

Transition Impact Retrospective

How the EBRD has advanced transition



European Bank
for Reconstruction and Development

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One Exchange Square
London EC2A 2JN
United Kingdom

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Contents

Foreword by Jean Lemierre	ii
Foreword by Leszek Balcerowicz	iii
Introduction	iv
Chapter 1	2
Analytical framework for the TIR	
Chapter 2	5
The EBRD's role in mobilising capital for the transition	
Chapter 3	6
Synopsis of PED project evaluations	
3.1 Overview	6
3.2 Transition impact ratings, by region	6
3.3 The sectoral perspective	7
3.4 Technical cooperation strengthens transition impact	8
Chapter 4	9
Transition impact at the sector level	
4.1 Overview	9
4.2 Summary results	9
Chapter 5	13
Legal transition assessment	
5.1 Current state of legal transition	13
5.2 Summary of legal transition impact	13
Chapter 6	15
Environmental transition assessment	
6.1 Environmental challenges	15
6.2 The EBRD's response	15
6.3 The EBRD's environmental impact and performance	16
Chapter 7	19
Conclusions	
Annex 1: EBRD operations by sector	22
Annex 2: Transition impact at the project level	32
Annex 3: Legal transition assessment – event line and methodology	33
Annex 4: Environmental compliance – lessons learned	38

Foreword

Jean Lemierre, President, European Bank for Reconstruction and Development

The EBRD has a unique mandate among international financial institutions. The Bank was established in 1991, to foster transition to an open market-oriented economy and to promote private and entrepreneurial initiative in the formerly centrally planned economies of central and eastern Europe and the former Soviet Union. The Bank tries to achieve these objectives by investing in projects with a private sector focus. It works with its partners on projects that advance the transition, are financially sound and would be less likely or less effective without its participation.

The process of moving from a centrally planned to a market economy requires deep legal and institutional change and radical changes to business practice. Although much remains to be done, there has been substantial progress in market reform in many of the EBRD's countries of operations. In particular, prices have been liberalised, enterprises have been privatised, and regulatory frameworks for banking and infrastructure have been developed. These developments are analysed in detail in the EBRD's annual *Transition Report*.

This *Transition Impact Retrospective* assesses how, in its first ten years of existence, the EBRD has contributed through its projects to the process of transition. The Bank has been active in

a number of areas over the last ten years, from financing of banks, to business start-ups and small enterprises, commercially oriented infrastructure, and large enterprise restructuring. The *Transition Impact Retrospective* shows that EBRD involvement has resulted in the finance of projects in the region worth over US\$ 50 billion. EBRD projects have generally been successful in meeting their transition objectives, especially in countries where the operating environment is conducive to private sector participation. The EBRD has been important in developing the legal framework for markets and in contributing to improved environmental performance.

The *Transition Impact Retrospective* has benefited from the comments of various experts in the field of transition. In this respect, I would like to thank: Professor Tim Besley (London School of Economics); Demetrios Papageorgiou (Rubicon Capital); Professor David Pearce (University College London); Professor Gerard Roland (ULB, Brussels); Marcelo Selowsky (World Bank); Professor Jan Svejnar (University of Michigan and CERGE, Prague).

The responsibility for the *Transition Impact Retrospective* is taken by myself on behalf of the departments within the Bank that contributed to the report: Office of the Chief Economist, Banking (including Resident Offices), Project Evaluation Department, Office of the General Counsel and Environmental Appraisal Unit.

Foreword

Leszek Balcerowicz, President, National Bank of Poland

Post-communist transition in central and eastern Europe and in the CIS has been one of the most fundamental institutional and social transformations at the turn of the 20th and 21st centuries. This has generally been a positive change, if compared with the alternative of a continuation of the Soviet regime in this region. The evolution of the economic performance recorded by the countries involved has depended on the magnitude of the external shocks they suffered, on their initial structural situations, and on the quality of the policies pursued, primarily in the area of institutional reform. Since these shocks were a given (a non-controllable factor), it is policy, including the creation of effective institutions, that has played a crucial role in shaping the economic performance of the post-communist countries, i.e., in advancing – to a lesser or greater extent – their transition towards an open, market-oriented economy with a suitably reduced role assigned to a restructured state.

The purpose of the *Transition Impact Retrospective* is to assess the impact of the EBRD on transition (the transition impact, TI) and to establish its main determinants. Ideally, one would wish that TI were measured by comparing real-life developments (taking account of EBRD activities) with the counterfactuals (no EBRD, and therefore no EBRD activities). However, one can understand the difficulties which prevented the authors from adopting this approach. They have instead employed very ingenious second-best methods to obtain the TI assessments. Their study makes a substantial contribution to exploring the general topic of post-communist transition, even if some questions unavoidably remain as regards the more specific issue of measuring the contribution of the EBRD to transition in the respective countries concerned.

The concept of the transition impact of the EBRD excludes, by definition, the financial returns from EBRD projects and conventional externalities, as captured by cost-benefit analysis. The TI is reduced, therefore, to the positive “systemic externalities”, or in other words, the systemic spillover effects. It is important to draw a clear distinction between: 1) the scale of a given EBRD activity in a given country; and 2) the impact proper (in controlling for the scale). Obviously, there could have been no impact without activity; yet additionally, as the report acknowledges, there might be certain thresholds of activity below which the operations of the EBRD (or other institutions) fail to produce any systemic spillovers.

As records on additional completed projects become available (including more closely comparable projects with different scales and across different countries), a further examination of the cross-country differences in scale of EBRD activities would allow some other important questions to be investigated. These include: what was the relative scale of activity of other comparable institutions? What was the role of various country characteristics? To what extent were the differences in scale attributable to the differing performance of the EBRD country teams or to other factors external to the countries in question?

By separating the analysis of scale from that of the impact proper one might perhaps obtain a better understanding of when insufficient TI was the result of insufficient scale (and what the reasons for this were), and when it stemmed from the unsatisfactory “systemic quality” of the project(s).

Notwithstanding these methodological remarks, I consider the substantive findings of the study to be highly interesting and useful from the policy point of view. I believe special attention should be paid to the following considerations:

- Strategic foreign investors enhance the TI of the projects in which they participate;
- Financial-cum-industrial conglomerates pose dangers to the transition process;
- Bank privatisations produce high systemic spillover effects;
- Economic restructuring (and reform) promotes environmental improvement;
- The institutional and economic framework generated by more advanced transition tends to produce a higher TI than in cases where transition is less advanced. This points to the existence of virtuous circles in the process of transformation, indirectly confirming the previous finding that more rapid and sustained market-oriented reforms are likely to produce better results than slow ones;
- The latter finding underscores the importance of projects aimed at introducing and improving the relevant commercial and legal environment for economic activity. Indeed, this is key to economic success. And, as is rightly pointed out in the report, these efforts should not stop at drafting legislation, but should focus on implementation, i.e., the development of the appropriate institutions. This is the most difficult and crucial part of the whole endeavour, one where issues concerning the nature of the domestic political regime cannot be avoided, and indeed must be tackled.

The *Transition Impact Retrospective* contributes to a better understanding of one of the most fundamental transformations in modern history, and illuminates the role of the EBRD in this process. It deserves to be widely read.

Introduction

Article 1 of the Agreement Establishing the EBRD states that the purpose of the Bank is to:

“foster the transition towards open market-oriented economies and to promote private and entrepreneurial initiative in the Central and Eastern European countries committed to and applying the principles of multiparty democracy, pluralism and market economics”.

As a result, the operations of the EBRD are guided by a general understanding of what constitutes transition towards open markets and pluralistic democratic systems. At the heart of the Bank’s activity is a conviction that the promotion of efficient private investment and entrepreneurial initiative in open and competitive markets is what drives the improvement in living standards in all economies. Given its absence for many decades, this is particularly so in formerly centrally planned economies. This *Transition Impact Retrospective* (TIR) is an attempt to assess the performance of the EBRD with respect to its transition mandate. The focus on transition means that other aspects of the EBRD’s strategy and operations – such as the commercial success of projects – are touched upon only where they are relevant for transition.

The TIR tries to identify the successes as well as the shortcomings the EBRD has had since it began investing in the region. It does this by relating the Bank’s activities to specific conditions in countries and sectors. It tries to measure the EBRD’s *transition impact*, defined as the Bank’s contribution to the introduction, strengthening and institutionalising of market processes in its 27 countries of operations. In doing this, the TIR abstracts

from projects’ financial returns (which measure projects’ private costs and benefits) and from social returns captured in standard cost benefit analysis. It builds on a methodology developed within the EBRD, published internally, and reflected in the Bank’s annual *Transition Report*.

The first decade of transition has seen progress in most countries in macro-economic stabilisation, price and trade liberalisation, and privatisation of state assets. Institutional reforms to support the emergence of market finance, commercialise public infrastructure and strengthen public administration, including the judiciary, have made slower progress, although the variation is large across the region. The creation of markets and private property has opened new opportunities for the people of the region to take the initiative, respond to incentives and create growth. Where democratisation has accompanied economic liberalisation, people now have a say not just in how to earn their living and spend their income, but also in how to be governed.

The EBRD continuously monitors and assesses progress in transition – most prominently in its *Transition Reports* – and periodically adjusts its operational strategy based on its understanding of transition. In the context of this evolving operational environment, it is believed that the Bank can currently have most impact on transition if it focuses on the following operational priorities.¹

- Promoting a sound financial sector that commands the confidence of domestic and foreign investors, facilitates transactions, and intermediates effectively between savers and investors.

- Supporting business start-ups and growth of small and medium-sized enterprises (SMEs).
- Financing market-based and customer-oriented infrastructure.
- Supporting the restructuring of potentially viable, large enterprises.

The EBRD recognises that major economic and social upheavals have accompanied structural change across the region. In the more advanced transition economies, social safety nets provided by the government were already in place or have been created to mitigate the negative consequences of transition for the most vulnerable. Further east, it has proved more difficult to address the social dislocations, due to the weaker (fiscal and administrative) capacity of the state, weaker governance and the associated poor investment climate, which limits the emergence of private sector employment alternatives.

Within the context of its mandate, the EBRD is increasingly proactive in trying to mitigate the hardship that is associated with economic reforms. SME finance is one area where the Bank’s operations can directly relieve poverty and social dislocation. Through its Russia Small Business Fund (RSBF), for instance, the Bank has created over 600,000 jobs – many clients of the RSBF have been women, and many have come from regions of Russia that have not benefited from the investment “boom” around Moscow and the other major cities. Building upon the success of the RSBF, the EBRD has set up similar schemes in Bosnia and Herzegovina, Georgia, Kazakhstan and Ukraine.

¹ These are elaborated in the EBRD’s strategy document *“Moving Transition Forward: Operational Priorities for the Medium Term”*, BDS99-24.

One aspect of reform that can be particularly painful is the need for price liberalisation, and particularly to adjust prices to cover costs in infrastructure projects. This is especially so in the power and municipal sectors, where tariff increases required as part of commercialisation and privatisation raise concerns about affordability. To meet these concerns, the EBRD assesses, as part of project appraisal, the affordability of tariff adjustments for low-income households and, if necessary, conducts policy dialogue with the relevant authorities and other international financial institutions to ensure that there is adequate social protection in place.

While the need to address the short-term social impacts of projects is essential, the focus of the TIR is on the EBRD's longer-term transition impact, that is, on the Bank's contribution to market development. For example, the TIR assesses the extent to which the Bank has facilitated the development of sustainable lending capacity to SMEs, or supported private entry within a context of effective regulation and/or liberalisation in infrastructure, or helped heavy industry to restructure and gain a competitive market position. Progress in this respect underpins social welfare in the longer term.

The methodology employed (see Chapter 1) assesses the EBRD's contribution to transition through its impact on capital flows to the region. The TIR analyses the role of the Bank in providing, or stimulating, higher *levels of capital flows*, and draws on earlier evaluations within the

EBRD of the *transition impact of the Bank's investment projects*. It complements this project-based analysis with an assessment of the EBRD's transition impact at the sector and country levels. Separate sections of the TIR look at the Bank's contribution to legal and environmental transition. The evaluations are based on consensus judgements, drawing primarily on views within the EBRD, specifically from the Banking Department (including Resident Offices), Office of the Chief Economist, Project Evaluation Department, Environmental Appraisal Unit and the Legal Transition Team.

The main conclusions of the TIR are:

- The EBRD has been an important contributor to foreign direct investment (FDI), particularly in South-Eastern Europe, the Southern CIS and Russia, but less important in the Western CIS where FDI as a whole has been low.² The role of the Bank has become relatively less important over time in the advanced transition countries, as commercial finance has become increasingly available.
- Over two-thirds of projects scored in the highest transition impact range when rated by the EBRD's Project Evaluation Department. Most investment projects have to be commercially viable to achieve their transition impact. However, financial success alone does not ensure that a project delivers high transition impact. The Bank has been more successful when it has worked with foreign strategic investors, though

there are instances where it has succeeded with local investors and/or management. Good transition impact was also achieved in public sector infrastructure projects when the Bank worked closely with governments on market frameworks and regulation.

- The EBRD's impact has varied by sector and country. As a rule, the Bank has been more successful in advancing transition (i.e., has achieved higher sector transition impact scores), at the sector level, in countries with a more advanced reform environment, although there are some notable exceptions. This is consistent with the findings at project level. However, project evaluations show that other factors (such as the presence of a strategic investor) are even more important determinants of project-level transition impact.
- The Bank has been successful in enhancing the commercial legal framework across the region. This includes improvements in bankruptcy law, concessions, corporate governance, financial market regulation, secured transactions, telecommunications, and arbitration in a diverse range of countries including Azerbaijan, Russia, Bosnia and Herzegovina, Hungary, Lithuania, and Poland.
- Many of the EBRD's projects have had specific environmental objectives. The Bank has been particularly successful in improving the environment in advanced transition countries, in the municipal sector and heavily polluting industrial sectors generally.

² The TIR uses the following regional definitions: Central Europe and Baltic States (advanced transition countries): Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia. South-Eastern Europe: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Romania. Western CIS: Belarus, Moldova, Ukraine. Southern CIS: Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Uzbekistan. The CIS is the Commonwealth of Independent States.

Analytical framework for the TIR

The EBRD has developed tools for assessing the transition impact of individual projects in the context of project appraisal and post-project evaluation. To assess the Bank's overall contribution, a link must be established between projects and indicators of transition progress at a more aggregated level.

The TIR adopts an approach that identifies five basic elements, each emphasising a different facet of transition:

1. an assessment of the EBRD's contribution to capital flows into the region;
2. project-level assessment, based on the evaluations of transition impact by the Project Evaluation Department (PED);
3. sector-level assessment, based on a "mapping" of EBRD projects into transition progress in different sectors;
4. an analysis of the Bank's contribution to the legal transition;
5. results of PED evaluations of the environmental impact of Bank projects.

The first element is straightforward and quantifies equity and non-equity capital flows directly associated with EBRD projects.

The second element is less straightforward, and requires some explanation.

Most benefits and costs of a project show up in its cash flow. If buyers are willing to pay a certain sum for a product, and it costs less in resources to produce it, the project adds value. In addition, there are also effects that do not enter the owner's private arithmetic. Input subsidisation, output market protection, or the transfer of an efficient and easily replicable management technique are all examples of factors that can drive a wedge between the private and the "social" balance of project inflows and outflows.

The technique that economics has developed for identifying such wedges is cost-benefit analysis (CBA). However, CBA is not well equipped to handle two sets of issues which are central to the transition process: radical structural change and learning of market-oriented methods and behaviour. Thus, for example, there are time-honoured methods for adjusting for the distortions created by subsidies and import barriers – distorted prices are replaced by opportunity costs to move from private to economic rates of return. What is much more complicated to think through is the benefit of, for example, the transfer of a management technique which may be well-established in market economies but relatively unknown in eastern Europe, or of the establishment of actors who radically improve the functioning of capital markets. In principle, these effects might be "priced" by estimating avoided transaction costs or the differential growth that results from them. In practice, it is impossible or disproportionately onerous to do so.

In project appraisal, those factors driving a wedge between financial and economic returns that can be quantified with relative ease should find their way into the calculation of the economic rate of return of a project – while recognising that its limited scope means that certain, perhaps important, costs and benefits of the project may not be reflected. Those project benefits and costs that are not amenable to quantification but that have a bearing on the process of change towards a market-based economy have conventionally been classified as "transition impact" in EBRD project documents.

Broadly speaking, the transition concerns bringing economic interactions onto a market basis and promoting private and entrepreneurial initiative. Accordingly, the EBRD has identified three dimensions in the analysis of transition impact:

- a) the creation, expansion and improvement of markets;
- b) the establishment and strengthening of institutions, laws and policies that support the market (including private ownership);
- c) the adoption of behaviour patterns and skills that have a market perspective.

These categories are generic in the sense that they apply to projects in all sectors. For purposes of project appraisal, sector-specific checklists identifying transition objectives have been developed. The power sector transition impact checklist is provided as an example in Box 1.1. Other sector checklists are presented in a companion paper to the TIR (published on the EBRD's Web site: www.ebrd.com).

The transition impact of a project then depends on three dimensions:

- a) country and sector context (current stage of transition and sector reform);
- b) related transition challenges (country or sector reform objectives); and
- c) the way that these challenges are addressed by project selection, design and implementation.

The third element of the TIR assesses the EBRD's transition impact at the sector rather than the project level. The rationale for taking a sectoral approach, as well as a project-level approach, is that there may be synergistic effects between projects. For example, the Bank may be more successful when it reaches a critical mass in a sector because it has more leverage as regards policy dialogue and related reform. The approach taken here is to measure transition impact against an "event line". Event lines are stylised sequences of changes that we observe as sectors move from their centrally planned past to a functioning market model.³

³ The use of event lines does not imply that transition is a linear movement along a defined path, and with a single, well-defined end.

Box 1.1

Transition challenges and Bank response in the power sector

Transition challenge	Bank response
Energy industry operates as part of a government department.	Bank finance of corporatisation process, corporatised company investment and institutional development (project implementation capacity).
Management approach geared towards engineering as opposed to business. Political interference in management decision making.	Bank sponsored introduction of management information systems, international accounting standards, procurement practices, long-term business planning.
Tariffs below long-run cost of supply, cross subsidy from large to residential consumers, barter settlement of bills and non-payment problems.	Bank-led tariff increases, subject to affordability constraints. Tariff rebalancing between large and domestic customers. Bank finance of efficiency improving investment to mitigate the extent of necessary price increase. Programme for increased cash collection in conjunction with Bank-financed project. Bank support for changes in the legal framework to allow cutting off of non-paying customers. Bank finance of improved metering and billing mechanisms. Bank involvement in distribution company privatisation and finance of privatised distribution companies.
Absence of a well functioning regulatory regime.	Bank support of regulatory development. Bank finance of companies operating within newly developed regulatory framework.
Monolithic industry structure: generation, transmission, distribution and supply operate as a fully integrated entity.	Bank role catalysing restructuring (vertical and horizontal unbundling) through policy dialogue. Support of institutional development, for example, creation of subsidiaries, and institutional development within subsidiaries (business planning etc.). Finance of company within separated structure.
Absence of the private sector and competitive pressure.	Finance of privatisation process (legal, contractual and regulatory framework, bidding process [invitation to bid, information, bidding, negotiation]) and privatised (divested, concessioned) distribution and generation companies.

Projects are related to appropriate points on this event line, and judgements made on the extent to which the Bank's projects actually drove movement along the event line in individual countries. A detailed description of the methodology and results of this sectoral transition impact analysis is contained in the companion paper to the TIR. Chapter 3 of the TIR analyses these results with a view to explaining where and why the Bank has been successful at the sector level.

