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**INTERNATIONAL FINANCE CORPORATION**

**MULTILATERAL INVESTMENT GUARANTEE AGENCY**

**COUNTRY PARTNERSHIP FRAMEWORK**

**FOR**

**SERBIA**

**FOR THE PERIOD FY16-FY20**

**May 22, 2015**

**South East Europe Country Management Unit  
Europe and Central Asia**

**The International Finance Corporation  
Europe and Central Asia**

**The Multilateral Investment Guarantee Agency**

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## CURRENCY EQUIVALENTS

Exchange Rate Effective April 1, 2015  
Currency Unit – Serbian Dinar (RSD) 100.00 = US\$ 0.895

## FISCAL YEAR

January 1 – December 31

## ABBREVIATIONS AND ACRONYMS

AAA	Analytical Advisory Services	MIGA	Multilateral Investment Guarantee Agency
IPF	Investment Project Financing	MoF	Ministry of Finance
BEEPs	Business Environment and Enterprise Surveys	NALED	National Alliance for Local Economic Development
B40	Bottom 40 percent of the population		
ALMPs	Active Labor Market Programs	NBS	National Bank of Serbia
CPF	Country Partnership Framework	NES	National Employment Service
CMU	Country Management Unit	NPLs	Nonperforming Loans
CPS	Country Partnership Strategy	OECD	Organization for Economic Co-operation and Development
DLIs	Disbursement Linked Indicators	PEFA	Public Expenditures and Financial Accountability
DIA	Deposit Insurance Agency	PIFC	Public Internal Financial Control
ECA	Europe and Central Asia	PLR	Performance and Learning Review
EC	European Commission	PPO	Public Procurement Office
ECD	Early Childhood Development	PPPs	Public-Private Partnerships
EBRD	European Bank for Reconstruction and Development	RC	Republic Commission for the Protection of Rights in Public Procurement Procedures
EIB	European Investment Bank	SAA	Stabilization and Association Agreement
EPS	Elektroprivreda Srbije	SAI	State Audit Institution
EU	European Union	SCD	Systematic Country Diagnostic
FDI	Foreign Direct Investment	SEE	South East Europe
FSC	Financial Stability Committee	SEIO	Serbia European Integration Office
GCI	Global Competitiveness Index	SILC	Survey on Income and Living Conditions
GDP	Gross Domestic Product	SOE	State-Owned Enterprise
HBS	Household Budget Survey	SORT	Standardized Operations Risk-rating Tool
IBRD	International Bank for Reconstruction and Development	T60	Top 60 percent of the population
IEG	Internal Evaluation Group	TFs	Trust Funds
IFC	International Finance Corporation	UAE	United Arab Emirates
IFIs	International Financial Institutions	UN	United Nations
IMF	International Monetary Fund	UNDP	United Nations Development Programme
LITS	Life in Transition Surveys	WB	World Bank
LPI	Logistics Performance Index	WBG	World Bank Group
LSMS	Living Standards Measurement Survey	Zeleznice Srbije	Railways of Serbia

	<b>IBRD</b>	<b>IFC</b>	<b>MIGA</b>
<b>Vice President:</b>	Laura Tuck	Karin Finkelston	Keiko Honda
<b>Director:</b>	Ellen A. Goldstein	Tomasz A. Telma	Ravi Vish
<b>Task Team Leader:</b>	Tony Verheijen	Thomas Lubeck	Franciscus Linden
	Lazar Sestovic	George Konda	

The last Country Partnership Strategy for the Republic of Serbia, Report No. 65379-YF, was discussed by the Board of Executive Directors on November 15, 2011. The last CPS Progress Report was dated August 25, 2014

# WBG - COUNTRY PARTNERSHIP FRAMEWORK FOR SERBIA

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# **FY16-20 COUNTRY PARTNERSHIP FRAMEWORK FOR SERBIA**

## **I. INTRODUCTION**

- 1. This program document presents the WBG program and results framework for the Serbia Country Partnership Framework (CPF) for FY16–20.** Serbia’s last Country Partnership Strategy (CPS) covered the period FY12-15, with the CPS Progress Report delivered on August 25, 2014. The timing of the new CPF follows the preparation of the Systematic Country Diagnostic (SCD) that informs the priorities and direction of the CPF to meet the World Bank Group’s (WBG) twin goals of reducing poverty and boosting shared prosperity for the bottom forty percent of the population (B40).
- 2. The new CPF comes at an opportune moment. For the first time since 2001, when the transition to a market economy began accelerating, Serbia has a government with a solid majority in parliament, enabling it to initiate and implement the deep reforms necessary to create a competitive economy and raise the income of the bottom forty percent (B40).** In addition, Serbia started the process of negotiating for EU membership in 2014, creating a further impetus for reform and opportunities to attract investment. The disastrous floods of May 2014 diverted the government’s attention for the first 100 days of its mandate. Since then, steady progress has been made in developing a framework for structural reforms that would bring macro-fiscal sustainability and create a market oriented and competitive economy. The medium term fiscal strategy, adopted in February 2015, provides the strategic anchor for this reform program.
- 3. Notwithstanding the new momentum on economic and structural reforms, Serbia faces serious challenges, most notably in declining living standards. Poverty has increased rapidly since the start of the global economic crisis in 2008, mainly as a result of a triple dip recession.** As illustrated in the SCD, the bottom forty percent of the population has been particularly affected. Structural reforms may, in the short term, possibly aggravate this trend. Bringing back growth is an essential condition for changing this dynamic: the pre-crisis period has shown that growth benefits the B40 more than other segments of society. A shift towards an export-driven economic model should help Serbia grow faster in the longer-run. However, the SCD notes that the majority of the bottom 40 is unlikely to directly benefit from export-led growth. While jobs created in high-productivity export sectors can have an important multiplier effect in creating jobs in non-tradable sectors, this might not be sufficient to create jobs for the B40. Hence, additional reform measures are needed to open up employment opportunities and boost shared prosperity.
- 4. The CPF goal is to support Serbia in creating a competitive and inclusive economy and, through this, to achieve integration into the EU.** The CPF is fully aligned with WBG twin goals, reflects SCD priorities and builds on the WBGs comparative advantage. The SCD demonstrates that the goal of achieving poverty reduction and shared prosperity in Serbia requires an economic strategy which is equitable and export-oriented, and should have a strong focus on creating employment, with an

emphasis on those policies and measures that could create meaningful employment for the bottom 40 percent.

5. **The CPF benefited from extensive consultations conducted during the preparation of the SCD**, including stakeholder consultations across the country and a series of country team meetings involving the IFC, MIGA and IBRD teams. It has also been informed by the CPS Completion and Learning Review, included in Annex 2.

## II. COUNTRY CONTEXT AND DEVELOPMENT AGENDA

### 2.1 Social and Political Context

6. **Serbia, with a population of 7.2 Million, is at a pivotal stage in its political development.** For the first time in over a decade Serbia has a government that can count on a clear majority in parliament and has shown a commitment to move forward long delayed reforms. If a social consensus around these reforms can be maintained, this would help position Serbia to capitalize on its strategic location and to progress in its EU accession process.

7. **Serbia's political and economic transition picked up pace in 2001**, when the coalition government led by Prime Minister Zoran Djindjic took office. Serbia's GDP per capita at that point was less than half of its 1989 level. In 2001, the new government launched an ambitious reform program for a rapid transition to a more market-oriented economy, normalization of relations with foreign creditors, and integration with regional, European Union (EU) and world markets.

8. **Serbia's political trajectory since 2001 has been characterized by two main features: domestic political fragmentation and efforts towards international reintegration.** Domestically, following PM Djindjic's assassination in March 2003, the formation of coherent political coalitions became increasingly difficult, which led to a succession of generally short lived governments that lacked the coherence required to follow through on the ambitious efforts at reform that had been initiated since 2001. The March 2014 elections resulted in the creation of a government with a strong majority, giving Serbia a new opportunity to overcome the growing fragmentation that characterized the past and build a momentum for reform. Internationally, following a decade of ostracism, Serbia has sought reintegration with Europe and the broader international community, a process that has been protracted and complex.

9. **The domestic fragmentation of politics was in part driven by disagreements around Serbia's most difficult political challenge, which has been its relation with Kosovo.** Kosovo officially declared its independence in 2008, and while Serbia does not recognize it as an independent state, several agreements were signed in recent years, allowing Serbia to progress on its EU accession process.

10. **Beyond Kosovo, a further key issue in domestic politics has been the process of dismantling the system of state and socially owned enterprises.** The initial process of privatization and transformation of ownership created a captured economy in which vested interests blocked or slowed down reforms in the interest of retaining control over the economy. The lack of decisive political action to dismantle the influence of special interests further protracted Serbia's painful economic transition.

11. **Serbia has made progress in its integration with European and international structures.** In November 2007, Serbia initialed a Stabilization and Association Agreement (SAA) with the EU. In March 2012, Serbia was granted EU candidate status. In June 2013, the European Council decided to open accession negotiations with Serbia and, in December 2013, the negotiating framework was adopted. On 21 January 2014, the 1st Intergovernmental Conference took place, signaling the formal start of Serbia's accession negotiations. Since the formal start of the negotiations, the EU accession process is moving largely on its predicted trajectory. Serbia has set a self-declared objective of being ready for entering the EU in 2020. However, the relationship with Kosovo remains fragile and continues to pose a challenge.

12. **Serbia has also engaged in rebuilding traditional relations with historical partners from the non-aligned movement, as well as expanding relations with partners looking for investment opportunities in Europe.** In recent years, this has proven to be increasingly beneficial with investment inflows from non-traditional partners becoming increasingly important, exemplified by the partnership with the UAE on various issues.

## 2.2 Recent Economic Developments

13. **Serbia's economy entered a recession in 2014, for the third time in six years.** While the recession in 2009 was mainly a result of the severe impact of the international economic crisis, recessions in 2012 and 2014 were primarily caused by natural disasters. In addition, weak domestic demand and various structural bottlenecks including the delayed privatization of remaining SOEs, non-reformed public enterprises, and a poorly performing banking sector, prevented the economy from recovering.

14. **The economy was tipped into the latest recession primarily by the May 2014 floods.** The floods are estimated to have caused around euro 864 million in damages and euro 648 million in losses. This translates into, respectively, 2.7 percent of GDP in damages and 2 percent of GDP in losses in 2014. The energy sector was most severely hit as two major lignite mines that serve as a source of fuel for thermal plants were flooded. Between May and December 2014, energy sector output was one third lower than in the same period in 2013.

15. **The 2014 recession was wide-spread, covering all sectors except agriculture and telecommunication services.** Energy, manufacturing and construction all experienced significant decreases in output in 2014. Energy output was 17 percent lower in 2014 than in 2013, while manufacturing output was 1.4 percent lower and construction 4.1 percent lower over the same period. Value added in the services sector decreased by 0.5 percent in real terms in 2014 compared to 2013.

16. **Export growth - although still positive - slowed down and could not prevent a further recession.** Since 2010, and in particular in 2013 when the carmaker FIAT started production in Serbia, exports were a significant driver of growth. However, in 2014, exports began slowing down, contributing negatively to GDP growth in Q3 and Q4. The main reasons for the slowdown of exports were lower production in the energy sector, lower foreign demand and sales volumes of FIAT, and a decrease in output in SOEs awaiting privatization. Exports started to recover in the first quarter of 2015 when they grew by 5.2 percent (compared to the same quarter 2014).

17. **The recession has not yet led to further increases in the unemployment rate.** In fact, the unemployment rate has decreased to 16.8 percent<sup>1</sup> in the fourth quarter of 2014, relative to 20.1 percent the year before, as 80,000 more jobs have been created, though mostly in the informal sector. Within the informal sector, most of the new jobs were created in agriculture. Youth unemployment dropped to 42 percent but remains still very high. Many young people are leaving the country in search of employment opportunities – in particular in Western Europe.

18. **Inflation has been low throughout 2014.** Since March 2014, inflation has been below the lower band of the inflation target of 4±1.5 percent, averaging at 2 percent (y-o-y). Lower inflation is primarily the result of low food prices in the first half of the year and the absence of adjustment of administratively controlled prices in the second half of the year. By year end inflation reached 1.7 percent. Core inflation averaged just 0.4 percent in 2014. Inflation averaged 0.9 percent in Q1 2015.

19. **Nominal and real exchange rates have been steadily depreciating during 2014.** The dinar depreciated in nominal terms by 5.2 percent in the course of the year, with pressure on exchange rate growing in the second half. The National Bank of Serbia (NBS) intervened regularly to prevent more volatile depreciation spending in total EUR 1.6 billion through December. In Q1 2015, the Dinar gained 0.6 percent against a weakening Euro, and NBS intervened purchasing EUR 170 million over the same period. The NBS' inflation targeting framework and commitment to maintain a flexible exchange rate are deemed appropriate, though reducing inflation volatility remains a challenge due to significant exchange rate pass-through and high levels of Euroization.

20. **The financial system is broadly stable, although weaknesses remain in some state owned banks.** The Serbian financial system weathered the first wave of the global financial crisis relatively well. However, a weak economic recovery, and significant depreciation resulted in a substantial increase in nonperforming loans (NPLs) which stood at 23 percent as of September 2014 and reduced profitability. While the banking system remains well-capitalized and liquid, difficulties have emerged, particularly in the domestically-owned segment of the banking system. Four banks have collapsed since 2011. Credit to private enterprises was on the decline between September 2012 and May 2014, though credits recovered in the second half of 2014, primarily as a result of the introduction of subsidized loans.

21. **With respect to fiscal policy, Serbia's consolidated general government fiscal balance has deteriorated since 2008.** Revenues fell over 2008-11, and after dipping again in 2013, recovered in 2014, in part due to increases in the VAT rate (Table 1). Expenditures on the other hand have grown steadily since the crisis. The result has been a steadily deteriorating general government fiscal deficit from around 2.6 percent of GDP in 2008 to the peak level of about 7.2 percent of GDP in 2012, which subsequently subsided to 5.6 percent in 2013. The decline in fiscal deficit in 2013 was primarily due to cuts in capital expenditures and subsidies and introduction of new rules for the indexation of salaries and pensions in the public sector, which lowered the wage bill and spending on pensions. The fiscal deficit in 2014 remained high at 6.7 percent of GDP (including amortization of called guarantees).

22. **In an effort to address the above macroeconomic challenges, the government agreed with the IMF on a 3-year Precautionary Stand-by Arrangement.** The program, approved by the IMF Board on 23 February 2015, seeks to implement ambitious fiscal consolidation and structural reforms to

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<sup>1</sup> For those age over 15. Source Statistics Office Labor Force Survey.



lower public expenditures, halt the rise in public debt, and put it on a downward trajectory by 2017. The projected fiscal targets 2015-17 in Table 1 are in line with this agreed consolidation program.

**23. Significant external and domestic downside risks remain to the macroeconomic framework.**

External downside risks include lower-than-expected economic recovery in the Eurozone or external financing shocks. Key domestic downside risks include the difficulty of implementing the necessary structural reforms aimed at fiscal consolidation. This includes sensitive SOE reforms which form the core of the IMF program. Given the political economy constraints to these reforms, the risk of incomplete or non-implementation of the IMF program remains a significant threat to macro-economic and fiscal stability in Serbia.

**Table 1. Key Macroeconomic Indicators and Projections**

	2009	2010	2011	2012	2013	2014	2015	2016	2017
Real GDP growth	-3.1	0.6	1.4	-1.0	2.6	-1.8	0.0	1.5	2.0
Contributions, in percentage points:									
Consumption	-0.5	-0.4	0.9	-1.2	-0.6	-1.0	-3.2	-0.2	0.4
Investment	-11.5	-1.3	2.6	0.6	-0.6	-0.7	0.9	1.1	1.1
Net Exports	8.9	2.3	-2.1	-0.4	3.8	-0.1	2.3	0.6	0.5
Exports	-2.1	4.3	1.6	0.3	7.4	1.6	1.4	2.2	3.1
Imports	-10.9	2.0	3.8	0.7	3.6	1.7	-0.8	1.6	2.6
Unemployment rate, average	16.1	19.2	23.0	24.0	22.1	18.9	19.0	18.0	17.0
Inflation, CPI (eop)	6.6	10.2	7.0	12.2	2.2	1.7	4.2	4.0	4.0
Fiscal Accounts	Percent of GDP, unless otherwise indicated								
Expenditures	44.2	44.6	43.1	46.6	43.5	46.6	44.2	42.4	40.7
Revenues	39.8	39.9	38.2	39.4	37.9	40.0	38.9	37.7	36.9
General Government Balance (including amortization of called guarantees)	-4.3	-4.7	-4.9	-7.2	-5.6	-6.7	-5.3	-4.7	-3.8
PPG debt (eop)	36.0	43.7	46.6	58.3	61.4	71.0	77.3	78.6	78.1
Selected Monetary Accounts	Annual percentage change, unless otherwise indicated								
Credit to non-government	16.0	26.9	7.7	9.8	-4.5				
Interest (key policy interest rate)	9.5	11.5	9.8	11.3	9.5	8.0			
Balance of Payments	Percent of GDP, unless otherwise indicated								
Current Account Balance /a	-6.1	-6.5	-8.6	-11.5	-6.1	-6.0	-4.3	-4.7	-4.4
Imports	-37.5	-42.4	-43.2	-44.2	-42.9	-44.6	-44.9	-43.9	-43.9
Exports	19.4	24.8	25.2	26.5	30.8	32.2	34.2	33.6	34.3
Foreign Direct Investment, net	4.4	3.0	5.5	2.1	3.6	3.7	4.0	3.8	4.0
Gross Reserves (in US\$ bill, eop)	15.2	13.3	15.6	14.4	15.4	12.0			
Exchange Rate, USD (average)	67.6	77.9	73.3	87.9	85.2	88.5			
GDP nominal in US\$ billion	42.7	39.4	46.5	40.7	45.5	43.6			

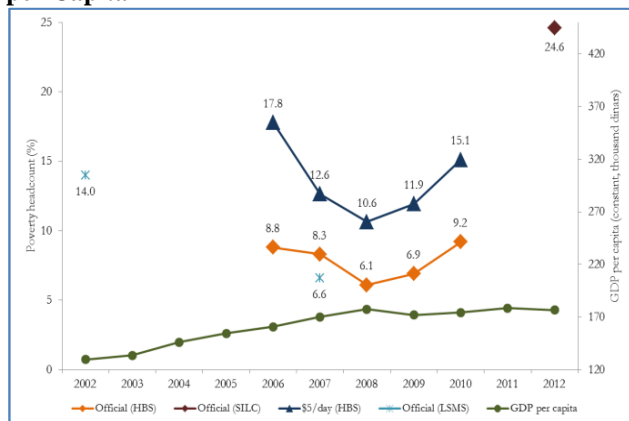
a) BoP data using BPM6 is available only as of 2012, for years 2009-2011 data is based on the earlier BOP Manual. *Source:* Ministry of Finance, NBS, IMF; WB staff estimates

## 2.3 Poverty Profile and Trends

### Poverty trends

24. **While economic growth prior to the crisis contributed to poverty reduction and shared prosperity, this progress has stopped since 2008.** The poverty headcount fell by more than half from 14 percent in 2002 to 6.6 percent in 2007, according to the LSMS data (see Figure 1). Considerable and sustained economic growth during this period as well as the growth of pensions, other social transfers, and international remittances led to a substantial decline in poverty in Serbia during 2002-2007. Still, poverty in Serbia remained higher than in the new EU Member States.

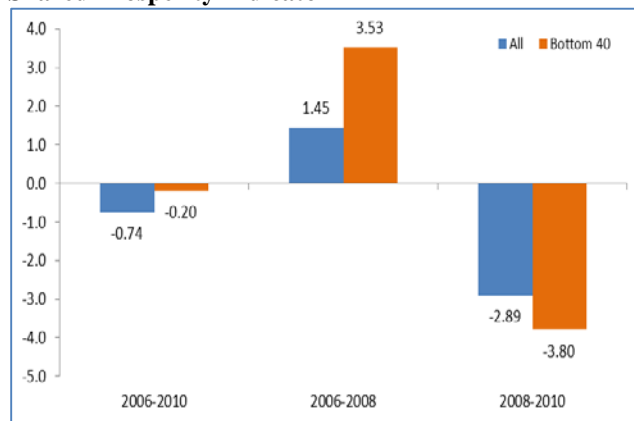
**Figure 1: Poverty Headcount (Percent) and Real GDP per Capita**



Source: Statistical Office of Republic of Serbia; ECAPOV data portal; WDI.

Note: Official poverty estimate in 2012 is based on income (EU-SILC data). Previous year estimates are based on consumption (LSMS and HBS data). Estimates based on these different survey instruments are not strictly comparable.

**Figure 2: National Consumption Aggregate-based Shared Prosperity Indicator**



Source: Estimates based on Statistical Office of Republic of Serbia's HBS data

25. **The downward poverty trend reversed after the onset of the global financial crisis<sup>2</sup>.** In 2012, Serbia adopted the EU relative poverty measure—the fraction of the population living below 60 percent of the median income—as its official poverty rate. The first EU-SILC survey for Serbia measured this indicator of relative poverty at 24.6 percent for 2012, higher than for all new EU Member States.

26. **Pre-crisis growth particularly benefitted the poor and B40, but these groups were also disproportionately hurt during the recent economic slow-down and recession (Figure 2).** The bottom of the welfare distribution experienced higher than average growth prior to the crisis. Between 2008 and 2010, however, mainly the lack of overall growth but also somewhat worsening inequality worked against the poor, also confirmed by the growth incidence curve and a growth-redistribution decomposition. Between 2005 and 2010, the decline in income of the B40 in Serbia was among the worst in ECA.

<sup>2</sup> Inferring longer and more recent time trends of poverty and shared prosperity is difficult since Serbia changed its official poverty measurement from a consumption-based, absolute poverty method using the HBS to an income-based, relative poverty method using the SILC.

27. **Poverty trends closely reflect what happened to rural poverty.** The increase in poverty rates after the crisis hit was particularly stark in rural areas, climbing from 7.5 percent in 2008 to 13.6 percent in 2010. When poverty changes are decomposed by urban-rural-population shift, changes in rural poverty account for the most: 93 percent of the national poverty reduction in 2006-2008 and 85 percent of the national poverty rise in 2008-2010.

28. **Losses in employment and labor income were the major contributor to the poverty increase and decline in welfare of the B40 following the crisis.** Labor market opportunities significantly worsened between 2008 and 2012, particularly for low-income earners. From 2008 to 2010, households where the head is unemployed or self-employed had higher poverty rates and registered a strong increase in poverty.

### Poverty Profile

29. **The poor and B40 are more likely to reside in rural and thinly populated areas.** In 2012, 36.2 percent of the population in thinly populated areas and 23.6 percent in other low-density areas were considered at risk of poverty, compared to 13.8 percent in densely populated areas (urban). Nearly half of Serbia's bottom two income quintiles live in thinly populated, rural areas. The at-risk-of-poverty rate (i.e. the share of the population living below 60 percent of the median income) was highest in the southern and eastern region of Serbia and lowest in Belgrade.

#### Box 1. Addressing Gender Gaps in Serbia: Diagnostics and Gender Mainstreaming

**Existing gender diagnostics and evidence point to persistent gender inequalities in Serbia.** While primary and secondary enrollment rates are similar, in labor markets gender gaps become more salient. The female employment rate of 33 percent in Serbia trails that of men in Serbia as well as women in ECA by 16 and 13 percentage points, respectively, resulting with a 16 percent loss in income per capita. A gender wage gap exists and is highest among low skilled workers, where it is more than 20 percent (Avlijas et al. 2013). Like in many other countries, gender differences in time use, limited child care enrollment, and skills profiles contribute to employment segregation and act as constraints on women's ability to work and be entrepreneurs (USAID 2010). Labor force participation rates drop for women in childbearing years, and only 13 percent of children under the age of three in Serbia were enrolled in child care centers between 2010 and 2011 (UNECE 2010). This situation is even more pressing among the Roma population, where women's employment rates are particularly low.

**While evidence of gender inequalities in employment opportunities has been growing, the analytical work focuses on exploring barriers to labor market participation that women face.** The Bank manages a Trust Fund (supported by the Swiss Agency for Development and Cooperation) aimed at building a knowledge base and promoting evidence-based policymaking to tackle gender inequalities. Also, Skills Measurement Program (STEP) is being implemented in Serbia to collect data on skill acquisition and skill requirements in the labor market. Another project, What Works for Women, is collecting and summarizing information on intervention design, cost, monitoring, and results of gender activities in Serbia and the wider Western Balkans region. In addition, a study is being carried out as well to understand the barriers to women's labor market participation related to child and elder care, both from the demand and supply of care. Also the Greater Than Leadership training program developed a reform proposal to help private companies comply with the gender equality law. Lastly, in coordination with the Serbian Government, the World Bank is also undertaking a Country Gender Assessment. The Assessment will make use of the latest available SILC data and focus on women's access to economic opportunities, with poverty and shared prosperity angles.

30. **The poor and B40 have weaker labor market outcomes than the rest of the population and rely heavily on social transfers.** Overall, Serbia has low labor force participation, structural unemployment of higher than 20 percent, and a significant informal economy. A large portion of the

poor and B40 are concentrated among those that are inactive, unemployed, or working in agriculture and lower-skill occupations. Thus, 37 percent of the B40 compared to 13 percent of the top 60 percent (T60) are unemployed, while 17 percent of the B40 are salaried workers (compared to 50 percent of the T60). The Roma population—the most vulnerable minority group—has a much higher poverty rate, lower educational levels and poorer labor market outcomes than non-Roma. About one third of Roma face absolute income based poverty (living below PPP \$ 4.30 a day), compared to only 8 percent among the non-Roma population, according to a World Bank/UNDP/EC 2011 survey. School enrollment rates and educational achievements are significantly lower for Roma children. Around 49 percent of working age Roma are unemployed.

## **2.4 Drivers of Poverty and Development Challenges**

31. **The Systematic Country Diagnostic highlights the dual challenge that Serbia is facing in building a competitive and inclusive economy.** This involves completing the transition from a state dominated to a private-sector driven economy, and moving from a consumption-based to an export-led growth model. Given Serbia's extremely low labor market participation rate at 49 percent in 2014, and the close relation between employment and prospects for prosperity, ensuring broader participation in the formal labor market is critical in responding to both challenges.

32. **While structural reforms may have short-term negative effects on growth and shared prosperity, they will offer sustainable new opportunities in the medium-term.** For instance, addressing the legacy of over 1,000 companies that remain in one way or another in state hands will involve significant redundancies. At the same time, privatized or corporatized SOEs might offer new job opportunities as these enterprises get new owners, and benefit from new technology and access to international markets. While resolving these enterprises, due consideration needs to be given to social mitigation measures. At the same time it should be noted that most of the workers in these enterprises are not part of the B40.

33. **The benefits of reforms in terms of rising living standards will come faster if reforms are implemented swiftly.** However, given the potential adverse effects on some poor groups, it is important in the short term to have in place complementary policies, such as well-targeted social assistance, supportive employment services, and less stringent labor taxation, to help the low-skilled find even casual jobs that will mitigate the distributional consequences of SOE reform and fiscal consolidation, providing short-term protection to the most vulnerable.

34. **Government needs to engage in a strong and coordinated push to improve the overall business environment.** The 2012 Country Economic Memorandum emphasized Serbia's potential in developing an export-driven growth model. Serbia's exports accounts currently for about 44 percent of GDP while in more advanced transition economies this ratio is above 80 percent. Sectors like the automotive and chemical industry, agribusiness and the service sector all are seen as having strong export potential, and the Serbia Innovation Fund has shown the possibilities to generate start-up businesses that can compete internationally.

35. **Barriers remain to achieving this positive turnaround. The Serbian business climate (ranked 91<sup>st</sup> globally according to Doing Business) remains a disincentive to investors,** as a result of an unfriendly administrative environment and restricted access to finance. In terms of infrastructure

connectivity—which includes telecommunications and electricity as well as transport infrastructure—Serbia ranks 111<sup>th</sup> in the Global Competitiveness index, lower than Serbia’s overall rank in competitiveness (94<sup>th</sup>).

36. **Fundamental governance and institutional challenges were highlighted in all stakeholder consultations in Serbia.** Despite improvements, trust in government and institutions such as parliament are still low (according to Eurobarometer in 2012 only 23 percent of Serbians surveyed reported trusting the government which by 2014 improved to 39 percent). Low levels of trust and confidence in institutions make it difficult to build social consensus around reforms thus posing a risk to the implementation of the government program. In addition to low levels of trust in institutions, Serbia also faces significant capacity constraints, both in the public service and in the judiciary. Capture of the economy, and in particular of SOEs has generated significant challenges to corporate governance practices in the broader state sector. Improved corporate governance will be an essential condition for attracting investment and know-how for critical SOEs such as EPS and Srbijagas.

37. **Beyond weak economic growth and institutional challenges, Serbia faces significant issues regarding inclusion.** This has three main elements; i) addressing the urban-rural divide; ii) creating opportunities for marginalized groups; and, iii) integrating emerging jobless into the labor market.

38. **The rural population, which accounts for 41 percent of the total population, has been particularly affected by the economic crisis and natural disasters.** The absence of financial possibilities for investment in small to medium scale agriculture prevents smallholder farms from producing the predictable outputs required by large retail companies. Modernizing the agriculture sector could potentially help addressing the urban-rural divide. However, years of neglect and poor management of subsidy and incentive schemes have created a deep crisis in this sector, a situation that risks to continue given the low appetite for reform in the sector.

39. **While enhancing shared prosperity constitutes the main challenge for Serbia, the country has pockets of extreme poverty, in particular among the Roma population.** Development partners have allocated resources to address Roma exclusion and lack of opportunity, but these have not yet had the desired impact. Government has so far not given this issue sufficient priority, given the numerous other challenges it faces. A more comprehensive approach is needed to address the main constraints preventing this community from building assets and creating opportunities.

40. **On supporting the unemployed, a reorientation of government programs to support job seekers is required.** A reform of the National Employment Service, the enhancement and better targeting of Active Labor Market policies, social security benefit reform and the strategic use of funds to attract new investments are critical elements of an approach to address this risk.

41. **In this respect, specific attention needs to be devoted to enhancing opportunities for women.** Female labor participation at 40.6 percent (Q4 2014) is particularly low, in part due to legislation on social security contributions, to the lack of affordable access to early childhood education and childcare for women during childbearing years and to cultural attitudes about gender equality. While achieving universal access to early childhood education is an essential long term developmental agenda, increased access for low-income groups and Roma should be given priority. Measures addressing constraints to part-time work, however, can be taken in the short term.

