



# Project Information Document (PID)

Concept Stage | Date Prepared/Updated: 06-Jun-2019 | Report No: PIDISDSC25635



**BASIC INFORMATION**

**A. Basic Project Data**

Country Serbia	Project ID P167634	Parent Project ID (if any)	Project Name Serbia: Competitive Agriculture Project (SCAP) (P167634)
Region EUROPE AND CENTRAL ASIA	Estimated Appraisal Date Sep 02, 2019	Estimated Board Date Nov 21, 2019	Practice Area (Lead) Agriculture
Financing Instrument Investment Project Financing	Borrower(s) Ministry of Finance	Implementing Agency Ministry of Agriculture, Forestry and Water Management	

**Proposed Development Objective(s)**

Improve market access for small and medium agricultural producers in Serbia

**PROJECT FINANCING DATA (US\$, Millions)**

**SUMMARY**

<b>Total Project Cost</b>	50.00
<b>Total Financing</b>	50.00
<b>of which IBRD/IDA</b>	50.00
<b>Financing Gap</b>	0.00

**DETAILS**

**World Bank Group Financing**

International Bank for Reconstruction and Development (IBRD)	50.00
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Environmental and Social Risk Classification

Moderate

Concept Review Decision

Track II-The review did authorize the preparation to continue



Other Decision (as needed)

## B. Introduction and Context

### Country Context

- 1. Following years of recession and slow growth, the Serbian economy expanded by 1.8 percent, on average, over the previous three years (2015–2017), while a stronger growth of 3.5 percent was estimated for 2018.** Over the previous three years, growth started to recover on the back of higher investment (average annual growth of 8.3 percent) and strong growth of exports (up 10.7 percent annually in real terms). Consumption recovered as well, but at a slower pace (at 1 percent annually in real terms). Growth of the industry and services sectors contributed most to the overall growth of the economy over the previous three years, while agriculture had a negative contribution to growth in 2015 and 2017. For 2018, growth was broad-based with all three major sectors growing faster than last year. As a result, the growth in 2018 reached 4.2 percent. The medium-term growth projections depend crucially on deeper and timelier structural reforms and progress with European Union (EU) accession.
- 2. The Government of Serbia (GOS) has implemented a successful fiscal adjustment but economic vulnerabilities remain.** In 2014, the GOS adopted an ambitious fiscal consolidation and structural reform program supported by the International Monetary Fund (IMF) and the World Bank. In the short term, the program focused on the control of aggregate wage and pension expenditures, improvements in tax administration, and reductions in subsidies to state owned enterprises. The implementation of these measures led to the reduction of budget deficits in 2015–2016 and budget surplus of 1.2 percent of gross domestic product (GDP) in 2017 and 0.5 percent of GDP in 2018, underpinned by strong revenue collection and lower than planned public spending ensuing, among others, from the interest payment savings and under-execution of public investment. As a result of prudent fiscal policies, public debt continues to decline and stood at 54.3 percent of GDP (at the end of December 2018), and is expected to continue declining during 2019, albeit at a slower pace. However, the country remains vulnerable to spillovers from regional developments and market volatility, thus ensuring fiscal sustainability and supporting private sector development, growth, and formal employment are important for Serbia's economic performance in the long term.
- 3. Over this same period, the prospects for accession to the EU provided an impetus for a broad spectrum of reforms.** In November 2007, Serbia initiated a Stabilization and Association Agreement with the EU. In 2012, it was granted an EU candidate status. Since the formal start of the accession negotiations in 2014, progress has evolved largely following its predicted trajectory. As of December 2018, Serbia opened 16 out of 35 chapters of the EU's Acquis Communautaire, of which two are provisionally closed.
- 4. Regional disparities of living standards are evident.** There is a high degree of variability of living standards within the country, with 25 percent of the population of Serbia (close to 1.8 million people) being at risk of poverty. Municipalities in the Southern and Eastern part of Serbia have high poverty incidence as compared to the rest of the country, with risk of poverty rates ranging between 13 and 63 percent within these regions. Better understanding of these geographic disparities can help the Government of Serbia design and target policies and programs to support growth, jobs, poverty reduction and social inclusion.



## Sectoral and Institutional Context<sup>1</sup>

5. **Agriculture plays an important role in the economy of Serbia.** Agriculture is the third largest sector, accounting for around 6 percent of GDP and 19 percent of formal employment, and the most important export sector, representing 23 percent of total exports. The impressive growth of exports of both primary and processed food products provides evidence of the competitiveness of Serbian production in international markets and of significant potential to further leverage the sector's growth to create jobs and income. From 2005 to 2016, the country's exports of primary food and beverage products increased 148 percent and of processed food products increased 83 percent. In 2016, Serbia accumulated an agricultural trade surplus of US\$650 million in primary products and of US\$525 million in processed food and beverage products.