The fourth element of the TIR adopts the same approach as the third element, but focuses on countries' legal systems. Using generic milestones for legal reform (for example, development of a framework for bankruptcy, securities, concessions, etc.) it assesses the extent to which the EBRD has been successful in helping countries to reach such milestones.

The fifth element of the TIR assesses the performance of the EBRD with respect to its environmental mandate, which directs the Bank to promote markets and entrepreneurship in a context of environmentally sound and sustainable development. Fostering sustainable development, like promoting transition, requires a combination of policy and project-level interventions, to develop an adequate institutional framework and introduce good environmental practice through concrete applications. In keeping with its comparative advantage, the EBRD's emphasis has been on the project level. The evaluation of the EBRD's environmental contribution therefore focuses on the Bank's success in demonstrating good practice and the compliance of its projects with international environmental standards.

All five elements in principle require a comparison between the actual development of the transition in the region and how it would have looked without the EBRD (the "counterfactual"). In practice, it would clearly be difficult to say how the region would have developed if the EBRD had not existed. What we can say, however, is that the Bank has been additional. Additionality refers to the EBRD's influence upon a project. A project is additional if it would not exist without EBRD participation, or would be materially different in terms of its design and implementation. Additionality is a key variable in the process of project appraisal at the EBRD, and a necessary condition for project approval.

Transition Impact Retrospective

The TIR measures the EBRD's transition impact against a "no project" situation. The TIR thus provides an upper bound for the Bank's influence in the region. To the extent that the EBRD has been additional, its projects would not have gone ahead without the Bank, or would have existed in a different form and had a lower transition impact. The TIR measures adequately the Bank's transition impact in the first case, but overestimates the Bank's contribution in the second. For a more accurate picture, it would be necessary to subtract from the TIR assessments the (smaller) transition impact of projects that would have gone ahead without the EBRD. Such a calculation would not be practical, and is not attempted in the TIR.

The TIR does not focus on the financial success of projects. To the extent that financial success is a necessary condition for transition impact, it may be inferred that projects with high transition impact have performed well financially. But there may also be projects rated low on transition grounds, which have nevertheless performed well financially. Furthermore, the TIR does not provide a cost-benefit analysis of the EBRD's activities (because, as discussed above, this cannot capture transition-related project innovations). By focusing exclusively on transition impact, the TIR does not do justice to the total economic benefit associated with the EBRD's activities.

The EBRD's role in mobilising capital for the transition

Effective transition requires massive improvements in the quality and allocation of capital assets. Because of limited domestic savings in the early years of the transition, foreign capital inflows have played a vital part in financing investment. Foreign capital, especially in the form of strategic investment, has served as a channel for transferring market-oriented knowledge, management skills and methods of good corporate governance. There is growing evidence that foreign direct investment (FDI) has contributed to transition and growth. The rank correlation coefficient between cumulative FDI per capita in the region and the EBRD's transition indicators is 0.9.⁴

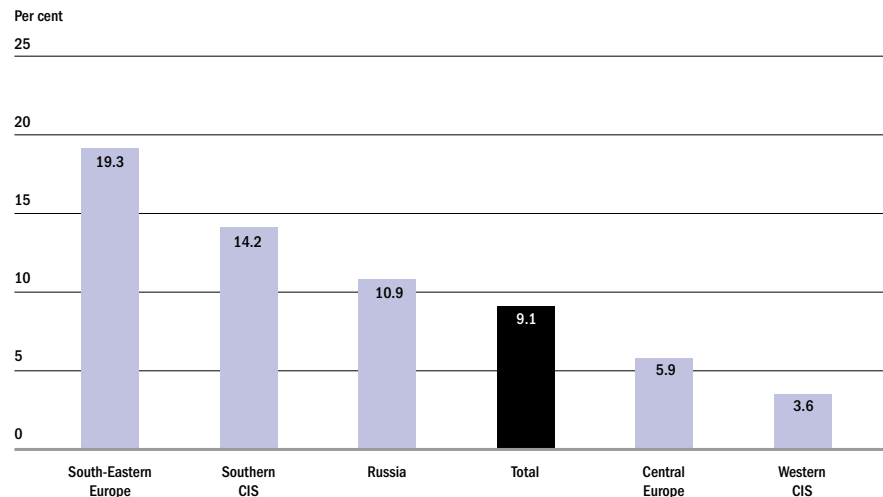
Foreign direct investment

A first indicator of the EBRD's contribution to transition is its role in mobilising foreign investment capital. The Bank is one of the largest direct investors in the transition economies (FDI is defined as investment that provides a measure of long-term control, usually 10 per cent or more of a company's capital). By the end of 2000, the Bank had been associated with almost US\$ 12 billion of FDI (including the capital invested by its partners).⁵ While it is difficult to establish causality, it is highly likely that a significant part of this investment would have been scaled down, postponed, or abandoned without the EBRD's participation. US\$ 12 billion represents over 9 per cent of cumulative FDI into the transition economies over the period 1991-2000. The share surpassed 15 per cent each year in the early years of transition before 1995, and again in 1998. A share of 6 per cent is estimated for 2000.

There is substantial variation across countries and regions in the foreign investment associated with the EBRD (Chart 2.1). The share of FDI into the region associated with the EBRD has declined since 1996, due both to the massive increase

Chart 2.1

Share of EBRD-associated FDI



of FDI into central Europe and to the EBRD policy of investing only where it does not displace private project finance (additionality). While the overall share for 2000 is forecast to be only 1.8 per cent (excluding investment funds), there are large variations among regions and stage of transition.⁶ At a cumulative level of almost 20 per cent, the Bank's FDI-share in South-Eastern Europe was more than five times higher than in the Western CIS (Belarus, Moldova and Ukraine). And while it has increased for Russia and the Southern CIS in recent years, it has declined in the Western CIS since 1998. This is due partly to the paucity of large, individual FDI transactions in these countries during the 1990s – in particular in infrastructure sectors – which dominate the totals in other regions.

Total EBRD financing

The EBRD has invested US\$ 16 billion in the region. In addition to this and to FDI associated with its projects, the EBRD has contributed to capital flows through its commercial syndications programme and the mobilisation of official co-financing. The total value of capital flows associated with EBRD projects was in excess

of US\$ 50 billion at the end of 2000. While this represents only a small share of capital flows into the transition economies, its importance at the longer maturity end of the market is far more significant. Data on total EBRD financing, and mobilisation, by sector is presented in Annex 1.

Indirect value of EBRD participation

A third contribution, still harder to estimate, is the improved access to external funding and perhaps an increase in capital flows as a result of EBRD projects. At the project level, there is circumstantial evidence – partly in evaluation reports – that the upgrading of information systems, skill levels and corporate governance, as well as the stamp of approval of an EBRD operation *per se*, have enabled EBRD clients to diversify and expand their financing sources. This is particularly evident in projects that support listings on foreign or domestic securities markets, in first-time syndications of bank-to-bank loans, and in trade guarantee lines. Examples are provided in the companion paper to the TIR. At the country level, the EBRD has also helped to facilitate private capital flows through its efforts to create an investment climate that is conducive to FDI.

⁴ Excluding the oil and gas economies of Azerbaijan, Kazakhstan and Turkmenistan. The simple average of the eight transition indicators in Table 2.1 of the *Transition Report* was used.

⁵ This includes direct equity investments supported by EBRD loans as well as EBRD equity. Note that, at an estimated US\$100,000 per workplace, this investment would have created or saved 120,000 jobs.

⁶ In four countries the share exceeds 25% (Kyrgyzstan, Azerbaijan, Georgia and Romania). In another five, it is at or below 3% (Armenia, Belarus, Kazakhstan, Turkmenistan and Czech Republic).

Synopsis of PED project evaluations



3.1. Overview

By early 2001, the EBRD had completed investments in 308 projects. The Bank's independent Project Evaluation Department (PED) has assessed 239, or 72 per cent, of them.⁷ PED evaluations thus provide a fairly representative picture of the Bank's transition impact at the project level. As stated in Chapter 1, project transition impact measures the degree to which a project succeeded in advancing transition, given a country's stage in transition and reform environment. It is measured on a scale of: high, medium, low, none, negative.

Based on the performance of the projects evaluated to date, PED concludes that the Bank has been successful in selecting projects that promote transition. Seventy-four per cent of the evaluated projects were given medium to high ratings for transition impact. This is a better result than the evaluated financial and overall project performance where scores are typically more modest. Still, one in every six or seven evaluated projects had no or a negative transition impact. Many of them were high profile failures in general industry or the banking sector that resulted in poor demonstration of corporate governance standards, despite the Bank's efforts.

Overall, the likelihood of a good transition impact rating depended on the following factors:

- Presence of a strategic investor. Working together with a strategic investor significantly increased the likelihood of a medium to high transition rating.
- Sectoral characteristics. In some sectors the Bank has found it easier than in others to achieve transition impact. Projects in infrastructure obtained the highest average ratings and general industry projects the lowest, with financial institutions scoring in between the first two broad sectors.
- Access to the government. Transition impact was rated higher on average for public sector infrastructure operations, not least because of the leverage the Bank enjoyed in these projects to affect system reform.
- Reform environment. The EBRD has been more successful in a conducive market-reform environment. The likelihood that a project has a good transition impact is positively associated with a country's stage in transition at the time of approval (measured as the country transition rating in the Bank's *Transition Report*).⁸

Transition impact ratings did not depend, on the other hand, on the size of the investments and the form of financing (loan or equity). Another recurrent lesson from the project evaluations is that concrete, in-house expertise makes project design and appraisal by the EBRD more effective and helps to generate transition impact. The Bank has been more successful in sectors where it has in-house expertise, particularly in the case of equity investments. The following sections look at these patterns in more detail. Annex 2 provides a statistical analysis of rating patterns.

3.2. Transition impact ratings, by region

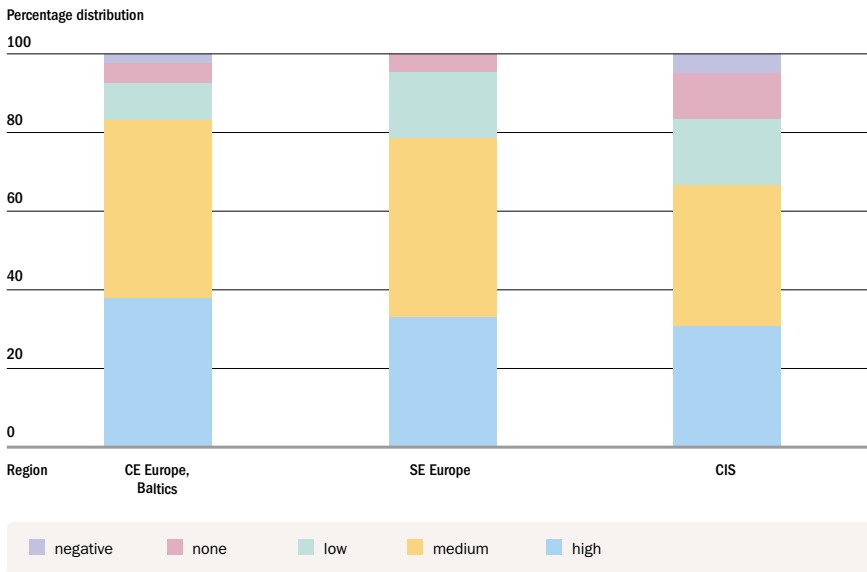
Chart 3.1 shows the percentage of projects that earned the two highest transition impact ratings in different regions. The chart shows that 83 per cent of projects in Central Europe and the Baltic States obtained the two highest transition impact ratings. It should be noted that many projects there were implemented when these countries were still at early or intermediate transition stages. About 78 per cent of projects implemented in South-Eastern Europe scored medium or high on transition impact. In the CIS, only 67 per cent drew these scores.

⁷ PED is in a separate Vice Presidency, independent of the Banking Department, within the EBRD. It is responsible for assessing projects, after completion, in terms of their compliance with the various elements of the Bank's mandate. In this sense it plays an accountability function between shareholders and management. It also has a mandate to formulate lessons learned from projects to improve the quality of future investment projects. Project evaluations are typically carried out one or two years after investments have been completed, late enough to verify the early achievements and for a more informed assessment of further transition impact potential than at approval.

⁸ The Bank assesses progress in transition in each country of operations in a set of transition indicators that are published annually in the *Transition Report*. Eight transition indicators are distinguished that cover enterprise privatisation and reform, trade and market reform, and financial institutions. Separate transition indicators are also produced for legal transition and transition in the infrastructure sector.

Chart 3.1

Post-evaluation transition ratings by region



The more detailed individual project evaluations confirm that favourable reform conditions and investment climates are important for project success. They provide an indication of the constraints encountered by private sector projects in countries with imperfect legislation, poor regulation, corruption, widespread barter, and lack of good governance standards for firms and financial markets. This point was highlighted in the aftermath of the crisis in Russia, where the operating environment declined, private projects (including in the banking sector) ran into difficulties, and the share of projects in the portfolio rating low on transition impact increased.

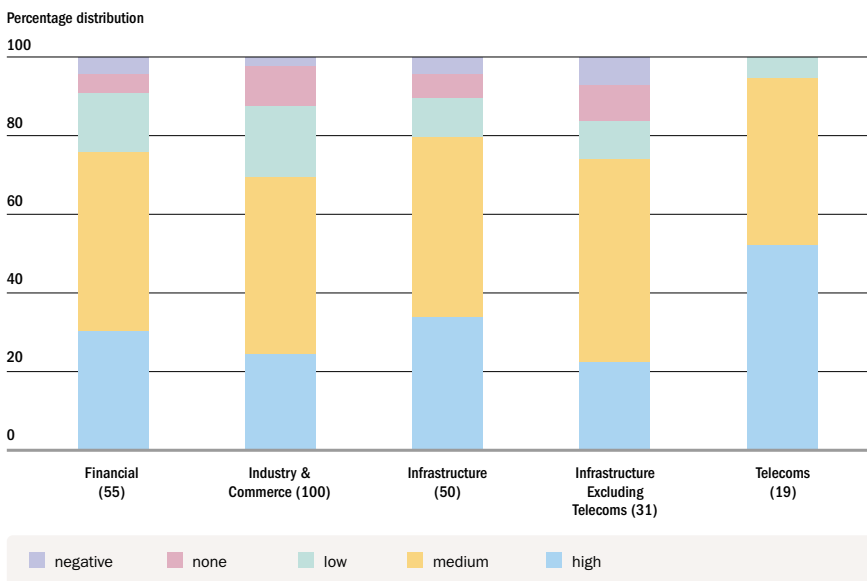
3.3. The sectoral perspective⁹

Infrastructure projects scored well on transition impact

As Chart 3.2 shows, the 50 evaluated infrastructure projects have scored particularly well on transition impact, especially when they involved intensive policy dialogue on institutional, regulatory and legal reform. The telecommunications sector (which accounts for the highest share of infrastructure projects evaluated by PED) provides a case in point. In the telecoms sector, the EBRD has focused on: network development and commercialisation (Bulgaria, Kazakhstan, Kyrgyzstan), privatisation to strategic investors (with OTE in Romania, and Ameritech/Deutsche Telekom in Hungary), development of the regulatory framework (Belarus, Bosnia and Herzegovina, Bulgaria, Latvia, Hungary), and new entry in value-added services (Romania, Hungary, Poland, Latvia, Russia, Croatia). Of 19 telecoms projects, 18 were rated medium or high on transition impact grounds.

Chart 3.2

Post-evaluation transition ratings by sector



These results suggest that finding high transition-impact projects that meet sound banking principles was less difficult in the countries that have pursued reform most vigorously. Statistical analysis confirms that a favourable environment increases the likelihood of a good transition impact (see Annex 2). However, the analysis also

indicates that the reform environment is less important in explaining transition impact than other factors, such as the presence of a strategic foreign investor in private sector projects or access to the government for suitably structured and conditioned projects in infrastructure.

⁹ Annex 1 presents more detailed and disaggregated results.

General industry projects obtained lower transition impact ratings

The EBRD's transition impact in commercial and industrial projects crucially depended on the presence of a foreign, strategic investor. Strategic foreign investors are a key determinant of transition impact (see Annex 2). They play a particularly important role when there is a need for deep restructuring. Projects with foreign sponsors typically achieved a medium or high transition impact rating, especially when the sponsor was a leading global industry player (e.g. Chokoladovny confectionery in the Czech Republic, Kruszwicka edible oils and Fiat in Poland, Ispat-Karmet steel in Kazakhstan).

On the whole, projects with exclusively domestic sponsors were less successful. They achieved a medium or high rating only half as often as did projects with foreign sponsors. Restructuring of enterprises with local sponsors has been impeded by insider (management) control, government influence and social constraints (for example, a large automotive project in Russia, a former state agribusiness complex and a steel group in central Europe). Projects with local sponsors and managers have also typically been unable to meet the challenges of a fast-changing operating environment, and have enjoyed only limited commercial success in emerging competitive markets. (An exception is Pliva pharmaceuticals in Croatia.) Close EBRD involvement, through nomination of corporate board members and collaboration with local managers, was generally not sufficient to overcome these problems (as in a building materials project and a steel conglomerate, both in central Europe). In complex restructuring projects with only domestic sponsors, low transition impact has also been associated with poor financial performance, and in "single company towns" deep restructuring faced social constraints (as in large automotive projects).

There are exceptions to these general findings – particularly in pharmaceuticals, chemicals and some natural resources projects – in cases where locally managed companies are competitive in world markets. More generally, transition impact was enhanced in projects with companies that have a strong comparative advantage. These industries include forest-related ventures (such as wood panelling), beverages, cement and other building materials. By contrast, for the complex restructuring of old "combinates" it was generally preferable to give control to new strategic investors with turnaround experience under market conditions.

Financial sector operations scored well on transition impact

Financial sector projects tended to have a higher assigned transition impact rating than general industry projects, although lower than those for infrastructure investments which could more often be conditioned to institutional reform. Low transition scores were most frequent in banking sector operations when privatisation of dominant state banks was slow. The same pattern emerged when lending to financial-industrial groups (FIGs) became prominent. In both situations, the environment was not conducive to the evolution of banking competition, and reflected regulatory capture and inadequate sectoral reform. The EBRD has been less successful in unreformed environments and where reform on paper was not followed up by adequate implementation. Conflicting objectives were a particular problem in some unreformed sectors. For example, the EBRD has had difficulty improving transparency of project banks operating in unreformed markets, where this might involve a loss of competitive advantage for badly regulated and poorly governed banks. This applies even in situations where the EBRD has been represented either at advisory council or board level, as for example in the former Tokobank in Russia.

Generally, the EBRD has only worked with state-owned banks when a strong commitment to reform has been signalled. Those were in countries where banking reform has moved forward: capital adequacy has moved towards international standards; International Auditing Standard (IAS) accounts have been introduced, banks have been or are to be privatised. There the EBRD has worked with local and foreign sponsors to support consolidation and enhanced competition (for example, Banka Austria Creditanstalt in Croatia, Tatra Banka in the Slovak Republic, Vilnius Banka in Lithuania, SKB Banka in Slovenia).

The EBRD has also contributed towards improved standards of business practice and corporate governance, particularly in more reformed contexts where stock market listing and credit rating by commercial agencies is under way (for example, Hansapank in Estonia, Varazdinska Bank in Croatia). Furthermore, the EBRD as a co-investor has tested both bankruptcy (Tokobank in Russia) and merger procedures (Hansapank in Estonia, Varazdinska Bank in Croatia). This should not be overstated, however. Evaluation reports suggest that the EBRD has had only a limited impact on improving corporate governance in the financial sector.