42. **Serbia faces significant risks in pursuing sustainable poverty reduction and progress to shared prosperity, principally related to three broad categories: 1) the external environment; 2) environmental risks, and 3) social and political risks.** As for external risks, Serbia's economy is closely linked with the economies of the EU and the Southeastern Europe, and a protracted slowdown there could jeopardize Serbia's macroeconomic stability and growth performance. With respect to the environment, Serbia is prone to a series of natural disasters that could seriously damage the economy and the well-being especially of vulnerable populations. Climate change will exacerbate these risks, and designing and implementing a risk mitigation program is critical. Finally, there are social and political risks that could undermine the sustainability of poverty reduction and shared prosperity, such as the tension between Serbia's EU ambitions and its policy toward other geo-strategic partners.

### **III. WORLD BANK GROUP PARTNERSHIP STRATEGY**

43. **The SCD provides a comprehensive analysis and assessment of Serbia's development challenges and constraints, and highlights eleven broad priority areas for achieving sustainable and inclusive growth, with the aim to achieving greater shared prosperity.** The CPF responds to these identified priority areas, while considering the fiscal constraints that Government will face for most of the CPF implementation period. The CPF also takes into account the Bank's comparative advantage as a leading institution in knowledge generation and diffusion in Serbia and the insights gained from the CPS Completion and Learning Report, Client Survey, IEG reports and stakeholder consultations.

44. **Following several years of low political stability and frequently changing governments, Serbia currently has a government with broad political support.** The government has also shown a strong commitment to market-oriented reforms. Hence, the CPF comes at an appropriate point in time, and covers the five year timeframe that Serbia has set for being ready to join the EU.

45. **Convergence is strong between the priority objectives flowing out of the SCD and the standards Serbia has to meet for joining the EU.** A functioning and competitive market economy and strong institutions are critical for EU membership, as are an enabling business climate and secure property rights and adherence to the 'Acquis Communautaire' in important policy areas such as energy and transport. The National Economic Reform strategy reflects these critical priorities. Social inclusion and gender equality are equally core elements of the European Integration agenda, and climate resilience is taking a growing importance in the EU's internal agenda. Leveraging the WBG's financial and knowledge resources can provide an important value added in EU accession processes, as previous accession processes have shown

#### **A. Government Program and Medium Term Strategy**

46. **The CPF comes at a time when government has approved a tough but realistic three year fiscal strategy and prepared a National Economic Reform program.** The CPF reflects the point that the country will be in the process of EU accession negotiations throughout the program implementation period. It should be noted that while these approved strategies and programs, along with the accession negotiation process, set an overall policy direction, they do not constitute a comprehensive national development strategy.

47. **The fiscal strategy and economic reform program place a strong emphasis on the**

**implementation of structural reforms. This reform has the dual objective of achieving fiscal sustainability and creating an enabling environment for investment and job creation.** The structural reform program's first priority is to reduce the state's footprint in the economy, by finalizing the privatization process of commercial socially and state owned enterprises, and by corporatizing large energy utilities and transport companies so that they are run, on a commercial and financially sustainable basis. A second priority area is the more effective use of public resources, including the reform of public service delivery systems, strengthening public financial management and public investment management. A third priority area is improving the business climate, through tax policy, permitting and licensing system reforms and overhauling the government's incentive systems to promote investment. This also includes reforming the financial system and easing access to credit for entrepreneurs. There is no overarching policy framework for stimulating inclusive growth in Serbia's development framework, which constitutes an important gap.

48. **A critical challenge Serbia faces is weak ability and capacity to implement reforms.** Even though there is a strong political commitment to the reform agenda described above, systemic weaknesses in the public administration frequently cause delays or distortions in implementation, even when political decisions are taken. As a result, Serbia frequently underperforms on critical aspects of its reform agenda. This implementation deficit is a structural problem, which the current government has recognized and committed to address.

#### **SYSTEMATIC COUNTRY DIAGNOSTIC: SERBIA'S PRIORITIES FOR GROWTH AND INCLUSION**

49. **The World Bank Group has been engaged in an intensive dialogue on the government's reform program, focusing on addressing economic legacy issues, reforming and strengthening the core public sector, stabilizing the financial sector, and designing a comprehensive approach to raise competitiveness and create jobs.** Given the nature of the challenge the Government is facing, and its fiscal and capacity constraints, prioritization of actions is critical. In this regard, *the SCD concludes that restoring and sustaining growth is a necessary but insufficient condition for poverty reduction and shared prosperity. Growth must also include meaningful job creation for the poor if it is to have optimal impact in reducing poverty and increasing the welfare of the B40.* Serbia bases its growth strategy on increased exports and increased investment in high-productivity export sectors, which are essential for inclusive growth and job creation for the B40. Complementary policy reforms and investments in other sectors (including non-tradables) are also needed to remove constraints for low, semi-skilled and part-time work, which are the main sources of employment for the poor and B40. In conclusion, restoring growth combined with specific measures to address constraints faced by the B40 in gaining employment is the most effective way to boost shared prosperity in Serbia.

50. **Based on this assessment, the SCD identified eleven broad priority areas, which were ranked on the basis of their impact on the twin goals.** This prioritization exercise led to three distinct groups of priorities: *foundational priorities, high impact priorities and supporting priorities.* Among the seven top priorities in the SCD *the first two are foundational,* without which the achievement of results in the other priority areas would be extremely difficult. The other five are considered high impact and the remaining four are supporting priorities.

**Table 2: Overall Impact Assessment of SCD Policy Priorities on the Twin Goals**

<b>Constraints/Medium Term Policy Objective</b>	<b>Impact on Twin Goals</b>
<b>Foundational Priorities</b>	
<b>Fiscal sustainability, financial and macro stability:</b> Restore debt sustainability and maintain macro and financial stability.	• High
<b>Governance and institutional capacity:</b> Create an effective institutional mechanism within government to coordinate, implement, and monitor reforms.	• High
<b>Priorities with Highest Impact on Twin Goals</b>	
<b>State Owned Enterprise (SOE) reform:</b> Reduce the state’s footprint in the economy and make the public sector more efficient by privatizing commercially oriented enterprises, restructuring large public utilities, and rightsizing the public sector.	• High
<b>Business climate reform:</b> Create an environment conducive to private sector-led investment, growth, and job creation.	• High
<b>Labor market institutions:</b> Strengthen these institutions to facilitate formal employment, create earnings opportunities for the less well-off, and help mitigate the negative consequences of SOE reforms.	• High
<b>Agriculture, self-employment:</b> Support higher agricultural productivity and rural incomes to improve the welfare of the B40 and reduce poverty.	• High
<b>Infrastructure:</b> Enhance the quality of public infrastructure to better support international, regional and domestic connectivity.	• Medium-High
<b>Other Supporting Priorities</b>	
<b>Water and sanitation:</b> Enhance Serbia’s water resource management, wastewater treatment, and environmental sustainability	• Medium
<b>Education and skills:</b> Expand access to and the quality of education for all, in particular marginalized groups; reduce inequity and increase workforce productivity by improving skills and learning outcomes.	• Medium
<b>Health:</b> Expand access to care for marginalized groups, reduce disparities and improve the quality of care and health outcomes, and reduce the fiscal risks related to personal spending on health.	• Medium
<b>Social protection:</b> Improve the coverage, equity, efficiency, and fiscal sustainability of pensions and the social assistance program.	• Medium

## **B. Proposed WBG Country Partnership Framework**

### **B.1 Lessons from CPS Completion and Learning Report, IEG evaluations and Stakeholder Consultations**

51. **The objective of the FY12-15 CPS was to support Serbia’s EU accession and help the Government strengthen competitiveness and improve the efficiency and outcomes of social spending in the context of severely constrained budgets.** The CPS focused World Bank Group support in two areas of engagement: (i) strengthening competitiveness; (ii) improved efficiency and outcomes of social spending. In addition, a commitment was made to continue to provide support to environmental sustainability through portfolio supervision on two operations.

52. **Overall performance under the previous CPS program was assessed as Moderately Satisfactory.** Regarding the competitiveness pillar, good progress was made on the infrastructure elements of the program. However, socially and politically sensitive reforms, including resolving loss making publicly and socially owned enterprises, took a long time to gain ownership. World Bank Group efforts to provide support were also hampered by a weak macro-fiscal situation. On the Efficiency of



Social Expenditure Pillar, the program provided lending and high-end advisory support throughout the CPS period. With respect to engagement on environmental sustainability, strong performance on energy efficiency was blended with weak performance on addressing environmental legacy issues.

53. **Despite some implementation challenges during the FY 12-15 CPS, the Bank remains a partner of choice for the Government in carrying out complex reforms.** The following key lessons from implementing the FY12-15 CPS were taken into account in the design of the FY16-20 CPF.

- **Close alignment with Government objectives, and those of other key partners, was important to the success of the WBG program.** The WBG program provided strong support on critical aspects of SOE and investment climate reform, and in improving the effectiveness of social expenditure, which correspond to critical government objectives. Alignment of CPS strategic goals with the EU regional strategy provided a basis for successful WBG interaction with the EU, particularly on the improvement of IPA funds absorption, and also strengthened the link with other development partners.
- **The WBG should maintain its strategic focus on assisting the government in getting growth back on track and ensuring that opportunities for the less well-off are enhanced.** The Bank has been at the forefront of dialogue on resolving economic legacy and transition issues and enhancing competitiveness. The long and consistent engagement over time has paid off, as government has initiated critical reforms that should help break the cycle of spiraling debt and weak investment. As this process progresses, continued attention needs to be devoted to creating opportunities for the bottom forty percent.
- **Flexibility and adaptability in the use of instruments is critical.** In a context such as Serbia, where policy implementation issues are often the greatest challenge, and where fiscal space reduces the scope for investment lending, the increased use of result-based financing is a logical way forward. However, clients do not yet have the same familiarity and comfort levels with result-based financing as with the investment lending and budget support instruments.
- **The WBG is well placed to provide high quality, timely, and relevant AAA, which can then form a solid basis for lending operations.** This was demonstrated, for example, by the Real Estate Management Project, which was preceded by an in-depth Technical Assistance that helped in mapping relevant sector issues and informed the design of the project, and also helped frame the WBG input to the drafting process of the law on Constructing Permitting. Non-lending work should continue even when lending is delayed, as it often provides for continuing counterpart engagement and knowledge base, which are critical for quick movement when the time comes.
- **The next CPF should build on focused objectives and clear outcomes, monitored by observable indicators.** The large number of outcomes in the earlier CPS results framework made it hard to focus on key priorities and to use the CPS as a practical tool for dynamic monitoring and adjustment.
- **An enhanced and structured partnership with the EU, in particular in the broad domain of economic governance, is essential as Serbia gets closer to EU membership.** The importance of this partnership will increase during the CPF as Serbia moves to negotiate new *Acquis* Chapters. Joint financing initiatives in critical reform areas (either through parallel financing or making use of the World Bank-EU framework agreement) or possibly joint sector budget support are potential instruments for stepping up joint engagement.
- **The challenging macroeconomic environment and poor corporate and financial governance poses constraints to IFC investment activity.** While the results overall have been

satisfactory, the quality of the IFC portfolio in Serbia has deteriorated as a result of weaker financial performance of some of the clients affected by the lower growth environment.

54. **The lessons learned from the Serbia FY12-FY15 CPS echo many of the lessons learned in recent CAS/CPS completion reports of other countries, such as Albania, FYR Macedonia, and Georgia.** The importance of: alignment with the country's priorities; continuing dialogue and partnership with counterparts and partners; flexibility and responsiveness as circumstances change; clear focus on limited number of priorities; and the value of knowledge products are generally reflected in all of these reports.

55. **The CPF design process benefited from a broad set of consultations.** Seven consultation meetings were carried out, including a specific focus group with the private sector. These discussions provided a rich array of insights in stakeholder perspectives, and focused in particular on governance/reform implementation capacity, Serbia's growth model, business climate issues, inclusion and the quality of services in health and education, agriculture and energy. The consultations outside Belgrade re-emphasized the rural-urban divide in economic opportunities, and the sense that local communities are left to fend for themselves.

56. **According to the FY 14 Serbia Country Opinion Survey findings, stakeholders have a positive view about how the World Bank operates in Serbia.** Stakeholders believe that there is a great opportunity for the WBG in supporting priority areas and Serbia's institutions through investment and capacity building. While collaboration with the Government is regarded as very strong, greater engagement with citizens emerges as a critical area for strengthening WBG's work on the ground. While respondents appear to hold very positive views about how the WBG operates in Serbia, improvements can still be made on how the organization reaches out and engages beyond government.

57. **IEG project evaluations highlight country risk factors and policy uncertainty as critical factors that negatively influence results.** In investment lending support, frequent changes of government and priorities of sector policies have led to substantial delays in project implementation and negatively impacted project outcomes. Weaknesses in preparation processes and Quality at Entry also emerge as critical issues. This is consistent with the overall public investment management problems Serbia is facing, and World Bank Financed projects still tend to fare slightly better than other externally financed projects. Nonetheless, where commitment is strong and consistent, strong outcomes can be achieved, such as in the Energy Efficiency Project. The development of better implementation tracking systems within government, both for policy reforms and for investment projects, is a critical condition to improve performance on portfolio implementation.

## **B.2 Overview of World Bank Group Strategy**

58. **The overarching goal of the CPF is to support Serbia in creating a competitive and inclusive economy and, through this, to promote integration into the EU.** The SCD shows that a transformation of the country's economic model is the only viable path for economic development in Serbia, including for achieving the shared prosperity goal. This transformation is also critical to the country's strategic European Integration objective, given that Serbia does not yet meet the EU criterion of having a fully functional market economy able to withstand competitive pressures within the European Union. Therefore the CPF seeks to assist the country in its efforts to transition to an export-oriented growth model, by transforming the role of the state, promoting competitiveness and improved functioning of the

investment climate and labor market, with the latter in particular supporting greater economic inclusion.

59. **The structure of the CPF is designed to support six top SCD priorities. Within these priorities, program selectivity is based on the following additional filters:** i) **country ownership and championship**, with a focus on areas which have both high impact and strong government reform championship; ii) **comparative advantage**, through a careful examination of the WBG's comparative advantage vis-a-vis other partners, and especially the EU, EBRD and EIB, both in terms of areas where each institution may have leverage and in terms of track record in program implementation; and iii) **strategic programming, including sequencing support strategically**. The approach to sequencing is in line with the government's emphasis on front loading fiscal consolidation and SOE reform, thus creating space for later investments. Strategic programming will be driven by the level of reform commitment; if this remains high, a greater emphasis will be placed on transformational and cross-cutting engagements using budget support and result-based financing instruments. If reform commitment wanes, the scope of engagement will be narrowed to those areas where commitment remains in place and a greater emphasis will be placed on using conventional investment lending.

60. **The rationale to build the CPF around six foundational and high impact priorities is based on these additional selectivity filters.** WBG engagement will focus on the following selected SCD priority areas:

- **Fiscal sustainability, financial and macro stability.** This is an area of WBG comparative advantage and long-standing engagement, where WBG brings established macro-fiscal analysis and detailed reform diagnostics. In particular, in the division of labor with the IMF, the WBG focuses its analytical, policy design and implementation support on structural aspects of the fiscal consolidation and expenditure management agenda.
- **Governance and institutional capacity.** Serbia's weak capacity to implement reforms and policies, as well as to deliver quality services, is a fundamental constraint to growth and inclusion. Without addressing the systemic issues in public sector management, it is unlikely that fiscal and sector reform programs will be implemented, either fully or in a timely manner, posing risks to all other objectives set out. The systemic issues include weak policy coordination and reform implementation capacity, an overly complex organization of the central state administration, including overlapping and duplicative institutions and functions, and the ineffective organization of service delivery structures. The WBG and the EU are jointly leading efforts in this area, with the Bank focusing on targeted elements of the reform agenda laid out in the Government's Public Administration Reform strategy and Action Plan.
- **State Owned Enterprise reform.** The WBG has been engaged in supporting the Serbian government in privatizing commercial SOEs for over a decade. This is an area where long haul engagement is critical and where the WBG is one of the few trusted partners of the government. This is a highly sensitive area of reform, but nevertheless recognized as a core condition for creating a competitive and sustainable development path. The second aspect of this agenda is related to the reform of utilities and public transport companies which need to be managed on a financially and fiscally sustainable basis. The WBG will lead efforts to corporatize and enhance performance of three critical SOEs: EPS (Electricity), Railways of Serbia and Roads of Serbia.
- **Business climate reform.** The WBG engagement in Serbia reflects a global comparative advantage in this area as well successful WBG engagement in neighboring countries, and exploits the complementarity of the IBRD and IFC. It brings WBG expertise in assisting the Government in pursuing the legal and regulatory reforms aimed at improving the business environment in the

broad sense, including support to improving property registration, construction permitting, trade facilitation, access to finance, and ease of paying taxes. In addition, support to building Serbia's innovation and technology transfer system will be continued. Pilot efforts in these two areas have yielded promising results and need to be scaled up to create a broader impact on employment generation.

- **Infrastructure.** Better regional connectivity through infrastructure development is essential to boost investment and growth in Serbia. The WBG has been heavily engaged in infrastructure development, both through investment support to highway and national road construction, improvements in road and rail sector management systems, and support to energy sector reconstruction and rehabilitation. Improved efficiency in spending and better quality maintenance of infrastructure will be pursued, as well as improved prioritization of public investments and facilitation of private sector investment. Engagement in infrastructure development will be continued in close coordination and cooperation with other IFIs as well as with the EU.
- **Labor market institutions.** The SCD highlights the importance of employment as the main vehicle for lifting the income of the B40. It also emphasized the constraints that current labor market regulations, policies and management pose to the objective of creating meaningful jobs, especially for marginalized groups with low labor market participation. The SCD highlights the importance of building human capital to increase labor productivity and enhance inclusion, including closing education enrollment gaps for low-income groups and Roma in pre-primary and tertiary education. The WBG is a leading partner to the government in knowledge work around the job creation and skills agenda, working on a broad range of reforms from National Employment Service Reform and labor market regulation to addressing current and future skill gaps. These reforms are critical to creating opportunities for youth, women, marginalized groups, as well as workers that have lost jobs in defunct SOEs.

61. **In the four supporting priority areas defined under the SCD, we will engage only narrowly in support of the top six priorities, in order to further fiscal consolidation, public administration reform, business climate improvement and labor market participation and inclusion.** The SCD priority areas not selected for direct support under the CPF also include one high priority area: agriculture and rural development. This area was identified in the SCD as an important dimension of shared prosperity. However, Government is looking to other partners, in particular the EU, to lead efforts to improve agriculture sector performance and boost rural development. Serbia also has important bilateral partners who are investing significant resources in irrigation and crop production, making it unnecessary for the WBG to lead efforts in this area.

62. **The structure of the CPF consists of two broad focus areas encompassing eleven CPF objectives.** The CPF focus areas and objectives are summarized below:

- **Focus Area 1: Economic governance and the role of the state** specifically addresses constraints to the effectiveness of economic governance: the size and management of the budget, the scope and capacity of the administration to implement reform and deliver services, the footprint of the government in the economy, and the performance of public utilities. The WBG will pursue five CPF objectives under this focus area, two of which correspond to the foundational priorities identified in the SCD. These are; i) *supporting sustainable public expenditure management*, and; ii) *assist in creating a more effective public administration &*

*improving select service delivery. A further three objectives correspond to strands of SOE reform; iii) a more efficient and sustainable power utility; iv) more efficient public transport companies, and; v) productive SOE assets transferred to private ownership.*

- **Focus Area 2: Private sector growth and economic inclusion** addresses significant constraints to private sector development and economic inclusion: financing, investment, connectivity, and labor market constraints. Specifically, the objectives and interventions are designed to strengthen the banking system, improve land management, improve infrastructure networks, increase renewable energy capacity and develop better skills and reduce barriers to labor market entry. Six CPF objectives have been identified in this focus area; i) *contribute to priority business climate improvements;* ii) *assist in creating a more stable and accessible financial sector;* iii) *support development of more efficient land and property markets;* iv) *enhanced infrastructure networks;* v) *reduced barriers to labor market participation,* and; vi) *assist in closing medium and long term skill gaps.*

### **Cross cutting theme**

63. **Responding to climate change and disaster risks will be a cross-cutting theme across the two focus areas, given the high risks that natural disasters pose to economic development and the impact of climate change on the poor.** The combination of droughts, harsh winters, and climate-related disasters such as floods has significantly influenced Serbia's production potential, especially in important sectors such as agriculture. This has a disproportionate impact on rural areas, which, as per the analysis in the SCD, are the most vulnerable segment of Serbian society. Mitigating the impact of climate change, and making the economy more climate resilient, will become an increasingly important part of Serbia's development agenda. This also coincides with a growing attention for climate change inside the EU, with which Serbia will need to align during the CPF period. Engagement in this area will have several aspects.

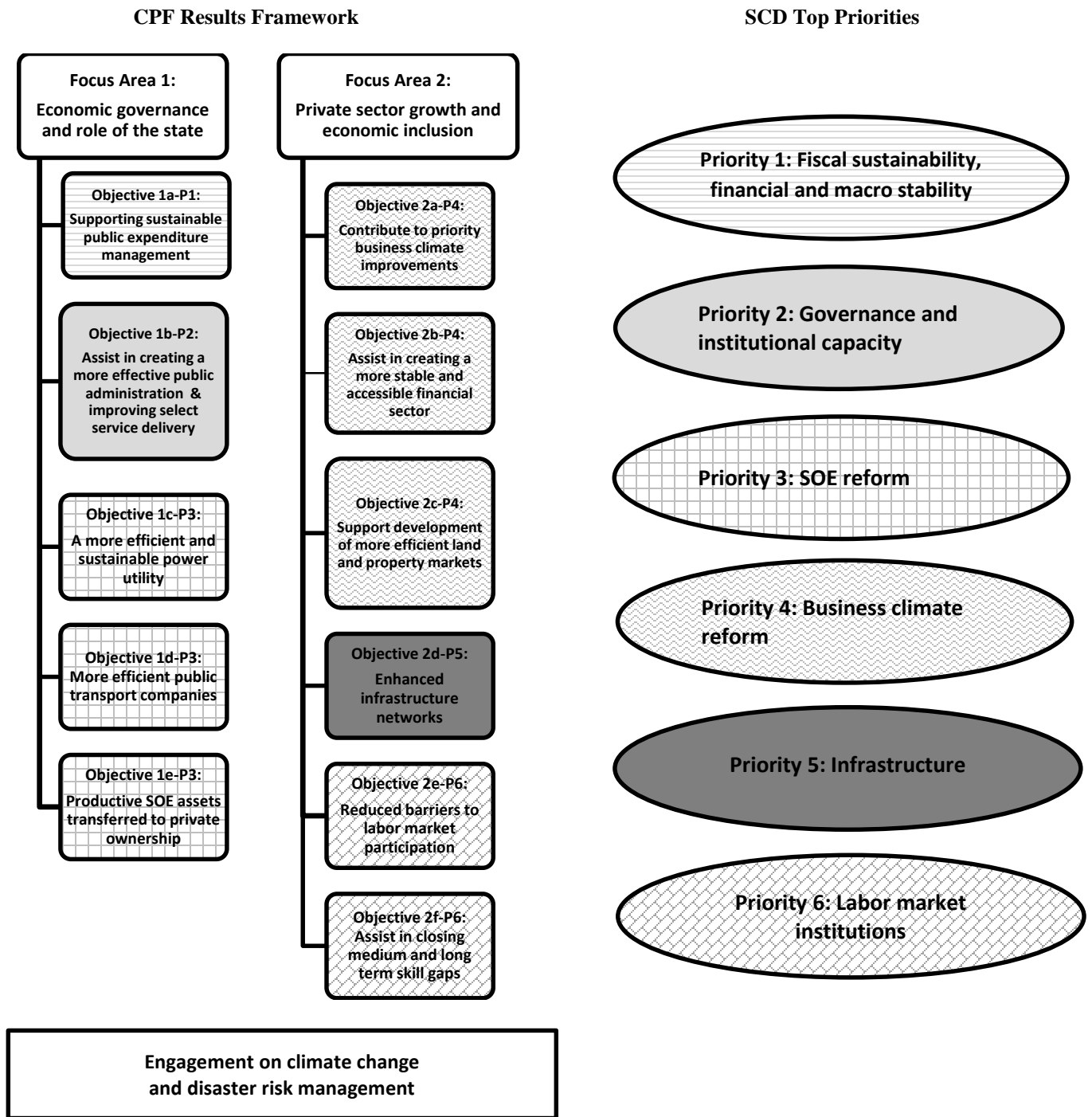
64. **The WBG leadership role in Disaster Risk Management, together with the EU and the UN system, makes the institution a critical partner to the design and implementation of risk mitigation measures.** Disaster Risk Management is an inherent part of the policy coordination and rationalization agenda (Objective 1b) as well of financial risk mitigation through the Catastrophic Risk Insurance Facility (Objective 2b). Climate risk mitigation will also be addressed through the engagement on energy sector reform (Objectives 1c and 2d), including greater use of renewable energy sources, and through the ongoing Emergency Recovery Loan, which has a flood protection component. The government has also expressed interest in a possible Catastrophe Deferred Drawdown Option in the outer years of the lending program. An analytical work program to better understand climate change induced risk to development will be developed and potential follow up activities integrated across the eleven CPF objectives.

### **Results monitoring**

65. **The CPF Results Framework will serve as tool to monitor implementation.** The CPF Results Framework, built around two focus areas with 11 CPF objectives and 18 outcome indicators is presented in Annex 1, and will serve as a management tool throughout implementation. Progress in CPF milestones will be annually monitored with the client and at mid-term under the Performance and Learning Review (PLR).

66. Figure 3 highlights the linkage between the selected SCD priorities and the CPF focus areas and objectives.

**Figure 3: Result Framework: Linkage between CPF Objectives and SCD Priorities**



Note: CPF Objectives grayscale-coded to show linkage to SCD top priorities

### B.3 Objectives supported by the WBG Program

<b>Focus Area 1: Economic governance and the role of the state</b>
CPF Objective 1a: <i>Supporting sustainable public expenditure management</i>
CPF Objective 1b: <i>Assist in creating a more effective public administration &amp; improving select service delivery</i>
CPF Objective 1c: <i>A more efficient and sustainable power utility</i>
CPF Objective 1d: <i>More efficient public transport companies</i>
CPF Objective 1e: <i>Productive SOE assets transferred to private ownership</i>

#### **CPF Objective 1 – Supporting sustainable public expenditure management**

67. **As set out in the SCD, sustainable public finances are a critical pre-condition for an improved growth outlook for Serbia and progress towards achieving the twin goals.** Indeed, sustainable fiscal consolidation and expenditure management are required to create the additional fiscal space and macro-fiscal stability which are key enabling conditions for the other objectives supported by the WBG program.

68. **Apart from being a prerequisite for growth and progress on other CPF objectives, engagement in this area will also help to increase inclusion and fight poverty, thus enhancing shared prosperity.** Improvements in public expenditure management can improve the quality and predictability of existing spending allocations in key areas such as social assistance, active labor market policies and infrastructure, and open up fiscal space for additional investments in these areas.

69. **The threat to macroeconomic stability remains high, due to growing public debt caused by expanding fiscal deficits, and issuance of guarantees to SOEs over the previous period.** Serbia's fiscal deficit has grown from 2.6 percent of GDP at the start of the economic crisis to around 6.7 percent of GDP in 2014. Efforts to curtail spending have been made in some important sectors (including pensions and the wage bill), but were more than compensated by increases in subsidies to SOEs. In addition, revenues dropped as the economy was going through repeated recessions. Putting public finances on a sustainable footing is an urgent need. Costly and ineffective subsidy programs and state guarantees for public and socially owned enterprises need to be reduced and, in most instances, phased out and the cost of providing public services should be assessed and where possible reduced. Downside risks, including those that are related to revenue forecasting, have to be better managed.

70. **Fiscal consolidation and improved expenditure management are at the core of Serbia's Fiscal Strategy and National Economic Reform Program,** which include the stabilization of the debt-to-GDP ratio by the end of 2017, the completion of privatization and a stop to issuing of guarantees for liquidity purposes for the remaining SOEs. Subsidies to companies such as Railways will be provided only to enable them to provide public interest services. The subsidy system for agricultural producers will also be reviewed for possible rationalization.

71. **In order to achieve sustainable public finances, the government needs to remain committed to the planned reduction in public expenditures, the improvement in management of these expenditures, and the reduction in the public debt-to-GDP ratio.** The WBG will continue its support

to Government to assist with the achievement of sustainable fiscal consolidation and expenditure management, through a deep engagement on analytical and advisory support as well as policy-based or results-based financing, working in coordination with other development partners.

72. **The WBG contribution to the Government's efforts in this area will focus primarily on support for rationalizing expenditures**, and will include transparency and efficiency measures in public sector wage bill management, pension system reform, SOE reform and selected aspects of subsidy reforms. Particular attention will be given to expenditure shifts which better target the B40 in rural areas. Rationalizing expenditures will create fiscal space which allows expansion of basic service delivery (e.g. health, education, water supply, flood protection) into rural areas where much of the B40 reside. Subsidy reform will also allow for reorientation of subsidies and means testing of social assistance beneficiaries to better reach the poor and B40. For example, current agricultural subsidies mainly benefit large mechanized producers in relatively well-off parts of the country. If these subsidies are reduced, it would create space for more income support for smallholder producers in poor rural areas, and this would help strengthen safety nets for this important segment of the B40.

#### **CPF Objective 1b – Assist in creating a more effective public administration & improving select service delivery**

73. **Effective public sector governance is important both for implementation of Government's reform program and delivery of quality public services.** Serbia lags behind regional comparators in a variety of measures related to public sector management and service delivery. For instance, in the *Global Competitiveness Report 2014-2015*, 'inefficient government bureaucracy' is highlighted as the most problematic factor for doing business.

74. **Serbia rates low on indicators of policy coordination and government effectiveness, hindering the implementation of critical reforms and service delivery.** Weak vertical and horizontal coordination severely limits government ability to implement reforms and deliver services. Low effectiveness in government is caused by, among others: i) Inefficient decision making processes that slow implementation and accountability; ii) an overly complex structure of government; and iii) a wage system that does not meet equity and fiscal transparency criteria.

75. **As a result of weak public management practices, service delivery outcomes are weak in spite of high spending.** For instance, Serbia spends significantly more on health than comparator countries to produce the same outcomes. There are only five hospital beds for every 1,000 Serbians, lower than the Europe and Central Asia average (developing countries only), in spite of Serbia spending considerably more. Similarly, high spending in education does not come with better performance. Results of PISA (2012) show that all OECD countries performed better than Serbia in reading, math, and science. Efforts to rationalize expenditure allocations through the introduction of per capita financing systems have not yet proven successful. However, the new impetus generated by the government's fiscal consolidation efforts provides an opportunity for reform in this area.

76. **The Public Sector Reform Strategy and Action Plan, adopted in 2014 and 2015 respectively, set out a broad reform agenda with rationalization and rightsizing at the center.** The WBG will selectively support the implementation of the Government's reform agenda through a combination of



instruments, focusing on diagnostic work on structural and functional organization of the public administration and on select aspects of implementation.

