OPERATION EVALUATION SUMMARY

Mid-sized corporate support facility

Regional

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EBRD EVALUATION DEPARTMENT

European Bank
for Reconstruction and Development

1 Executive summary

The mid-sized corporate support facility was a €250 million framework intended to provide a streamlined approval process for loans of up to €20 million to existing Bank clients experiencing difficulties obtaining short-term financing due to local banks being affected by the global financial crisis. The facility aimed to support fundamentally sound Bank clients, by financing primarily short-term working capital loans refinancing and the completion of capital investments, commenced by the clients before the crisis. By demonstrating the EBRD's support and confidence in its clients, the facility was also to act as a catalyst for attracting co-lenders and ensure the continued engagement of local commercial banks. The ultimate objective was for facility loans to be refinanced by commercial banks as soon as normal conditions returned to the credit markets.

The facility differed from the Bank's usual operations in that it provided working capital financing and refinancing which the Bank usually does not provide, at least on its own. Otherwise, the facility was essentially a mechanism designed to streamline the approval process which was of critical importance for this type of financing and under the given circumstances.

In the course of this evaluation EvD has also looked more broadly at the Bank's financing facilities and frameworks which represent some 50 per cent of all signed operations. Assessment of the Bank's entire facilities/frameworks portfolio is not the purpose of this evaluation but observations on the Bank's approach may help put it into better context and could also contribute to an ongoing discussion about such facilities between Bank Management and the FOPC.

1.1 Findings

- The large number of financing facilities available at the Bank creates confusion and "facility fatigue" among some bankers.

In the last ten years the Bank has approved 96 facilities, 25 of which have been in the last three years. There are some overlaps among the various facilities while the application of others is limited by their strict eligibility criteria.

There is scope for consolidating some facilities and/or standardising their eligibility criteria. The introduction of more fundamental changes, such as the universal delegation of approval for all smaller projects (below €20 million) to OpsCom or SBIC, would result in a substantial decrease in the number of facilities.

- The Bank's usual focus on financing capital investments in the corporate sector makes it difficult for the Bank to act as an *ad hoc* working capital provider, even in a time of crisis.

Only three of the ten facility sub-projects can be regarded as working capital loans. Clients who used the facility to finance new capital investments commented that the need for very speedy approval, the limited amount required and the revolving nature of working capital financing puts it more naturally within the remit of local banks, even if their costs are slightly higher.

The introduction of new facilities, particularly those which aim to provide a type of financing not usually offered by the Bank, requires a careful approach while the demand for such financing should be tested with a smaller budget envelope.

- Companies which are financially sound are likely to continue receiving working capital financing from local banks, even during a crisis.

As the Bank sets high standards for its clients, many of them represent a well-managed, corporate elite in their countries. They are likely to continue attracting short-term financing from their house banks, even during a crisis.

Financially sound companies, such as most Bank clients, are likely to continue to attract local bank short-term financing even during a crisis.

- A financial crisis (and some of its side effects, like currency devaluation) may paradoxically help well-positioned companies to expand their business.

Some of the facility clients (which used it to finance capacity expansion) commented that their business thrived during the crisis as new foreign customers appeared searching for better value quality products. In particular, many agribusiness companies in the Bank's region were able to exploit their competitive advantage. Devaluation of local currencies (40 per cent in case of hryvnia) further improved their competitiveness in the international market.

The impact of an economic or financial crisis varies among the Bank's corporate clients. Manufacturers of good value quality products can thrive, expanding their business (particularly export) helped by local currency devaluation.

1.2 Recommendations

The Bank should consider a review of procedures related to approval of smaller projects. A key objective of numerous Bank facilities is to streamline approvals for smaller projects (some below €10 million, others below €20 million). The large number of facilities (60 active at the end of 2012) and their various eligibility criteria are seen by many as confusing and not lending themselves to active marketing to the clients.

The Bank should consider a review of facilities which have similar objectives with a view toward consolidation or standardisation where possible. This might also include a review of changes to the approval policies for smaller projects, such as greater delegated authority at the Board level. Such a review would also consider the scope of documentation required to support such a process, including reporting back to the Board on performance of smaller operations.

It is noted that a recommendation along these lines was made to FOPC on 1 March 2012 (CS/FO/12-05 and CSF/FO/12-06) by the Bank's Management. The issue was acknowledged but better impact assessment in respect of financing facilities (also involving EvD) was advised, while the key decision on facilities consolidation and/or minimum threshold for Board approvals of all projects was deferred.