Capital markets remain thin in most of the EBRD's countries of operations, and deepening of the capacity for financial intermediation remains a key transition challenge.

3.4. Technical cooperation strengthens transition impact

The project evaluation reports demonstrate that well-designed technical cooperation (TC) support can strengthen the transition impact of investment projects. This applies both to public and private sector projects. A recurrent lesson from the evaluation of TC operations is that the forms of contracting and funding that enhance client "ownership" make a significant difference to the effectiveness of TC funding.

Transition impact at the sector level

4.1 Overview

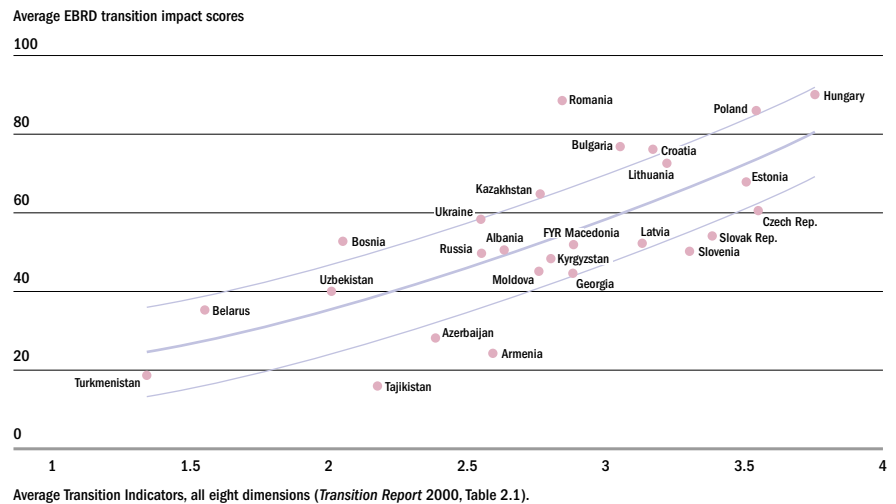
Exclusive focus on the evaluation of individual projects can miss synergistic and scale effects associated with sustained investment support in a sector, involving many independent projects. A sector-level assessment was undertaken to examine the broader, sector-level transition impact of Bank financing. The question asked is: to what extent did the EBRD, through projects and other activities, influence sectoral transition?

Progress in transition was measured as the achievement of a set of specific sectoral reform benchmarks. Detailed reform benchmarks (“transition events”) were defined for the 12 sectors that constitute the main areas of activity of the EBRD.¹⁰ For example, in the power sector reform benchmarks would include corporatisation and unbundling, followed by improvements in the regulatory framework, the introduction of the private sector and eventually market liberalisation. In a second step, EBRD projects were screened for components that may contribute to the achievement of the benchmarks: for example, covenants on the separation of accounts that prepare the ground for the unbundling of power utilities. Lastly, a judgement was made whether: (i) the projects had the intended transition impact; (ii) EBRD involvement was critical to secure this particular transition impact; and (iii) the change achieved contributed to progress along the transition “event line” for the sector as a whole.

The sectoral impact in each country was classified as none (for example, no projects), minimal, moderate, significant

Chart 4.1

Transition Indicators (TR2000) and EBRD Transition Impact



and very significant. Judgements were made on the basis of PED reports, interviews with Banking teams and assessments by country and sector economists. The criteria for the classifications and a more detailed description of the methodology, together with sector benchmarks, criteria and judgements (with validations), are contained in the companion paper to the TIR.

4.2 Summary results¹¹

Absolute scores

Results indicate that, on average across countries, the EBRD has had the most significant impact overall in the banking sectors of the region, followed by SMEs and the power sector. Transition impact in the energy efficiency sector (narrowly defined),¹² natural resources, non-bank financial institutions, and property and tourism has been relatively small. This

result is partly explained by the small number of countries in which the Bank has been active in these sectors.

Chart 4.1 presents weighted averages of sector transition impact scores for each country. These are plotted against the country transition indicators taken from the *Transition Report 2000*.¹³ On a scale of 0 (no impact) to 4 (very significant impact) the EBRD’s activities in Hungary, Poland and Romania score best overall, while those in Armenia, Tajikistan and Turkmenistan are judged to have had the weakest impact.

The plot indicates that higher transition impact scores at the sector level (aggregated to the country level) are associated with a higher-quality business environment, as represented here by the country-level transition indicators. The regression line in the chart is clearly upward sloping.

¹⁰ The 12 sectors and the distribution of commitments across them are as follows:

Financial Institutions (30%)	Industry and Commerce (40%)	Infrastructure (30%)
<ul style="list-style-type: none"> • Banking • Non-bank FIs • SMEs 	<ul style="list-style-type: none"> • Agribusiness • General Industry • Natural Resources • Property and Tourism • Telecoms 	<ul style="list-style-type: none"> • Energy Efficiency • Municipal/Environment • Power • Transport

¹¹ Detailed results by country and sector (312 separate scores) are presented in the companion document to the TIR.

¹² Further contributions to energy efficiency, which have probably outweighed those of projects from the EBRD Energy Efficiency Team, have obviously been associated with power sector projects and certain operations in general industry.

¹³ Unweighted average of the eight transition indicators relating to enterprises, markets and the financial sector.

Transition Impact Retrospective

Although it is difficult to establish cause and effect – the EBRD’s transition impact over the past ten years may have influenced the 2000 country transition indicators – it appears that the Bank has been more effective in achieving transition goals in environments that had undergone market-oriented reform.

This result is consistent with the idea of “market selection,” which suggests that the most successful strategy for market transformation is the selected support of market leaders to foster commercial success. The chances of commercial success arguably increase with progress in transition and associated improvements in the business environment. This is not to argue that the achievement of commercial success in higher transition countries is a foregone conclusion. To repeat Chapter 1 of the TIR, the EBRD has aimed to ensure that it is additional in the projects in which it participates. In other words, the Bank has continued to reduce the commercial risks associated with projects, bringing projects into being that would otherwise not go ahead, or enhancing projects that might go ahead without EBRD participation.

Relative scores

Tables 4.1–4.4 are designed to avoid some of the pitfalls of absolute scores by grouping countries both in accordance with their relative level of transition and the relative strength of the EBRD’s sector impact.¹⁴ This approach goes some way towards separating country from project management and/or strategy issues in explaining the Bank’s impact. The middle range groups results within 20 per cent either side of the level considered “normal” for the particular stage of transition (i.e., the one predicted by the regression line). Those above/below this band indicate a particularly strong/weak impact. A first result, which appears throughout the tables (though less markedly for industry and commerce), is the clustering of countries within the central band. This is consistent with the close association between impact and environment discussed above. However, there are also important exceptions.

Table 4.1

Overall transition indicators/impact

Transition indicator	(Impact: Deviation from expected range)		
	Better than expected	Within range	Less than expected
High	Croatia Poland	Hungary Estonia Lithuania Latvia	Czech Republic Slovak Republic Slovenia
Medium	Bulgaria Kazakhstan Romania	Albania FYR Macedonia Georgia Kyrgyzstan Moldova Russia Ukraine	Armenia
Low	Bosnia and Herzegovina	Uzbekistan Belarus Turkmenistan	Azerbaijan Tajikistan

Table 4.2

Financial sector transition indicators/impact

(Financial sector transition indicator)	(Impact: Deviation from expected range)		
	Better than expected	Within range	Less than expected
High	Lithuania	Hungary Poland Estonia Czech Republic	Slovenia
Medium	Bulgaria	Croatia Latvia FYR Macedonia Kazakhstan Kyrgyzstan Moldova Romania Slovak Republic Ukraine	Armenia
Low	Albania Bosnia and Herzegovina	Uzbekistan Russia Belarus Georgia Tajikistan	Azerbaijan Turkmenistan

¹⁴ Country transition indicators in each case are those most relevant for the respective sector grouping. In Table 4.1 overall averages for all transition indicators are used, as in Chart 4.1. In Table 4.2 those transition indicators referring to the financial sectors are used (Table 2.1 of the *Transition Report 2000*). In Table 4.3 it is the transition indicators relating to enterprises and markets. Finally, for infrastructure (Table 4.4) averages of the indicators of progress in transition in infrastructure, prepared for the *Transition Report 1999*, were utilised.

Table 4.3

Industry and commerce transition indicators/impact

(Enterprises and markets transition indicator)	(Impact: Deviation from expected range)		
	Better than expected	Within range	Less than expected
High	Hungary Poland	Slovak Republic Estonia	Czech Republic Slovenia
Medium	Romania Croatia Kazakhstan Russia Ukraine	Bulgaria Lithuania Kyrgyzstan FYR Macedonia Albania	Georgia Latvia Moldova Armenia
Low		Uzbekistan Turkmenistan Bosnia and Herzegovina	Azerbaijan Belarus Tajikistan

One interpretation of Table 4.1 is that, in the countries in the left-hand column (Bosnia and Herzegovina, Bulgaria, Croatia, Kazakhstan, Poland and Romania) the EBRD has been particularly successful, taking account of the limitations of the operating environment. In the right-hand column, the EBRD has been less successful in pursuing its transition mandate than the operational environment (as measured by transition indicator¹⁵) might have permitted. This may reflect concerns with democracy and human rights issues that have led to difficulties forging relationships with certain countries. It may also reflect problems associated with non-performing projects in small countries that reduce opportunities for further participation.

Table 4.4

Infrastructure transition indicators/impact

(Infrastructure transition indicator)	(Impact: Deviation from expected range)		
	Better than expected	Within range	Less than expected
High	Romania	Poland Estonia Latvia Hungary Slovenia	
Medium	Bulgaria	Lithuania Croatia Moldova Russia Kazakhstan	Slovak Republic Czech Republic Georgia Armenia
Low	Ukraine Uzbekistan	Azerbaijan Belarus Bosnia and Herzegovina FYR Macedonia Kyrgyzstan Albania	Tajikistan Turkmenistan

These conclusions are sharpened in a sectoral perspective, shown in Tables 4.2–4.4. As in Table 4.1, these tables present the EBRD's transition impact in broad sectors plotted against a sector-specific measure of transition progress in different countries.¹⁶

¹⁵ The same result holds if country risk ratings are used as the proxy for operational environment.

¹⁶ Countries contained within a band of 20% of the predicted level are listed in the central column.

In the financial sector, the Bank's impact has been above expectations where it has played an instrumental role in the early privatisation of state banks (Lithuania, Bulgaria) or has been crucial in the creation of the first private banks (Albania, Bosnia and Herzegovina). An important aspect of the Bank's financial sector work was the provision of finance to SMEs. Box 4.1 discusses the example of the EBRD's involvement in the Russian SME sector.

In the industry and commerce group, the Bank's impact has been greatest where it

has been involved in high-visibility demonstration initiatives: Matav in Hungary was the first telecoms privatisation (see Box 4.2), DOEP was the first major investment by a multinational in Ukraine's agro-processing sector, Pliva was the first foreign listing in Croatia, and Ispat-Karmet was the first large industrial restructuring in Central Asia. But it also appears that, for sector impact, the size of investment projects played a role. In each of the countries in the left-hand column, the EBRD has sizeable and, thus, visible individual investments.

In the infrastructure sectors, the common thread in the relatively successful countries (except for Uzbekistan) appears to be the choice of a systemic or sector-wide approach in power (Ukraine, Bulgaria), transport (Romania) and municipal utilities (Romania). Another important ingredient of success was high profile commercialisation (for example, municipal utilities in Uzbekistan). These have led, or are likely to lead, to replication.

Box 4.1

EBRD transition impact in the Russian SME sector

In Russia the Bank demonstrated how, with the availability of a soft component of funding for technical assistance, a rather versatile and long-lasting approach to SME finance can be achieved. The Bank-supported Russia Small Business Fund (RSBF) is entirely a private sector operation: it is not covered by sovereign guarantees and the EBRD's loans and technical assistance are provided directly to the participating banks. As the local banking system can mobilise far greater resources than foreign programmes over the medium and long-term (and have an existing branch network), the EBRD's focus is on encouraging the participation of local banks. The programme has provided the smallest

borrowers with lasting access to finance by stimulating the interest of the local banking system and building up its technical capacity. The key to any programme of this kind lies in its sustainability. The RSBF has demonstrated that micro and small enterprises can become a key target group for local banks, provided that profitability is achieved through a high loan volume and low arrears and loss rates. The programme is supported by the G-7, EU and Switzerland. The overall size of the fund is US\$ 300 million, of which a large portion, over US\$ 50 million, is intended as technical assistance. By early December 2000, the RSBF had disbursed US\$ 431 million in 36,720 small and micro loans.

Box 4.2

EBRD transition impact in the Hungarian telecoms sector

The EBRD's operations in the Hungarian telecoms sector – particularly its equity investment – had a significant transition impact. At the enterprise level the Bank contributed to the privatisation of Matav, the state telecoms company. The Bank's participation in this process (the first privatisation of a major telecoms provider in the region) gave confidence to potential strategic investors. It helped build confidence in the legal and regulatory framework, particularly with regard to the transparency and credibility of

the key rules. Widespread private ownership has now been achieved after the government sold its remaining 5.75 per cent stake in Matav. The Bank has also been involved, sometimes actively, in a variety of regional and mobile telecoms investments as well as in television. Together, these investments probably contributed to creating what is today one of the most decentralised and competitive telecommunications and media industries in the region.

Legal transition assessment

As noted in the previous chapters, the EBRD is more effective in promoting the transition where there is a high-quality operating environment. An extensive and effectively implemented commercial legal system is a critical component of a market-friendly operating environment. For this reason, the EBRD has assisted its countries of operations in building sound legal and regulatory systems. The strategic objective guiding the Bank's legal transition work, and incorporated in the Bank's Legal Transition Programme (LTP), is:

To improve the legal environment of the Bank's countries of operations by fostering interest in, and helping to define and implement, legal reform through the provision of legal technical assistance and policy and strategy advice focused on the development of the legal rules, institutions and culture necessary to support a vibrant market-oriented economy.

To achieve this objective, the Bank has organised the LTP around four activities: (i) assessment of the state of legal transition, (ii) setting international standards, (iii) outreach, and (iv) technical assistance projects. These activities are focused on six legal sectors important to the Bank's operations and the development of a sound investment environment: bankruptcy, corporate governance and company law, concessions, financial markets, secured transactions and telecommunications. In 1995 the Bank created the Legal Transition Team, a group of dedicated lawyers focused on legal transition to implement the LTP.

5.1 Current state of legal transition

The development of an effective commercial legal system in the EBRD's countries of operations has been an uneven process. Part of this unevenness has been due to a lack of political consensus on the direction of economic and legal reform in some transition countries. Clear political leadership and a coherent legislative strategy are prerequisites for the development of a sound legal framework. There has been generally steady progress in the adoption and updating of commercial and financial laws throughout the region. However, the EBRD's Legal Indicator Survey, which measures the extensiveness and effectiveness of commercial and financial laws in the region, consistently reveals that the difficult work of building effective legal institutions to implement and enforce new laws remains incomplete. This lack of implementation threatens the effectiveness of new commercial and financial laws and undermines the public's confidence in the establishment of the rule of law.

Countries seeking accession to the European Union (EU) have tended to lead the way in legal reform, with the prospect of accession acting as a major incentive to harmonise laws and regulations with the European Community's *acquis communautaire*. Increased international attention to the investment climate has been a driving force behind recent improvement in legal transition in the CIS countries. Financial market legislation has been a particular focus of legal reform efforts, with EU accession and an increased global emphasis on improved corporate governance and financial standards pushing transition countries to improve both their laws and practice in this area.

5.2 Summary of legal transition impact¹⁷

Overview

The EBRD has designed its country-specific legal transition projects to address the legal reform challenges that arise in the specific focus sectors of the LTP. These projects are undertaken using a combination of the Legal Transition Team's expertise and consultants, supported by technical cooperation funds. In order to determine the Bank's impact in assisting legal transition in the region, we evaluated only those completed projects that were supported by TC funds. The transition impact of in-house advice and expertise, and of ongoing projects, have not been included in the assessment.

The procedure was first to assess each project completed under the LTP and then aggregate those assessments for the specific legal area in each of the Bank's countries of operations. Due to the inevitably long-term nature of legal transition projects – the average project now runs well over a year – there were no completed LTP projects to assess in the following countries: Armenia, Bulgaria, Croatia, Estonia, Georgia, Kazakhstan, Latvia and the Slovak Republic. However, there are ongoing legal transition projects in many of these countries.

The transition impact of LTP projects has varied across the region and across its focus areas. The transition impact of legal reform projects usually consists of two components: legislative drafting and implementation. A project can achieve success in one (drafting of a new law, amendments or regulations) but have minimal impact in the other (failure to implement the changes). For example,

¹⁷ A detailed assessment is provided in Annex 3.

in Tajikistan the Legal Transition Team provided comments and suggestions for revising the Tajik pledge law, which were eventually incorporated into the amended law. However, the Tajik Government has yet to implement these changes by creating a pledge registration system. This split transition impact can be seen in a number of the projects assessed as having a moderate or medium transition impact. (See Annex 3.)

The bulk of the assessed legal transition projects fell into the middle impact range, with most projects having a moderate or medium impact on legal transition. Unlike the EBRD's investment operations, the transition impact of LTP's legal projects is not related systematically to the state of general economic reform or the quality of the operating environment. LTP has had a significant impact in countries such as Azerbaijan, Bosnia and Herzegovina, and Turkmenistan. The key determinants of successful legal transition projects are consistent political will on the part of the government, to see the reform effort to its conclusion (including effective imple-

mentation), and in-house legal expertise in the reform area to supervise and lead the project.

In all but one of the LTP focus areas, the Bank has had a project that produced a medium or significant legal transition impact. In corporate governance, where only one regional project was available to be assessed, the impact was minimal. However, in two financial market projects in the Czech Republic and Russia (focused on capital market and securities law reform), there was a corporate governance component and both have had a significant impact on legal transition in the sector.

Challenges of legal transition

As the Legal Transition Team's approach to legal reform projects has developed over time, attention has shifted from legislative reform to implementation and legal institution building. The EBRD's research and Legal Indicator Surveys have revealed that, while the commercial and financial laws in the region have steadily improved

over the first transition decade, a large implementation gap persists. As the Bank develops projects to help fill this gap, its legal transition assistance becomes more complex and time-consuming. Building legal institutions (pledge registries, independent regulatory agencies, etc.) and training staff require more resources and a more intensive in-country effort. As a result, it becomes more difficult and costly to design and implement effective legal transition projects.

In addition to this difficulty, the EBRD's legal transition projects are inherently political and often become subject to political delays and obstacles that are beyond the Bank's control. The Legal Transition Team has tried to mitigate this political risk to transition impact by ensuring high-level governmental support for the Bank's legal reform projects. More importantly, the projects are designed and implemented in such a way as to try to include the various interests and institutions involved in drafting, adopting and applying or enforcing the proposed legal change. In this way, we try to devise

Environmental transition assessment

6.1 Environmental challenges

Under Communism, environmental standards and regulations, although normally set at demanding levels, were typically ignored. The energy and resource efficiency of industry was low, and its environmental management capabilities were weak. Pollution control equipment was often worn out or non-existent. Environmental disasters were treated as state secrets and public participation in environmental decision making was limited and poorly organised.

The collapse of the centrally planned economies significantly reduced the resources available to the public sector to upgrade and maintain facilities such as water supplies and waste-water treatment plants. It also resulted in severe disruption to the mechanisms that deliver environmental protection, such as monitoring regimes and plant inspections. Together with reduced health expenditures and changes in lifestyle, environmental degradation has in many transition countries contributed to a reduction in life expectancy.