77. **As regards diagnostic work, the WBG will assist government in carrying out a cross-cutting diagnostic of the public administration system** with the aim of eliminating duplication and overlaps, and abolishing redundant institutions inherited from the past. An analysis will also be done of how frontline service delivery management in health, social protection and education can be improved, with a particular emphasis on services that create opportunities for the B40. Functional reviews of the Ministry of Finance and the Ministry of Agriculture and Environment will also be conducted.

78. **Following the completion of the reviews, implementation support will be provided to the implementation of reform measures in select service delivery areas**, as set out below, with the possibility to add other sectors once the program of functional reviews is completed. The selection of these areas is based on World Bank Group prior engagement and comparative advantage.

79. **A first aspect of reform implementation to be supported is the overhaul of investment and export incentive systems.** With the removal of commercial SOEs as a factor discouraging foreign and domestic investment, the role and performance of agencies charged with incentivizing investment and export promotion takes on added importance. The Government has committed to implementing the results of a functional and performance audit of the three main agencies involved in the investment incentive and export promotion system.

80. **As a second focus area, services in the justice sector are particularly critical for the competitiveness and inclusion agendas, and for EU accession.** Business investment and expansion are constrained by weak service delivery performance by the justice system and its inability to impartially, efficiently and transparently enforce rights and mediate business disputes. High court fees and attorney costs, cumbersome processes, lengthy delays, inadequate enforcement, and constantly changing legislation disproportionately affect SMEs and disadvantaged citizens. Greater efficiency is needed to allow the judiciary to provide services to the B40 in the more remote, rural areas of the country. The recently completed comprehensive Judicial Functional Review shows that trust in the judiciary is low due to perceived corruption, inefficiency and inconsistency. Inefficient processes cause delays for parties, and procedural abuses are unchecked. Serbian courts are also less accessible than those in EU member states and neighboring countries due to high court and attorney fees. The MDTF-JSS will continue to support the justice sector in improving performance to align with EU standards.

81. **Reform implementation support will also be provided to the health sector, where the WBG had a constructive engagement in the previous CPS period.** The Second Health Sector project includes support for sector expenditure rationalization and broad health sector restructuring. Finally, the WBG will provide capacity building support under a Multi-Donor Trust Fund in the area of disaster risk mitigation, which is a critical element of addressing climate-change related challenges. The Trust Fund was set up following the disastrous May 2014 floods and provides a broad range of support for building institutions and tools to analyze and prevent climate-related disasters as well as for reducing climate-change related risks to the economy.

### **CPF Objective 1c - A more efficient and sustainable power utility**

82. **The weak performance of state owned energy utilities impacts negatively on the business climate and poses a drain on budget resources.** The steady deterioration of their financial position coupled with deteriorating energy infrastructure are among the critical factors that increasingly weigh heavily on budget resources, threaten the delivery of critical services necessary to support growth, and discourage private sector investment.

83. **The WBG reengaged with the electricity utility “EPS” following the 2014 floods, and supported the company in recovery and reconstruction of critical infrastructure to mitigate the impact of the disaster.** This gave rise to an enhanced dialogue on corporatization and financial sustainability of the company, which was conducted jointly with the IMF and EBRD. If EPS restructuring is successful, the company will be a major asset to Serbia, bringing benefits to the state (as shareholder) and to consumers (in better services) and contributing to fiscal stabilization.<sup>3</sup> If restructuring fails, the downside risks could wipe out all the hard-earned savings from the fiscal consolidation process.

84. **Given the comparative advantage of the WBG, EPS restructuring will be a central area for engagement through both advisory support and policy or result-based lending.** IFC may engage with EPS once the company is financially viable. WBG and EBRD engagement with EPS is further complemented by EBRD and EU support to Srbijagas and both engagements will be closely coordinated.

85. If a commercially acceptable power purchase agreement (“PPA”) is adopted, IFC will support FDI into renewable energy, helping Serbia achieve its obligations on renewable energy under the Energy Community with the EU. Increasing the share of electricity generated through renewables will also mitigate climate change risks. Continued support to the introduction of energy efficiency measures will be provided to reduce waste and decrease energy intensity in production.

#### **CPF Objective 1d - More efficient public transport companies.**

86. **The WBG has historically had a strong engagement on institutional reform and investment in the roads sector,** given the importance of access to infrastructure for competitiveness and employment creation. Improved road connections were identified as a critical factor to creating growth and employment in rural areas, which would be of particular importance to the B40. In this respect, the integration of multiple road sector agencies (in particular Roads of Serbia and Corridors of Serbia) initiated in 2015 will create a stronger, more cost-efficient and better integrated management system for public roads. In addition, Serbia’s road safety strategy and the system of performance-based maintenance were all designed with strong WBG support. The implementation of these reforms will lead to improved sector management at lower cost over the next years, allowing for more investment in improving connectivity.

87. **In addition to road sector reform, the WBG has also provided analytical and advisory support to railway reform,** and in particular the corporatization and financial consolidation of Železnice Srbije (Railways of Serbia). The reorientation of the company towards commercially viable cargo services and rationalization of passenger operations is important both from a macro-fiscal and a competitiveness perspective.

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<sup>3</sup> The time and cost of connecting to electricity remain excessively high compared to countries with similar power system size: 131 days in Serbia as compared to 38 days in Slovenia or 30 days in Chile.

88. **Going forward, WBG support will focus on supporting the implementation of structural and financial consolidation plans for the road and rail sector enterprises discussed above,** by providing both financial support to offset reform cost and hands on advisory support. This support will be provided jointly with EBRD, the EU and the IMF. IFC support on the design and implementation of PPPs and potentially concessions, in particular in the roads sector, could complement IBRD engagement on corporatization and financial consolidation.

#### **CPF Objective 1e - Productive SOE assets transferred to private ownership**

89. **State involvement in the economy needs to be reduced to create space for private sector-led growth.** Completing privatization of the remaining commercial SOEs is a central element of this agenda. Reaching this objective will result in reallocation of assets from their current non-productive uses to more productive uses in the private sector.

90. **Commercial SOEs in Serbia have posed a significant drain on scarce fiscal resources.** The 140 companies in restructuring alone cost Serbia up to Euro 1 billion in direct and indirect subsidies over the previous five years. The companies in the portfolio of the Privatization Agency generated total losses of 690 Million Euro in 2013, or over 2 percent of GDP. They have significant negative spillover effects to large public utilities, which in turn need costly state support. They also lock up potentially valuable assets that cannot be redeployed for economic use.

91. **More importantly for Serbia's development prospects, commercial SOEs also pose a significant constraint on private investors.** The presence of a large number of enterprises under restructuring in almost all sectors of the economy, some of which are protected from bankruptcy, has created a strong perception of an uneven playing field and discouraged private investors. This impedes Serbia's transition to an export-driven growth model which is essential for boosting shared prosperity.

92. **It is critical that the SOE resolution process proceed with due consideration for affected workers.** The First Public Enterprises Reform DPL supported the design and implementation of an important set of social mitigation measures for workers to be released by the firms under the Privatization Agency portfolio. These measures will be continued in the next phase of reform and are an integral part of the state budget. It should be noted that the workers in these SOEs are generally not part of the B40.

93. **The WBG has been engaged on the SOE privatization agenda for many years, and has been the main development partner to support the government in the sensitive and difficult final phase of the process, involving 526 companies in the portfolio of the Privatization Agency.** Based on high level dialogue and hands on technical advice, a privatization and resolution program for this portfolio was crafted and agreed. The implementation of the program is supported under the Public Enterprise Reform DPL series. The first operation in the series was approved on March 24, 2015. The second operation, planned for December 2015, will support the government in completing the resolution of the Privatization Agency portfolio by providing financial support to offset reform cost, and by delivering advice on technical aspects of reform implementation.

<p><b>Focus Area 2: Private sector growth and economic inclusion</b></p> <p><b>CPF Objectives:</b></p> <p><i>Objective 2a: Contribute to priority business climate improvements</i></p> <p><i>Objective 2b: Assist in creating a more stable and accessible financial sector</i></p> <p><i>Objective 2c: Support development of more efficient land and property markets</i></p> <p><i>Objective 2d: Enhanced infrastructure networks</i></p> <p><i>Objective 2e: Reduced barriers to labor market participation</i></p> <p><i>Objective 2f: Assist in closing medium and long term skill gaps</i></p>
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**CPF Objective 2a – Contribute to priority business climate improvements**

94. **The establishment of a competitive business environment will significantly help to reduce poverty and create new opportunities for the B40.** Simplification of tax procedures, a reformed process for issuing construction permits and improved performance of the customs administration should help promote new investments, both in export oriented sectors and in the non-tradable sectors which are critical for employment creation for the B40. In addition, addressing property issues will help all citizens- but particularly those less well-off- to define and protect ownership rights. This would then be a basis for easing access to credit and promoting entrepreneurship.

95. **As a small, open middle-income economy, Serbia’s main path to prosperity is to improve significantly its business climate, leading to an increase in investments that will allow more successful international integration, especially with Europe.** This focus area is critical for growth and poverty reduction and for increasing incomes through employment. Serbia ranks relatively low compared to its neighbors in the 2015 WBG Doing Business (DB) report. Serbia ranked 91 out of 189 economies, below neighboring countries such as FYR Macedonia (30), Montenegro (36), Bulgaria (38) and Romania (48). In the region it is ahead of only Bosnia and Herzegovina (107). Serbia faces specific challenges in four areas covered by DB report: i) dealing with construction permits (rank 186); ii) paying taxes (rank 165); iii) trading across borders (rank 96), and; iv) enforcing contracts (rank 96).

96. **According to the Business Environment and Enterprise Survey (BEEPS) 2013, the top three impediments to businesses are regulatory and political instability, tax rates, and competitors in the informal economy.** Other major obstacles are corruption, access to finance, tax administration, the court system, crime, customs, and trade regulations. Business climate reforms that will be important to all types and sizes of firms are; (a) reducing the time it takes to obtain construction permits; (b) making policy and regulation more predictable, and consistently enforcing laws and regulations through better administrative coordination and supervision including inspection reform, simplification of tax procedures and removal of administrative barriers; (c) combating the informal economy and continuing to restructure SOEs; and (d) improving contract enforcement and insolvency mechanisms.

97. **Regarding trade facilitation and border crossings, Serbia is ranked 63rd out of 160**

**countries in the World Bank's Logistics Performance Index<sup>4</sup> 2014**, a marked improvement from its 83rd ranking in 2010. The lowest ranking is in customs (113<sup>th</sup>) which adversely impacts border crossing times and costs. Serbia's ranking in the LPI is lower than all comparator countries suggesting that improvements are possible.

98. **For large and exporting enterprises, facilitating customs and trade seems particularly critical.** All these measures are vital for Serbia to secure current investments, attract more investments, create broad-based growth and job opportunities, and increase exports and competitiveness. Also, bearing in mind Serbia's prospective EU accession as well as a strong trade relationship, business environment reform should take into consideration the approximation of Serbian legislation with EU laws.

99. **Through its advisory and lending engagements, the WBG will contribute to improving Serbia's performance in three critical aspects of the business climate; paying taxes; trading across borders and resolving insolvency.** Some other key aspects of the business climate, in particular access to finance and planning and construction, are addressed under CPF objectives 2b and 2c, given the WBG's in depth engagements in these areas. The instruments to assist with the three elements of the business climate covered under this objective are IFC and IBRD advisory support and pilot initiatives (e.g. the Innovation Fund and Technology Transfer Facility), which will be deployed selectively. Pilots will be scaled up where successful.

#### **CPF Objective 2b – Assist in creating a more stable and accessible financial sector**

100. **The WBG has a strong engagement in the financial sector, including the ongoing Deposit Insurance Agency Strengthening Project (which will continue until mid-2016), a broad set of advisory engagements and IFC investments in private banks and state-owned banks being privatized.** Financial sector issues are multi-faceted. Support under the new CPF will build on the earlier engagement and aims, in particular, to address reform of state-owned banks and access to finance. Inadequate access to finance was highlighted as a critical binding constraint to economic growth and development, affecting SMEs in particular. All these aspects are critical to making the financial sector more accessible and stable, which will in turn stimulate economic activity and job creation, which, as set out in the SCD, is the most critical factor in boosting shared prosperity in Serbia.

101. **The chronically high rate of NPLs in Serbia, currently standing at 23% of total loans, increases banks' risk aversion, dampens credit growth, jeopardizes profitability and presents a systemic risk for the banking sector.** The domino-effect caused by insolvent companies preventing loan repayment, as well as potential savings and investments, further increases the cautiousness of banks. Improving the regulatory framework for NPL resolution is a key to decreasing the internal risks faced by the financial system in Serbia.

102. **The resolution of NPLs in Serbia is impeded by lengthy insolvency proceedings, unclear**

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<sup>4</sup> In 2007 the World Bank launched the Logistics Performance Index (LPI), a benchmarking tool that measures performance along the logistics supply chain within a country. Based on a worldwide survey of global freight forwarders and express carriers, the LPI helps identify challenges and opportunities along the supply chain. Using a 5-point scale, the LPI looks at six areas of performance: (i) customs; (ii) infrastructure; (iii) international shipments; (iv) logistics competence; (v) tracking and tracing; and (vi) timeliness.

**positions of classes of creditors, legislation protecting debtors rather than creditors, weak supervision over insolvency administrators, and lack of technical knowledge among the judiciary where court proceeding and execution of security can take years.** The IMF, as part of its current standby facility is coordinating a working group of IFIs including IFC, EBRD and the World Bank Group to address the NPL problem in Serbia.

103. **Apart from addressing the issue of NPLs, the WBG strategy in the financial sector also aims to support access to finance for small and medium sized enterprises as well as individuals.** In the context of a broad WBG engagement, IFC will directly support the financial sector through a set of products and instruments. First, IFC began an advisory project in November 2014 with the Government of Serbia to implement the Debt Resolution Program, with primary focus on the legislation that would provide for better debt resolution, allowing for better out-of-court restructuring and sustaining viable businesses. A component of the advisory work also focuses on the training of judges in foreclosure proceedings. While engaging in this area, particular attention will be given to improving access to finance for SMEs and agribusiness.

104. **Second, IFC will support the creation of a secondary market for distressed assets and NPLs.** Similar to its strategy in Latin American and Asian countries, the IFC approach in Serbia is to help the country through its network of partners across the ECA region that would allow IFC to source, structure, and co-invest in all classes of distressed assets in the countries. However, depending on banks' excess liquidity, a risk remains that banks might hesitate to sell portfolios at the offered discounts. However, tackling NPLs by trying to buy NPL portfolios from the banks would be possible if the debt resolution program is done in parallel with regulatory changes, which are being coordinated with the Development Partner group mentioned above.

105. **Third, once the NPL situation improves, and subject to demand from the market, IFC will invest in the financial sector using its debt and equity financing as well as short term finance to support trade finance.** IFC's financing will target underserved sectors of the Serbian economy to improve access to finance. Using a range of products, IFC will engage with selected banks to support SMEs facing limited access to finance despite being the main sector that generates new jobs in the country. IFC will continue to support home ownership by providing long term loans to banks for mortgages. To facilitate the increase of the dinarization of the economy as one of the key objectives of the Government, IFC will encourage local currency lending and will continue its dialogue with the NBS on an IFC Dinar Issuance Bond. Following the recent successful privatization of Čačanska banka in cooperation with EBRD, IFC will continue its dialogue with the government on the privatization of the remaining state owned bank where IFC is a shareholder (Komercijalna Banka), as well as on the completion of insurance sector privatization.

106. **A further element of financial sector strengthening, directly related to climate-change risks, is the regional Catastrophic Risk Insurance Facility.** This facility was created in 2012, and has been operational in Serbia since 2014. It provides previously non-existent protection to both enterprises and citizens against climate-related disasters.

107. **Finally, MIGA will continue to engage in providing guarantees to Banks and other financial sector institutions,** which constitutes the main part of MIGA engagement in Serbia.

#### **CPF Objective 2c – Support development of more efficient land and property markets**

108. **Issues related to land and property are major impediments to investments and economic growth in Serbia.** Security of property rights is a crucial building block for successful market economies. Real estate property is a key input to most production and investment processes, as well as a foundation for social stability and people's well-being. Addressing property management issues should help all citizens, but particularly those in the B40, to clarify and protect ownership rights. This would be a basis for easier access to credit and promoting entrepreneurship. An effective and transparent land registration system is particularly critical to reviving economic activities in rural areas, including in agriculture, hence meeting this objective will have a directly positive impact on boosting shared prosperity.

109. **Over the last decade important improvements in Serbia's land administration have been made such as creation of a unified register of real estate and real estate rights** (supported through the WB-funded Real Estate Cadaster and Registration Project). However, the data on land, ownership, buildings, utility lines, etc. - all vital information for most government services - need to be completed and made more easily available. The property registration system needs to be modernized, and the efficiency of the registration process increased. These improvements could be achieved by streamlining processes for property registration, resolving the backlog of cases, improving data quality and upgrading the IT system to allow for easy on-line access to data and services.

110. **Reforming the process for issuing construction permits is critical for enabling investments in land and property.** Investors closely watch developments in construction permitting because it could be the determining factor for making a decision to invest in Serbia or not. For several years construction permit issuance processes were the area most criticized by Serbia's Foreign Investors Council. The new legal framework on planning and construction adopted in December 2014 is considered an important step forward, even if it is at an early stage of implementation.

111. **A more efficient construction permitting system would support the private sector in expanding their businesses.** Streamlining the construction permitting process, creating the system of unified procedures, and redefining the role of institutions in the construction permitting procedures will also help spur job growth in the construction and other related sectors of the Serbian economy. The recent initiation of e-permitting is an important step forward, but needs to be rolled out.

112. **On this objective area, it is particularly important to address gender aspects of property registration and records.** Women entrepreneurs are particularly affected as properties are almost invariably registered to males, making it extremely difficult for female entrepreneurs to access credit.

113. **Delivery of support under this objective will be primarily provided under the recently approved Real Estate Management Project,** which supports both improvements in property registration, property valuation and the implementation of select aspects of the new Law on Planning and Construction.

114. **In addition, MIGA has initiated a guarantee engagement in the real estate sector, which would further broader WBG engagement under this objective.**

#### **CPF Objective 2d - Enhanced infrastructure networks**

115. **Connectivity is a further critical driver of competitiveness, and the quality of infrastructure networks is an important factor in Serbia's ability to shift the economy towards export-orientation.** Both a need and a large potential exist for improvement in the quality of Serbia's transport infrastructure. According to the Global Competitiveness Index (GCI) 2014-15, a highly comprehensive index that captures 12 pillars of competitiveness, Serbia ranks 94<sup>th</sup> out of 144 countries. Serbia's rank in infrastructure—which includes telecommunications and electricity as well as transport infrastructure—at 111<sup>th</sup>, is lower than its overall rank.

116. **The CPF consultation process brought out the criticality of the connection to infrastructure networks for the development of small cities, rural areas and communities,** where most of the B40 reside. Where such towns and cities lack access to infrastructure networks, economic decline has been significantly deeper, and the number of people falling back into poverty greater, showing the direct impact of infrastructure connections on rural economic development.

117. **The WBG contribution to the improvement of infrastructure networks will focus on road, railway and energy networks. As regards the road sector, the WBG will work together with EIB and EBRD to complete the Corridor X highway and to put in place an effective system of managing and maintaining other major national roads.** This engagement builds on a long standing dialogue the WBG has had in the transport sector. As regards Corridor X, many sections of the Corridor X motorways south of Belgrade are under construction and are expected to be completed in the next few years with the exception of a 6 km section that was to be funded by the Hellenic Fund. Other than this section, resources have been committed by the Government of Serbia and international financial institutions (IFIs) for the completion of the motorways. The completion of this major highway and the improvement of connecting roads will help enhance economic opportunities for rural areas and small towns, and in this way enhance shared prosperity.

118. **In addition, the WBG will engage on Railway Sector reform, primarily by supporting the reform of Railways of Serbia, with a focus on creating efficient cargo services.** In this respect, investment in the rehabilitation of the track, particularly along Corridor X and Route 4 connecting to the port of Bar in Montenegro, is necessary. While loans have been secured from the EIB, EBRD and Russia for infrastructure along Corridor X, these investments need to be implemented along with railway sector reforms in order to maximize the benefits of the physical improvements. Finally, IFC engagement on PPPs and infrastructure concessions, in roads, airports and other facilities, will be pursued.

119. **For the development of the energy sector it is vital to link EPS to the Region's Energy networks, thus contributing to economic growth through enhanced international and local connectivity.** With annual final consumption of about 28 TWh, Serbia is one of the largest power markets in South East Europe and its strategic geographic position at the heart of the Balkans gives it an important role in the power trade in South East Europe. Connected to eight countries, the main regional trading pattern is a flow of electricity from the EU member states to its neighbors and within the region. In 2014, about 12 TWh flowed through Serbia, equivalent to 44 percent of its own annual energy consumption. Furthermore, a significant portion of the country's hydropower potential is from rivers that border neighboring countries.

120. **Decisions in managing water have both domestic and regional implications for energy security, water quality, climate change mitigation and adaptation, and ecological protection.**



Improved network connectivity will be coupled with efforts to enhance energy efficiency, as an element of the climate adaptation agenda. The planned energy sector governance project will focus on upgrading the existing network so it can work as part of an integrated regional power network. This project would also contribute to enhancing energy efficiency and mitigating climate change risks, through support to the implementation of the national energy efficiency action plan.

### **CPF Objective 2e - Reduced barriers to labor market participation**

121. **Serbia faces a situation where more than 60 percent of the adult population is not employed.** Not surprisingly, this group of people also constitute the majority of the B40, and the lack of labor income is also the key constraint to lift them out of poverty. They consist mostly of two groups: (i) the (pre-) transition generation, aged 40 and older, who either lost their jobs during transition and never found a proper new job, or entered the labor market right during the onset of transition and never gained a strong foothold; and (ii) certain groups, especially minorities like Roma, but also women, who were never strongly attached to the labor market, to this day. Getting this large part of the adult population into to work is the most critical element of enhancing shared prosperity in Serbia. It would also bring a significant growth impulse to the Serbian economy.

122. **Progress on this agenda requires labor market reforms as well as removing obstacles to investment in the non-tradable sector, in agriculture and micro and small enterprises.** Given the skills profile of the B40, an export-led growth strategy with a focus on high-productivity jobs will not be sufficient to generate jobs for the B40. Indeed, the current profile of those from the B40 who have jobs reveals that the most of them work in the non-tradable sector, especially services, and work for micro or small firms. Also, in advanced OECD countries, many of the B40 work in flexible, non-standard jobs, especially part time. Unlocking the potential of this nonexistent segment of the Serbian labor market is key for the B40. The CPF will focus on a set of reforms that will specifically help to create employment opportunities for the B40.

123. **The first priority in labor market reform is revising the minimum social security contribution policy, while taking into account the fiscal impact.** The current design of contributions puts a high burden on low wage earners, especially for part-time work. The base for the minimum social security contribution is set at 35 percent of minimum wage. This means that any job that earns less than 35 percent of average wage is subject to the same minimum contribution. This is especially expensive for part-time work because the minimum contribution is not adjusted for hours worked. For certain low-paying jobs at the very low end, the earned income would actually not be sufficient to pay the required minimum contribution, clearly making any kind of low-paying part time work prohibitive in the formal sector. Yet, it is exactly these kinds of jobs that would create a stepping stone for many in the B40 to enter the formal labor market and take advantage of economic opportunities. Before legislating this reform it is important to conduct a careful fiscal impact analysis.

124. **In addition, there is further need for reform in the design of social benefits.** A number of benefits come with considerable disincentives for formal work, thereby closing off the single best route to escaping poverty for the B40. For many beneficiaries, taking up any kind of formal job would (i) either result in a considerable decrease in net income because earned income would not make up for lost benefits and taxes due; or (ii) only marginally increase net income so that the tradeoff between no work and work is not favorable. Redesigning these benefits to truly reward formal work is again a necessary pre-condition to activate the B40.

125. **Combined, these reforms should be the crucial first step to unlock the potential of a new segment in the Serbian labor market, one that has not existed before.** It is a segment of—mostly—low-paying formal part-time jobs, that in many OECD countries make up a considerable part of the labor market. It should help to bring back the 40+ generation into work, but also excluded groups like Roma and, importantly, women. For the latter, additional measures, like providing care facilities for children and elderly, might be necessary to help women reconcile care duties with career goals.

126. **Further reforms of key labor market institutions like the National Employment Service (NES) are necessary.** The focus needs to be on ensuring efficient match making between job seekers and employers and providing good quality services to beneficiaries and employers. This will require a focus on vacancy collection, profiling of beneficiaries, deployment of more and better case managers, a focus on active jobs seekers (as opposed to registered unemployed), and better targeting and monitoring of active labor market programs.

127. **In terms of support to be provided, the Competitiveness and Jobs Project (FY 16 deliverable) will provide financing** for the implementation of key aspects of the reform agenda outlined here, focusing on enhancing the effectiveness of investment and export promotion programs, developing systems to promote innovation and technology transfer and addressing barriers to labor market entry. Given that these reforms will take time to generate a sustained impact, a follow up project could be considered in the later years of the CPF.

#### **CPF Objective 2f – Assist in closing medium and long term skill gaps**

128. **A critical condition for achieving long term employment growth is closing skill gaps, both in the short and long term.** Shorter term measures include the introduction of reforms in vocational and, to a lesser extent, tertiary education systems to better align programs with labor market needs. Reforming the vocational training system to respond to labor market needs can be of potential benefit to the B40 in particular. While such reforms will take time to be implemented and have their full impact, it is important that work starts now, so that relevant skills will be available for investors as the economy expands. The reform of programs based on improved forecasting of medium term labor market needs will be pursued both through dialogue with the Ministry of Labor and Social Protection as well as with the Ministry of Education and Science.

129. **Addressing long term skill gaps through enhanced access to Early Childhood Education is not only important for overall employment growth but also removes a critical barriers to female labor market participation.** Therefore, closing enrollment gaps for early childhood development – particularly for low-income and vulnerable groups – would be a “double win”. Early childhood education is critical to increasing long-term productivity and inclusion, but would also generate benefits in the short term by reducing labor market barriers for mothers of young children. Single female-headed households are more likely to be within the B40, and this reform would unlock opportunities for this group specifically.

130. **The planned Skills project will help address both short and long term skills gaps, focusing on vocational training, but in particular on enhancing access to Early Childhood Education,** which is a critical constraint to long term skills development, especially among vulnerable and disadvantaged

groups. Partnerships with other development partners, including potentially non-governmental partners, will be sought to ensure that comprehensive support is provided to this agenda.

### **C. Implementing the FY16-20 Country Partnership Framework**

131. **The Serbia CPF for FY16-20 builds on WBG ongoing portfolio, which aligns well with the proposed objectives of the new CPF.** *In terms of IBRD support*, there are currently seven active projects with commitments totaling US\$1.1 billion. These projects support investments in roads, health, financial sector, energy, water, flood protection, and land and property management. Considering the CPF priorities, engagement in water management will be phased out during the CPF period, while health sector engagement will be pursued in the context of the fiscal consolidation and effective service delivery objectives. Serbia's portfolio performance has been slightly below ECA average performance, with disbursement rate averaging 16.2 percent over the last ten years. It should be noted that in FY 15 disbursement levels are likely to reach 50 percent as a result of the shift to more result-based financing operations. *As regards IFC support*, IFC built a portfolio through its robust program during the previous strategy period, albeit with deteriorating quality in the manufacturing and agribusiness sectors. IFC has currently an active committed portfolio of US\$417 million (US\$414 outstanding), allocated in 24 projects, mostly in the manufacturing, services and agriculture (US\$216 million) as well as in the financial markets (US\$198 million). In the infrastructure sectors IFC has only 1 percent of its portfolio in one development project (US\$3 million). In addition, IFC has 10 active advisory services projects focused in the areas of Trade and Competitiveness, Renewable Energy, Resource Efficiency, Corporate Governance, Tax Simplification, SME Banking, Investment Climate in Agribusiness sector, and PPPs. Through its investment and advisory portfolio IFC would be able to continue to address a number of strategic objectives as identified in the CPF for the period FY16-FY20. Serbia is one of MIGAs largest exposures with engagements in particular in the financial sector.

132. **In terms of program size, the authorities have requested a strong front-loaded program, given the need to finance important upfront reforms and adjustments.** The lending program set out in Table 3 is indicative and actual lending will depend, among other things, on country demand, performance and IBRD financial capacity. In the event reform commitment wavers and/or the medium-term macro-fiscal framework is off-track, the IBRD lending program would be calibrated downward and instruments would be adjusted and take advantage of those remaining reform and investment opportunities that have a clear linkage to achievement of the twin goals. In FY 15, IBRD commitments rose to US\$ 444 million, including a US\$ 300 million Emergency Recovery Loan that responded to the May 2014 floods, but also paved the way for renewed policy dialogue on the energy sector. The government has requested lending for FY16 at the level of US\$ 475 million. The Government indicative borrowing plan for FY 17 amounts to US\$ 320 million and for FY 18 to US\$ 280 million.

133. **IFC investments are expected to be in the order of US\$ 400-600 million over the five year CPF**, subject to the progress with resolving the problem of NPLs, the government's implementation of enabling regulations to support private sector investment in renewable energy, further improvements of the business environment and the growth outlook in Europe.

134. **MIGA will continue to explore and diversify guarantee opportunities.** Currently, MIGA's engagement is concentrated in the financial sector as a reflection of demand for its products and services.

Going forward MIGA will explore options to engage in other sectors, as exemplified by its ongoing engagement in a real estate development project.

**Table 3: CPF Indicative IBRD Lending Program FY16-20**

<b>FY</b>	<b>PROJECT</b>	<b>IBRD (US\$ million)</b>
<b>FY16</b>	Serbia Competitiveness and Jobs RBF	100
	Public Sector Employment and Performance RBF	75
	Serbia Public Enterprise Restructuring DPL 2	100
	Public Expenditure and Utilities Reform DPL 1	200
<b>Sub-total FY16</b>		<b>475</b>
<b>FY17</b>	Public Expenditure and Utilities Reform DPL 2	200
	Inclusive Education and Skills Project	50
	Financial Sector Reform Project	70
<b>Sub-total FY17</b>		<b>320</b>
<b>FY18</b>	Public Expenditure and PFM DPL or PforR	180
	Energy Sector Development Project	100
<b>Sub-total FY18</b>		<b>280</b>
<b>FY19</b>	Transport Sector Governance Project	130
	Development Policy Loan or CAT DDO	130
<b>Sub-total FY19</b>		<b>260</b>
<b>FY20</b>	Second Competitiveness and Jobs Project	100
	Development Policy Loan or PforR	160
<b>Sub-total FY20</b>		<b>260</b>
<b>TOTAL</b>		<b>1,595</b>

135. **The CPF brings a greater focus on results.** The choice of instruments in the indicative program includes Additional Financing for well performing operations, policy-based lending in support of macro-fiscal and structural reforms and IPFs, including several with results-based financing aspects, in diverse sectors such as public sector employment and wage reform, education, transport, competitiveness and skills.

