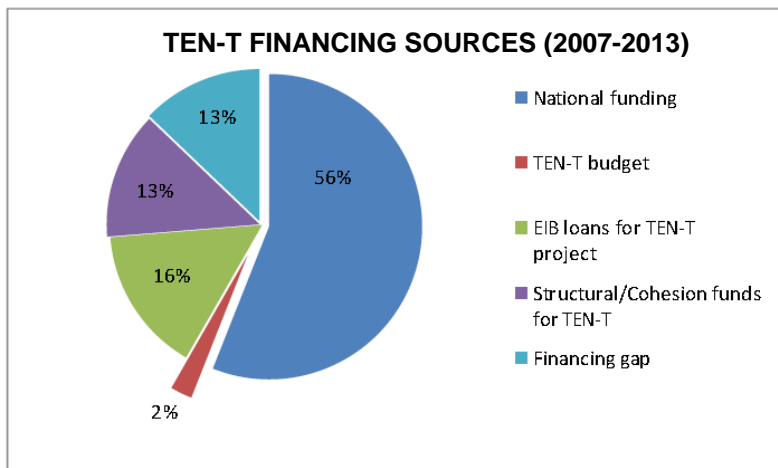
4.1 Background on the TEN-T Programme and PPPs

The TEN-T programme has been described¹³ as consisting of “*hundreds of projects – defined as studies or works – whose ultimate purpose is to ensure the cohesion, interconnection and interoperability of the trans-European transport network, as well as access to it. TEN-T projects, which are located in every EU Member State, include all modes of transport (i.e. road, rail, maritime, inland waterways, air, logistics, co-modality and innovation)*”. There is no comprehensive, publicly available database of the TEN-T programme, listing all projects and their implementation status.

The TEN-T programme will provide the infrastructure needed for a smooth functioning of the internal market, to ensure economic, social and territorial cohesion and to improve accessibility across the entire European Union (EU) territory. The TEN-T is mainly defined through maps, which were last updated through decision No 661/2010/EU of the European Parliament and of the Council of 7 July 2010. A further revision of the programme has been recently agreed.

Within the TEN-T programme, there are 30 Priority Projects (or axes), which have been identified on the basis of proposals from the EU MS and are included in the EU guidelines for the development of the TEN-T as projects of European interest. Of the 30 Priority Projects, 18 are railway projects, 3 are mixed rail-road projects, 2 are inland waterway transport projects and one refers to Motorways of the Sea. This choice reflects a high priority to more environmentally friendly transport modes, contributing to the fight against climate change. Some of the Priority Projects are very large-scale and have already been completed. Further important sections of the remaining 26 Projects have also been completed in recent years.

The remaining cost of implementing the TEN-T network has been estimated by the EC at EUR 500 billion, including EUR 253 billion for the Priority Projects. The investment needs for the programming period 2007-2013 were estimated at EUR 350 billion. This was a sizeable investment for public sector budgets to undertake and the EC estimated that there would be a funding gap of 13% or some EUR 45 billion (see graph below), which could not be covered from public sources, including EC funds and EIB loans. The EC therefore encouraged the private sector to play a greater role in the financing of EU transport infrastructure.

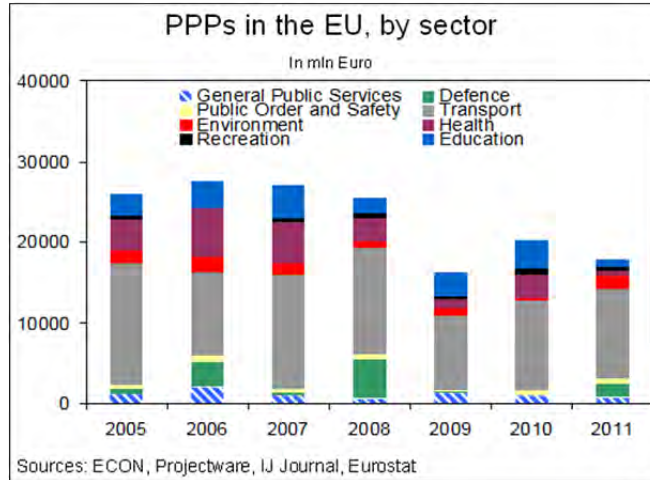


Source: Mid-Term Evaluation of the TEN-T Programme 2007-2013 by SDG (2011).

There is little direct evidence available on the impact of the financial crisis since 2008 on the implementation of the TEN-T overall. According to the EC’s “Mid-Term Review” of the Multi Annual Programme, the crisis had a mixed impact on the portfolio of 92 TEN-T infrastructure projects that started in 2007 and were set to be completed by 2013. Some projects benefited either from reduced market prices under increased competition or from additional funding either from EIB or as part of national recovery plans, whereas the majority were affected by budgetary cuts and will inevitably be

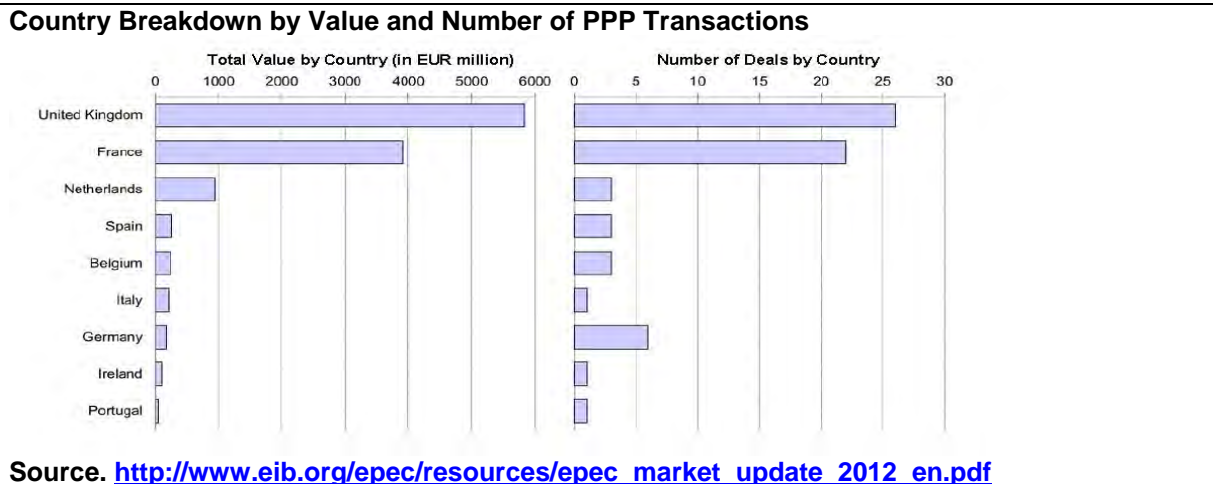
¹³ TEN-T Agency website and Presentation by the TEN-T Funding & Financing Perspectives Expert Group n°5 (2010) http://tentea.ec.europa.eu/download/events/june2010infoday/ppp/ruyters_20100601_ppp_seminar_superfinal.pdf.

delayed. For the 92 projects, the participation of the private sector and the presence of Public-Private Partnerships (PPP) were limited.



Since the information available specifically on transport sector PPPs is limited, it was, therefore, assumed within this evaluation that the general pattern observed for the overall PPP market shows similar trends for the transport sector. This was confirmed anecdotally in the survey and interviews. Interestingly, transport – which accounts for the largest share of total PPP financing requirements – shows only moderate fluctuations over time. Nevertheless, the graph indicates that shortly after the introduction of the LGTT in 2008, the heyday of PPPs in the transport sector was over.

Only nine MS have a noteworthy PPP market, of which the UK and France are by far the leading MS both in terms of value and number of deals. The Netherlands follow in terms of deal value and Germany in the number of deals. This concentration in North Western Europe may represent a geographical limitation for the use of the LGTT.



4.2 Review of the EIB’s Portfolio of TEN-T and LGTT Projects

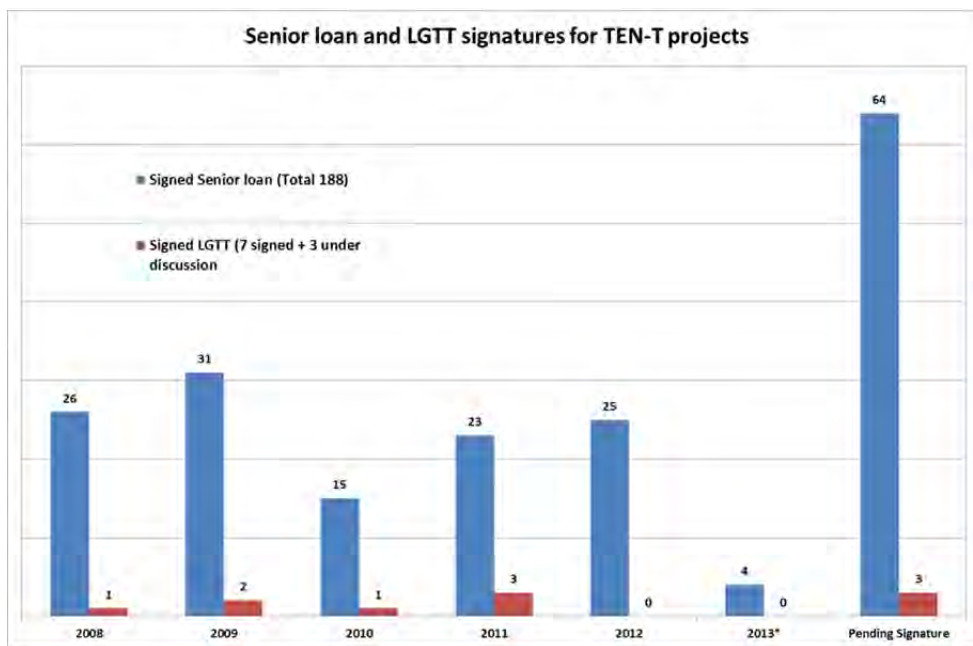
Two approaches have been used to assess the potential market for LGTT. In the first (section 4.2) the EIB’s TEN-T portfolio is reviewed as a proxy for the potential LGTT market and a sub-set of potentially eligible projects created. In the second (section 4.3), the projects recorded by the EIB team as forming the LGTT Pipeline are assessed. In Section 4.4, the portfolio sub-set was compared to the LGTT pipeline project list.

The EIB has a long history of TEN-T financing and is financing a sizable portion of implemented TEN-T projects. With no current comprehensive TEN-T programme public database listing all of the projects and their implementation status, the EIB’s overall TEN-T portfolio was thought to be of suitable character to identify a sub-set of projects potentially eligible for the LGTT instrument.

4.2.1. EIB TEN-T Portfolio

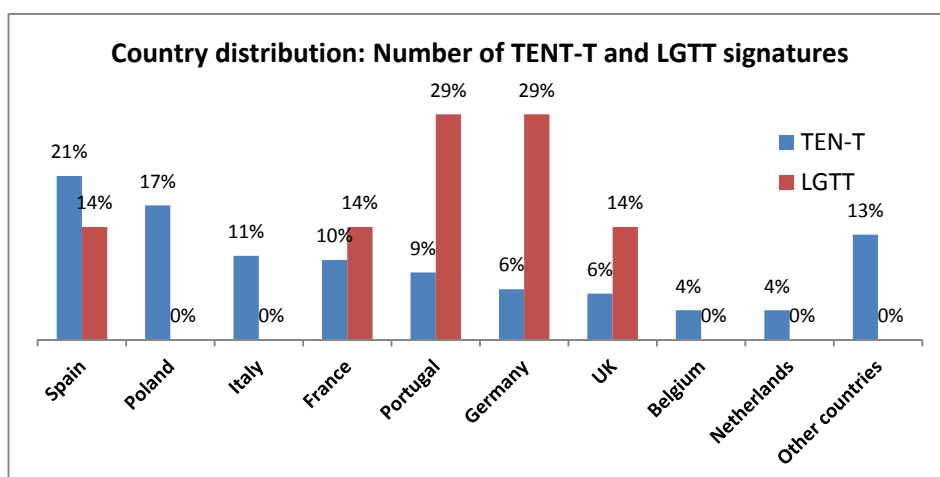
Since the launch of the LGTT in 2008, 188 TEN-T projects have been signed (65%)¹⁴ by the EIB or are pending signature (35%) for a total loan amount of EUR 58bn. Half of this amount corresponds to road projects, one third to rail projects, and the rest to air (11%) and maritime (7%) projects. By countries, the top signatory is Poland (23%), followed by Spain (20%), Italy (12%), France (9%), UK (7%) and Germany (7%). On average, the EIB has been financing EUR 305m per project, although there is a large variation in the size of the loans (minimum amount of EUR 12m, and maximum amount of EUR 1,300m).

The chart below presents, for the 188 projects of the EIB TEN-T portfolio, the annual number of approved senior loans and LGTT for TEN-T projects from 2008 to March 2013. The LGTT was used in a very small proportion of these projects. Following the peak in 2011 (3 LGTT signatures) there have been no LGTT signed agreement in 2012 and the first half of 2013.

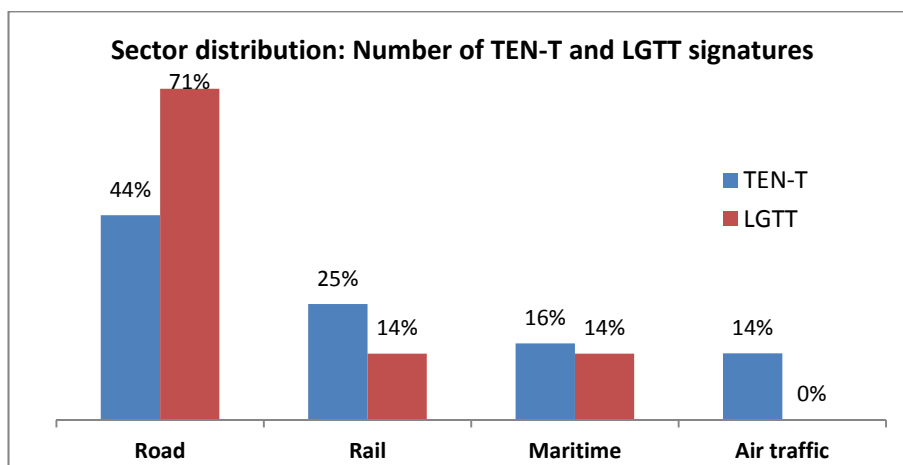


As can be seen from the figure on next page, comparing the EIB TEN-T portfolio and the LGTT portfolio, the countries where LGTT agreements have been signed are countries with the higher numbers of TEN-T projects. The exceptions are Poland and Italy (in the case of Italy there are projects in the pipeline but not signed).