The transition process offers the prospect of addressing many of these issues. Transition is leading to a reduction in environmental pressure through:

- More efficient use of energy and other resources, as industry and private consumers begin to react to price signals, payment discipline increases, subsidies are phased out and prices are raised to full cost-recovery levels (complemented by targeted support for low-income households).
- Replacement of worn out production capacity by modern, more efficient facilities equipped with proper pollution control systems and recycling capabilities.

- Reduction in the environmental impacts through the introduction of good industrial and resource extraction practices, including the reduction of gas flaring, control of water pollution, management of toxic wastes, and decommissioning and site clean up.
- Reduction in emissions from energy production through the introduction of modern power and heat production and distribution technology and the use of less polluting fuels.
- Improvements in the status of health and safety training, monitoring, reporting and environmental management.

The challenge for all transition countries is to resume economic growth without a corresponding increase in polluting emissions. There is some evidence that, in the more advanced transition countries, pollution intensity and economic growth are now de-coupled. In less advanced transition countries, emissions remain closely linked to economic indicators.

To ensure environmentally sustainable development in the long term, the above short-term transition benefits have to be combined with reforms in environmental policy and regulation. This entails improvements in environmental legislation, the involvement of civil society and cooperation with the private sector.

Reform of environmental legislation will require pragmatic policy instruments and regulatory processes. This includes the establishment of environmental funds, particularly in the early transition countries, to channel money collected as environmental fees and fines to environmental investments; and the use of financial incentives to achieve energy and other resource efficiency, waste reduction and the use of clean technologies.

Increased public involvement, associated with political decentralisation and enhanced corporate governance, will push environmental issues up the political agenda and should ensure effective public participation and developmental programmes on projects with significant potential environmental and social impacts.

The private sector has an important role to play in providing and financing, in partnership with the public sector, environmental services such as waste management, waste-water treatment and water supply. The private sector also contributes in areas such as energy conservation (through energy service companies), pollution control and the manufacture of environment-related products.

6.2 The EBRD's response

The EBRD seeks to advance environmental transition primarily by demonstrating, and setting standards for, good environmental practice, and by ensuring that all its projects comply with international environmental and health and safety standards. To achieve this, the Bank has established a system of environmental due diligence that includes the environmental appraisal of every project, starting at or before concept clearance. Financial intermediaries working with the Bank are required to develop equivalent procedures.

The EBRD has advanced environmental transition by promoting a policy dialogue with civil society on environment-related issues by implementing its Public Information Policy. In particular, it requires its clients to provide information and listen to the concerns of those affected by potentially environmentally significant projects. Ensuring compliance with environmental, health and safety, and public participation standards in all projects is the task of the Bank's Environmental Appraisal Unit.

The Bank seeks to directly improve environmental quality through the work of its Energy Efficiency, Municipal and Environmental Infrastructure (MEI), Power, Transport, Industry and Commerce, and Natural Resources teams:

- The EBRD’s portfolio of water, waste-water and waste management investments. In St Petersburg, for example, the Bank – jointly with the EU and Nordic donors – is financing the urgent rehabilitation and reform of the toxic waste management system, thus addressing an important regional pollution “hot spot”.
- Investments in energy efficiency and conservation. To date the Bank has signed 14 projects with energy service companies (ESCOs). Projects in many other sectors also contribute to the more efficient use of energy.
- More general investments in the power sector that reduce losses (in generation/transmission and distribution) and/or introduce new fuel sources (gas, hydro, geothermal), both of which result in lower emissions.
- The provision of medium- and long-term financing for environmental and energy efficiency purposes via credit lines to local banks. Examples of such transactions include the Budapest Bank Credit Line for Environment and Energy (Hungary), and the PBK General Purpose and Energy Efficiency Credit Facility (Slovak Republic), both undertaken jointly with EU Phare.
- The Bank contributed to Regional Equity Funds focused on making private sector equity investments in the energy efficiency industry. Examples of such transactions include the Dexia FondElec Energy Efficiency and Emissions Reduction Fund, and the Environmental Investment Fund.
- Environmental Action Plans associated with projects in industry and natural resources.

Table 6.1

Rating of projects in environmentally most significant sectors¹

	number	%	%
Environmental performance evaluated projects: 113			
Excellent	35	31	} 51
Good	23	20	
Satisfactory	38	34	34
Marginal	17	15	} 15
Unsatisfactory	0	0	
Highly Unsatisfactory	0	0	
Extent of environmental change evaluated projects: 113			
Outstanding	3	3	} 42
Substantial	44	39	
Some	52	46	46
None	14	12	} 12
Negative	0	0	

¹ The evaluations of 113 projects include also 39 projects that have been evaluated in the special study “Evaluation of Environmental Performance of EBRD”. The Environmental Appraisal Unit (EAU) has assisted in carrying out 27 desk studies and field surveys. PED has validated and approved all documents prepared by EAU.

In addition to its project-related work, the EBRD participates in environmental capacity building through technical cooperation initiatives. It supports the Environmental Action Programme for Central and Eastern Europe, principally through the Project Preparation Committee (PPC), and has recently become an Executing Agency of the Global Environment Facility (GEF). The Bank also serves as the Administrator of the Nuclear Safety Account (NSA), the Chernobyl Shelter Implementation Plan (SIP), and for three nuclear plant decommissioning funds in Bulgaria, Lithuania and the Slovak Republic.

6.3 The EBRD’s environmental impact and performance¹⁸

The environmental impact of EBRD projects and their adherence to environmental standards is assessed by PED as part of their project evaluations and recently in a special study on environmental performance. Projects were evaluated according to two criteria. “Environmental performance” measures how well the environmental objectives of the project have been met, while “extent of environmental change” evaluates the improvement in environmental quality achieved during project implementation; for example, the reduction in pollution

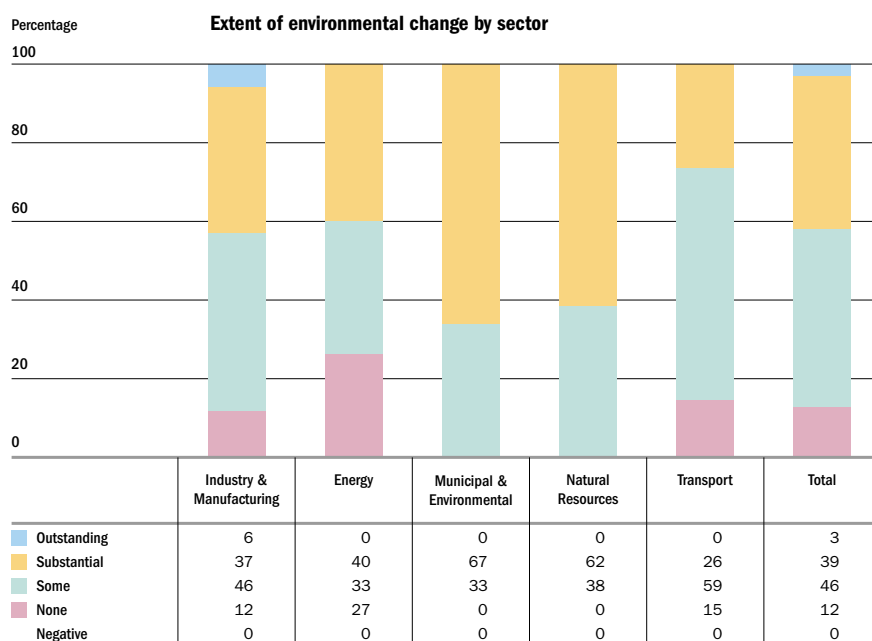
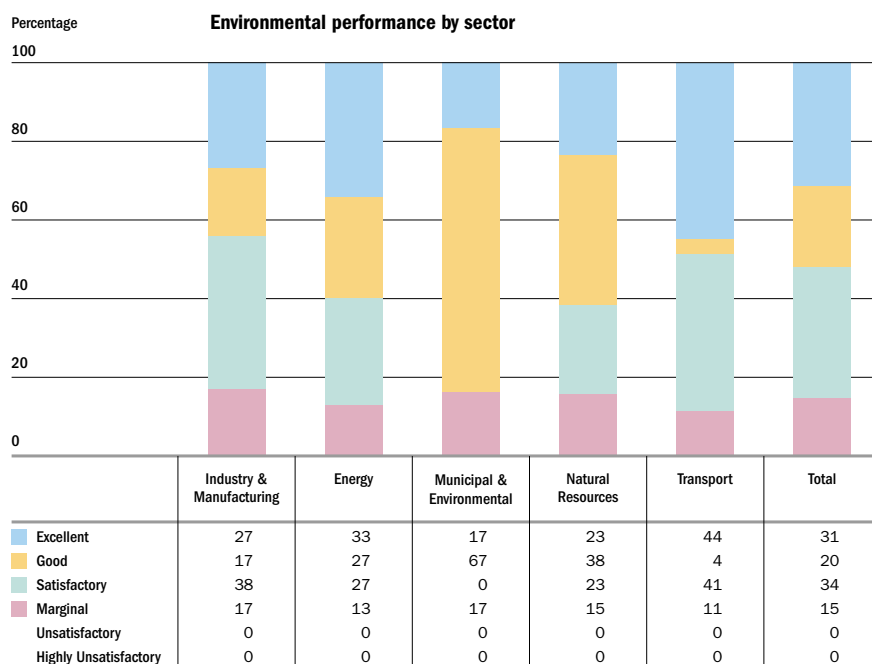
loads, improvements in health and safety and environmental risk management, and institutional development.

The Bank’s environmental impact was most significant in industry and manufacturing, energy, municipal and environmental infrastructure, natural resources and transport (the environmentally most significant sectors) compared with other sectors.

Table 6.1 shows the ratings of environmental performance and extent of environmental change for 113 projects reviewed in the most environmentally significant sectors between 1996 and 2000. Environmental performance in the most environmentally important sectors has been *good* or *excellent* in 51 per cent and *satisfactory* in 34 per cent of the evaluated projects. In other words, the majority of projects were successful in meeting their environmental objectives, which in most cases had to do with the mitigation of negative impacts and regulatory compliance. Good environmental performance appears to be linked to overall project success, and satisfactory or better environmental performance was achieved by only few projects that did not also obtain a successful overall rating.

¹⁸ Lessons learned from the Bank’s approach to environmental transition are presented in Annex 4.

Chart 6.1

Environmental performance and extent of environmental change by sector

The extent of environmental change has been rated *outstanding* or *substantial* in 42 per cent of the projects. The level of success depends not least on the starting point. In some cases, the environmental situation was at a high level before the project started and the potential for environmental improvement was thus limited. “Greenfield” projects – such as oil drilling and associated pipelines or road networks in environmentally sensitive areas (such as the taiga) – are bound to have harmful effects on the environment. To measure the EBRD’s environmental impact, greenfield projects were evaluated against a “counterfactual” project in which the Bank’s financing and environmental procedures were not used (rather than a “no project” scenario).

Environmental performance and extent of environmental change by sector

The environmental performance and extent of environmental change of 113 reviewed projects by sector is shown in Chart 6.1.

Many of the early industrial projects involved facilities with worn-out or non-existent pollution control equipment and uneconomical manufacturing processes. This provided a good potential for environmental improvements, although upgrading such facilities requires expertise about the industry-specific process technologies and about “state of the art” pollution control.

Energy projects are particularly important in abating air emissions. The only unsuccessful project from an environmental performance point of view has been the Maritza East Power Plant in Bulgaria. No improvements in reduction of air emissions have been achieved so far, due to delays in the installation of EBRD-funded flue gas desulphurisation equipment. When implemented in 2001, the reduction in sulphur emissions will be substantial.

MEI projects, with their focus on improving water supply, waste-water treatment and waste management, are environmentally important and have all had a positive impact on the environment.

Projects in the natural resources sector tend to be highly sensitive environmentally and require careful (and time-consuming) environmental due diligence. In many mining and oil drilling projects, the Bank has been able to demonstrate good economic and environmental practice in regions where existing pollution levels are high. All evaluated projects have been judged to have contributed to environmental improvement to some degree.

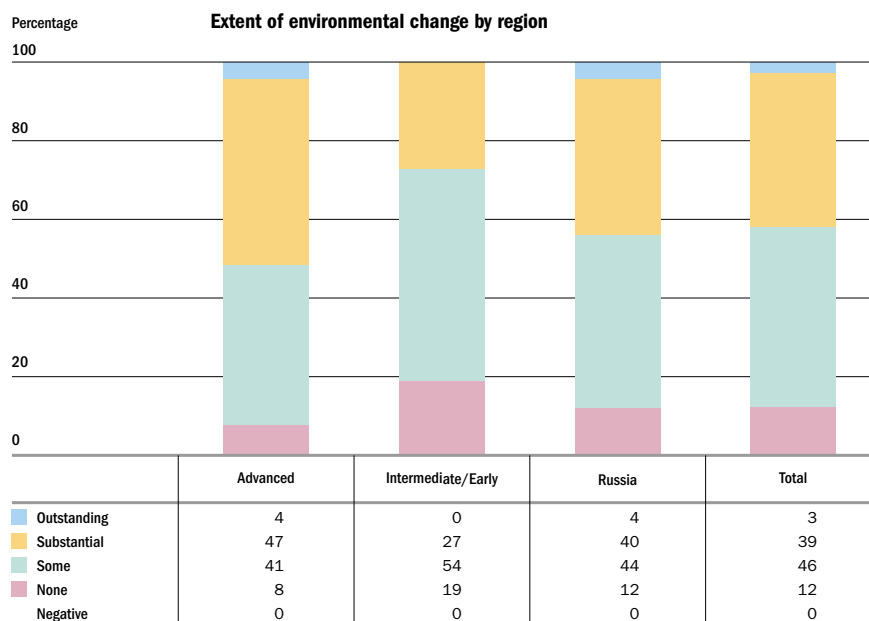
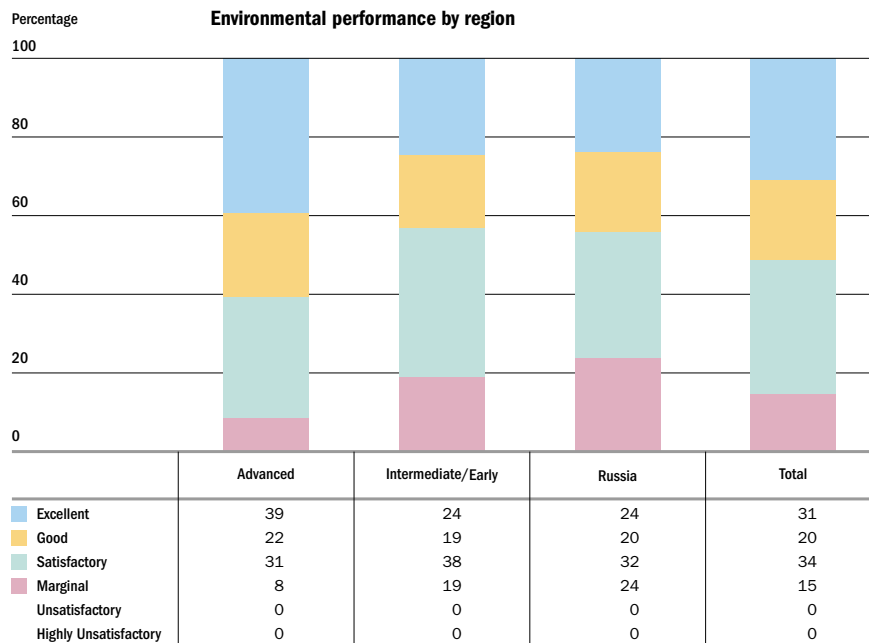
The transport sector has significant potential impacts on traffic-related emissions, and on marine and land pollution.

Environmental performance and extent of environmental change by region

Chart 6.2 shows the environmental performance of EBRD projects by region. A large share of the 113 evaluated projects (45 per cent) was in the advanced eastern Europe region, where environmental performance has been above average. There have been more projects with outstanding or substantial environmental change in advanced countries (51 per cent) than in intermediate/early transition countries (27 per cent). Forty-four per cent of the Russian projects also performed well. In part this was due to the fact that the low starting point in many oil drilling and mining projects created a good potential for positive environmental change.

Chart 6.2

Environmental performance and extent of environmental change by region



Conclusions

The evaluation of the EBRD's transition impact identifies certain patterns and important lessons that are relevant for the future activities of the Bank.

The EBRD has been an important contributor to foreign direct investment in the region. It has been especially successful in promoting FDI in South-Eastern Europe, the Southern CIS and Russia. In the early part of the 1990s, it played a significant role for FDI into Central Europe. It has been much less active in the Western CIS (Belarus, Moldova, Ukraine). Not only was FDI into these countries fairly limited, but the Bank has been associated with only a small (and falling) fraction of it.

Evaluation ratings of investment projects' transition impact were analysed by broad country and sector groups. Many projects scored well, with over two-thirds obtaining ratings in the medium and high transition impact range. The EBRD has been relatively successful in infrastructure, particularly when it has used its leverage to improve the operating environment through policy dialogue with the local authorities and insistence on project conditionality. In industry and commerce, the Bank has been more successful when it has worked with strategic investors. In the absence of strategic investors, both transition impact and financial sustainability have been lower, due to the limited capability of local sponsors and managers to support restructuring for competitive markets. This occurred even when the EBRD was closely involved, but was less pronounced in companies with a competitive advantage, and in sectors where the Bank has built in-house expertise or networks. In the financial sector, as in other sectors, the Bank has been more successful in reform-minded

countries. In countries where reform has been slow – poor regulation, limited transparency in corporate governance, lack of clarity in administrative and tax framework, barriers to entry, subsidies, price distortions – investments tended to be less successful.

The EBRD's impact on the transition process varies strongly by sector and country of operations. An important reason for this variation is the limited regional coverage of a number of sector programmes. A second factor is the receptiveness of the operational environment (in particular, the host government) to transition stimuli, and the close link between transition impact and commercial success. As a rule, the Bank has had less impact in low transition countries, where the operational environment is less conducive to private investment and to the effective transmission of project spill-overs. However, there are important exceptions to this rule in each sub-region and at all levels of transition. The more successful experiences, though not always replicable, may offer lessons for raising the Bank's impact in the future. Lastly, sector success has tended to be associated with high-visibility, often large-scale interventions.

Since 1995 the EBRD has had a dedicated team focusing on legal transition, in particular the development of commercial law. The Bank's Legal Transition Team has ongoing projects in most countries and has achieved significant success in a diverse range of countries, from Azerbaijan, Bosnia and Herzegovina, Russia and Turkmenistan, to the Czech Republic, Hungary and Lithuania. Legislation has been drafted and implemented in a number of areas, from bankruptcy law to concessions, corporate governance,

financial market regulation, secured transactions, telecommunications and arbitration. Where the Bank has been less successful, this is typically through a failure of the government to implement legislation drafted under the Legal Transition Programme. In recognition of this, the Legal Transition Team has begun to focus more on implementation capacity and institution building.

An important Communist legacy was, and unfortunately still is, a degraded municipal and industrial infrastructure giving rise to huge environmental and health and safety concerns. The EBRD has helped to improve environmental quality by financing projects with specific environmental objectives and by applying environmental requirements to all operations. In implementing its environmental mandate, the Bank was most successful in advanced transition countries, suggesting that the receptiveness of the operational environment is again crucial for success. Projects in municipal and environmental infrastructure, which often have explicit environmental objectives, have been particularly successful. The Bank also made a difference in heavily polluting sectors such as industry, power and natural resources, where substantial improvements could be secured, often against a low starting point. However, there is still much potential to improve the Bank's environmental performance and in particular its impact, and seek more projects with higher potential for positive environmental change. As the Bank steps up its activities particularly in intermediate and early transition countries and Russia, its project portfolio may become more demanding to appraise and implement successfully from the environmental point of view.