136. **Given the continued emphasis on larger and transformative operations, the number of operations in the IBRD portfolio is likely to remain stable at around 6-8 active operations.** The WBG will seek to leverage our own resources for investment, results-based operations and development policy lending with grant financing from other partners for technical and advisory services. As an example, the World Bank engagement in public sector employment and pay reform will be complemented and supported by an EU financed IPA grant for advisory support and technical assistance.

137. **The CPF seeks to maximize the synergies among the IBRD, IFC and MIGA.** Strong collaboration exists between the IBRD and IFC in the area of business environment where the teams work jointly. Active collaboration in transport, competitiveness, skills development and health is foreseen during the CPF period. IFC will strengthen its current investments and advisory services in energy and banking sector, and will further lend support to agribusiness, renewable energy, SMEs,

transport, health and waste management. All three institutions are providing mutually reinforcing assistance in the energy and financial sectors. MIGA is involved in 4 sector guarantee operations, including in the financial sector. Supporting foreign investment through political risk guarantees, in close coordination with the IFC and IBRD, will remain a strategic priority for MIGA's activities in Serbia.

138. **Operationally relevant analytical work, knowledge support and technical assistance will be a key part of the CPF program, strategically aligned in support of the CPF objectives and the proposed project portfolio.** Analytical work under the program will aim to fill, where feasible, the knowledge gaps identified under the SCD, namely in the areas of labor demand, climate change, Roma issues and skills, to provide the analytical foundations for the proposed operations under the CPF and for ongoing policy dialogue and implementation support, and to put in place the analytical foundations for the next SCD. Traditional forms of dissemination of this analytical work (for example, press conferences and workshops) will be combined with innovative channels of communication including social media.

139. **As in the past, in-depth cross-sectoral analytical work will be complemented by just-in-time analysis to support the government in addressing particular policy challenges that the country faces.** Examples of just-in-time work could include strengthening the out-of-court restructuring and insolvency framework and an assessment of energy tariff reform and their welfare impact. In addition, a policy coordination and implementation tracking assessment will be done, linked to CPF monitoring. The pipeline of in-depth analytical work on the core bottlenecks for growth and shared prosperity will be based on the findings of the ongoing Public Finance Review. Other proposed analytical work includes a programmatic poverty analytical work program, a financial sector assessment, energy sector strategy and analytical work on public investment management and social sector financing.

140. **The knowledge gap in some areas, including those identified in the SCD, will be closed by regional analytical work.** The bank plans to initiate several regional reports or technical assistance activities covering a range of topics – Roma; education; climate change; gender; competitiveness; energy and pensions. This new approach to analytical work should be more cost-effective; to provide for synergies and might spur regional cooperation in responding to some of the challenges that are common to the whole region.

141. **The progressive integration of the Trust Fund portfolio in the WBG overall program, as seen in the previous CPS, will be further deepened.** Currently there are ten Trust Funds amounting to US\$22.8 million focused on judicial reform, innovation and technology transfer, public financial management assessment, Roma inclusion, and disaster risk management. Annex 1 indicates how these Trust Funds support the eleven CPF objectives.

142. **The CPF Results Matrix presented in Annex 1 will serve as a management tool throughout implementation.** Progress in CPF milestones will be annually monitored with the client and at mid-term under the Performance and Learning Review (PLR). The CPF Results Framework has been prepared by a multi-sector team. An annual review on progress on result indicators will be held by focus area.

143. **The re-institution of regular portfolio performance reviews at the country level will help create better and higher level oversight of program performance and allow for timely resolution of emerging bottlenecks.** The portfolio performance reviews will be conducted at two levels: i) annual

portfolio reviews under the leadership of the Ministry of Finance; ii) quarterly reviews will be conducted with relevant ministries to seek resolution of emerging issues related to problem or high risk projects. In addition, an annual review will be conducted with a particular focus on assessing progress on the CPF supplementary indicators. An emphasis will be placed on results oriented implementation support, which will underpin portfolio reviews, and will encourage greater proactivity for poorly-performing operations.

## **C. 1 Review of Government Procurement and Financial Management Systems**

### *Public Procurement*

144. **The Republic of Serbia adopted a new Public Procurement Law (the Law) on December 29, 2012, which became effective on April 1, 2013.** The Law is a significant effort to bring the Serbia public procurement system close to international procurement standards, but more importantly a step forward towards the alignment with the EU Procurement Directives (2004/18), as required by the Stabilization and Association Agreement (SAA) between the EU and Serbia. To ensure implementation of the Law, a number of implementing regulations and model tender documents have been adopted during 2013.

145. **The Law sets forth important objectives of ensuring efficiency and effectiveness, competition and transparency and preventing corruption and other abuses in the public procurement process.** The above considerations are reflected in a number of articles throughout the Law, including those providing for publication of notices through the portal of public procurement, introduction of mandatory procurement planning, creation of register of bidders, involvement of civil supervisor, provisions on preventing corruption and conflict of interest, post-employment restrictions for procuring entity staff, etc. Similarly, the Law reflects good international practice in providing for a complaints review mechanism.

146. **Notwithstanding the above achievements, there is still room for further improvement including related to the institutional framework.** Currently, two main institutions that ensure implementation of this law are the Public Procurement Office (PPO) and an independent entity responsible for review of complaints (the Republic Commission for the Protection of Rights in Public Procurement Procedures - RC). However, the role of PPO in initiating changes/amendments in the primary legislation is not clearly defined in the Law. Additionally, the Law's objectives would be better served if its application is extended to all procuring entities, expands the conflict of interest provisions, spells out the due process requirements for inclusion of a bidder in the list of negative references<sup>5</sup>, and circumscribes application of domestic preferences only as price preference, and not weights/points, and defines the "domestic input". While the Law provides for the use of Electronic Auction, an e-procurement platform has not yet been developed to support these requirements.

147. **The World Bank will continue to provide technical support to further strengthen public procurement system in Serbia.** This support shall be in line with the government's four year Public Procurement Strategy 2014-2018 and the 2015 Action Plan. The process of amending the PPL should be closely monitored, and the Bank should provide technical assistance to increase transparency, efficiency and competitiveness in the public procurement system as well as strengthen external audit

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<sup>5</sup> The complexity of such process for giving "a negative reference" has led to a situation that no company so far has been put on the list.

carried out by the State Audit Institution.

### *Public financial management*

148. **A number of reforms of the public financial management system have been undertaken in the last several years. Nonetheless, according to the forthcoming Public Expenditures and Financial Accountability (PEFA) assessment, further substantial improvements are required in certain areas.** Annual budget preparation as well as multi-annual planning remains weak and faces issues repeatedly vis-à-vis the process and its timeliness. Capital investments will need to be based on more precise and meaningful cost-benefit analysis and linked to sector strategies in order to enable efficient use of resources and yield better results. Public Internal Financial Control (PIFC) framework, as envisaged by the EU chapter 32 on financial control, has been established by provisions of the Budget System Law, nevertheless functions of internal audit and financial management and control in practice still require significant development.

149. **Consequently the use of country systems by the Bank is limited.** The WB projects rely on country systems only in the area of flow of funds with the project designated accounts being opened in the NBS since 2012. This also contributes to enhancement of the Government's budgeting and financial reporting, since IFI's projects with the funds flowing through commercial banks, often remained excluded from state budget and in some cases even from annual financial statements. Country systems in other areas are currently not used, due to either already existing heavy work load on some institutions (such as the State Audit Institution) or further improvements needed in the country systems (such as Public Internal Financial Control).

## **C.2 Partnership and Coordination**

150. **Collaboration and coordination with development partners will remain strong with WBG engagement leveraging other partners' assistance.** Serbia, as a middle income country, has a small number of active development partners, and relies to a large extent on IFIs and bilateral lenders for financing its development needs. The only significant source of grant financing comes from EU IPA resources, which are expected to amount to Euro 200 Million annually during the CPF implementation period. Some of these resources may be used for budget support, but a large portion will be used for capacity building support. In the current fiscal context, seeking complementarities between EU grant financing and IFI budget and investment support is particularly critical. The WBG and the EU have already partnered in a number of priority sectors, e.g. on public administration reform, disaster risk mitigation, strengthening statistical capacity, innovation and technology transfer and railway and road sector reforms. This partnership is expected to expand further. Cooperation and coordination with bilateral partners (in particular Switzerland, Norway, Sweden and USAID) remains strong, with coordinated financing and MDTF arrangements in place in several sectors, including public sector reform, disaster risk mitigation, competitiveness and innovation and judicial reform.

151. **The Government has a dual donor coordination mechanism, with coordination of grant financing managed by SEIO (Serbia European Integration Office) and loan financing by the Ministry of Finance.** Coordination of grant and loan financing has been a challenge in the past, and coordination mechanisms are being strengthened, with the Ministry of Finance taking a lead role.

#### IV. MANAGING RISKS TO THE CPF PROGRAM

152. **The overall risk to achievement of the development objectives outlined in the CPF is substantial.** Overall, categories which poses high risk to reaching CPF objectives include: the macroeconomic outlook; political and governance and environmental and social factors. Institutional capacities for implementation of public policies pose a substantial risk to reaching CPF objectives. All other categories are ranked as moderate. The risks to the CPF development objectives are summarized in the Standardized Operations Risk-rating Tool (SORT) table below.

153. **Macroeconomic risks stemming from emerging or continuing domestic and external imbalances are high.** Most importantly, the government ran a very high fiscal deficit over the previous several years (ranging between 4 and 7.2 percent of GDP) which resulted in a significant increase of the public debt (from less than 40 percent before the crisis to over 70 percent by end 2014). In addition, the current account deficit at 6 percent of GDP is still high and prospects for a more significant expansion of exports are limited, having in mind the economic outlook for the Eurozone and the CEFTA region, which are Serbia's main trading partners. Consequently, the stock of external debt is expected to remain high over the CPF period. While the government tries to mitigate macroeconomic risk, the Serbian economy remains vulnerable to external shocks and to slower growth in the Eurozone, in particular, which is the main destination for exports and the source of FDI and remittances for Serbia. A related risk is failure to implement the IMF program, most likely due to social pressures which would block SOE or other sensitive fiscal reforms. If macroeconomic risks (external in particular) increase and implementation of the IMF program is inadequate or fails, this will pose a high risk to the CPF program, in particular to CPF Objective 1a (Supporting sustainable public expenditure management) given that a significant portion of planned financing operations are DPLs, which require the stable macro-economic framework codified in the IMF program. If commitment to reform wanes and the macro-economic situation deteriorates, the lending program would be scaled down accordingly, with a focus on IPFs or PforR in support of areas where country ownership remains high and which are critical to Serbia's progress in achieving the WBG Twin Goals.

154. **Despite a welcome degree of political stability in the country, a high likelihood remains that political and governance factors could adversely affect CPF development objectives over the medium-term.** At the moment Serbia has a high level of political stability since one political party holds an absolute majority in the parliament. The government is pursuing an ambitious reform agenda and the WBG is seen as the key partner. Consequently, the political risk is presently assessed as moderate, but might increase over the course of the CPF. Nevertheless, the governance risk is high due to weaknesses in the public sector management system, which negatively impacts on policy implementation and sustainability of reforms. The legislative framework for anti-corruption and ethics in the public sector is in place and aligned with European good practices. However, implementation is uneven. Thus, the overall risk rating in terms of political and governance risk is substantial. As in the case of macro-economic risks, deterioration in the level of political stability and in the quality of governance would have implications for reaching the CPF objectives and for the WBG program, which in this case would be re-oriented to support for those areas where reform commitment remains in place and with relevance to the WBG Twin Goals. Objectives that would be impacted most by increased political and governance risks include Objective 1b (Assist in creating a more effective public administration & improving select service delivery) and Objective 1e (Productive SOE assets transferred to private ownership) since



reaching either of the objectives would include public sector staff retrenchment which in turn requires a strong political support and a good governance.

**Table 4: SORT Table**

<b>Risk Categories</b>	<b>Rating</b>
Political and governance	H
Macroeconomic	H
Sector strategies and policies	M
Technical design of project or program	M
Institutional capacity for implementation and sustainability	S
Fiduciary	M
Environment and social	H
Stakeholders	M
<b>Overall</b>	<b>Substantial</b>

155. **Serbia experienced recently both severe droughts and floods which caused significant material damages and losses thus suggesting a high likelihood that exogenous environmental could adversely affect the achievement of CPF objectives.** Although the impact of previous natural disasters was concentrated in some parts of the country, the economy was in recession twice because of adverse weather conditions (in 2012 and 2014). Environmental risks, including droughts, flooding, severe storms, earthquakes, and landslides will increase due to the impact of climate change and certain actions by citizens related to use of land, water and other natural resources. In addition, some of the envisaged reforms (reduction of pensions and public sector wages; reform of SOEs, included in Objectives 1a: Supporting sustainable public expenditure management; and Objective 1e: Productive SOE assets transferred to private ownership) might have a significant adverse social impacts on the poor, and other vulnerable groups and have the potential to contribute directly to increased social fragility.

156. **Institutional weaknesses in implementing agencies may undermine progress in spite of strong political commitment for reforms.** Implementation of difficult reforms, as planned by the government, often is delayed or completely stalled since it involves coordination across several agencies or across different levels of government. Line ministries have a relatively good in-house capacity, but external consultants still play an important role in the design and even sometimes in implementation of policies and decisions. Another problem that weakens government capacities is a substantial staff turnover. Wages in the central government administration are not competitive and are not in line with the complexity of the work that is required. Existing capacities would be better used if operational rules, processes and systems are better defined. Oversight and control mechanisms remain weak, and instances of minor fraud and corruption are common across the public sector in Serbia. If the risk from institutional weaknesses is not addressed some of the CPF objectives might be affect, most importantly: Objective 1b: Assist in creating a more effective public administration & improving select service delivery; and objective 2b: Assist in the creation of a more stable and accessible financial sector.

157. **Significant efforts are underway by the Serbian authorities to address previously mentioned risks and the WBG will provide significant support to that aim.** Thus in order to minimize macroeconomic risks the government has signed a 3 year Stand-By agreement with the IMF which was prepared in close coordination with Bank's teams. Institutional capacities and governance risks will be to some extent addressed by providing capacity support to line ministries including through TFs, TAs and including more targeted capacity assistance in new IBRD lending. The institutional risk will also be mitigated through careful sequencing of projects recognizing and addressing the country's weaknesses, and providing built-in flexibility for course correction. In order to promote sustainability there will be an increased use of Government structures during implementation. Operations will increasingly incorporate strong M&E arrangements and will strengthen monitoring systems.

## ANNEX 1. CPF RESULTS MATRIX (2016 – 2020)

### FOCUS AREA 1: ECONOMIC GOVERNANCE AND THE ROLE OF THE STATE

The SCD identified eleven priority areas for actions required to restore growth and make it inclusive and thus progress toward the twin goals. Of these, two are foundational and 5 are high impact. Focus Area 1 addresses the two foundational and one of the high impact priorities. These priorities directly support the goals of the country's fiscal strategy and economic reform program that focus on fiscal sustainability and better management of public resources, structural reforms related to SOEs, and on corporatizing large energy utilities and transport companies. It also supports significant priorities of Serbia's Public Sector Reform Strategy and Action Plan, adopted in 2014 and 2015 respectively. Focus Area 1 thus specifically address identified constraints to the effectiveness and size of the public sector: the size and management of the national budget, the size and organizational structure of the public administration, the capacity of the administration to implement reform and deliver services, the large footprint of the government in the economy, and the delivery of public utilities. Specifically, this Focus Area is designed to reduce constraints to growth and shared prosperity caused by the Government's fiscal un-sustainability, limited administrative capacity, and structural inadequacies and inefficiencies.

Five CPF Objectives are grouped under this Focus Area:

CPF Objective 1a: Supporting sustainable public expenditure management

CPF Objective 1b: Assist in creating a more effective public administration & improving select service delivery

CPF Objective 1c: More efficient and sustainable power utility

CPF Objective 1d: More efficient public transport companies

CPF Objective 1e: Productive SOE assets transferred to private ownership

#### CPF Objective 1a: Supporting sustainable public expenditure management

##### Intervention logic:

Sustainable fiscal consolidation and expenditure management is a key prerequisite for macroeconomic stability and growth, and for creating the enabling environment for the delivery of other CPF objectives. The authorities adopted an ambitious program (supported by the IMF) in January 2015 to halt the rise in public debt and put it on a downward trajectory by 2017. The program is outlined in the recently approved Fiscal Strategy 2015-17 and it includes actions aimed at: i) improving efficiency of public spending, enhancing revenue measures, ensuring financial sustainability of large SOEs (utilities and transport) thus reducing the need for new subsidies

and eliminating quasi fiscal deficits; ii) strengthening public financial management, including public investment management and public debt management; and iii) maintaining financial sector stability through reducing NPLs and debt resolution, strengthening financial sector supervisory institutions and managing effectively the government’s ownership stake in the banking sector. Absent fiscal consolidation there is a clear risk that government debt will be on an unsustainable path, raising risk premiums and financing costs, with the potential for disruptions to the government’s access to financing and for increased macro-fiscal instability. Such a scenario would adversely impact growth and risk future cuts in core public expenditures if a sharp fiscal adjustment is then required. The WBG will support the government’s fiscal consolidation and expenditure management efforts through a range of instruments, including Development Policy and Result Based financing, throughout the CPF period in order to ensure that the consolidation process is not undermined through in-efficient ad hoc expenditures, and the expenditure program is in line with the medium-term fiscal strategy. The SOE DPL series, the Public Expenditure and Utilities Reform DPL series, the Public Expenditure Management DPLs/RBFs will all be contributing to this CPF Objective. Prior action areas of the budget support operations are also supported through several TF financed TA projects and closely coordinated with the EU, the IMF and other European development partners. The design of financing operations will be informed by in-depth analytical work and TA activities which also directly contribute to this objective. For example, engagement on cost savings on the public sector wage bill will further contribute to medium term fiscal sustainability. Improving public investment management and management of PPPs is important for ensuring that scaling up public investment supports macro-fiscal stability and growth. Rationalizing and partially redirecting agricultural subsidies would bring about fiscal savings as well as ensure that a greater portion of subsidies benefit the B40 in rural areas.

CPF Objective Indicators	Supplementary Progress Indicators	WBG Program
<p>Reduction of public expenditures through lower direct subsidies and guarantees to SOEs</p> <p>Direct subsidies (million Euro):</p> <p>Baseline (average 2010-2014): 250 Target (2020): to be less than 150</p> <p>Annual guarantees for liquidity purposes (million Euro):</p> <p>Baseline (average 2012-2014): 265</p>	<p>Freeze on public sector wage indexation in years in which the share of general government salaries (excluding severance payments) is expected to exceed 7 percent of GDP.</p> <p>Freeze on public sector pension indexation in years in which pension spending is expected to exceed 11 percent of GDP.</p>	<p><b>Current Portfolio:</b></p> <p>Serbia Public Enterprise Restructuring DPL 1 (FY 15)</p> <p><b>Pipeline:</b></p> <p>Serbia Public Enterprise Restructuring DPL 2 (FY 16)</p> <p>Public Expenditure and Utilities Reform DPL series (2 operations, FY 16 and FY 17)</p>

<p>Target (2015): less than 50</p>	<p>Attrition and targeted reduction of public sector employees in line with the budget calendar adoption of the Fiscal Strategy.</p>	<p><b>Proposed:</b></p> <p>Public Expenditure Management DPL/PforR (FY 18) CAT DDO (FY 19)</p> <p><b>Ongoing TA:</b></p> <p>Public Expenditure and Financial Accountability (PEFA) Serbia Public Finance Review Serbia A&amp;A ROSC update Macro-economic monitoring</p> <p><b>Proposed ASA:</b></p> <p>Public Expenditure policies for growth Country Economic Memorandum Programmatic poverty assessment</p>
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**CPF Objective 1b: More effective public administration & select service delivery improvements**

**Intervention Logic:**

Implementation deficits, convoluted decision-making process and institutional fragmentation stand out as fundamental challenges to Serbia’s ability to implement the essential reforms needed to build a competitive inclusive economy. The same factors also account for weak sector service delivery performance, whether it in social services or in providing services to businesses and investors. Low trust in institutions and high levels of politicization further aggravate the systemic problems. Addressing the structural problems in public sector governance is a condition sine qua non for the implementation of the Government’s program and for the delivery of the WBG program itself. The Public Sector Reform Strategy and Action Plan, adopted in 2014 and 2015 respectively, set out a broad reform agenda. An important theme of the Reform Strategy is the rationalization of the overall government architecture (through a

horizontal functional audit) and the right sizing of critical sectors. Through the Strategy, the government aims to improve the quality of public administration and service delivery. These efforts will be jointly supported by the WBG and the EU. The CPF will selectively support the government's reform agenda through a combination of instruments, focusing on areas where government has demonstrated the most willingness to reform. Building on ongoing analytical work on Public Financial Review, Public Expenditure and Financial Accountability Assessment (PEFA), TA on Wage Bill, and Functional Review, the CPF will enhance the government's rationalization agenda by supporting elements of the proposed reforms that would improve government efficiency and service delivery. In addition to focusing on foundational elements of structural and functional organization of the public administration system, the WBG will engage in supporting service delivery improvements in a select number of sectors. The Public Sector Employment and Performance Project will be focused on cross-cutting support to frontline service delivery. A first sectoral focus will be the reform of the overhaul of investment and export incentive systems, which have been largely ineffective in attracting investment. The Government has committed to a functional and performance audit of the three agencies involved in the investment incentive and export promotion system. Second, the MDTF-JSS will continue to provide targeted TA to support the justice sector to align with EU standards. Finally, The Second Health Sector project includes support for sector expenditure rationalization, including broad health sector restructuring, and will also be one of the priority sectors for the government rightsizing efforts. Capacity development and institution building on Disaster Risk Management will also be provided to enhance the government's forecasting and response capacity for climate-induced disasters.

CPF Objective Indicators	Supplementary Progress Indicators	WBG Program
<p>A plan to strengthen the policy-making and coordination system prepared by end 2016 and implemented by 2019</p> <p>Indicator: Metcalfe Scale rating improved</p> <p>Baseline (2015): 2 Target (2019): 4</p>	<p>Right Sizing (Organizational rationalization) plans for at least 4 sectors designed and implemented by end 2017</p> <p>Overall institutional architecture of the administration rationalized by end 2017</p> <p>Justice sector has started to implement the recommendations contained in the Serbia Judicial Functional Review beginning with a freeze on filling vacant positions before the analysis on right-sizing is completed. All recommendations to be implemented by end 2018</p>	<p><b>Current portfolio:</b> Second Health Sector Project (FY 14)</p> <p><b>Pipeline:</b> Public Sector Employment and Wage system RBF (FY 16)</p> <p><b>Proposed:</b> Public expenditure and PFM DPL/PforR (FY 18) CAT DDO (FY19)</p> <p><b>Ongoing TA</b></p>

<p>Reduce percentage of non-medical staff employed in public health facilities in Serbia (by 15 percent)<sup>6</sup></p> <p>Baseline: 30 percent of public sector health workers are not medically trained (estimate based on 2013 data)</p> <p>Target: 25 percent or less of public sector health workers are not medically trained</p>	<p>Functional review completed for the Serbia health sector, which identifies priorities and targets for reducing non-medically trained staff, including confirming baseline and targets for 15% reduction of non-medical staff</p>	<p>Wage bill management ECA PFM TF Right Sizing TA (IPA financed) MDTF for Justice Sector Support TF on Disaster Risk Management</p> <p><b>Proposed TA</b> Per capita financing systems in social sectors</p> <p><b>Proposed ASA:</b> Policy management and implementation tracking assessment</p>
<p><b>CPF Objective 1c: A more efficient and sustainable power utility</b></p>		
<p><b>Intervention logic:</b></p> <p>Large energy utility SOEs structurally underperform due to poor facilities, state interference in their management, and a lack of professional management. The government has made the financial sustainability of energy utility and other SOEs an important element its program and policies. Towards the end of the 2011-2015 CPS decisive progress was made on both aspects of this agenda. Key legislative reforms were introduced and reform plans for the largest utilities framed and adopted. The comprehensiveness of approach and political commitment provide a unique opportunity to make progress on this most central element of Serbia’s economic reform agenda. In addition reform of utilities should help to increase access to utility services to marginalized groups (Roma in particular) and to those in rural areas (where poverty is much higher). Finally, engagement on increase the portion of electricity derived from renewable sources will both mitigate climate change risk and help Serbia meet its obligations under the European Energy Community. Under the CPF, the WGB will invest further to support utility financial consolidation, with a focus on EPS, with other IFIs and international partners providing support to a similar process in the gas utility Srbijagas. Given the complexity of these reforms, and the cost of implementation, budget or result based financing support will be considered along with advisory support. A series of DPL or RBF engagement should help remove policy and capacity constraints to effective infrastructure investments, which could be followed in the outer years of the CPF period by a specific operation to address remaining issues in the electricity sector.</p>		

<sup>6</sup> Gender disaggregated data for this indicator are currently not available but will be collected during the implementation of the Second Health Sector Project and added during the CPF PLR process

CPF Objective Indicators	Supplementary Progress Indicators	WBG Program
<p>EPS corporatization completed and financial sustainability achieved</p> <p>Indicators:</p> <p>Collection rates increase from 93% (2014) to 95% (2019)</p> <p>Distribution losses decrease from 14% (2014) to 12.1% by 2019</p> <p>Increase Serbia’s renewable energy generation capacity in wind increases by 100 MW</p> <p>Baseline (2015):</p> <p>Wind energy: 0 MW</p> <p>Target (2019):</p> <p>Wind energy: 100 MW</p>	<p>EPS established as a Joint Stock Company (2017)</p> <p>Strategic partner for EPS identified and equity stake sold by 2019</p> <p>Debt/EBITDA ratio below 3 by end 2016</p> <p>No further accumulation of SOE and budgetary institutions payables/arrears to EPS by end-2017</p> <p>Enabling regulations for investment in renewables enacted</p> <p>Power Purchase Agreement adopted</p>	<p><b>Current Portfolio:</b></p> <p>Emergency Recovery Loan (FY 15)</p> <p><b>Pipeline:</b></p> <p>Public Expenditure and Utilities Reform Development Policy Loan Series (2 operations in FY 16 and FY 17)</p> <p><b>Proposed</b></p> <p>Energy Sector Development IPF (FY 18)</p> <p>IFC engagement on transport and utility sector PPPs</p> <p><b>Proposed ASA:</b></p> <p>Serbia Energy sector strategy</p> <p>Energy tariffs reform and impact on the bottom 40</p> <p>IFC investment into wind power projects</p>



**CPF Objective 1d: More efficient public transport companies**

**Intervention logic:**

Large transport sector SOEs structurally underperform due to chronic underfunding, state interference in their management, and a lack of professional management. This poses a serious challenge to the business climate, as poor infrastructure facilities discourage investment and economic activity, which particularly affects opportunities for the large portion of the B40 that live in rural areas and small towns. The government has made the financial sustainability of transport sector SOEs an important element its program and policies. Towards the end of the 2011-2015 CPS key legislative reforms in the transport sector were introduced, and reform plans for the Road and Railway sector SOEs framed and adopted. The comprehensiveness of approach and political commitment provide a unique opportunity to make progress on this most central element of Serbia’s economic reform agenda. The WGB will invest further to support public transport SOE corporatization and financial consolidation. Given the complexity of these reforms, and the cost of implementation, budget or result based financing support will be considered along with advisory support. IFC support on the design and implementation of PPPs and potentially concessions will complement IBRD engagement on corporatization and financial consolidation. In these sectors, a series of DPL or RBF engagement should help remove policy and capacity constraints to effective infrastructure investments, which could be followed in the outer years of the CPF period by specific operations to address remaining issues in the railway and road sectors.

CPF Objective Indicators	Supplementary Progress Indicators	WBG Program
<p>Serbia Railways restructured and cargo company operating without subsidies</p> <p style="padding-left: 40px;">Subsidy to cargo company RSD 10.4 Billion in 2014, and zero in 2019</p> <p>Roads maintained under Performance based maintenance reaches 3000 kilometers</p>	<p>Establishment of autonomous infrastructure, freight and passenger companies</p> <p>Number of traffic units (passenger km + ton km) per staff</p> <p style="padding-left: 40px;">Baseline (2013): 206,500 Target (2017): 290,000</p> <p>Transform Roads of Serbia into autonomous agency with guaranteed budget and accountability for results</p>	<p><b>Current Portfolio:</b></p> <p>Road Rehabilitation Project (FY 13) Corridor X (FY 10)</p> <p><b>Pipeline:</b></p> <p>Public Expenditure and Utilities Reform Development Policy Loan Series (2 operations in FY 16 and FY 17)</p> <p><b>Proposed:</b></p> <p>Transport Sector Governance IPF (FY 19)</p>

<p>Kilometers of roads under performance based maintenance in 2015: 0 Target for 2018: 3000</p>	<p>Milestone: service level agreement signed and in effect by end 2016</p>	<p>IFC engagement on transport and utility sector PPPs, including on waste management in Belgrade IFC ECA Corporate Governance Project</p> <p><b>Ongoing TA:</b></p> <p>CFRR regional EU-REPARIS<sup>7</sup> program, and EQ-FINREP<sup>8</sup> country project IFC ECA Corporate Governance Project Railway Sector TA</p> <p><b>Proposed TA/ASA:</b></p> <p>WBIF western Balkans infrastructure facility Public Investment in Transport</p>
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**CPF Objective 1d: Productive SOE assets transferred to private ownership**

**Intervention Logic:**

The state looms overly large in the Serbian economy and its presence needs to be reduced to create space for private sector-led growth. The continued presence of a large number of ineffective and mostly insolvent commercial SOEs poses a disincentive to potential investors, a serious distortion to the investment climate, and comes at significant cost to the budget. Scarce resources that could be used to attract investment and create jobs are instead diverted to prop up loss making SOEs. These same SOEs cause losses in utilities and transport companies (by not paying bills due) and to the health and social insurance funds (by not paying contributions). Fiscally, the sovereign guarantees required by these SOEs create a vicious cycle of underperformance and fiscal drain. The government has made privatization of commercial a centerpiece of its program and policies. Given the fundamental challenge SOEs in their current form pose to economic growth and inclusion, support to this agenda will be a central element of the WBG lending and analytical program. Budget support instruments to support reforms will be used to support the reform agenda to the extent feasible. This includes the SOE DPL series to complete privatization of commercial SOEs, and Public Expenditure Management DPL or RBF to address

<sup>7</sup> Road to Europe: program of accounting reform and institutional strengthening

<sup>8</sup> Enhancing quality of financial reporting

redundancy issues. Hands on TA and advisory support will continue through the program period, including post-privatization support. This includes advice and support related to increase in number of participants in public works in regions where most of SOEs were located. According to the SOE DPL1 the number of participants in public works will increase from 2,882 in 2013 (1,187 female and 1,695 male) to at least 6,000 in 2015.

