

PROGRAM INFORMATION DOCUMENT (PID)**CONCEPT STAGE**

Report No.: AB6992

Operation Name	Serbia Public Enterprise Restructuring DPL 1
Region	EUROPE AND CENTRAL ASIA
Country	Serbia
Sector	General finance sector (30%); General industry and trade sector (30%); Central government administration (20%); Capital markets (10%); General energy sector (10%)
Operation ID	P127408
Lending Instrument	Development Policy Lending
Borrower(s)	REPUBLIC OF SERBIA
Implementing Agency	The Ministry of Finance (MoF) of the Republic of Serbia will be responsible for overall implementation of the proposed operation. Other key ministries and agencies involved in the operation will include: the Ministry of Economy and Regional Development (MoERD), Ministry of Environment, Mining and Spatial Planning (MOEMSP), Privatization Agency (PA), and the Ministry of Labor and Social Policy
Date PID Prepared	May 1, 2012
Estimated Date of Appraisal	October 19, 2012
Estimated Date of Board Approval	November 29, 2012
Corporate Review Decision	Following the corporate review, the decision was taken to proceed with the preparation of the operation.

I. Key development issues and rationale for Bank involvement

As part of the transition to a market economy in the early 2000's, Serbia introduced a variety of structural reforms in the enterprise and banking sectors, and put in place mechanisms to cushion the

social impact of these reforms. Enterprise reforms included privatization of socially-owned enterprises¹. The Bank supported these reforms through financing and TA.

The role of the state in the enterprise sector remains pervasive. The current portfolio of public enterprises consists of about 1,300 enterprises that employ more than 280,000 people (about 16 percent of the formal workforce, of which an estimate 40 percent are women²). These 1,300 enterprises can be segmented into three groups: (i) enterprises managed by the Privatization Agency³ to be divested; (ii) a small group of state-owned enterprises (SOEs), primarily utilities (e.g., electricity) and a few commercial enterprises (e.g., pharmaceuticals); and (iii) municipal enterprises.

The enterprises in the public sector suffer from poor performance despite substantial state support. In 2010, public enterprises in Serbia had aggregate losses of about EUR1 billion (3.5 percent of GDP). Many of the loss making enterprises survive thanks to direct and indirect state support subsidies (e.g., arrears to other state entities). In 2010, budgetary cash flows to public enterprises in the form of subsidies, payments to cover arrears to pensions and social contributions, and payments guarantees were approximately 2.5 percent of GDP, and about 2.0 percent of GDP in 2011. In addition to being sizable, allocation process of direct subsidies remains not transparent and is not driven by a cost-benefit analysis. Direct subsidies are dwarfed by the contingent liabilities that have been accumulated by public enterprises to various state entities (some 11 percent of GDP), and include guarantees to public enterprises (5.9 percent of GDP⁴) and arrears to other state entities (for unpaid taxes, contributions, etc.) estimated to above 4 percent of GDP.

Improving the efficiency of public enterprises and decreasing the ownership role of the state in the enterprise sector is critical for the overall competitiveness of the economy, and will also have a positive fiscal impact.

II. Project Objective(s)

The objective is to enhance contribution of the public enterprise sector to the competitiveness of the Serbian economy by: (i) freeing up fiscal space by decreasing subsidies, improving the budget contributions of profit making enterprises and generating privatization revenues; (ii) divesting assets from unviable public enterprises to more productive activities; (iii) improving the quality of service provision by public and municipal utilities.

The proposed DPL will contribute to the “competitiveness” strategic pillar of the CPS FY12-15.

¹ The concept of “Socially Owned Enterprises” is unique to the Former Yugoslav Republics, and is defined by enterprises which are the collective property of the employees, and as such are not considered to be public or private in nature.

² Note that administrative data are not disaggregated by gender. As discussed at greater length in the PSIA section it is not possible to have a precise estimate of workers in the sector from the LFS, and the same apply to its gender disaggregation.