Transition Impact Retrospective – Annexes

Contents

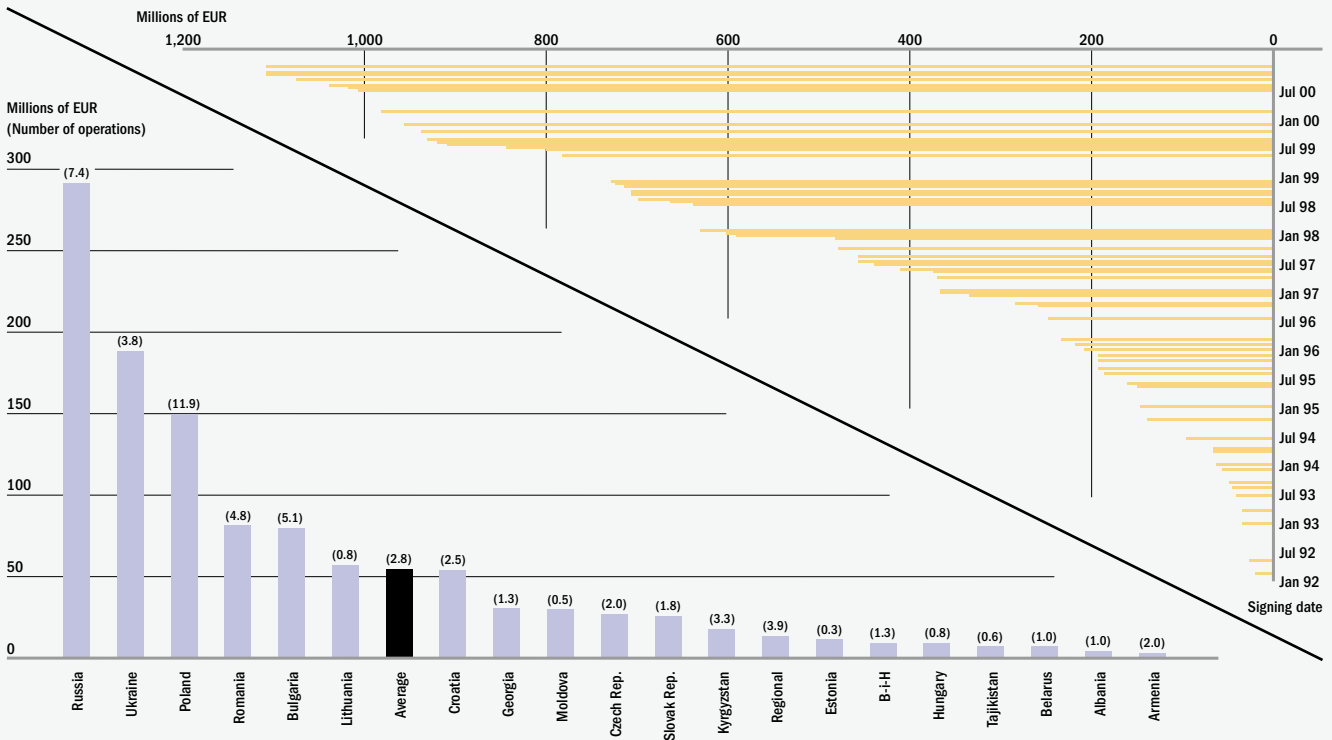
Annex 1: EBRD operations by sector	22
Annex 2: Transition impact at the project level	32
Annex 3: Legal transition assessment – event line and methodology	33
Annex 4: Environmental compliance – lessons learned	38

Annex 1: EBRD operations by sector

Bank's operations in the Agribusiness sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

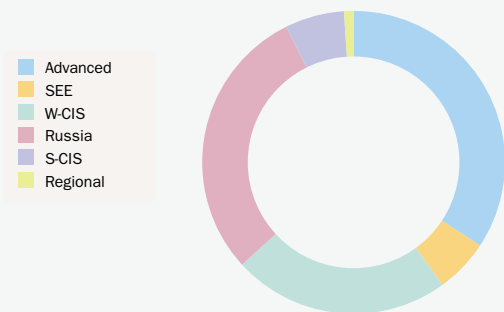


Chart 3

Sectoral breakdown of total commitments

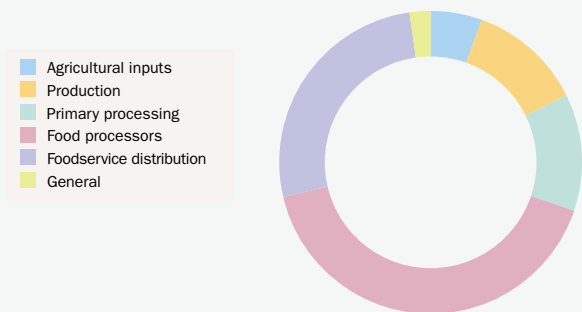


Table 1

Finance of EBRD operations

(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	45%	90%	425%
SEE	12%	74%	362%
W-CIS	13%	83%	199%
Russia	15%	85%	395%
S-CIS	15%	85%	320%
Regional	100%	100%	726%
Total	24%	89%	359%

Table 2

PED transition impact ratings

(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	1.67	12
SEE	2.13	8
W-CIS	2.00	3
Russia	3.00	1
S-CIS	0.50	2
Regional	–	0
Total	1.81	26

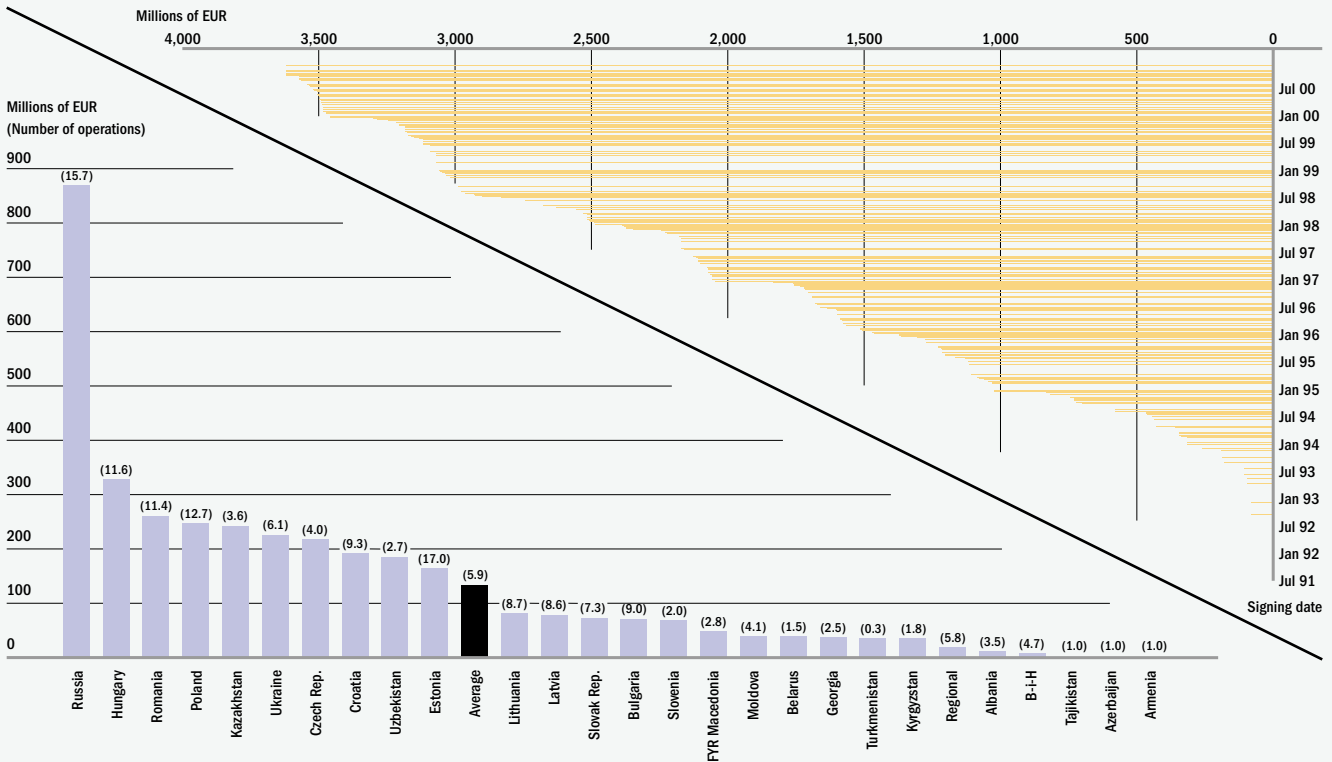
Ratings range from -1 (negative) to 3 (high)

Advanced Eastern Europe: Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia. South-Eastern Europe: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Romania. Western CIS: Belarus, Moldova, Ukraine. Southern CIS: Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Uzbekistan.

Bank's operations in the Banking sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

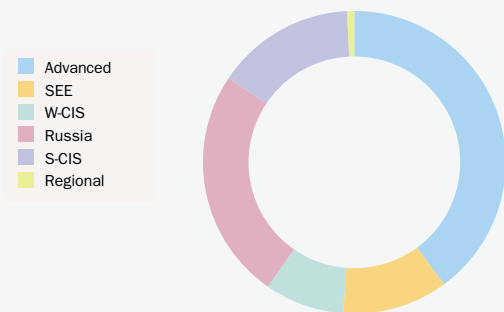


Chart 3

Sectoral breakdown of total commitments

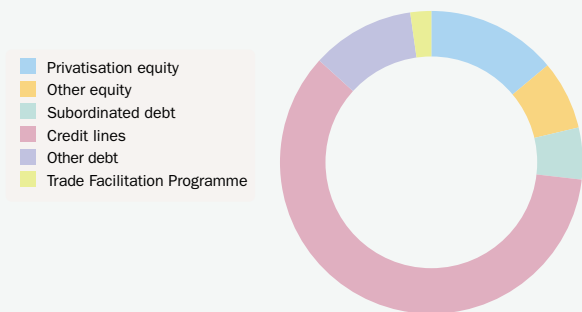


Table 1

Finance of EBRD operations

(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	40%	100%	191%
SEE	19%	98%	445%
W-CIS	4%	100%	158%
Russia	7%	100%	170%
S-CIS	2%	100%	126%
Regional	0%	100%	178%
Total	21%	100%	201%

Table 2

PED transition impact ratings

(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	2.16	37
SEE	1.78	9
W-CIS	2.33	3
Russia	1.18	11
S-CIS	2.00	3
Regional	2.50	2
Total	1.95	65

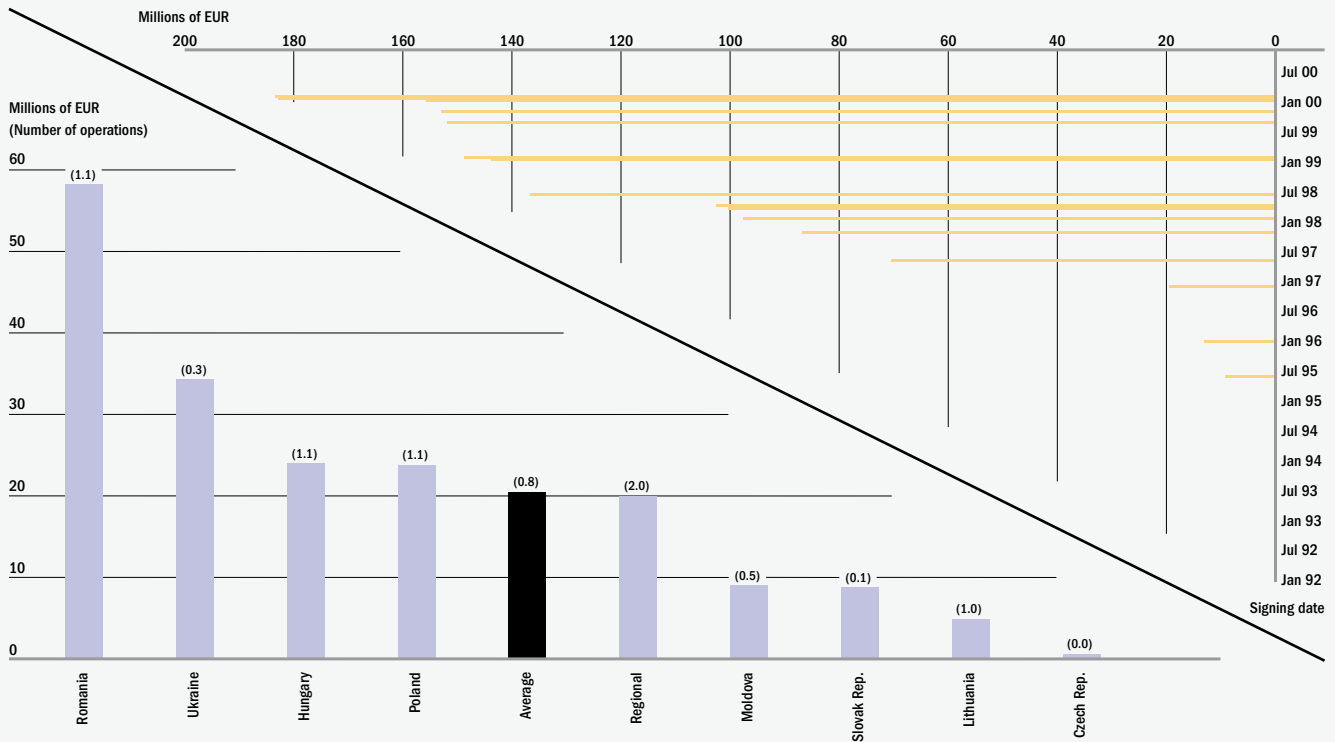
Ratings range from -1 (negative) to 3 (high)

Advanced Eastern Europe: Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia. South-Eastern Europe: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Romania. Western CIS: Belarus, Moldova, Ukraine. Southern CIS: Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Uzbekistan.

Bank's operations in the Energy Efficiency sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

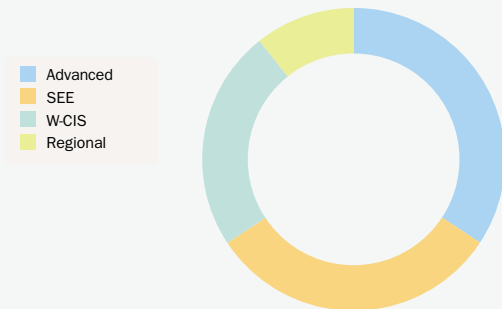


Chart 3

Sectoral breakdown of total commitments

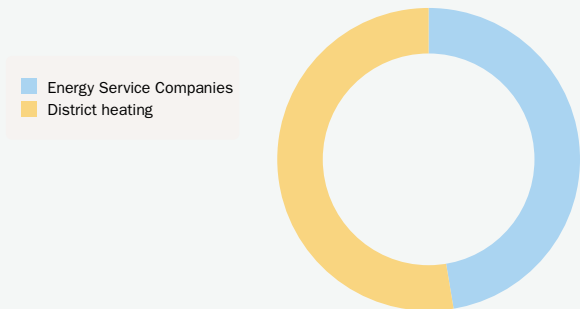


Table 1

Finance of EBRD operations
(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	33%	100%	434%
SEE	4%	12%	212%
W-CIS	0%	0%	199%
Russia	-	-	-
S-CIS	-	-	-
Regional	100%	100%	500%
Total	23%	49%	300%

Table 2

PED transition impact ratings
(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	3.00	1
SEE	-	0
W-CIS	-	0
Russia	-	0
S-CIS	-	0
Regional	-	0
Total	3.00	1

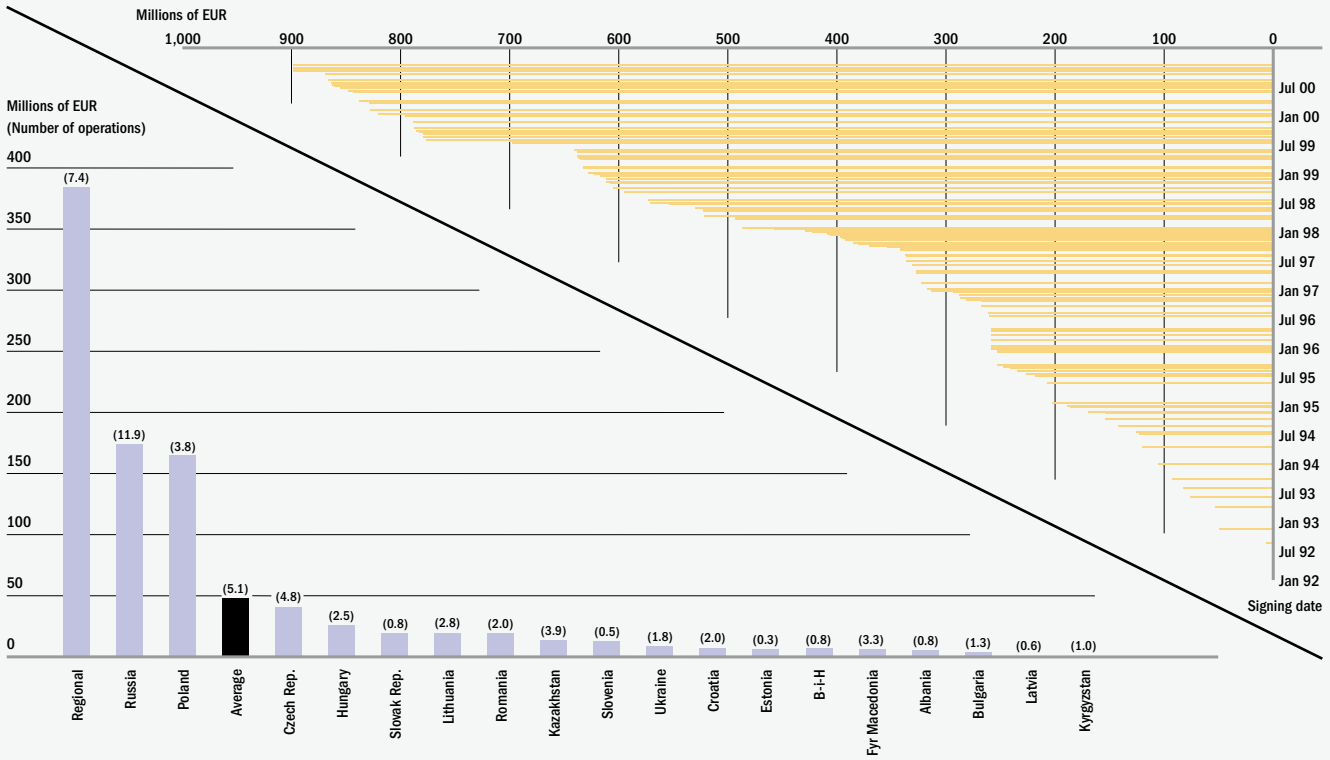
Ratings range from -1 (negative) to 3 (high)

Advanced Eastern Europe: Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia. South-Eastern Europe: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Romania. Western CIS: Belarus, Moldova, Ukraine. Southern CIS: Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Uzbekistan.

