Report Number: ICRR0022398

1. Project Data

Country
Serbia

Practice Area (Lead)
Macroeconomics, Trade and Investment

Programmatic DPL
Planned Operations: 2
Approved Operations: 2

Operation ID
P155694

Operation Name
Public Exp. and Utilities DPL1

L/C/TF Number(s)
IBRD-86940

Closing Date (Original)
31-Mar-2018

Total Financing (USD)
207,515,267.85

Bank Approval Date
18-Jan-2017

Closing Date (Actual)
31-Mar-2018

	IBRD/IDA (USD)	Co-financing (USD)
Original Commitment	200,000,000.00	0.00
Revised Commitment	200,000,000.00	0.00
Actual	207,515,267.85	0.00

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Operation ID
P161184

Operation Name
Public Exp. & Public Utilities DPL2 (P161184)

L/C/TF Number(s) IBRD-86940,IBRD-88310	**Closing Date (Original)** 30-August-2019	**Total Financing (USD)** 182,547,856.98
Bank Approval Date 20-Mar-2018	**Closing Date (Actual)** 30-August-2019	

	IBRD/IDA (USD)	Co-financing (USD)
Original Commitment	200,000,000.00	0.00
Revised Commitment	200,000,000.00	0.00
Actual	182,547,856.98	0.00

2. Program Objectives and Pillars/Policy Areas

a. Objectives

The PEPU-DPL Series had the following objectives: (A) Improve public expenditure management through strengthened public financial management and public administration reform; (B) Improve the financial sustainability and efficiency of energy sector public enterprises; and, (C) Improve the financial sustainability and efficiency of transport sector public enterprises and state-owned companies. (PD DPL1, 2016, pp.1-2; and PD DPL2. 2018, pp. 1-3).

For the purpose of this Review, we have unpacked these into four objectives:

- **Objective One:** Strengthen public financial management to improve public expenditure management;
- **Objective Two:** Public administration reform to improve public expenditure management;
- **Objective Three:** Improve financial sustainability and efficiency of energy sector public enterprises; and,
- **Objective Four:** Improve the financial sustainability and efficiency of transport sector public enterprises and state-owned companies.

b. Pillars/Policy Areas

The PEPU-DPL Series was structured around four pillars/policy areas that were identical to the four objectives above.

Pillar I had two prior actions (PD, DPL1, Table Annex 1, p.38; and PD, DPL2, p. 13).

- PA #1 (DPL1): The Ministry of Finance adopted the framework for monitoring the implementation of the

Law on Deadlines for Payments in Commercial Transactions, which has been revised to include public-public transactions, including those of state-owned enterprises.
- PA #2 (DPL2): The Borrower has: (a) issued the Decree on Work and Role of Budget Inspection, to strengthen the budget inspection supervision and enforcement function. (b) adopted the Public Internal Financial Control (PIFC) Strategy and its associated action plan, to provide a framework for planned future developments of financial management and control and internal audit functions; and (c) through its Ministry of Finance, amended the Rulebook on the Budget Execution System, in order to ensure that accurate, complete and up-to-date information on budget commitments are available at the time when budget commitments are incurred.

Pillar II had three prior actions (PD, DPL1, Table Annex 1, p.38; and PD, DPL2, pp. 15-16).

- PA #3 (DPL1): Borrower adopted the Law on the Ceiling on Public Sector Employees setting the criteria of determining the maximum number of employees in the public sector, from 2015 to 2018, as well as the scope and limits for reducing their number in order to achieve the established said maximum; and (b) established, as required by said law, the first institution-level limits on the number of employees in the public sector.
- PA #4 (DPL1): The Borrower adopted the Law on the Salary System of Public Sector Employees to rationalize the public sector pay structure.
- PA #5 (DPL2): The Borrower has: (a) amended the Law on Public Sector Employees Salary System. (b) enacted the Law on Employees in Public Services; and (c) enacted the Law on Salaries of Employees in Bodies of Local Sub-Government Units and Provincial Authorities, all with the objective to provide the legal framework for the mapping of positions between the Public Sector Jobs Catalogue and the new pay grades set forth in the Law on Public Sector Employees Salary System.

Pillar III had five prior actions (PD, DPL1, Table Annex 1, p.39; and PD, DPL2, p. 19-21).

- PA #6 (DPL1): The Borrower: (a) through its Council of the Energy Agency, approved a 3.8 percent increase of the electricity tariff for guaranteed supply; (b) amended the Energy Vulnerable Customers Program to increase coverage of targeted beneficiaries; and, (c) increased the budget for said program.
- PA #7 (DPL2): The Borrower, through the Council of the Energy Agency, has approved an increase of the electricity tariff for guaranteed electricity supply in calendar year 2017 and continued to protect vulnerable households from such electricity tariff increase by increasing the number of beneficiaries of the Energy Vulnerable Customers Program in calendar year 2017 compared to calendar year 2016.
- PA #8 (DPL1): The Borrower, through the Supervisory Board of *Elektroprivreda Srbije* (EPS) (state-owned electricity company): (a) adopted a labor optimization plan for 2016-2019 setting out the medium-term targets, process, compensation packages, selection criteria, grievance mechanisms and timeline for reductions in staffing; and (b) issued the first call for voluntary separations to implement the 2016 target for net staff reduction.
- PA #9 (DPL2): The Borrower, through the Supervisory Board of *Elektroprivreda Srbije* (EPS) has: (a) updated the labor optimization plan for calendar year 2017, including annual targets, compensation packages, eligible categories, selection criteria, and grievance mechanisms for EPS; and (b) issued the second call for voluntary separations.
- PA #10 (DPL1): The Borrower adopted a financial consolidation plan for *Srbijagas* (state-owned gas company) that defines measures to increase revenues and reduce costs.

Pillar IV had five prior actions (PD, DPL1, Table Annex 1, p.40; PD, DPL2, pp. 25-27).

