RECENT ECONOMIC AND SECTORAL DEVELOPMENTS

Growth and External Performance

Serbia’s economy moved back into a recession in 2014, primarily as a result of the May 2014 floods. The contraction in activity moderated in the fourth quarter of the year to 1.8 percent (year-on-year), leading to an estimated annual decline in real GDP of 1.8 percent (year-on-year) in 2014. A drop in private consumption and private investment contributed to almost all of the contraction in activity in 2014. Although exports still contributed positively to growth, their weakening performance was offset by imports, resulting in a small negative net contribution of external demand to growth. On the production side, agriculture and some services helped to limit the depth of the recession. However, industrial output fell by 6.5 percent in 2014, with the energy sector particularly hit by the floods.

External balances also remain under pressure. The current account deficit in 2014 remained around 6 percent of GDP; even though the goods and services deficit decreased slightly, other components of the current account deteriorated. Most importantly, remittances decreased by almost 13 percent. Nearly two-thirds of the current account deficit was financed through foreign direct investment (FDI), which reached €1.2 billion. The dinar depreciated 2 percent against the euro in the fourth quarter of the year, despite heavy intervention by the National Bank of Serbia (NBS) in the foreign exchange market that led to a reduction in official reserves of 11 percent in 2014.

Inflation remained subdued throughout 2014, averaging around 2 percent (year-on-year) since March 2014, well below the inflation target range of 4±1.5 percent. This is primarily the result of low food prices in the first half of 2014 and the absence of adjustments on administratively controlled prices in the second half of the year. Core inflation averaged 0.5 percent in 2014.

Public finances are still under pressure, although some difficult measures were introduced in 2014. The Government introduced a hiring freeze and a reduction in public sector wages and pensions, but that was not sufficient to prevent an increase in the fiscal deficit in 2014. The expenditure slippages, including called guarantees, in the fourth quarter particularly contributed to the 2014 fiscal deficit, which widened to 6.7 percent of GDP (up from 5.6 percent in 2013). Central government debt (including guarantees) amounted to 69 percent of GDP at end-2014. Fiscal consolidation will be the focus of the recently approved International Monetary Fund (IMF) program.

Despite recent improvements, unemployment rates remain high, particularly among the youth. Unemployment (among those 15 years and older) increased from 13.6 percent in 2008 to a peak of 23.9 percent in 2012. As the pace of economic contraction moderated throughout 2014, the unemployment rate declined to 16.8 percent in the fourth quarter of the year. However, only two-thirds of the improvement in 2014 was the result of increased employment; the rest was due to an increase in the inactive population and a declining labor force participation rate. Unemployment remains particularly high among the youth at 47 percent.

Fiscal Performance

The fiscal deficit in 2014 is estimated to have remained high at 6.7 percent of GDP (including amortization of called guarantees). Expenditures went up in 2014 to reach 46.6 percent of GDP, a significant increase compared to the 2013 level of public expenditures (43.5 percent of GDP). Most of the fiscal slippage happened in the last quarter of 2014, when the support to state-owned enterprises (SOEs), including subsidies, net lending, and activated guarantees, increased significantly, more than offsetting improved revenue performance in the same quarter. Public debt (including guarantees) reached 71 percent of GDP at end-2014.

The 2015 budget approved by Parliament in December 2014 targets a deficit reduction of 0.7
percentage points of GDP relative to 2014. Around four-fifths of the adjustment is planned to come from higher revenues (primarily from the additional taxation of wages in the public sector), while most of the relatively limited expenditure savings are from a lower wage bill and reduced subsidies. Importantly, however, the budget sets out a policy of no longer issuing new guarantees to cover SOE losses. According to the fiscal strategy, the consolidated fiscal deficit is expected to decline to 3.8 percent of GDP by 2017, thereby bringing public debt into a declining trajectory.

Public Financial Management

Reforms led to the strengthening of a number of public financial management (PFM) dimensions. Notable improvements have been made in the effectiveness of the treasury system, including the establishment of improved financial control and accountability arrangements and increased transparency in public finances. The Government brought into the budget and/or closed a number of extra budgetary funds; brought on and consolidated the Treasury own revenues that had previously been at the disposal of different government institutions; and made a significant effort to eliminate arrears in the public sector (in particular in health, roads, and local governments) by introducing a new law on payment deadlines and a new system of commitment control within the Treasury. Public Internal Financial Control (PIFC), established by provisions of the Budget System Law, continued to develop in both internal audit and at a slower rate of financial management and control. The State Audit Institution (SAI) is on a constant path to increase its capacity and coverage of audited public funds and to improve its methodology and the types of audits it performs. The new Public Procurement Law of April 1, 2013, represents a step toward conformity with European Union (EU) standards and has also brought about visible results and progress in the area of economy and efficiency.

An unaffordable public sector wage bill is a pressing problem for the Government. The general government wage bill has grown significantly in recent years and now accounts for nearly 30 percent of total public expenditure and over 11 percent of GDP. The onset of severe fiscal pressures following the global economic crisis has forced the Government to take extraordinary measures to reduce expenditures, including the wage bill. A hiring freeze1 was imposed in 2013, the indexation formula was scaled down, a ceiling on maximum public salaries was legislated, and the number of contract employees that a ministry or agency could hire was limited to 10 percent of its total staff. In addition, in late 2014, the Government passed a law that calls for a 10 percent reduction in all salaries in the public sector above RSD 25,000. The same law envisages a 10 percent cut in pensions in Serbia.

In order to address this issue, the Ministry of Finance created a Registry of Employees in the Public Sector, which contains information about 750,000 employees. In addition to this registry, the Ministry of Finance, together with the Ministry of Public Administration and Local Self Government, plans to update the Registry of Institutions in the Public Sector.

Figure 2. Public Debt as % of GDP

Financial Sector

The banking sector in Serbia is relatively stable, but weak credit growth hampers economic recovery. Serbian banks are in general well capitalized, with capital ratios that exceed 20 percent. They are also liquid, with the ratio of core liquid assets to total assets also over 20 percent. The banks are thus well positioned to deal with shocks. The Serbian banking sector is dominated by subsidiaries of banks headquartered in the EU, which hold about 75 percent of the market. The deleveraging process

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1 The Government of Serbia introduced a 1:5 replacement ratio in the public sector (for every five employees who leave the public sector, one employee may be hired).
started in the beginning of 2014, with foreign banks reducing their exposure to the country from about 44 percent of GDP in the beginning of year to 38 percent in the third quarter.

**Although the system is relatively healthy, financial intermediation is low, and credit growth has stagnated since 2012.** Financial intermediation in Serbia is lower than in most other countries in the Western Balkans, with the private sector credit-to-GDP ratio accounting for about 52 percent in 2014. Bank lending to the private sector was stagnant in 2012, then fell to negative numbers starting in April 2013. The slowdown in credit growth has particularly hit corporations; growth to that sector is still negative and well below the levels seen in early 2012. Growth in household credit was only 5 percent in August 2014 compared to about 14 percent in August 2012 (figure 3).

**Figure 3. Credit Growth by Sector, Percent**

High and rising levels of nonperforming loans (NPLs) are a major constraint for credit growth. Serbian banks have the second-highest level of NPLs in the Western Balkans. The NPLs to total loans ratio increased from 21.4 percent in 2013 to 23 percent as of June 2014 (figure 4). A major driving force of NPLs, which is also a serious credit risk for banks, is the high volume of foreign exchange lending, with about 70 percent of loans denominated in a foreign currency. Although bank loan loss provisioning is among the highest in the region, it should be interpreted in light of the NBS’ recent loosening of classification requirements, which now allow banks to understate the level of problem loans. Thus, actual NPL levels are probably higher than reported in official statistics.

**Banks are more cautious about lending and interest rates are high.** Banking sector profitability, as measured by return on assets, is still weak at 1.1 percent as of June 2014 and has not reached its pre-2008 financial crisis level. Poor profitability, combined with high levels of NPLs and foreign exchange lending, increases bank exposure to credit losses. Serbian interest rates are relatively high compared to other Western Balkan countries. This is driven by the significant credit risk that banks are facing, as well as high NPLs and the stricter prudential policies that have been put in place to maintain stability. This has further decreased access to credit for both corporations and households.

**Figure 4. Nonperforming Loans and their Provisioning**

At the moment the banking system is adequately capitalized as a whole, the performance of state-owned banks remains weak. In 2012 and 2013, three small banks in which the state had an ownership stake (Agrobanka, RBV, and PBB) and one private bank (Univerzal) failed, mainly because of governance weaknesses that led to a significant deterioration in asset quality. The bank failures raised concerns—particularly about the quality of the assets in some other state-owned banks, the effectiveness of governance and oversight, and the bank resolution process.
framework, including the limited resolution options and poor communication between the NBS and the entity responsible for bank resolution, the Deposit Insurance Agency (DIA)—all of which need to be systematically addressed.

The World Bank is financing a project to strengthen the Deposit Insurance Agency (DIA). The DIA is a critical source of financial stability in Serbia, as it provides coverage for insured deposits of up to €50,000 and also takes the lead on bank resolution.

**Business Environment**

Despite improvements, the private sector in Serbia is still relatively underdeveloped and uncompetitive. Less than one-quarter of the working-age population has a job in the formal private sector. Exports have recently been growing rapidly, but they still remain at less than 40 percent of GDP, while in more successful new EU member states this ratio is twice as high.

**Doing Business 2015** ranked Serbia 91st out of 189 economies in terms of ease of doing business, well below most regional peers. This represents a drop of 14 places compared to the previous report. There was a modest drop in distance to frontier, from 63.46 percent in 2014 to 62.57 percent in 2015, so the drop in ranking was due largely to the fact that other countries improved more than Serbia, rather than that Serbia backtracked on reforms. Nevertheless, Serbia still ranks below what its GDP per capita would suggest and below most of its regional competitors; it is ranked only 20th out of the 26 Europe and Central Asia (ECA) countries, for example. In the 2015 ranking, particularly problematic areas are the process of securing construction permits, with Serbia ranked in the bottom 10 countries of the world, and procedures related to paying taxes, a proxy for overall regulatory and red tape burdens. Enforcing contracts is also a weak spot (Serbia ranks 21st out of 26 ECA countries). In the latest *Global Competitiveness Report* (GCR), Serbia ranks 101st out of 148 countries.

The new Government recognizes the need to improve Serbia’s business environment and is implementing concrete steps. The New Law on Construction and Planning was adopted in February 2015, and its implementation should streamline the process of issuing construction permits. One of the key issues identified by investors and employers is the rigidities in the labor market, which the new Labor Law adopted in July 2014 aims to address. In particular, the new law will make it easier to hire and fire employees and will also reduce some of the administrative burdens related to employment. Amendments to the Bankruptcy Law (adopted in August) will improve the efficiency of enforcement and reduce the scope for abuse by better defining various procedures and introducing deadlines to reduce implementation delays. The new Privatization Law, also adopted in August last year, is aiming to unlock the privatization process that has ground to a halt in recent years by increasing flexibility and introducing clear deadlines for the completion of the process. The authorities are also finalizing the new umbrella Law on Inspections, expected to be adopted by summer 2015. Finally, the Government has established a high-level working group (led by the Deputy Prime Minister and co-chaired by the Minister of Finance and the Minister of Economy) tasked with addressing *Doing Business*–related reforms. The working group is developing a cross-ministerial action plan and is consulting closely with the private sector. These activities are expected to result in improvements in the business environment and in improved *Doing Business* rankings in the next couple of years.

**Poverty and Social Protection**

The recent downward trend in the incidence of poverty in Serbia was reversed in 2009 by the financial crisis. Official data for measuring absolute poverty up until 2010 indicate that poverty had
increased to well above its precrisis level. As the basis for Serbia’s poverty measurement from 2012 onward, the Statistical Office introduced the Survey of Income and Living Conditions (SILC), which is used in EU member states to monitor poverty. The first round of SILC was conducted in 2013 with Instrument for Pre-Accession Assistance (IPA) funding and under the supervision of the World Bank. Based on this survey, the latest official poverty rate—defined as the fraction of the population living below 60 percent of the median income—was estimated at 24.6 percent. A second round of SILC has been carried out, and results will be available in the coming months. The SILC and EU methodology for measuring poverty is not comparable to the data and methodology used previously, so it is not possible to have a final assessment of recent poverty trends. Nevertheless, poverty estimates based on macroeconomic and labor market indicators suggest that poverty remains persistently higher than its precrisis level, and that it has increased since 2010. Despite the measurement uncertainties, it is clear that one of the largest minorities in Serbia, the Roma population, is also among the most vulnerable. Around 30 percent of Roma face absolute income-based poverty, compared to 8 percent among the mainstream population.

The social assistance reforms introduced by the Government were designed to mitigate the poverty impact of the crisis, as they aimed to increase access to means-tested programs, which are small relative to other programs (0.4 percent of GDP). The largest of them, Financial Social Assistance (FSA), formerly known as MOP (Material Support for Families), reaches only a fraction of the poor. Following the adoption of the New Social Welfare Law in 2011, the spending on FSA increased to 0.34 percent of GDP, but this is still below the regional average of 0.5 percent of GDP.