Bank's operations in Equity Funds

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

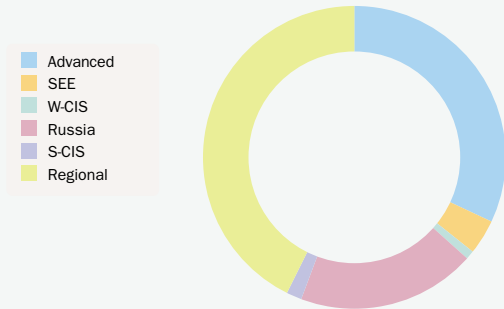


Chart 3

Sectoral breakdown of total commitments

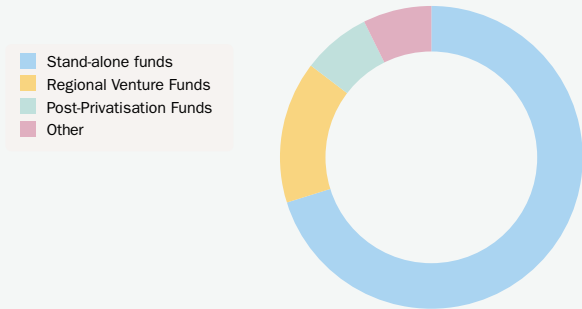


Table 1

Finance of EBRD operations

(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	84%	100%	521%
SEE	95%	100%	630%
W-CIS	100%	100%	675%
Russia	83%	100%	325%
S-CIS	42%	100%	355%
Regional	100%	100%	694%
Total	91%	100%	560%

Table 2

PED transition impact ratings

(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	1.67	12
SEE	2.13	8
W-CIS	2.00	3
Russia	3.00	1
S-CIS	0.50	2
Regional	0.00	0
Total	1.81	26

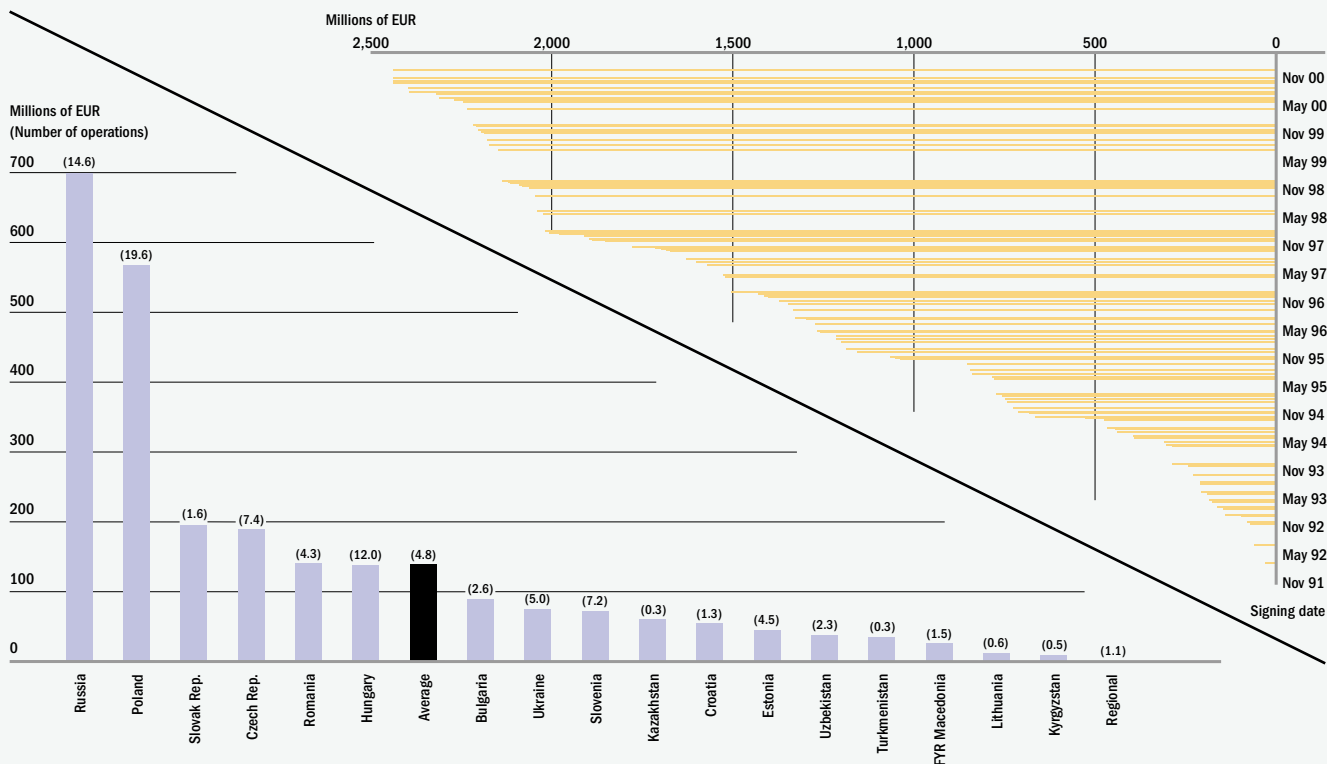
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Bank's operations in the General Industry sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

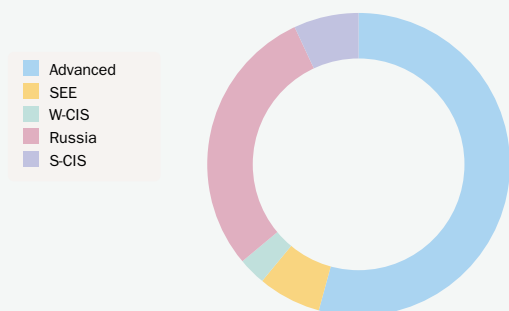


Chart 3

Sectoral breakdown of total commitments

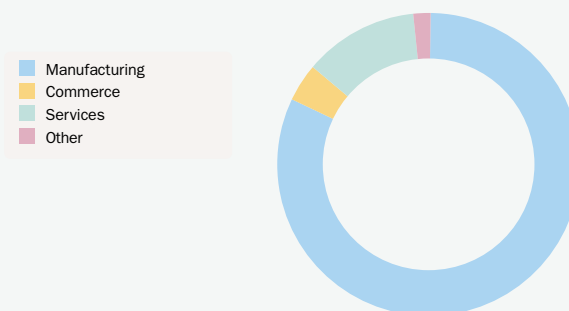


Table 1

Finance of EBRD operations
(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	24%	100%	418%
SEE	45%	100%	394%
W-CIS	26%	100%	622%
Russia	5%	95%	469%
S-CIS	29%	100%	491%
Regional	–	–	–
Total	21%	99%	479%

Table 2

PED transition impact ratings
(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	1.74	35
SEE	1.75	4
W-CIS	–	0
Russia	1.36	11
S-CIS	2.00	2
Regional	–	0
Total	1.67	52

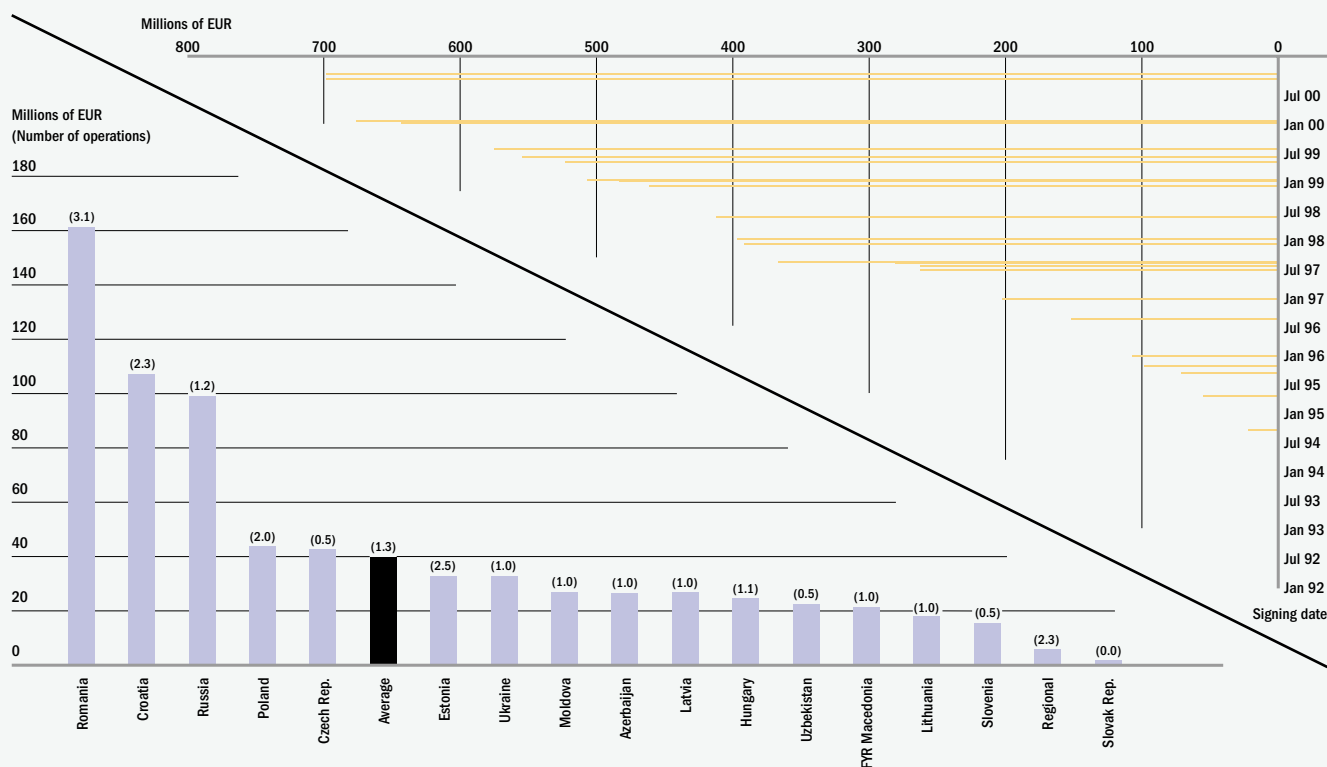
Ratings range from -1 (negative) to 3 (high)

Advanced Eastern Europe: Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia. South-Eastern Europe: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Romania. Western CIS: Belarus, Moldova, Ukraine. Southern CIS: Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Uzbekistan.

Bank's operations in the Municipal sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

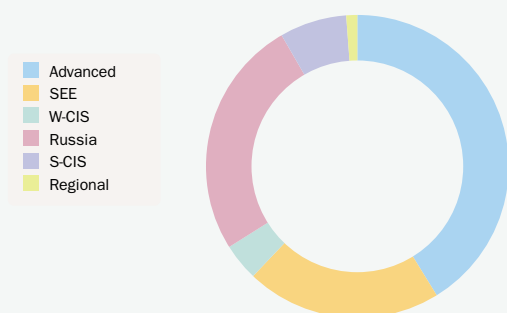


Chart 3

Sectoral breakdown of total commitments



Table 1

Finance of EBRD operations

(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	0%	29%	307%
SEE	0%	14%	250%
W-CIS	0%	0%	165%
Russia	0%	0%	587%
S-CIS	0%	0%	335%
Regional	100%	100%	584%
TOTAL	1%	20%	324%

Table 2

PED transition impact ratings

(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	2.00	2
SEE	3.00	1
W-CIS	–	0
Russia	3.00	1
S-CIS	–	0
Regional	–	0
Total	2.50	4

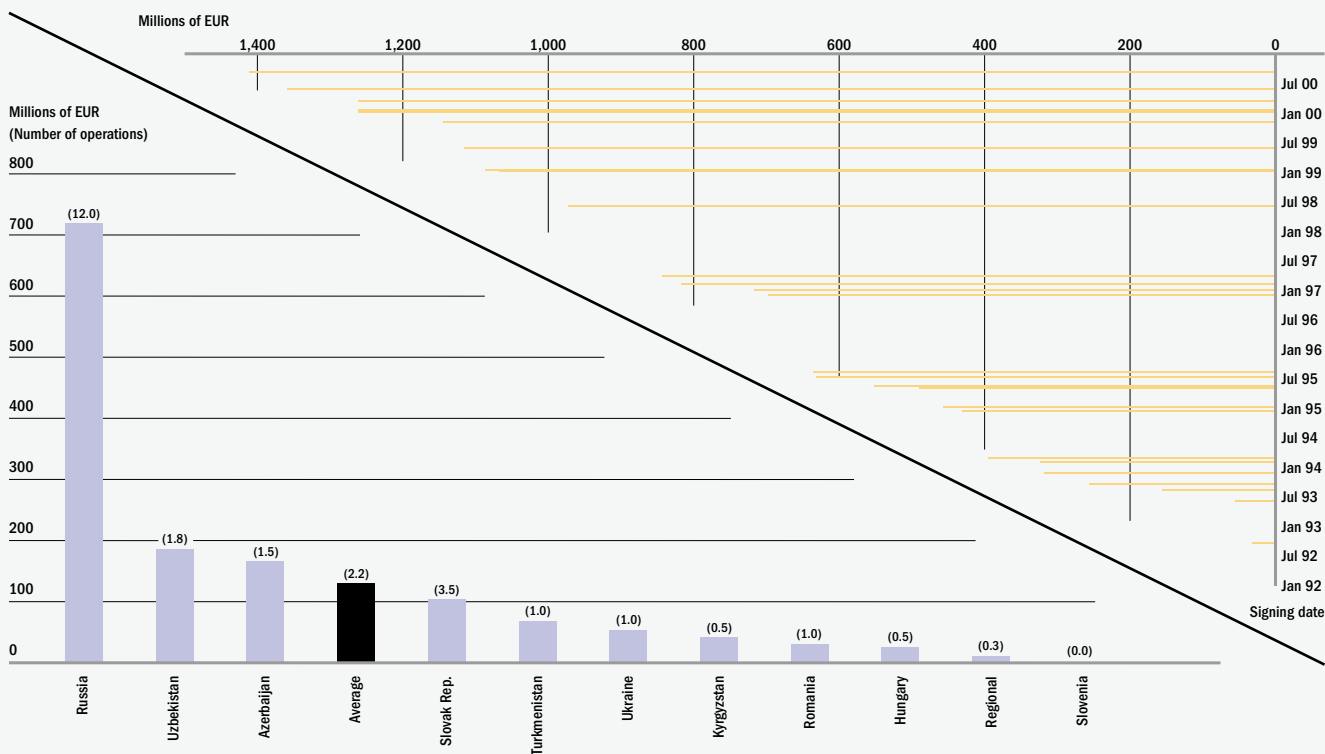
Ratings range from -1 (negative) to 3 (high)

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Bank's operations in the Natural Resources sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

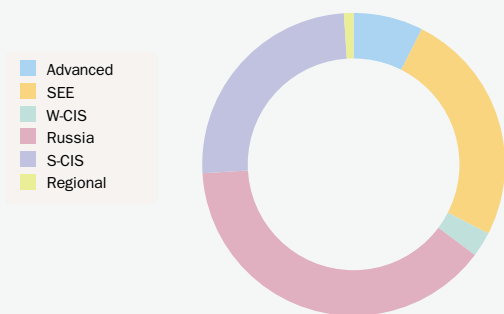


Chart 3

Sectoral breakdown of total commitments

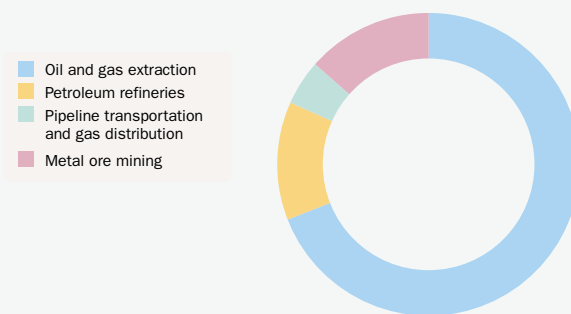


Table 1

Finance of EBRD operations

(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	33%	78%	687%
SEE	0%	0%	135%
W-CIS	0%	17%	252%
Russia	3%	78%	550%
S-CIS	3%	78%	837%
Regional	0%	100%	6199%
Total	6%	77%	681%

Table 2

PED transition impact ratings

(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	1.00	3
SEE	2.00	1
W-CIS	1.00	1
Russia	2.14	7
S-CIS	1.50	2
Regional	-	0
Total	1.88	8

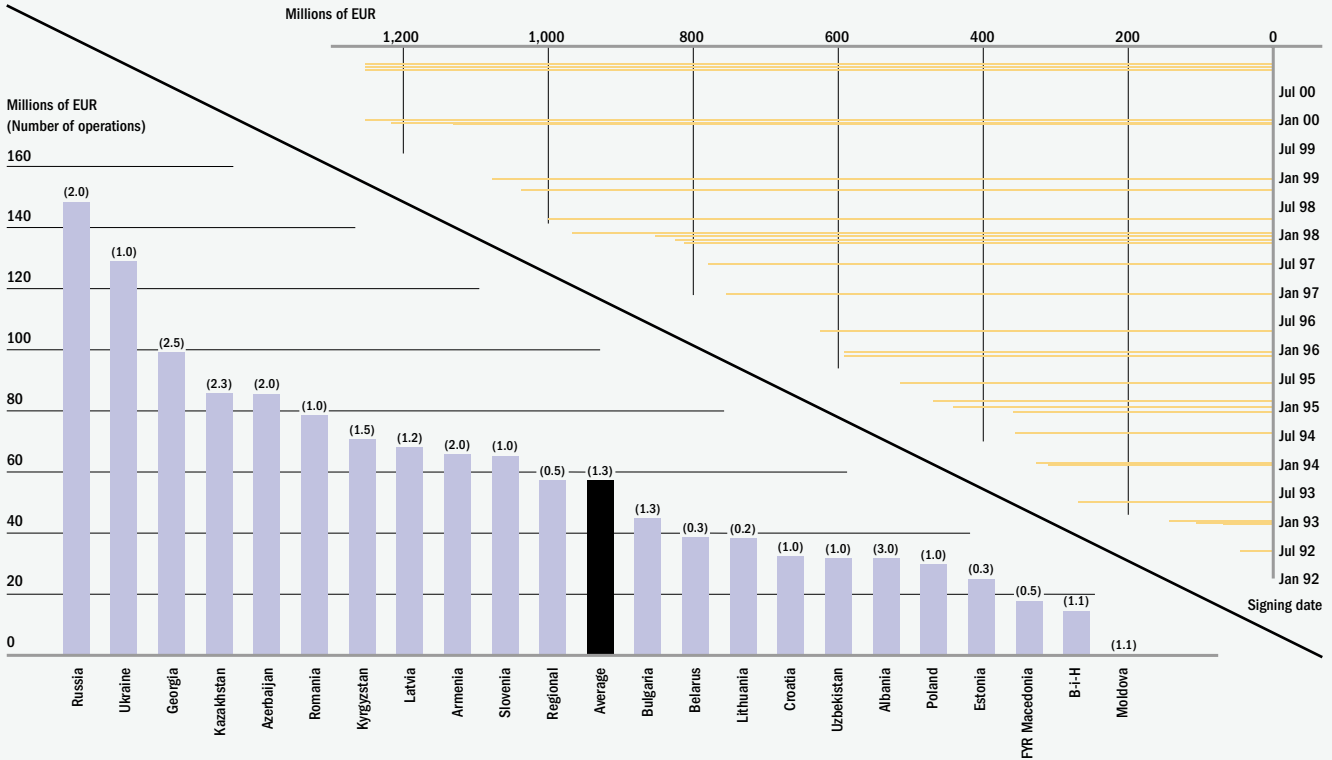
Ratings range from -1 (negative) to 3 (high)

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Bank's operations in the Power sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