- PA #11 (DPL1): The Borrower: (a) implemented a new framework for railways financing through conclusion of the track access contracts between the state-owned infrastructure rail company and the state-owned freight and passenger rail companies and approving a public service obligation agreement; and (b) adopted new performance criteria for the state-owned infrastructure, freight and passenger rail companies.
- PA#12 (DPL1): The Borrower: (a) through the Decisions of the General Assemblies of the respective railway companies, adopted labor optimization plans for 2016-2020 setting out the medium-term targets, process, compensation packages, selection criteria, grievance mechanisms and timeline for reductions in staffing; and (b) through the management of the respective railways companies, initiated the 2016 target for staff reduction by communicating to the companies' respective employees the option for their participation.
- PA #13 (DPL2): The Borrower, through each Railway Company has a) updated its labor optimization plan for calendar year 2017, including the annual targets, eligibility criteria, compensation packages, and grievance mechanisms; and (b) achieved the targets for calendar year 2017 set forth in said labor optimization plan.
- PA #14 (DPL2): The Borrower: (a) implemented a new framework for railways financing through conclusion of the track access contracts between the state-owned infrastructure rail company and the state-owned freight and passenger rail companies and approving a public service obligation agreement; and (b) adopted new performance criteria for the state-owned infrastructure, freight and passenger rail companies.
- PA #15 (DPL2): The Borrower, through PERS, has prepared and approved a framework for a service level agreement to be entered with MCTI, for purposes of a) defining the performance standards for different road classes, based on pavement conditions, operational standards, and safety;(b) require the Borrower, through MCTI to provide an agreed financing for roads to achieve the agreed performance standards; and (c) holding PERS accountable for agreed performance standards.

c. Comments on Program Cost, Financing and Dates

The PEPU-DPL Programmatic Series consisted of two IBRD loan operations: DPL1, which was approved for USD 200 million, disbursed USD 207.5 million; and DPL2, which was also approved for USD 200 million but disbursed USD 182.5 million. Differences between approved and disbursed amounts were due to changes in the USD/EUR exchange rate.

DPL1 was approved on January 18, 2017 and became effective on May 29, 2017 and closed on March 31, 2018 as originally scheduled. DPL2 was approved on March 20, 2018 and became effective on July 10, 2018, and closed on August 30, 2019, as originally scheduled.

3. Relevance of Design

a. Relevance of Objectives

The objectives were highly relevant to country conditions, the government's strategy and the Bank-supported country strategy at appraisal and closing.

The country was facing a mounting fiscal and debt crisis. After a long period of stop-and-go reform in 2014, a new government was elected in part on a platform to implement major fiscal consolidation and to reverse adverse debt dynamics. It also aimed to initiate structural reforms to improve the efficiency of large state-owned enterprises. Public debt had reached almost 76 percent of GDP at end-2015, more than a 30-percentage point increase since 2010, reflecting unsustainable increases in public sector wages and pensions and direct and indirect subsidies to overstaffed, inefficient, loss-making state-owned enterprises (SOEs). The government agreed with the IMF on a Stand-By Arrangement and began implementing difficult fiscal consolidation. By 2016, the fiscal deficit was reduced to 1.2 percent of GDP (from 6.7 in 2014 and 3.5 in 2015) and public debt began to decline but there remained a large fiscal and SOE reform agenda.

The objectives dovetailed with the government's National Economic Reform Program and the Fiscal Strategy for 2016-18, which emphasized medium-term fiscal consolidation and a reduction of public debt to below 50 percent of GDP. Building on short-term improvement in the control of the wage bill in 2015, which saw a reduction in public sector wages and freeze on government employment, the Strategy outlined further ambitious fiscal reforms that included restructuring of large SOEs, rationalizing their employment, and strengthening their financial positions. Both government strategies were anchored in the EU membership accession process. Finally, the PEPU-DPL Series' objectives aimed to contribute to the first focus area of the Bank Group's Country Partnership Framework (CPF) for the period 2016-2020 on economic governance and the role of the state. The Series directly supported CPF objectives on sustainable management of public spending, effective public administration, and improved service delivery, efficient and sustainable public power sector and transport companies. CPF focus areas and objectives reflected Systematic Country Diagnostic's identified constraints, which included fiscal sustainability and financial and overall macro stability, strengthening government capacity and institutions, and SOE reform.

b. Relevance of Prior Actions

Rationale

The theory of change was credible with prior actions clearly linked to and expected to contribute to the objectives. Assumptions behind prior actions appear sound; electricity tariff adjustment was expected to lead to higher revenues to improve the financial position of the electricity company. The poverty impact of this action was appropriately mitigated by the expansion of a relevant social protection program. By limiting the future fiscal and quasi-fiscal transfers to the energy companies, the reforms helped increase fiscal space that could be used to increase social spending and productive public investments. Similarly, prior actions on a new framework for financing railways and performance standards, in conjunction with other actions, contributed to improving financial performance of railways, limiting fiscal risks to the budget.

Prior actions

Pillar I – Strengthen public financial management to improve public expenditure management

PA #1 (DPL1) addressed the long-standing and politically difficult public-public arrears problem, which undermined fiscal and financial discipline and the quality of PFM. It was a difficult measure to adopt and it potentially had a large impact on the objective of strengthening public financial management to improve expenditure management. The prior action aimed to contribute to the objective of improving public financial management and expenditure management by limiting fiscal risks from these arrears to the budget, improving aggregate fiscal discipline and public resource allocation as well as public service delivery in public administration, energy and transport sectors. This prior action contributed to this objective through the implementation of the amended Law Deadlines for Payments in Commercial Transactions ("RINO Law"), specifically through the adoption of the monitoring framework. (Relevance of PA #1: HS).

PA #2 (DPL2) expanded the monitoring framework for arrears by focusing on lagging elements of the public financial management system. The arrears problem was multifaceted and required not only a monitoring framework but also strengthening of government capacity and supporting mechanisms for monitoring and management of arrears through better supervision and financial management controls, and tighter requirements to register arrears. (Relevance of PA #2: HS).

The relevance of the prior actions under the Pillar I is judged to be highly satisfactory.