2 Project ratings

The operation is rated “partly successful”, primarily due to “satisfactory” achievement of its operational objectives.

The additionality is rated “largely verified” as there is evidence that some local commercial banks continued to provide working capital financing to their financially sound clients, the same type of clients as those targeted by the facility.

The financial performance of the facility is rated “good”. Revenues from several of the sub-projects exceeded projections but higher material and/or labour costs squeezed the profitability ratios of most of the sub-projects below those forecast at approval. Nevertheless, all sub-projects have been repaying their loans on schedule and have remained generally compliant with their financial covenants.

Bank handling is rated “satisfactory to good”. It recognises the very good organisation and efficient promotion of the facility within the Bank by the facility management team, as well as the generally fast and good quality sub-projects processing by their respective teams. On the other hand, based on several interviews at Resident Offices (ROs), there is evidence that the effort by line bankers to promote the facility to potential clients was not always focused and may not have been conducted with sufficient dedication of time and resources. Where financing was agreed, the facility sub-projects were generally well prepared, with clearly stated objectives and adequately defined performance monitoring metrics in terms of physical project completion, financial performance of the borrower, as well as TI benchmarks (adopted from the original projects or set anew in one case).

Transition impact (TI) is rated “good”. With regards to the transition benchmarks in aggregate (set for four original transactions related to four sample sub-projects) 57 per cent had been achieved at the time of the approval of the sample sub-projects, while at the time of evaluation 65 per cent of these benchmarks were achieved. Despite the rather marginal impact of the facility sub-projects on the incremental achievements of the TI benchmarks, the overall impact of the facility's financing was very positive (if it is assumed that clients could have experienced serious financial distress or even have gone bankrupt without it). This rating also reflects the Bank’s engagement in policy dialogue in Ukraine, in particular its contribution to a successful resolution of VAT reimbursement issue, which helped address the facility clients’ liquidity problems.

Environmental performance is rated “marginal” and environmental change is rated “some” as several reviewed projects show that it is usually environmental compliance and the implementation of ESAPs adversely impacted by cost-cutting induced by a financial crisis.

Table 1. Summary of ratings

Relevance	
Additionality (Fully verified, largely verified, partly verified, not verified)	Largely verified
Effectiveness	
Achievement of operation objectives (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Satisfactory
Project financial performance (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Good
Efficiency	
Bank handling (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Satisfactory to Good
Bank investment performance (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Good
Impact and sustainability	
Transition impact (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Good
Environmental and social performance (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Marginal
Extent of environmental and social change (Outstanding, substantial, some, none/negative)	Some
Overall performance rating (Highly successful, successful, partly successful, unsuccessful)	Partly Successful

3 Project relevance to the EBRD’s mandate

3.1 What was the rationale behind this project?

The context of this operation must be clearly understood at the outset: the depth and scope of the financial crisis, and the speed with which it metastasized, caught virtually all market participants by surprise. A particular concern within the EBRD was its potential to roll back hard-won gains in transition, market-rooted policies and still-nascent reforms.

The facility was designed as an important component of the Bank’s response to the crisis. By limiting its applicability to existing clients, the facility was expected to substantially shorten financial and legal due diligence and to offer an accelerated sub-project approval process. However, the facility had a number of limitations as it was restricted to “fundamentally financially sound” clients; instruments outside the mainstream of the Bank's activities were to be "approached with caution"; and new projects were excluded.

In recent years, facility sub-projects have accounted for just under 50 per cent of all projects signed by the Bank. Many of these facilities are highly specialised by sector, region or country but in 2009 there were some whose objectives and eligibility criteria were not dissimilar to those of the facility as recognised by the time of final approval.

The Facility for Medium-Size Projects (FMSP), approved exactly one year before the facility, had similar eligibility criteria for sub-projects, except that it targeted new rather than existing clients. EvD’s 2009 interim review of the facility (PE09-440) highlighted the low utilisation rate of FMSP, citing "the abandonment of projects by sponsors as a result of the crisis" as the main reason for the slow take-up. The disappointing performance of a similar facility, directly owing to the crisis, should have raised questions about the need for yet another facility or at least presented the option of expanded the FMSP criteria to cover existing clients.