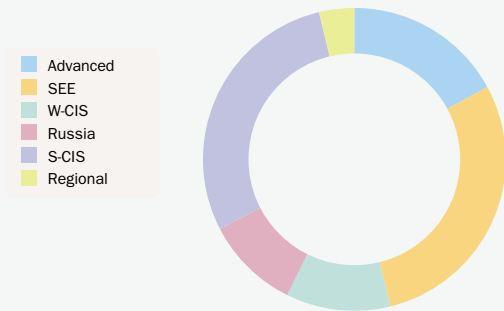


Chart 3

Sectoral breakdown of total commitments

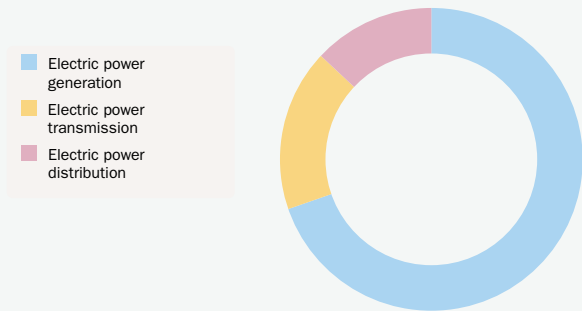


Table 1

Finance of EBRD operations (% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	0%	11%	186%
SEE	0%	0%	460%
W-CIS	0%	0%	127%
Russia	0%	16%	216%
S-CIS	0%	16%	275%
Regional	100%	100%	500%
Total	5%	15%	268%

Table 2

PED transition impact ratings (average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	2.50	4
SEE	2.00	1
W-CIS	-	0
Russia	-	0
S-CIS	1.00	3
Regional	-	0
Total	1.88	8

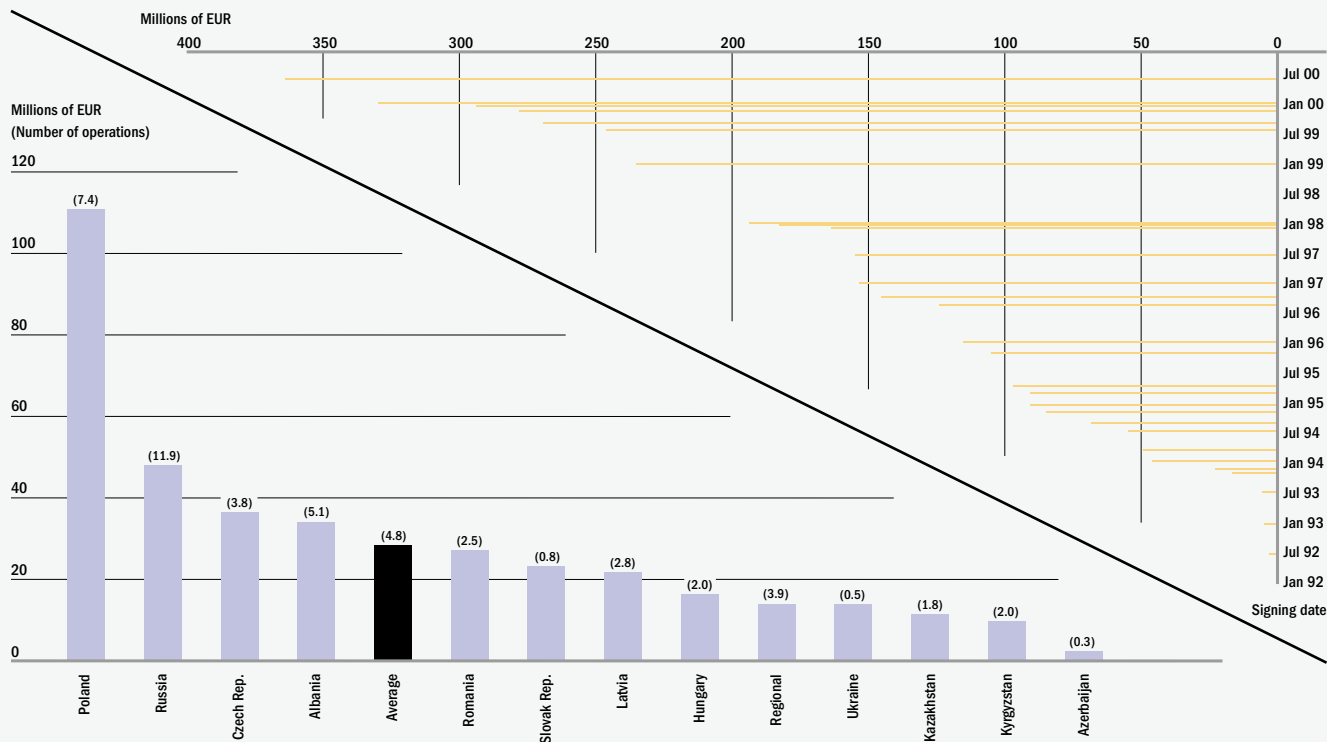
Ratings range from -1 (negative) to 3 (high)

Advanced Eastern Europe: Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia. South-Eastern Europe: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Romania. Western CIS: Belarus, Moldova, Ukraine. Southern CIS: Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Uzbekistan.

Bank's operations in the Property and Tourism sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

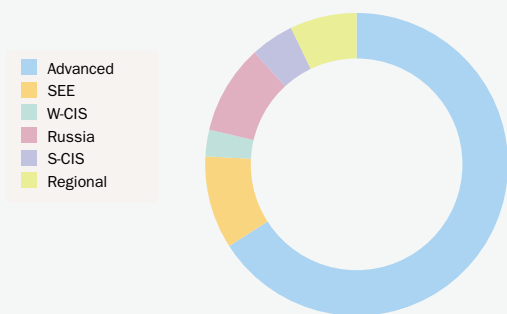


Chart 3

Sectoral breakdown of total commitments

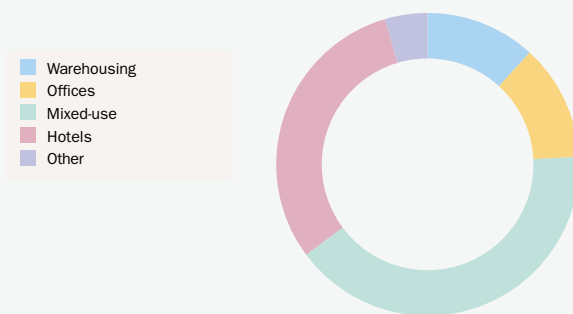


Table 1

Finance of EBRD operations

(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	44%	100%	450%
SEE	8%	100%	238%
W-CIS	46%	100%	291%
Russia	19%	100%	287%
S-CIS	0%	100%	289%
Regional	100%	100%	740%
Total	35%	100%	389%

Table 2

PED transition impact ratings

(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	2.14	7
SEE	2.33	3
W-CIS	-	0
Russia	2.00	1
S-CIS	-	0
Regional	-	0
Total	2.18	11

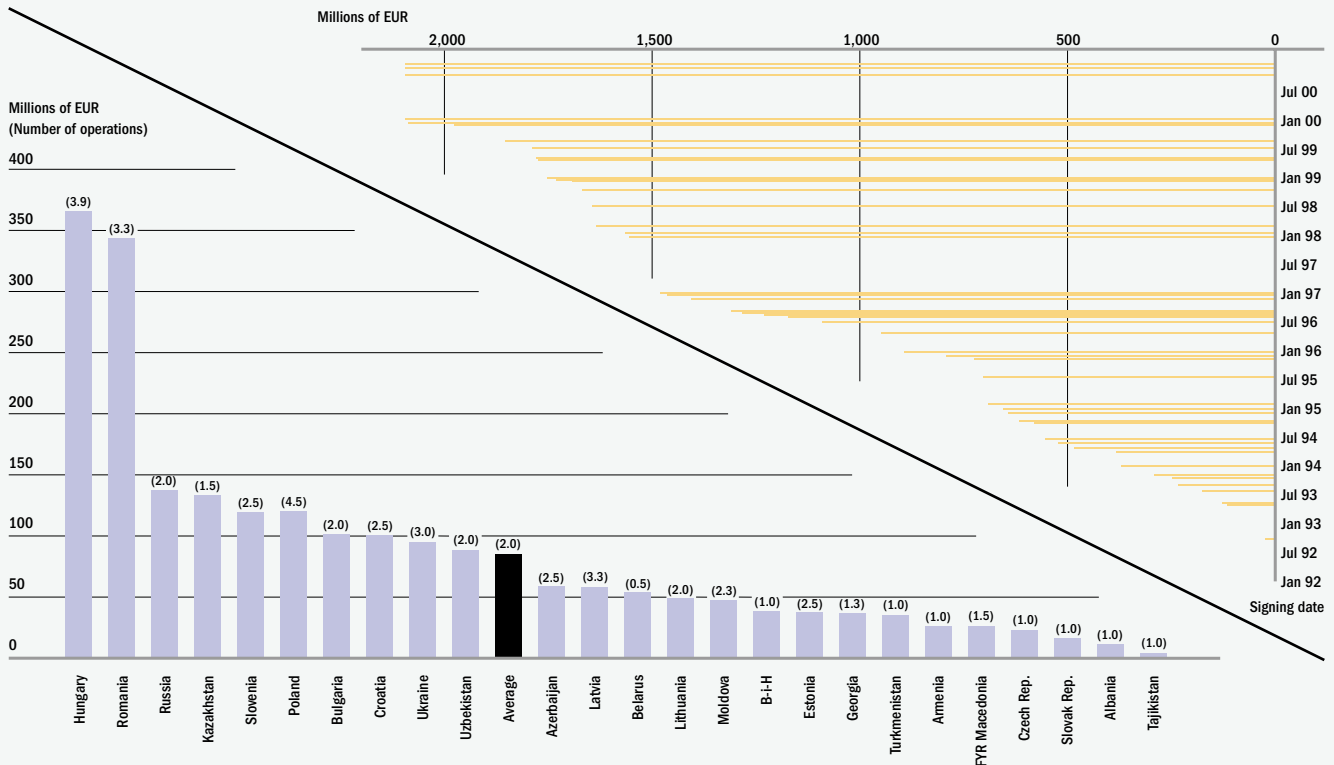
Ratings range from -1 (negative) to 3 (high)

Advanced Eastern Europe: Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia. South-Eastern Europe: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Romania. Western CIS: Belarus, Moldova, Ukraine. Southern CIS: Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Uzbekistan.

Bank's operations in the Transport sector

Chart 1

Total commitments by country and cumulative commitments by signing date



Notes: Vertical bars represent total commitments in each country. The number above the bars represents the number of operations; operations may be counted as fractional numbers if multiple sub-loans are grouped under one framework agreement. Horizontal lines represent cumulative commitments by signing date of each operation.

Chart 2

Regional breakdown of total commitments

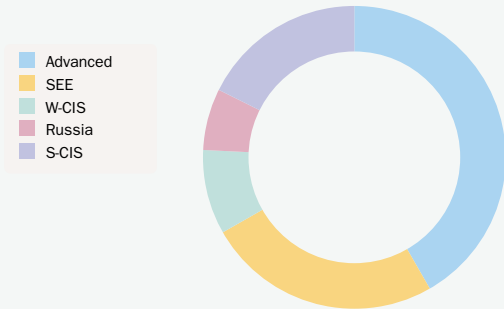


Chart 3

Sectoral breakdown of total commitments

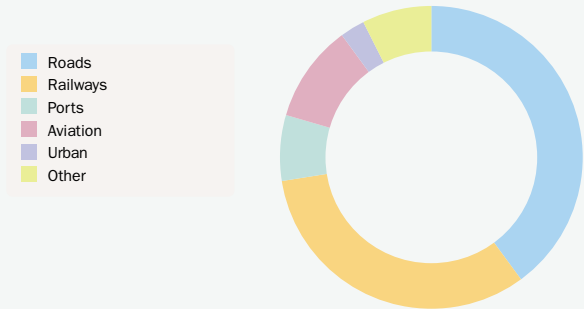


Table 1

Finance of EBRD operations

(% of EBRD equity and of EBRD private portfolio in total EBRD finance, mobilisation ratio)

	% equity	% private	% mobilisation
Advanced	0.5%	21%	489%
SEE	0%	2%	492%
W-CIS	1.5%	11%	178%
Russia	0%	0%	167%
S-CIS	0%	0%	159%
Regional	-	-	-
Total	0.3%	10%	381%

Table 2

PED transition impact ratings

(average transition impact rating and number of projects evaluated)

	average rating	# of projects
Advanced	1.83	6
SEE	3.00	1
W-CIS	2.00	2
Russia	2.00	1
S-CIS	3.00	1
Regional	-	0
Total	2.09	11

Ratings range from -1 (negative) to 3 (high)

Advanced Eastern Europe: Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia. South-Eastern Europe: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Romania. Western CIS: Belarus, Moldova, Ukraine. Southern CIS: Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Uzbekistan.

Annex 2: Transition impact at the project level

The EBRD's Project Evaluation Department has so far assessed 239 projects, or 72 per cent of completed operations. This is a sufficient number of evaluations to draw some preliminary conclusions about the factors and project characteristics that have, in the past, determined the Bank's transition success at the project level.

A statistical analysis – based on a binary regression (probit) model – was carried out to relate project transition impact ratings to a number of project characteristics. The analysis showed that among the most important factors to influence the likelihood of a successful project transition rating are:

- the country-level reform environment (measured as the country transition rating at the time of project approval)
- the project sector, and
- whether or not the project had a strategic foreign investor.

The following table shows estimates for the probability of a medium or high transition impact rating as a function of these project characteristics:

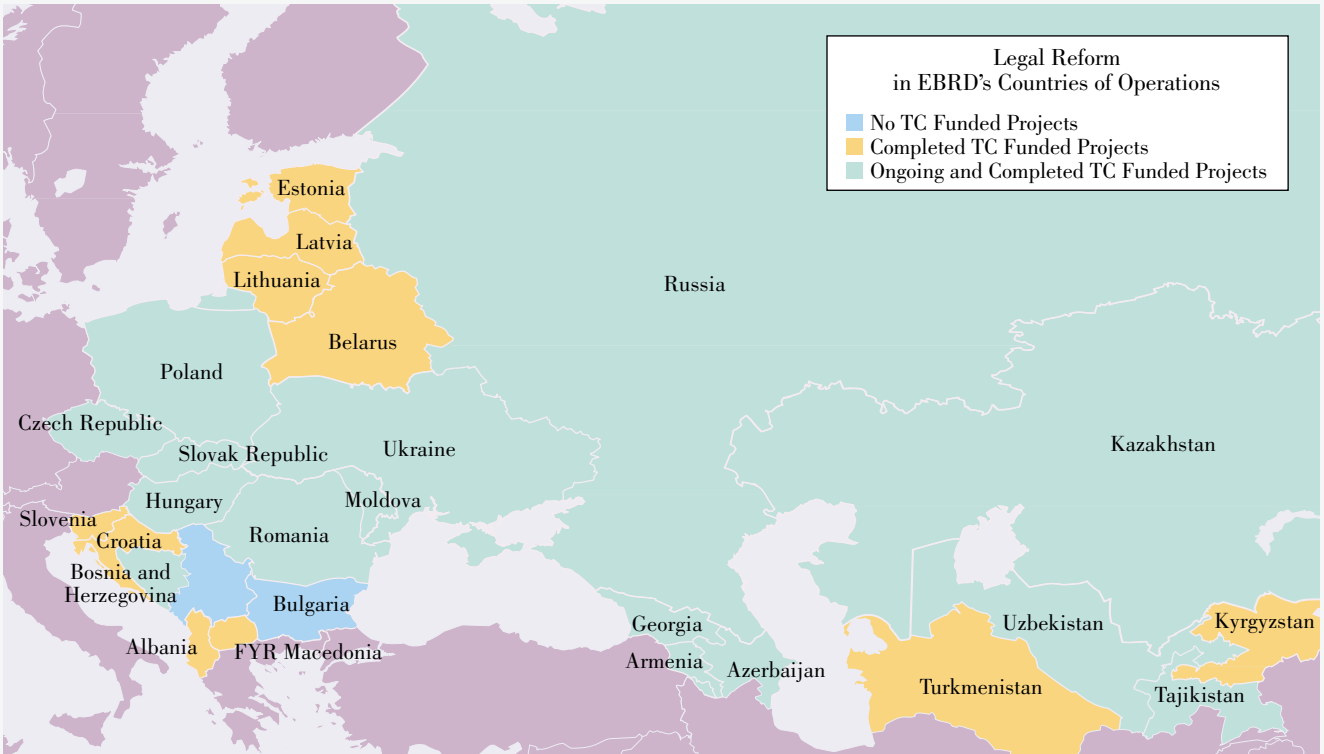
Project type	Country transition stage		
	Early	Intermediate	Advanced
	%	%	%
General Industry			
without strategic investor	14	19	24
with strategic investor	32	36	41
Infrastructure			
without strategic investor	31	35	40
with strategic investor	48	52	57
Financial Institutions			
without strategic investor	26	30	35
with strategic investor	43	47	52

Notes: The early, intermediate and advanced transition stages here refer to country transition ratings of 2.0, 2.6 and 3.3, respectively, using the methodology of the *Transition Report* (range of scores from 1 to 4).

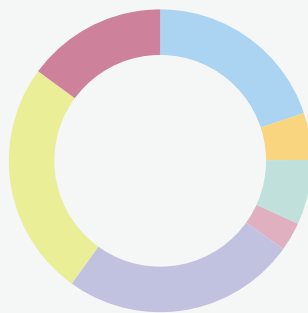
Annex 3: Legal transition assessment – event line and methodology

Legal transition impact assessment

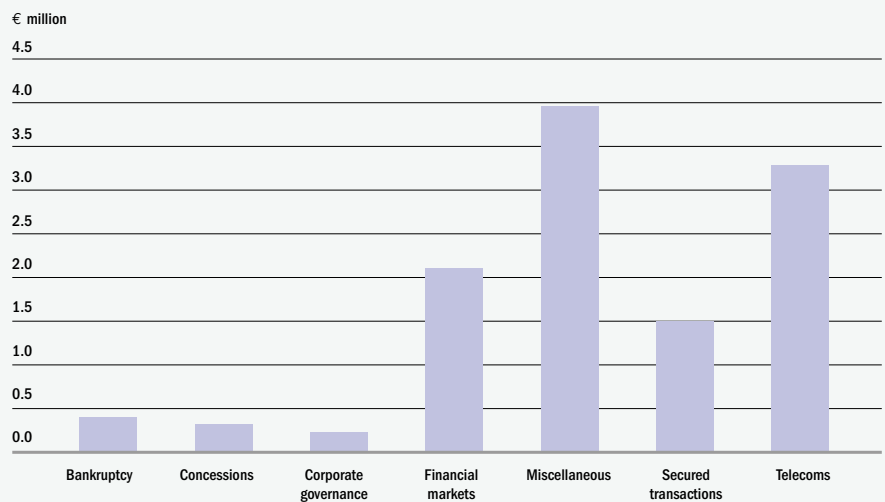
Legal transition statistics



Legal reform projects by focus area



TC funds committed to legal reform projects



Legal transition event line

In the transitional process from a command to a market economy and while developing a democratic political system, the EBRD's countries of operations must transform their legal system – laws and legal institutions – through a series of steps or “events”. These events include the adoption of a constitution, preparation of civil, penal and procedural codes, adoption of implementing laws, reorganisation of the judiciary, creation of effective implementing institutions and agencies, and their adoption of implementing regulations. Given its private sector mandate, the EBRD's Legal Transition Programme (LTP) has focused its activities on assisting the development of the commercial legal framework in the countries of operations.