Pillar II -- Public administration reform to improve public expenditure management

PA#3 (DPL1) aimed to address poor management of public employment and the public sector wage bill to support long-term fiscal consolidation and efficiency of the public sector. The lack of effective control on employment and wages led to a rising public sector wage bill, undermining efforts for fiscal consolidation. To address it, the Law on Ceiling on Public Sector Employees was enacted to provide staffing ceilings for individual government institutions. (Relevance of PA3: S).

PA#4 (DPL1) streamlined the legislative framework for public sector pay and employment. Serbia's previous system of public sector pay and employment was excessively complex, with "71 different elements of remuneration, 16 different base salaries, 900 job coefficients and more than 2,200 job titles." The adoption of the umbrella Law on the Salary System of Public Sector Employees rationalized the public sector pay structure. A single spine pay system was expected to improve transparency, equity, predictability, and control by ensuring that equal positions across different occupations are paid equal wages. The prior action targeted an important fiscal challenge and its contribution to the public administration reform was expected to be significant. (Relevance of PA#4: S).

PA#5 (DPL2) moved these reforms further along the results chain by supporting amendments to the Law on the Salary System of Public Sector Employees and enactment of two laws on employment in public services and subnational governments, which helped establish an effective pay grading system within a unified legal framework (Relevance of PA#5: S).

The relevance of prior actions under the Pillar II are judged to be satisfactory.

Pillar III -- *Financial sustainability and efficiency of energy sector public enterprises*

PA#6 (DPL1) addresses the underpricing of electricity, which was at the root of financial losses of the state electricity company EPS. Without tariff adjustments, no improvement in the financial position of the EPS was possible. This was part of the EPS medium-term financial consolidation plan and contributed to limiting fiscal risks to the budget from EPS's inability to service state guarantee loans, which were a significant contingent liability for the budget. The action allowed EPS to cover 95 percent of operating costs; as such, it could be expected to significantly improve the financial sustainability and efficiency of EPS. To cushion the impact on the poor, the action doubled the budget allocation for targeted social assistance, expanded targeted households from 60,600 to 80,500, and increased coverage of poor households under the Energy Vulnerable Customers (EVC) Program. The increase in tariff was critical to addressing the poor financial performance of EPS and the EVC measure addressed its impact on the poor. (Relevance of PA#6: HS).

PA#7 (DPL2) extended the measures from PA#6 to 2017: tariff increased was approved for 2017 calendar year and it further increased coverage of targeted beneficiaries for the protection of the poor in 2017. The value added was that tariff increases would be approved on an annual basis. In this case, the social element of tariff increases—enhanced coverage of vulnerable households—was also extended. (Relevance of PA#7: S).

PA#8 (DPL1) directly addressed overstaffing and the adequacy of the EPS workforce, the other critical component of EPS restructuring and financial consolidation. EPS had a significant surplus of employees when benchmarked with similar companies in the region. It was estimated that 15 percent of its workforce was redundant (PD, DPL1, p.20). The action ensured that EPS Supervisory Board: (a) adopted a labor optimization plan for 2016-2019 setting out medium-term targets, processes, compensation packages, selection criteria, grievance mechanisms and a timeline for reductions in staffing; and, (b) issued the first call for voluntary separations to implement the 2016 target for net staff reductions. The plan featured a combination of natural attrition and voluntary reduction of employment with incentives and involuntary separation with severance pay in a subsequent stage. (Relevance of PA#8: S).

PA #9 (DPL2) extended the EPS labor optimization measures of PA#8 to calendar year 2017, also setting annual targets, compensation packages, eligible categories, selection criteria, and grievance mechanisms for EPS; and issued the second call for voluntary separations. While the PA#8 resulted in the adoption of the medium-term optimization plan and started the call for voluntary separations, this needed to be followed by annual actions. (Relevance of PA#9: S).

PA#10 (DPL1) targeted the financial turnaround and financial sustainability and efficiency of the other large energy company, *Srbijagas* (state natural gas company), which was among the largest loss -makers in the country with short-term liabilities to the government of about 3.3 percent of government revenues in 2015. The underlying problems were multiple: lack of financial discipline and low collection, excessive debt, and weak internal controls, among others (PD, DPL1, p.22, paragraphs 56-57). The prior action targeted adoption of a comprehensive financial consolidation plan for *Srbijagas* that defined measures to increase revenues and reduce costs on a sustainable basis. (Relevance of #PA: S).

The relevance of prior actions under Pillar III is judged to be satisfactory**.**

Pillar IV -- Financial sustainability and efficiency of transport sector public enterprises and state-owned companies

PA #11 (DPL1) targeted the Railways company's poor financial performance underpinned by low labor productivity and traffic intensity, overstaffing, and overdue investment in upgrading the network; these issues also reflected lack of clarity about track access and performance criteria for both freight and passenger rail companies. This action had the government implement a new framework for railways financing through conclusion of the track access contracts between the state-owned infrastructure rail company and the state-owned freight and passenger rail companies and approve a public service obligation agreement; and adopt new performance criteria for the state-owned infrastructure, freight and passenger rail companies. (relevance of PA#11: S).

PA#12 (DPL1) sought to address overstaffing and arbitrariness in employment practices of the Railways company. The action sought to adopt (a) labor optimization plans for 2016-2020 with medium-term targets, process, compensation packages, selection criteria, grievance mechanisms and timeline for reductions in staffing; and (b) initiate the 2016 target for staff reduction by communicating to the companies' respective employees the option for their participation. The action, if implemented, was expected to lead to a 30 percent reduction in staffing by 2020 compared with 2014 (PD, DPL1, p.26, paragraph 67). (Relevance of PA#12: S).

PA #13 (DPL2) extended the PA#12 which was the adoption of the medium-term optimization plan by updating the Railways company's labor optimization plan for 2017, including the annual targets, eligibility criteria, compensation packages, and grievance mechanisms; and by achieving the targets for 2017 set forth in the plan. Each year, the annual plan must be updated in view of actual progress with implementation. (Relevance of PA#13: S).