Nevertheless, when considering the rationale behind the creation of the facility, one should not underestimate the importance of the political and economic mood prevailing at the time of its approval. The impact of the financial crisis was impossible to predict but there were numerous calls for international financial institutions to take action. The EBRD wanted to demonstrate its willingness to join crisis-response efforts with a relatively substantial programme, offering its corporate clients rapid "no frills" relief to their financing problems. Therefore, one could argue that there was no time for market testing and cautious steps and the best solution at the time was to proceed with new large headline-grabbing programmes.

3.2 Did the project provide additional support to the market?

Ultimately, the impact of the crisis on the Bank's mid-size corporate clients was not as adverse as anticipated, particularly on those which remained in a relatively good financial condition. A selection of these financially sound clients were interviewed by EvD and commented that while their local banks tightened credit and increased interest rates during the crisis they continued to finance their working capital needs as they had before the crisis. Less financially healthy clients confirmed the high utility and uniqueness of the facility as the only available source of working capital financing or short-term debt restructuring at that time. Paradoxically, the Bank was even more additional in the case of four loans provided to finance new capital investments because such financing required longer tenors than working capital loans and such tenors were rarely available in any of the Bank's countries of operations during the crisis.

Although there are no doubts as to the Bank's relatively strong additionality in respect of the particular sub-projects actually financed by the facility, the additionality of the facility itself must be rated only “largely verified” due to its limited utilisation which, to a certain extent, also reflected the limits of the Bank's additionality in offering such financing.

Table 2. Additionality ratings

Additionality (Fully verified, largely verified, partly verified, not verified)	Largely verified

4 Project objectives

Table 3. Rating of objectives

Achievement of objectives (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Satisfactory
Company financial performance (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Good
Project financial performance (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Good

4.1 What were the objectives and to what extent were they achieved?

– Finance about 25 crisis-response sub-projects, utilising €250 million of facility funding.

Of the Bank’s 135 corporate clients, 24 clients/projects were considered suitable for facility financing. However, ultimately about two-thirds of them turned out not to be so. This objective is rated “partially achieved”.

– Streamline due diligence and project approval process, substantially cutting inception to disbursement time.

Four out of ten sub-projects were for €10 million or less and approved by OpsCom under one-stop procedures, substantially shortening the approval time. Six projects with loans over €10 million were approved relatively quickly, despite the requirement to obtain the Board's "no objection". Two more financially complex projects had to return for a second OpsCom approval and therefore took longer to process but despite this only one project exceeded the average time for processing corporate projects under normal procedures, which is approximately nine months. Post-signing monitoring is estimated to have taken only about one man-month, compared to the average of 10 needed to monitor 10 separate stand-alone projects.

This objective is rated “achieved” as processing projects through the facility cut the approval time by approximately 66 per cent.

Overall, the achievement of objectives is rated as “satisfactory” as the key objective behind the facility was to build a critical mass of projects and use up all, or nearly all, the funds available under the facility, which was partially achieved.

4.2 How did the project/company perform financially?

All four companies which borrowed under the sub-projects examined as samples for this evaluation performed reasonably well, repaying their loans on time and complying with their financial covenants. All of them, however, have performed below the projections made at approval.

Of the remaining sub-projects, EBITDA and net profits improved for three clients while one showed a slight deterioration and another was hit more heavily by the crisis and was in breach of most financial covenants.

Overall, despite problems still being experienced by selected clients even in 2011, most of them showed a clear recovery trend. This was particularly pronounced in respect of agribusiness and agri-related equipment producers as well as utilities, while the slowest to recover were producers of building materials and home fittings, mainly due to the higher cost of raw materials. Overall, the financial performance of the facility is rated “good”.

5 Project handling efficiency

Table 4. Efficiency ratings

Bank handling (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	Satisfactory to Good

5.1 How well did the Banking team handle the project?

Forecast of demand for the type of financing to be offered by the facility was based more on anecdotal evidence than on thorough market research, while political peer pressure played an important role leading to the creation of this facility. After approval, the Bank organised its work under the facility well, with the facility OL providing frequent and exhaustive information to all team leaders and countries of operations.

The Bank's marketing effort was also well prepared but not always implemented in the most efficient way by the bankers at the front line. Bankers confirmed that they were provided with extensive information about the facility which they conveyed to clients but it seems there was no dedicated effort or concerted action to pro-actively market the facility to clients. Some bankers interviewed by EvD admitted they were confused about the large number of facilities available at the EBRD and preferred to channel new sub-projects through more familiar facilities. The facility was also viewed as relatively inflexible with tight eligibility criteria.