CPF Objective Indicators	Supplementary Progress Indicators	WBG Program
<p>Commercial SOEs under the Privatization Agency Privatized</p> <p>Indicators: Number of remaining companies in the PA portfolio</p> <p>Baseline (2015): 526</p> <p>Target (2019): &lt;50</p>	<p>Number of companies under PA portfolio resolved through asset and equity sales: 178 by end 2017 (out of a current total of 526 companies)</p> <p>Number of participants in public works in regions where most of SOEs were located will increase from 2,882 in 2013 (1,187 female and 1,695 male) to at least 6,000 in 2015 (to be monitored by gender).</p> <p>Post privatization support of two SOEs realized through advisory and/or investments</p>	<p><b>Current Portfolio:</b></p> <p>Serbia Public Enterprise Restructuring DPL 1 (FY 15)</p> <p><b>Pipeline:</b></p> <p>Serbia Public Enterprise Restructuring DPL 2 (FY 16)</p> <p>IFC investments and/or advisory services</p>

## FOCUS AREA 2: PRIVATE SECTOR GROWTH AND ECONOMIC INCLUSION

The SCD identified eleven priority areas for actions required to restore growth and make it inclusive and thus progress toward the twin goals. Of these, two are foundational and five are high impact. Focus Area 2 addresses three of the high impact priorities. These priorities directly support the goals of the country's fiscal strategy and economic reform program that focus on creating an enabling environment for investment, including financial sector viability, connectivity, and job creation. This Focus Area 2 thus specifically addresses significant identified constraints to private sector development: investment, financing, connectivity, and labor and property markets inadequacies. Specifically, the objectives and interventions are designed to strengthen competitiveness, stabilizing the banking system, improving land management and infrastructure networks, developing better skills, and reducing barriers and disincentives to labor market entry.

Six CPF Objectives are grouped under this Focus Area:

CPF Objective 2a: Contribute to priority business climate improvements

CPF Objective 2b: Assist in the creation of a more stable and accessible financial sector

CPF Objective 2c: Support the development of more efficient land and property markets

CPF Objective 2d: Enhanced infrastructure networks

CPF Objective 2e: Reduced barriers to labor market participation

CPF Objective 2f: Assist in closing medium and long term skill gaps

### CPF Objective 2a: Contribute to priority business climate improvements

**Intervention Logic:** Creating a competitive business environment together with labor market strengthening will help achieve the fundamental objectives of boosting growth and shared prosperity by generating meaningful employment, including jobs for the B40. As a small, open middle-income economy, Serbia's main path to prosperity is to significantly improve its business climate leading to more successful international integration, especially with Europe, through an increase in investments. The business environment is understood in the broad sense, including the administrative and regulatory barriers that are addressed under 'Doing Business' and BEEPS, but also considering broader issues such as connectivity, trade facilitation and access to finance for SMEs. As a demonstration of its commitment to taking a comprehensive approach to developing a more competitive business climate, the Government recently established a Task Force for coordinating and systematically addressing business climate reforms, headed one of the Deputy Prime Ministers. The WBG will support the government in addressing select aspects of the business climate agenda, under this objective the focus will be placed on paying taxes, trading across borders and insolvency procedures. Some other critical priority areas are addressed under objective 2b and 2c. The main support instrument in these three areas will be IFC advisory support, while the IBRD

financed Competitiveness and Jobs project will support overall government efforts to address regulatory and administrative constraints, facilitate innovation and technology transfer and improve economic participation overall and for the B40 in particular.

CPF Objective Indicators	Supplementary Progress Indicators	WBG Program
<p>Improve <i>Doing Business Distance to Frontier</i> (DTF) DB2015: 62.57; Target DB2019: 72,</p> <p>Special focus on:</p> <p style="padding-left: 40px;">Trading across Borders DTF: baseline DB 2015 – 72.13; Target DB2019 – 85</p> <p style="padding-left: 40px;">Paying taxes DTF: baseline DB2015 – 48.9; target DB2019 - 64</p> <p style="padding-left: 40px;">Resolving insolvency: baseline DB2015 – 57.9 target DB2019 – 74</p>	<p>Trade facilitation - intermediate steps: Improvements of customs information system that would simplify procedures and automate clearances by end 2017</p> <p>Simplification of tax procedures through better usage of on line filing and elimination of redundant processes by 2018.</p> <p>Amendments to the insolvency law and regulations; trainings and awareness campaign for insolvency practitioners, courts and other stakeholders by end 2015</p>	<p><b>Current Portfolio:</b></p> <p>IFC Southeast Europe Regional Tax and Transparency Project (2012-2015)</p> <p><b>Pipeline:</b></p> <p>Serbia Competitiveness and Jobs RBF (FY 16) Second Competitiveness and Jobs Project (FY 20)</p> <p><b>Ongoing TA:</b></p> <p>IFC Western Balkans Agribusiness Competitiveness Program TF funded CFFR Accounting and Auditing project IFC Debt Resolution Project IFC ECA Corporate Governance Project</p>

**CPF Objective 2b: Assist in the creation of a more stable and accessible financial sector**

**Intervention logic:**

A stable, efficient and accessible financial sector is a necessary condition for private sector-led economic growth and shared prosperity. The Banking sector in Serbia is going through a difficult period, some banks were closed down; non-performing loans have increased; and the role of state in the banking sector remains significant. The chronically high rate of NPLs in Serbia increases banks' risk aversion, dampens credit growth, jeopardizes their profitability of and presents a systemic risk for the banking sector.

Improving the regulatory framework for NPL resolution is critical to decreasing the internal risks that the financial system in Serbia is facing. Inadequate insolvency proceedings, weak supervision over insolvency administrators, and lack of technical knowledge among the judiciary all impede the resolution of NPLs in Serbia. As part of the ambitious program adopted by the Government (supported by the IMF), the Government has committed to maintaining financial sector stability through reducing NPLs and debt resolution, strengthening financial sector supervisory institutions and managing effectively the government’s ownership stake in the banking sector. The IMF, as part of its current standby facility is coordinating a working group of IFIs including IFC, EBRD and the World Bank to address the cleanup of the NPL problem in Serbia. The WBG has a broad engagement in financial sector reform, through IFC investments in two state owned banks under privatization, through a support operation to strengthen the Deposit Insurance Agency and through various advisory initiatives on Banking Supervision and Regulation and to address the high ratio of Non-Performing Loans. This engagement will be continued throughout the CPF period, supplemented by a proposed Financial Sector Operation and additional analytical work to address the insolvency issue. The WBG strategy in the financial sector in Serbia also aims to support the return of access to finance for small and medium sized enterprises and individuals. In the context of WBG engagement, IFC will directly support the financial sector through a set of products and instruments: First, IFC will look for opportunities to help will any systemic restructuring and resolution of NPLs in Serbia. IFC began an advisory project in November 2014 with the Government of Serbia to implementing the Debt Resolution Program that is addressing the above-mentioned issues, with primary focus on the legislation that would provide for better debt resolution, allowing for better out-of-court restructuring and sustaining feasible businesses. A component of the advisory work also focuses on the training of judges in foreclosure proceedings. The IFC advisory projects are now being implemented within the Finance and Markets Global Practice.

<b>CPF Objective Indicator</b>	<b>Supplementary Progress Indicators</b>	<b>WBG Program</b>
<p>Reduction of share of Non-Performing Loans (NPLs) in total loans provided</p> <p>Baseline: 22.5 percent (2014) Target: less than 18 percent (in 2019)</p>	<p>Number of state owned banks reduced to a maximum of 3 by end 2018</p> <p>Deposit Insurance Fund replenished and balance sustained</p> <p>Increased debt recovery rate through out of court workouts and insolvency</p> <p>Indicator: proceedings Baseline: 29.2 % (2014) Target: 40% percent (2018)</p>	<p><b>Current Portfolio</b></p> <p>Strengthening Deposit Insurance Agency Project (FY 14) IFC investments in state owned banks SEE Catastrophic Risk Insurance Facility (FY 12)</p> <p><b>Pipeline:</b></p>

<p>Increased availability of enterprise financing coming from banks  Percent of firm financing coming from banks  2013: 15 percent  2019: 29 percent<sup>9</sup></p>	<p>Credit growth exceeds GDP growth from 2018</p>	<p>IFC Western Balkans Debt Resolution Exit Program</p> <p><b>Proposed:</b></p> <p>Financial Sector Project (FY 17)  IFC support to privatization of state owned banks</p> <p><b>Ongoing TA</b></p> <p>Western Balkans Financial Sector TA</p> <p>CFRR regional EU-REPARIS<sup>10</sup> program, and EQ-FINREP<sup>11</sup> country project</p> <p>Technical assistance on non-performing loans  Technical assistance on implementation of deposit insurance and bank resolution framework  IFC banking sector assistance</p> <p><b>Proposed ASA:</b></p> <p>Financial Sector assessment</p>
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<sup>5</sup>BEEPs Survey; 2008 percentage was 29 percent and the goal is to return to the pre-crisis level

<sup>10</sup> Road to Europe: program of accounting reform and institutional strengthening

<sup>11</sup> Enhancing quality of financial reporting

		Strengthening the out of court restructuring and insolvency framework
<b>CPF Objective 2c: Support the development of more efficient land and property markets</b>		
<p><b>Intervention logic:</b>  The regulation and management of land and property markets in Serbia remain below European Standards, creating serious impediments to investments and economic growth. Security of property rights is a crucial building block of successful market economies. Real property itself is a key input to most production and investment processes, as well as a foundation for social stability and people’s well-being. Over the last decade important improvements in Serbia’s land administration, have been made, such as creation of unified register or real estate and real estate rights (supported through the WB-funded Real Estate Cadaster and Registration Project). However, the data on land, ownership, buildings, utility lines, etc., need to be made complete and more easily accessible. Reforming the process of issuing construction permit is critical for enabling investments in land and property, as investors watch the developments in construction permitting as they are related to important indicators such as employment and financing. In this area, it is particularly important to address gender aspects of property registration and records. Women entrepreneurs are particularly affected as properties are almost invariably registered to males, making it extremely difficult for female entrepreneurs to access credit. WBG support under this objective will continue to be provided by the Real Estate Management Project and IFC advisory services.</p>		
<b>CPF Objective Indicator</b>	<b>Supplementary Progress Indicators</b>	<b>WBG Program</b>
<p>Improve <i>Doing Business Distance to Frontier</i> (DTF)</p> <p>Construction Permits DTF: baseline DB2015 – 29.14; target DB2019 - 44</p> <p>Efficiency of property registration system improved.</p> <p>Average number of days to complete recording of</p>	<p>System for electronic issuing of building permit established and applied</p> <p>Rules, procedures, methodologies and information on property registration widely and easily accessible and procedures operate for public to verify their information</p>	<p><b>Current Portfolio</b></p> <p>Real Estate Management Project (FY 15)</p> <p><b>Pipeline</b></p> <p>MIGA Real Estate Development Guarantee</p>



<p>purchase/sale of property in the land administration system</p> <p>2005: 48 2019: 4</p>	<p>Five mobile teams operational in major registration offices to assist people with disabilities; Roma; women in rural areas and others with difficulties accessing land administration services.</p>	
<p><b>CPF Objective 2d: Enhanced infrastructure networks</b></p>		
<p><b>Intervention logic:</b></p> <p>Connectivity is a critical driver of competitiveness, especially considering Serbia’s objective to transform the economy towards export-orientation. Serbia continues to suffer from significant infrastructure gaps, which hinders the country’s ability to attract and retain investments and stifles development opportunities in the rural areas where a large portion of the B40 reside. There is both a need and a large potential for the improvement in the quality of Serbia’s transport infrastructure and services and the in the efficiency of resource use and service delivery. While some of the issues in this area are related to the performance of SOEs (and are addressed directly under CPF Objectives 1c and 1d), there are broader aspects that need attention, such as sector management, physical investments and partnerships with the private sector. Under the CPF, the WBG will continue to pursue two critical ongoing infrastructure projects, Corridor X, and Road Rehabilitation and Safety. The WBG will work to complete the Corridor X highway and to put in place an effective system of managing and maintaining other major national roads. This engagement builds on a long standing dialogue the WBG has had in the transport sector. As regards Corridor X, many sections of the Corridor X motorways south of Belgrade are under construction and are expected to be completed in the next few years with the exception of a 6 km section that was to be funded by the Hellenic Fund. Other than this section, resources have been committed by the Government of Serbia and international financial institutions (IFIs) for the completion of the motorways. This engagement will be complemented by IFC advisory support on PPPs and infrastructure concessions, in roads, airports and other facilities. In addition to road and rail connectivity, the WBG will also support Serbia’s further integration in European energy networks. This will enhance efficiency and reduce cost, and through this helps enhancing EPS financial sustainability and mitigating climate change impact. In addition to an IBRD lending engagement on energy sector governance, IFC will consider support to energy sector diversification to broaden Serbia’s energy mix.</p>		
<p><b>CPF Objective Indicators</b></p>	<p><b>Supplementary Progress Indicators</b></p>	<p><b>WBG Program</b></p>
<p>Corridor X completed</p>	<p>Financing for all Corridor X lots secured by end 2015</p>	<p><b>Current Portfolio:</b> Corridor X (FY 10)</p>

<p>Kilometers to be completed by end 2017: 46</p> <p>Power exchange SEEPEX by Q3 2016 and market coupling 4M MC (Hungarian, Romania, Czech Republic, and Slovakia) by Q2 2017.</p>	<p>Volume of trade in SEEPEX to reach 5 percent of domestic consumption by end 2017.</p>	<p>Road Rehabilitation and Safety Project (FY 13)</p> <p><b>Pipeline:</b></p> <p>Public Expenditure and Utilities Reform DPL series (FY 16 and FY 17)</p> <p><b>Proposed:</b></p> <p>Transport Sector Governance IPF (FY 19) Energy Sector Development IPF (FY 18) IFC PPPs in infrastructure</p> <p><b>Ongoing TA:</b></p> <p>IFC advisory support and financing of PPPs</p> <p><b>Proposed TA/ASA</b></p> <p>Serbia Energy sector strategy Public Investment Management Energy tariffs reform and impact on the Bottom 40</p>
<p><b>CPF Objective 2e: Reduced barriers to labor market participation</b></p>		
<p><b>Intervention logic:</b></p> <p>More than 60 percent of the adult population in Serbia is not employed, and even fewer are formally employed. Not surprisingly, this group of people constitutes the majority of the B40, and the lack of labor income is the key constraint to lifting them out of poverty.</p>		

They consist mostly of two groups: (i) the (pre-) transition generation; and (ii) certain groups, especially minorities like Roma, but also women and youth, who have never been strongly attached to the labor market. Bringing these people into the labor market is the most critical element of enhancing shared prosperity in Serbia. It would also bring a significant growth impulse to the Serbian economy. Progress on this agenda requires labor market reforms as well as removing obstacles to investment in the non-tradable sector and micro and small enterprises. The first priority in labor market reform is revising the minimum social security contribution. The current design of contributions puts a high burden on low wage earners, especially for part-time work. In addition, there is further need for reform in the design of social benefits, as a number of benefits come with considerable disincentives for formal work. Combined, these reforms should be the crucial first step to unlock the potential of a new segment in the Serbian labor market and should help the 40+ generation into work, but also excluded groups like Roma and, importantly, women. For the latter, additional measures, like providing care facilities for children and elderly, and closing skill gaps might be necessary. Importantly, institutions like the National Employment Service and the active labor market programs (ALMPs) it provides need to be considerably strengthened. The focus needs to be on ensuring efficient match-making between job seekers and employers, and on providing high quality services to beneficiaries and employers. The WBG interventions in this area will explicitly focus on disadvantaged groups in the labor market, in particular the transition generation, women, youth, workers released by SOEs, and Roma. The social pillar of the SOE DPL series, and the Competitiveness and Jobs RBF will be the main instruments to support the labor market reform agenda. The WBG program will also continue to work on strengthening Serbia's innovation and technology transfer systems as a way to enhance labor market opportunities in the long term, in particular for youth.

CPF Objective Indicators	Supplementary Progress Indicators	WBG Program
<p>Social Security contribution system rationalized to incentivize part time and low wage employment</p> <p>Percentage of total formal employment in part time work 2014 (Q3): 106,000 (Source: LFS) 2019 (Q3): 150,000 (Source: LFS)</p>	<p>Legislation passed to reform Social Security system</p> <p>Reduced tax wedge for low-wage earners</p> <p>Indicator: Tax wedge on income from half-time job at minimum wage for single earner with no children reduced from 44.6 percent (2015) to 37.1 percent or lower by 2019</p> <p>Number of new jobs sustained through IFC's investments and advisory: 2,500</p>	<p><b>Current portfolio:</b> Serbia Public Enterprise Restructuring DPL 1 (FY 15)</p> <p><b>Pipeline:</b> Serbia Public Enterprise Restructuring DPL 2 (FY 16) Serbia Competitiveness and Jobs RBF (FY 16) Second Competitiveness and Jobs Project (FY 20)</p> <p><b>Proposed:</b></p>

<p>NES services enhanced:</p> <p>Performance indicators:</p> <p>Number of active job seekers per case worker:</p> <p>2014: 1,238 (registered unemployed)</p> <p>2019: 800 (active job seekers)</p> <p>Increased number of registered unemployed who found a formal job<sup>12</sup></p> <p>Baseline: 232,280 (2014)</p> <p>Of which:</p> <p>Male: 109,789</p> <p>Female: 122,491</p> <p>Increased number of registered unemployed women who found formal job</p> <p>Baseline: 122,491 (2014)</p>	<p>Number of Certified Case managers reaches 600</p>	<p>IFC's financing and advisory services</p> <p><b>Ongoing TA</b></p> <p>Western Balkans Jobs TA</p> <p><b>Proposed TA and ASA:</b></p> <p>Skills, employment and labor markets</p> <p>Strengthening ICT sector for investments and jobs</p>
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<sup>12</sup> On all the below targets an increase in numbers is expected, and targets will be identified in the course of the already initiated work on enhancing the capacity of the NES

<p>Increased number of registered unemployed youth (15-24) who found formal job:</p> <p>Baseline:  Male: 19,100 (2014)  Female: 22,498 (2014)</p> <p>Increased number of registered unemployed Roma who found formal job:</p> <p>Baseline:  Male: 959 (2014)  Female: 633 (2014)</p>		
<p><b>CPF Objective 2f: Assist in closing medium and long term skill gaps</b></p>		
<p><b>Intervention logic:</b></p> <p>Closing skill gaps is an important element of Serbia’s economic transformation agenda. While in the short term skill supply is not a critical constraint to investment and economic development, any uptick in demand will generate skill shortages in sectors that are potential drivers of growth. While in the medium term this skill gap can be closed by reforming and enhancing vocational education and training programs, the best long term investment strategy for Serbia is to improve the access and quality of Early Childhood Education, which, while mandatory, only sees participation of a fraction of poor and disadvantaged households. The latter would also have a positive impact on female labor market participation as universal Early Childhood Education would make it easier for women to seek employment, especially for women in single female headed households. A comprehensive approach including both elements of the skill enhancement agenda needs to be put in place.</p> <p>The proposed Skills Project will help address medium- and long-term constraints to inclusion and productivity. Continued engagement through programmatic TA and ESW on skills, labor market regulation, and TA on Gender and Roma will support government in policy and instrument design. Continued engagement through programmatic TA and ESW on skills and TA on Gender and Roma will support government in policy and instrument design.</p>		
<p><b>CPF Objective Indicators</b></p>	<p><b>Supplementary Progress Indicators</b></p>	<p><b>WBG Program</b></p>

<p>By 2019, 98 percent of all children attend pre-school education at age 6 <sup>13</sup></p> <p>Baseline: 92 percent (school year 2012/13)</p> <p>Target: 98 percent (2019)</p>	<p>Body for accreditation of preschool institutions and programs established</p>	<p><b>Ongoing:</b></p> <p>Serbia Innovation Project (IPA financed, FY 12)</p> <p>Serbia Technology Transfer Project (IPA financed FY 15)</p> <p><b>Proposed:</b></p> <p>Skills and Inclusive Education Project (FY 17)</p> <p><b>Ongoing TA</b></p> <p>Step skill survey</p> <p>Western Balkans Roma TA, including adolescent girls initiative</p> <p><b>Proposed TA:</b></p> <p>Skills, employment and labor markets</p> <p>Educational Regional AAA</p>
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<sup>13</sup> Currently no gender disaggregated data are available for this indicator, but such data will be collected in the course of the WBG engagement and introduced at the mid-term CPF PL

## ANNEX 2: FY12-FY15 CPS COMPLETION AND LEARNING REPORT

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<b>CPS Board Discussion:</b>	November 15, 2011
<b>CPS Progress Report (Board Presentation)</b>	August 25, 2014
<b>Period Covered by CPS Completion Report:</b>	November 2011 – June 2015

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### INTRODUCTION

1. **This Country Partnership Strategy Completion and Learning Report (CPSCLR) reviews the experience of implementing the FY12–15 World Bank Group Country Partnership Strategy (CPS) for the Republic of Serbia (Report No. 65379-YF, November 15, 2011).** The document provides a self-assessment of: (i) the extent to which the CPS was successful in achieving its stated objectives; (ii) the WGB performance in terms of the design and implementation of the program; (iii) the CPS contribution to the Corporate Twin Goals of eliminating poverty and boosting shared prosperity of the bottom forty percent of the population; and (iv) lessons learned from the implementation of the CPS program that should be considered during the preparation of the new Country Partnership Framework FY16-20. In addition to discussions with the country team and Government counterparts, this assessment is based on reference documents such as the CPS, the CPS Progress Report, Project Appraisal Documents, Implementation Status Reports, ICRs, supervision reports, and reports related to Economic and Sector Work. The findings of the CPSCLR have informed the preparation of the FY16-FY20 CPF.

### I. SUMMARY OF KEY FINDINGS AND RATINGS

2. **The objective of the FY12-15 CPS was to support Serbia’s EU accession and help the Government strengthen competitiveness and improve the efficiency and outcomes of social spending.** The CPS was implemented in the context of severely constrained budgets and political instability, and both of these had limiting effects on achieving the CPS objectives. Serbia’s macro-fiscal sustainability has deteriorated over the program period. Political indecisiveness and the adoption of policies playing to specific voter group interests in the first years of the program period, combined with a stalemate on structural economic reforms aggravated an already dire fiscal situation. While greater political stability in the latter half of the program period halted to some extent expansionary policies, entitlements gained have proven hard to roll back, meaning that even under a status quo scenario debt levels will continue to rise. Debt is projected to rise to over 70 percent of GDP by the middle of 2015.

3. **The CPS program contributed to achievement of positive development outcomes in the areas of competitiveness, social spending, and environmental sustainability.** Supporting Serbia’s EU accession aspirations was the overarching theme of the CPS. The CPS program focused on two Pillars of engagement: (i) strengthening competitiveness; and (ii) improving efficiency and outcomes of social spending. In addition, a commitment was made to continue to support environmental sustainability through two operations carried over from the previous CPS.

The CPS contribution to specific development outcomes in these three areas of engagement are summarized in Attachment 1. Contributions to these outcomes came from a combination of interventions carried forward from the FY08-11 CPS, from new operations especially in the final two years of the program, and from a substantial analytical work and non-lending technical assistance. Attachment 2, Tables 2, 2a and 3 provide a breakdown of planned and actual operations and knowledge and advisory activities for the FY12-15 CPS respectively.

4. **The CPS Overall Development Outcome is rated Moderately Satisfactory.** This rating is based on: (i) an aggregate and comprehensive assessment of the achievements in each of the three results areas and the individual outcomes which formed the basis of the CPS Results Framework (Attachment 1); (ii) the contribution of the CPS to the objective of supporting Serbia's EU accession; and (iii) the support provided in response to the 2014 floods.

5. **Progress against the development outcomes under the Strengthening Competitiveness Pillar is rated Moderately Satisfactory.** Of the 12 outcomes under this pillar, 8 were achieved, 2 mostly achieved, and 2 partially achieved. The program has made important development contributions on a broad array of issues affecting competitiveness. A critical focus of the program was on supporting the government in its efforts to move away from a state-led economic model to a private sector driven model based on inward and external investments. Around this over-arching objective, support has focused on closing critical infrastructure gaps, improving management of transport sector institutions, unlocking innovation and technology transfer potential, financial sector strengthening, investment climate improvement, judicial sector reform, improved efficiency in agriculture, and enhanced water management. Support in all these areas has been underpinned by lending and advisory support using IBRD, IFC and MIGA instruments.

6. **While good progress was made on the infrastructure elements of the program, socially and politically sensitive reforms such as privatizing and closing loss-making SOEs, have taken a long time to gain ownership.** Apart from the protracted consensus building process around public and socially owned enterprises reforms, the World Bank Group efforts to provide support were hampered by a weak macro-fiscal situation, and the suspension of the IMF program, which ruled out the provision of budget support for most of the CPS period. Irrespective of this, significant progress was made on this most sensitive, but critical, element of the program towards the end of the CPS period. The momentum generated by the now revived enterprise privatization and resolution process creates further opportunities for addressing corporate governance and sustainability issues for those strategic enterprises that will remain in state hands, including energy sector utilities, the railways, etc. SOE reform and resolution will also be a critical factor in leveling the playing field and bringing in much needed investment.

7. **Progress against the development outcomes under the Improving Efficiency and Outcomes in Social Spending Pillar is also rated Moderately Satisfactory.** Of the 8 outcomes under this pillar, 5 were achieved, 1 mostly achieved, 1 partially achieved, and 1 not achieved. The program provided lending and high end advisory support throughout the CPS period, focusing initially on all aspects of social expenditure. Towards the end of the program, a deepened focus on the health sector was opted for, given the commitment of the counterparts to pursue reforms in this sector.



8. **The third result area, engagement on environmental sustainability, is rated Moderately Unsatisfactory.** This is reflecting strong performance in improving energy efficiency (where the one outcome was achieved) but weak performance on addressing environmental legacy issues (where the one outcome was not achieved). In the latter area, resistance from vested interest effectively blocked implementation of the single project in the portfolio that focuses on environmental legacy issues. The Project was subsequently cancelled in February 2015.

9. **The CPS program effectively supported the EU accession process.** While not reflected in specific outcomes in the Results Framework, the WBG successfully provided extensive support to the EU accession process, both through direct engagement in administering and supporting IPA-financed programs and a largely EU-financed Multi Donor Trust Fund in the justice area, and by providing other advisory support relevant to EU accession objectives.

10. **Finally, a significant part of program resources was allocated to the response to the 2014 flood emergency.** The Bank demonstrated flexibility and responsiveness, and provided strong and catalytic support to assess and address damages and mitigate risks arising from the catastrophic floods that hit the country in May 2014. USD 300 million was allocated to support Serbia in meeting critical needs in the energy and agriculture sectors, repairing damaged flood control infrastructure, and helping the country better respond to natural disasters. So far USD 103.7 million were disbursed. This operation in particular helped to mitigate potential risks to economic development from energy shortages (having in mind that the work of the main power generation plant was endangered) and the destruction of farmer livelihoods expanded on even greater area than originally affected. In addition, the bank shifted resources within the existing undisbursed portfolio to meet immediate recovery needs, beginning with prioritizing under the USD 100 million Road Rehabilitation and Safety Project to finance recovery of heavily damaged road sections and purchase of ambulance vehicles, portable ECG and ultrasound equipment from the remaining USD 2.7 million of the Delivery of Improved Local Services Project. While not expressed in formal result indicators, this was a critical additional program achievement to be taken into account in program assessment.

11. **The overall rating of the WBG performance is Good.** The World Bank Group made a strong contribution to the pursuit of CPS objectives, the majority of which were either achieved or mostly achieved. Given the political difficulties encountered during the first half of the CPS period, and the challenges posed by the economic crisis and the flood emergency, this is a strong result, reflecting commitment and flexibility. The work during the CPS period was based on a strong analytical underpinning, as well as reliance on the new Bank's instruments where traditional budget support instruments could not be used. The WBG developed good cooperation with the Government and other donor and international organizations, and its knowledge products (including but not limited to Public Expenditure Review; Country Economic Memorandum etc) were highly relevant and often formed the basis for the design of reforms and their support by other development partners.

12. **The CPS design and quality at entry was Good.** The CPS objectives were well aligned with the Serbia's government development priorities. The assessment on which the CPS was based remained relevant throughout the implementation period. However, it should be noted that the original CPS Results Framework was overly complex and at times not measurable. The WBG took

full advantage of the Progress Report to amend and simplify the Results Framework and bring it more closely into line with the objectives of the CPS.

13. **Although the CPS preceded the articulation of the Corporate Twin Goals, the WBG engagement in Serbia over the CPS period was closely aligned with the Twin Goals of eliminating poverty and boosting shared prosperity.** Both CPS pillars address these goals. **Competitiveness** is central to eliminating poverty and promoting shared prosperity. In a country where a large portion of the bottom forty percent live in rural areas, the outcomes related to infrastructure connectivity and agricultural modernization are of particular relevance. Other outcome areas of direct relevance to boosting shared prosperity are those related the Innovation Fund and the creation of the Climate Risk Insurance Facility, which mitigates potential climate related risks to farmers. Improving social services is of particular relevance to reducing poverty and boosting shared prosperity. The emphasis on the access of Roma children to health care, improvements in the operation of the Disability Fund and improved performance of health sector institutions all have a direct impact on the opportunities of poor and vulnerable groups to build assets and escape poverty.

14. Moreover, in setting its Corporate Goals, the WBG further urged that **the two goals should be pursued in ways that sustainably secure the future of the planet and its resources, promote social inclusion, and limit the economic burdens that future generations inherit.** The cross-cutting CPS area of addressing environmental legacy and sustainability further links the CPS to the corporate goals.

15. **There are a number of critical lessons from the FY12-15 CPS to be applied to the FY16-20CPF.** These include the importance of aligning the WBG program with the objectives of the government and of key partners, the need to combine a long-haul engagement with flexibility and adaptability, the pivotal role of NLTA and knowledge products in overcoming resistance to difficult reforms, the importance of focusing on a small number of outcomes that can be effectively monitored, and the need to enhance partnership with the EU, including through joint financing initiatives.

## II. HIGHLIGHTS OF ASSESSMENT OF DEVELOPMENT OUTCOME

16. **During the CPS period IBRD delivered US\$ 784 million in new loans, of which US\$ 690 million was Investment Project Financing and US\$ 100 million budget support. During the CPS, IFC financed \$682 million in 16 projects, US\$ 610 million for its own account (\$519 disbursed) and US\$72 million through mobilization from the commercial banks.** In addition, IFC has financed three regional projects, with a Serbia component, for a total of \$120 million allocated for those purposes (these regional projects include financing for: a construction material company, investment fund focused on MSMEs, and an insurance company) covering between three and five countries mainly from the Southeastern Europe, with option to expand the coverage going forward.