¹⁴ As at March 2013



With regard to sectoral distribution, the guarantee instrument has been used most often for road projects. The subsector distribution reflects the fact that a) more road projects were tendered during the period and b) road projects typically use a transport PPP whereas corporate structures are predominant in ports and airports (with very few ring-fenced¹⁵ structures).



4.2.2. Eligible TEN-T projects

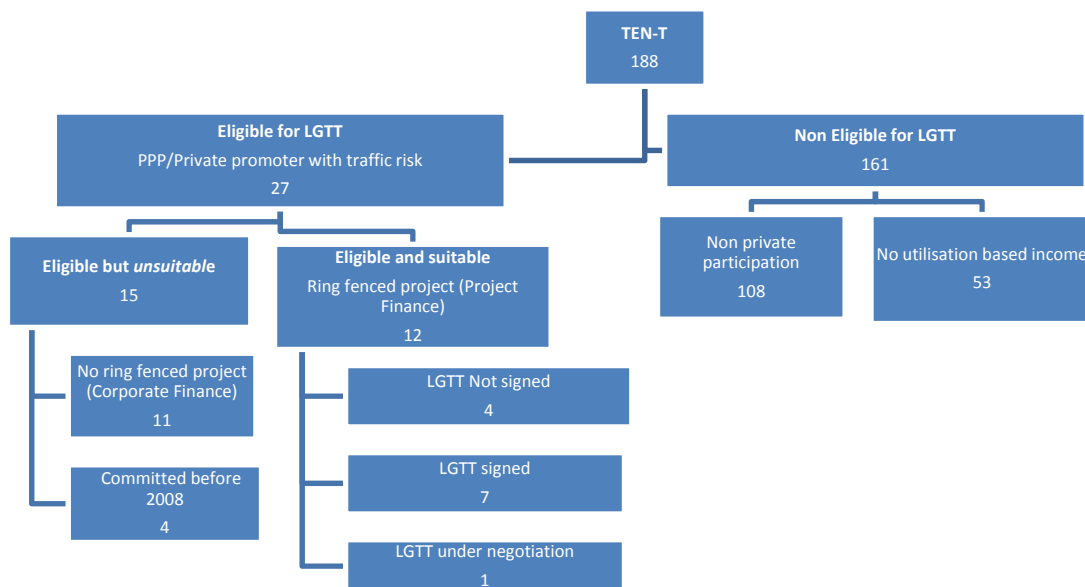
The LGTT Agreement includes four different eligibility criteria listed in the box hereunder.

- Eligibility criteria for the LGTT instrument (LGTT Cooperation Agreement, § 10)**
1. TEN-T Projects compliant with Community law are eligible for LGTT Operations.
 2. The financial viability of the project benefiting from an LGTT Operation shall be based, in whole or in part, on revenues, tolls or other utilisation based income.
 3. The TEN-T Project eligible for an LGTT Operation shall benefit from the support of national authorities and demonstrate an appropriate level of private financial participation.
 4. Should the EC Contribution available on the LGTT Account be insufficient to meet all the eligible applications, priority shall be given, to the extent possible, to TEN-T Priority Projects.

¹⁵ Ring-fencing occurs when a portion of a company's assets or profits are financially separated without necessarily being operated as a separate entity

The EC’s reasoning for approvals to date has been restricted to criterion n° 1, and establishes whether or not a project is a TEN-T¹⁶. This then suggests the other three criteria are assessed during the due diligence process by the Bank, and arguably even as a consequence of EIB offering the LGTT (i.e. a road project might become a viable toll road PPP with the use of the LGTT).

In order to identify a list of potentially eligible projects for the use of the LGTT from the EIB portfolio, EV has used the four eligibility criteria to classify the 188 projects in the Bank’s overall TEN-T portfolio (see Appendix 6).



The fulfilment of the first criterion is easily identified. As stated in the LGTT Agreement, the EIB sent the applications to the EC and DG MOVE and received confirmation on the operation’s status as a TEN-T project.

The second criterion implies the exclusion of all projects not having utilisation based income (e.g.: public projects without payment, concessions with availability payment), reducing the list of projects to the ones which have traffic revenue risk (real and shadow tolls). Although the original purpose of the instrument was to cover traffic risk during the ramp-up period, the eligibility criteria within the LGTT Agreement do not refer to ramp-up risk explicitly.

The third criterion, on support of national authorities and private financial participation, has some uncertainty regarding the ‘appropriate level of private financial participation’:

- a. Project finance deals are deemed eligible as long as the project is suitably ring-fenced and reliant on traffic revenues and has a private finance element. With one case of precedence in the sample, projects with a 100% private sector borrower have in this section also been classified as potentially eligible for LGTT.
- b. However, publicly owned transport companies are ruled out. Uncertainty arises in the situation, which is not uncommon in the transport sector, that the public authority has let a concession to a limited but publicly owned company which raises finance from commercial banks. For the purposes of this section such projects were excluded, as EIB’s view was that they were not eligible.

There was also uncertainty whether ‘support from national authority’ means financial or just political support. One project in the sample (#24) is clearly only the latter.

The fourth criterion, to prioritise TEN-T priority projects in case of scarcity of funds, has never been applied as the EC Contribution was more than sufficient for the number of applications received.

¹⁶ Article 11.4 of the EC-EIB Cooperation Agreement: “The Designated Service, represented for the purposes of this paragraph by the director in charge of Trans-European networks in DG TREN, shall confirm within 15 Business Days of the receipt of the fact-sheet whether the operation envisaged is a TEN-T Project”.

Following these assumptions, and as shown in the diagram above, a high proportion (161 of 188 or 85.6%) of the TEN-T projects signed (or pending of signature) for senior loans by the EIB would be non-eligible for the LGTT, as 1) there is no private participation for 108 projects (57.4%), or 2) there is no utilisation based income for 53 projects (28.2%).

The potentially eligible projects for the use of the LGTT represent just 27 projects or 14.4% of the EIB overall TEN-T portfolio in terms of number of projects. This would have been, in principle, 'the market' for LGTT, as currently designed. However, out of this list of 27 potentially eligible projects, 15 are considered unsuitable for the use of the LGTT as alternative financial commitments were already in place at the time of the possible introduction of the instrument (four projects) or they were set up as a corporate rather than a project finance deal (nine projects).

In the latter cases, rather than ring-fencing the revenues of the new project and raising funds against this future revenue stream (the risks of which LGTT is designed to mitigate), the project can be secured in other ways. If it is an extension of an existing facility or an extension to a network which is already the business of a company and the borrower therefore has a track record and an established balance sheet, the simplest finance route is often a corporate loan secured against the company balance sheet. Such projects do not need a separate guarantee covering traffic risk if this is small in respect to the size of the balance sheet.

As a result of the above screening process carried out by EV, there were 12 projects to which LGTT could have been allocated or 6.4% of the overall TEN-T portfolio (e.g.: projects potentially eligible and suitable for LGTT), of which:

- 7 have been signed with an LGTT.
- 1 has been signed post-evaluation (project #28) but did not use LGTT.
- Of the remaining four, one was considered for the use of the LGTT (project #19). The team worked on pre-bid offers but the winning bidder did not take up the offer of LGTT (this project is analysed in this evaluation). For the other three projects, in principle, one is on hold, and the other two have been signed with a different finance structure that makes them 'de facto' unsuitable for the LGTT (e.g.: refinance operation and intermediate loan).

This sub-set of 12 projects can then be compared to the projects which were *actually* brought forward.

4.3 LGTT Pipeline and Signed Projects

Since the launch of the LGTT, the EIB has submitted 29 LGTT Eligibility Fact Sheets (EFS) to the EC for TEN-T eligibility confirmation¹⁷. These 29 projects have constituted the '**LGTT Pipeline**'¹⁸, the projects preselected by EIB for the use of the LGTT. As noted at the start of the previous section, this appears slightly different from the 27 projects adjudged to be eligible from an assessment of the EIB's wider TEN-T portfolio.

The historical LGTT Pipeline can be disaggregated into: (i) projects signed with LGTT, (ii) projects signed without LGTT and (iii) projects postponed. Three projects constitute the "**current LGTT Pipeline**", projects where the LGTT is currently under discussion.

Since 2008, the expected financial total guaranteed through LGTT could have exceeded EUR 3bn for the 29 projects. Up to date 16% of this amount has been signed (7 projects) and a further 18% is under negotiation (3 projects). The remaining amount (66%), corresponding to 19 projects, has been cancelled because either the underlying projects were cancelled/postponed or they were signed without an LGTT. See *historical and current LGTT Pipeline Table in 4.3.1*.

4.3.1. LGTT Pipeline Review

The table overleaf shows the LGTT Pipeline, with the 29 projects that were considered for the use of the LGTT. By sectors, most of the 29 projects in the LGTT pipeline were road projects (21), followed by rail (4), maritime (2) and air (2) projects. To date, 5 road projects have been signed, 1 rail project and 1 maritime project. No LGTT was signed for an air project so far.

¹⁷ Source: LGTT Operational reporting to the European Commission as of December 31st 2012.

¹⁸ The differences between the LGTT Pipeline and the classification of the TEN-T projects eligible for LGTT elaborated by EV in 4.2.2 are explained in 4.3.1.

By countries, seven projects were preselected for LGTT in France, six in Italy, four each in Portugal and Germany, three in Poland, and one project each in Greece, Netherlands, Romania, Spain and UK. This led to two project deals signed in both Germany and Portugal and one in France, Spain and the UK, a geographical distribution in line with EU PPP distribution as noted before.

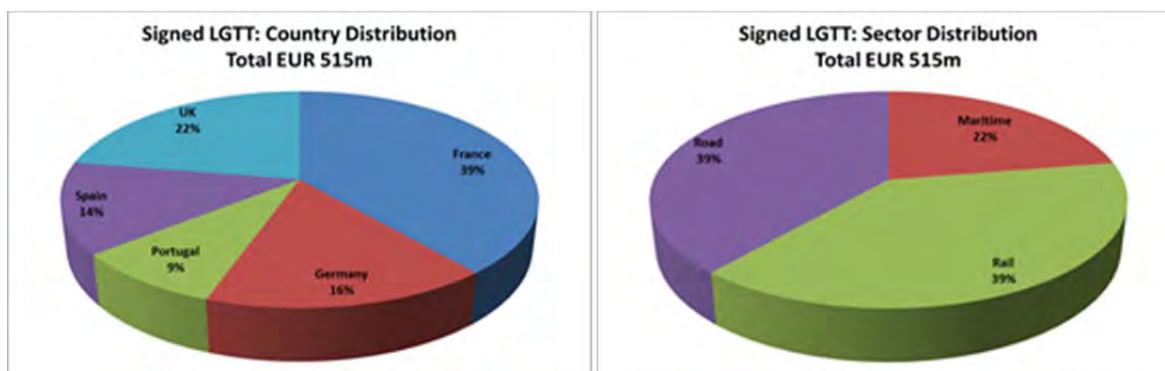
The EC confirmed that 27 out of the 29 projects in the original LGTT pipeline were TEN-T, one project in Romania and one in Portugal were rejected for not being TEN-Ts. Only two of the seven projects (#26 and #20) fulfil the criterion of being a priority TEN-T. However, this is in line with the overall TEN-T portfolio: where only 38 out of the 188 TEN-T projects were priority projects. Another project (#21) includes a significant proportion of non-TEN-T priority road sections.

As noted before, the current LGTT Pipeline has 3 projects that are under discussion.

Historical and current LGTT Pipeline

	Country	Sector	LGTT m EUR	Comments on Eligibility	Included in 4.2.2 TABLE
PROJECTS CANCELLED OR POSTPONED					
1	Germany	Road	80		No, as the 188 TEN-T projects only includes active projects
2	France	Rail	100		
3	France	Road	70		
4	Italy	Road	50		
5	Romania	Road	150	Rejected by EC: No TEN-T	
6	Portugal	Road	100	Rejected by EC: TEN-T<50%	
7	France	Rail	35		
8	France	Rail	20		
9	France	Road	70		
10	Netherlands	Maritime	80		
11	Germany	Road	70		
12	Greece	Air	150		
13	Italy	Road	200		
14	Italy	Road	200		
PROJECTS SIGNED WITHOUT LGTT					
15	Poland	Road	200	Non eligible (Availability)	Part of 161 non eligible
16	Poland	Road	200		
17	Portugal	Road	100		
18	Poland	Air	20	Non Eligible (no private participation)	
19	France	Road	160	Eligible and suitable	Part of 14 eligible and suitable
PROJECTS SIGNED WITH LGTT					
20	Portugal	Road	20	Eligible and suitable	Part of 14 eligible and suitable
21	Portugal	Road	25		
22	Germany	Road	25		
23	Spain	Road	70		
25	Germany	Road	60		
26	France	Rail	200		
24	UK	Maritime	115		
CURRENT LGTT PIPELINE					
27	Italy	Road	200	Non Eligible (100% Public entity)	Part of 161 non eligible
29	Italy	Road	160	Non Eligible (100% Public entity)	Part of 161 non eligible
28	Italy	Road	200	Eligible and suitable	Part of 14 eligible and suitable
-	France	Road	200	Information non available	Added March 201 ¹⁹ 4
-	France	Road	200	Information non available	Added March 2014
TOTAL LGTT PIPELINE: 29 Projects for a total amount of EUR 3130m					

¹⁹ The final two projects were added to the pipeline as part of the review of this report in March-April 2014 but were not included in the original analysis in this section.



4.4 Conclusions from the LGTT portfolio review

The main differences between the 29 projects preselected by the EIB for the use of the LGTT (historical and current LGTT pipeline) and the 27 projects classified by EV as potentially eligible for LGTT are the following:

Active projects: The projects in the LGTT pipeline are projects where LGTT was initially proposed by the EIB, some of them were later cancelled or postponed and others were signed (with or without LGTT). The EV classification detailed in section 4.2.2 is based on 188 active TEN-T projects, signed or pending of signature.

Eligible projects: EV classification in 4.2.2 is based on the LGTT Agreement Eligibility criteria, and thus projects with no private participation or with no utilisation-based income were classified as non-eligible.

