

# **Privatisation of municipal heating plants**

## **Summary of the Operation Performance Evaluation Review**

### **April 2006**

#### **THE PROJECT**

The project loan was approved by the Board in 2000. Prior to the EBRD's involvement, a commercial bank was providing bridge financing. (This was restructured as part of the project.) As the other bank was unable to provide additional finance, the EBRD was brought in to enable expansion into the district heating market.

#### **PROJECT RATIONALE**

The Bank's rationale for participation in this project was predicated initially on the government's decision to privatise municipal district heating plants. The Bank's objective was to help increase private participation in this process, to improve plant efficiency through skills transfer, plant upgrades and effective management, and provide a demonstration effect by increasing participation of local banks in the sector.

#### **ACHIEVEMENT OF OBJECTIVES**

The project had the following objectives:

- to enable the project entity to rent, refurbish and manage selected district heating plants (*Fully accomplished*)
- to further private sector participation in the financing and operation of municipal district heating (*Fully accomplished*)
- to further improve environmental quality by achieving EU emissions standards for these plants (*Fully accomplished*)

#### **OVERALL ASSESSMENT**

The Bank's operation, overall, is rated ***Highly Successful***. This rating reflects the fact that the project has accomplished what it set out to do – provide district heating services to communities in secondary cities and smaller towns, via the private sector, based on efficient operations which set high environmental standards and offer a reliable service at an affordable price. It has contributed to the successful transition of district heating services from municipal and state ownership to public-private partnerships and has rehabilitated the plants it operates and converted several to gas. Finally, its plants have performed well, providing a very reliable service to its customers.

The Bank's additionality is *Verified in all respects*. Transition impact is rated *Excellent*. Environmental performance under this project, based on the performance of the individual subprojects, is rated *Excellent*. Environmental change is rated *Outstanding*. Project objectives have been fully implemented under this project and achievement of objectives is rated as *Excellent*. The project's financial performance is *Good*. Bank handling is also rated *Excellent*.

The project is in full compliance with the Bank's Municipal and Environmental Infrastructure Policy, the Energy Operations Policy, the Bank's Environmental Policy, and the country strategy. This project is highly relevant; it serves secondary cities and towns providing a vital public good – district heating – on a competitive private sector basis.

#### **MAIN OPER ISSUES AND LESSONS LEARNED**

**Strong regulators lead to less corruption.** Strong and transparent regulators lead to less corruption and an even playing field that allows for fair competition under known rules, leading to the best outcome for the consumer and acceptable terms for the private sector.

**The Bank should clarify the information it seeks in annual environmental reports and only ask for what is needed.** The Bank does not need annual environmental reporting from all clients. It is more useful to understand the project - “know your client” - and tailor environmental and other reporting to key project stages. Specifically, environmental reporting for this project would be most useful if the Bank received “before” and “after” emissions reports for each subproject which would allow the Bank to access the environmental footprint of the project.

**The initial wave of privatisation is not the EBRD’s only chance to enter a market.** Privatisation may occur in multiple phases – in this case, major cities, followed by secondary cities, followed by consolidation. Each phase is an important step in transition and each presents a different set of opportunities in which the EBRD may participate. The Bank was able to participate in the second phase even though it missed the first phase.

**Strong sponsors are equally important in mature markets.** The success of this project and the EBRD’s ability to enter into a maturing market (second phase transition) was built on the strength of a strong sponsor committed and willing to take a long-term view. The sponsor’s excellent corporate governance standards and proven managerial skills ensured the success of this project.

**Strong project management in selecting and implementing the right engineering design is key to success.** The success of this project was partly based on the strong technical experience of the parent company/client and their ability to make the right technical decisions (plant conversions versus rehabilitation) and to implement those decisions (re-engineering of existing plants and distribution systems) through effective engineering project management. This company’s plants were all well designed, maintained and operated.