FSA coverage is still low despite recent reforms for expansion. The adoption of the Social Welfare Law has resulted in an expansion of FSA, as evidenced by a 30 percent increase in the number of beneficiaries. However FSA still doesn’t provide sufficient coverage, as only 11 percent of the poorest quintile receive it. The low coverage of FSA is potentially due to the additional conditions of the means/asset-test (in addition to the income test). In fact, the eligibility threshold is well below the income of the bottom decile, which helps in achieving good targeting but also limits the coverage.

A recent World Bank note on labor activation provides entry points to address the broader social safety net and activation agenda in Serbia. These involve introducing income disregards in social benefit design, promoting stronger coordination between employment services and social welfare centers, and profiling social assistance beneficiaries to link them with targeted activation programs.

Labor

Recent developments in the Serbian labor market give reason to be hopeful about the beginning of a jobs recovery. The unemployment rate dropped to 20.3 percent in the second quarter of 2014 (down from a peak of 25.5 during the crisis), while at the same time labor force participation (49.6 percent, up from 46.1 percent) and employment rates (39.5 percent, up from 34.3 percent) improved. However, these labor market improvements seem to be driven by an increase in informal employment. After a decrease in informal employment during the recession, informality rates are now rapidly increasing, from 18.2 to 21.2 percent in just one year. Overall, Serbia’s challenges in the labor market remain stark. The main challenge is to create more formal jobs for the transition generation—born 1975 or earlier—before they are too old to work, while at the same time ensuring that the young have the right skills for the jobs of the future. Hence, Serbia faces a two-pronged jobs challenge: (i) creating—for the most part—low productivity and flexible jobs for the transition generation in the formal economy, while (ii) making sure that the young choose entirely different career paths than their parents.

In order to address these challenges, the World Bank, through its technical assistance on labor markets operational support through the State-Owned Enterprises Reform Development Policy
Loan (SOE DPL) and the Competitiveness and Jobs Results Based operation, has identified the following immediate reform priorities. First, in order to allow the creation of more so-called mini and midi-jobs (relatively low-paying and casual formal part-time jobs), the minimum social security contribution needs to be abolished or reformed to reflect actual hours worked. Second, formal own-account work and micro-entrepreneurship need to be fostered through technical training on self-employment and start-up support, either through active labor market programs (ALMPs) or micro-credits. Third, the capacities and financing of the National Employment Service need to be considerably enhanced to allow for a properly working labor market. Priorities are to decrease the caseload of case workers, decentralize services and financing, and redesign ALMPs. The improvement of incentives for formal jobs for a targeted subset of disadvantaged workers is also the focus of these operations. The amended Labor Code that was enacted in July 2014 brings some changes, such as allowing for more flexible work arrangements and severance payments that are paid based on tenure with the last employer.

Health Sector

Recent trends in Serbia’s health indicators point to continuous improvement. Health outcomes have improved significantly over the past decade, and Serbia now has an epidemiological pattern like most countries in Eastern Europe. Additionally, many indicators are equal or better than those in the most recent EU member states. Average life expectancy, for example, at 74.3 years is almost equal to averages in the new EU members. However, Serbia spends almost twice as much per capita on health as comparable countries and has similar health outcomes, indicating that health sector efficiency is a concern. Total health spending accounts for about 10.8 percent of GDP. Furthermore, public expenditure on health per capita increased approximately 130 percent between 2001 and 2011. As much as 7.23 percent of Serbia’s 2014 budget has been allocated to health. The share of out-of-pocket expenditure for health is 38 percent. The sector took steps toward rationalization of the system by setting the groundwork for productivity-based payment, reducing the number of beds and staffing, increasing copayments, and reducing the generosity of the benefits package. However, the area of prevention, especially with regard to noncommunicable diseases (NCDs), remains inadequate.

Financing reform and improving efficiency in health care delivery remain the main challenges in the sector. Despite many improvements in recent years, the health care system still suffers from numerous inefficiencies and low productivity. The Ministry of Health and the Health Insurance Fund initiated financing reforms at both the primary and secondary levels that will replace the input-based system of financing in the health sector—in which providers were paid according to historical budgets—with a new system that will introduce a productivity factor into the payment of providers.

Photo 2. Vehicles for Palliative Care in Primary Health Care Centers Procured under the World Bank–Financed Project

For primary care, the Government has opted for performance-based payment, a formula combining per capita payments, the number of services, and preventive care services. Patients register and get treated by a doctor of their choice as the primary point of contact, thus limiting the need for referrals. A portion of the salaries of primary health care providers is directly linked to the number of patients registered and the number of services provided. The output-based payment system linking a percentage of salaries to productivity was introduced in September 2012.

In the secondary, hospital level of care, the Ministry of Health and the Health Insurance Fund are moving toward a Diagnosis-Related Group (DRG) system. DRG is a hospital payment system of care in which hospitals are paid on a per-case basis, calculated on an average cost of treating a patient during an entire episode. The DRG system creates an incentive to increase the number of treated cases, while at the same time minimizing costs. International experience shows that implementing
such reforms can generate substantial savings and increase productivity.

The Government of Serbia has realized significant savings from introducing centralized procurement for pharmaceuticals, medical devices, and supplies. The Law on Public Procurement provided the legal grounds for the introduction of centralized procurement, and the Ministry of Health and Health Insurance Fund are working toward putting the new procedures into practice. The first pooled procurement for hospital drugs was completed in December 2013, and savings amounted to €35 million. The World Bank continues to provide technical support for the further expansion of centralized procurement to other areas, such as prescription drugs, where more substantial savings are expected. The Bank also supported the health sector in Serbia through the Delivery of Improved Local Services (DILS) Project, which closed on March 31, 2015.

The Bank’s support will continue through the Second Serbia Health Project, approved by the Board on February 25, 2014, signed on July 10, 2014, and expected to become effective in April 2015. The Second Serbia Health Project is an investment operation that supports the Government in enhancing the efficiency and quality of the Serbian health system by strengthening health financing, procurement, maintenance, and quality improvement systems, and by managing priority NCDs, including cancer treatment. The project will contribute to improved financial incentives and greater transparency and accountability by promoting the efficient purchasing of pharmaceuticals and medical products and strengthening the quality of service delivery.

Education

Despite a relatively high level of public expenditure on education (consolidated expenditures on education in Serbia amount to around 5 percent of GDP), the country’s education system is performing below international averages in terms of student achievements. Results of the Program for International Student Assessment (PISA) in 2003, 2006, and 2009 revealed that (a) Serbia’s 15-year-olds are performing below the Organisation for Economic Co-operation and Development (OECD) averages in reading, mathematics, and science literacy, and (b) the portion of students considered functionally illiterate is still very high (roughly one-third of students taking the PISA test). However, the PISA results also revealed that Serbia’s students significantly improved their scores between 2006 and 2009.

The key reform challenges in the education sector in Serbia are the need to increase the efficiency of public spending in education, improve the quality of teaching and learning in schools, and implement inclusive education policies as legislated in the Framework Education Law of 2009. The Government has been addressing these challenges through: (i) efforts to optimize the existing school network, consolidate class sizes, and rationalize the education labor force, in order to adjust the size of the education system to the declining number of students; (ii) the piloting of a draft formula for per student financing in 16 municipalities (10 percent of all Serbia’s municipalities) during the school year 2011–12, as a part of per student financing reform; (iii) the introduction of learning standards, a reform of the final examinations at the end of compulsory and secondary education, and efforts to strengthen the schools’ external evaluation system; and (iv) extensive work on introducing a mechanism to support the inclusion of the most vulnerable groups of children, including Roma and the disabled, into the regular education system.

The World Bank has supported the education sector in Serbia through multiple instruments. The DILS project supports the delivery of local services in the sectors of education, health, and social protection. Until the fall of 2012, the Bank provided multiannual support to the Serbia Education Technical Assistance program in order to help the Government address the challenges in educational quality and financing. The technical assistance supported the creation of expenditure databases for Serbia covering 2005–10, using government budget data and the BOOST methodology for the analysis of public expenditure. Under this effort, a separate Serbia Education Module for 2010 was created, with data on school and municipal characteristics, student

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5 The BOOST initiative was launched four years ago to improve and standardize the way public expenditure data are collected, organized, and utilized in order to support the Bank’s analytical work on fiscal and expenditure policy and its dialogue with client countries.
achievements, and spending on education. The technical assistance included an assessment with recommendations on monitoring student achievements, teacher policies, and school finance strategies.

Pending work in the education sector includes implementation of technical assistance with funding from the Western Balkans Investment Framework (WBIF), a multilateral instrument—including the EC, the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB), the Council of Europe Development Bank (CEB), the World Bank, and bilateral donors—established to support the accession of Western Balkan countries into the EU. In Serbia, the WBIF is financing the development of systems to monitor education inclusion, with the World Bank as a main implementing partner.

Pension System

The Serbian pension system is the single largest expenditure item in the state budget, and Serbia had the second-highest pension spending-to-GDP ratio in the ECA region at 14 percent in 2012, second only to Ukraine. The problems include a benefit level that is too high and eligibility conditions that allow more than half of new retirees to retire below the normal retirement age of 65 for men and 60 for women. Both the benefit levels and the retirement age were addressed in the 2003 and 2005 pension legislation, but those efforts proved to be insufficient to resolve the problems. In 2009, which was the last year in which comparable data are available, Serbian pension spending per beneficiary averaged 63 percent of GDP per capita, while the average for all European and Central Asian countries, including Western Europe, stood at 46 percent.

In 2010, the Parliament approved new legislation that gradually raises the earliest retirement ages and limits the indexation of pensions to bring the benefit levels closer to international norms, thus enhancing the fiscal sustainability of the pension system. Although the changes introduced in the new law are rather modest in scope, it is a step in the right direction. Along with a mandatory pension system, there is also a voluntary (third pillar) pension system supervised by the NBS. Since 2008, the Serbian pension system has been administered through a single Pension and Disability Fund of the Republic of Serbia (PDF), established through the consolidation of three formerly separate funds (for employees, the self-employed, and farmers). The recently enacted Law on Pensions brings Serbian law closer to compliance with international norms for pension provision. One of the country’s weakest areas in its pension policy was the high degree of early retirement. The new law continues to allow for early retirement but provides an actuarial adjustment for those who choose this option, as other European countries do.

In the past decade, all of these reforms were supported by the World Bank through a mix of investment (Consolidated Collection and Pension Administration Reform Project, otherwise called PARIP, which closed in September 2012), and technical assistance support.

Agriculture

Like the rest of the Serbia’s national economy, the agriculture sector is challenged by the need to increase competitiveness in response to wider opportunities for trade and to align laws, policies, and institutions with those of the EU. Given its importance to the Serbian economy, with 10 percent of GDP, 23 percent of exports, and 21 percent of the workforce, a successful response to these challenges is imperative, a response that has been somewhat uneven thus far. Some regions and commodity groups have embraced the new opportunities created by increased integration with western and central Europe and have grown strongly, while other regions and commodity groups have contracted. Serbia’s legacy of small and medium-sized farms and deep-seated regional disparities partly explain this response. An erratic policy framework has also contributed to this stagnation and unbalanced growth and hampered the resolution of the underlying structural constraints.
There is a growing need to address these issues sooner rather than later. Free trade with the EU has already begun as the first step toward EU accession, changing Serbia’s traditional domestic and international markets for agricultural commodities and increasing competition. The Government is now cutting public expenditure to redress serious fiscal imbalances, reducing the level of public support for agriculture at a time when considerable public and private investment is required. The agriculture sector is also under pressure to hasten its efforts to utilize a €200 million EU Instrument for Pre-Accession Assistance in Rural Development (IPARD) support program to assist the transition to EU membership.

Various economy-wide factors influenced the concurrent patterns of agriculture sector growth, both before and after the global financial crisis. At the regional level, the greater export orientation of Vojvodina resulted in strong real growth rates before 2009 and lower but still positive growth rates after 2009. Central Serbia exhibited minimal growth before 2009 and negative growth afterward. A comparison by subsector shows high precrisis growth rates for crop production, consistent with its stronger export orientation, and lower growth rates after 2009. The livestock sector exhibited minimal growth, both before and after 2009.

Two contrasting conclusions emerge from these comparisons. First, where export-oriented production and marketing systems were built prior to the global financial crisis—as for specific crops at the commodity level and for Vojvodina at the regional level—the impact of the crisis has been less severe. This is consistent with economy-wide trends and bodes well for future growth. The observed growth patterns for Central Serbia and livestock are more disconcerting, however, in that neither benefited substantially from strong precrisis growth. This minimal response, together with the limited subsequent impact of the financial crisis, suggests that deep-seated structural constraints are the major impediments to growth in both cases. The prospects for future growth are thus limited unless these underlying constraints are resolved.