17. **During the period of the CPS, the Government of Serbia has been pursuing an overarching country goal of integration into the EU, focused on three contributing clusters**

**of objectives: enhanced competitiveness, efficient and effective social service delivery, and environmental and social sustainability.** The three clusters were broken down in ten strategic goals: (i) closing critical infrastructure gaps; (ii) strengthened irrigation systems and institutional framework to support increased agricultural production; (iii) improved investment climate; (iv) stimulate and harness innovation capacity; (v) strengthened banking system; (vi) strengthened fiscal performance; (vii) sustained improvement in human development outcomes; (viii) more informed and effective policymaking to reduce poverty and increase social cohesion and equality; (ix) address environmental legacy issues; and, (x) enhanced energy efficiency. Further details on progress toward achieving country-level goals are provided in Attachment 3.

**18. The three result areas of the CPS are closely aligned with the country's priorities, and specifically address the strategic government's goals as specified in the CPS.** The 22 outcomes in the CPS Results Framework directly reflect these goals (the new growth model; fiscal discipline and EU integration), and are logically linked to the country's priorities. Of these 22 outcomes, 14 (63%) were achieved, 3 (14%) were mostly achieved, 3 (14%) were partially achieved, and 2 (9%) were not achieved. This performance, coupled with the CPS contribution to Serbia's accession and the WBG quick response to the flood lead to an overall rating of Moderately Satisfactory.

### **Pillar I. Strengthening Competitiveness**

**19. Serbia's weak macro-economic performance affected the achievement of the program in this pillar.** Macroeconomic performance was driven by the fall out of the Eurozone economic crisis and by an insufficiently firm response to this crisis in the early part of the CPS period. Weak macro-economic performance affected the program in two main ways. In direct terms, the inability to provide budget support made it impossible to use development policy lending as potentially the most effective instrument the Bank Group has at its disposal to support macro-fiscal reforms and competitiveness. Related to this, the imperative for the government to take corrective measures reduced the political space for measures that would boost competitiveness, but would impose social cost in the short term. In indirect terms, the resource constraints caused by the fiscal crisis narrowed the space for investment in measures and program that could positively affect competitiveness.

**20. Regardless of these fundamental constraints, the CPS contributed to strengthening competitiveness and improving the business environment in Serbia.** This was achieved through investment and policy support to reforms in the financial sector, in enterprise development, land administration, infrastructure development, judicial services, and, most critically, in addressing the long unresolved public and social enterprises reform agenda. In relation to the State and Socially owned Enterprise agenda, policy dialogue and advisory support were pursued over a 2.5 year period, resulting in: a) a strengthened legal framework for public enterprise management, privatization and bankruptcy; b) the initiation of a phased resolution process for the 502 enterprises that remained in the portfolio of the Privatization Agency; and c) the development of restructuring programs for critical large utilities and transport enterprises. Throughout this period, the Government relied heavily on technical inputs and advice from the World Bank Group. Despite the delay in the provision of budget support, for macro-fiscal reason, tangible progress was made on this agenda. Outcomes in this area of strengthening competitiveness and improving the business environment have been partially achieved.

21. **In the financial sector, the WBG helped create a stable and orderly process in which complex issues facing the banking system could be addressed.** This was achieved through a combination of result-based investment lending to strengthen the Deposit Insurance Agency (DIA), strategic investments in two major public banks by IFC, and intensive dialogue on core aspects of financial sector and banking reforms throughout the CPS period (including NPL resolution, state owned bank reform, banking supervision and resolution frameworks). These measures aimed at strengthening the DIA and domestic banks will, over time, help restore credit growth and support economic activity. Outcomes related to this area of engagement have been partially achieved.

22. **On enterprise development, IFC investments and advisory support to agribusiness and other firms helped these enterprises weather economic adversity.** While success has been mixed, the continued presence of IFC in major enterprises in Serbia serves as a signal to other potentially interested investors. Through its portfolio clients, IFC provides about 12,000 direct jobs (out of which more than 2000 female jobs), reaches up to 63,000 farmers and provides 48,000 loans to SMEs.

23. The IPA-financed Innovation Fund and Technology Transfer facilities, administered by the World Bank Group, helped creating entrepreneurial opportunities for technology-driven innovators. While this initiative needs scaling up for it to have an impact on economic activity, it has succeeded in giving a boost to emerging entrepreneurs. Outcomes related to this engagement have been achieved.

24. The Real Estate Management Project was approved only towards the end of the CPS period. However, it was preceded by an **in-depth Technical Assistance engagement on land and real estate management, which helped in mapping all relevant sector issues and informs the design of the project.** The technical assistance and advisory engagement also helped frame the World Bank Group's input to the drafting process of the law on Constructing Permitting and Planning, which is set to address the area in which Serbia lags most on investment climate related indicators. Outcomes related to this engagement have been partially achieved.

25. **Regarding the closure of critical infrastructure gaps, the Corridor X and Road Rehabilitation projects are implemented in close coordination and partnership with other IFIs,** and provide an integrated response to the government's strategic objective of enhancing Serbia's position as a trade and transit country. While coordination and logistical issues stifled implementation in the early phase of the CPS period, performance improved markedly in the last two years, raising the possibility that Corridor X will be completed by end 2016 and critical road rehabilitation works will be completed shortly after. Both projects have also created basis to enhancing road sector management. Finally, analytical and advisory engagement on railway sector reform has resulted in an [endorsed] road map for reform of the state railway company, the performance of which both holds back Serbia's export potential and its role as a transit and trade up in Southeastern Europe. Outcomes related to these engagements have been achieved.

26. **Engagement on judicial system reform, through the Bank-administered Multi-Donor Trust Fund, has resulted in an in-depth assessment of judicial service performance,** which

has established a broadly agreed benchmark based on which progress will be measured by both the EU and the government. This should help resolve the significant bottlenecks in contract enforcement currently posed by a poorly performing judiciary. Most of the outcomes related to this engagement have been achieved.

## **Pillar II. Improving Efficiency and Effectiveness of Social Spending**

**27. Lending engagements in this area have been limited to two operations, both of which aimed to address inefficiencies in social sector management and finance critical investment.**

The first operation, Strengthening Local Service Delivery project (DILS) focused on addressing weaknesses in sector financing frameworks in health, education and social protection.

**28. The second Health Project drills down on issues identified during DILS implementation** and add further dimensions, such as an in-depth engagement on centralized procurement of pharmaceuticals, which is considered exemplary in the ECA region. Hence, while engagement has been focused, it has been well targeted and addressed core issues in social sector financing and service delivery. Some of the aspects of sector financing supported through DILS and related analytical work remain to be fully implemented. Hence, outcomes in this area are partially achieved.

**29. The deepened engagement in the health sector was completed by support to broader transparency and equity reforms in the public sector wage and employment system.** With a very difficult fiscal situation throughout the CPF period, which negatively affected income growth of the bottom forty percent of the population, efficiency gains in social expenditure were critical to ensure continued access to basic services by the lower percentile income groups. An EU IPA financed engagement on developing SILC household surveys will provide an improved basis for tracking the impact of social expenditures in future years.

**30. Engagement in this pillar of the CPS was underpinned by a rich array of analytical and advisory work,** including; a) support to poverty assessments and the IPA financed support to undertaking the first two SILC surveys; b) in-depth work on Roma inclusion in education and health service provision; c) a social accountability engagement, and; d) work on public sector wages and municipal finances. As a result, government is equipped with better tools to understand and diagnose poverty dynamics, assess the appropriateness and design of policies to foster inclusion of the Roma population, and has been able to design a comprehensive program of reform in public sector employment and wage bill management. The analytical work on municipal finance will feed into ongoing reforms of municipal financing frameworks. Most of the outcomes of the analytical engagement on this pillar of the CPS have been achieved.

## **Cross cutting area: addressing environmental legacy and sustainability**

**31. Program performance on this cross-cutting area has been mixed.** Attempts to address environmental legacy issues in the area around the RTB Bor copper mine and smelter have not generated results, due to resistance from vested interests and insufficient commitment by government counterparts to implement the remaining elements of the program. On this aspect of

the program the outcome was not achieved.

32. **Regarding energy efficiency, the first energy efficiency project closed in FY 14 and achieved majority of its objectives.** This project had a powerful impact setting an example in showing that energy efficiency reforms can work in Serbia, regardless of widespread skepticism. Unfortunately a follow up project was not taken forward due to fiscal constraints. However, objectives related to the first project were achieved.

### Accession to the European Union

33. **Serbia made significant progress towards EU membership in the program period.** The Stabilization and Association Agreement entered into force on September 1, 2013, and EU membership negotiations were initiated on 21 January 2014. Historically the speed of Serbia's EU accession progress has often been dependent on political factors. However, as membership negotiations progress, economic governance and the strength of institutions will gain growing importance.

34. **The World Bank Group has provided advisory and implementation support to the Government on key aspects of the European Integration agenda throughout the CPS period.** This included work on issues of economic governance, social inclusion, competitiveness and innovation and legal and judicial reform. On innovation and technology transfer and legal and judicial reform the Bank has in addition administered IPA-financed projects. On legal and judicial reform in particular, the conduct of a broad functional review of the judicial system and performance helped in defining objective benchmarks for the EU accession negotiation process.

### Emergency Response and Flood Protection

35. While not a CPS objective, **the World Bank Group response to the 2014 flood emergency absorbed USD 300 million (about a quarter of the lending envelope), supporting critical mitigating measures in the energy, agriculture and water management sectors.** The rapid response by the Bank helped formulate a comprehensive support program in time for the 2014-2015 winter season that reduced risks of vulnerable groups lacking access to electricity for heating and supported small and medium size farmers affected by the floods. Engagement on flood protection follows on from the Irrigation and Drainage project, which closed in 2014, and which financed critical flood protection works throughout Serbia, but in particular on the Danube and Sava rivers. The performance of these protection works prevented damage from flooding in the areas covered during the 2014 floods. The outcomes related to this project were achieved.

## III. WORLD BANK GROUP PERFORMANCE

36. **The overall rating of WBG performance is Good.** The World Bank Group made a strong contribution to the pursuit of CPS objectives, the majority of which were either mostly or partially achieved. Given the political difficulties encountered during the first half of the CPS period, and

the challenges posed by the economic crisis and the flood emergency, this is a strong result. The work during the CPS period showed a strong knowledge-based engagement, as well as adaptability where traditional budget support instruments could not be used.

**The FY 14 Serbia Country Opinion Survey findings demonstrate that the World Bank Group is highly valued for much of the work that it does in the country.** Stakeholders believe that there is great opportunity for the WBG in supporting priority areas and Serbia's institutions through investment and capacity building. While collaboration with the Government is regarded as very strong, greater engagement with citizens emerges as a critical area for strengthening WBG's work on the ground. The survey findings show that those stakeholders who are more familiar with the WBG's work and who collaborate with the WBG, nearly across the board, have significantly more positive ratings than those who do not collaborate with the WBG.

37. **The CPS quality at entry was good,** but some weaknesses, in particular in the Results Framework, are worth noting and considering in the next CPF. The analytical assessment on which the CPS was based remained relevant throughout the implementation period. Objectives were well aligned with the country's development priorities, with more than half of the monitored outcomes falling under the Government's enhancing competitiveness objective. Strong support was also provided to the EU accession process, both through direct engagement in administering and supporting IPA-financed programs, and by providing advisory support relevant to EU accession objectives.

38. **The CPS design was characterized by continuity, flexibility, complementarity and synergy within the lending program and between the lending and non-lending elements.** The WBG coordinated planned interventions with development partners, in particular the EU, other IFIs and the IMF.

39. **The program continued to move toward greater selectivity related to sectors of engagement and portfolio consolidation, while using a broad spectrum of instruments.** Selectivity in terms of sectors in which the Bank provides support was driven largely by client demand, the WBG's comparative advantage, and exposure limits. Closure or restructuring of some of projects helped the consolidation of portfolio in order to focus on a smaller number of projects. Given the fiscal challenges, legacy issues and absorption capacity Serbia is facing, a greater use was made of Result-Based Financing instruments in the second half of the CPS period (as it was the case with the DIA project), which might continue going forward. The potential for using budget support remains considerable, especially if the implementation of the fiscal consolidation program is successful. A closer partnership with the EU has evolved around issues of economic governance, including through World Bank administered IPA initiatives and through parallel financing of programs and reform efforts.

40. **The CPS results framework had some weaknesses.** While it captured the gist of the Bank's program, the results framework contained too many indicators and outcomes, not all observable. Data shortages were not sufficiently considered as potential risks. Some indicators were difficult to monitor, because the client did not have the capacity to provide the data. The WBG took steps to correct these weaknesses in the CPS Progress Report.

41. **While important country-level risks were identified and addressed, the CPS did not discuss risks to the WBG program.** The strategy document noted risks such as the Eurozone crisis, continued fiscal pressures, and delayed reforms. CPS interventions successfully mitigated the risk of financial instability exacerbated by the Eurozone crisis and contributed the efforts to reduce unemployment. In retrospect, the main challenges to the program were: (a) the introduction of budget ceilings, which affected the speed of project implementation and disbursements; (b) political instability; (c) implementing agencies' capacity constraints, which led to slower than expected start up and implementation of some projects; and (d) in the case of infrastructure projects, issues such as land acquisition and availability of qualified contractors. While these challenges caused implementation delays, most projects achieved their development objectives or are on track to do so. The WBG program was concentrated in areas of strong client commitment well aligned with Government priorities, which helped mitigate the risks to WBG-supported operations.

42. **Quality of implementation was Good.** Close follow up and implementation support helped overcome engrained program delivery issues that complicated delivery in the early years of the CPS period. Delays in implementation and delivery occurred primarily in the first half of the CPS period, and were caused mainly by frequent changes in counterparts, protracted government formation processes after elections, and the going off track of the IMF program in early 2012. These delays were largely eliminated after the formation of a more stable coalition government in late 2012, with the number of projects in problem status reduced to one by early 2014, and lending delivery reaching projected amounts for the CPS period. To facilitate implementation, all projects were assigned a contact person in the local office, and some projects had field based Task Team Leaders. This close and continuous portfolio management resulted in adjustments to lessons of experience and evolving needs; except for the most recent approvals, every project in the Bank's portfolio was restructured at least once.

43. **The CPS reflected a partnership between the World Bank and IFC,** set out in a Joint Business Plan for Serbia.

44. **The Bank tailored its support in response to changing circumstances.** Just-in-time support was effective in dealing with new challenges and provided timely assistance to the Government while also contributing to achievement of most outcomes. The Bank has been able to offer the Government high-quality development solutions while rapidly preparing new lending operations in response to changed circumstances. The Bank was also able to adapt its instruments to evolving conditions, especially when budget support operations could not be used due to macro-fiscal performance. Finally the Bank demonstrated flexibility and responsiveness to flood emergency in Serbia. The Bank team participated in the post disaster needs assessment, and the Bank approved US\$300 million ERL to assist in mitigating the impact of the floods.

45. **Coordination with development partners was continuous and effective.** As a middle income EU candidate country, Serbia has a relatively small number of active development partners, with most bilateral donors cutting back on their presence over time. Donor coordination is managed by the Government through the Ministry of Finance (loan financing) and Office for European Integration (SEIO). The World Bank team maintained regular contact with these coordinating bodies and actively participated in development partner coordination/information



sharing events, including as part of the new CPS preparation. Regular consultations with the IMF, with other IFIs and with the EU are also held. The World Bank also works effectively with the UN Country Team.

#### IV. ALIGNMENT WITH WBG CORPORATE GOALS

46. **Although the CPS precedes the articulation of the WBG Twin Goals of ending poverty and promoting shared prosperity, it was well aligned with these goals.** Economic growth, particularly one that promotes private sector-led job creation and employment opportunities for broad segments of the population, is necessary for reducing poverty and boosting shared prosperity in a sustainable manner in Serbia.

47. **The Country Economic Memorandum that was delivered early in the CPS period highlights the importance of transforming Serbia’s economic development model towards a private-sector drive and export orientated approach.** The SCD that was completed in parallel to this report draws further conclusions on how shared prosperity can be boosted in Serbia, and highlights the importance of increase in employment in that context. Formal employment is the single most important driver of income growth and asset building for the bottom 40 percent. Hence the critical questions for Serbia are how to achieve sustainable growth and how to ensure that this growth translates into greater economic participation, through jobs creation.

48. **Given Serbia’s poverty profile, where a large portion (36 percent) of the bottom forty percent live in rural areas, the outcomes related to infrastructure connectivity and agricultural modernization are of particular relevance.** Connections to transport corridors enhance opportunities for rural economic development and enhanced agricultural resilience and improved agricultural yields have a direct positive impact on rural poverty reduction. In both these areas outcomes have either been partially or fully achieved. Other outcome areas of direct relevance to boosting shared prosperity are the opportunities created for young entrepreneurs through the Innovation Fund and the creation of the Climate Risk Insurance Facility, which mitigates potential climate related risks to farmers.

49. **The outcomes pursued under the second CPS pillar are of particular relevance to reducing poverty and boosting shared prosperity.** The emphasis on the access of Roma children to health care, improvements in the operation of the Disability Fund and improved performance of health sector institutions all have a direct impact on the opportunities of poor and vulnerable groups to build assets and escape poverty.

#### V. LESSONS AND SUGGESTIONS FOR FY16-20 CPF

50. **The Bank remains a partner of choice for the Government in carrying out complex reforms, as shown by the analysis of the implementation of the FY12-15 CPS and the FY14 Country Opinion Survey finds that the World Bank Group is highly valued in much of the work that it does in the country.** The Bank must build on the experience of this partnership and continue to engage with the Government in focusing on the areas where it can have the greatest leverage pursuing its goals of reducing poverty and sharing prosperity. The Country Opinion

Survey also emphasizes public sector governance and growth related areas such as private sector development and jobs creation, employment, and capacity building as top development priorities in the country on which the World Bank can have a substantial contribution.

51. **The lessons learned from the Serbia FY11-FY15 CPS echo many of the lessons learned in recent CAS/CPS completion reports of other countries**, such as Albania, FYR Macedonia, and Georgia. The importance of: alignment with the country's priorities; continuing dialogue and partnership with counterparts and partners; flexibility and responsiveness as circumstances change; clear focus on limited number of priorities; and the value of knowledge products are generally reflected in all of these reports.

52. **The following key lessons should be taken into account in the design of the FY16-20 CPF.**

- **Close alignment with Government objectives, and those of key partners, was important to the success of the WBG program.** Alignment of CPS strategic goals with the EU regional strategy provided a basis for successful WBG interaction with the EU, particularly on the improvement of IPA funds absorption, and also strengthened link with other development partners.
- **The WBG should maintain its strategic focus on assisting the government in getting growth back on track and ensuring that opportunities for the less well-off are enhanced.** The Bank has been at the forefront of dialogue on resolving economic legacy and transition issues and enhancing competitiveness. The long and consistent engagement over time has paid off, as government has initiated critical reforms that should help break the cycle of spiraling debt and weak investment. As this process progresses, continued attention needs to be devoted to creating opportunities for the bottom forty percent, and in particular for marginalized and vulnerable groups. Government has shown a strong awareness of this issue in the way it has designed the fiscal consolidation program, and is considering measures to better target social protection programs as well as active labor market policies. A continued engagement on resolving structural impediments to growth, job creation and competitiveness and targeting social assistance is therefore essential.
- **The complex economic problems of Serbia require a long haul engagement.** The WBG's approach of thinking in terms of project cycles is not well adapted to the complexity and longevity of issues that Serbia faces. Addressing complex and socially painful legacy reforms requires a long upfront engagement in dialogue and support, for which the Bank's focus on rapid delivery of lending operations is ill-suited. The use of NLTA facilities has helped, in part, overcoming this challenge, but with declining budgets for analytical work the sustainability of this model is in doubt, yet it is essential to building a meaningful partnership with countries such as Serbia.
- **Flexibility and adaptability in the use of instruments is critical.** In a context such as Serbia, where policy implementation issues are often the greatest challenge, and where fiscal space reduces the scope for investment lending, the increased use of result-based

financing is a logical way forward. However, clients do not yet have the same familiarity and comfort levels with this instrument as with the tradition investment lending and budget support instruments. An increased effort to build understanding of the benefits of these instruments in Serbia's specific context needs to be made.

- **The WBG is well placed to provide for high quality, timely, and relevant AAA, which can then form a solid basis for lending operations.** This was demonstrated, for example, by the Real Estate Management Project, which was preceded by an in-depth Technical Assistance that helped in mapping relevant sector issues and informed the design of the project, and also helped frame the WBG input to the drafting process of the law on Constructing Permitting. Non-lending work should continue even when lending is delayed, as it often provides for continuing counterpart engagement and knowledge base, which are critical for quick movement when the time comes. The results of the Country Opinion Survey (2014) also show that the WBG knowledge products are highly valued in terms of both quality and usefulness to development.
- **The next CPS should build on focused objectives and clear outcomes, monitored by observable indicators.** The large number of outcomes in the CPS results framework made it hard to use as a practical tool for dynamic monitoring and adjustment, and complicated focusing on key priorities.
- **High-level policy dialogue was crucial for achieving a number of outcomes,** particularly in the area of State and Socially Owned Enterprise reform, public sector wage and employment reform and energy and transport sector reform. Such dialogue needs to be sensitive to changing political circumstances and take advantage of opportunities presented by new Governments as they commit to revised strategies and new policies.
- **An enhanced and structured partnership with the EU, in particular in the broad domain of economic governance, is essential as Serbia gets closer to EU membership.** The importance of this partnership will increase during the CPF as Serbia moves to negotiate new *Acquis* Chapters. Joint financing initiatives in critical reform areas (either through parallel financing or making use of the World Bank-EU framework agreement) or possibly joint sector budget support are potential instruments for stepping up joint engagement.
- **The challenging macroeconomic environment or poor corporate and financial governance poses constraints to IFC investment activity.** While the results overall have been satisfactory and the IFC portfolio in Serbia has remained profitable, its quality has deteriorated as a result of weaker financial performance of some of the clients affected by the lower growth environment.

## CPSCLR Attachment 1

**Table 1: Summary of CPS Program Self-evaluation**

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
<i>Pillar I – Strengthen Competitiveness</i>			
<p><b>Country Development Goals</b>            Infrastructure            Irrigation Systems and Institutional Framework to Support Increased Agricultural Production            Investment Climate            Innovation Capacity            Strengthened Fiscal Performance with Sustained Improvement in Human Development Outcomes Through More Efficient, Effective Social Spending            More Informed and Effective Policymaking to reduce poverty and Increase Social Cohesion and Equality            Strengthened Banking System</p> <p><b>Issues and Obstacles</b>            Missing links on the Serbian portion of Corridor X (one of the Pan-European Corridors of which Serbia is a key transit country); Road safety a concern.            Dilapidated water sector impairs functionality of essential drainage and flood control infrastructure in Serbia. Strong Water User Laws needed; and stronger flood defense.            The role of the state in the corporate sector remains pervasive, with fiscal implications in the form of direct and indirect subsidies and consequences for growth and competitiveness:            Inadequate infrastructure and weak institutional and enforcement capacity in the judiciary erodes public and business confidence.            The capacity for planning, budgeting, allocating, executing and controlling public funds needs strengthening.            Corporate financial reporting has improved but lags behind EU practices.            Low levels of insurance against natural disasters            The current system and composition of R&amp;D funding does not support Serbia’s agenda to modernize and enhance its competitiveness.</p>			
<b><u>Road Transport</u></b>			
<p><b>Motorway network expanded as a foundation for future improvement in transport efficiency</b>, as indicated by:  <b>Indicator:</b> Number of km constructed on two motorways (E-75 and E80):  <b>Baseline</b> (2009): 0 km  <b>Target</b> (2016): 40.57 km</p>	<p><b>Mostly Achieved:</b> All four lots on the E-75 were awarded in March 2012. The works started in May 2012 and completion is still expected by October 2015. Road construction on E80 is expected to be completed by December 2015. A total of 9km of the main roads and 17km of access roads have been completed i.e. fully paved, while final signalization, landscaping and minor finishing works to be completed at later stage and at the same time for the entire length of road. In</p>	<p><b>SPN:</b> FY10 Corridor X project (P108005)  <b>AAA:</b> Supporting Rail Policy Reform (EW)  <b><u>New financing since CPS:</u></b> FY13 Roads rehabilitation and Safety Project  <b>TF:</b> Supporting Rail Policy Reform (EW)</p>	<p>Importance of strong institutional capacity and project preparation and management skills to maintain satisfactory implementation progress and reduce the need for variation orders, costly claims by contractors and commitment fees on loans.            Importance of sector autonomy based on clear service level agreement arrangements with the government to ensure accountability and improved service</p>

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
	addition, approximately 5.6km of the main road is in the stage of the final testing, awaiting for the last layer of asphalt.		
<b>Action plan for reform of PEPS (Public Enterprise: Roads of Serbia) adopted by 2015.</b>	<b>Achieved:</b> Merger of Roads of Serbia and Corridors of Serbia created a reformed single roads agency		
<b>National Road Safety Strategy developed and launched by 2015.</b>  <i>Milestone:</i> Adoption of National Road Safety Strategy and implementation of Road safety pilot projects. <i>Baseline</i> (2009): No strategy <i>Target</i> (2015): Strategy adopted and four pilot projects implemented. Results indicator(s) in this area to be developed under next CPF.	<b>Achieved:</b> A Lead Agency has been established under the new Road Safety Law; and the National Road Safety Strategy, a road safety cost model and terms of reference for the accident database have been prepared. Two road safety pilot projects completed.		
<b><u>Irrigation</u></b>			
<b>Improved agriculture sector resilience to floods and improved agricultural yields</b> , as indicated by: <i>Indicator:</i> Number of additional flood protection schemes: <i>Baseline</i> (2006): 0 new or rehabilitated schemes <i>Target</i> (2013): 42 flood protection schemes covering 550,000 ha and 1.8 million people along Danube, Sava, Tisa and Tamis rivers	<b>Partially Achieved:</b> Activities on rehabilitating flood control and drainage rehabilitation infrastructure are completed on 44 schemes covering 440,000 hectares country-wide, providing an increased level of protection to approximately 1.1 million people. Target number of flood control and irrigation schemes to be strengthened was scaled down due to the late adoption of the Water Law. The recent floods demonstrated that a critical gap remains.	<b>SPN:</b> FY06 Irrigation and Drainage Project (P087964) <b>IFC investments</b> in under-served segments of the economy: SME, agribusiness, energy efficiency and renewable energy, municipalities, and rural areas.	Making project components dependent on the adoption of certain legislation presents significant timing risks. The formulation or amendments of laws are political processes where the Bank can only have a limited influence and these are essentially governed by the local politics. This is true even when the government recognizes the need for legal amendments, but reforms might be opposed by a number of interest groups that rely on the status quo to maintain their economic position.
<b>Improved capacity for increased agricultural yields</b> <i>Baseline</i> (2006): Wheat yield 3.5 tons/ha, corn yield 2.2 tons/ha <i>Target</i> (2013): 20% increase in average yields	<b>Achieved:</b> The interventions under the project to improve drainage and irrigation contributed to increased crop production of up to 36.5%, taking into account total effects of the yields increase, change in the sowing structure and reduction of costs, converted to the level of yields increase.		Complexity of multi-stakeholder's involvement in countries with no consensus on medium-term development, and with unclear delineation of duties and responsibilities, presents a significant implementation risk. The lack of an agreed vision in the sector reforms

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
			<p>especially as it relates to the institutional mandates and organizational structure lead to significant organized resistance to changes.</p> <p>A PIU with substantial decision making power helps project implementation when the responsible Ministry is challenged due to frequent changes at the top. However, while a relatively successful project may be implemented, the overall impact on the institutional system remains limited.</p>
<p><b><u>State Owned Enterprise Reform</u></b></p>			
<p><b>Improvement of corporate governance model for SOEs, by introducing rules for management appointments, increasing accountability and transparency of their performance, to be implemented by a dedicated and resourced unit within the government in charge of the state enterprise portfolio</b></p>	<p><b>Achieved:</b> The Parliament has adopted a new PE Law, introducing objective rules for appointments, improving governance structures, and increasing transparency through various enhanced reporting requirements.</p>	<p><b>Lending:</b> SOE DPL  <b>IFC:</b> banking and insurance privatization and participation on the board of directors;  <b>IFC:</b> PPPs in infrastructure;  Support infrastructure projects at municipal level;  <b>IFC investments:</b> (i) short-term financing and trade products; (ii) mezzanine and equity investments; (iii) SME funding support through financial intermediaries.  <b>AAA:</b> FY12 Country Economic Memorandum;  <b>AAA.</b> Municipal Finance Expenditure review, 2013, (P145374)  <b>IFC Advisory Services:</b> IFC assisted the Serbian Chamber of Commerce to develop voluntary Corporate Governance Code; support to nine private companies to improve corporate governance.</p>	<p>Legislative reforms are often the “easy part” of reforms, while real challenge lies with the implementation. When faced with difficulties in implementation, in many cases the first instinct for authorities is to engage in legal changes, rather than addressing the weaknesses in institutions and procedures that are supposed to implement the reforms. In designing operations for the new CPF, a lot of consideration should be put on choosing instruments and developing programs that facilitate implementation.</p>
<p><b>Potential social impact of SOE reform managed via payment of allocated funds to redundant workers:</b></p> <p><b>Baseline:</b> RSD 0 in 2013 budget  <b>Target:</b> Total allocations in the 2014 budget amounts to 2.8 billion RSD and 2015 budgets amounts to 16 billion RSD (approximately EUR 130 million)</p>	<p><b>Achieved:</b> The Government allocated sufficient resources in the budget to provide severance payments to redundant workers. In 2014 it was budgeted RSD 3.3 billion and the whole amount was spent in order to finance severance packages to approximately 4,500 workers. Resources allocated in the 2015 budget are adequate to compensate a further 20,000-25,000 redundant workers.</p>		