6. **Agriculture is undergoing a process of structural transformation towards a modern agri-food system.** Primary agriculture, an important source of income and employment in the past, has diminished its contribution to the rapidly diversifying economy of Serbia. The declining share of primary agriculture in GDP and employment signals a process of transformation that provides ample opportunities for developing a modern, dynamic and more competitive agri-food system, able to generate better jobs up and downstream and improve income and livelihoods in the rural space. Improvements in labor and land productivity have contributed towards the expansion of agricultural output in Serbia. This is important as it leads to an increase in the supply of raw materials at lower costs to agri-processors, which in turn supports a much larger scale of operation, promotes horizontal integration, and reduces overall costs, all factors that increase the competitiveness of the whole agri-food system, as the country prepares for EU accession. Improving productivity is more than just raising yields and decreasing costs; it is also about raising food quality, moving into higher value products by using improved technology and practices<sup>2</sup>.

7. **Sector growth is geographically differentiated and narrow based in terms of composition of production.** Growth patterns in agriculture are influenced by regional disparities in sector performance and composition, with a positive sector growth in the Northwestern parts of the country and contraction of production in Southeastern Serbia. The autonomous province of Vojvodina, in the North, is the key driver of agricultural output in Serbia, with 43 percent contribution to national agricultural GDP (in 2014) with large scale production of commodities. Between 2003 and 2013, crop output in Serbia expanded, mainly due to increased production in Vojvodina, as the other three regions recorded only a marginal expansion or even a decline (South and East Serbia). Livestock output declined over the same period, with all regions, except Vojvodina, recording contraction rates between 24 percent (Sumadija and West Serbia) and 33 percent (South and East Serbia). In the same period, livestock output in Vojvodina increased by around 13 percent.

8. **Despite regional comparative advantages, structural factors underpin the regional disparities.** There are important structural limitations to agriculture in Serbia - very small and fragmented land holdings, ageing and declining farm labor force, low efficiency and productivity, low use of technology, high labor intensity, low financial liquidity and capital availability for investment (especially for smallholders) and outdated production management practices. Despite all of these, economic opportunities exist in rural areas. Cereals, vegetable oils and edible fruit have historically driven growth of agricultural production and exports, with Vojvodina's larger producers benefiting the most. Only one percent of the farms in Serbia have 50 hectares or more of land and most of them are in Vojvodina<sup>3</sup>, while farmers who own less

<sup>1</sup> This section borrows from the World Bank Group Sector Study "New Opportunities and Old Constraints: The Context for Agriculture Sector Development in Serbia" by Garry Christensen (2016) as well as from a recently completed Agriculture Public Expenditure Review by Demetris Psaltopoulos and Svetlana Edmeades.

<sup>2</sup> World Bank. 2019. Harvesting Prosperity: Technology and productivity Growth in Agriculture".

<sup>3</sup> Only one percent of farms in South Serbia cultivate more than 50ha of land, while in Vojvodina, 10 percent of farms cultivate more than 50ha of land.



than 5 hectares of land account for 78 percent of all holdings and 25 percent of the total cultivated area in Serbia and are concentrated in the South and East Serbia.

9. **Broadening the scope for sector growth to include small and medium scale producers may be key to sector transformation.** Although fragmented farm structures are often perceived as a challenge to scale economies and competitiveness, with high transaction costs preventing the many small producers from engaging in markets, in the case of Serbia, recent public expenditure analysis shows that smallholders<sup>4</sup> are the most technically efficient producers in the country and hence, supporting their development can improve sector growth. Hence, consolidation at the product level, through aggregation and economic clusters, may hold the key to development, enabling the specialization of small efficient units and their integration into broader value chains. Middle size farms, which are often seen as the drivers of growth in the sector, are found to be the worst performers in terms of technical efficiency in Serbia, posing a question on the adequacy of the enabling environment for their agricultural development. These producer segments also specialize in agricultural products that are not scale intensive yet can hold important value proposition and drive the generation of jobs and growth in rural areas. Improving the enabling environment to support the productive inclusion of small and medium scale producers can drive the process of structural transformation of agri-food systems in Serbia.