Eligible and suitable projects : Out of the 12 eligible and suitable for LGTT projects in the EV analysis in section 4.2.2, 7 have been signed with LGTT, one without LGTT (#19) and one is in the current pipeline. The remaining 3 projects are not in the LGTT Pipeline as they were not considered for LGTT.

From this assessment it can be concluded that:

- LGTT addresses only a very small part of the TEN-T market (14%), focusing on PPPs/Private Finance/utilisation based income schemes. The main demand for it is in countries which have a PPP culture and experience (with the exception of Portugal & Italy).
- LGTT appears to be more suitable for road projects than for other transport sub-sectors. The reasons for that are diverse and may include that a) more road projects were tendered during the period and b) road sections can be more easily ring-fenced than elements of air and maritime transport infrastructure.
- In the identification process, projects which are considered eligible for LGTT are those which already had the characteristics that were required by the LGTT Agreement, including an appropriate share of private sector participation.
- The launch of LGTT coincided with a deep and extended financial crisis.
- A total amount of EUR 3bn could have been guaranteed across the 29 projects preselected by the EIB for the use of the LGTT (see historical and current pipeline table). To date 16% of this amount has been signed (7 projects) and a further 18% is under negotiation (3 projects). The remaining amount (66%) corresponding to 19 projects has been cancelled because either the underlying projects were cancelled (11) or they were signed without an LGTT²⁰ (5) or LGTT was removed from the negotiations (3).

4.5 Sample Selection for LGTT Evaluation

In order to be able to draw comparisons between TEN-T projects with and without LGTT, the sample for in-depth evaluation includes five LGTT transactions (nos. 1-5 below), as well as two projects

²⁰ 2 have been evaluated in-depth in this Evaluation.

which were in the original LGTT pipeline, but where LGTT was not used for different reasons (i.e. *A63* in France and *Gdansk Airport* in Poland).

Project n°	Country	Year of signature	LGTT Amount (m EUR)
20	Portugal	2008	20
22	Germany	2009	25
23	Spain	2010	70
26	France	2011	200
24	UK	2011	115
18	Poland	2011	-
19	France	2012	-

5. EVALUATION FINDINGS

This chapter presents the results of the evaluation at project and instrument level of the LGTT according to the standard evaluation criteria (i.e. relevance, effectiveness, efficiency and sustainability), the Bank's contribution as well as for management by EIB.

5.1 Relevance

Relevance is the extent to which the objectives of a project / an instrument are consistent with EU policies, EIB priorities, national, regional, and local strategies as well as beneficiaries' needs. It also takes account of the internal coherence of objectives and the relevance of the design. Hereunder relevance is discussed first at instrument level and subsequently at project level.

5.1.1 Relevance of the LGTT at Instrument Level

a) Relevance to EU Policies

This section is based on a comparison of the objectives of the LGTT, as presented in § 3.2, with the policies of the EU, as presented in § 2. From this comparison it appears that the LGTT was and is highly relevant within the EU policy context for the following reasons:

- It aims at supporting the implementation of the TEN-T which underpins the Lisbon Agenda and the Europe 2020 policy. The objective of the LGTT to anticipate / accelerate the implementation of eligible TEN-T projects can be considered a response to the observed delays in the implementation of the TEN-T.
- The intermediate objective of the LGTT to increase private sector participation in the financing of the TEN-T is consistent with EU policy in that regard and the promotion by the EC of the concept of PPPs. Further, by aiming at leveraging private financing, the LGTT is consistent with the objectives of the EU Growth Initiative launched in 2003.
- The LGTT Agreement gives a preference to TEN-T priority projects and cross-border projects, although in a limited way, i.e. through prioritising the former in case of capital rationing needs and – for the latter – through a larger closing fee to EIB.

b) Relevance in Relation to EIB Policies, Strategies and Priorities

In June 2005, the Bank set a new strategy described in "Towards a New Strategy for the EIB Group" endorsed by the Board of Governors. The main objectives included, amongst others, a progressive increase in risk-taking, the use of new financial instruments and further cooperation with the European Commission. The strategy also noted the creation of the TEN-T Guarantee Instrument.

The Bank's Corporate Operational Plan (COP) 2006-2008 further elaborated the new strategy, and noted specifically that the EIB Group will develop new financial instruments in cooperation with the EC. Amongst the initiatives announced was the further development of the Structured Finance Facility (SFF). SFF was created in 2001 with a strong focus on TEN-T and enabled the Bank to take

risk that it was previously unable to take (low investment grade and beyond) using financial products with a lower credit profile (including mezzanine and subordinated debt).

The COP 2007-2009, for the first time, included reference to the LGTT as one of the two financial instruments (the other one being RSFF) to be launched in 2007 managed by the EIB, thereby highlighting a new dimension of enhanced cooperation between the EIB and the EC. The document supports the EIB's active involvement in setting up the LGTT. Subsequent COPs to date²¹ systematically refer to LGTT and have included it as component of one of the Bank's Key Performance Indicator (KPI): KPI 4.b. Although a specific numeral target has never been set at the LGTT level, this underlines its importance for the Bank²².

To reflect the specificities of the LGTT and retain its relevance, the CRPG was adjusted to address issues such as size limits of LGTT operations, maximum acceptable cumulative exposure of SFF and LGTT operations, as well as pricing of the LGTT.

Against the above background, it can be concluded that the development and utilisation of the LGTT as a joint EIB-EC instrument was indeed a relevant response to EIB policies, strategies and priorities, with regard to new financial instruments, cooperation with the EC and support of the TEN-Ts, the latter being a COP priority objective.

It was also consistent at the time of its introduction with the Bank's stated policy to increase risk taking. By embedding the LGTT into the already established SFF, the Bank assured that the LGTT would be compatible and relevant with its overall risk-taking strategy. The LGTT instrument furthers a number of EIB objectives: increased risk taking, development of a new financial instrument in cooperation with the European Commission. The LGTT also supports the blending objective of EC & EIB resources, and enables the Bank to support long term investment projects in a priority area defined in the EIB's Corporate Operational Plan (COP), namely TEN-T projects.

c) Relevance in Relation to Market Needs

The EC supported by EIB conducted market testing exercises in 2004 and 2005 in order to understand the needs of the market for an instrument like the LGTT.

According to the EC Staff Working Paper²³, as well as interviews with key persons involved in the early design of the instrument, the first principle was to provide guarantee cover for traffic revenue ramp-up risk in the core sense, i.e. the risk of growth trends being slow to mature as traffic gradually discovers a new transport infrastructure²⁴. This risk was initially considered largely uncorrelated between projects so that a portfolio of a limited number of projects would be sufficiently diverse to mitigate any portfolio risk.

The first phase of the market testing was conducted in March 2004 when public authorities, mainly ministries, PPP taskforces, financial institutions, monoline insurers and advisers were asked for their views on what was later called in EC papers the "original" EC proposal for a loan guarantee instrument. This "original" EC proposal was broader in scope than that of the EC Staff Working Paper because it intended to cover "post construction risk such as the risk of traffic and/or revenue shortfalls" suggesting that risks other than traffic revenues might be considered.

This "original" proposal was for a partial guarantee of a portion of senior debt during the ramp up period, with risk being shared between the EC, EU MS and the private sector. The proposal as presented in the first phase is described in greater detail in the Aide Memoire in Annex 2. From the Feasibility Report the general opinion reported is that it would be welcome and useful. It was noted as having a strong symbolic effect, with a "stamp of approval" from the EC sending a positive signal to the markets but respondents were also sceptical about the financial added value of the proposal. It was felt that a net reduction in funding costs was unlikely and that the effect on creditworthiness of the project would be "limited or negligible" because of the conditions that the guarantee was partial

²¹ COP 2008-2010, 2009-2011, 2011-2013, 2012-2014

²² KPI 4.b covers SFF, RSFF and LGTT instruments. Reporting on the indicator has evolved from a numeral target to a signature limit.

²³ Annex to the LGTT Feasibility Report from the market testing

²⁴ S&P in their 2002 publication on Traffic Risk in Start-up Toll Facilities define traffic ramp-up as follows: *A ramp up period reflects a toll facility's traffic performance during its early years. The ramp up period reflects users' lack of familiarity with a new highway, bridge or tunnel and its benefits- an information lag and a community's general reluctance to pay tolls. Ramp up has three dimensions: Scale of the ramp up (magnitude of the departure from forecasts), duration of ramp up (from instantaneous to beyond 5 years) and extent of catch up.*

and restricted to projects of certified investment grade. The usefulness of mezzanine or other subordinated debt to the enhancement of creditworthiness was stressed.

Based on this feedback the EC “fine-tuned” its proposal and embarked on a second phase of market testing, with a further selection of rating agencies, advisers and monoline insurers, but there is no separate summary of the further feedback. It was concluded that the guarantee was sufficiently welcomed by the market to proceed. The changes included: the risk-sharing philosophy was modified to require both MS and private sector contributions at least equivalent to the ramp-up guarantee (but not risk sharing of the guarantee itself); the creditworthiness test was reduced to “near investment grade”²⁵; and the conversion of the guarantee into a subordinated tranche with the EC acting as “patient lender” was explicitly acknowledged.

The revised proposal in 2005 specifically stated that the guarantee might be extended to availability and performance risks provided that these can be reasonably assessed and isolated from risks related to mismanagement.

The scope of coverage finally implemented in the LGTT Agreement (2008) has been described in § 3.3. It covers all traffic risks during the ramp-up period, i.e. not only ramp-up risk in the core sense (users gradually discovering the infrastructure), but also other risks associated with modelling traffic levels during the ramp-up period (such modelling often includes parameters such GDP, fuel prices, development of competing/alternative infrastructures etc.,).

In terms of **direct alternative** instruments, no comparative guarantee product was or is available in the marketplace and it has an additional benefit for the private sector of being publicly-supported. The risk-sharing associated with the LGTT is entirely between the EC and the EIB without formal involvement of either member states or the private sector. However, sponsors and lenders have used other means of protection as **indirect alternatives** in some cases. These include additional contingent mezzanine debt or equity and reserve accounts, although it is recognised that there is an additional price for this protection which is balanced by belief in tighter control over the financial management.

In order to gauge the current market sentiment, the key results of an updated market enquiry conducted in Apr-May 2013 are summarised in Annex 5. 40 stakeholders (of whom some 20 responded) were invited from the EC, national public authorities, major banks and project sponsors to provide the evaluation with an updated opinion on the LGTT. There is consensus that EIB was seen as the right choice of partner for the merging instrument and the EC, because of its experience with TEN-Ts/PPPs, institutional set up, regional coverage and alignment of objectives with those of the EC.

Stakeholders agreed that the LGTT did cover a risk prevalent in transport PPPs which is difficult to control for the private sector, although the current appetite from the private sector to take on traffic risk has diminished substantially. This is reflected in the portfolio review where the potentially eligible projects for the use of the LGTT represent just 27 projects or 14.4% of the EIB overall TEN-T portfolio in terms of number of projects. Thus, it would appear that LGTT is now perceived as a niche product and financiers consider the risk of traffic risk *throughout* the lifetime of the concession as the current key risk.

Thus, over the evaluation period, the instrument coverage has been relevant to market needs and there remains no direct alternative, although the current perception of the key risk may be wider than the initial coverage offered by LGTT (which is addressed under effectiveness).

5.1.2 Internal Coherence of Objectives and Relevance of the Design

The assessment of relevance of design evaluates whether the objectives are internally coherent and whether the design was conducive to reaching the objectives of the operations.

²⁵ In the Staff Working Paper attached to COM (2005)75 there is an Annex (no 3, Technical Paper) which purports to demonstrate, amongst other things, that the instrument is best suited to projects near investment grade, defined as BB according to the Standard & Poor rating scale. It also states that guaranteeing a small fraction of senior debt is sufficient to give adequate security to senior debt, and provides a methodology for provisioning (which was not used later), to show that the optimum portfolio size was 30 projects allowing the instrument to cover its costs. The paper makes many assumptions and simplifications, and uses equations and tables where key terms are not explained, that the conclusions cannot be confirmed as reliable by this evaluation.

The EC has accepted for some time that the TEN-T network can only be completed in a reasonable timescale if private finance is attracted into the programme. The sum of available EU grants plus state funds was simply not sufficient to meet the needs²⁶. Thus, it was initially perceived that barriers to private investment in TEN-T projects existed, and that the EC might be able to reduce some of these barriers²⁷, hence the intermediate objective of attracting higher private sector participation²⁸ was logically consistent with the overall objective. The operational objective is to focus on, and reduce, one specific risk to which private sector partners and their financiers were exposed in proposed projects, thereby reducing one potential barrier. Thus, the three levels of objective were coherent at the time of launch but are based on two significant assumptions:

- i. That the barriers to private sector participation can be addressed, at least partly, by action from the EC in the form of a financial instrument; and
- ii. That the specific risk – traffic related revenue risk during the ramp-up period – is a key barrier which, if removed, would lead to more projects or to projects being completed more quickly.

The initial quantification of the scale of the product required to address this risk was made in 2005 at a time when markets were not in crisis and were intended to strictly limit the public intervention effect to a narrowly defined risk which, it was assumed, was causing wider market failure. The narrowness of the coverage has been challenged in both the original market testing by the EC, and the updated market enquiry undertaken during this evaluation.

However, the design has evolved through its implementation stage. The Table in Annex 3 and accompanying notes summarise the main aspects of the design of LGTT which evolved over time, from the first proposals to the LGTT Agreement between EIB and EC to application in practice in the deals using LGTT. Thus, the relevance of some of the design (particularly the financial design) has been improved with each new application at project level (as noted in the next section) and as a response to the deep and extended economic downturn which developed just as the product was implemented in the first projects in 2008.

There is one area of the technical design within LGTT which has raised issues of relevance. While LGTT was initially required to cover all forms of transportation modes within TEN-T, the ex-ante evaluation of projects required a statistical / probabilistic modelling of risks and expected loss. By contrast to road projects, where traffic consists of a granular mass of individual transport users, projects in the port and rail sector initially depend strongly on singular choices of transport operators to move large blocks of traffic (i.e. ships/shipping routes, trains/service schedules) to/from the infrastructure. There is a concern, shared by the EIB's technical services, as to whether the stepped nature of port / rail traffic lends itself to probabilistic analysis required for the modelling of expected loss for the LGTT and whether the probability functions normally applied offer a reasonable fit.