A commercial legal “event line” is the sequence of changes that the Legal Transition Team has observed as countries build the legal and regulatory foundation for a functioning market economy. It should be noted that the events identified below often develop and evolve simultaneously and are interrelated. Each event itself contains a series of sub-steps that a country must go through and each event is subject to review and revision over time. The following commercial legal events are not necessarily in sequence:

- *Private property* – Legalisation of private ownership of both moveable and immovable property would typically develop through constitutional provisions, which would be further elaborated in specific laws, including mortgage and secured transaction laws. Development of registration systems for land and both moveable and immovable collateral would be needed.
- *Privatisation* – Privatisation of state-owned/state-run enterprises could be done on a sector basis and could require enterprise restructuring legislation to help create attractive candidates for private owners.
- *Competition law* – Competition rules and an independent competition authority are needed to supervise and ensure the fairness of the privatisation and liberalisation processes.

- *Central bank and banking system* – Creation of a two-tier banking system with a central or national bank as the first tier often with authority over both monetary policy and bank supervision. (Alternatively, an independent agency can take on the supervisory and regulatory functions.) The second tier would include privately owned banks. Bank privatisation and bank bankruptcy legislation may be required.
- *Company law/commercial codes* – Creation of new commercial entities through the adoption or revision of basic provisions in a civil or commercial code. Specific legislation could then be adopted for each commercial form with frequent amendments to provide for changing economic circumstances. Company registries also become necessary.
- *Taxation and accounting* – Creation and subsequent refinement of the tax system and the requirement that local companies follow internationally accepted rules and procedures for accounting and auditing.
- *Regulated industries* – The liberalisation and/or privatisation of state-owned utilities and state-run services will require specific laws as well as the creation of independent regulatory bodies. Often the regulatory function must go through a series of evolutionary steps before a truly independent regulator is established.
- *Concessions/private financing of infrastructure or services* – Legislation would be closely associated with the change in ownership structure of utilities and public services. This legislation could include a framework concessions law and/or a series of laws/regulations that govern different sectors (e.g., water, electricity, transport, etc.). Production Sharing Agreements would be included in this “event”. Public procurement legislation would also be needed to ensure transparency and fairness in the granting of concessions.
- *Insolvency/bankruptcy* – Legislation should provide for both liquidation and restructuring options and contain clear procedures for the initiation and

conclusion of bankruptcy cases. May require specialised courts or judges and the regulation of bankruptcy administrators or trustees. Legal framework should also create an environment conducive to workouts and consensual restructuring.

- *Capital markets* – Legislation that allows for and facilitates the establishment of efficient capital markets and the creation of independent bodies to regulate and supervise the markets. Could also include legislation creating an independent (possibly private) stock exchange.

Given the broad range of events that must take place in the development of an effective commercial legal system, the EBRD's LTP has focused its efforts on six legal sectors that are most relevant to the Bank's investment strategies and where the Bank has accumulated the most practical experience and expertise through its operations: (i) bankruptcy, (ii) company law and corporate governance, (iii) concessions, (iv) financial market regulation, (v) secured transactions, and (vi) telecommunications regulation.

Legal transition impact classifications

Categories used to measure transition impact intensity of the EBRD's legal transition activities are as follows:

Minimal: The project had little or no impact on the specific legal sector, despite the Bank's efforts. This category could include the following situations: (i) the client changed its priorities after the project was approved and requested legal assistance that the Bank could not provide; (ii) legislation was drafted but never adopted or put into force; (iii) the legislation was drafted but the comments were never taken into account in the final draft approved; (iv) the legislation was drafted and approved, but never implemented, (v) there was no transfer of know-how.

Moderate: The project had a moderate impact on legal transition. There was some transfer of know-how, and efforts were made to implement specific reforms but these were incomplete or unsuccessful. However, because of change in political

and/or economic circumstances or lack of cooperation on the part of the recipient country, the project did not attain its overall legal transition objectives.

Medium: Many of the project's objectives were attained. There was transfer of know-how, and initial efforts were made to implement legislative changes. The project had a noticeable effect in improving the overall legal framework in the specific legal sector.

Significant: The objectives of the project were fully attained, there was transfer of know-how to the recipient country, and the respective legal framework of the specific legal sector was substantially improved. In addition, implementation and/or enforcement efforts were effective, including the creation or modernisation of independent regulatory bodies and the training of regulatory staff and/or judges.

Overview of Bank's legal transition impact

Legal assessments and *Law in transition*

The EBRD undertakes other legal transition activities that are regional in nature and can have a more indirect, though still significant, impact on legal development in the Bank's countries of

operations. Included in this group of activities is the Bank's legal sector assessment work, including the Office of the General Counsel's (OGC's) annual Legal Indicator Survey of lawyers in the region (LIS), and the Bank's legal journal, *Law in transition*. While these activities are more difficult to assess on a country basis using the scale described above, the Legal Transition Team has a number of examples and experiences where these legal transition activities have led to positive transition outcomes in the Bank's countries of operations.

Legal sector assessments benchmark the development of key commercial law sectors in each country against international standards, providing a clear analysis of the gaps in the existing legislative framework. As a complement to these assessments the LIS provides a snapshot of how lawyers practising in the region perceive the extensiveness and implementation of commercial and financial laws and regulations. Taken together, the sector assessments and the LIS results provide the transition countries (and legal assistance providers) with information to identify legal reform opportunities. This analysis can be used by the transition countries to undertake reform efforts on their own or with the assistance of others.

Legal reformers in a number of countries have already used the results of the LIS, published in each *Law in transition* and *Transition Report* since 1995. For example, following publication of the LIS insolvency results, the Hungarian Bankruptcy Association contacted the Bank to discuss future reform efforts and the Supreme Arbitrage Court of Belarus provided OGC with an unsolicited article highlighting the recent changes in the Belarus bankruptcy law. (Belarus was rated as "inadequate" in the 1999 LIS.) Following the publication of OGC's Regional Survey of Secured Transactions Laws (a legal sector assessment) in *Law in transition* and on the EBRD's Web site, the Czech Government expressed interest in starting a secured transaction legal reform project that had been stalled for some time. (The Czech Republic was rated as "unreformed" in the Regional Survey.)

Law in transition, the EBRD's legal journal, serves as a key tool to promote legal transition in the Bank's countries of operations. The OGC produces *Law in transition* twice a year, in English and Russian. The journal provides information, analysis and criticism to those people directly involved in the legal transition process – government officials, parliamentarians, judicial officials – as well as lawyers, consultants and donors providing legal reform assistance. Each issue of the journal features a specific topic of legal reform and a number of general articles as well as updates on legal developments and events in the region. *Law in transition* is distributed free to over 4,000 people with additional copies provided to the Resident Offices for further distribution. In addition to the reactions to the publication of assessments in *Law in transition* described above, OGC has received numerous comments on the journal as well as unsolicited articles from lawyers in the EBRD's countries of operations that seek to describe existing legal problems or ongoing legal reform efforts. In just two years since it was published in its expanded form, *Law in transition* has become recognised as one of the leading legal journals on transition countries.

Table 1

Legal transition impact intensity – legal reform projects

	Minimal	Moderate	Medium	Significant
Bankruptcy Law	Kyrgyzstan		Regional Project	Azerbaijan Russia
Concessions		Poland Romania	FYR Macedonia	
Corporate Governance		Regional Project		
Financial Markets		Regional Projects		Czech Republic Russia
Secured Transactions		Kyrgyzstan Tajikistan	Azerbaijan Moldova	Hungary
Telecommunications	Ukraine		Albania Belarus Poland	Bosnia and Herzegovina Lithuania
Miscellaneous (arbitration, foreign investments law, subsoil law and training)		Slovenia Uzbekistan	Azerbaijan Kyrgyzstan Regional Training Project	Turkmenistan

Albania: Medium

The EBRD has had an important impact in the reform of the legal framework in the telecommunications sector in Albania. The Bank has completed three projects in this sector, two of which have been very successful. The projects enabled the adoption of a new sector policy, facilitated the award of licences to the main operators, assisted in the drafting of a new telecommunications law and prepared tender documents for the award of the second GSM licence. This assistance has recently led to a very successful bidding process for the second GSM licence in the country, with bid offers exceeding all expectations.

Azerbaijan: Medium

The impact of the EBRD in the development of the legal framework of Azerbaijan has been considerable. The Bank has been involved in three projects. One of these led to the reform of the bankruptcy law and influenced considerably the investment climate in the country. Through the secured transactions project the Model Law on Secured Transactions was largely publicised in the country and the new Law on Pledge introduced some of the features promoted by the Bank. However, implementation remained a problem. Similarly, another project focused on reforming foreign investment protection legislation and resulted in a transfer of know-how to the client, but did not lead to effective changes to the legal system.

Armenia: None

The Bank has an ongoing project in the telecommunications sector.

Belarus: Medium

The EBRD has completed phase one of a project on the reform of the telecommunications sector in the country. This project had a considerable impact. With the Bank's assistance, negotiations between the Belarussian authorities and the successful bidder were completed and the award of the GSM licence to a privately held company became possible. In addition the Bank's assisted in the preparation of a new telecommunications law.

Bosnia and Herzegovina: Significant

The Bank has completed three projects on the reform of the telecommunications sector in the country. The two latest projects have been very successful. The first of these projects led to the adoption of a Memorandum of Understanding among the two Entities and state government, which opened up a dialogue among the various parties. The second project led to the adoption of the State Telecommunications law, the establishment of the Independent Regulatory Agency, the drafting and award of the international licences as well as the drafting and adoption of the tariff policy.

Bulgaria: None

The Bank has had no involvement in the country's legal transition.

Croatia: None

The Bank has had no involvement in the country's legal transition.

Czech Republic: Significant

The EBRD has had a major impact in the reform of the financial markets legislation in the Czech Republic. The Bank assisted in the development of the Czech Securities Commission, through proposing amendments to the securities legislation, which were enacted in 2000. In addition, the project assisted with the establishment of the Securities Commission and training for senior officers and other Commission staff.

Estonia: None

There has been one project on telecommunications reform, which was completed in 1996 and was not evaluated.

FYR Macedonia: Medium

The EBRD has completed a project on the reform of the Energy and Concession Law. The proposed amendments to the law were fully endorsed and accepted by the legislature. The new concessions and energy regime in the country has been an important factor in the improvement of the investment climate.

Georgia: None

The Bank has an ongoing legal reform project in the country, in the telecommunications sector.

Hungary: Significant

The EBRD has completed two projects on the implementation of secured transactions legislation in the country. These focused on assisting with the registration of moveable assets and were very successful. Following the Bank's assistance, a well-functioning central registry entered in operation. The system has operated successfully since 1997 and is widely seen as a model for other countries in the region. The Bank also assisted in identifying ongoing implementation issues and suggested amendments to the Civil Code to address these. Following lengthy discussions a set of amendments to the Civil Code were recently presented to Parliament.

Kazakhstan: None

The Bank has an ongoing legal reform project in the country, in the telecommunications sector.

Kyrgyzstan: Moderate/Medium

The Bank has completed two legal reform projects in the country. One of them, on the implementation of commercial arbitration law, has been on hold within the Kyrgyz Government. However, as a result of this project Kyrgyzstan signed the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, which permits the enforcement of foreign arbitral awards in Kyrgyz courts. Plans to adopt implementing legislation based in the UNCITRAL model law have been put on hold. The Bank's second legal reform project focused on bankruptcy reform. While the Bank provided comments to improve the Kyrgyz bankruptcy law, the Kyrgyz Government has not followed up to implement these suggestions.

Latvia: None

The Bank has one ongoing legal reform project to assist in the development of the secured transaction law and registration system.

Lithuania: Significant

The EBRD has had a major impact on the reform of the telecommunications regulatory framework in the country. The Bank's legal reform project led to the adoption of a new telecommunications sector policy and the liberalisation of the sector.

Moldova: Medium

The EBRD has completed a project on the reform of the secured transactions legal regime in the country. The Bank, in cooperation with the German assistance agency, GTZ, assisted with the drafting of a new Pledge Law, which was later enacted. The new law draws on the EBRD Model Law on Secured Transactions and provides a basic legal framework for secured credit. However, the final draft of the law included some less-than-satisfactory provisions.

Poland: Moderate/Medium

The EBRD has completed two legal reform projects in Poland. One of the projects consisted in analysing municipal public-private partnerships legislation in the country. Although the analysis of the legislation was completed, this was not reflected in any changes in the legislation. As a result the impact of the project in the country was moderate. The second project consisted in developing a programme for the telecommunications sector and helped the Polish Government establish an independent telecommunications regulatory body and harmonise the telecommunications regulatory framework with EU rules. The project had considerable impact in the country.

Regional Training Projects: Moderate/Medium

The EBRD has completed three regional legal reform projects covering legal training, corporate governance and insolvency. The first regional project provided training on commercial law issues for private practitioners, judges and government officials. The seminars and training were effective in transferring legal know-how and international best practices in a number of legal areas. In the second regional project, the Bank commissioned a study and assessment of the corporate governance practices in a number of its countries of operations. While this study

was quite comprehensive and included a number of recommendations for revisions in laws and corporate practices, it has not influenced change in the countries. The final regional project was an insolvency conference organised in conjunction with the World Bank's initiative to develop international principles of insolvency law and practice. The conference brought together insolvency practitioners, government officials, judges and lawyers to discuss the proposed principles and reform experiences. The conference was quite successful in transferring know-how and eliciting transition country input on the development of the international principles.

Romania: Moderate

The EBRD has completed one legal reform project that entailed analysis of the municipal public-private partnerships legislation in the country. The analysis of the legislation was completed and there was transfer of know-how. However the project did not lead to changes in the legislation and its impact was moderate.

Russian Federation: Significant

The EBRD has undertaken a series of projects aiming to reform the laws regulating legal entities and the securities markets. These projects have been very successful: a number of amendments proposed under the projects have been approved by the full Parliament, while others have been approved by the Duma and await enactment. In addition, the projects developed concept papers analysing securities legislation issues which have been approved by the Russian Securities Commission. The Bank also has ongoing projects focusing on improving corporate governance practices in Russia.

Slovak Republic: None

The Bank has an ongoing secured transactions reform project in the Slovak Republic.

Slovenia: Moderate

The EBRD has completed a project that entailed drafting a foreign investment law. The draft law was prepared but its suggestions were not fully taken into account by the legislature and therefore had only moderate impact. The Bank also has an ongoing project to develop a framework concessions law in Slovenia.

Tajikistan: Moderate

The EBRD completed a project on the development of a secured transactions law. The Bank produced an extensive analysis of existing laws in order to assist in identifying the necessary reforms and the best ways of implementing them. While accepting the Bank's assessment, the Tajik Government has not made progress on reforming the secured transactions law.

Turkmenistan: Significant

The Bank completed a project on the reform of the taxation, accounting and investment related laws in the country. The project was very successful and led to the amendment of the taxation legislation and the effective implementation of the revised tax law.

Ukraine: Minimal

The EBRD developed a project on the telecommunications sector in Ukraine in 1995, which was related to a potential Bank investments in the country. However, the project did not have an impact because of the lack of transparency in the development of the investment project and lack of political will. The Bank has an ongoing telecommunications regulatory reform project in Ukraine, which has the full backing of the Ukrainian Government.

Uzbekistan: None

The Bank is currently involved in a leasing law project.

Annex 4: Environmental compliance – lessons learned

Features of successful projects

Quality of sponsor

In large environmentally sensitive projects it has been very advantageous to involve a financially and technologically strong and committed foreign sponsor in order to meet the environmental objectives of the project. Good process and environmental technology transfer creates a sustainable basis for competitive and environmentally sound production.

Due diligence

The projects involving industrial restructuring often have a high potential for positive environmental change. Strategic options of how to achieve the greatest environmental benefit need to be assessed as part of the Environmental Due Diligence (EDD). The restructuring of the company, often separating the new core business from outdated production processes, can safeguard the sustainability of the project from a financial and environmental point of view. A thorough EDD, including identification of key environmental risks and liabilities, has usually contributed to greater confidence on the part of potential foreign strategic investors.

Scope of involvement

Environmental change can be realised both directly, through the environmental measures defined in the Environmental Action Plan, and indirectly through measures aimed at production and quality improvements which also result in environmental improvements. When a project involves the streamlining of products and production processes, any potentially adverse environmental effects of the products have to be taken into account. Expansion of production often increases the material flow and may entail increased waste streams. Assessing the economic and environmental benefits of recycling, recovery of waste materials and cleaner production measures has been a standard part of EDD in environmentally successful projects.

Environmental management

Strengthening of environmental management has been an important part of sustainable institutional development. Comprehensive and well designed environmental management systems (EMS), often based on ISO 14001, can improve environmental risk management and performance. A certified EMS also achieves positive marketing value, particularly in export markets. Training of staff in environmental management in the early stage of projects develops understanding, and helps set environmental objectives and the management of environmental change.

Public participation

Establishing public information for large environmentally and socially sensitive projects has been a key element in improving the dissemination of environmental information and creating a productive cooperation between the Bank, sponsors, NGOs, the general public and the regulatory authorities. It has been very important to select a neutral and communications-adept coordinator for such public fora in order to avoid disputes between parties.

Cooperation with authorities

Joint discussions with environmental authorities and sponsors after setting the principal environmental objectives of the project have been an effective tool to promote mutual understanding of project-based environmental priorities and to obtain information on the objectives of the authorities.

Backward linkages

Local pollution control technologies have been actively sought in environmentally successful projects in the search for economically and technically viable solutions. This has also been justified from the point of view of developing the domestic pollution control equipment industry.

Features of less successful projects

Quality of sponsor

In general, projects starting from a low level of environmental performance require a strong and committed international partner to be successful. It is very important that sponsors are committed to the environmental objectives sought by the EBRD and sign up to the environmental objectives, reporting requirements, and standards in the project agreement. A common feature in some unsatisfactory projects is that there are cultural and institutional constraints in committing to health and safety programmes, to the environmental action plan and to continuously develop good operational and housekeeping procedures.

Due diligence

In some unsatisfactory projects investment decisions were based on too vague a technical analysis. This often leads to the underestimation of costs, frequent changes in the investment programme and, on industrial projects, lack of knowledge of the interrelationships between different process components. Sufficient time and funding needs to be allocated for the feasibility study, which should contain reliable investment and operation cost estimates.

Monitoring

Environmental monitoring capacity was often insufficient in unsuccessful projects. Setting and monitoring environmental targets must be based on reliable and quantitative monitoring data in order to motivate management and operators to continuously improve their environmental performance. Environmental milestones and performance indicators need to be agreed in advance and performance should be duly documented. Key environmental requirements identified during EDD should be included in the conditions of completion for added leverage.

Cooperation with authorities

A feature in some unsatisfactory projects is insufficient communication with the environmental, health and safety authorities. The authorities should be consulted in the early stages of project development. Regulatory environmental, health and safety requirements need to be identified for all projects, regardless of the project sponsor's identity or corporate programmes.

Cooperation with co-financiers

Some projects failed because there was no clear lead organisation among the involved financiers. The issue is particularly prevalent if co-financiers have different environmental requirements. Coherence in responsibilities and reporting between IFIs on co-financed projects is essential and is a topic which is being addressed by the IFIs. On co-financed projects the participating IFIs should, wherever possible, specify identical documentation requirements regarding environmental matters.

Commitment of project team

There is a need for project teams to take "ownership" of the environmental aspects of their projects throughout the project cycle. Project teams, in collaboration with EAU, should ensure that all sponsors, including large international sponsors, provide appropriate information throughout the Bank's involvement in their projects.

Proactive identification of opportunities

No systematic effort is generally made to seek out investments with a high potential for positive environmental impact. A special PED study on environmentally significant sectors concluded that the proactive development of environmentally beneficial projects would need more resources for the development of new approaches to complement the present mode of operation.