PA #14 (DPL2) aimed to support the restructuring of the Railways via new contractual framework for railway operating companies through track access charges and public service obligation for the infrastructure and passenger railway companies respectively. This was an important component of reform because these obligations helped the government limit budgetary financing to the companies. (Relevance of PA#14: S).

PA #15 (DPL2) was targeting improvements in the policy framework for company *Putevi Srbije* that manages national road and tolled motorway network. The budget was providing substantial transfers to the company without clear and monitorable service agreements and standards. The action approved a framework for a service-level agreement to be entered into with the Ministry of Construction, Transportation and Infrastructure (MCTI) for purposes of a) defining the performance standards for different road classes;(b) requiring the Borrower, through MCTI to provide agreed financing to achieve the agreed performance standards; and (c) holding PERS accountable for agreed performance standards. The results chain was relatively clear but required a number of actions for it to contribute to the improvement in the financial position of the road company, including that newly defined standards are implemented as verified by appropriate checks or audits and the financing is used in line with allocations. (Relevance of PA#5: MS).

The relevance of prior actions under Pillar IV is judged to be satisfactory.

With the relevance of prior actions under the first pillar highly satisfactory, under the second, third and fourth pillar satisfactory, overall rating for relevance of prior actions is satisfactory.

Rating

Satisfactory

4. Relevance of Results Indicators

Description of RIs by Pillar, the PAs they support, baseline and target values, and status

RI (number and description)	Associated PA	Baseline/target	Status[1]
Pillar 1: Improved public expenditure management through strengthened public financial management			
RI1: share of executed payments for public to public commercial transactions which were previously registered as commitments within deadlines prescribed by legislation	PA1, PA2	Baseline (2015): 60 percent Target (2018): 90 percent	Actual (2019): 95.4 Actual (2018): 95.8
Pillar 2: Improved public expenditure management through public administration reform			
R2: number of employees in the public sector, as determined by the Law on the Ceiling on Public Sector Employees, does not exceed the total of institutional-level limits set under the Law and its decisions	PA3	Baseline (2015): exceed limit Target (2018): does not exceed limit	Actual (2018): does not exceed limit
R3: share of positions within education, health and social protection sectors mapped to new grades.	PA3, PA4, PA5	Baseline (2015): 0 Target (2018): 75 percent	Actual (2018): 0 percent.
Pillar 3: Improve the financial sustainability and efficiency of energy sector public enterprises			
R4: convergence of the guaranteed electricity supply tariff to reach market parity level.	PA6, PA7	Baseline (end-2015): 64 percent of market parity Target (end-2018): 80 percent of market parity	Actual (2019): 77.3 percent Actual (2018): 55.8 percent
R5: number of total beneficiaries of the Energy Vulnerable Program.	PA6, PA7	Baseline (2014): 60,000 households, of which 27 percent were female headed Target (2018): 70,000 households, of which 30 percent were female headed households.	Actual (2018): 76,604 households, of which 53 percent female headed households

[1] If the RI has been dropped prior to the final approved operation in the series, note "Dropped" in place of "actual."

RI6: increase in the share of the EPS workforce with education above secondary-level.	PA7, PA8, PA9	Baseline (2015): 0 Target (2018): 5 percent	Actual (2019): 4.2 percent Actual (2018): 3.4 percent
RI7: Srbijagas' collection rate of current receivables.	PA10	Baseline (2015): 80 percent Target (average for 2016-18): 87 percent.	Actual (2019): 91.8 Actual (2018): 92.3 percent (average 2016-18)
RI8: Approval of 10-year development plan of the Gas Transport Operator and 5-year development plan of the Distribution System Operator, which were in accordance with the adopted economic and financial appraisal methodology.	PA10	Baseline (2016): No Target (2018): Yes	Actual (2018): No
Pillar 4: Improve the financial sustainability and efficiency of transport sector public enterprises			
RI9: level of annual direct budget operational support to the Railways Companies.	PA14	Baseline (2015): RSD 13.5 billion Target (2018): RSD11 billion	Actual (2019): RSD 13.04 billion. Actual (2018): RSD 11.29 billion
RI10: labor productivity (measured by train kilometers per employee) and in asset utilization (measured by passengers per kilometer of track and ton per kilometer of track).	PA11, PA14	Baseline (2015): zero Target (2018): 15 percent (for both indicators)	Actual (2019): 80 (labor productivity), 10 percent (cargo), and 15 percent (track utilization). Actual (2018): 19 (labor productivity), 27 percent (cargo), and 3 percent (track utilization).
RI11: Reduction in the annual wage bill of Railways companies.	PA12, 13	Baseline (2015): zero Target (2018): 25 percent.	Actual (2019): 25 percent (from 2016 base) Actual (2018): 23 percent (from 2016 base)
RI12: Progress with government in agreeing with *Putevi Srbije* (Roads of Serbia) on performance levels for the different road classes with associated guaranteed funding levels committed.	PA15	Baseline (2016 budget): No Target (2019 budget): Yes	Actual (2018): No

Rationale

Indicators under Pillar 1

RI1 was clearly stated and outcome oriented, with clear baseline and target and directly related to the objective of strengthening PEM and PFM. It was also impacted by PA #1 and #2 on payment arrears. While this was only one indicator measuring progress in this area, it was important and relevant given the pervasive problem of arrears. (Relevance of RI1=S).

The relevance of Results Indicator measuring achievement of Pillar I is judged to be satisfactory.

Indicators under Pillar 2

RI2 is a clearly measured achievement of PA #3 establishing the ceiling on public sector employees. It was linked in a clear results chain from the objective two on public administration reform via prior action #3 to RI2, which is in turn is the same as DLI3 in the parallel operation, the Modernization and Optimization of Public Administration Program for Results (PforR). (Relevance of RI2: S).

RI3 was somewhat revised under DPL2, moving the emphasis from paid wages to mapping of positions to new pay grade system). RI3 is linked to the PA#3, PA#4, and PA#5, and objective two. The revised indicator and target were similar to and incentivized by DLI1 in the PforR (Relevance RI3: S).