Despite this one caveat, which appears to result in detailed discussion between services for each new project, the initial narrowly defined design has been adapted to remain relevant.

5.1.3 Relevance of the LGTT at Project Level

The evaluation of use of LGTT in the sample of five projects rated all five as satisfactory against relevance. In summary, this rating is mainly driven by choice of projects being relevant to EU and EIB policies because they were indeed TEN-T projects (in two cases TEN-T Priority Projects) of high national priority, that a blending of EC and EIB resources occurred and that the LGTT design was adapted to market needs in such a way that it would cover a proportion of project risk that would help to enhance senior debt quality, which in turn was important to facilitate financial close.

The existence of other traffic impact risk factors, beyond core ramp-up risk, during the ramp-up period was observed in the project sample. This included traffic flow impacts from residual road works, the opening of competing transport infrastructures and, since the projects were initiated during a period of economic crisis in Europe (2008-2012), there was considerable uncertainty about the modelling of base year traffic and economic growth trends.

Although the initial belief had been to restrict cover to ramp-up risk only, the LGTT Agreement itself allowed cover of wider traffic risk during the ramp-up period, and this gave EIB a greater range of

²⁶ Estimated in the TEN-T regulations of 2007 to be 600bn EUR between 2007 and 2020

²⁷ First raised in EC Communication on the Growth Initiative in November 2003

²⁸ Ref EC Communication on the Feasibility of an EU Loan Guarantee Instrument for TEN-T COM(2005)75

flexibility to apply the instrument. The in-depth evaluation of the use of LGTT in the five projects led to the following conclusions regarding the intended risk coverage by the instrument:

- It can be argued that three of the projects evaluated in depth only had a minor element, if any, of ramp-up traffic risk in the core sense, since they were brownfield projects, upgrading existing transport infrastructures with established and known traffic flows.
- Both the amounts and the timing of the payment of the LGTT suggest that the instrument was in all cases used to provide cover for more than ramp-up risk in the core sense and – depending on the scenario retained – potentially served in some cases to provide risk cover for other traffic risks or beyond the ramp-up period. For two projects, this potentially included some tariff risk.
- In most projects, the amounts and timing of the payment of the LGTT were driven by the intention to re-establish financial ratios and – where mini-perm²⁹ financing structures were in place – to enhance the potential for re-financing. In these latter cases, the timing of the one-shot payment of the LGTT coincided with the re-financing date. In the most extreme of these cases, the payment date for the LGTT was so far beyond the ramp-up period that the LGTT will now not be available when it would be most needed to cover traffic risk during the ramp-up period as it materialises.

Interestingly, by not constraining the LGTT to only cover ramp-up traffic risk in the core sense and by even extending the risk coverage through the LGTT to cover risks beyond traffic and even beyond the ramp-up period, its impact on credit enhancement and pricing of senior debt potentially increased, improving the relevance of the instrument.

It appears, from the sample evaluated in depth, that the instrument was relevant to meeting financial and operational objectives (including financial close) but that it had less relevance to the intermediate objective of facilitating larger private sector involvement. In order for the LGTT to fundamentally change the structuring of projects, it would have to be introduced from the start of the project cycle, before the choices on public versus private, or forms of income generation etc. This would entail renewed focusing on marketing and on providing special support to those countries where there is little or no PPP culture.

5.1.4 Conclusions and rating against relevance

RATING: SATISFACTORY

At instrument level, this evaluation found that the objectives of the LGTT, as per the reconstructed intervention logic, were relevant to EC and EIB policies and were internally consistent with one another. It had no direct alternative. However, the initial evidence for some of the design assumptions, around a narrowly-defined ramp-up risk as a major impediment to private sector involvement, was unclear at the time the instrument was launched. There was some evidence that a less tightly focussed instrument could have had wider market appeal initially and a bigger effect overall.

There is consensus that EIB was seen as the right choice of partner for the emerging instrument and the EC.

At project level, all of the five operations from the sample which used the LGTT were rated as satisfactory against relevance. This rating was mainly driven by the fact that the projects chosen were indeed TEN-T projects (in two cases they were TEN-T priority projects), and the LGTT offer was designed in such a way that it covered a portion of project risk that would help to enhance senior debt quality, which in turn was important to facilitate financial close.

It appears appropriate to give more weight to its continued relevance at project level, based on trial and adaptation in transactions, than to the early design faults at instrument level which led to it becoming a niche product. This implies an overall rating of **satisfactory** against relevance.

²⁹ "Perm" is short for "permanent", alluding to permanent financing. Mini perm financing is something a developer would use until a project has been completed and can therefore start producing income. In other words, a developer will use this type of financing prior to being able to access long-term financing or permanent financing solutions.

5.2 Effectiveness

Effectiveness relates to the extent to which the objectives of the project or instrument are achieved. The operational and intermediate objectives are evaluated mainly through the project evaluations since the potential direct and indirect contribution is at project level. The overall objectives of the LGTT instrument are potentially achieved through the sum contribution of the individual projects and are therefore evaluated at LGTT instrument level.

5.2.1 Effectiveness of the LGTT at Project Level

The use of LGTT within the five sample projects scored satisfactory on effectiveness. This largely reflects the achievement of operational objectives (e.g. risk coverage) and to some extent achievement of intermediate objectives (e.g. senior debt costs).

Achievement of Operational Objectives

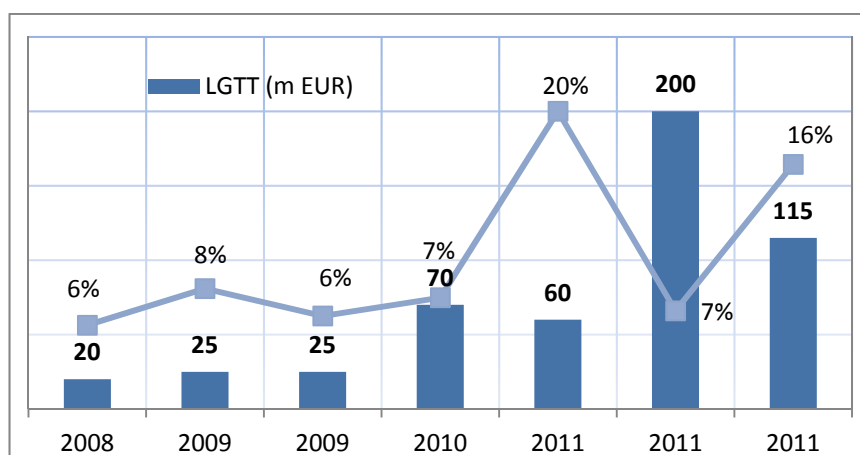
The first operational objective of the LGTT is to cover traffic risk during ramp-up through a guarantee, and the second operational objective was to improve the ability to service senior debt. The project-level evaluation reveals the following:

- All road projects in the sample are brownfield, where most of the estimated traffic is based on established traffic on existing roads, and only a small share of the traffic (up to some 20%) is captured from other roads and therefore subject to core ramp-up risk. Nevertheless, these projects are exposed to other traffic risks during ramp-up period. Modelling of the LGTT coverage by consultants suggests that the coverage extends beyond ramp-up risk in the core sense and, in two projects, extends beyond the ramp-up period.
- In some of the sample projects the LGTT was structured with a one-shot payment rather than with contingent payments throughout the ramp-up period. The payment date for the one shot was the date foreseen for re-financing which was often (but not always) the end of a ramp-up period.
- In one project (#22), the LGTT injection is scheduled well beyond the ramp-up period and the payments of the LGTT will hence not be available during the critical ramp-up years where they would now be most needed.
- For the projects where no LGTT was provided, the obvious initial downside effect is the additional costs of alternative protection.
- For projects with LGTT and where it has been drawn, no distribution is made to the shareholders for as long as the LGTT has not been paid, a strong disincentive to sponsors to call on the guarantee unnecessarily since it has an impact on their return on equity.

Therefore, this operational objective is generally achieved.

The evidence of interview and a consultant's review of the financial close models for projects show that the LGTT is often structured in such a way that it redresses financial ratios to levels clear from default, thereby improving the ability to service senior debt. As mentioned above, the timing of the "one-shot" payment coincides with the refinancing date, where the LGTT injection would serve the purpose of prepaying some of the senior debt, thereby enhancing financial ratios and making re-financing more likely, which is a significant financial event. This way of structuring the LGTT proved particularly useful to facilitate re-financing in projects with miniperms structures.

As the graph below shows that the scale of the LGTT has been growing in relation to the senior debt. The first batch of projects, during the first two years, had LGTT amounts of EUR 20-25 m, representing 6%-8% of the total senior debt. Since then, the amount of LGTT and proportion of senior debt has been increasing, reaching the maximum allowed level in absolute terms (EUR 200 m) or in relation to the senior debt (20% of the senior debt).



In conclusion the evaluation found that LGTT largely achieved its operational objectives at project level to cover traffic risk during ramp up (and beyond) and improve the ability to service senior debt.

Achievement of Intermediate Objectives

The first intermediate objective is the reduction of the risk margin on senior debt. This evaluation found evidence that the EIB senior debt cost may have been reduced in three out of the five LGTT projects evaluated (#20: -10 bp, #23: -10pb and #24: -63bp). For the commercial bank senior debt, however, no evidence of reduced margin was produced, and most reports suggested LGTT only facilitated the loan approval in the banks’ credit committees without a pricing effect.

There was indirect evidence that the use of LGTT may have resulted in pricing increases being avoided on some commercial bank loans. For example one road project (#20), provided an indicative pricing during the pre-Best-And-Final-Offer (BAFO) stage based on the sponsor’s traffic case. A lender’s traffic audit suggested reduced traffic flows and threatened the robustness of the project. While there was significant pressure to increase the pricing no increase occurred following the use of the LGTT. Furthermore, by comparison to indirect alternative instruments, which borrowers considered using instead of the LGTT (e.g.: equity or ramp up reserve accounts), LGTT generally was lower priced and therefore an attractive product.

The second intermediate objective is for the LGTT to facilitate the involvement of the private sector. Most of the counterparts interviewed described LGTT as a very useful instrument to facilitate the financing of infrastructure projects particularly in a difficult economic/crisis period and to facilitate closure of a project under a PPP structure, locking in private sector participation and smoothing the process in reaching financial close.

In conclusion, this evaluation found mixed evidence of LGTT impact on intermediate objectives, although it should be noted that there was impact in areas where EIB has direct influence (pricing of EIB senior debt) and less impact in areas where EIB has indirect influence, relying on market behaviour in, for example, the pricing of commercial debt.

Achievement of Overall Objective

The overall objective was to anticipate/accelerate the implementation of TEN-T projects and, ultimately, to contribute to improved transport links. It is difficult to assess what the impact would have been if LGTT had not been included in the financial structure. Alternative indirect forms of protection mechanisms were viewed as both more expensive and requiring time to arrange. These could include potentially greater equity commitment required from the sponsor, increased senior debt costs, or a modified repayment profile.

There is no evidence that any shareholder or financier was dependent on the introduction of LGTT alone, although there was one project in the sample which reported no real alternative to LGTT available and where financial close may not have happened without the LGTT. Regarding the achievement of the overall objective, LGTT did not therefore anticipate, but has, on occasions, contributed to accelerate the financial close of deals, and the launch of TEN-T projects in a difficult economic market.

5.2.2 Effectiveness of the LGTT at Instrument Level: achievement of the overall objective

The effectiveness of the LGTT as a market instrument is rated as partly unsatisfactory. While there is consensus that LGTT facilitated financial close at project level in 7 of 14 eligible projects (50%), the detailed development of offers for these projects was at bidding and tender stage in their project cycle, effectively eliminating the potential for the LGTT to reach the objectives of greater private sector involvement and accelerated implementation³⁰. And, as noted in the portfolio review, the signed deals represent 1 in 5 of the initial LGTT target which itself was a small portion of the total TEN-T market. Given the a) late stage at which LGTT was “plugged in” projects (bidding/tender) and b) very limited market share of LGTT eligible TEN-T projects, there was no anticipation/acceleration of TEN-T implementation at instrument level. At most, the LGTT very incidentally contributed to improve transport links and supported the Lisbon Agenda.

On the positive side, after 2008, commercial banks became much more risk averse and the EIB/LGTT involvement made it easier for commercial banks to get the project through their credit risk committees. In two cases (e.g.: projects #23 and #26) the finance structure included public subsidies and interviews suggested that the level of subsidy may have been reduced as a result of the inclusion of LGTT. However, no quantifiable evidence was produced.

5.2.3 Conclusions and rating against effectiveness

RATING: SATISFACTORY

At instrument level the evaluation concluded that the overall objectives of the instrument to anticipate/accelerate the implementation of TEN-T projects by increasing private sector participation were not met, partly because of the late project cycle stage at which it was considered (bidding/tender) The fact that LGTT was only used for a very limited number of TEN-T projects -20% of the initial target- also supports this argument.

The evaluation at project level demonstrates that the LGTT has been successfully used to cover a specific element of traffic risk, and thereby to have a positive impact on the ability to service senior debt. It was used in 7 of 14 potentially eligible projects. The LGTT was considered to have facilitated financial close in all of the projects, which is a positive outcome even if it had become a niche product. Some evidence was also found that LGTT prevented some private investors from pulling away from the projects during the crisis. However, all projects would have happened without the instrument although potentially with some delays and a higher cost. LGTT was crucial in preventing a quantifiable delay in one project.

In spite of the limitations of LGTT, the operational and most of the intermediate objectives have been met, supporting a satisfactory rating at project level.

The overall rating against the effectiveness criterion is **satisfactory**, within a context of its impact at project level in a difficult economic market, rather than as a wider market intervention.

5.3 Efficiency

Efficiency concerns the extent to which project benefits/outputs are commensurate with resources/inputs. At project level, this evaluation tries to assess whether the benefits of using the LGTT (i.e. earlier provision of transport infrastructure) are commensurate with the cost of providing it. At instrument level, assessment was based on whether the LGTT was the most efficient way to achieve the intended benefits.

5.3.1 Efficiency of the LGTT at Project Level

Only one of the five projects evaluated which used the LGTT was rated as satisfactory against efficiency. The other four projects were rated as partly unsatisfactory. Overall, at project level, the LGTT does not appear to be an efficient instrument when measured against the combination of improvement in time-lines and cost effectiveness.