This paradox of Serbia’s agriculture sector—stagnant sector growth despite a substantial increase in agricultural exports—reflects both the opportunities and constraints the sector faces as it prepares for EU accession. Clearly, Serbia has the ability to compete in European and international markets for these commodities. Cereals, vegetable oils, and edible fruit products have led the boom in agricultural exports, which has increased agricultural export earnings by more than $US1.5 billion since 2006.

Figure 5. Agriculture Growth Rates

However, the substantial contraction of livestock output has offset the growth of crop production and exports, resulting in zero growth for the sector in aggregate. Livestock production, which accounts for approximately 40 percent of total sector output, has contracted during the same period, and imports of livestock products have increased. The challenge for agriculture is to broaden the basis for sector growth in order to include more farmers, more land, and more commodities.

Transport

The floods in May 2014 resulted in significant damage to the transport infrastructure, especially in Kupanj, Valjevo, and Obrenovac. Damages to national and local roads were estimated at US$51 million and US$32 million, respectively, while costs to railway infrastructure were estimated at US$37
million. The damages to airports were somewhat lower at US$1.2 million. In addition to the devastation to infrastructure, the damages to transport vehicles were about US$11 million, three-quarters of which were in Obrenovac.

The integration of the Serbian transport network into the regional and pan-European network is critical for Serbia’s economic and social development. Through the ongoing Corridor X Highway Project, the Government and international financial institutions (IFIs) are financing the construction of several road segments on Corridor X, the most important Trans European Network (TEN-T) in Serbia. About €1.6 billion is envisioned for completing the missing road links on Corridor X. Progress has been significantly delayed due to the regional economic downturn, which contributed to financial difficulties and the bankruptcies of some road construction companies, and also due to delays in procurement and land expropriation. The main reasons for the delay have been addressed and implementation progress has improved, with two new contracts recently awarded. However, the Government has no financing in place for the section Srpska Kuća to Levosoje, the Corridor 10 E-75 road, which is now the only unfunded section and a critical link for the continuity of the corridor.

The road network is estimated to have an asset value of about US$13 billion, but connectivity and road conditions need improvement to support economic growth. Despite the importance of the road network, it remains in poor condition.

According to the 2014–2015 GCR, Serbia is ranked 114th out of 144 countries on the quality of roads. Recurrent expenditures on maintenance were stable for years at the level of US$383 million per year until 2012, when they dropped significantly as a result of the financial crisis and the Government’s commitment to completing the Corridor X Highway Project and the Belgrade bypass. Although the above amount would be close to what is estimated to be needed for normal maintenance, there is a significant maintenance backlog that is estimated to require financing of US$700–$900 million.

Figure 7. SEETO6 Regional Participants: Number of Fatalities, 2003–13

The past few years have shown progress on reducing the number of fatalities, but these efforts need to continue, as the social and economic costs of road accidents remain significant. Some estimates suggest that the cost of fatalities and injuries could be as high as 2 percent of GDP based on 2008 accident figures. The Government recognizes the importance of road safety and adopted a new road safety law in 2009 that mandates the incorporation of an independent safety audit by an accredited road safety auditor in road design. A Road Safety Strategy has been developed under the Corridor X project and is expected to be adopted by the end of 2015.

The Government intends to address the maintenance backlog to improve the overall quality of the national road infrastructure and further strengthen road safety through an IFI-supported National Road Rehabilitation and Safety Program. The first phase of the program (the Road Rehabilitation and Safety Project, RRSP) is rehabilitating and enhancing the safety of about 1,125 kilometers of road sections with the financial support of several IFIs over the next five years at an estimated cost of €400 million. The EU is also supporting the improvement of maintenance practices through an IPA grant. The program draws from the Ministry of

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6 South-East Europe Transport Observatory.
Transport’s 2009 Serbia Transport Strategy and Master Plan that envisages €4.6–€5.0 billion spent on maintenance between 2009 and 2027. It builds on the Road Network Analysis carried out under the previous Bank-financed Transport Rehabilitation Project (TRP). The current post-floods emergency road reconstruction needs for the national road network are being met through a restructuring of the RRSP.

In July 2014, the Government announced a plan to merge the public company Corridors of Serbia (CoS) into the Public Enterprise Roads of Serbia (PERS). This is an important step in the organizational reform of the road sector as proposed in the Action Plan prepared under the Bank-financed technical assistance component of the Corridor X project. While several actions proposed in the Action Plan have been implemented, two remaining key reforms are needed to achieve the desired sector efficiency: (i) the introduction of service-level agreements between the transport line ministry and PERS; and (ii) competitive tendering for road maintenance works. While the merger will bring improvements to the way in which road transport infrastructure is delivered and maintained, there is some concern that progress on the ongoing Corridor X project could be impacted by the speed of the merger. The World Bank is collaborating with the Government to help ensure that the transition does not create serious disruptions or implementation delays.

The 2014–15 GCR ranks Serbia 83th out of 104 countries on the quality of its rail infrastructure. The Government has embarked on a major reform program toward transforming Serbian Railways (SR) into a modern institution. A new legislative framework has been developed in line with EU directives and a regulatory body has been established. In addition, the Government is in the process of reorganizing SR into four independent entities: an Infrastructure Manager, a Passenger Company, a Cargo Company, and a holding company for a transition period. The decision is expected to be adopted by the Government in May 2015. The reform plans to draw from a time-bound action plan in a reform policy note prepared by the Bank in collaboration with the Government and SR in December 2014, as well as various forms of technical assistance from EBRD, EIB, and the EU.

The Bank supports the transport sector through the ongoing Corridor X project and the Road Rehabilitation and Safety Project. Both projects aim to improve road quality and safety through the construction and improvement of the standards of Serbia’s road network, building on earlier efforts under the completed Transport Rehabilitation Project. In addition, the World Bank continues to support railway reforms.

Energy

While the Government has succeeded in resolving some of the most critical energy security issues over the last decade, Serbia still faces the risk of electric power shortages. Serbia is ranked poorly in the 2013 Doing Business report with respect to the reliability of electricity (it costs more than five times the OECD average as a percentage of GDP to establish a secure electricity supply), and the Bank’s 2008 Business Enterprise and Performance Survey (BEEPS) showed that 33 percent of firms considered electricity a problem, more than double the level in 2005 and representing the sharpest increase in any of the obstacles registered in the survey. The entire electricity system is old, with low system reliability and low efficiency. In generation, 53 percent of the power plants are more than 30 years old and will have to be retired over time, despite the ambitious rehabilitation programs that are planned. Less than 25 percent of the transmission lines and substations are in good condition. As a result, capacity constraints in the transmission system make it difficult to accommodate new generation capacity (especially renewables) and increased regional trade.

There is therefore an urgent need to invest in new generation, transmission, and distribution to address the supply gap and an unfinished reform agenda. Already by 2008, generation capacity was not able to meet peak demand. This trend is expected to continue, with a gap of about 400 megawatts by 2015. Total investment needs to address the supply gap are estimated to be about €16 billion by 2020 (about 4 percent of GDP annually), with the public sector able to provide no more than a quarter of that amount. Hence, private sector participation would need to increase from almost nothing today to €12 billion by 2020. The new Energy Law is a step in the right direction, as it facilitates competition in the sector. Further corporatization plans for EPS and EMS (state-owned enterprises that produce and distribute electric power, respectively) will also improve their ability to compete in the market.
In May 2001, Serbia, together with Montenegro, assumed membership in the World Bank. Since 2006, Serbia has been a World Bank member as an independent country. During the Country Partnership Strategy (CPS) for FY12–15, the International Bank for Reconstruction and Development (IBRD) delivered US$784 million in new loans to Serbia, of which US$684 million was for investment project financing and US$100 million for budget support.

The Bank is continuing to work with the Government of Serbia on a DPL series centered on reform of the SOE sector. The first operation in the series was approved by the Board in March 2015, and the second operation is expected to be delivered around mid-FY16. The operation is organized around three pillars: (i) accelerating the restructuring and divestiture program for the Privatization Agency portfolio and selected SOEs operating in the commercial sector; (ii) strengthening the governance, regulatory, and institutional frameworks and the monitoring and transparency arrangements for SOEs; and (iii) mitigating the social and labor market impact of the SOE reform program. The first operation is primarily about putting in place the right regulatory framework and establishing an initial track record on resolving enterprises. The second will focus on implementation—in particular, the timely resolution of the Privatization Agency portfolio. Going forward, it will be important to ensure that proper mechanisms (through social programs in the first instance, and later other labor market measures) to cushion the impact on redundant workers remain in place.

Analytical and Advisory (AAA) Program: The lending program is underpinned by strong AAA activities carried out over the past several years as well as new programs. In particular, the Bank has prepared the first Systematic Country Diagnostic (SCD), which identifies key bottlenecks for growth and development in Serbia and serves as a major input for the new Country Partnership Framework (CPF) which is under preparation. The recent Municipal Finance Expenditure Review provides an analysis of municipal public finances in Serbia. Advice has also been provided on public sector wage system reform, based on ongoing programmatic technical assistance. The Bank prepared a Railways Reform Policy Note.

The Serbian economy is highly energy intensive and wastes a lot of this scarce resource. In 2011, the consumption of primary energy in Serbia for every dollar of GDP was six times higher than in Germany, five times higher than in France, three times that of Slovenia, and almost twice that of Romania. Problems in the energy sector reflect the cumulative effect of policies that channeled mass subsidies to firms and the population through cheap energy. This stimulated excessive and wasteful consumption, making the Serbian economy very energy intensive and at the same time depriving the energy sector of capital to develop its capacity to meet the growing demand.

Compounding these challenges, the need to comply with the strict environmental requirements of the EU will call for yet more funding. Existing large power plants will have to reduce their emissions, and the required standards will be tightened even more after 2016. Total estimated investment requirements to meet EU directives in the power sector are on the order of €800–€900 million.

The World Bank has supported the energy sector of Serbia through the Energy Efficiency Project and the Energy Community of Southeast Europe Program, whose goals are to improve energy efficiency in public buildings and the power transformation system. The Bank remains ready to support Serbia’s energy sector in the process of EU integration.
that outlines the key reform steps needed to transform the sector into an efficient growth engine and provides information on the costs of delays in undertaking the necessary reforms. Under the WBIF Trust Fund on inclusive education, the Bank will support the Ministry of Education in reviewing the current approach to inclusive education with an emphasis on monitoring and evaluation. The ultimate goal is to improve the situation of vulnerable children and increase the quality of education for all. In addition, the Bank is looking at the challenges that vulnerable groups such as Roma face in accessing social services and will propose policy recommendations in this regard. The World Bank has also provided multiannual technical support to the education sector, with new technical assistance grants, including the WBIF and the Poverty and Social Impact Assessment of the Per Student Financing reform (PSIA).

In March 2015, the portfolio consisted of seven active investment projects for a total of US$1,074 million, and two trust funds in the amount of US$20.66 million. Serbia’s portfolio performance is above the target level, with the disbursement ratio at the third quarter of FY14 at 30.9 percent. The Government has requested the cancellation of the Bor Regional Development Project, which is being processed.

In response to the catastrophic floods that occurred in May 2014, the World Bank approved a Floods Emergency Recovery Project in October 2014 in the amount of US$300 million. The project includes investments in three priority sectors: energy, agriculture, and flood protection. A new Real Estate Management Project was approved by the Board on March 16, 2015, aiming to strengthen the cadastre, improve real estate valuation, and enhance the effectiveness of property tax assessment and collection.

In addition to the International Development Association (IDA)7/IBRD portfolio, there is a Multi-Donor Trust Fund for Judicial Reform in the amount of US$10.1 million, the EU IPA-funded Serbia Innovation Project in the amount of US$10.56 million, and the new Serbia Technology Transfer Project in the amount of US$3.5 million.

Serbia is a participant in the Road to Europe – Program of Accounting Reform and Institutional Strengthening (REPARIS). This program helps countries to adapt laws and regulations governing financial reporting and develop the related institutions and also assists countries in bringing their financial reporting framework in line with EU requirements. REPARIS is a Bank- and recipient-executed (hybrid) Multi-Donor Trust Fund, currently funded by the Governments of Austria, Switzerland, and Luxembourg and managed by the World Bank Centre for Financial Reporting Reform (CFRR).

International Finance Corporation

Serbia became a shareholder and member of IFC in 2001. IFC works with private sector clients, government, and civil society to bring the benefit of global expertise to the country through its advisory services and investment projects. IFC’s committed investment portfolio in Serbia as of June 30, 2014, was US$642.5 million. In FY14, IFC invested US$302.4 million in Serbia, including US$215 million mobilized from IFC partners.

IFC’s priorities in Serbia include agribusiness, climate change, and improvements in the investment climate. IFC is also focusing its investment services on increasing access to finance by supporting the development of local financial institutions, especially those that concentrate on small and medium-sized enterprises (SMEs). Across all sectors, IFC prioritizes investment in Serbia’s less-developed regions and in projects that contribute to greater economic diversification and regional integration. IFC’s advisory services aim to improve the investment climate and the performance of private sector companies and to attract private sector participation in the development of infrastructure projects.