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
<b>Judicial Performance</b>			
<p><b>Improved efficiency and services of the judiciary through supporting the Government’s justice sector reform agenda and Serbia’s EU accession process, as measured by:</b></p> <p>Progress in negotiations under Chapters 23 and 24 of the EU accession agenda.</p>	<p><b>Mostly Achieved:</b> EC Progress Report for 2014 noted “some progress” in the judiciary. Functional review of the Serbian Judiciary provided the basis for the Action Plan for opening of the negotiations under the Chapter 23, covering also issues that come under Chapter 24.</p> <p>With support of the MDTF-JSS the WB completed Serbia Judicial Functional Review in July 2014 which served as the key analytical input to the government’s Action Plan for Opening Negotiations under the Chapter 23. Serbian judiciary finalized this Action Plan which is being reviewed by the EU Commission. The Action Plan will be used as a base for prioritization of activities outlined in the National Judicial Reform Strategy 2013-2018</p> <p>Based on the Functional Review, and in coordination with national stakeholders and MDTF-JSS development partner, the WB will realign MDTF to further strengthen EU accession process and support the implementation of National Judicial reform Strategy 2013-2018.</p>	<p><i>TF:</i> FY11 Justice Sector Support  <i>TF:</i> FY12-16 Justice Sector Support (MDTF)  <i>AAA:</i> FY11-14 Western Balkans Public Financial Management &amp; TF supported projects  <i>AAA:</i> FY11-14 Programmatic Western Balkan Financial Sector TA</p>	<p>Ensure local ownership. It is not clear who is in the lead of the reform process. Leadership in Serbian judiciary is divided between several institutions. To achieve meaningful and sustainable change it is important that all actors are consulted in the identification of reform priorities and included in the design and implementation of reform activities. The WB has provided assistance appreciated by the national stakeholders and the Bank’s partners. The MDTF will continue to support Serbia’s EU accession.</p> <p>Change of business practice. After the initial phase where focus was on ensuring independence, we are now focusing on the efficiency and quality of services provided by the judicial system. Previous attempts to address these problems by adding more staff failed to produce desired results and even exacerbated the problem. The best way to deal with these issues is to review existing business practices in courts and prosecutors’ offices and change them in a way which would contribute to the efficiency and quality of judicial services. This will require a shift in the leadership’s perception of the problem and stronger involvement of international partners.</p>

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
<b><u>Public Financial Management</u></b>			
<p><b>Legal framework in place for strengthened transparency of corporate financial reporting in line with EU standards.</b></p>	<p><b>Achieved:</b> Two laws, namely Law on Accounting and Law on Auditing were passed in July 2013, marking visible progress in bringing the legislative and institutional environment in the area of corporate financial reporting closer to EU <i>acquis communautaire</i>. However, actual practices in accounting and auditing lag behind the reforms in the legal framework, and very recent changes in the <i>acquis communautaire</i> will require additional adjustments to Serbian law governing financial reporting.</p>	<p>AAA: Regular Economic Reports AAA: FY12 Regional REPARIS</p>	<p>Creating appropriate legislative and institutional framework is only the first step in strengthening public financial management, while enforcement of the laws and achieving development results in practice remain challenging aspect of the reform process. Sustainable reform of corporate financial reporting requires a multifaceted effort including improvements in education and professional training; enhancement of the legal regulatory framework; and strengthening of the professional bodies. It is critical to secure input and support from the major stakeholders in corporate financial reporting to support this multifaceted effort.</p>
<b><u>Catastrophic Risk Insurance</u></b>			
<p><b>Monetary impact of floods reduced by the provision of catastrophe insurance, as indicated by:</b> <b>Indicator:</b> Increase in total coverage of firms and individuals brought about by Europa Re. <b>Baseline:</b> 2% <b>Target:</b> 15%</p>	<p><b>Partially Achieved:</b> The amendment to the Insurance Law enabling the operations of the Europa Re in Serbia was adopted only at the end of December 2013. Financial products of Europa Re have been launched. Sales of flood insurance commenced at the end of September 2014 in the aftermath of major floods. While the SEE CRIF program made flood and earthquake insurance products available to the Serbian homeowners only recently, it is estimated that the penetration of flood insurance is increasing and is around 3-4 percent.</p>	<p><b>SPN:</b> SEE Catastrophic Risk Insurance Facility (P110910)</p>	<p>Political support is insufficient to ensure action. The definition of indicators for future project should take this difficulty into account. Public information campaigns can be very useful in building support and in speeding up the uptake of risk insurance. Despite the successful completion of all technical work and entering into business partnership agreements with local insurance companies to distribute catastrophe insurance products, Europa Re is unlikely to reach the initial sales targets by the end of 2014 due to the delays with the enactment of amendments to the Insurance Law and its failure to provide a timely approval</p>



CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
			for the insurance products developed under the SEE CRIF program.
<b><u>Innovation Capacity</u></b>			
<p><b>Established institutional capacity to stimulate innovative activities in the enterprise sector, as indicated by:</b></p> <p><i>Indicator 1.</i> Additional funds raised by Serbia Innovation Fund to support innovation: Baseline 2011: €0 Target 2014: €20 Million</p> <p><i>Indicator 2.</i> Startups have been financed and new products and processes have been launched by beneficiary enterprises.</p> <p><b>Baseline</b> (2011): 0 startups financed and no new products <b>Target</b> (2014): 10 startups financed and 8 new products and processes</p>	<p><b>Achieved:</b> Established and fully operational Innovation Fund successfully deployed pilot financial instruments resulting in financing of the startups and companies. Total funds raised so far amount to: €35 million.</p> <p>64 start-ups have been financed and 10 new products have been launched</p>	<p><b>New Financing:</b> FY12 Serbia Innovation Fund (P126229);</p> <p><b>AAA:</b> FY11-14 Western Balkans TA on Science, R&amp;Innovation (TF);</p> <p><b>AAA:</b> FY13Western Balkans Study on Employment and Innovation (TF);</p> <p>FY 12-FY 15 Innovation (TF)</p> <p><b>Key Partners:</b> EU Delegation</p>	<p>An institution built from the ground up w/ strong capacity based on international good practice: Israel, Finland Solid governance structure w/ international peer review + independent Investment Committee Visible results in building the entrepreneurial ecosystem + start-ups w/ new IP, products on the market and revenue, investments raised + ~ 600 knowledge jobs created /sustained</p> <p>Ownership at the Ministry level critical for the reforms to go through, individual project at the research institute require handholding to make commercialization transaction reality</p>
<b><u>Strengthened Banking Sector</u></b>			
<p><b>Enhanced financial and institutional capacity in the Deposit Insurance system</b> as measured by:</p> <p><i>Indicator 1:</i> Cumulative inflows into the DIF Baseline: NA Target: US\$150 mil</p> <p><i>Indicator 2:</i> DIA performing its legally mandated technical functions in any future bank failures in which DIF resources are utilized <b>Baseline:</b> No <b>Target:</b> Yes</p>	<p><b>Achieved.</b></p> <p>The inflows into the DIF have exceeded US\$150 mil.</p> <p>Recent resolutions were done properly and the target was achieved.</p>	<p><b>New Lending:</b> <i>Deposit Insurance Strengthening IPF (FY14)</i> <b>TA:</b> <i>FINSAC</i> <b>IFC:</b> Support for the privatization of two state owned banks (Cacanska banka and Komercijalna banka) <b>Key Partners:</b> EBRD and IMF</p>	<p>Results Based Financing can be an effective instrument for strengthening an institution over the course of several years through the achievement of Disbursement Linked Indicators (DLIs). Much of our past work (both lending and TA) has been focused on stabilizing the financial sector and the Bank must now focus more on policy measures that can stimulate credit growth and the contribution of the financial sector to overall growth in the country.</p>

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
<b><i>Pillar II – Improved Efficiency and Outcomes in Social Spending</i></b>			
<p><b>National Priorities</b>  Strengthened fiscal performance  More informed and effective policymaking to reduce poverty and increase social inclusion</p> <p><b>Issues and Obstacles</b>  Health spending is inefficient  Pension reform agenda remains unfinished  Public sector remains too large; input financing needs to be reformed.  Poverty data needs to be more fully assessed  Gender needs to be better mainstreamed</p>			
<b><u>Health Spending</u></b>			
<p><b>Accountability and quality of public health spending improved</b>, as measured by:  <b>Indicator 1:</b> Percent of PHCs adopting clinical pathways  Baseline: 0% of PHCs have adopted clinical pathways  Target: 25%  <b>Indicator 2:</b> PHCs using fully operational health management information system (HMIS) platform.  <b>Baseline</b> (2008): 0%  <b>Target</b> (2014): 85%</p>	<p><b>Achieved:</b> Accountability and quality: 39.62% of PHC have adopted clinical pathways and 95.7 percent of PHCs use fully operational health management information system (HMIS) platform.</p>	<p><b>SPN:</b> FY08 DILS Project (P096823)  <b>AAA:</b> Education TA, Phase 2 (P118286)  <b>IFC:</b> Investments and advisory in health PPPs.  <b>New Operation: Second Serbia Health project:</b> Year One Results expected change by end of CPS.</p>	<p>Due to the relatively frequent Government change leading to inconsistency in strategy and priorities, attempts should be made for the reforms to be very gradual and divided into smaller, logical steps which will ideally show results respectively, and for which it would be easier to provide Government’s commitment. Those smaller areas then, fully developed, may create a rational complete system. The MoH is somewhat reluctant to address inefficiencies, particularly when it comes to consolidation of the workforce, or scaling up performance based payment, mainly because of the impact on political capital, effect on media and public (not seldom twisted), but sometimes also for social reasons. The MoH and the Government could use assistance in formulating and sending appropriate message that would be well understood and accepted by the public (Examples: (i) for medical providers – those who perform better and have better results should be better</p>
<p><b>Needs of vulnerable groups being addressed by trained medical staff and associates</b>, as measured by:  <b>Indicator:</b> Number of Roma children vaccinated through Roma health mediators:  <b>Baseline</b> (2008): 0  <b>Target</b> (2014): 18,795</p>	<p><b>Achieved:</b> Nearly 500 medical staff and associates trained to recognize the needs of vulnerable groups; 15 Roma health mediators 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, Government institutionalized Roma health mediators by funding their salaries from national budget. According to MoH data collected by the Roma health mediators, there are</p>		

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
	41,559 children age 0-15 in the 60 municipalities covered by the program. The target represents 45% of this total.		rewarded, instead of “all the salaries will be cut; (ii) for the public – you want your health insurance money to be spent towards better care, more narrowly – to have more physicians, nurses, better and more modern equipment and up-to-date diagnostics instead being spent on mechanics, plumbers, accountants, etc). So far, the Government has not been very successful in passing these messages and perhaps this should be addressed.
<b><u>Disability Financing</u></b>			
<p><b>Innovative services for the disabled developed, piloted, and scaled up across the country</b>, as indicated by:</p> <p><i>Indicator:</i> Sign language interpretation services for the deaf and escort services for the blind and people with impaired vision available  <b>Baseline:</b> Not available  <b>Target:</b> Available across the country</p>	<p><b>Achieved:</b> Internal operating procedures of the Disability Fund of the Ministry of Labor and Social Policy (MoLESP) have been reformed to enable funding of the results-oriented projects. 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). Services are available across the country and are sustainable (financed through Disability Fund Grants). When people with disability need some services they apply for it and get it in time.</p>	<p><b>SPN:</b> FY08 DILS Project (P096823)</p>	
<b><u>Pension Administration</u></b>			
<p><b>Effectiveness of pension administration improved</b>, as indicated by:  <i>Indicator:</i> Decline in administrative costs/pension expenditures  <b>Baseline</b> (2005): 2.2%  <b>Target:</b> 1.5%</p>	<p><b>Achieved:</b> Improvements in effectiveness of administration indicated by administrative costs/pension expenditures achieved. Revised target of 1.5% achieved. The original 2005 baseline figure was revised from 4% to 2.2% (in 2005).</p>	<p><b>SPN:</b> FY08 DILS Project (P096823)  <b>SPN:</b> FY05 Consolidated Collection and Pension Administration Reform Project (P090418)  PEDPL Series (P108759 and P120399)</p>	<p>Despite the fact that some reforms have been undertaken the real results on spending may not be visible in the longer run as pension reform usually limited impact on short term period.</p>

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
			In order to remove administrative costs obstacles and make business process more efficient the central registry should be used in such a way to make it functional and effective for social sectors, tax authorities and employers registering their employees.
<p><b>Long-term sustainability, adequacy and transparency of the pension system improved,</b> as indicated by:  <b>Indicator:</b> Total pension expenditure to GDP ratio  <b>Baseline</b> (2005): 13.4%  <b>Target:</b> 12%</p>	<p><b>Not Achieved:</b> Spending on wages and pensions increased although indexation formulas were implemented. Spending on pensions increased to 13.8 percent of GDP in 2013 (compared to 12.4 percent of GDP in 2008). Spending on public sector wages increased as well – 11.2 percent of GDP in 2013 compared to 11 percent in 2008. The primary instrument for Bank support in this area was the PEDPL series, of which the third was cancelled. In the case of pension since the GDP declined after the economic crisis, making it difficult the shares of pension as a percentage of GDP despite positive changes in indexation.</p>		
<b>Other Social Spending</b>			
<p><b>Better-informed decision-making on public expenditures,</b> as indicated by:  Fiscal Council established and operational  <b>Baseline:</b> Fiscal Council not operational  <b>Target:</b> Fiscal Council operational and State Audit Institution completes external audit of final accounts for RoS and at least 10 other external audits.</p>	<p><b>Mostly Achieved:</b> Fiscal Council is now established and operational. The State Audit Institution (SAI) audits final accounts of the RoS continuously since 2008. The SAI increased its capacity and number of annual audits during the CPS period. Latest data relates to 2012 financial statements, for which the SAI issued more than 60 audit reports, including those of final accounts of the RoS, stand-alone financial statements of various ministries, local self-governments, State Owned Enterprises, the National Bank of Serbia etc.</p>	<p>PEDPL Series (P108759 and P120399)  <b>SPN</b> FY08 DILS Project (P096823)</p>	<p>While some progress in the area of social inclusion has been made by putting in place strategies, plans and policies to address vulnerable group inclusion, the effectiveness of these policies varied. There remain various groups, such as ethnic minorities, disabled and displaced persons that face challenges in accessing social services. At both national and local levels there remains a need for technical assistance and capacity building. This assistance should focus on designing, promoting and implementing effective social</p>

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
<p><b>Central and local per capita funding formulas in the education sector tested (Ministry of Education and Science)</b>  <b>Baseline:</b> No funding formulas  <b>Target:</b> Formulas tested and rolled out.</p>	<p><b>Not Achieved.</b> Central and local per capita funding formulas were supposed to be piloted in 15 municipalities but the MOE did not approve it and the pilot was not implemented.</p>		<p>inclusion policies, programs and projects. It is also important to put in place project monitoring tools that can provide timely and consistent information on progress and impacts of inclusion policies and programs.</p>
<p><b><u>Poverty Analysis and Monitoring</u></b></p>			
<p><b>Poverty analysis and monitoring more closely aligned with EU methodology</b>, as indicated by:  <b>Indicator:</b> Completion and publishing of the SILC survey.  <b>Baseline:</b> SILC survey results not published  <b>Target:</b> Published.</p>	<p><b>Achieved:</b> SILC 2013 Completed First aggregate results published by the Statistical Office in a press release in December 2013; Bank’s quality assessment report of 2013 SILC completed; SILC 2014 data collection completed. Initial poverty analysis using the 2013 SILC completed (profiles of the poor and different parts of the income distribution, correlates of poverty, employment and income types, access to basic services).</p>	<p><b>AAA:</b>  Western Balkans Programmatic Poverty Assessment  Western Balkans Smart Safety Nets and Activation  FY12-13 Survey of Income and Living Conditions (TF)  FY13-15 Poverty and Social Impact Analysis  FY12-13 Regional Monitoring and Evaluation (TF)  Western Balkans Programmatic Gender Monitoring  Western Balkans Jobs TA</p>	<p>Quality and availability of data are key to poverty and shared prosperity monitoring and analysis. Data collection and poverty measurement in Serbia, especially based on a new survey instrument and new methodology, faces certain challenges (e.g. sample size, field work quality control, comparability over time) and can benefit from cross-country learning. So continued partnership with the Government, including the Statistical Office and the Social Inclusion and Poverty Reduction Units, will be important.  Supporting policy and shared prosperity analysis linked to other sectors would not only inform policies but also lay the analytical foundations needed for the next SCD and CPF. For example, over this current CPS cycle, PSIA work and poverty simulation of disaster impacts were informative to other sectors’ work and can be expanded.</p>

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
<i>Environmental Sustainability</i>			
<p><b>National Priorities</b> Address urgent environmental legacy issues arising from mining sector restructuring in the Bor region Increase Energy Efficiency</p> <p><b>Issues and Obstacles</b> The old and polluting copper mining complex has been extremely harmful to the environment, with legacies that continue to threaten the area. Serbia remains one of the most energy inefficient countries in ECA.</p>			
<b><u>Environmental Condition of Bor Region</u></b>			
<p><b>Urgent environmental legacy issues addressed</b>, as indicated by: <i>Indicator:</i> Reduction of environmental risks related to the poor state and risk of possible failure of the Veliki Krivelj collector</p> <p><b>Baseline:</b> collector at risk of collapse <b>Target:</b> Works have been completed and collector replaced</p>	<p><b>Not Achieved:</b> Design for the new collector completed. Contract for civil works awarded in January 2013. In mid-2013, the closing date of the Bor project was extended to September 2015. In extending, the Bank and the authorities agreed to significantly reduce the scope of its activities, including: (1) cancellation of the environmental remediation activities and monitoring activities, other than those related to the construction of Veliki Krivelj Collector bypass; and (2) discontinuation of the activities related to socio-economic component. However, following continued protracted delays loan funds were cancelled at the request of the Government in February 2015.</p>	<p><b>SPN:</b> FY08 Bor Regional Development Project (P092999)</p>	<p>Complex projects with multiple stakeholders and unclear delineation of responsibilities make the project implementation extremely challenging.</p> <p>Project implementation is heavily suffering without strong Project champion in times with frequent political changes, regardless of technical merits.</p>
<b><u>Energy Efficiency</u></b>			
<p><b>Improve energy efficiency in public buildings to lower the heating bill and improve health and environment for users.</b></p> <p><i>Indicator 1:</i> Lower heating bills for public buildings: <b>Baseline:</b> No savings <b>Target:</b> US\$2.5 million per year saved</p>	<p><b>Achieved</b></p> <p><b>Achieved:</b> Savings from the energy system rehabilitation are around US\$2.5 million per year. Annual energy consumption in public buildings (schools and hospitals) reduced by 60% on average.</p>	<p><b>SPN:</b> FY04 Energy Efficiency Closed, April 2013. (P075343) <b>IFC:</b> Advisory and financing energy efficiency and Balkan Renewable Energy Program.</p>	<p>Going beyond pilot demonstration projects to large-scale energy efficiency programs require upfront consideration to a transition strategy which should address sustainability and replicability issues. Ensuring the participation and increase the interest of end-users and local self-governments is an important element in this transition;</p>

CPS Outcomes/Cluster of Outcomes, Outcome Indicators and Milestones	Status and Evaluation Summary	Lending and Non-lending Activities that contributed to the Outcome	Lessons and suggestions for the new CPS
<p><b>Indicator 2:</b> Emissions targets achieved in four categories (SO<sub>2</sub>, NO<sub>x</sub>, Ash and CO<sub>2</sub>):  <b>Baseline:</b> 0 emissions targets met  <b>Target:</b></p>	<p><b>Achieved:</b> Project achieved targets in reducing emissions in all four categories (SO<sub>2</sub>, NO<sub>x</sub>, Ash, and CO<sub>2</sub>).  In the project sites, no actual sulfur dioxide emission; no actual ash, soot &amp; other solid particles emission; significantly reduced nitrogen oxide emission; and significantly reduced carbon dioxide emission (in total ca. 90% achievement).</p>		<p>It is critical to ensure that project implementation arrangements are fully integrated within the Government administration to build capacity. Special attention should be given during implementation to ensure that individual and organizational capacity which is built during implementation is not lost after the project is closed.</p>

### Summary of Results

Results	Number	Achieved	Mostly Achieved	Partially Achieved	Not Achieved
<b>Pillar 1: Outcomes</b>	<b>12</b>	<b>8</b>	<b>2</b>	<b>2</b>	<b>0</b>
<b>Pillar 2: Outcomes</b>	<b>8</b>	<b>5</b>	<b>1</b>	<b>0</b>	<b>2</b>
<b>Environmental Sustainability: Outcomes</b>	<b>2</b>	<b>1</b>	<b>0</b>	<b>0</b>	<b>1</b>
<b>OVERALL CPS: Outcomes</b>	<b>22</b>	<b>14 (63%)</b>	<b>3 (14%)</b>	<b>2 (9%)</b>	<b>2 (14%)</b>

## CPSCLR Attachment 2

**Table 2: Planned Lending Program and Actual Deliveries (2012-2015)**

CPS Plans (FY2012 – 2015)		Status		
FY	Project	US\$(M)	Project	US\$(M)
		IBRD		IBRD
2012	Public Expenditure DPO	100		
Subtotal		100		
2013	Private/Financial Sector (PFDPO) 1	100		
	Road Rehabilitation and Safety	100	Road Rehabilitation and Safety	100
	Health Sector	40		
Subtotal		240		100
2014	PFDPO 2		Health Sector Enhancement	40
	Energy Efficiency		Deposit Insurance Agency Strengthening	200
	Investment Operations (tbd)*			
Subtotal				240
2015	PFDPO 3		Floods Emergency Recovery Loan	300
	Investment Operations (tbd)*		Real Estate Management Project	44
			Public Enterprise Reforms DPL 1	100
Subtotal				444
Total lending FY12-15		340	Total lending FY12-15	784

\*Possible projects included Cadastre, Skills project and Agriculture project

**Table 2a: Investment Lending & Budget Support**

CPS FY 2012 – 2015	Planned US\$(M)	Status US\$(M)
New Investment Lending	140	684
Development Policy Loans	200	100
Total Lending	340	784



**Table 3: Planned Non lending Services and Actual Deliveries (2011-2014)**

<b>CAS PLANS (November 2011)</b>		<b>STATUS</b>
<b>2012</b>	Country Economic Memorandum	Completed in FY12
	Innovation (TF)	Actual FY12-16
	Justice Sector Support (MDTF)	Actual FY12-16
	Municipal PFR	Completed in FY13
	Energy Strategy	Dropped
	Education TA	Completed in FY12
	Survey on Income and Living Conditions (TF)	Actual FY14-15
	Poverty and Social Impact Analysis	Actual FY 13- 15
	Western Balkans REPARIS	Actual FY12-17
Western Balkans TA Science, R&D and Innovation [renamed: Western Balkans Regional Research & Development Strategy for Innovation]	Completed FY12-14	
Western Balkans Programmatic Financial Sector Development	Completed FY12-14	
Regional Monitoring and Evaluation (TF) [renamed: Monitoring and Evaluation Capacity Development for the Western Balkans and Turkey]	Completed FY14	
Regional Smart Safety Nets	Completed FY13-14	
Western Balkans Programmatic Gender Monitoring	Actual FY13-15	
Western Balkans Programmatic Poverty Assessment	Actual FY13-15	
Promoting Employment through Skills Development TA	Dropped ( <i>Serbia is participating in the Programmatic Western Balkans Jobs Challenges TA</i> )	
Western Balkans Public Fin. Mgt/PEFA (TF)	Dropped	
Western Balkans Regional Health AAA	Actual FY13-16	
<b>PROGRESS REPORT PLANS (August 2014)</b>		<b>STATUS</b>
<b>2014</b>	Municipal PFR 2	Completed in FY14
	Serbia Real Estate Management TA	Completed in FY14
	Serbia Government Debt and Risk Management TA	Actual FY11-FY17
	Belgrade Debt Management TA	Completed in FY14
	Supporting Rail Policy Reform (EW)	FY15
	Country Fiduciary Assessment	Dropped

	Macro Modeling Support TA	Completed in FY14
	Agriculture Sector Dialogue TA	FY15
	Serbia Inclusive Education	FY15
<b>PROGRESS REPORT PLANS (August 2014) – Regional Western Balkans AAA</b>		<b>STATUS</b>
	Mainstreaming Roma	Completed in FY14
	Western Balkans Jobs Challenges	Actual FY13-FY16

## CPSCLR Attachment 3

### PROGRESS TOWARD ACHIEVING COUNTRY-LEVEL GOALS

1. The CPS was aligned with and contributed to progress toward the overarching country goal of integration into the EU and to three contributing clusters of objectives, which were broken down in ten strategic goals.

2. **The three clusters of objectives are enhanced competitiveness, efficient and effective social service delivery and environmental and social sustainability.** One strategic objective, fiscal sustainability, is of an overarching nature. For this reason, and considering the centrality of macro-fiscal sustainability through the program period, this element will be discussed separately.

#### European Integration

3. **Serbia made significant progress towards EU membership in the program period.** The Stabilization and Association Agreement entered into force on September 1, 2013, and EU membership negotiations were initiated on 21 January 2014. Historically the speed of Serbia's EU accession progress has often been dependent on political factors. However, as membership negotiations progress, economic governance and the strength of institutions will gain growing importance.

4. **Serbia still does not meet the 'functioning market economy' criterion, which is one of the critical benchmarks for joining the EU.** Hence an emphasis on structural economic reforms and competitiveness will remain a core element of Serbia's country level goals. Institutional strengthening, both across the public administration and in specific regulatory agencies, will be a further element of focus, as is social inclusion and in particular income growth of vulnerable groups.

5. **The World Bank Group has provided advisory and implementation support to the Government on key aspects of the European Integration agenda throughout the CPS period.** This included work on issues of economic governance, social inclusion, competitiveness and innovation and legal and judicial reform. On innovation and technology transfer and legal and judicial reform the Bank has in addition administered IPA-financed projects. On legal and judicial reform in particular, the conduct of a broad functional review of the judicial system and performance helped in defining objective benchmarks for the EU accession negotiation process.

#### Achieving macro-fiscal sustainability

6. **Serbia's macro-fiscal sustainability has deteriorated over the program period.** Political indecisiveness and the adoption of policies playing to specific voter group interests in the first years of the program period, combined with a stalemate on structural economic reforms aggravated an already dire fiscal situation. While greater political stability in the latter half of the program period halted expansionary policies, entitlements gained have proven hard to roll back,

meaning that even under a status quo scenario debt levels will continue to rise. Debt is projected to rise to over 70 percent of GDP by the middle of 2015.

7. **Expansionary fiscal policies combined with weak economic recovery in the Eurozone Serbia had a negative impact on GDP growth**, which varied between modest contraction (-2 percent in 2014 and -1.5 percent in 2012) and modest growth (+2.6 percent in 2013). A much stronger growth performance is needed both to converge with the EU, to reduce growing debt levels and to boost income levels of the bottom forty percent.

8. **In September 2014 the Government announced a new package of fiscal consolidation and structural economic reform measures** with the aim to stabilize the macro-fiscal situation and to stop the increase of public debt as a percentage of GDP.

9. **Following the adoption of this package, negotiations on a new precautionary standby agreement were initiated with the IMF, and concluded in December 2014.** The IMF program was approved by the IMF board on February 23, 2015. The program covers, apart from expenditure reduction measures, the reform of the state and socially owned enterprise sector, with an emphasis on the large public utilities and public transport enterprises. This reflects the extent to which successful fiscal consolidation in Serbia depends on addressing the deep problems in these sectors.

10. **Weak growth performance and growing fiscal deficits have particularly affected the bottom forty percent of Serbian society, who have suffered disproportionately.** Many of the gains made during the period of growth (2001-2008) have been lost after 2009 as incomes of the bottom forty percentile of the population declined faster than those of the top sixty. The Systematic Country Diagnostic emphasizes the disproportionate negative effect of economic decline on rural dwellers, low skilled workers and marginalized groups.

11. **Macro-fiscal dynamics made it impossible for the World Bank Group to provide much needed budget support during most of the CPS period.** The absence, until September 2014, of a credible consolidation program, the lack of an IMF program and growing debt levels meant that planned budget support operations were not delivered, except for one DPL on State Owned Enterprise Reform. While efforts were made to support pockets of reform initiatives through other instruments, for instance in the financial sector, opportunities for lending-based engagement were constrained.

## **Competitiveness**

12. **Regardless of government efforts to address constraints, Serbia's business climate continues to pose a critical hurdle to boosting private sector investment and improve competitiveness.** Serbia ranks 91<sup>st</sup> out of 189 economies in the 2015 Doing Business report, below most countries of the region (it is 22<sup>nd</sup> out of 26 ECA countries), and lower than what one might expect from its GDP per capita level. Overall, Serbia's ranking slipped 14 points between *Doing Business 2014* and *Doing Business 2015*, from 77<sup>th</sup> place to 91<sup>st</sup>. This outcome indicates that other countries are reforming more vigorously, and Serbia will need to undertake substantial reforms should it wish to improve or even maintain its ranking. Serbia ranks behind most of its neighbors, including FYR Macedonia (30), Slovenia (51), Montenegro (36), Hungary (54), Bulgaria (38),

Romania (48), Croatia (65), and Albania (68), and ahead of only Bosnia and Herzegovina (107). It should be noted that the problematic performance of Serbia is mainly driven by excessively low rankings on construction permits and paying taxes, which are of particular concern. Tax administration improvements are an element of the new IMF program, which should also help progressing on reforms.

**13. The latest Global Competitiveness Report by the World Economic Forum ranks Serbia 94<sup>th</sup> out of 144 countries.** The unfavorable macroeconomic and business environment, with weak protection of property rights and burden of government regulations has a negative impact on creation of new businesses and the day-to-day operations of companies, and on incentives for long-term investments including FDI, which are critical to the creation of new jobs to offset the large numbers of jobs that may have to be cut from the public sector.

**14. One of the major legacies of Serbia's transition is the continued presence of a large number of state-owned enterprises, which have strong distortive effects on the economy.** There are about 1,300 state owned enterprises employing about 16 percent of the formal Serbian workforce (~270,000 employees). Heterogeneous in nature, they can be segmented in two groups: (1) state and socially owned enterprises, and (2) municipally owned enterprises. The first group can further be segmented to public utilities, commercial companies, and companies in the Privatization Agency (PA) portfolio. Overall, public sector enterprises make significant net losses, which are estimated at about 3 to 4 percent of GDP or more than EUR 1 billion, and require significant state support to remain afloat. This includes significant direct budget subsidies and soft loans, as well as indirect support in various forms (unpaid taxes and contributions, guarantees for loans, arrears to other state entities and public utilities). In addition, the inability of various creditors and suppliers (both private and state owned) to collect payments for their services from companies in restructuring<sup>14</sup> is a major market distortion.

**15. While important progress has been made, especially since summer 2014, on resolving the 502 enterprises in the portfolio of the Privatization Agency, the process has not been completed.** Full completion of this process remains critical given the direct and indirect cost these companies impose on the budget and the negative impact they have on the investment climate. In early 2015, the Government approved a detailed plan for resolving the situation of the SOE's and included in the 2015 budget RSD 16 billion for severance packages for redundant workers. Resolving or corporatizing the remaining large enterprises, including public transport and utility companies will therefore remain a core issue on the policy agenda going forward.