An interesting outcome of the project interviews was the confirmation that LGTT, as applied to date, generally benefitted lenders or banks more immediately than project sponsors The LGTT is considered a competitively priced instrument and a cost-effective solution for the lenders. Alternative

³⁰ The original assumption being that by facilitation of the private sector involvement, the implementation of TEN-T project would be accelerated.

forms of protection were not direct alternatives and, as such, required more cost and more effort to develop. The existence of LGTT therefore presented a payment protection for lenders which was directly available and allowed them to absorb a short-term pricing benefit financially (hence no commercial pricing improvement) while the sponsors benefit indirectly from the greater certainty of Financial Close, a protected senior debt, and there are then longer-term benefits to equity providers (i.e., the project sponsors).

In the one project rated as satisfactory against efficiency, the use of the LGTT was stated to have made a critical contribution to reaching Financial Close and that in the absence of the LGTT there would have been a time delay of up to 2 years. In this project, the economic benefit of the prevented delay – which is considered a second-best benefit compared to the acceleration of projects originally intended – was worth a multiple of the administrative cost of providing the LGTT and hence the LGTT was viewed as an efficient instrument in this one case.

In the four projects rated partly unsatisfactory the LGTT facilitated reaching Financial Close. In the absence of the LGTT, Financial Closure could have been achieved by other means but at a higher cost of financing. No time saving was noted.

5.3.2 Efficiency of the LGTT at Instrument Level

Efficiency at instrument level is assessed from the impact on the market and from the use of public money overall allocated (amount spent versus amount provisioned).

According to the updated market enquiry, there remains no direct comparative guarantee product to the LGTT available in the marketplace, in terms of the specific risk covered. Respondents drew comparisons to monoline insurances, although these were only available for investment grade projects, whilst LGTT aimed at below-investment-grade projects, and monolines were disappearing from the market following the start of the financial crisis when the LGTT was first implemented in projects. Sponsors and lenders have been using other means of creating similar downside risk protection through contingent mezzanine debt or equity and reserve accounts, although these tended to be more expensive than the LGTT. Against that backdrop, LGTT is viewed as a cost-effective solution for a very specific type of risk.

In terms of the use of public money, EC representatives drew the positive comparison between the LGTT and grant funding of similar projects. It was noted that it would require a multiple of the amount of an LGTT in a project to achieve the same effect in terms of risk coverage, given that the LGTT is a guarantee where the amount covered is a multiple of the capital provisioning needed. Again, therefore there is a positive impact.

However, this must also be viewed in the context of the amount provisioned. Altogether only EUR 100 m in total have been used in provisioning, the instrument appeared to be over-supplied for a narrow market or in other words, large quantities of money were reserved for the instrument without being used for the purposes intended, reducing the efficiency of the instrument. As a sign of recognition of this, the EC has now diverted EUR 200 m of the EUR 500 m initial contribution to the Project Bond Initiative (PBI) and EUR 50 m to grant funding.

5.3.3 Conclusions and rating against efficiency

RATING: PARTLY UNSATISFACTORY

Efficiency concerns the extent to which benefits/outputs are commensurate with resources/inputs. At project level, the LGTT is considered a cost-effective solution from the lenders perspective. It has, however, had no impact on time-lines in four of five cases evaluated.

At instrument level, with hindsight, the size of the fund (EUR 1 billion) was either too large for the instrument as designed or possibly could have been used more flexibly for a more widely applicable product. The financial crisis which reduced the number of LGTT candidate projects exacerbated this issue. In spite of being a unique product on the market (no direct alternatives), and its interesting pricing, the narrow application and generous provisioning prevented it from being an efficient instrument for improving the TEN-T network programme, and this led to an overall **partly unsatisfactory** rating.

5.4 Sustainability

Sustainability is the likelihood of continued long-term effects and the resilience to risk over the intended life of the project/instrument. At project level the continued impact of LGTT on updated traffic projections was evaluated. At instrument level, evaluation was on the basis of whether aggregate losses are in line with expectations or exceed them currently in the portfolio of LGTT operations, hence endangering the sustainability of the instrument and its capacity to provide any further benefit, and whether there continues to be market demand for the instrument.

5.4.1 Sustainability of the LGTT at Project Level

The evaluation of sustainability at project level rests – where possible – on updated traffic forecasts and financial models, mainly to assess to what extent the LGTT, if drawn and converted into a mezzanine loan, is likely to be repaid over the lifetime of the project. Qualitative assessments were applied if there was a lack of updated traffic information or there was a lack of clarity around financial models and their working assumptions.

The assessment at project level is based on only a snapshot of the current situation regarding traffic levels and assumptions looking forward. There is no assurance that traffic levels will stabilise in the future and if trends continue declining, the assessment of sustainability could produce a different result. The prolonged global economic crisis, which potentially marks the end of a long economic cycle, raises many questions regarding forecasting parameters used in an instrument like the LGTT.

In three of five projects from the sample, traffic is significantly (15%-30%) below the estimates made at appraisal, mainly because of the crisis (Germany, Spain and Portugal). The evaluation evidenced that it is not core ramp-up risk which is problematic but rather base line traffic and growth rates, which are lower than expected across Europe.

According to updated traffic forecast and financial models, LGTT is only likely to be drawn in one case, project #22. However, the #22 loan is much more likely to be repaid, provided the project does not default before the LGTT becomes available³¹. In another project, #23, traffic is expected to be below trigger levels, but it is not expected that the LGTT will be drawn because of a shortened construction period leading to an early implementation date. In a third case, #20, the concession was cancelled due i.a. to the suspension of the construction works. Therefore, all senior debt has been cancelled, rendering the LGTT unnecessary.

On average, therefore, LGTT sustainability has been rated as satisfactory (three satisfactory, one unsatisfactory and one excellent), which – given the financial crisis and its impacts on traffic levels across Europe – is a positive achievement.

5.4.2 Sustainability of the LGTT at Instrument Level

To reflect the specificities of the LGTT, the CRPG was adjusted to address issues such as size limits of LGTT operations, maximum acceptable cumulative exposure of SFF and LGTT operations, as well as pricing of the LGTT. Whilst it is recognised that a guarantee instrument which cannot be drawn would be useless, it is sensible to protect the instrument against risks which it is not intended to cover or against excessive downside cases of the risk it intends to cover. In that regard, key elements of the design of a guarantee are the conditions under which it can be called. From a time series analysis of the conditionality used in the five projects sampled, highlighted in Annex 3, it appears that the EIB went through a learning curve and built a series of protections into the legal documentation e.g. against events of default (which LGTT cannot cure) and traffic dropping below a floor level. Such protections, so long as they are acceptable to the market, enhance the financial sustainability of the LGTT as an instrument.

Sustainability at instrument level also requires evaluation of whether a reasonable deal flow can be sustained for the LGTT looking forward. As noted earlier, the initial analysis assumed a largely uncorrelated pattern of risk between projects so that a portfolio of a limited number of projects would be sufficiently diverse to mitigate any portfolio risk. The crisis context suggests this assumption does not hold since risks have become more correlated across Europe with the whole sector affected and the potential market itself has reduced in size.

³¹ At the time the present report was proposed for discussion in the Management Committee, this project was under restructuring.

As noted in § 4.3.1, there are currently three road projects in the LGTT pipeline, indicating that the deal flow continues at a much slower pace than assumed and raises questions over the future market impact of the instrument.

5.4.3 Conclusions and rating against sustainability

RATING: SATISFACTORY

The evaluation of LGTT considered sustainability as the likelihood of continued long term effects and the resilience to risk over the intended life of the LGTT.

At project level it assessed whether LGTT provided sufficient coverage against traffic risk so as not to compromise the repayment of the loan. Despite the findings of overestimated ex-ante traffic forecasts, the evaluation assessed sustainability at project level as satisfactory with no perceived risk that repayment of the loans would be compromised by traffic risk. This has been achieved during a financial crisis which created an access to finance issue which further justified EIB's intervention in the projects.

At instrument level, the evolution of the instrument design has improved its sustainability across projects but there are questions about the scale of its market.

Taking into account the considerations described above, and that the evaluation has a focus on the role of the EIB to set-up and implement the instrument, the sustainability for the overall initiative was rated **satisfactory** provided there remains a market for the product.

5.5 EIB Contribution

The EIB contribution section identifies the three dimensions of value added provided by the Bank: financial contribution, institutional and technical contribution and financial facilitation. The evaluation findings for these will be presented first at the project level and thereafter at the instrument level.

5.5.1 EIB Contribution to the use of the LGTT at Project Level

All of the five projects which used the LGTT included in the sample for in-depth evaluation were rated as high (3 projects) or significant (2 projects) against EIB contribution. The projects without LGTT have no ratings because LGTT was not used.

Financial Contribution

In most of the external interviews there was an acknowledgement that the EIB/EC, through its development of the LGTT, had attempted to fill a gap in risk coverage, which was particularly difficult to quantify, with an initially untested product. There was therefore an understanding that there would be inevitable trial and error with early projects and this was handled in a flexible manner.

The actual impact of LGTT on the pricing of EIB senior debt at project level was constrained by senior loan pricing decisions which are determined through EIB internal risk assessment procedures and are not necessarily based on the expected loss analyses and pricing systems associated with the LGTT. Therefore evidence of the pricing impact on EIB senior loans was limited to 3 of the 5 projects and, as noted under effectiveness, there was evidence produced of a possible impact on commercial loans in only one of the 5 cases.

However, most opinion suggests that any alternative to LGTT was indirect and more costly. Opinion appears to see LGTT as a possible equivalent to something between mezzanine and equity, both of which would be more costly than the LGTT as it is currently priced. Thus, the EIB/EC financial contribution is seen as high by most project players.

Further, in cases where the LGTT supported the refinancing of mini-perm structures, the cost of refinancing loans would be significantly below the cost of maintaining the mini-perm, which would normally be stepped up, if refinancing did not happen. Thus, while this may be considered by some as a positive side-effect, it added to the view that EIB financial contribution was positive.

Institutional / Technical Contribution

There was general acknowledgement that the work around LGTT had a limited impact on the traffic due diligence used by sponsors and other lenders, although the EIB had an important role to negotiate the senior debt conditions (as an independent party with no ties to the project sponsors).

However, one comment of note was that earlier involvement and better co-ordination between the EIB officers involved might have improved the promoters understanding of the product.

The difficulties of defining or separating out core ramp-up risk and the general optimism bias in estimating traffic volumes at tendering stage continued to be an issue despite interaction with EIB staff. Further, the scale of intervention required to make a meaningful impact on traffic risks appeared to be beyond the resource available for LGTT in the early projects. Feedback suggested that EIB's contribution to the financial structuring of the project was normally limited to explaining how best to ensure the functioning of the LGTT.

Financial Facilitation

There was a strong consensus of opinion that the EIB staff assigned to projects were seen as expert financial facilitators who adopted a flexible approach to working with borrowers and lenders, and there was a strong market signalling effect from the presence of both the EIB brand in each project and the LGTT. The LGTT was regarded as a potential solution to a problem, and greatly assisted the Financial Close of the individual projects.

5.5.2 EIB Contribution at Instrument Level

Financial Contribution

To assess the cost coverage of the LGTT instrument alone (i.e., excluding the costs and revenues related to other elements of the corresponding lending projects – in this case the EIB senior debt), a separate ad-hoc assessment in March 2013 was performed by the EIB service in charge at the request from EV. The assessment estimated the 2011 cost coverage of the LGTT instrument alone at 75%. Using this adjusted figure the conclusion is that the EIB does financially contribute to the instrument and, as such, the EIB's financial contribution is evaluated as high.

It should be noted that the accuracy of the calculations for LGTT Instrument alone is affected by internal time recording. Because time-recording codes were not set up immediately when work started on the future LGTT, the cost-coverage calculations do not capture the cost incurred by the Bank in the setting-up phase of the LGTT, i.e. prior to 2007 when no revenues were made on the instrument and there were significant costs associated with marketing, start-up and early assessment of projects.

Institutional / Technical Contribution

Section 3.1 and 5.1.1 (b) provides an overview of the history of policy and development of the instrument. It highlights that EIB expertise was involved from the early market testing in 2004 through the subsequent fine-tuning which led to the allocation of funds and the approval to proceed in 2007-2008 to the still on-going implementation of the instrument. In the view of the EC Commission (DG ECFIN and DG MOVE), EIB's expertise as a promotional bank in general and in the financing of TEN-T PPPs in particular, as well as its market access and reputation were essential for the development and the marketing of the LGTT.

Although the core methodological approach for risk sharing goes back to intellectual work within the EC, the development of a financial product around it, the translation of the approach into workable procedures, as well as taking the product to the market was largely the effort of the EIB and this has been mapped in Appendix 2. Whilst the European Council had initial concerns of a potential moral hazard to the EIB in using the LGTT for the benefit of its own senior debt, the EC viewed the EIB as the only qualified institution, to act as partner, for the following reasons:

- It needed an institution like the Bank which had in place a set of services required to run an instrument like the LGTT, covering marketing department, treasury and risk management, technical and legal support
- Neither commercial banks nor other international or national promotional banks had the country coverage (EU 27) coupled with PPP experience of the EIB.
- EIB and EC are both EU institutions which have prior experience of cooperation, and reasonably consistent objectives.

In terms of marketing, the EIB engaged in a number of activities, including discussions with key market participants, presentations to potential clients and at industry fora (e.g. PPP symposiums)³². There are records of some 40 presentations in 2008 on the LGTT or making mention of it, to a variety of audiences ranging from investors for individual projects and banks to rating agencies and public sector institutions. These presentations and detailed discussions with a variety of stakeholders suggest that EIB spent a reasonable effort to fulfil its duty regarding awareness-raising, although some interviewees expressed a concern that marketing materials for clients were insufficient.

The recent decision by the EC to use the EIB for the Project Bond Initiative (PBI) appears to further indicate continued confidence in EIB's capabilities. Against this background, EIB's institutional and technical contribution is evaluated as high.

Financial Facilitation

To assess financial facilitation at the instrument level, this evaluation looked at the extent to which EIB's participation facilitated other sources of added value and, in particular, if other products were developed in the market as a result of LGTT providing the example.