Recent IFC investment projects in Serbia include:

- €57 million loan to Victoria Group to support the development of the private sector in Serbia, where revitalizing agribusiness is essential for creating jobs.
- €50 million loan to Atlantic Group to support the development of agribusiness and

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7 By the end of the FY13, all IDA-funded projects in Serbia had closed.
cooperation in a region (including Serbia) that is still recovering from the crisis.

- €50 million for a minority stake in Titan Cement Cyprus, owned by Greek cement manufacturer Titan Cement. The investment will support Titan’s subsidiaries in the Western Balkans: Cemertara Kosjeric in Serbia, Cementarna USJE in FYR Macedonia, and SharrCem in Kosovo.

- €70 million loan to the Serbian unit of Société Générale to finance agricultural development.

- €45 + €25 million loans to MK Group, a Serbian food producer, to modernize and expand production.

- €20 million loan to PMC Automotive Serbia, a joint venture between Italian automotive suppliers CLN Group and PROMA Group.

- €50 million loan to UniCredit, equally divided between a housing line (focusing on low-income households) and an agribusiness line supporting one of Serbia’s key sectors.

**IFC has also invested in the following Serbian banks and companies:** Banca Intesa, Continental Bank, EFG, Komercijalna Banka, Unicredit Bank, Vojvodjanska Banka, ProCredit Bank and ProCredit Leasing, Farmakom, Kronospan, and Porr.

**Recent advisory projects include:**

- **The Balkans Renewable Energy Project** works to develop the renewable energy market, with a special emphasis on small hydropower plants (SHPs) in Western Balkan countries with the highest impact potential: Albania, Bosnia and Herzegovina, FYR Macedonia, and Serbia. (Supported by the Ministry of Finance of Austria)

- **The Southeast Europe Tax Transparency and Simplification Program** works in Albania, Bosnia and Herzegovina, Croatia, Kosovo, FYR Macedonia, Montenegro, and Serbia to achieve two objectives: simplify tax administration procedures to reduce tax compliance costs, particularly for SMEs; and improve the legal framework and efficiency of the administration of international taxation procedures, with a focus on transfer pricing and double taxation treaties. (Supported by the Swiss State Secretariat for Economic Affairs [SECO])

- **The Western Balkans Trade Logistics Project** works in Albania, Bosnia and Herzegovina, Croatia, Kosovo, FYR Macedonia, Montenegro, and Serbia to achieve two objectives: reduce the number of documents and days needed for goods to be exported and imported; and streamline procedures for the flow of cargo by road, air, and river. (Supported by the EU)

- **Public-Private Partnerships**: IFC provides advice on designing and implementing public-private partnership (PPP) transactions to national and municipal governments to improve infrastructure and access to basic services such as water, power, health, and education. (Supported by donor partners Austria, Norway, and Switzerland)

- **The Agribusiness Standards Advisory Program** endeavors to help increase access to markets for the food sector by promoting the uptake of agribusiness standards, including food safety and environmental and social standards.

- **The Western Balkans Debt Resolution and Business Exit Program** in Serbia supports the Government in improving its insolvency framework in order to strengthen loan recovery and increase returns to creditors by enabling viable businesses to rehabilitate and return assets back into productive use.

- **IFC’s Corporate Governance Program in Serbia** is aimed at improving corporate governance practices in companies and financial institutions, as well as enhancing the corporate governance framework at the institutional, regulatory, and policy levels.
SERBIA: CORRIDOR X HIGHWAY PROJECT

Key Dates:
Approved: June 9, 2009
Effectiveness: November 6, 2009
Closing: December 31, 2016

Financing in million Euro*:

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<td>Total Project Cost</td>
<td>330.70</td>
<td>178.70</td>
<td>152.00</td>
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*As of February 28, 2015; Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Context: The integration of the Serbian transport network into the core regional transport network is recognized as a key policy objective for the economic and social development of the country. The Serbian section of Corridor X, with its 792 kilometers of roads and 760 kilometers of railway lines, forms a part of the South East Europe Transport Observatory (SEETO) regional “Comprehensive Network” and is also a part of two important Pan-European transport infrastructure networks. One is connecting Budapest with the Bulgarian capital of Sofia and the other links Greece to the south.

The Government views the development of Corridor X as the country’s key transport priority that will help facilitate sustainable economic development and ensure that the country capitalizes on its geographical position. The Bank was requested to assist the Government with the preparation of the entire program for the two southern sections of Corridor X. The Government also requested that the Bank contribute financing in parallel to the other international financial institutions (IFIs) and the Hellenic Plan for the Economic Reconstruction of the Balkans (HiPERB*). During project preparation, the Bank led a review of the technical and economic viability, a review of the preparation of the Resettlement Policy Framework, the Corridor-level environmental impact assessments, and a review of the proposed engineering design.

The Project Development Objectives are to increase transport efficiency and improve traffic safety on the three project sections of Corridor X, between Niš and Dimitrovgrad, and between Grabovnica and Donji Neradovac, respectively, and to improve road management and road safety in Serbia.

The project objectives will be achieved by financing (i) the construction of two sections of the motorway on E-75, totaling 38 kilometers between Grabovnica and Grdelica and between Čarićina Dolina and Donji Neradovac; (ii) the construction of 8.67 kilometers of the motorway on an E-80 section of the corridor between Dimitrovgrad and the border with Bulgaria (Dimitrovgrad Bypass); (iii) technical assistance in the area of road safety; and (iv) implementation assistance and institutional support.

Results achieved to date:

- For the construction of two motorway sections between Grabovnica and Grdelica (5.6 kilometers) and between Čarićina Dolina and Donji Neradovac (32 kilometers) on the E-75 road to FYR Macedonia: four lots on the E-75 were awarded in March 2012, with work commencing in May 2012. Completion is expected by November 2015. The project was recently restructured to use savings available under Components 1 and 2 to provide for the construction of a 5.8 kilometer extension of the E-75 motorway between Čarićina Dolina and Vladičin Han, known as Lot 6. A contract for construction of Lot 6 has been awarded, with estimated completion by March 2017.

- For the construction of 8.67 kilometers of the Dimitrovgrad Bypass, a motorway between Niš and the border with Bulgaria, close to Dimitrovgrad (E-80): the contractor for Lots 1 and 2 declared bankruptcy in July 2013 and left the site. At the time of the bankruptcy, road construction on Lot 1 was at 56 percent completion, on Lot 2, the bridge, at 88 percent. A new contract for the remaining works was formed in July 2014, with a 15-month construction period. Construction of the tunnels under Lot 3 achieved substantial completion in October 2014.

- A Road Safety Agency has been established under the new Road Safety Law, and a road safety strategy has been prepared and is expected to be adopted in 2015. Procurement of the comprehensive road crash database has been initiated.

- The Action Plan for the Reform of the Roads of Serbia (PEPS) has been prepared.

Key Partners: The Bank team works closely with the Ministry of Construction, Transport, and Infrastructure of the Republic of Serbia; Corridors of Serbia, a limited liability company; and the public enterprise “Roads of Serbia.”

Key Development Partners include international financial institutions: the European Bank for Reconstruction and Development (EBRD) and the European Investment Bank (EIB).

*Financing under the Hellenic Plan has been suspended.
**SERBIA: BOR REGIONAL DEVELOPMENT PROJECT**

**Key Dates:**
- **Approved:** June 20, 2007
- **Effective:** December 16, 2008
- **Closing:** Revised, September 30, 2015

**Financing in million US Dollars:**

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<tr>
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<td>IBRD Loan</td>
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<td><strong>Total Project Cost</strong></td>
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<td><strong>9.77</strong></td>
<td><strong>15.48</strong></td>
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*As of March 1, 2015; Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.*

**Context:** Initially, the project had a broader focus and was aimed at the mitigation of poorly managed legacy sites from mining operations in Serbia's Bor region and social impacts of the restructuring of the local RTB Bor mining and metallurgical company. With partial results from the job creation component and uncertainty about whether some of the project sites earmarked for environmental remediation could be redeveloped under concessions to private investors, it was decided to comprehensively restructure the project in early 2013 and (i) refocus the project on the replacement of a collector under one of the mine tailing disposal facilities, and (ii) discontinue or cancel all other activities.

**The Project Development Objective** is to support the Government in addressing the structural hazard of the river water collector under the Veliki Krivelj tailings disposal facility, which is one of the most urgent environmental legacy issues of the mining sector in the Bor region.

**The Project focuses on:** The replacement of the Veliki Krivelj collector (a 2.5 kilometer concrete main pipe with a diameter of 3 meters), which rests at the bottom of the mine tailings facility that has been constructed on top of it, is considered the most pressing environmental concern of the original project intervention. The collector, carrying much more weight from the material above than what it was designed for, is in very poor condition, though regular repair works have managed so far to maintain its integrity. Collapse of the collector would block the river discharge and immediately jeopardize the stability of the massive mine tailings disposal facilities that have been constructed in the Kriveljska River valley. The full replacement of the collector with a bypass tunnel in hard-rock around the tailings disposal facility is considered the only viable solution to eliminate this high risk.

**Results achieved to date:**

**Environmental liabilities of the mining sector in the Bor region:**
- In February 2015, the Borrower requested cancellation of the project due to a lack of time to complete the works by the project closing date.

**Fostering new sources of economic growth and job creation in the Bor region (component discontinued):**
- Nearly 850 unemployed people benefited from the temporary employment programs (i.e., public works); as of June 2012, nine training programs for over 600 unemployed persons were completed.
- The reconstruction works on the future location of the Business Incubator in Majdanpek have been completed. However, the registration of the incubator, the selection of tenants, and the procurement of the necessary equipment were not finalized.
- Under the microfinance program, the Opportunity Bank of Serbia disbursed 53 loans. Due to the slow disbursements resulting from low demand, the credit line has been cancelled.

**Key Partners:** The Bank team works with (i) the Ministry of Energy and Mining, which is responsible for implementation of the environmental management and remediation component; (ii) the Ministry of Economy and Regional Development, which focused on socioeconomic regeneration activities; and (iii) the Project Management Unit housed within the Ministry of Energy and Mining.

**Key Development Partners:** Project preparation activities were funded by a Japanese PHRD (Policy and Human Resources Development) grant, while an EU-EAR grant financed technical assistance for the restructuring and privatization of RTB Bor.
Key Dates:
Approved: February 25, 2014
Effective: November 26, 2014

Financing in million EUR:

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<tr>
<td>Total Project Cost</td>
<td>145.3</td>
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<td>145.3</td>
</tr>
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Context: While Serbia has an extensive framework for dealing with problematic banks, the failure of several small banks in 2012 and 2013 led the Government to begin working on a reform program to improve this framework. As part of a broader set of reforms, the Government has requested a World Bank loan to strengthen the financial and institutional capacity of the Deposit Insurance Agency (DIA). In addition, the resolution of these banks (which was successful, as the stability of the overall system was preserved) has depleted the Deposit Insurance Fund (DIF), which creates risks to the Serbian financial system. These risks stem from the possibility of not having adequate resources to cover insured depositors at a time of bank failure. Bank failures, even of a small size bank, have the potential to shake confidence in the entire banking system, if depositors sense that their deposits are not secure. To strengthen the DIA, the project has two main goals: (i) financing the DIF with sufficient resources (from external creditors, government budget, bank premiums, recoveries, and investments) to allow the DIA to meet its deposit insurance and bank resolution obligations and serve as a core part of the financial sector safety net, and (ii) ensuring that the DIA has the institutional capacity to manage the financial resources it has available.

The Project Development Objective is to strengthen the financial and institutional capacity of the DIA, so as to enable it to meet its deposit insurance and bank resolution obligations and serve as a core part of the financial sector safety net.

Project Design: Considering the importance not only of financing the DIF but also strengthening the DIA, the majority of the project consists of a results-based component that finances the DIF based on the achievement of Disbursement Linked Indicators (DLIs). This is complemented by a technical assistance component that provides assistance to achieve the DLIs and strengthens the institutional capacity of the DIA. Thus the project has two Components that aim to accomplish the Project Development Objective: 1) a results-based component of €144.23 million that strengthens the financial capacity of the DIA based on satisfactorily achieving DLIs that improve its ability to meet its deposit insurance and bank resolution obligations; and 2) a technical assistance component of €0.71 million that aims to strengthen the institutional capacity of the DIA to meet its deposit insurance and bank resolution obligations and achieve the DLIs.

For component 1, World Bank financing will be disbursed based on evidence of the achievement of six DLIs: DLI 1 – Premiums: Increase premiums charged to banks to increase the flow of funds to the DIF; DLI 2 – Backup Funding: Ensure that the Government puts in place a stand-by facility that the DIF can access; DLI 3 – Governance: Improve the independence of the governance bodies of the DIA; DLI 4 – Information sharing between financial safety net providers: Ensure that the DIA has the appropriate information to fulfill its mandate; DLI 5 – Recoveries: Improve the performance of the DIA’s mandate to recover assets from bankrupt and liquidated banks; DLI 6 – Early detection and timely intervention: Improve the information base on state-owned banks to ensure early detection and timely intervention.