However, processing was very efficient and (with one exception) considerably shortened the approval time. The sub-projects were generally well prepared with clearly stated objectives and adequately defined performance monitoring metrics. Monitoring was also highly efficient as sub-projects were combined with the original projects during credit and PMM reviews. The facility itself was monitored by the OL through an Excel spreadsheet, which might not be seen as the most sophisticated way but is still in line with the standard for monitoring other facilities at the Bank. The sub-projects did not require incremental transition impact and most of them did not have new TI benchmarks. A review of TIMS for the original projects demonstrated uneven quality, with some of the TIMS giving a good description of the status of TI benchmark fulfilment while others needed updating.

Reporting on facility performance to the Board was good with two reports presented. These reports provided fairly exhaustive and accurate coverage of the facility's performance.

6 Project transition impact and sustainability

Table 5. Transition and environmental impact ratings

	OPA	EvD
Realised transition impact (Excellent, good, satisfactory, marginal, unsatisfactory, negative)	*Not rated*	*Satisfactory to Good*
Potential transition impact (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	*Not rated*	*Good*
Risk to potential transition impact (Excessive, high, medium, negligible, low)	*Not rated*	*Medium to High*
Overall transition impact (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	*Good*	*Good*
Environmental and social performance (Excellent, good, satisfactory, marginal, unsatisfactory, highly unsatisfactory)	*Good*	*Marginal*
Environmental and social change (Outstanding, substantial, some, none/negative)	*Not rated*	*Some*

6.1 What were the expectations for transition at approval?

The facility itself had no transition potential rating nor transition risk rating as this was to be determined for each sub-project. The sub-projects were not required to bring any incremental transition impact as the stated aim of the facility was to "protect and reinforce the transition gains of the original operations".

6.2 What was EvD’s assessment of transition impact?

The impact of the facility sub-projects on the "protection and reinforcement of the transition gains of the original transactions" was uneven and varied among the sub-projects. By helping its clients address their working capital shortages, restructure short-term debt or complete capital investments, the Bank helped them stay afloat, avoid financial distress or even bankruptcy, which would arguably eradicate any transition achievements. However, analysis shows that "protection and reinforcement of transition gains" was more successful where the client's underlying business model was better suited for a time of crisis.

The facility clients unanimously confirmed that the EBRD's continuing engagement with them during the crisis reassured and renewed the confidence of their suppliers, clients and local banks. Moreover, it is noted that the transition/additionality objectives for some of the sub-projects included "continuation of policy dialogue with the host government" and this is particularly relevant to Ukraine, where the Bank was actively involved (alongside other IFIs) in a dialogue with the government in respect of overdue VAT reimbursements and the facility clients confirmed that the Bank played a positive role in bringing it to resolution.

The facility's overall transition impact is rated “good” in recognition of its overwhelmingly positive impact on the financial performance of its clients, which in turn helped them diminish the risk of financial distress and the loss of any transition gains already achieved under the original transactions. However this rating is granted with a proviso that some of the facility's individual sub-projects, if rated, would warrant lower ratings on account of their disappointing progress with the fulfilment of the original project's TI benchmarks.

6.3 What was the impact on the environment?

– Environmental and social performance

Similar to the transition impact, the facility sub-projects were not expected to bring incremental environmental or social benefits.

Of the four evaluation sample sub-projects, three had problems related to the implementation of the ESAPs agreed with the Bank under the original projects. One did not implement (or even prepare) a stakeholders' engagement plan, while another failed to construct a WWTP required under the ESAP. Most remarkably, in one case the client made no progress with introducing a requirement for its suppliers to apply sustainable forest management and commented that, in the context of rapidly increasing wood prices and a high demand for wood, it had little influence on the practices applied by its suppliers, which was not envisaged when the ESAP was agreed with the Bank.

The environmental and social performance of the facility is rated “marginal”.

– Extent of environmental and social change

Notwithstanding the above described cases, at least one facility sub-project successfully promoted environmental change. This was the introduction of freon-free technology in display coolers where the facility financed the acquisition of a refrigerator manufacturing technology line which utilised green gases. This was one of the first applications of such technology in the CIS and reportedly has already been replicated by two other producers in Russia.

The extent of environmental change brought about by the facility sub-projects is rated “some”.