The relevance of Results Indicator measuring achievement of Pillar II is judged to be satisfactory.

Indicators under Pillar 3

RI4 was conceptually linked with PA#6 and PA#7. However, “market parity levels” were not uniquely defined and subject to interpretation. A quantitative target measuring cost recovery, for example, would have been less ambiguous than market parity. This was a weakness in the definition and design of this indicator, as also noted in the ICR. (Relevance of RI4: MS).

RI5: The target for 2018 was revised down under DPL2 to 70,000 households, of which 30 percent were female headed households. It measured well the impact of PA#6 and #7 that sought to cushion the impact on the poor of increases in electricity prices by expanding the social protection program for vulnerable households. It also measures well the progress towards the achievement of objective 3. Definition of RI5 is clear and data on vulnerable households available. Relevance of RI5: S).

RI6 was revised under DPL2 from the original *reduction in annual EPS wage bill relative to 2014 from baseline zero to 10 percent in 2018*. RI6 aimed to measure the impact of PA#7 and PA#8 establishing and implementing labor optimization plan to reduce substantial excess employment in EPS. Part of the optimization plan also dealt with the adequacy of the workforce but this was not the primary aim of the PAs 6-7. In that regard, RI6 does not measure the impact on EPS employment or wage bill. It does not directly measure progress towards strengthening financial sustainability and efficiency of EPS. In that regard, the original formulation of RI6 was more relevant than the revised version. (Relevance of RI6: MU).

RI7: This indicator measured adequately the impact of PA# 10 on the adoption of the financial consolidation plan of *Srbijagas* with respect to collection of revenues. It is recognized as an important step towards actual strengthening of financial position of the company. However, it does not fully measure the impact on cost, past-due receivables, nor improving the company’s overall financial position. In that regard, the indicator is partial and an intermediate outcome sought by the action. Also, it measures only one dimension of progress towards objective 3 with respect to the financial sustainability and efficiency of the company. The indicator is clearly defined. (Relevance of RI7: MS).

RI8 measures an input. Its measurement of the impact of the financial consolidation plan of *Srbijagas* is indirect and ambiguous. It is unclear how much it measures progress towards the objective 3 of strengthening financial sustainability of energy companies. On the other hand, it does show a link with unbundling of distribution systems and modernization of the company, which could lead to lower distribution losses. (Relevance of RI8: MU).

The relevance of Results Indicators measuring achievement of Pillar III is judged to be moderately satisfactory.

Indicators under Pillar 4

RI9 measured the impact of PA#14, which aimed to established new contractual framework for access to tracks and public service obligations that would allow rationalizing of the budget support. Performance criteria for these enterprises were also adopted. These were structural changes expected to lead to improved financial performance and, therefore, reduced budget support on a sustained basis. (Relevance of RI9: S).

RI10 measured improvements in labor productivity (measured by train kilometers per employee) and in asset utilization (measured by passengers per kilometer of track and ton per kilometer of track) relative to 2015, The indicator was well defined and measured impact of prior action (PA#14) and contributed to objective 4 in a logical chain, leading from the improvement in labor productivity, asset utilization and passengers carried that measured the impact of the new financing framework and performance criteria, contributing improving financial sustainability and efficiency of the company. (Relevance of RI10: S)

RI11 aims to measure impact of PA#12. It is clearly defined with baseline and target but the indicator could have been strengthened if it was based on data from the audited financial statements. However, such statements were unavailable so annual financial reports of the company were used as the data source (Relevance of RI11: S.).

RI12 is qualitative, and more in the nature of action than an indicator measuring impact of PA#15. It is unclear the extent to which the indicator measures progress towards objective 4 of financial sustainability and efficiency of public transport companies. (Relevance of RI12: MU).

The relevance of Results Indicators measuring achievement of Pillar IV is judged to be satisfactory.

Given the satisfactory relevance of indicators under the first and second pillars and moderately unsatisfactory under the third, and satisfactory under the fourth pillar, overall relevance of RIs is judged **satisfactory**.

Rating

Satisfactory

5. Achievement of Objectives (Efficacy)

OBJECTIVE 1

Objective: Strengthen public financial management to improve public expenditure management

Supported by PAs 1- 2
Progress measured by RIs 1.

Rationale

The share of executed public-to-public transactions increased strongly, exceeding the target, and laying the foundation for improved payment discipline and stronger public financial and public expenditure management. Achievement of RI1 target is rated ***High.***

As a result, the achievement of Objective 1 is judged to be ***Highly Satisfactory***.

Rating

Highly Satisfactory

OBJECTIVE 2

Objective: Public administration reform to improve public expenditure management;

Supported by PAs 3, 4 and 5
Progress measured by RIs 2 and 3

Rationale

The achievement under this objective was limited. On the positive side, the number of employees in the public sector, as determined by the Law on the Ceiling on Public Sector Employees, did not exceed the total of institutional-level limits set under the Law and its decisions, which prevented continuation of excessive employment in the public administration; this contributed to the preconditions for public administration reform. (The target for RI2 was fully achieved—***High***.). However, the broad intention of this reform--that public sector employment is matched with skills needed for efficient administration and professional requirements -- was not achieved in part because reduction of employment was not targeted but voluntary, due to political constraints. This resulted in the departure of skilled staff and the emergence of skills shortages in some parts of the public sector. This reform has not progressed during the pandemic (2020), which shifted government priorities. Both RIs were supported by similar DLIs in the PforR. (RI3 achievement was ***Negligible)***.

With one achievement of the targets for one indicator High and one Negligible, overall achievement of this objective is judged to be ***Moderately satisfactory***.