Results achieved to date:
- Project implementation began in December 2014.

Key Partners: The Bank team works closely with the Ministry of Finance, the National Bank of Serbia, and the Deposit Insurance Agency, which is responsible for overall project implementation. Key Development Partners include the International Monetary Fund (IMF), the European Bank for Reconstruction and Development (EBRD), the U.S. Agency for International Development (USAID), and the European Commission (EC).
Context: The road network, estimated to have an asset value of US$13 billion, extends 40,800 kilometers, including about 9,500 kilometers of national roads. Despite being a major asset for Serbia, the quality of the road infrastructure appears to have declined in the past few years. The poor quality of roads manifests itself in high vehicle operating costs and inadequate road safety and reduces Serbia’s overall trade competitiveness. The Ministry of Construction, Transport, and Infrastructure (MCTI) has initiated a National Road Network Rehabilitation Program (NRNRP) to improve the quality and safety of priority national roads, thus improving the connectivity of the entire road network. With the support of the EU, MCTI has developed a Transport Strategy and a Master Plan that envisage a €4.6–€5.0 billion investment in maintenance and rehabilitation between 2009 and 2027. About 5,000 kilometers of national roads (slightly over 50 percent of the national road network) have been identified as high priority, and financial support from several international financial institutions (IFIs) is being sought to implement the rehabilitation works. In the first phase, about 1,125 kilometers will be rehabilitated, incorporating safety considerations into the design.

Serbian authorities are improving road safety, but the social cost of traffic accidents remains high. The level of injuries and fatalities caused by traffic accidents is a growing social and economic cost for the country. Between 2001 and 2010, there were about 9,000 fatalities and 190,000 injuries resulting from road traffic crashes in Serbia. While there is no official estimate of the socioeconomic costs of road accidents in Serbia, some estimates suggest a cost as high as 2.0 percent of GDP. During the past few years, the Government of Serbia has been earnest in road safety institutional and policy reforms. The Road Safety Law (RSL), adopted on May 29, 2009, represents the first major update in legislation since the 1980s and addresses many aspects of the EU Transport acquis communautaire and the recommendations given in the Road Safety Capacity Review funded by the World Bank Global Road Safety Facility. In 2009, the Republic of Serbia passed legislation mandating the incorporation of an independent safety audit by an accredited road safety auditor in road design.

The Project Development Objective is to improve the condition and safety of the national road network for road users by supporting the Republic of Serbia in the implementation of the first phase of its National Road Network Rehabilitation Program (NRNRP).

The objectives will be assessed based on: (i) improvements in road conditions measured by a reduction in the International Roughness Index (IRI) for the roads covered in the first phase of NRNRP from 5.42 to 2.5; and (ii) improvements in road safety measured by a 10 percent reduction in fatal road traffic accidents on the roads covered in the first phase of NRNRP.

The project objectives will be achieved by financing (i) road rehabilitation and safety investments (€264 million) and (ii) institutional strengthening (€3.10 million).

Results achieved to date:

- Six contracts for emergency works, triggered after severe floods in May 2014, have been awarded and signed. The works are expected to start in April 2015, as soon as weather conditions improve and contractors mobilize.
- The selection of the supervision consultant for emergency works is in its final stage, and the tender for technical assistance to the Project Implementation Team (PIT) has been launched.

Key Partners: The Bank team works closely with the Ministry of Construction, Transport, and Infrastructure of the Republic of Serbia, the Public Enterprise “Roads of Serbia,” and the Ministry of Finance. Key Development Partners: the European Bank for Reconstruction and Development (EBRD) and the European Investment Bank (EIB).
SERBIA: SECOND HEALTH PROJECT

Key Dates:
Approved: February 25, 2014
Effective: Expected in April 2015
Closing: September 30, 2019

Financing in million US Dollars*:

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<td>Total Project Cost</td>
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</tr>
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* N.B. The loan was made in Euros, and the USD amount may change in line with exchange rates.

Context at Project Design: Total health spending in Serbia accounts for about 10.4 percent of GDP, or twice as much per capita as in comparable countries, yet health outcomes in Serbia are similar to those countries. It is critical that Serbia increase the productivity of its health spending, particularly given the fiscal constraints, the increasing demand for health care from an aging population, and the disease burden leaning toward noncommunicable diseases (heart disease, stroke, and cancer, in particular). To address these issues, the Second Serbia Health Project will support reforms toward productivity-based health care financing, the efficient purchasing of pharmaceuticals and medical products, and the continuous improvement of the efficiency and quality of health care.

The Project Development Objective is to contribute to improving the efficiency and quality of the public health system of the Republic of Serbia through the strengthening of: (i) health financing, purchasing, and maintenance systems; and (ii) the quality improvement systems and management of selected priority noncommunicable diseases.

The range of sector issues addressed by the project include: (1) strengthening primary health financing and supporting hospital financing reforms; (2) establishing efficient centralized procurement in health while strengthening health technology assessment capacity and the maintenance of medical equipment; (3) improving cancer management and strengthening the quality of health care; and (4) supporting project implementation.

Results achieved to date:
- The project is not yet effective. However, the centralized (pooled) procurement of pharmaceuticals has already proved to improve the efficiency of the Serbian health care system. Centralized procurement was piloted during the preparation of the project for one-third of the drugs used in the public health care system and resulted in reducing the cost by €25 million for 2014. Lower-income groups will in particular benefit from an increased efficiency as they are directed toward the public health care system. Cost savings will contribute to ensuring that public funds deliver a maximum level of service for everyone.

Key Partners: The Bank team works closely with (i) the Ministry of Health, Health Insurance Fund, Institute for Public Health, and Agency for Accreditation, as beneficiary agencies; and (ii) the Public Procurement Office, Committee for the Protection of Bidder’s Rights, Committee for Protection of Competition, and the Agency for the Fight Against Corruption, as the key national partners in reform toward the centralized procurement of pharmaceuticals and medical devices.

Key Development Partners include the European Commission and the World Health Organization (WHO).
Key Dates:
Approved: October 3, 2014
Effectiveness: March 6, 2015

Financing in million US Dollars*:

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</table>

* equivalent to €232.2 million

Context: Unprecedented rainfall in May 2014 caused massive floods, resulting in the declaration of a national state of emergency in Serbia. The heavy rainfall led to a rapid and substantial increase in water levels in eight of the main rivers in western, southwestern, central, and eastern Serbia. Flash floods destroyed houses, bridges, and sections of roads, while rising water levels resulted in flooding in both urban and rural areas. The disaster resulted in 51 deaths, with approximately 32,000 people evacuated from their homes and around 110,000 households cut off from an electricity supply. Overall, the floods affected some 1.6 million people in Serbia, or about one-fifth of the total population living in 49 municipalities.

The recent natural disaster has exacerbated significant fiscal challenges that the country faces. The Government of Serbia conducted a Recovery Needs Assessment (RNA) that revealed that the total value of the disaster’s impact is roughly €1.7 billion, or over 4 percent of GDP.

The Project Development Objective is to: (i) help restore power system capability to reliably meet domestic demand; (ii) protect the livelihoods of farmers in flood-affected areas; (iii) protect people and assets from floods; and (iv) improve Serbia’s capacity to respond effectively to disasters.

The Floods Emergency Recovery Project focuses on the priority sectors identified in the RNA and addresses immediate to short-term needs arising from the crisis. The project will help close the financing gap and ensure the continued provision of power services during the upcoming 2014/2015 winter and recover critical energy infrastructure. In the agriculture sector, the project will forestall a likely decline in direct support to farmers in affected areas at a time when the fiscal accounts are under severe stress. In addition, the project will also help improve resilience to disasters by financing investments in critical flood prevention infrastructure.

Results achieved to date:
The project became effective on March 6, 2015. Under the overall coordination of the Office for Reconstruction and Flood Relief, the project implementation is progressing well.

- Power import purchases helped avoid any power supply interruptions during the 2014/2015 winter season.
- Dewatering of the Tamnava mine field is progressing well and is expected to be finalized in the second quarter of 2015.
- It is estimated that around 122,000 farmers living in the flood affected areas have received support under the Farm Incentives Program.

Key Partners: The Bank team works closely with the Public Enterprise, “Elektroprivreda Srbije” (EPS), the Directorate of Agrarian Payments (DAP), and the Directorate of Water Management (DWM).

Key Development Partners: The European Union (EU) and the United Nations (UN), with the World Bank providing financial and expert support to conduct the RNA.
## Key Dates:

**Approval:** March 24, 2015  
**Amount:** SOE DPL1: €88.3 million (US$100 million equivalent)  
**Effective:** expected within 180 days of the approval date  
**Disbursed in full:** --

## Context:

Despite significant achievements in the early years of the transition to a market economy (over 2,700 enterprises privatized), the role of the state in the enterprise sector remains pervasive, with about 1,200 state-owned enterprises (SOEs), employing more than 250,000 people. While this is a very heterogeneous group of enterprises, overall they perform poorly, have weak governance mechanisms, and remain prone to political interference. Overall, public sector enterprises make significant net losses, which in 2013 amounted to about €1 billion, and require significant state support to remain afloat. Many of these enterprises receive significant direct budget subsidies and soft loans, as well as indirect support in various forms, including unpaid taxes and contributions, state guarantees for loans, and arrears to other state entities and public utilities. This has fiscal implications and creates significant distortions and misallocations of production factors, deterring private sector investments.

The reform of SOEs is critical to the success of the Government’s economic program, contributing to medium-term fiscal consolidation efforts as well as economic recovery through improved economic efficiency. The absence of SOE reform for the past decade has allowed Serbia to fall behind its neighbors in the economic transition, preventing the country from realizing its potential and contributing to stalled growth and job creation in recent years. This is the first in a series of two programmatic DPLs designed to support Serbia’s structural reform program of the SOE sector.

### The Project Development Objectives

The Project Development Objectives are to reduce state participation and the level of direct and indirect support to the real sector; enhance SOE performance, governance, and accountability; and mitigate the short-term social and labor impacts of the SOE restructuring and disposition plans. These objectives will be achieved through supporting reforms carried out by the Government of Serbia, revolving around three policy areas: (i) accelerating the restructuring and divestiture program of the Privatization Agency portfolio and selected SOEs operating in the commercial sector; (ii) strengthening the governance, regulatory, and institutional framework and monitoring and transparency arrangements for SOEs; and (iii) mitigating the social and labor market impact of the SOE reform program.

## Expected Results:

- **Reduction of direct and indirect support to companies in the Privatization Agency portfolio:**
  - Annual direct subsidies and soft loans (€ mil.): baseline (average 2010–12): 85; target (2015): less than 10
  - New taxes and social contribution arrears (€ mil.): baseline (avg. 2010–12): 190; target (2016): less than 20

- **Reduction of direct subsidies and issuance of new guarantees for liquidity purposes for large SOEs:**
  - Annual guarantees for liquidity purposes (€ mil.): baseline (average 2012–14): 265; target (2015): less than 100


- **Number of redundant workers receiving compensation from the Transition Fund increases from roughly 5,700 (2014) to at least 10,000 (2015).**

- **At least 30 percent of workers made redundant from public enterprises during 2015 and register with the National Employment Service.**

- **Number of participants in public works increases from 2,882 in 2013 to at least 6,000 in 2015.**

## Key Partners:
The Bank team works closely with the Ministry of Economy; Ministry of Finance; Ministry of Labor, Employment, Veteran and Social Affairs; and the Privatization Agency. **Key Development Partners** included the IMF, the EU Delegation in Serbia, and the Swiss State Secretariat for Economic Affairs (SECO).
SERBIA: REAL ESTATE MANAGEMENT PROJECT

Key Dates:
Approval: March 16, 2015
Effectiveness: expected within 180 days of the approval date
Closing: December 31, 2020

Financing in million US Dollars*:

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<tr>
<td>Total Project Cost</td>
<td>44.0*</td>
<td>0</td>
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</tr>
</tbody>
</table>

*As of March 30, 2015

Context:
Despite persistent problems in the broader economy, Serbia’s real estate sector has seen considerable improvement over the past decade. Ten years ago, the cost and time required to register property rights were excessive, only 20 percent of the country was covered in “land books” (legal registers maintained by municipal courts), and there was a mismatch between these books and the records of the Republic Geodetic Authority (RGA). With the help of an earlier Bank-financed project, the time required to register transactions has been reduced, cadastral offices have been renovated, important geodetic infrastructures have been built, and customer satisfaction has improved.

Although these improvements are significant, Serbia’s real property registration services remain below European standards. The Real Estate Cadastre is not interoperable with other key government registries, and online services are limited. Over 30 percent of RGA’s analog cadastral maps have yet to be digitized. The data held by RGA on land, ownership, buildings, etc. are vital information for most government services and need to be made complete and more easily available. Investments in geodetic infrastructure are needed and RGA services need to be made more readily accessible to individuals, including members of vulnerable groups. Property valuation and taxation is another area where Serbia has made limited progress, as it lacks the complete and accurate data necessary to establish the tax base. RGA still needs to record all buildings in the cadastre to ensure that all properties are included in the property tax and that the legalization of buildings that are currently built informally can proceed smoothly.