³ The Privatization Agency is part of the Ministry of Economy that was created by the privatization law to manage the resolution of socially-owned enterprises through sale, bankruptcy or liquidation.

⁴ Out of the 5.9% of GDP in guarantees that are outstanding, 1.8% were issued in 2011.

III. Project Description

The reforms supported by DPL series aim to reduce the scope of state involvement in the enterprise sector by completing the privatization agenda and improving the performance of enterprises which are likely to remain in the public domain in the near to medium-term. The DPL will support reforms to: (i) define clear criteria of future actions for each set of public enterprises; (ii) set a time-bound process to implement these actions; and (iii) create incentives for all involved parties. As a first step, a decision needs to be made which enterprises the government wants to retain and those that it wants to divest. For the enterprises that the government decides to divest, the DPL will support the divestiture process and creation of the policy conditions. For the ones that the government decides to retain, the DPL will focus on improvements in governance and accountability, efficiency and performance. In both cases, the common element of the interventions supported by this DPL series will be reduction of state subsidies and transfers.

Although public enterprises in Serbia are heterogeneous in nature, they all share a number of issues: (i) weaknesses in their governance model; (ii) poor performance and dependence on significant state support; (iii) disincentives and complexity in divesting their assets; and (iv) limited labor mobility as a constraint to increased efficiency. In order to tackle these four cross-cutting issues, the DPL is structured according to four pillars.

Corporate and financial governance – implementation of improvements in the governance framework for public enterprises, focusing in particular on large enterprises that will remain state-owned for the foreseeable future;

Performance management – development and introduction of performance management systems with the goal to minimize government support (e.g., subsidies, guarantees) and to improve quality of service provisions;

Transactions – privatization transactions following the best suitable global practice;

Mitigating the social and labor market impact – cushioning the social costs of the public enterprise reforms and enhancing existing mechanisms to facilitate labor mobility out of the non-private sector.

These four pillars are interrelated and involve a significant number of state and municipal institutions. The proposed DPL series will serve as a coordination platform for the policy and implementation aspects of the reform.

IV. Poverty and Social Impacts and Environment Aspects

Poverty and Social Impacts

This DPL series is being launched against a difficult backdrop for living conditions in Serbia with poverty and unemployment rising steadily since 2008. In 2010 (the last year for which we have data) poverty reached 9.2 percent (it stood at 6.1 in 2008). Between 2009 and 2010 poverty increases have been concentrated in rural areas, though detailed analysis reveals that urban areas have seen large increases in the group of households between 100 and 150 percent of the poverty line, raising concerns on the effects of further shocks to the urban economy. Unemployment continues to climb despite the recovery in growth – it was estimated at 23.7 percent in November 2011 for individuals 15 and over (rising from 19.2 in April 2010).⁵ As a result currently, the employment rate stands at only 35.3 percent, meaning that 36 percent of the working age population, (aged 15 and older), have a job (formal or informal). Cognizant of these challenges, this PPERDPL includes a social pillar, which is being designed in close coordination with the PSIA activities. The structure of the PSIA work program mirrors the two components of the social pillar, namely: (i) addressing the employment aspects of the restructuring and (ii) addressing concerns for the affordability of municipal utility services for vulnerable consumers.

Environment Aspects

The current privatization legislation already covers relevant environmental aspects to be dealt with in the process of public enterprise restructuring, and the EU accession process provides the direction for Serbia toward the adoption of an environmental framework coherent with the European ones. The proposed operation would ensure that an appropriate environmental framework is in place to cover legacy issues which would need to be addressed by the new owners or by the government.

V. Tentative financing

Source:	(\$m.)
Borrower	0
International Bank for Reconstruction and Development	200
Total	200

VI. Contact point

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⁵ A more detailed update in these trends is provided by World Bank (2012) “Western Balkans Programmatic Poverty Update. Poverty Update for the Republic of Serbia”, in process.

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