The Mid-term Review for the LGTT (2011)³³ notes that *"The first years of the implementation have provided EIB with invaluable market knowledge, structuring experience and an understanding of the TEN-T financing issues. These allowed for the continuous product development that enabled the LGTT to be adapted to cope with a large variety of projects and financial structures, and to effectively contribute to the implementation of the TEN-T programme.*

In a wider context, these insights help in defining future financing instruments and solutions to be developed, that could complement the LGTT to provide an enhanced platform (portfolio of product) supporting the successful implementation of the TEN-T programme and achieving 2020 objectives. The portfolio of products developed under the same umbrella would allow structuring solutions to be provided to the widest range of TEN-T projects addressing different risk profiles and financing solutions.

LGTT has enabled the EIB and the European Commission to develop a market reputation within the project finance market as a credit enhancement provider, paving the way for the development of further credit enhancement instruments (e.g. 2020 Project Bonds)."

With regard to the development of alternative products in the market, evidence from the individual projects shows that there was indirect alternatives in the form of some tailoring of existing facilities to cover similar risks but no clear market alternative developed. Sponsors and lenders used mezzanine debt, contingent equity and reserve accounts to provide equivalent protection and the general perception is that these options are usually more expensive. It appears that the LGTT remains a unique guarantee instrument for the purpose of covering traffic risk during the ramp-up period.

Against this background, EIB's institutional and technical contribution is evaluated as significant.

5.5.3 Conclusions and rating against EIB contribution

RATING: HIGH

At **project level** the EIB's financial contribution and financial facilitation through the LGTT was viewed positively as the LGTT was considered a lower-priced financial product which covered a particular type of risk, thereby positively influencing commercial banks credit decisions and facilitating financial close. The opinions expressed in interview suggest that technical and institutional contribution was rated as significant.

At the **instrument level**, EIB made essential contributions throughout the LGTT product cycle from the early concept stage and market testing through to the implementation of the instrument. Financial facilitation for future joint EC/EIB instruments is considered a positive outcome.

The tracking of actual cost recovery for the LGTT has been difficult to assess and it is recommended that further examination is required.

Overall, EIB's Contribution to the LGTT is therefore assessed as **high**.

³² EV counted more than 150 presentations related to the LGTT on the OPS computer network drives.

³³ http://ec.europa.eu/economy_finance/financial_operations/investment/europe_2020/documents/annex_2a_en.pdf

5.6 EIB Management of the LGTT

5.6.1 EIB Management of the Use of LGTT at Project Level

LGTT operations are embedded into the normal EIB operations cycle from project identification to signature. Key modifications to the process concern the inclusion of an LGTT eligibility check with the EC at "Fact Sheet A" (FSA) stage and the production of a Final Note on the use of the LGTT to the Management Committee, from which a section on the financial structure is sent in copy to the EC, both in line with the Article 11 of the LGTT Agreement.

The use of LGTT in all five of the projects included in the sample for in-depth evaluation was rated as partly unsatisfactory against EIB management. A common pattern of small issues across the project cycle was identified.

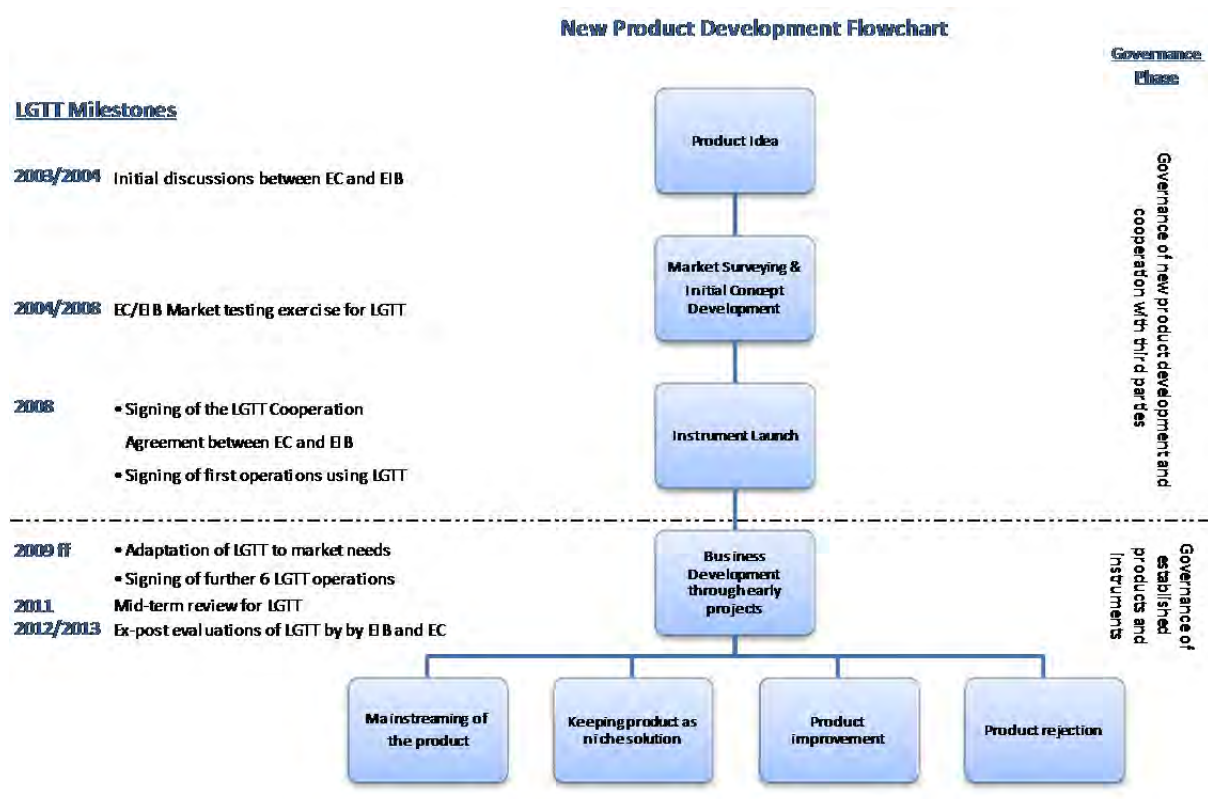
- i) Typically the practice is that EIB involvement in developing an LGTT offer starts at or just before tender or BAFO stage. To have an impact on accelerating project implementation and/or more private sector participation) may require involvement by EIB/LGTT at an earlier stage.
- ii) At appraisal stage there was no clear guidance on a standard instrument approach to the traffic analysis, on important details such as which probability levels of the traffic trigger to accept for an instrument that is generally perceived to cover below investment grade risk, or how the size and the timing of the payment of the LGTT was determined in relation to the expected losses from traffic shortfalls and the duration of the ramp-up period. It was noted, however, that all of these factors are reportedly discussed on a case-by-case basis with the Credit Risk and PJ Departments.
- iii) The CRPG is the only procedural or guidance document in the EIB in which LGTT specificities have been documented. The evaluation raises this issue whether indeed sufficient written guidance is provided to officers dealing with the LGTT, in particular in support functions who are not dealing with the instrument on a daily basis.
- iv) There is consensus that negotiation and signature stage generally worked well, with flexibility and expertise brought by the EIB to each of the projects. It was noted that LGTT negotiations fitted within existing timetables and there were no recorded delays despite some very complex, intense negotiations. A learning curve was observed with regard to the integration of protections for the LGTT into the documentation with a positive impact of the sustainability of the instrument.
- v) At implementation, follow-up and monitoring stage lacked a dedicated resource for the monitoring of the instrument (e.g. to follow amounts signed, amounts at risk to be drawn or lost and headroom free for new operations) so that the Bank could monitor its interests separate from its senior and mezzanine debt interests in projects. This issue has been recognised by the services.
- vi) While the EIB met, at project level, its contractual reporting duties, the individual project evaluations highlight that this does not always cover substantial or even material change in the individual project risk profile. It is therefore noted that further early reporting when project circumstances change would reflect better the proposed spirit of the cooperation necessary between EIB and EC.

The ratings therefore reflected a combined impact or pattern of issues, which highlighted the pilot nature of the early projects rather than the Bank's typically consistent, well-documented systems.

5.6.2 EIB Management and Governance of the LGTT at Instrument Level

This section focuses on the appropriateness of EIB's management and governance of the LGTT at the level of the instrument from its conception to current operations. It is structured according to the typical stages of new product development as depicted in the flowchart.

In the first period of initial market testing through survey and discussion and concept development, governance is very much a shared responsibility with trial and error of ideas and plans. In the second stage after instrument launch, business development brings the importance of the Bank's internal control systems, although with governance oversight shared with the EC.



Source: EV

The assessment is based on the review of documents (e.g. the EC’s market testing reports, the LGTT cooperation agreement, the 2011 LGTT Mid-term review, EIB COPs), as well as on interviews with key EIB staff. It should be noted that this evaluation found it difficult to trace all the documents relevant for the assessment and considers it desirable – as a matter of transparency – that they were stored or hyperlinked in a central place to facilitate their retrieval

Initial product idea, market testing and product development

Best practice within EIB for this type of market testing practice has progressed since the time that the LGTT was initially developed (2004-2007).³⁴ Whilst the EC was chairing the market testing exercise, EIB provided its support both concerning financial instruments and market knowledge to that. There are records that the EIB team kept its governing bodies informed throughout development and implementation of the LGTT and it engaged in market development efforts. During this phase management is hence evaluated as satisfactory.

Product launch

The instrument launch phase for the LGTT was 2008, which saw a number of key milestones, including the signing of the LGTT Agreement between the EC and the EIB (“the LGTT Agreement”), the setting up of the organisational and procedural framework within the EIB, the holding of the first LGTT Steering Committee and the signing of the first LGTT operation.

It was expected that the implementation of the LGTT product would create a considerable work load for EIB, in particular for market development; appraisal and negotiation as well as setting the monitoring tools for follow up, setting the necessary account structure to receive EC funding for LGTT provisioning, knowledge spreading inside and outside the Bank. The approval obtained from the Board to sign the LGTT Agreement, therefore, also covered a budget adjustment for 5 posts deemed necessary to support the implementation of LGTT in 2008.

³⁴ See e.g. the stakeholder consultation for the PBI: http://ec.europa.eu/economy_finance/consultation/europe_2020_en.htm.

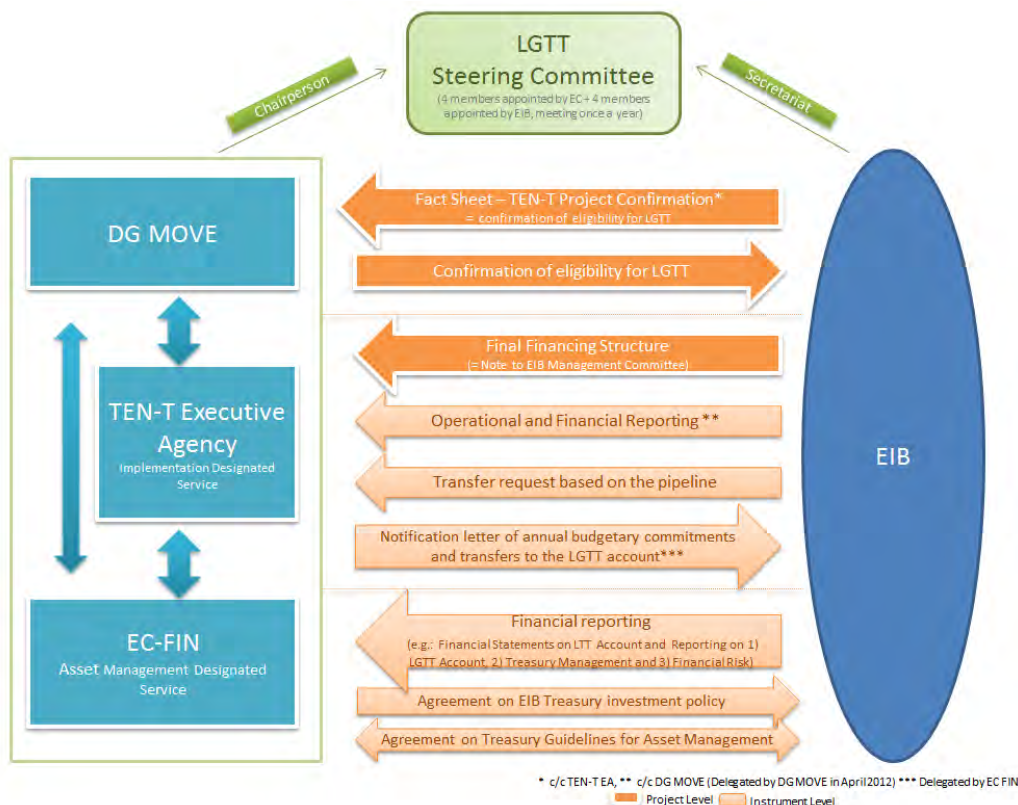
The key marketing material remains the LGTT Fact-Sheet published in 2008 in five different languages (DE, EN, ES, FR, IT). This is a short information document on the objectives and workings of the LGTT (see http://www.eib.org/attachments/press/2008-005-fact_sheet_en.pdf).

The electronic archives of OpsA contain some 40 presentations on the LGTT or making mention of it (see § 5.5.2). Detailed discussions were held with a variety of stakeholders, including e.g. the German Ministry of Transport on utilising LGTT for up-coming motorway projects in Germany. Thus, there was a reasonable effort to fulfil its duty on awareness-raising, as per Article 3 of the LGTT Agreement. In line with Article 19 of the LGTT Agreement, the presentations and the LGTT Fact Sheet make mention of the EC contribution to the instrument.

In line with Article 3 of the LGTT Agreement, the Bank opened an LGTT dedicated accounting ledger. In line with the requirement of Article 5, the LGTT has been made subject to rules and procedures of the EIB's CRPGs and – more specifically – those of the SFF. In May and December 2008, necessary adjustments to the CRPGs were authorised by the Management Committee and introduced to reflect the introduction of the LGTT and to facilitate first LGTT operations.

An important launch milestone was the first meeting of the LGTT Steering Committee on 17 July 2008. This first meeting recognised that LGTT was still in a pre-project phase and that the Steering Committee may need to adjust the instrument in the light of experience. It also served to agree on rules of procedure of the LGTT Steering Committee and for EIB to present the mode of operation, the EIB's pricing policy and present a pipeline of eight projects eligible for LGTT, of which EIB Board approvals had been obtained for five and an LGTT Agreement had been signed for one operation (i.e. #20, signed 30/05/2008).