The Project Development Objective is to improve the efficiency, transparency, accessibility, and reliability of the Republic of Serbia’s real property management systems.

This project supports the Serbian Government’s economic reform agenda in several important ways: a) property valuation and taxation activities will enable fiscal consolidation and reduce the fiscal deficit; b) e-governance for enabling access to real estate information will improve the business climate, attract investors, and reduce transaction cost and time; c) the development of real estate markets will boost small and medium-sized enterprises that use real estate as collateral; and d) the development of a National Spatial Data Infrastructure (NSDI) will advance European integration.

Results:
- The project is not yet effective.

Key Partners: The Bank team works closely with the Ministry of Construction, Transport and Infrastructure; the Ministry of Finance; and the Republic Geodetic Authority.
SERBIA: JUSTICE SECTOR SUPPORT

MULTI-DONOR TRUST FUND FOR JUSTICE SECTOR SUPPORT (MDTF-JSS) IN SERBIA

Key Dates:
Approved: November 2008
Effective: January 2009
Closing: June 2016

Financing in thousand US Dollars*;

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*Source MyTF as of March 2015; Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Context: Since its political transformation in 2000, Serbia has accelerated its justice sector reforms, recognizing their importance for EU accession. The reform efforts were focused on strengthening governance, improving the business climate, combating corruption, and improving state accountability and effectiveness. However, the overall reform impact so far has been less than anticipated; public trust and confidence in the judiciary remain low, institutional capacity constraints affect reform coordination, and the implementation of fragmented donor-financed projects and programs have outpaced the already low capacity of the Ministry of Justice (MOJ), whose overall ability to coordinate, prioritize, sequence, resource, and implement a multiyear sectoral strategy remains weak.

The Project Development Objective is to facilitate the acceleration of Serbia’s EU integration pertaining to the justice sector by providing an appropriate financing vehicle, the necessary tools, focused short-term analytical and policy advice, and capacity-building technical assistance to Serbia’s MOJ and judiciary. This “hybrid” trust fund consists of five components, where the second component is executed by the Client and other components are executed by the Bank. Component 1 provides advisory services to strengthen justice sector reform in the areas of: (i) Institutional Capacity Building of MOJ, the judiciary, and the Ministry of Finance (MoF); (ii) Resource Management and Aid Coordination; (iii) Legal and Institutional Environment; (iv) Judicial Facilities and Infrastructure; and (v) Outreach, Monitoring, and Evaluation. Component 2 provides technical assistance in the same five areas, as well as in the area of access to justice. Components 3, 4, and 5 cover supervision, administration, and program management of the trust fund.

Results Achieved:

Recipient Executed
The MOJ (i) created a Project Implementation Unit and a Reform Facilitation Unit, staffed with short-term and long-term experts in judicial reform; (ii) adopted the new Justice Reform Strategy for the period 2013–2018; (iii) developed a comprehensive IT strategy report for Serbia’s justice sector; (iii) shared leadership and organization of the Partners’ Forum; and (iv) in the area of access to justice, supported the drafting process for the preparation of a new Law on Free Legal Aid. The MDTF will support its implementation through the training of free legal aid providers and an outreach program for free legal aid users.

Bank Executed
- At the request of the European Commission, MOJ, and Serbian judiciary, the World Bank prepared a Serbian Judicial Functional Review, which is the main analytical input for the preparation of the Action Plan for opening negotiations under Chapter 23. The report was presented to Serbian judicial authorities and the wider public in January 2015. Together with the Chief Justice and representatives of the MOJ, the Functional Review was presented to the EU Commission in Brussels in February 2015.
- To support MOJ’s efforts to draft the Free Legal Aid Law, the Bank prepared two analytical products: the Fiscal Impact Analysis of the Free Legal Aid Law and the Cross Country Comparison of Free Legal Aid Mechanisms. Both reports were completed in January 2014.
- Supported the MOJ in the transformation process of the MDTF-JSS to a hybrid facility.
- Through advisory work, supported the production of a set of products: (i) through the Review of the Results and Implementation Status of the 2006 National Judicial Reform Strategy and the facilitation of the collaborative effort, assisted the MOJ in developing the National Judicial Reform Strategy 2013–2018; (ii) supported a baseline survey of justice sector performance and service delivery in 2010; and (iii) delivered the Judicial Public Expenditure and Institutional Review in early 2012.
- In the area of resource management, the capacity-building program to support the introduction of an automated case management system in courts of general jurisdiction was completed in 2010.
- The trust fund has a critical role in co-leading the work of the Partners’ Forum, which brings together the representatives of international donor partners who are the trust fund contributors.
- As an outreach tool, a trust fund website was established (www.mdtfiss.org.rs).

Key Partners: The Bank team worked closely with (i) the Ministry of Justice of the Republic of Serbia; (ii) High Judicial Council, State Prosecutorial Council, Republic Prosecutor Office, and other key justice sector institutions, and (iii) MDTF-JSS Contributing Partners (EU Delegation, SIDA, DfID, and the Governments of Switzerland, Slovenia, Denmark, the Netherlands, Spain, and Norway).

Key Development Partners included USAID, Council of Europe, and Organization for Security and Cooperation in Europe (OSCE), with which the Bank team coordinated closely on reform priority issues.
In an attempt to modernize the national innovation system, the Government of Serbia has implemented a series of reforms focused primarily on the public research and development (R&D) sector, including science infrastructure improvement. This project addresses some missing elements of the Serbian innovation system and ailing aspects of the research sector that are likely to be vital for improving Serbia’s long-term competitiveness.

The Project Development Objective is to assist in building the institutional capacity to stimulate innovative activities in the enterprise sector by: (i) supporting the operationalization of the Serbia Innovation Fund (IF); (ii) piloting financial instruments for technological development and innovation in enterprises; and (iii) encouraging selected research and development institutes (RDIs) to engage in technology transfer and commercialization and assisting in formulating RDI sector reform policy.

Results Achieved:

**Recipient Executed**

Capacity Building of the Innovation Fund (IF):
- Strong advisory team established in the IF, including strategic, operations, and regional advisors.
- Diaspora-led Investment Committee established, with experience in venture funds, technology, and research sectors.
- IF staff trained internationally on due diligence and management of innovation support programs.

Implementation of Financial Instruments to Support Enterprise Innovation:
- Two grant programs (mini and matching) established to finance innovative ideas in start-ups and technology development in existing firms.
- Four calls for proposals conducted in the period 2012–14, with a total of 53 awardees: 12 matching grant and 41 mini-grant awardees.
- Notable results: 11 companies have generated revenue from the sale or lease of their innovative products; seven companies have established international cooperation; and two companies have secured distributors for the U.S. market.
- In order to protect intellectual property, companies have submitted eight Patent Cooperation Treaty (PCT) applications, three European Patent Office (EPO) applications, and five U.S. patent applications, along with patent applications in China, Australia, India, and Japan.
- At the national level, 23 patent applications have been submitted, together with eight trademark applications and six copyright applications, and 13 companies have established new business cooperation or partnerships.

**Bank Executed**

Technical Assistance to Research and Development Institutes:
- Detailed technical assessment reports delivered to four RDIs, focused on improving management, technology transfer, and commercialization practices. Detailed technical support provided in an attempt to commercialize selected pool of innovative project proposals.
- Three high-level workshops have been delivered to participating RDIs, focusing on RDI institute management, RDI sector reform, and technology transfer.
- Mini Policy Note on the RDI sector delivered upon the request of the Ministry of Education, Science and Technological Development (MoESTD) to guide the Government’s RDI sector reform program.

Key Partners: The Bank team works closely with (i) the MoESTD, which is leading the science, technology, and innovation reform program in Serbia, (ii) the IF, which is implementing Components 1 and 2 of the project, and (iii) Serbian RDIs, the main recipients of technical assistance under Component 3. Through the project Steering Committee, the team also engages the Ministry of Finance and Economy, the National Council, and the EU Delegation. Key Development Partners include the European Commission. The EC is funding this initiative through the European Union Instrument for Pre-Accession Assistance (IPA) 2011 funds that support the national innovation system.
SERBIA: RESEARCH, INNOVATION, AND TECHNOLOGY TRANSFER PROJECT (TRUST FUND)

Key Dates
Approved: December 2014
Closing: July 2018

Financing in million US Dollars*

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</tbody>
</table>

*As of March 2015.

Context: Building on the institutional capacity developed under the Serbia Innovation Project (SIP), the new Serbia Research, Innovation and Technology Transfer Project (SRITTP) aims to design and pilot programs to facilitate the commercialization of public sector research and development (R&D), support collaborative research between public sector R&D organizations and private industry, and facilitate strategic planning to enhance Serbia’s competitive positioning in the European research community.

In order to stimulate the transfer of public research, this project will support efforts to enhance the technology transfer capacity and effectiveness of local institutions. Joint research-industry projects are crucial to improving the competitiveness of Serbia’s enterprises, as well as to establishing the enhanced capacity of both RDIs and enterprises to participate in the EU’s next framework program for innovation, Horizon 2020. Aimed at facilitating further strategic planning, the project will support the design of the new Research and Innovation Strategy, which will focus on systematically improving research excellence as well as the economic impact of R&D and innovation support programs.

The Project Development Objective is to facilitate the reorientation of the public research sector toward the needs of the private sector. The project will support a framework for increasing the efficiency of future investments in research and innovation in Serbia and will consist of the following parts: (1) Establishment of a technology transfer facility (recipient executed); (2) Technical assistance for the design and implementation oversight of a collaborative R&D grant scheme by the Innovation Fund (Bank executed); and (3) Technical assistance for the development of a Research and Innovation Strategy and an R&D Infrastructure Roadmap and corresponding Action Plan(s) (Bank executed).

Expected Results:

- Establishment of a Technology Transfer Facility. In order to take advantage of the economies of scale, a centralized Technology Transfer Facility (TTF) will be established at the Innovation Fund (IF), which will provide support services to local Technology Transfer Offices (TTOs) and R&D and innovation support organizations to enhance their capacity and effectiveness to consummate deals.

- Design and implementation of a collaborative R&D grant scheme by IF. Under SRITTP, a Collaborative R&D Grant Scheme is proposed to foster pre-competitive, industry-driven research. The objective of the Collaborative R&D Grant Scheme is to encourage stakeholders to increase collaborative activities, foster closer links between research and industry, and utilize existing infrastructure in public sector R&D institutions. The Collaborative R&D Grant Scheme will provide financial assistance (grants of up to €300,000) to third parties with the aim of bringing together ideas/projects with the best potential from the private and research sector to implement activities that will, on the one hand, explore the research and technological potential, and on the other, provide clear prospects for commercial use and exploration.

- Development of a Research and Innovation Strategy and an R&D Infrastructure Roadmap and corresponding Action Plan(s). The project will provide support to the MoESTD in the design of the new Research and Innovation Strategy 2016–2020.

Key Partners: The Bank team works closely with (i) the MoESTD, which is leading the science, technology, and innovation reform program in Serbia and is the main recipient of the technical assistance under Component 3 of the project, and (ii) the IF, which is implementing Components 1 and 2 of the project through the Project Steering Committee. The team also engages with the Ministry of Finance, the Ministry of Economy, the National Council for Science and Technological Development, and the EU Delegation. Key Development Partners include the European Commission. The EC is funding this initiative through the European Union Instrument for Pre-Accession Assistance (IPA) 2013 funds that support the national innovation system.
Projects Closed in the Last Six Months
(IBRD)
SERBIA: DELIVERY OF IMPROVED LOCAL SERVICES (DILS) PROJECT

Key Dates:
Approved: March 18, 2008
Effective: March 10, 2009
Closed: March 31, 2015 (applies to health sector activities)
The education and social protection sector activities closed on December 31, 2013.

Financing in million US Dollars*:

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<tr>
<td>Total Project Cost</td>
<td>42.88**</td>
<td>36.45</td>
<td>6.43</td>
</tr>
</tbody>
</table>

*As of July 30, 2014. **Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Context at Project Design: The Government has been considering decentralizing service delivery and reforming the intergovernmental public finance system, which are both critical to improving health, education, and welfare outcomes in Serbia. In these social sectors, decentralization was seen as a key feature of the sector strategies adopted by the line ministries toward achieving the desired improvements.

The Project Development Objective (PDO) was to increase the capacity of institutional actors and beneficiaries in order to improve access to, and the efficiency, equity, and quality of, the local delivery of health, education, and social protection services in a decentralizing environment. Project restructuring took place in July 2012, when the project description and the results framework were refined.