10. **Rethinking and redirecting policy instruments and incentives can increase the speed of sector transformation.** Agricultural budget support has been aligned with the EU budget support framework, and a Directorate for Agrarian Payments has been established to administer national direct payments (subsidies) and rural development investments (both national and EU Instrument for Pre-Accession and Assistance for Rural Development (IPARD) grants). Subsidies and transfers dominate agricultural spending (2011-2017) and, on average, account for 82 percent of sector expenditure. They are found to negatively affect sector productivity and efficiency and are thought to contribute towards freezing the current dual farm structure. Emphasis on area and headage payments<sup>5</sup> reduce the incentives to increase productivity, preserve farm structures dominated by smaller farms and do not contribute to the acceleration of the structural transformation process<sup>6</sup>. Further, coupled output subsidies distort the allocation of productive resources. When the above are combined with the low (at least until 2017) level of funds dedicated to rural development, including the provision of public goods (agricultural infrastructure, R&D, advisory services, etc.), it creates a policy framework which constrains farm restructuring and the potential of smaller and medium-sized farms, that currently dominate Serbian agriculture, to increase their size, modernize production systems, benefit from expanding markets and contribute to a competitive agri-food sector and to a vibrant rural economy.

11. **Despite ample EU resources, productive investments, through rural development grants, are underutilized.** IPARD funds in the amount of EUR230 million (including national co-financing) have been allocated to Serbia for the programming period of 2014-2020 in annual instalments. Serbia has received accreditation for 2 of the 11 IPARD measures<sup>7</sup>. Although the scope of these measures is broad, actual number of beneficiaries is limited, with most small and medium scale producers not being able to take advantage of this productive support due to the complex application process and the requirement for upfront financing. A key constraint in the uptake of IPARD grant support is the complexity of the application process, due to the numerous requirements which applicants often can't fulfill, added to limited capacity in the Directorate for Agrarian Payments for review and approval. In addition, a limiting factor is the requirement of an upfront payment of the full grant amount by the applicant, which assumes availability of financial resources, with

<sup>4</sup> In the context of Serbia, small producers are those with an economic size of up to 8,000 euros; medium producers are those with an economic size between 8,000 and 25,000 euros.

<sup>5</sup> Criticized for not relying on objective and valid baseline indicators, as well as the poor definition of eligibility criteria (Bogdanov et al., 2017)

<sup>6</sup> It is noted that leased agricultural land is excluded from farm support (Bogdanov, 2016).

<sup>7</sup> Accredited measures in 2018 are *Investments in Physical Assets of Agricultural Holdings* and *Investments in Physical Assets for Processing and Marketing of Agriculture and Fisheries Products*; 2 more are planned for accreditation in 2019 - *Farm diversification and business development* and *Technical assistance*; and 2 additional ones for 2020 – *LIDER program for local development and organic production*.



reimbursement of 50 percent after all investment criteria have been fulfilled, ex post. This requirement alone makes IPARD grants difficult to access for the majority of small and medium scale producers in Serbia.

12. **National program resources can shift the sector equilibrium from low productivity to high value for small and medium scale producers in Serbia and encourage convergence of the National and EU programs over time.** For rural development grants, boundaries are established between eligible beneficiaries of the national rural development program and those eligible to apply for IPARD support, based on either size or production potential. All producers not eligible for IPARD support, are eligible for national program support. Reaching out with national investment funds to the small and medium producers of Serbia, especially in the South and Southeast of Serbia, can improve these producers' productive inclusion and competitiveness, and enable them to actively participate in the process of structural transformation of agriculture in Serbia and preparing them for EU accession.

13. **Improving financial inclusion for productive investments can stimulate broader private sector participation.** While around two thirds of adults in rural areas in Serbia have accounts with financial institutions, only 14% of them have loans to operate, start or expand farm and small business activities. Most medium and larger farmers and medium/larger SMEs have access to finance as banks have the right expertise, systems and products to serve these agricultural segments profitably. However, smaller farmers have very limited access to bank financing and mostly rely on off takers and input suppliers to finance their inputs. This type of value chain financing does not cover longer term funding for equipment, machinery and is currently decreasing as these players try to re-focus on their core business. The long-term goal is the development of efficient, competitive markets, producing to EU standards which requires better inclusion of small-scale producers (among them women and youth) in modern supply chains, an increase in investments in machinery, equipment and knowledge as well as the modernization of processing and marketing. For this to be achieved, however, public funds are not sufficient resources and bank financing can play a catalyst role in the further development and competitiveness of the sector.

14. **A combination of targeted public incentives and private financing can improve sector productivity and competitiveness.** A policy mix that focuses on the improvement of competitiveness and value addition capacity of the agri-food system in Serbia can have important sectoral and economy-wide growth effects by inducing positive spillovers to other economic sectors and contributing to employment, poverty reduction and economic prosperity of rural areas. The public expenditure analysis has shown that direct payments do not promote technical efficiency and productivity growth and slow down the structural transformation in Serbian agriculture. Reducing the direct payments envelope and significantly increasing the rural development one (including advisory and farm extension services and R&D) is therefore paramount for improving the performance of the sector. To enable that, a different set of financial mechanisms may be required, to enable small and medium scale producers to access finance and participate in productive decisions, such as matching grants<sup>8</sup> and public guarantee funds that reduce the risk to producers and other financial institutions, hence stimulating financial and productive inclusion. At present, small farmers do not have financial records, do not have business plans, they find bank requirements challenging and, most importantly, they lack collateral. Matching grants and technical assistance (TA) can create the conditions for banks to finance investments of farmers that are not their typical clients. Matching grants can create the required equity for the banks and TA can ensure bankability of the business plan