The general framework of cooperation between the EC and the EIB in relation to the LGTT as largely described in the LGTT Agreement is depicted hereunder:



Source: EV

Overall it would appear that EIB managed the launch phase efficiently, rapidly amending its processes and organisation, and bringing about a pipeline of eight projects, including one signed operation. In terms of governance, EIB's governing bodies were duly consulted (one exception may have been the NPC) regarding key steps in view of setting up the LGTT, the requirements of the LGTT Agreement were adhered to and LGTT specificities were embedded in EIB's general workflow for operations and reflected in its CRPG, although this was not further developed as experience grew

in using the instrument. Against that background EIB management during the launch phase is rated as satisfactory.

Business/product development phase

The further development of the product largely happened through step changes in the specific design of the LGTT for individual transactions and is documented in the project documentation and to some extent in the mid-term review (2011) rather than in a central document or manual for the LGTT. A table in Annex 4 has, therefore, been developed during this evaluation to show how the product has been adapted from project to project. The patterns identifiable would include:

- Pricing is in line with CPRG guidance for LGTT, and also reflects combined administration fee and upward modulation.
- The scale of LGTT commitment has stepped up from 20m EUR to 200m EUR, possibly reflecting an increased understanding of the scale of intervention required in order to enhance financial robustness, and an increase in utilisation rate of remaining budget. Indeed, the evaluation at project level suggests that the size of the LGTT were set such that in some projects it covered traffic risks beyond traffic risk during ramp-up. Once called, however, the LGTT becomes a subordinated loan exposed to all project risks.
- The pattern of change for conditions precedent generally appears to indicate (1) additional protection of the EC/EIB position, such as, for example, the introduction of a traffic floor in one project after lessons learned in another (2) more tailoring in response to a greater understanding of the market need as evidenced by the most recent projects and (3) the move away from a very specific/small tool to cover a broader/longer-term coverage of risk.

A mid-term review was an internal EIB exercise (although the results were made available to the EC). In addition to mapping some of the change, it also came forward with five key recommendations that went beyond the gradual adaptations of the LGTT design to individual projects. These were discussed by the LGTT Steering Committee:

- To allow EIB to directly provide the stand-by facility;
- To increase the availability period of the instrument (a) to the construction period and (b) to be available throughout the operating period;
- To allow LGTT to cover other than traffic related revenue risks, in particular for TEN-T projects and important rail PPPs that are procured on an availability-payment basis;
- To allow LGTT to be drawn even in default scenarios subject to parameter conditions in order to improve senior debt recovery perspectives;
- To provide advisory service to potential clients.

The recorded EC response to the recommendations was brief but noted the legal constraints for extending the product and the need for proper scrutiny of the recommendations. This evaluation has therefore not included this in the evaluation of ratings.

In summary, it is clear that the EIB developed and refined the LGTT in the period 2008-2012 within the confines of the LGTT Agreement, largely as a response to market needs.

5.6.2 Reporting to the European Commission

There are two aspects of importance regarding the reporting to the EC: the regular reporting and the Steering Committee reports. Financial reporting requirements for the LGTT from the Bank to the EC have been analysed in Annex 4.

The Steering Committee is viewed as a reporting opportunity contractually. It has met irregularly *despite a commitment within the LGTT Agreement to meet annually*. The meeting notes suggest that much of the discussion was driven by the reporting of project proposal progress rather than by changes to the LGTT design and it is clear that EIB reporting is largely as assigned in the Agreement.

Operational reporting is performed largely as required, although two areas were raised in interview with the EC

(i) the reporting on financial risk related to signed LGTT operations. Here no report has been submitted so far, although the evaluation at project level has shown that at least in one of the projects, there was reason for concern about increased risk as a consequence of continuously decreasing traffic volumes, both actual and expected. This observation is linked with other observations regarding a lack of specific monitoring of signed LGTT operations.

(ii) understanding the various documents requires a level of specialisation in the subject matter and there was a concern on the part of the TEN-T Agency that the documents are somewhat opaque from their viewpoint.

For the financial reporting, this evaluation found no central record. In general, the conclusion would be that reporting has been compliant but the quality could be improved.

5.6.3 Conclusions and rating against EIB management

As noted earlier in this section, the use of LGTT in all five of the projects included in the sample for in-depth evaluation was rated as partly unsatisfactory against EIB management. A common pattern of issues across the project cycle was identified which included the lack of clear guidance for key decisions and the lack of dedicated resource for monitoring.

At instrument level, the development of the LGTT product and the continued application of EIB workflow patterns to the projects is evidence of a smart system at work in an evolving market. However, there are also a list of areas which would benefit from strengthening: the clarification of responsibilities for monitoring, the development of cost recovery more in line with the instrument needs, central recording of progress with product refinement, reporting to and Steering Committee meetings with the EC, portfolio/instrument level management, and a much fuller debate around the future needs of the LGTT particularly with regards to a stronger pipeline.

RATING: SATISFACTORY

The overall management of the initiative was considered **satisfactory**

At project level, there was a partly unsatisfactory rating which reflected a common pattern of issues, which may be the result of the fact that LGTT was initially experimental and has become niche rather than a mainstream bank product as anticipated.

At instrument level, EIB Management of the LGTT was rated satisfactory overall. EIB has handled the initial period of product conception well and launched the product in an efficient way, improvements are needed, notably on guidance provided to LGTT officers, cost recovery, attribution of monitoring responsibilities, gaps in reporting to the EC.

6. CONCLUSIONS AND RECOMMENDATIONS

Conclusions and recommendations presented hereunder are numbered in a way where conclusion C1 corresponds to recommendation R1 etc. (the exceptions to this are R4 relates to C1, R5 relates to C4 and C5, and R6, 7, 8 relate to C8).

6.1 Conclusions

As explained in §3.2, the LGTT as an instrument was intended to accelerate the implementation of TEN-T projects through the coverage of traffic risk during ramp-up. Its use in projects was expected to enhance senior debt quality and reduce senior debt cost, and thereby to facilitate larger private sector participation. Of 14 projects potentially eligible for the LGTT only seven eventually used LGTT. In all deals which used LGTT, it clearly facilitated financial close. However, of the five LGTT projects evaluated, there was only one (project #22) where LGTT had a stated impact on the timeline through preventing a delay for financial close.

C1: While there was a strong marketing effort in the early years, the detailed development work on LGTT offers to potential beneficiaries has been late in the project cycle (typically at tendering or at Best and Final Offer (BAFO) stage). This was too late to influence the instrument objectives of increased private sector participation or accelerated implementation of TEN-T projects, although it brought greater assurance that projects were ready for implementation and allowed better concentration on project or operational objectives.

At the same time, a market survey was conducted as part of the evaluation leading to the following observations on the instrument's attractiveness to the market

- Traffic risk during ramp-up is a small element of traffic risk and often related to medium to long-term traffic growth risks, which is the current main concern of private investors. The narrow definition of the risk coverage impeded the relevance of LGTT initially.
- The mechanism of indirect funding through Standby Liquidity Facility (SBF) providers was seen as an unnecessary complication of the instrument to the market. Currently, the funding is used to back a guarantee in favour of commercial banks which then provide a contingent SBF. The SBF can then be drawn by the project company in the case of unexpected reductions in traffic income of the project during the initial ramp-up period to assure senior debt service.
- A comprehensive and readily understandable product guideline was lacking.

C2: LGTT took four years to be brought to the market after the market testing. This proved too long since the markets deteriorated substantially in the four years, a result of Europe's financial crisis. The deterioration in the markets, led to much reduced market volumes, reducing the potential pipeline for the LGTT. The initial suggestion of 35 projects became a potential 14 eligible deals, and resulted in 7 signed deals. The current pipeline has 3 potential projects.

C3: There was no instrument level ex-ante assessment as to how likely the LGTT was to achieve its objectives. Without this assessment the emphasis quickly moved on to the practicalities of using the funds efficiently, and quantified targets were obscured in the development process.

C4: All sample projects have experienced reduced traffic volumes and, in one case within the sample, traffic is 30% down on initial forecasts. The evaluation notes difficulties with traffic forecasting at the end of an economic cycle, and with the greater potential of correlated risks between projects in such severe economic conditions.

C5: Despite this, the stated objectives at project level, to cover traffic risk during ramp-up and to improve ability of borrowers to service senior debt, were largely met. LGTT clearly facilitated financial close in a difficult market in all deals which used it. However, the timing of the guarantee was often linked to refinancing dates rather than ramp-up period per se. The funds guaranteed were more clearly linked to refinancing requirements and credit ratios rather than scale of traffic revenue losses.

C6: Finally, there was consensus that the EIB was the right choice of partner for the EC providing the expertise and resource to develop, market and manage the early growth of LGTT. The experience with the instrument has helped in the development/shaping of further partnerships with the EC, although there is a view that some additional reporting/house-keeping would bring further comfort.

6.2 Recommendations

The recommendations are presented below:

R1: A stronger up-stream marketing effort

Projects are only considered for assessment when they already have the characteristics that the LGTT essentially tried to promote. Emphasis should be on initial screening at an early stage when they still have the potential to be turned into projects with utilisation-based income and private participation. The LGTT should be promoted vis-à-vis the public authorities taking decisions regarding the procurement strategy for such TEN-T projects, so that these authorities can consider the possibility of using LGTT when making their decision. This would allow the instrument to have an impact on improved levels of private participation and implementation, and improve the impact on the overall TEN-T programme. Special efforts should be allocated to those countries where there is no PPP culture, perhaps in partnership with EPEC.

A more comprehensive and readily understandable product guidelines document/website for customers should be produced, since there is now greater knowledge within EIB about the specificities of the LGTT and the various ways of using it. This would be linked to recommendations in R1.

R2: Shorter lead time for new instruments

When LGTT was finally offered four years after the initial market testing, the financial and economic crisis had already eroded the number of LGTT candidate projects. It is essential that the lead time

needed by EC/EIB to set up new financial instruments and take them to the market is kept short (say not more than one year). Once set up, there should be emphasis on retaining the instrument's relevance and sustainability through, for example, revision of the instrument design based on an independent mid-term evaluation reflecting any changes to the market needs.

R3: *Ex-ante assessment as to whether global objectives can be met*

There was no assessment as to whether the LGTT was likely to achieve the objective to accelerate implementation for the TEN-T programme overall or at project level. For any revised or new instrument, EC/EIB should include an ex-ante test in the market and feasibility assessment to assess the likelihood of the instrument achieving its overall objectives. For each potential project, EIB should carry out and present an explanation of how a potential project will contribute to the implementation of the TEN-T programme.

R4: *The provider of Standby Liquidity Facility*

Market participants perceived the instrument to be complex, and specifically that indirect funding through Standby Liquidity Facility providers seemed an unnecessary additional complication of the instrument. There should be further discussion with the EC about mandating the EIB to directly provide liquidity to projects rather than through third-party Standby Liquidity Providers.

R5: *Clearer updated guidance and management of documents is needed for EIB Officers involved in the use of LGTT*

Documents related to LGTT at instrument level and at project level are sometimes difficult to trace. EIB should enhance its document management systems and discipline by, for example, creating a central platform, where all relevant documents are stored or hyperlinked.

EIB should also develop written guidance for officers dealing with the LGTT, in particular in support functions who are not using the instrument on a daily basis (e.g. guidelines for and revenue risk analysis in the context of LGTT operations). The analysis of the sample of projects suggests that the European economic crisis of recent years has had a significant effect across all projects.

R6: *Monitoring at instrument level going forward*

EIB should clarify and formalise responsibilities for the monitoring of LGTT and its transactions, with a view to facilitate sufficient focus and avoid conflict of interest issues. EIB should set up the capacity to monitor LGTT at instrument level, such that assessment can be quickly made of, for example, amounts signed, amounts at risk to be drawn or lost, headroom etc. EIB should also consider the option of dedicated monitoring of LGTT project transactions by a separate officer. This may require grouping with the monitoring of other joint instruments with similar potential conflict of interest issues.

R7: *Availability and quality of cost recovery information at instrument level*

Operational services should work with SG/IS/PBA (and other Bank's services as appropriate) to ensure separation of costs/revenues related specifically to such instruments from those linked to other elements of corresponding lending projects (e.g. senior debt in the case of LGTT). This recommendation should in particular be considered in the context of the Horizon 2020 implementation of the Horizon 2020, the Connecting Europe Facility and other new joint instruments, and in support of recommendations arising from the Joint Actions Working Group (SCC/SMCBAP 2011-0088).

In addition, the operational services should ensure the quality of instruments-related time records. In particular, specific attention should be paid to (i) timely creation of relevant product codes, which will enable proper tracking of pre- and post- signature costs, and (ii) ensuring the completeness and accuracy of time records of relevant staff working on such activities.

R8: *Further development of partnership with EC*

Whilst most of the reporting to the EC is performed as required, there were areas for improvement. In order to further promote the development of the partnership between EIB and EC it is recommended that

- At project level, EIB should enhance reporting to EC on financial risks for signed LGTT deals e.g. where risk profiles for individual projects are deteriorating significantly.
- At an instrument level, EC/EIB should hold LGTT Steering Committee meetings more regularly or record why they are not held.

- EC/EIB should confirm whether the development of further coverage of traffic risk beyond the ramp-up period is a workable option to enhance the relevance of design of the instrument to market participants and increase its likelihood of being effective.

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APPENDICES

Appendix 1: Aide-mémoire

POSSIBLE EU GUARANTEE INSTRUMENT TO SUPPORT TEN TRANSPORT PROJECTS³⁵

Within the framework of the European Initiative for Growth, the European Council of 12 December 2003 invited the Commission, in co-operation with the Member States, to examine the idea of developing a specific EU guarantee instrument for certain post-construction risks in TEN transport (TEN-T)³⁶ projects, to report on the results of the examination, and, if appropriate, to present a proposal in this regard. It is essential that the guarantee instrument should provide a workable response to the needs of market operators who will finance and manage the projects concerned. The Commission has therefore started a process of market testing with interested parties.

The Guarantee instrument

Aim: The Facility would offer guarantees covering specific commercial risks. The aim of the instrument is to

- leverage private sector funding of TENs
- reduce the financing cost of projects
- to accelerate the conclusion of financial packages.

Risk covered: The EU guarantee instrument would focus on post-construction risks in projects such as the risk of traffic and/or revenue shortfalls.

Period covered: The guarantee would partially cover shortfalls measured relative to an agreed break-even base scenario during an initial period (3-5 years) of the post construction phase.