The range of sector issues addressed by the project included: (1) transforming financing models through the development of a public financing framework that increases efficiency while compensating for inequities across municipalities and promoting rationalization of the service networks at the local level; (2) improving access and equity through the use of new approaches and models for delivering services to excluded groups; (3) improving accountability and quality by supporting sector ministries, local authorities, and other local service providers to assume their new roles and responsibilities, including regulation, oversight, quality assurance, management, planning, budgeting, and service delivery; and (4) supporting project implementation.

Results Achieved to date:

Education
- **Financing**: National per student funding formula for pre-university education (primary and secondary schools) has been developed, and local formulas are being developed through the pilots. The first pilot took place in 16 (10 percent) of Serbia’s municipalities in the school year 2011–12. Piloting continued in 2013 in order to make further progress on adjustments to the local formulas. By project closure, this activity had been partially completed.
- **Access and equity**: School and municipal grants were used in support of capacity building for the inclusive education of children with learning difficulties, disabilities, and/or socioeconomic disadvantages (including Roma), where schools and preschools benefit from teacher training (21,000 participants), small civil works, and the purchase of various teaching tools and equipment.
- **Accountability and quality**: Student learning outcomes were monitored through Serbia’s participation in the Program for International Student Assessment (PISA) 2009 and 2011, Trends in International Mathematics and Science Study (TIMSS) 2011, and the Teaching and Learning International Survey (TALIS) 2013, as well as through the strengthening of the school external evaluation system.

Health
- **Financing**: With amended health legislation, current laws and bylaws allow the use of capitation- and output-based formulas; and a framework with methodology and criteria for the allocation of equalization funds has been developed (both PDOs met).
- **Access and equity**: Nearly 2,000 medical staff and associates have been trained to recognize the needs of vulnerable groups; 15 Roma health mediators were financed from the loan funds, resulting in 19,818 vaccinated children, over 2,500 registered with a primary health care (PHC) physician, 600 pregnant and new mothers receiving health checks, and more than 1,200 women able to choose a gynecologist. In 2012, the Government institutionalized Roma health mediators by funding their salaries from the Republic of Serbia national budget.
- **Accountability and quality**: 51 percent of PHC centers have completed the quality accreditation process; all of the targeted 50 PHC centers have adopted clinical pathways, and 86 percent of PHCs use the fully operational health management information system (HMIS) platform.

Social Protection
- **Access and equity**: Internal operating procedures of the Disability Fund of the Ministry of Labor, Employment and Social Policy (MoLESP) reformed to enable funding of the results-oriented projects; and innovative services have been developed, piloted, and scaled up across the country (sign language interpretation services for the deaf and escort services for the blind and people with impaired vision).
- **Accountability and quality**: The development of the management information system (MIS) in the MoLESP is completed. Funds for the MIS to finance infrastructure and communication costs have been secured by the MoLESP for 2014 to complete MIS implementation, which reflects MoLESP’s commitment to this important intervention.

Key Partners: The Bank team worked closely with (i) the Ministry of Health, Ministry of Education, and Ministry of Labor and Social Policy, as beneficiary agencies; and (ii) the Standing Conference of Towns and Municipalities, as the key national partner in contact with local authorities.

Key Development Partners included the European Commission, the World Health Organization (WHO), the United Nations Children’s Fund (UNICEF), United Nations Development Programme (UNDP), the UK Department for International Development (DFID), and the Swiss Agency for Development and Cooperation (SDC).
IFC Projects - Active
Victoria is a leading agro-industrial group in Serbia, with a primary focus on processing soybean and sunflower oilseeds and grain trading. The Group employs over 1,800 people. IFC’s loan of €57 million (US$74.13 million equivalent) will be used to finance the Group’s permanent working capital financing needs and restructure its debt financing toward a longer-term, more stable structure that is suitable for the nature of the Group’s operations. The long-term facility will be used partially to provide the input financing to farmers needed to produce oilseeds for processing on the Group’s plants. Thereby, IFC’s investment is expected to strengthen the support to farmers and increase the sustainability of the Group’s operations.

The Project Development Objective. IFC provided Victoria Group with long-term financing that is currently not possible to secure from commercial banks or capital markets locally. By providing a loan to Victoria Group, IFC is supporting the development of the private sector in Serbia, where revitalizing agribusiness is essential for creating jobs and lowering a 20 percent unemployment rate.

The development impact of the project is expected to include:

- Strengthening agribusiness linkages and support to farmers: given the strong linkages of Victoria Group with farmers, provision of longer-term permanent working capital will help ensure the stable access of pre-harvest financing to farmers.
- Preserving jobs: the Group employs about 1,800 people across its operation and collaborates with about 400 partners, which in turn supply the Group from over 25,000 farmers.
- Increasing tax revenues: IFC’s investment will contribute to the growth of government revenues from taxation.
- Addressing food security concerns: IFC’s investment will contribute to food security and to meeting the challenges of increasing demand and the food crisis.

IFC’s expected additionality includes:

- Crisis response and countercyclical support: In light of the fluid economic situation in Serbia in the context of the Eurozone crisis, the local banking sector has cut liquidity on the domestic market. Through the project, IFC is stepping up its presence on the local market, helping to restore confidence and increase investment in Serbia.
- Diversified funding base: At a time of financial strain for local banks, IFC is starting its relationship with Victoria, a new partner that will benefit from a further diversified funding base as a result of IFC’s presence.

Key Partners: N/A.
Serbia: Société Générale

Key Dates:

Approved: June 18, 2012
Signed: June 25, 2012

IFC Financing (million US Dollars):

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<td>2012</td>
</tr>
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</table>

In the context of the Joint IFI Action Plan for Central and Eastern Europe (CEE), Société Générale (SocGen), which is the French bank with the largest exposure in the CEE region, has approached IFC to provide an investment package to eight subsidiaries, including Serbia, for an aggregate investment amount of up to €270 million (equivalent US$365 million). IFC provided Société Générale Srbija with a €70 million (US$94.5 million equivalent) loan to increase access to finance for Serbian agribusinesses, supporting economic growth, employment, and exports. In 2010, IFC also approved a €40 million agribusiness loan to Société Générale in Serbia.

The Project Development Objective. The loan is part of IFC’s strategy to strengthen the region’s banking sector and support the country’s economic recovery by boosting lending to the agribusiness sector. In Serbia, about 45 percent of the population lives in rural areas and about one-third rely on agriculture for their livelihood. Agriculture is a key part of Serbia’s economy, accounting for about 20 percent of GDP. In 2011, Serbia’s total agricultural exports increased by 20 percent year-on-year, reaching US$2.8 billion (€2.2 billion).

The development impact of the project is expected to include:

- Strengthening financial institutions in Serbia
- Supporting agribusiness projects in Serbia in partnership with SocGen subsidiaries
- Contributing to economic growth and poverty reduction

IFC’s expected additionality includes:

- Enhancing the capacity of SocGen subsidiaries in Serbia to provide funding to agribusinesses whose access to finance has been curtailed by the global financial crisis
- Providing financing under the Joint IFI Action Plan

Key Partners: N/A.
IFC provided a €20 million loan to PMC Automotive Serbia, a new metal-stamping factory near Kragujevac, to strengthen Serbia’s car industry and boost the overall economy. PMC Automotive Serbia is a joint venture between CLN Group and PROMA Group, two Italian automotive suppliers. The PMC factory will supply parts to FIAT’s plant in Kragujevac. The FIAT plant will manufacture the new FIAT 500L, a subcompact car with improved fuel efficiency. The current production capacity of the FIAT plant, 20,000 cars per year, is expected to grow to 140,000 cars per year in 2013, and possibly more than double that number by 2015.

The Project Development Objective. The PMC factory, located in a supplier park less than a kilometer from FIAT’s plant, is expected to generate 370 jobs. The total cost of the project is estimated at €37 million. The project will strengthen Serbia’s car industry and generate new exports.

The development impact of the project is expected to include:

- Sustainable employment creation: The project is expected to create at least 367 skilled jobs in Sumadija District, a frontier region of Serbia.
- Support for foreign direct investment (FDI) in Serbia: Channeling FDI is a priority for Serbia. The project will contribute to balancing Serbia’s large current account deficit.
- Support for export-oriented industry: The project will sell its products to FIAT’s assembly plant in Kragujevac, which will export 90 percent of its production.
- Technology transfer: CLN and PROMA are FIAT-trusted suppliers and have state-of-the-art technologies and efficient processes. Local staff will be trained to new, highly competitive standards.

IFC's expected additionality includes:

- Crisis response and countercyclical role: Current market conditions in Europe magnify IFC’s countercyclical role, as most of the European banks, especially the Italian banks that are active in Eastern Europe, have been limiting their exposure to emerging markets due to funding and capital constraints. By providing long-term financing that matches the cash flow of the project, IFC is sending a signal to the market that it is willing to finance sound projects and companies.
- Risk mitigation: CLN and PROMA are still in the early stages of their expansion to emerging markets and the project is their first investment in Serbia. Partnering with IFC, especially in frontier regions, provides comfort to CLN and PROMA in terms of country knowledge and contacts in the public and private sectors.

Key Partners: N/A.
Based in Belgrade and Novi Sad but with operations across Serbia and Ukraine, the MK Group is involved in (i) agricultural crop production; (ii) sugar production; (iii) storage, transportation, and trading of agricultural commodities, and (iv) other miscellaneous activities. Established in 1983, the MK Group is a privately owned company and a market leader in all of its key lines of business. MK Group has embarked on a €87 million investment plan that consists of: (i) the acquisition of Carnex AD Meat Industry (“Carnex”), the Serbian brand leader in processed meat products; (ii) the upgrade and expansion of Carnex’s vertically integrated operations; and (iii) the expansion and modernization of the Group’s primary agriculture operations. IFC’s support to this project entails two loans: €45 million (US$55.82 million equivalent) and €25 million (US$33.5 million equivalent).

The Project Development Objective. IFC provided MK Group with long-term financing that is currently not possible to secure from commercial banks or capital markets locally. By providing a loan to MK Group, IFC is supporting the development of the private sector in Serbia, where revitalizing agribusiness is essential to creating jobs and lowering a 20 percent unemployment rate. IFC’s loan will enable the Group to further diversify and expand its operations in sectors where it already operates as well as adjacent industries, namely livestock and meat production.

The development impact of the project is expected to include:
- Operational turnaround and efficiency improvements at Carnex, a large employer and former regional leader
- Support to an agricultural company involved in value-added production in a sector important to Serbia’s economy
- Extension of the MK Group’s reach to farmers and improvements in the agricultural infrastructure
- Demonstration effect by encouraging other companies to invest in the region
- Increased tax revenues

IFC’s expected additionality includes:
- enabling the company to conservatively leverage its growth through acquisition and investment upgrades by providing financing at reasonable rates as well as longer tenors appropriate for the type of investment and not otherwise available in the country
- diversifying the Group’s funding base
- sharing its global and industry knowledge as the Group enters new product segments

Key Partners: N/A.
MIGA issued €7.125 million (US$8.47 million) and €0.475 million (US$0.56 million) guarantees to Bank Austria Creditanstalt AG for its €7.5 million loan guarantee and €0.5 million shareholder loan made in support of HVB Banka Jugoslavija a.d. (HVB-SAM) in Serbia and Montenegro. The guarantees are for a period of 10 years and provide coverage against the risks of transfer restriction, expropriation, and war and civil disturbance.

HVB-SAM was established in December 2001 and offers a wide range of products and services, including payment services, deposits, and term account maintenance; trade finance services and corporate finance, including long-term lending and treasury services; and investment banking services.

The project will provide for an expansion of HVB-SAM operations by allowing it to increase its lending portfolio, mainly to small and medium-sized enterprises (SMEs), including retailers, and general commerce and food-related enterprises. HVB-SAM's additional loans will be provided predominantly to SMEs, which will increase SMEs’ access to financing and support economically sound projects.
MIGA has provided Raiffeisenbank a.s of the Czech Republic a US$24.8 million guarantee covering its non-shareholder loan to Raiffeisen Leasing d.o.o. (RLSM) in Serbia and Montenegro. The guarantee covers the risks of transfer restriction and expropriation for a period of five years. This is the third project supported by MIGA involving a loan to RLSM.

The project is part of an overall regional expansion strategy of Raiffeisen International Bank-Holding AG. By expanding operations in Serbia and Montenegro, RLSM will increase the availability of financing alternatives, providing leasing services to manufacturers and exporters in Serbia and Montenegro, mostly SMEs.
MIGA issued a guarantee for US$11.7 million to Bank Austria Creditanstalt (BACA) AG covering its guaranty for a loan made by the German Development Bank (Kreditanstalt für Wiederaufbau, KfW) to BACA’s subsidiary, HVB Banka Serbia and Montenegro a.d. (HVB-SAM), in Belgrade, Serbia and Montenegro. The guarantee is for 10 years, and covers the risks of transfer restriction, expropriation, and war and civil disturbance.

MIGA issued two guarantees to the investor covering an €8 million investment in the project in fiscal 2004. The project is expected to increase longer-term financing and generate competitive pricing for retail and corporate clients. The funds will be dedicated almost exclusively to SMEs, including in the retail and food sectors. HVB-SAM is expected to play an important role in the ongoing restructuring of Serbia and Montenegro’s financial sector by providing knowledge, technical solutions, and new products. HVB-SAM employs 146 staff in seven branches and expects to add more local employees over the next five years. HVB-SAM’s staff will benefit from on- and off-site training.