Rating

Moderately Satisfactory

OBJECTIVE 3

Objective: Improve the financial sustainability and efficiency of energy sector public enterprises;

Supported by PAs 6, 7, 8, 9, and 10
Progress measured by RIs 4, 5, 6, 7, and 8

Rationale

Objective 3 was supported by PAs targeting an increase in electricity tariffs (PA#6 and 7), employment rationalization of EPS (PA#8 and 9), and the adoption of the financial consolidation plan by *Srbijagas* (PA#10). Overall, the achievement under this objective was very limited with most indicators falling short on achievement and some on relevance as well. The main example is that planned increase in the guaranteed electricity supply tariffs--which was the key measure necessary for the improvement of the financial position of the electricity company--fell short of the target (RI4 achievement was rated ***Modest***.).

The increase in the share of the workforce of the EPS was neither achieved nor particularly relevant as it did not adequately capture the impact of the PAs nor would its achievement be reasonably expected to contribute to Objective 3. Moreover, recent analysis of EPS financial performance by Serbia's fiscal watchdog agency, Fiscal Council, indicates that overall financial performance during 2015-18 did not improve, that operating profitability remains extremely low and that the company lacks significant resources to ensure adequate operations and maintenance and basic investments needed to maintain the capital stock, its medium term plan. (Fiscal Council, "Analysis of Operational Performance and Recommendations for Reform and Investments," 14, 2019). Achievement of RI7 is judged ***Negligible.***

The collection rate of the *Serbiagas* did increase, exceeding the target but this indicator did not adequately capture the impact of the PA nor overall improvement in financial sustainability and efficiency of the company. Exogenous factors, including falling natural gas prices during the period 2015-19, might have also provided incentives for commercial and household customers to increase their payments and, therefore, collection rates. Therefore, it is not clear that the improvement in the collection rate can be fully, or even partially, attributed to the internal improvement in efficiency of collection, which could then contribute to the overall efficiency sought by the Objective 3. For these reasons, despite nominal achievement, this indicator is judged ***Modest***.

The approval of development plans were neither particularly relevant, nor were they achieved. Plans alone do not imply an improvement in the financial sustainability nor gains in efficiency as sought by the Objective 3. This Review judges achievement of this indicator as ***Negligible.***

By contrast, one achievement under this objective was substantial increase in the beneficiaries of the Energy Vulnerable Program. While neither the associated prior action nor this reform and the associated indicator directly contributed to the objective of strengthening of financial sustainability and efficiency of EPS, it did so indirectly. By providing subsidies to vulnerable population, it makes the increases in tariffs more socially sustainable over the long term. Also, the indicator explicitly took into account gender dimension of "electricity vulnerability" because female headed households were particularly vulnerable as noted by the Poverty/Social

Analysis. Notably, 31.9 percent of households in Serbia are headed by a female. In addition, female-headed households spent a much larger share of expenditure on energy (13.2 percent) than male-headed households (11.3 percent) (PD, DPL1, Annex 4, P. 53, 57).).Taking into account the strong relevance and design of this indicator to measure the impact of the prior action, the achievement of RI5 target is judged ***High.***

Overall, with only one indicator High, two Modest and two Negligible, the achievement of this objective is considered ***Moderately satisfactory***.

Rating

Moderately Satisfactory

OBJECTIVE 4

Objective: Improve financial sustainability and efficiency of transport sector public enterprises and state-owned companies

Supported by PA# 11, 12, 13, 14 and 15

Results Indicators: 9, 10, 11, and 12

Rationale

Actions under this objective substantially contributed to the its achievement. For example, the government reduced budgetary support to transport companies, hardening their budget constraint and laying the foundation for improved financial management and financial sustainability of the companies. Achievement of Target is judged ***Substantial***.

It is also notable that important indicators of labor productivity and cargo were exceeded albeit not for asset utilization of passenger rail. These indicators well measured the impact of the corresponding PA and progress to Objective. Achievement was judged ***Substantial.***

The targeted reduction in the wage bill was achieved with some delay, contributing to the stronger financial position of the transport companies even though it was not fully clear if it was achieved with sustainable reduction in excess employment. Indicator achievement is judged ***Substantial***.

Progress with government in agreeing with Putevi Srbije (Roads of Serbia) on performance levels for the different road classes with associated guaranteed funding levels committed was not achieved but progress was reported and guaranteed funding is expected to improve financial performance in the future. Indicator Achievement is judged ***Modest***.

With three result indicators (RI9-11) Substantial and one (RI12) Modest, the achievement of this Fourth objective is judged Satisfactory.

Rating

Satisfactory

Overall Achievement of Objectives (Efficacy)

Rationale

RI Relevance and Efficacy Ratings

<table>
<tr><th>Results Indicator</th><th>Relevance</th><th>Efficacy rating (from RI and/or complementary evidence)</th><th>Pillar Efficacy</th><th>Overall Efficacy Rating</th></tr>
<tr><td colspan="4">Pillar 1: Improved public expenditure management through strengthened public financial management</td><td rowspan="5">Moderately satisfactory</td></tr>
<tr><td>RI1</td><td>S</td><td>High</td><td>Highly satisfactory ("all pillar RI targets are rated high")</td></tr>
<tr><td colspan="4">Pillar 2 Improved public expenditure management through public administration reform</td></tr>
<tr><td>RI2</td><td>S</td><td>High</td><td rowspan="2">Moderately Satisfactory ("At least half Pillar RI targets are rated modest or better")</td></tr>
<tr><td>RI3</td><td>S</td><td>Negligible</td></tr>
<tr><td colspan="4">Pillar 3: Improve the financial sustainability and efficiency of energy sector public enterprises</td><td rowspan="5"></td></tr>
<tr><td>RI4</td><td>MS</td><td>Modest</td><td rowspan="4">Moderately satisfactory ("Most pillar RI targets are rated modest or lower")</td></tr>
<tr><td>RI5</td><td>S</td><td>High</td></tr>
<tr><td>RI6</td><td>MU</td><td>Modest</td></tr>
<tr><td>RI7</td><td>MS</td><td>Modest</td></tr>
</table>

RI8	MU	Negligible		
Pillar 4: Improve the financial sustainability and efficiency of transport sector public enterprises				
RI9	S	Substantial	Satisfactory ("Most (two thirds or better) RI targets are rated Substantial; no targets are rated negligible")	
RI10	S	Substantial		
RI11	S	Substantial		
RI12	MU	Modest		

Overall, the reforms supported by the Series helped strengthen fiscal consolidation, substantially reduce public debt, and improve financial position of state enterprises. As a result, the economy and the budget entered the COVID19 crisis in 2020 in a much stronger position than before the reform. This permitted the government to provide large fiscal response during the pandemic to help cushion the social and economic impact (Fiscal Council, April 2021).