**16. Financial sector risks remain and pose a further constraint to growth and competitiveness.** While the banking sector overall is considered healthy, weak credit growth, a high incidence on NPLs and a still incomplete reform process in the public banking sector pose downside risks on economic performance. World Bank support through policy dialogue and the implementation of the Deposit Insurance Agency Support project has played an important role in

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<sup>14</sup> Companies in restructuring are the most problematic sub-segment of companies in the Privatization Agency portfolio. These 162 companies were until recently legally protected from enforcement by creditors and from bankruptcy (following the amendments to the Privatization Law in May 2014, this protection will effectively expire in May 2015).

framing a broader consensus among government and development partners on how to address financial sector challenges.

17. **Important progress has been made in addressing critical infrastructure gaps to facilitate trade and transit, in both of which Serbia has important potential comparative advantages.** Completion of the remaining stretches of Corridor X is on track and a comprehensive road rehabilitation program for national roads is being implemented. Reform of the railway sector has also been initiated. Lending support in the road sector has been instrumental to progress in these areas. Further improvements to border management and progress on reforming the railway sector would further enhance Serbia's position in this respect.

18. **Land and property registration, land use planning, construction permitting and ease of paying taxes continue to pose critical challenge to the investment climate and business environment.** Progress made on land and property registration and management earlier has not been sustained and progress in the other above mentioned areas has been very slow. Even if legislation is being adopted on most or all of these issues, achieving a notable improvement will take significant time as implementation in these areas typically lags.

19. **Advisory and selected lending support have been provided by the World Bank Group throughout the CPS period,** with new lending operations coming on stream in the last two years of the CPS period to support aspects of financial sector reform, road sector reform and land and real estate management, as well as policy based lending support for the SOE resolution process. The Bank Group has played a leading role in dialogue in most aspects of competitiveness, which has helped in defining technical solutions as well as in building ownership for reforms.

20. **Through its advisory services, IFC has been supporting improvements in the legal framework that would ultimately allow IFIs to engage in dinar lending.** Also, recently IFC launched IFC's Debt Resolution Program in Serbia. This program is expected to reduce lending risks and lead to increased lending in the country. The program will be implemented over the period of next three years. It will cover legal and regulatory reform, as well as provide capacity building services relating to debt resolution in Serbia.

### **Efficient and effective social service delivery**

21. **Serbia's key human development indicators and access to basic services remain generally good.** Serbia performs better than other countries at similar income levels in the Human Development Index, school enrollment rates, life expectancy and infant and maternal mortality. Serbia's key health outcomes, including life expectancy and infant and maternal mortality rates, have improved and are comparable to the ECA averages. However, challenges with disparities, efficiency and quality of care remain. In the Human Opportunity Index, which reflects coverage as well as equality of opportunity, Serbia performs well relatively to ECA countries in primary school completion and access to water, sanitation and electricity but not so well in the domain of secondary school completion.<sup>15</sup>

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<sup>15</sup> World Bank Group's Visualize Inequality Dashboard.  
<http://www1.worldbank.org/poverty/visualizeinequality/index.html>

22. **Concerns persist with service quality and inequality of opportunities, particularly across wealth groups, ethnic lines, and regions.** These are caused mainly by weak efficiency and equity in certain public spending and service delivery. Governance and institutions for public service delivery and social safety nets need strengthening, to achieve high and equitable outcomes for the amount Serbia spends on public services. Important progress in strengthening public service delivery management was achieved under the Local Service Delivery Project and the Second Health Sector Strengthening project, which focused on supporting sector reforms and on providing critical equipment.

23. **Apart from issues with public service quality and access, an unaffordable public sector wage bill remains a pressing problem for the Government of Serbia.** The general government wage bill has grown significantly in recent years and now accounts for nearly a quarter of total public expenditure and almost 11 percent of GDP. Structural weaknesses in wage and establishment control systems have resulted in a bloated public sector with more than 780,000 employees, 2,200 job titles, 71 different elements of remuneration, 16 different base salaries, 900 different job coefficients, 19 laws and a plethora of by-laws that regulate salary levels in 11,000 budget institutions.

24. **Short-term measures to reduce the wage bill have been taken. However, a sustainable long-term solution for high fiscal deficits and low efficiency of the public sector requires an in-depth and comprehensive reform of the public sector.** In this respect, the Government has committed to a set of measures to enhance transparency, equity, and efficiency in the public sector wage system and to implement right-sizing measures. Implementation of these measures is planned from 2015-2018.

25. **Overstaffing or staffing imbalances are most evident in some sectors such as education (where the ratio of administrative to teaching staff is high), health (an overstaffed non-medical cadre),** the judicial system, local government and police and security forces. Advisory support on Public Sector employment and wage bill management was provided by the World Bank throughout the CPS period.

### **Environmental and social sustainability**

26. The environmental legacy issues remain significant, both in relation to state-owned and privately-owned enterprises. The level of efforts varied significantly during the period, but generally remained insufficient. Overall economic situation, lack of consistent support from high-level decision makers and relatively weak enforcement mechanisms contributed to slow and in most cases non-systematic actions from relevant institutions. Legal provisions in respect to environmental legacy issues remain incoherent and without practical implementation tools. The Bank-supported Bor Regional Development Project, which aimed to support the government in resolving the urgent environmental issues in Bor Region, was delayed due to above reasons and had not progressed beyond design stage.

## **IFC in Serbia: CPS Completion Report**

1. Serbia is IFC's fifth largest exposure in ECA (as of January 2014), with a committed portfolio of about \$445.6 million, all of which disbursed. During the CPS, IFC financed \$682 million in 16 projects, \$610 million for its own account and \$72 million through mobilization from the commercial banks. **This was at the range of \$600-800 million anticipated for the CPS or more than 50 percent compared to the previous CPS.** IFC placed significant focus on the financial sector financing 9 projects in numerous banks. In the real sector, IFC's investments were focused on the agribusiness, automotive and renewable energy sectors. In addition, IFC has financed three regional projects, with a Serbia component, for a total of \$120 million allocated in 3 projects (construction material company, investment fund focused on MSMEs, regional insurance company).

2. IFC rates its performance in Serbia as **moderately satisfactory**. IFC's program was consistent with Serbia's development priorities, WBG strategy and IFC's strategic focus areas. During the CPS, IFC focused on support for Serbia to become more competitive and reduce regional inequalities. This was consistent with IFC's strategic focus areas, and the CPS objectives. IFC investments responded to market conditions, filling the financing voids and offering products and services that often were not easily available commercially. Longer tenor, higher environmental and social standards, and better corporate governance that were embodied in IFC investments, as well as IFC's global knowledge were the key value-added. In addition, IFC contribution to MIGA program in the country was significant. IFC facilitated \$543 million MIGA financing in three large projects.

3. While the general experience and results of this increased level of IFC investment activity in Serbia has been positive, several projects have suffered from the challenging macroeconomic environment or poor corporate and financial governance. While the IFC portfolio in Serbia has remained profitable, its quality deteriorated as a result of weaker financial performance of some of the clients affected by the lower growth environment, coupled with persisting weaknesses in corporate governance and financial management. The level of non-performing loans (NPLs) has increased from nearly zero in FY12 to 18.8 percent in January 2015, because of some of IFC's agribusiness clients in Serbia struggling to meet their debt service obligations in a timely manner.

### **IFC program has been focused on Pillar 1 - Strengthening Competitiveness**

4. IFC promised to remain engaged in the financial sector, as well as to focus on agriculture and agri-business exports, renewable energy projects (wind, biomass and small hydro) and private sector participation in infrastructure projects through investments and public-private partnerships.

5. The CPS identified the *financial sector* as a generally strong core element under the competitiveness pillar. IFC interventions, targeted to help Serbia maintain financial resilience, have proceeded as planned, with positive results. IFC supported seven client banks by providing short-term liquidity, capital injections, and long-term finance for on-lending to the agribusiness sector. IFC financing in the banking sector, including local banks, provided a unique



countercyclical financing package by further strengthening banking sector capital base and their financial capacity in times of global economic slowdown. IFC supported its existing bank clients through both debt, sub-debt and equity instruments, to further strengthen their capital base at a time where Basel II capital requirements were to be adopted in Serbia. IFC financing made possible for the banks to bolster their operations within underserved segments of Serbia economy, including the agribusiness industries, MSMEs and access to finance to lower income population. Complementing its traditional instruments, IFC mobilized \$543 million MIGA guarantees for the Serbian subsidiaries of Western European banks, helping them manage increased capital adequacy requirements and maintain presence. However, during the CPS period, discrete but important vulnerabilities in the financial system emerged. IFC was committed to continue supporting the privatization of its two portfolio banks and possibly assist with the privatization of the biggest state insurer. However, the envisaged privatization of IFC's client banks with state participation has been somewhat slower due to challenging market conditions and changing government priorities. Nevertheless, Cacanska banka was sold to a Turkish Banking group in early 2015 and IFC played a leading role in the price and other negotiation terms. IFC is now assisting the Government select a privatization advisor for Komercijalna Banka, a much larger and more valuable institution. Also, because of collapsing interest rates and lack of lending opportunities banks started to prepay IFC loans.

6. In addition to investments, through its advisory services, IFC has been supporting improvements in the legal framework that would ultimately allow IFIs to engage in dinar lending. Also, recently IFC launched IFC's Debt Resolution Program in Serbia. This program is expected to reduce lending risks and lead to increased lending in the country. The program will be implemented over the period of next three years. It will cover legal and regulatory reform, as well as provide capacity building services relating to debt resolution in Serbia.

7. In the *infrastructure sector*, IFC has continued to promote resource efficiency and renewable energy. To this end, IFC InfraVentures Fund made its first investment in Serbia to support development of a 100MW wind power plant. However, introduction of greater private sector participation in infrastructure finance has been delayed. As a result, IFC's investments in the infrastructure sector, where IFC prioritizes renewable energy, have also been delayed due to the slower than expected pace of implementation of the required regulatory reforms.

8. IFC has also been looking for opportunities to use its advisory services to help Serbia attracting private sector participation in development of infrastructure projects. IFC's Infrastructure Advisory Program team for ECA was based in Belgrade during the CPS reporting period showing IFC's commitment to support the country attract private investments in the infrastructure sectors through PPPs. IFC's first PPP mandate in the country was signed in November 2014 with the City of Belgrade, engaging IFC as the lead transaction advisor for attracting a private partner for development of the waste treatment and disposal facilities, through a long-term PPP model. Initial market sounding, term sheet preparation, financial modeling, and preliminary technical and legal assessment of the project are completed. Pre-tender investors' conference was successfully held on March 25-26. The project was presented to more than 40 interested companies from around the world. Request for Expressions of Interest has been launched and analysis of the transaction is underway with the goal to award the tender by end FY16.

9. From August 2012, IFC has been implementing in Serbia its regional Balkan Renewable Energy Program. IFC has been working to develop renewable energy market in Serbia through assisting the Ministry of Energy to improve the regulatory framework, working with private companies on technical development of wind, small hydro and biomass power projects, as well as supporting local banks to build their capacities in renewable energy and project finance. The program activities enabled construction of more than 80 renewable energy power plants in Serbia, facilitating more than US\$100 million of investments and avoiding more than 100,000 tCO<sub>2</sub>/a. In addition, IFC has been supporting WBG activities in Serbia including WB's Flood Emergency Recovery Project as well as WB's missions relevant for the Serbian energy sector.

10. In the *Corporate Sector*, IFC focus has been in the agribusiness sector where IFC has financed \$233 million allocated in five projects as well as \$27 million in automotive industry. IFC investments aimed on supporting a sector important to the Serbian economy, support companies involved in value-added production and exports, strengthening of agribusiness linkages and support farmers and job preservation in frontier regions in Serbia, and support regional FDIs and south-south investments. By financing export oriented automotive sector IFC objective was to contribute to balancing Serbia's large current account deficit and to create sustainable jobs in frontier region of Serbia.

11. In addition to its investment program, to support the corporate sector, IFC has been implementing its regional Corporate Governance Program in Serbia. Since April 2012, 9 Serbian companies and financial institutions have received corporate governance services. In addition, the program assisted the Serbian Chamber of Commerce to develop voluntary Corporate Governance Code which is considered to be the most comprehensive one in the Western Balkans region.

12. Through its Resource Efficiency Program, IFC has been promoting resource efficiency by helping companies to identify and implement best practices and reduce the consumption of resources (energy, water, materials). IFC provided assistance to six private companies with a focus in the agribusiness sector, contributing to reduction of 1000 tons of solid waste and 6,300 tons of eCO<sub>2</sub>/year and \$6 million per year in cost saving. Recently, IFC launched Agribusiness Standards Program to help increased access to markets for the food sector by promoting the uptake of agribusiness standards, including food safety, environmental and social standards.

13. IFC has been contributing to improved investment climate in Serbia through its Trade Logistics Program to streamline clearance procedures along the Danube and at the Belgrade Airport. Through its Tax Transparency and Simplification Project assisted Serbian Parliament to adopted amendments to the Corporate Income Tax Law which reduced compliance burden for business related to filing of transfer pricing documentation.

### ANNEX 3. WB - IFC INDICATIVE PROGRAM FY16-21

SUPPORTING SUSTAINABLE PUBLIC EXPENDITURE MANAGEMENT	CURRENT PORTFOLIO	PIPELINE/PROPOSED LENDING	ASA/TA AND LINK TO THE LENDING PROGRAM
		<p>Serbia Public Enterprise Restructuring DPL 1 (FY 15)</p>	<p><b>Pipeline:</b></p> <p>Serbia Public Enterprise Restructuring DPL 2 (FY 16)</p> <p>Public expenditure and Utilities Reform DPL Series (2 operations) (FY 16 and FY 17)</p> <p>CAT DDO (FY 19)</p> <p><b>Proposed:</b></p> <p>Public Expenditure and PFM DPL or PforR (FY 17)</p>
ASSIST IN CREATING A MORE EFFECTIVE PUBLIC ADMINISTRATION & IMPROVING SELECT SERVICE DELIVERY	<p>Serbia Health Project (FY 14)</p>	<p><b>Pipeline:</b></p> <p>Public Sector Employment and Performance RBF (FY 16)</p> <p>CAT DDO (FY 19)</p> <p><b>Proposed:</b></p> <p>Public Expenditure and PFM DPL or PforR (FY 17)</p>	<p><b>On-going TA:</b></p> <p>Wage bill management TF (Public Sector Employment and Performance RBF)</p> <p>Right Sizing TA (IPA) (Public Sector Employment and Performance RBF)</p> <p>MDTF for Justice Sector Support</p> <p><b>Proposed TA and ASA:</b></p> <p>Per capita financing systems in social sectors (Public Sector Employment and Performance RBF)</p> <p>Policy management and implementation tracking assessment</p>

<b>MORE EFFICIENT POWER UTILITY</b>	Emergency Recovery Loan (FY 15)	<p><b>Proposed:</b></p> <p>Public expenditure and Utilities Reform DPL Series (2 operations) (FY 16 AND FY 17)</p> <p>Energy Sector Development Project (FY 18/19)</p> <p>IFC engagement on transport and utility sector PPPs, including on waste management in Belgrade</p>	<p><b>Ongoing TA:</b></p> <p>IFC Indicator Based Reform Advisory in ECA CFRR regional EU-REPARIS<sup>16</sup> program, and EQ-FINREP<sup>17</sup> country project</p> <p>Public Investment Management (Transport sector governance project, energy sector development project, Public Expenditure and PFM DPL)</p> <p><b>Proposed TA:</b></p> <p>WBIF western Balkans infrastructure facility</p> <p><b>Proposed ASA:</b></p> <p>Serbia Energy sector strategy (Energy Sector development project)</p> <p>Energy tariffs reform and impact on the Bottom 40 (Energy Sector Development Project)</p>
<b>MORE EFFICIENT PUBLIC TRANSPORT COMPANIES</b>	Corridor X project (FY 10) Road Rehabilitation Project (FY 13)	<p>Public expenditure and Utilities Reform DPL Series (2 operations) (FY 16 AND FY 17)</p> <p>Transport Sector Governance Project (FY 19/20)</p> <p>IFC engagement on transport and utility sector PPPs, including on waste management in Belgrade</p>	<p><b>Ongoing TA:</b></p> <p>IFC Indicator Based Reform Advisory in ECA CFRR regional EU-REPARIS<sup>18</sup> program, and EQ-FINREP<sup>19</sup> country project</p> <p>Public Investment Management (Transport sector governance project, energy sector development project, Public Expenditure and PFM DPL)</p> <p><b>Proposed TA:</b></p> <p>WBIF western Balkans infrastructure facility</p> <p><b>Proposed ASA</b></p> <p>Public Investment Management (Transport sector governance project, Energy Sector Development Project))</p>

<sup>16</sup> Road to Europe: program of accounting reform and institutional strengthening

<sup>17</sup> Enhancing quality of financial reporting

<sup>18</sup> Road to Europe: program of accounting reform and institutional strengthening

<sup>19</sup> Enhancing quality of financial reporting

<p><i>PRODUCTIVE SOE ASSETS TRANSFERRED TO PRIVATE OWNERSHIP</i></p>	<p>Serbia Public Enterprise Restructuring DPL 1</p>	<p><b>Pipeline:</b> Serbia Public Enterprise Restructuring DPL 2 (FY 16)</p>	
<p><i>CONTRIBUTE TO PRIORITY BUSINESS CLIMATE IMPROVEMENTS</i></p>	<p>IFC Southeast Europe Regional Tax and Transparency Project (2012 – 2015)</p>	<p><b>Pipeline:</b> Serbia Competitiveness and Jobs RBF (FY 16) IFC Investment to support Agribusiness/Trade and Supply Chain Second Competitiveness and Jobs Project (FY 20)</p>	<p><b>Ongoing TA:</b> IFC Indicator Based Reform Advisory in ECA IFC Western Balkans Agribusiness Competitiveness Program CFRR regional EU-REPARIS<sup>20</sup> program, and EQ-FINREP<sup>21</sup> country project TF funded CFRR Accounting and Auditing project IFC Debt Resolution Project</p>
<p><i>ASSIST IN THE CREATION OFA MORE STABLE AND MORE ACCESSIBLE FINANCIAL SECTOR</i></p>	<p>Climate Risk Insurance Facility (FY 12) Strengthening Deposit Insurance Agency Project (FY 14) IFC investments in state owned banks</p>	<p><b>Pipeline</b> IFC Western Balkans Debt Resolution and Business Exit Program Financial Sector Project (FY 17)) IFC support to privatization of state owned banks</p>	<p><b>Ongoing TA</b> Western Balkans Financial Sector TA (Financial Sector Project)</p>

<sup>20</sup> Road to Europe: program of accounting reform and institutional strengthening

<sup>21</sup> Enhancing quality of financial reporting

			<p>CFRR regional EU-REPARIS<sup>22</sup> program, and EQ-FINREP<sup>23</sup> country project</p> <p>Technical assistance on non-performing loans IFC banking sector assistance</p> <p><b>Proposed AAA:</b></p> <p>Financial Sector assessment (Financial Sector Project) Strengthening the out of court restructuring and insolvency framework</p>
<p><i>SUPPORT DEVELOPMENT OF MORE EFFICIENT LAND AND PROPERTY MARKETS</i></p>	Real Estate Management Project (FY 15)	<p>IFC Investment to support Asset Management Companies</p> <p>MIGA Real Estate Development Guarantee</p>	
<p><i>ENHANCED INFRASTRUCTURE NETWORKS</i></p>	<p>Corridor X Project (FY 10)</p> <p>Road Rehabilitation and Safety Project (FY 13)</p>	<p><b>Pipeline:</b></p> <p>Public expenditure and Utilities Reform DPL Series (2 operations) (FY 16 and FY 17)</p> <p>Transport Sector Governance Project (FY 19)</p> <p>Energy Sector Development Project (FY 18)</p> <p>IFC PPPs in infrastructure</p>	<p><b>Ongoing TA:</b></p> <p>Serbia--Supporting the Rail Policy Reform (Public Expenditure and Utilities reform DPL series and Transport Sector Governance project)</p> <p>IFC advisory support and financing of PPPs</p> <p>Public Investment Management (Energy Sector Development Project, Transport Sector Governance project, Public Expenditure and PFM DPL)</p> <p><b>Proposed TA and ASA</b></p>

<sup>22</sup> Road to Europe: program of accounting reform and institutional strengthening

<sup>23</sup> Enhancing quality of financial reporting

			<p>Serbia Energy sector strategy (Energy Sector development project)</p> <p>Public Investment Management (Transport sector governance project, Energy Sector Development Project))</p> <p>Energy tariffs reform and impact on the Bottom 40 (Energy Sector Development Project)</p>
<p><b>REDUCED BARRIERS TO LABOR MARKET PARTICIPTION</b></p>	<p>Serbia Public Enterprise Restructuring DPL 1 (FY 15)</p> <p>Serbia Innovation Project (IPA financed FY 12)</p> <p>Serbia Technology Transfer Project (IPA financed (FY 15))</p>	<p><b>Pipeline:</b></p> <p>Serbia Public Enterprise Restructuring DPL 2 (FY 16)</p> <p>Serbia Competitiveness and Jobs RBF (FY 16)</p> <p>Second Competitiveness and Jobs Project (FY 20)</p> <p><b>Proposed:</b></p> <p>Competitiveness 2 (FY 20)</p>	<p><b>Ongoing TA</b></p> <p>Step skill survey (Skills Project)</p> <p>Western Balkans Jobs TA (Competitiveness Project)</p> <p>Western Balkans Roma TA, including adolescent girls initiative (Skills Project)</p> <p><b>Proposed ASA:</b></p> <p>Innovations and growth (Competitiveness and Jobs RBF)</p> <p>Skills, employment and labor markets (Skills Project, Competitiveness and Jobs RBF))</p> <p>Educational Regional AAA (Skills Project)</p>

<p><i>ASSIST IN CLOSING MEDIUM AND SHORT TERM SKILL GAPS</i></p>	<p><b>Ongoing:</b></p> <p>Serbia Innovation Project (IPA financed, FY 12) Serbia Technology Transfer Project (IPA financed FY 15)</p>	<p><b>Proposed:</b></p> <p>Skills and Inclusive Education Project (FY 17)</p>	<p><b>Ongoing TA</b></p> <p>Step skill survey (Skills Project)</p> <p>Western Balkans Roma TA, including adolescent girls initiative (Skills Project)</p> <p><b>Proposed ASA:</b></p> <p>Skills, employment and labor markets (Skills Project, Competitiveness and Jobs RBF)</p> <p>Educational Regional AAA (Skills Project)</p>
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## ANNEX 4. INDICATIVE SEQUENCING OF IBRD LENDING\*

(FY16-21)

	Evolution of Portfolio and New Projects (in numbers)				
	FY16	FY17	FY18	FY19	FY20
<b>Portfolio</b>	6	7	8	8	8
<b>Closing Projects</b>	1	1	1	1	2
<b>New Projects</b>	2	2	1	1	1
<b>DPLs</b>	2	1	1	1	1
<b>Projects end of FY (excluding DPLs)</b>	7	8	8	8	7
	New Commitments (in US\$ million)				
<b>New indicative Commitment in FY (including DPLs)</b>	475	320	280	260	260
<b>Total Indicative Commitment at the end of FY (excluding DPLs)</b>	1047	779	609	629	719

\*Total indicative new commitment during the CPF period is US\$ 1.6 billion

## ANNEX 5. DEVELOPMENT PARTNERS IN SERBIA AND AREAS OF ENGAGEMENT

DEVELOPMENT PARTNERS	SECTORS															
	MACRO PFM	ENERGY	HEALTH	SOCIAL PROTECTION	WATER	AGRI	TRANSPORT	PUBLIC ADMIN	JUSTICE	LAND	URBAN	LOCAL GOV	NATURAL RESOURCES (ENVIRONMENT)	EDUCATION	PRIVATE SEC DEV	FINANCIAL SEC DEV
DENMARK		✓				✓			✓						✓	
EBRD		✓					✓						✓		✓	✓
EIB							✓							✓		
EU	✓	✓	✓	✓		✓	✓	✓	✓				✓	✓	✓	✓
GERMANY (GIZ & KfW)	✓	✓			✓			✓	✓	✓		✓	✓	✓	✓	✓
IMF	✓	✓						✓				✓				✓
NETHERLAND					✓	✓			✓				✓			
NORWAY								✓								
SLOVENIA									✓							
SPAIN							✓		✓				✓			
SWEDEN			✓						✓				✓			
SWITZERLAND	✓	✓	✓	✓				✓				✓			✓	✓
UK (DFID)									✓							
UN		✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	
USAID	✓						✓				✓	✓			✓	
WHO			✓				✓									
WB	✓	✓	✓	✓	✓		✓	✓	✓	✓		✓	✓	✓	✓	✓

**ANNEX 6. SORT**  
**(STANDARDIZED OPERATIONS RISK-RATING TOOL FOR SERBIA)**

<b>Risk Categories</b>	<b>Rating</b>
Political and governance	H
Macroeconomic	H
Sector strategies and policies	M
Technical design of project or program	M
Institutional capacity for implementation and sustainability	S
Fiduciary	M
Environment and social	H
Stakeholders	M
<b>Overall</b>	<b>Substantial</b>

## ANNEX 7. SELECTED INDICATORS OF BANK PORTFOLIO PERFORMANCE AND MANAGEMENT

As of date: 05/11/2015

Indicator	2012	2013	2014	2015
<b>Portfolio Assessment</b>				
Number of Projects Under Implementation <sup>a</sup>	8	5	6	8
Average Implementation Period (years) <sup>b</sup>	6.6	4.7	3.4	2.3
Percent of Problem Projects by Number <sup>a, c</sup>	12.5	60.0	16.7	12.5
Percent of Problem Projects by Amount <sup>a, c</sup>	5.8	73.2	3.2	2.1
Percent of Projects at Risk by Number <sup>a, d</sup>	12.5	60.0	16.7	12.5
Percent of Projects at Risk by Amount <sup>a, d</sup>	5.8	73.2	3.2	2.1
Disbursement Ratio (%) <sup>e</sup>	23.2	17.8	18.6	31.0
<b>Portfolio Management</b>				
CPPR during the year (yes/no)				
Supervision Resources (total US\$)				
Average Supervision (US\$/project)				

Memorandum Item	Since FY 80	Last Five FYs
Proj Eval by OED by Number	27	8
Proj Eval by OED by Amt (US\$ millions)	916.4	273.8
% of OED Projects Rated U or HU by Number	11.1	37.5
% of OED Projects Rated U or HU by Amt	3.4	11.4

a. As shown in the Annual Report on Portfolio Performance (except for current FY).

b. Average age of projects in the Bank's country portfolio.

c. Percent of projects rated U or HU on development objectives (DO) and/or implementation progress (IP).

d. As defined under the Portfolio Improvement Program.

e. Ratio of disbursements during the year to the undisbursed balance of the Bank's portfolio at the beginning of the year: Investment projects only.

\* All indicators are for projects active in the Portfolio, with the exception of Disbursement Ratio, which includes all active projects as well as projects which exited during the fiscal year.

## ANNEX 8. OPERATIONS PORTFOLIO (IBRD/IDA AND GRANTS)

As of date: 05/11/2015

Closed Projects 35

<u>IBRD/IDA *</u>	
Total Disbursed (Active)	330.58
of which has been repaid	2.26
Total Disbursed (Closed)	1,162.33
of which has been repaid	154.87
Total Disbursed (Active + Closed)	1,492.91
of which has been repaid	157.13
Total Undisbursed (Active)	834.15
Total Undisbursed (Closed)	2.33
Total Undisbursed (Active + Closed)	836.48

### Active Projects

Project ID	Project Name	<u>Last PSR</u>		Fiscal Year	<u>Original Amount in US\$ Millions</u>			Cancel.	Undisb.	<u>Difference Between Expected and Actual Disbursements<sup>a/</sup></u>	
		Supervision Rating			IBRD	IDA	GRANT			Orig.	Frm Rev'd
		<u>Development Objectives</u>	<u>Implementation Progress</u>								
P092999	BOR REG DEVT	U	U	2007	33	10	17.74938272	15.29465	33.229442		
P108005	CORRIDOR X HIGHWAY PROJECT	MS	MS	2010	388			186.6399	197.29948	68.19072	
P146248	Deposit Insurance Strengthening Project	S	S	2014	200			49.21783			
P152018	Floods Emergency Recovery Project	#	#	2015	300			299.25	152.70933		
P147050	Real Estate Management Project	#	#	2015	44				44		
P127876	ROAD REHABILITATION AND SAFETY PROJECT	MS	MS	2013	100			99.75	24.605457	1.438791	
P129539	Serbia Health Project	S	S	2014	40				40	1.3333333	
P127408	YF First SOE Reform DPL	#	#	2015	100				100		
Overall Result					1205	10	17.74938272	834.1523	275.25248	69.62951	

## ANNEX 9. STATEMENT OF IFC'S COMMITTED AND OUTSTANDING PORTFOLIO

Amount in US Dollar Millions  
Accounting Date as of: 03/31/2015

FY Approval	Company	Committed					Disbursed Outstanding				
		Loan	Equity	**Quasi Equity	*GT/RM	Partici pant	Loan	Equity	**Quasi Equity	*GT/RM	Partici pant
8/12/2006	Banca intesa beo	0	57.13	0	0	0	0	57.13	0	0	0
2011	Cacanska banka	2.3	8.91	0	0	0	2.3	8.91	0	0	0
0	Camex	8.79	0	0	0	0	8.79	0	0	0	0
2011	Eurobank serbia	8.25	0	0	0	0	8.25	0	0	0	0
2011	Farmakom m.b.	42.96	0	0	0	32.22	42.96	0	0	0	32.22
0	Grand prom	11.01	0	0	0	0	11.01	0	0	0	0
0	Ivicom	0	0	3.19	0	0	0	0	0	0	0
1985	Jugobanka	0	0	0	0	0	0	0	0	0	0
2012/15	Komercijalna bg	16.11	0	53.7	0	0	16.11	0	53.7	0	0
2010	Kronospan srb	13.88	0	0	0	0	13.88	0	0	0	0
2012	Mk doo	30.76	0	0	0	0	30.76	0	0	0	0
2012	Pmc automotive	19.09	0	0	0	0	19.09	0	0	0	0
0	Porr jagodina	0	0	1.43	0	0	0	0	1.43	0	0
0	Porr leskovac	0	0	1.58	0	0	0	0	1.58	0	0
2010	Procredit serbia	3.07	0	0	0	0	3.07	0	0	0	0
2005/12	Unicredit bank	42.91	0	0	0	0	42.91	0	0	0	0
2013	Victoria group	61.22	0	0	0	0	61.22	0	0	0	0
2012	Vino zupa	13.43	0	0	0	0	13.43	0	0	0	0
1987	Vojvodjanska	0	0	0	0	0	0	0	0	0	0
<b>Total Portfolio:</b>		<b>273.78</b>	<b>66.04</b>	<b>59.9</b>	<b>0</b>	<b>32.22</b>	<b>273.78</b>	<b>66.04</b>	<b>56.71</b>	<b>0</b>	<b>32.22</b>

\* Denotes Guarantee and Risk Management Products.

\*\* Quasi Equity includes both loan and equity types.