Eligible projects: The guarantee would be available to TEN-T projects that are economically sound and cost-effective and, after grant aid, have an acceptable prospect of financial viability. An investment grade rating could be certified by an independent third party (e.g. rating agency). A priority would be given to cross-border projects, in line with the Quick Start programme³⁷ of the European Initiative for Growth.

Beneficiaries: The guarantee would be available to debt providers who would benefit from appropriate debt-service for the initial period of the post-construction phase. Loans backed by EU guarantees would benefit from a 0% risk weighting.

Guarantee type: As a debt-service guarantee the instrument would work in a similar way to the insurance offered by monoline insurers. The guarantee instrument would provide the beneficiary with a time-limited substitute for the revenue sources that would normally support regular debt repayments. The guarantee would therefore not cover acceleration of debt repayment.

Guarantee rate: The guarantee instrument would cover a share of the annual debt service over the respective period (3-5 years), the remainder to be taken by the Member State(s) and the private sector.

Risk premium: The intention is to charge the beneficiary a premium calculated on a risk basis.

³⁵ Please note that this aide-mémoire is based on the initial proposal following the Commission Communication of November 2003. It was used during the market testing exercise in Spring 2004. This is not the final proposal for the design of the instrument

³⁶ The legal basis for the TEN-T is provided in the Treaty of the European Union. On July 1996 the European Parliament and the Council adopted a Decision on Community guidelines for the development of the trans-European network (TEN-T). These guidelines comprise roads, railways, inland waterways, airports, seaports, inland ports and traffic management systems which serve the entire continent, carry the bulk of the long distance traffic and bring the geographical and economic areas of the Union closer together. These guidelines are a general reference framework for the implementation of the network and identification of projects of common interest (TEN-T projects).

³⁷ Following a request by the European Council in October 2003, the Commission and the EIB established a list of projects in an enlarged Union meeting the following criteria: high level of maturity, trans-frontier dimension, impact on growth and innovation in the enlarged EU and benefits to the environment. In addition to transport sector, the Quick Start list includes projects related to research, innovation and development as well as broadband networks.

Risk sharing with Member States: The Commission would expect the Member States to offer at least comparable support to the project as that offered by the instrument.

Risk sharing with the private sector: A portion of the risk would be borne by the private sector.

Event of default: The event of default would be defined as the shortfall measured relative to an agreed break-even base scenario.

Issues for discussion

- (a) Whether the EU guarantee would respond to market demand.
- (b) Alternative ways of leveraging private sector investment.
- (c) Impact of the EU guarantee on the financing costs of projects.
- (d) Whether the EU guarantee could substantially facilitate the conclusion of financial packages.
- (e) Appropriateness of a debt service guarantee.
- (f) Added value vis-à-vis monoline insurers.
- (g) Minimum critical mass.
- (h) Reasonable risk sharing between Private sector/Member States/Community.
- (i) Whether non-commercial post construction risk, such as failure to meet contractual commitments by public authorities, are adequately covered by other legal or market mechanisms (insurance).
- (j) Applications of risk sharing techniques on the management of the portfolio.

Appendix 2: Analysis of the various components of LGTT Design

Each aspect and its relevance to the ultimate objectives of LGTT are discussed below.

- Scope of Risk

By the time the LGTT Agreement and regulation were written it was clear that only risks related to demand were covered, effectively ruling out availability based schemes. From discussions with EC and EIB staff it emerged that the key reason for this was that availability risk is often related to performance risk, a risk that the private sector should be in control of and hence cover. Whilst this definition restricted the number of eligible projects for LGTT, it is based on a sound rationale.

- Eligibility

A key application issue is that projects when selected by EIB no longer have the potential to increase utilisation-based income, private sector participation or improve timelines. The eligibility criteria therefore have limited impact on setting the successful direction of the instrument. In addition, there may be a geographical market constraint since, in principle, all EU MS and all TEN-T sectors are eligible for the instrument, the LGTT appears more suited for application in countries which have a culture in private infrastructure financing and in the road sector, which limits the market potential for the application of the instrument.

- Priority

In the EC communications of 2005 the guarantee is considered to be particularly applicable or useful to cross border projects and large and complex projects. It was proposed that if there was a need to prioritise, such projects should be given precedence. The TEN-T regulation of June 2007 stressed that the priority for TEN-T funds generally was the priority corridors especially cross-border links and removal of bottlenecks.

The LGTT Agreement, under the guidance on eligibility, assigns priority to TEN-T Priority Projects but does not specifically mention cross-border projects in the main text. However it includes an incentivised higher closing fee for EIB for a cross-border section of a Priority Project (almost three times that for a non-cross-border section). It is not clear how LGTT has been geared to this use. Cross border projects often have difficulty in reaching maturity because neither country views them as a domestic priority and the levels of traffic are often very low, making them unsuitable for real or shadow toll based PPPs.

- Portfolio effects

Though the initial estimates appear to agree on a portfolio size of 30-35 projects, the Credit Risk Department of the Bank expressed concerns in a note of April 2007 that demand for the product might not be able to generate a sufficiently large and diversified portfolio to compensate for the potential losses on a single project (without specifying how big they thought this would be).

- Creditworthiness Rating of Projects

The early concept papers at first suggested projects should be investment grade and later that they should be near investment grade (described in the EC Technical Note as not lower than BB according to S&P rating). This requirement was removed prior to drafting the LGTT Agreement. The relaxation of the requirement in the update seems to have been essential since otherwise even the 7 deals signed may have been excluded. While the senior debt of the same projects is D- or better, the LGTT component of projects were rated in the band E according to EIB's loan grading system.

- Pricing

The EC concept paper (COM(2005)76) proposed that the instrument, being equivalent to mezzanine financing, should be priced "according to the risk taken and reflecting management costs" and should at least cover the expected costs of the instrument. The TEN-T regulation rephrases this as being in line with the relevant rules and criteria of the EIB, as is the current practice.

- Conditions Precedent

Key elements of the design of a guarantee are the conditions under which it can be called. The concept papers from the EC refer to conditions often applied by SBF providers to protect themselves from materially adverse change or violation of performance covenants. These often make them less convincing to rating agencies looking for improved creditworthiness. A proposed benefit of an EU guarantee instrument is to protect the SPF providers from major project risk and thereby achieve a

reduction in premiums. The concept documents and the LGTT Agreement do not specify any conditions precedent.

However the provider of the guarantee is clearly EIB, and CRD raised similar concerns to those of SBF providers – how a guarantee aimed at solving a very particular ramp up risk could be protected so as not to be drawn to cover other problems and particularly not if after the call the project would still default. CRD proposed a number of conditions precedent in their paper of April 2007:

- The projects loan life cover ratio (LLCR) should be above 1.0 following drawdown
- If necessary standby equity should be available to ensure this (CRD were under the impression also that LGTT had to be matched by standby equity to maintain gearing ratios).
- That the project had an acceptable tail (i.e. the period after senior debt is repaid) to repay the subordinated debt.

There was a belief at CRD that an event of default under the ramp-up risk could not be isolated and they, in fact, proposed widening the guarantee to cover any default. In the eyes of market participants, of course, any conditions precedent were considered as a complication of the instrument, which compromised its attractiveness, by comparison to other forms of risk cover which were unconditional (e.g. equity).

- Risk and Revenue Sharing

Once the initial idea of risk-sharing with the public and private partners was dropped it became an issue of how to share the risks and revenues between the EC and EIB. The risk sharing described in Annex II of the LGTT Agreement is relatively straightforward – EC and EIB each cover 50% of the Expected Loss (EL) and Capital Allocation whilst EIB covers any residual risk. For revenue sharing the LGTT Agreement refers to an Appendix which is a Technical Note from ECFIN-L1. This is similar to the note attached to the Staff Working Paper referred to above, which explains the provisioning system, through equations and tables and eventually resulting in a risk-sharing table.

Whilst the risk sharing mechanism seems generally fair, it has been found to be relatively demanding on EIB capital at a time when capital adequacy is given greater importance. A new proposal has therefore been made to use the EC contribution as a first loss piece for the LGTT portfolio. This proposed change is considered to be a consequence of the changing attitudes to use of capital in EIB rather than a failing of the original design.

- Choice of Partner

The concept papers talk of a managing agent for the guarantee instrument, though EIB was “an obvious candidate”. By the time Regulation (EC) No 680/2007 was put in place, the decision to use EIB had been made. Based on a review of the market testing phase undertaken in 2004 and on interviews with the TEN-T Executive Agency and the EC’s DG MOVE undertaken in April 2013 evidence suggests that the EC needed a banking partner for the LGTT and could not have implemented the instrument by itself. The requirements stipulated in EU regulations, including Financial Regulation 1605/2002, make it easier for the EC to work with a public sector body.

The EIB, being a public sector institution under the Treaty on the Functioning of the European Union (TFEU) with the mandate to further EU policy objectives within all EU MS, therefore appeared best placed with the right status, alignment of objectives and regional coverage to be mandated with the implementation of the LGTT. Furthermore EIB was regarded as having competences essential for the implementation of the LGTT, including its experience with the financing of relevant projects in EU MS, marketing, risk assessment, as well as treasury operations. There was no other public sector bank alternative to EIB with the required EU-wide coverage. The fact that the EC has also selected EIB for implementing the Project Bond Initiative underlines the confidence it has in EIB to implement innovative financing instruments.

Aspect	“Original” idea (Founding papers and press)	As in Cooperation Agreement	In practice	The initial evaluation questions for each aspect
Concept	Traffic ramp up is the risk key deterrent to private sector funds	Article 2 point 5 agrees with original idea	Seems to be viewed almost as important, if not more so, as pre-payment of senior debt at or around refinancing stage	Were there other reasons? Key barriers for private sector investments in TEN-Ts are the lack of mature projects and the long lead times of such projects. Whilst addressing the barrier of excessive risk transfer to the private sector to some extent, LGTT is unlikely to overcome these overriding barriers.
Eligibility	All TEN-T sectors	All TEN-T sectors, utilisation based income, public and private participation	Seems to have been followed though NPST say does not need to be PPP (not sure this matches CA)	Was this right? Suitable for rail? LGTT is only eligible for a part of the TEN-T pipeline, so it cannot have a big impact on advancing the TEN.
Priority	Strong emphasis on cross borders, bottlenecks and multi-country	Closing fee for Priority projects and higher one for Priority cross border projects	Not enough projects to prioritise	Are PPPs the right way to go? Would cross border projects be done on traffic risk basis?
Size – overall capital allocation	500 MEUR x 2	Same (Art 2 point 4) but actual transfer based on EIB requests	Total pool of funds reduced due to lack of demand, 200MEUR diverted to bonds	Was drawdown of 1bnEUR ever feasible?
Size – limit as % of Senior Debt	5%, 10% and 20% all mentioned	20%	20% max, but usually less	What criteria used to set this?
Scope of risk	Ramp up period but not only traffic? Only partial cover – public and private should share	Clearly traffic only and no reference to risk sharing other than EC/EIB	Still traffic though situation with respect to other EoDs gets murky in later deals	EP report on new financial instruments includes general recommendation to minimise the transfer of demand risk to the private sector. Question why assign it at all to the private sector who cannot control it?
Rating of project deal	“Near investment grade”	Not specified	None were worse than E- but does that comply?	Not sure any went from “near” to “full” investment grade as a result of LGTT
Target portfolio size	EC papers suggest 30, CRD concerned it would be too small but logic in paper faulty	Not mentioned	Unlikely to be ever achieved – so should provisioning have changed?	
Provisioning	EC papers show a “front-loaded” system and talk of refining	Not mentioned. CPRG rules used	CPRG rules give fixed capital allocation for a given EL	Should this be affected by portfolio size and composition?

	method over time			
Pricing	Full risk margin plus op costs	Confirmed. Residual risk also included (allows for upward modulation)	All rates at mezzanine stage include upward modulation	If LGTT is fully priced (i.e. not subsidised), why should it lower overall financing cost?
Conditions	LLCR ≥ 1 (CRD), tail, EoD limits, SBF support matched by equity	Not clear – just says subject to conditions precedent	Conditions varied over time – seemed to get more lenient	Was this pushed too far (CRD seemed to think so)
Pay-out in the event of default	Included	Included	First deals no, last 4 increasingly allowed	
Trigger	Traffic x% below base – CRD proposed any EoD triggers prepayment of Senior Debt	Very broad criteria for call of guarantee – any default up to SBF value	All have a traffic trigger below base or downside case, some have a “floor”	Can it be triggered by other EODs in effect
Availability period	Usually 5, 7 in exceptions	Usually 5, 7 in exceptions	3 to 7 years	
Pay-out to SBF provider	Annual or one go at end, full amount	Not specified	Mainly one shot but two with contingent option	Why have an SBF provider between EIB and the sponsor? This would only increase cost of the instrument without clear benefit.
Treasury arrangements	Unknown at that time	Investment and liquidity rules in Annex V, timing of payments into and out of LGTT account	To be investigated	Do EC think it is a zero loss deal? The regulation reads that way.
Risk and Revenue Sharing	Magnette paper proposals Unclear and seems unfair – was it used?	Risk: Simple 50:50 of EL + UL Revenue: EL + UL plus prorata share of EIB lending rate (Magnette paper referred to but not used)	Seem to follow main text of CA but ignore annex	
EIB cost coverage and fees (including timing of payments)	Unknown at that time	EIB flat fee per year of 4% plus closing fees plus treasury management fee	Not sure – Mark cannot track these payments yet	Get update of MCO papers to see what overall cost coverage is now
Consequences of cancellation	Unknown at that time	EIB tries to get a penalty fee	Upfront fees cover any cancellation costs	

Cost of LGTT offset by savings in senior debt	Referred to in many presentations e.g. LGTT fact sheet	Not explicitly mentioned	Not claimed in many cases – will need to dig to see where it did occur	LGTT only covers a very small part of the overall risk (even only a small part of the traffic risk), so is it appropriate to expect a large impact on financing cost?
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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:

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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)
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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)).
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26. Evaluation of Cross-border TEN projects (2006 - available in English (original version) German and French).

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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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54. Ex post evaluation of EIB’s Investment Fund Operations in FEMIP and ACP countries (2013 – available in English)
55. The loan guarantee instrument for TEN-T projects (LGTT) – An evaluation focusing on the role of the EIB in the implementation of the instrument (2014 - available in English)
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