With achievement of the first objective highly satisfactory and the second and third moderately satisfactory and fourth satisfactory, the overall efficiency rating efficacy is ***Satisfactory***.

Overall Efficacy Rating
Satisfactory

6. Outcome

Rationale

The relevance of prior actions was rated **satisfactory**. The achievement of objectives was rated **satisfactory**. Results indicators were generally well defined. Data were available to measure achievements. However, relevance of a few indicators could have been improved to better capture the impact of the prior actions. Prior actions were well selected, supporting an ambitious reform agenda, and many could have been expected to meaningfully contribute to achievement of objectives. A somewhat weaker element of design were results indicators, whose quality and consistency varied somewhat, in some cases featuring indirect links with prior actions and objectives, with respect to the second and third objectives. Two results indicator targets (out of 13) were moderately revised down to make them more realistic given the longer-than-expected time for reform implementation.

a. Rating

Satisfactory

7. Risk to Development Outcome

Risk to development outcomes going forward is substantial, notwithstanding achievements on significant fiscal consolidation and progress with structural reform agenda supported under the Series. The Series tackled some of the difficult reform areas—public administration reform and SOE reform—in addition to measures to strengthen PFM and expenditure management, which may encounter resistance, especially from the SOEs. Political and governance risks to implementation and outcome remain, including political sensitivity to wage policy reforms. These risks will be partially mitigated by a new DPF on public sector efficiency and green growth, which is under development, and that will give sector ministries more control over replacing departing staff, while enabling strategic redistribution across functions. Stakeholder and social risks remain substantial because of the potential resistance by unions and employees to rightsizing of the workforce in state enterprises and by public concern about the social impact of electricity tariff adjustments. One risk that did decline is the macroeconomic risk, which is now considered moderate. This reflects substantial progress on macroeconomic reform, primarily fiscal consolidation which resulted in a significant reduction in public debt, from 76% of GDP in 2015 to 53% in 2019, overperforming on the original baseline trajectory of public debt in the Debt Sustainability Analysis (DSA) on approval of the first operation. The wider fiscal space, even with the large fiscal response to the COVID19 crisis in 2020 and additional borrowing by the government planned in 2021 (Fiscal Council, April 2021) has reduced macroeconomic risks to the achievements of this programmatic series.

8. Assessment of Bank Performance

a. Bank Performance – Design/Preparation

Rationale

The quality of the prior actions was substantial under all pillars. Prior actions were well linked to the objectives. Most reflected substantial reform actions that helped push the broad reform agenda forward, such as the increase in electricity tariffs, reduction in the payment arrears, and increase in the number of beneficiaries of the Energy Vulnerability Program as well as substantial actions in support of the strengthening of the financial position of transport companies. At the same time, the ambition of some of the reforms supported by prior actions was probably unrealistically high for the time frame, especially with respect to the reform of energy SOEs. This also reflects the overestimation on the part of the Bank of institutional capacity and underestimation of political economy constraints to some of the difficult reforms such as the rightsizing of the civil service and SOE workforce, which was necessary for long-term sustainability. With the hindsight, therefore, more realistic time frame for difficult reforms would have made for a stronger design. Also, several results indicators had limited relevance in measuring progress towards reform objectives. Fewer and more directly relevant indicators would have made for a better design.

The design reflected the key lesson from the past that in order to ensure sustainable fiscal consolidation and restructuring of major SOEs, Serbia needed to address head on financial sustainability of these companies with politically difficult actions and reforms that included tariff increases, reduction of payment arrears, the wage bill, and achieve other improvements in indicators of SOE productivity. Also, the CLR of the previous CPS FY12-15 has highlighted the need to closely align the Bank's operations with government's objectives. The Series was, indeed, closely aligned with the government's reform program and, in particular, its Fiscal Strategy. Also, the CLR highlight the need to ensure a strong link between the Bank's knowledge and design of the operations (see below).

The analytical underpinnings behind the Program design was strong. The 2015 Public Expenditure and Financial Assessment report which stressed the need to improve arrears monitoring, payment discipline, and ex ante commitment controls, directly informed corresponding prior actions. Also, significant technical assistance from a Bank administered trust fund supported by the Swiss State Secretariat for Economic Affairs and the European Commission, and from the European Bank for Reconstruction and Development (EBRD) and other development partners, informed reforms. It is also notable that the PEPU DPL series was closely linked and reinforced by the Bank's SOE Reform DPL series, the PforR on Modernization and Optimization of Public Administration, and the Competitiveness and Jobs project.

The Bank appropriately assessed key ex ante risks as substantial, especially on the political, governance, and stakeholder/social fronts as well as on the macroeconomic framework, given the large scale of fiscal adjustment involved. The Bank also carried out solid poverty/social and environmental risk analysis that informed the design, especially on the protection of vulnerable households.

Finally, in the preparation of the Series, the Bank team engaged in extensive consultation within and outside the government. The consultations were held with representatives of the EU, the IMF, Swiss State Secretariat for Economic Affairs and the European Commission, and EBRD, as well as the Fiscal Council, Serbia's fiscal watchdog agency. The team has consulted the Council's independent assessments of the fiscal situation and SOEs. The collaboration at the team level, with regular exchange of information and team meetings, with the IMF was especially strong.

Rating

Moderately Satisfactory

b. Bank Performance – Implementation

Rationale

The Bank team has monitored progress toward achievement of targets using the results framework during the life of the series but it is not clear if similar monitoring on the part of the government and relevant SOEs has continued on an ongoing basis.