The project is part of an overall World Bank Group effort to help Serbia and Montenegro stimulate short-term growth and build effective institutions.
RAIFFEISEN LEASING D.O.O. (RLRS)

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<tr>
<th>Project name</th>
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<tr>
<td>Project ID</td>
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<td>Status</td>
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MIGA has issued a guarantee of up to US$40.1 million covering Raiffeisen Zentralbank Österreich AG’s (RZB) €30 million shareholder loan to its subsidiary, Raiffeisen Leasing d.o.o. (RLRS) in Serbia. The coverage is for a period of up to six years against the risks of transfer restriction and expropriation of funds.

The Serbian financial sector is currently feeling the effects of the financial crisis and experiencing a flattening of customer demand. At the same time, leasing products as a financing vehicle for SMEs are vital. Therefore RZB plans to extend this €30 million loan to allow RLRS to continue to serve its existing clients, as well as generate new business. This would be MIGA’s fifth guarantee in support of this project.

This project is expected to contribute to the development of the financial sector in Serbia by improving access to finance, particularly to segments of the economy that are currently underserved. The project will meet the increasing demand for leasing as a form of asset financing.

One of the main objectives of the World Bank Group’s Country Partnership Strategy for Serbia, which is broadly structured around the Serbian Government’s development strategy, is encouraging dynamic private sector–led growth. The project is consistent with this objective, as it will support investment flows into Serbia at a time when investor appetite has largely disappeared due to the ongoing global financial crisis.
### Project Details

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<tr>
<th><strong>Project name</strong></th>
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<td><strong>Gross exposure</strong></td>
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MIGA has issued a guarantee of up to €95 million covering UniCredit Bank Austria AG’s (UBA) €100 million shareholder loan to its subsidiary, UniCredit Bank Serbia JSC (UBSR). The coverage is for a period of up to five years against the risks of transfer restriction, expropriation, and war and civil disturbance.

The loan will provide UBSR with long-term liquidity and improve UBSR’s asset-liability management by matching assets and funding of similar maturities. The loan is part of a broader funding strategy of the UniCredit Group to finance its subsidiaries and is particularly important in view of the current turmoil in financial markets worldwide, including Serbia.

MIGA supports this project in conjunction with the Financial Sector Initiative framework recently presented to MIGA’s Board of Directors as part of a coordinated international response to the ongoing global financial crisis. Serbia, like many other countries in the Europe and Central Asia region, is currently facing difficult fiscal adjustments along with the need for external financing. MIGA’s support to the project will supplement the International Monetary Fund’s program for Serbia by injecting liquidity into the UBSR, boosting confidence in Serbia’s financial sector, and contributing to the improvement of the country’s financial stability.

One of the main objectives of the World Bank Group’s Country Partnership Strategy for Serbia is to encourage dynamic private sector–led growth. The proposed project is fully consistent with this objective.
MIGA has issued a guarantee of up to US$13.8 million covering Raiffeisen Zentralbank Österreich AG’s (RZB) €10 million shareholder loan to its leasing subsidiary, Raiffeisen Rent d.o.o. (RRRS) in Serbia. The coverage is for a period of up to six years against the risks of transfer restriction and expropriation of funds.

The Serbian leasing market is currently feeling the effects of the financial crisis, with most leasing entities experiencing a decrease in liquidity. At the same time, the demand for operating leases as an asset financing option continues to increase for SMEs. RZB plans to extend this €10 million loan to allow RRRS to maintain its business by servicing its existing clients and to expand its operations by attracting new clients. This is MIGA’s sixth guarantee in support of RZB’s leasing subsidiaries in Serbia.

This project is expected to contribute to the development of the financial sector in Serbia by improving access to finance, particularly to segments of the economy that are currently underserved. The project will also help meet the increasing demand for leasing as a form of asset financing. The project is consistent with the World Bank Group’s Country Partnership Strategy for Serbia. The strategy supports the encouragement of private sector–led growth and also provides opportunities and broadens participation in growth.
 PROCUREMENT CENTRAL BANK MANDATORY RESERVES COVERAGE

<table>
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On December 22, 2010, MIGA issued a guarantee of US$4.4 million to ProCredit Holding (PCH) covering its investment in its subsidiary in Serbia. The coverage is for a period of up to 10 years against the risk of expropriation of funds for mandatory reserves held by the subsidiary in the central bank of its jurisdiction.

This project is part of a master contract that MIGA has issued. PCH is headquartered in Germany and is the parent company of 21 banks (ProCredit group). The ProCredit group is a provider of finance to some 750,000 micro, small, and medium-sized enterprises (MSMEs) in Latin America, Eastern and Central Europe, and Africa. Throughout the world, banks are required to maintain mandatory reserves with the central banks of their respective jurisdictions. The ProCredit group’s capital adequacy ratio (CAR) is calculated according to the German Banking Act. Under this act, at a consolidated level, reserves deposited at the various central banks can attract a risk weighting of 100 or even 150 percent, depending on the country. This risk weighting determines the amount of equity required to maintain a specified CAR in accordance with the German Banking Act.

The guarantee issued by MIGA will help PCH obtain capital relief from the CAR requirements. By obtaining MIGA’s insurance against the risk of expropriation of funds, the risk weighting for mandatory reserves held at the central bank can be reduced. A lower risk weighting will allow PCH to free up equity currently tied up for CAR maintenance purposes, thereby allowing these funds to be injected into its subsidiary banks. This in turn will allow PCH’s emerging market subsidiary banks across its network to increase their lending activities.

MIGA’s support will help PCH optimize its capital management across its 21 banks, allowing PCH to direct equity to subsidiaries with the greatest need. These banks will be able to offer additional financial services to MSMEs at a time of macroeconomic challenges. Supporting productive small businesses will help stimulate growth, generate employment, and reduce poverty.

MIGA’s support for this project is aligned with the World Bank Group’s microfinance strategy, which includes improving the supply of microfinance in large but underserved markets; enhancing deposit capacity by assisting microfinance institutions in savings mobilization; promoting capacity building; creating and shaping markets; and fostering innovation.
On July 28, 2011, MIGA issued a guarantee of US$80.6 million to ProCredit Holding (PCH) covering its investment in its subsidiary in Serbia. The coverage is for a period of up to 10 years against the risk of expropriation of funds for mandatory reserves held by the subsidiary in the central bank of its jurisdiction.

MIGA was previously covering a total of US$4.4 million under the project. The additional coverage of US$80.6 million complies with ProCredit’s request to convert outstanding capacity to current coverage in order to consolidate all of its political risk insurance requirements under the MIGA framework.

This project is part of a master contract that MIGA has issued. PCH is headquartered in Germany and is the parent company of 21 banks (ProCredit group). The ProCredit group is a provider of finance to some 750,000 MSMEs in Latin America, Eastern and Central Europe, and Africa. Throughout the world, banks are required to maintain mandatory reserves with the central banks of their respective jurisdictions. Currently, the ProCredit group’s capital adequacy ratio (CAR) is calculated according to Basel II, but in the future it will also be calculated according to the German Banking Act. Under this act, at a consolidated level, reserves deposited at the various central banks can attract a risk weighting of 100 or even 150 percent depending on the country. This risk weighting determines the amount of equity required to maintain a specified CAR in accordance with the German Banking Act.

PCH has approached MIGA to obtain capital relief from the capital adequacy ratio requirements. By obtaining MIGA’s insurance against the risk of expropriation of funds, the risk weighting for mandatory reserves held at the central bank can be reduced. A lower risk weighting would allow PCH to free up equity currently tied up for CAR maintenance purposes, thereby allowing these funds to be injected into its subsidiary banks. This in turn will allow PCH’s emerging market subsidiary banks across its network to increase their lending activities.

MIGA’s support will allow PCH to direct equity to subsidiaries with the greatest need. The additional services these banks will be able to offer will help stimulate growth, generate employment, and reduce poverty.

MIGA’s support for this project is aligned with the World Bank Group’s microfinance strategy, which includes improving the supply of microfinance in large but underserved markets; enhancing deposit capacity by assisting microfinance institutions in savings mobilization; promoting capacity building; creating and shaping markets; and fostering innovation.
MERCATOR – SERBIA

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On July 15, 2011 MIGA issued a guarantee of US$12.8 million for reinsurance of the SID Bank, Inc.; Ljubljana coverage to the Mercator retail group (Mercator) in Serbia. MIGA’s reinsurance for the investment results in a gross exposure of US$277.4 million. MIGA is reinsuring the investment for a period of up to six years, against the risks of transfer restriction, expropriation, and war and civil disturbance.

MIGA’s support to SID Bank, Inc.; Ljubljana is in accordance with MIGA’s mandate to cooperate with national entities of its member countries, as stated in MIGA’s Convention. By providing facultative reinsurance, MIGA is allowing SID Bank, Inc.; Ljubljana to reduce its net exposure to Mercator and to free up capacity for other investment insurance projects.

Mercator is helping to stimulate exports among Balkan countries by carrying goods from the other countries in each of its retail locations. As a result, Mercator is expanding the venue for suppliers to sell not only in their respective countries but also in neighboring countries where Mercator has an established presence. In addition, Mercator’s further expansion in the Balkans, supported by SID Bank, Inc.; Ljubljana and MIGA, will provide employment and retail training opportunities in these countries.

MIGA is also helping to establish best practices with respect to corporate governance, as well as environmental and social policies in the host countries.
On July 15, 2011, MIGA issued a guarantee of US$16.7 million for reinsurance of the SID Bank, Inc.; Ljubljana coverage to the Mercator retail group (Mercator) in Serbia. MIGA’s reinsurance for the investment results in a gross exposure of US$277.4 million. MIGA is reinsuring the investment for a period of up to six years, against the risks of transfer restriction, expropriation, and war and civil disturbance.

MIGA’s support to SID Bank, Inc.; Ljubljana is in accordance with MIGA’s mandate to cooperate with national entities of its member countries, as stated in MIGA’s Convention. By providing facultative reinsurance, MIGA is allowing SID Bank, Inc.; Ljubljana to reduce its net exposure to Mercator and to free up capacity for other investment insurance projects.

Mercator is helping to stimulate exports among Balkan countries by carrying goods from the other countries in each of its retail locations. As a result, Mercator is expanding the venue for suppliers to sell not only in their respective countries but also in neighboring countries where Mercator has an established presence. In addition, Mercator’s further expansion in the Balkans, supported by SID Bank, Inc.; Ljubljana and MIGA, will provide employment and retail training opportunities in these countries.

MIGA is also helping to establish best practices with respect to corporate governance, as well as environmental and social policies in the host countries.
On March 1, 2013, MIGA issued a guarantee totaling €190.0 million (approximately $250.1 million) covering an investment by Eurobank Ergasias S.A. (Eurobank) of Greece in its Serbian subsidiary, Eurobank AD Beograd. The coverage is for a period of three years against the risk of expropriation of funds for mandatory reserves held by the subsidiary in the central bank of its jurisdiction.

Eurobank is a universal banking group with a significant network of retail banks across Central, Eastern, and Southeastern Europe. The group’s subsidiary banks are required to maintain mandatory reserves at the central banks of their respective jurisdictions, generally based on the volume of customer deposits that these subsidiaries hold. The banks are thereby exposed to the risk of expropriation of funds by the respective central bank. This exposure leads to higher risk weights on these assets at the consolidated level, resulting in increased capital allocation for country risk exposure. At the consolidated group level, the risk weighting determines the amount of equity required to maintain a specified capital adequacy ratio (CAR) in accordance with Greek banking law.

MIGA’s guarantee will help Eurobank obtain capital relief from the CAR requirements. By obtaining MIGA’s insurance against the risk of expropriation of funds, the risk weighting for mandatory reserves held at the central bank can be reduced. This will free up equity tied up for country risk purposes, which can be deployed to support its subsidiary’s franchise in Serbia. Eurobank Beograd’s role in supporting productive businesses, including SMEs, through credit extension helps stimulate growth, employment generation, and—ultimately—poverty reduction in Serbia.

As a participant of the European Bank Coordination Initiative (also known as the Vienna Initiative), Eurobank pledged to support its Serbian subsidiary, keeping it well capitalized. Eurobank’s continuing support for its systemically important subsidiary contributed to supporting the Serbian economy in the aftermath of the financial crisis. Capital adequacy well in excess of the regulatory requirement provides Eurobank Beograd in Serbia with a cushion to withstand potential shocks and helps position the bank for future growth.

MIGA’s coverage to Eurobank is consistent with the goals of the crisis response initiative for the ECA region launched by the World Bank Group in January 2012. As part of the initiative, MIGA seeks to support capital-constrained banks active in the region. The project is also aligned with the World Bank Group’s strategy for Serbia as it seeks to address the spillover from the financial crisis.