All PEPU-DPL1 indicative triggers were converted to Prior Actions (PAs) for PEPU-DPL2 with minimal changes to PAs #1 and #3 to better reflect the pace of reform. Results indicators 1 and 11 were revised somewhat during negotiations of the second operation to better reflect the associated prior actions.

The Bank adapted and implemented mitigating measures to address risks identified ex ante (e.g., stakeholder and social risks) by engaging in consultations with the government, unions, SOEs, and other government agencies, and experts and development partners. The Bank's support for the expansion of the vulnerable groups program was a mechanism directly addressing the social risks. The Bank undertook regular macroeconomic monitoring but more could have been done to ensure that the monitoring and evaluation of program indicators was an integral part of the government's M&E framework. The Bank has also used technical assistance from a Swiss agency as noted above to address identified technical capacity constraints.

There was significant stakeholder and donor coordination. The Bank collaborated and coordinated well with the IMF and other development partners. The IMF focused on macro-critical parts of public financial management and public administration reform while the Bank program complemented the Fund, especially in the areas of clearance of energy sector arrears and reform of Srbijagas. The Bank coordinated with the EBRD on the restructuring of railways companies, and EBRD parallel restructuring loan focused on the complementary issue of the governance of the electricity company. Finally, the Bank coordinated with the EU, which also supported the Bank program as the structural reforms were framed in the context of Serbia's EU membership accession process.

Rating

Satisfactory

c. Overall Bank Performance

Rationale

Bank performance is judged Satisfactory. The objectives and prior actions were highly relevant and selected based on extensive analytical work and technical assistance, and in close coordination and complementarity with the IMF and other development partners. At the same time, the Bank assessed key risks appropriately and mitigated social risks through poverty/social analysis which informed the sound design of an important prior action and associated indicator.

Overall Bank Performance Rating

Satisfactory

9. Other Impacts

a. Social and Poverty

The DPL Series acknowledged the potential negative impact of some prior actions (PA #12 and #13) related to rightsizing of the workforce of EPS and Railways companies as well as the prior action #6 on increasing electricity tariffs. It supported support packages to redundant workers as well as the doubling of the budget for and expanding the coverage of the targeted social protection program for households vulnerable to electricity prices. The actual impact on redundant workers was more limited than expected because most of the reduction in employment that occurred happened as a result of natural attrition with retiring workers and some departing voluntarily. In terms of the impact on vulnerable households, there were notable impacts. In 2017, the average number of beneficiary vulnerable households increased from around 42,000 to 64,000 and the benefit was further extended to cover a new beneficiary group: households that have members with disabilities (Energy Subsidy Reform Facility (ESRF), Serbia brief, ESMAP, February 2018). Poverty rate (at $5.5 dollars in PPP terms) declined from 25.3 in 2015 to estimated 17.4 percent in 2020. The 2021 Macro-Poverty Outlook for Serbia notes that "the Serbian economy entered only a mild recession of -1 percent in 2020 thanks to the significant fiscal stimulus program of around 13 percent of GDP; a result, there was not a substantial increase in poverty, which is estimated to be close to its 2019 level." (p.1).

b. Environmental

Prior actions on electricity tariffs and railways and associated reform agenda, if sustained, are likely to have some positive environmental impacts but only over the medium-to-longer term because of the time needed for Serbia's economy to reduce its dependence on coal and fossil fuels for electricity generation and heating. PA #6 on increases in electricity tariffs contributed to some rationalization of demand for electricity, which is largely generated from coal and other fossil fuels. Also, prior actions on Railways restructuring (#11 and #13) likely had favorable impact on the more efficient use of tracks and, therefore, may have contributed to improved efficiency and use of fossil fuel with concomitant benefits for the environment.

c. Gender

Prior Action (#6) on the social protection program contributed to protecting female headed households vulnerable to electricity price increases. The share of female headed household in the program went up from 27 percent in 2015 to 53 percent in 2018, much higher than the target. Given that female headed households are much more vulnerable to changes in electricity prices due to their different income levels, this was an important social measures to cushion the impact of the adjustment in electricity tariffs.

d. Other

None identified.

10. Quality of ICR

Rationale

The ICR is candid and comprehensive. It lays out well the country context at approval and during the life of the Series. It is detailed, specific, and rich in data, including explicit reference to data sources. It provides a clear and credible theory of change. It discusses prior actions and their rationale in sufficient detail. Presentation of the achievement and results framework is clear and easily understandable. Finally, it provides a candid reassessment of risks to development outcomes. Therefore, the quality of the ICR is rated **high.**

a. Rating

Substantial

11. Ratings

Ratings	ICR	IEG	Reason for Disagreement/Comments
Outcome	Satisfactory	Satisfactory	
Bank Performance	Satisfactory	Satisfactory	
Relevance of Results Indicators	---	Satisfactory	
Quality of ICR	---	High	

12. Lessons

This Review concurs with the lessons from the ICR, which are summarized below. The fourth lesson is revised to include emphasis on social protection mechanisms to counter the negative impact on the vulnerable. The Review adds lessons on results indicators and reform ambition.

1. Development partner coordination, supportive technical assistance, complementary Bank operations, a programmatic approach, and strong analytic underpinnings were key factors in the success of this DPL series.
2. Incentivizing implementation of prior actions with DLIs from a parallel PforR did not ensure the implementation of the new wage policy due to political sensitivities and the need for additional analysis.
3. Strong political will is decisive for advancing complex, politically sensitive reforms and for effectively negotiating with vested interests, as is government ownership and communication strategy towards stakeholders. In this case, two key ministers supporting the design of the series left during implementation, creating a challenge for some reform components.
4. Political sustainability of DPL supported structural reforms with negative social impact can be enhanced when reforms are accompanied by mitigation measures to cushion the impact on the vulnerable, be it

through the compensation packages in the context of redundancies or expanded social protection mechanism to cushion the impact of increases in social sensitive prices of public utilities.

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13. Project Performance Assessment Report (PPAR) Recommended?

No