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<sup>8</sup> Matching grants are an instrument aimed at promoting private sector development which has been used extensively over the past years, in particular for agriculture development. A matching grant is defined as a one-off, non-reimbursable transfer to project beneficiaries, for a specific purpose, based on the condition that the recipient makes a contribution for the same purpose. These grants can be used for a variety of activities including technical assistance, investment in assets or financing of working capital. Total grant financing dedicated to agriculture reaches 650 million USD or almost twice the volume of those outside of agriculture. In addition, the proportion of matching grants projects supporting agriculture has significantly increased in the 2000s. Recent interest for this instrument to support agriculture might be due to growing concerns about other forms of support which distort financial markets such as interest rate subsidies, as well to the compatibility of such agricultural subsidies with World Trade Organization requirements.



and prepare the client to approach the bank. Finally, if commercial banks require additional safeguards for their investments, they will be able to access credit guarantees to be soon provided by the Development Credit Authority (USAID Guarantee Program) and European Investment Fund (EIF) including risk sharing through a new IFC project.

15. **Greater resilience to climate and market risks can further boost the overall sector performance.** The reliance on agricultural commodities increases Serbia's exposure to price volatility, which added to the increasing number of extreme climatic events in Serbia (droughts and floods) further exacerbates agricultural growth volatility. Projected increases in temperatures and declines in precipitation will affect rainfed crops, which dominate Serbian agriculture. Production is concentrated in the north (Vojvodina), where crops are vulnerable to decreasing precipitation and increasing temperatures, primarily during the summer growing season. Rainfed maize may decline by as much as 58 percent due to reduced rainfall and higher temperatures in summer. Increases in temperature have already brought about increases in fungal diseases and pests that reduce crop production. Cereals and fruits are the most important agricultural products in terms of production area and economic output; fruit production is particularly vulnerable to spring frost, hail, extremely low winter temperatures, low precipitation and/or heavy rainfall events<sup>9</sup>. Hence, diversifying the sector base has important climate mitigation (reducing risks) and climate adaptation (improving resilience) implications for the country.

16. **As Serbia advances in the process of sector transformation and alignment to EU acquis, the effectiveness of public service delivery becomes critical to improving sector performance.** Serbia has committed to align its national agricultural policy to the Common Agricultural Policy (CAP) of the EU by the date of accession. To this end, the country is required to have all the necessary systems in place to manage and receive funds from the EU and to make payments to beneficiaries in Serbia in accordance with EU rules and procedures. An Integrated Administration and Control System (IACS), along with other tools, are necessary for the efficient utilization and monitoring of support funds. Systems for monitoring results (and not only expenditures) will also be required by the reformed CAP, starting in 2020. EU membership unlocks significant financial assistance to farmers under the EU's CAP, yet it also imposes stricter food safety and other trade-related requirements to agricultural production. Enhancements in digital approaches can improve targeting, efficiency of spending, food safety monitoring, as well as support the governance structure of the sector. The innovation environment in Serbia would need to be strengthened and uptake of emerging digital technologies by farmers improved to help lower transaction costs and facilitate information access about best farming practices, inputs, prices, access to credit and markets. This will improve transparency, reduce innovation hurdles and support an enabling environment for productive and financial inclusion of agricultural producers in Serbia.

#### Relationship to CPF

17. **The proposed project is consistent with the Serbia Country Partnership Framework (CPF) for the period of FY16-20.** While the SCD identified agriculture as a priority sector for the twin goals, the CPF did not originally envisage an operation because of counterpart readiness. However, engagement with a new team at the MAFWM demonstrates a new strategic drive and opportunity to make an impact. Therefore, as part of the program update permitted under the PLR, the Bank decided to re-engage in this sector. Through productive investments targeting small and medium scale producers and strengthening the information systems of the agricultural sector, the project aims at increasing sector competitiveness, while providing economic opportunities in rural areas, as the country moves closer to EU membership. The Performance and Learning Review (PLR) of the CPF identifies agriculture as one of the high priorities for the Government with an important dimension of shared prosperity. The project is also aligned with the strategic goals of the National Agricultural and Rural Development (NARD) strategy for 2014-2024: i) growth of production and income stability; ii) growth of competitiveness with adjustments to domestic and foreign markets requirements and technical-technological

<sup>9</sup> USAID. 2017. Climate Risk Profile: Serbia:

[https://www.climatelinks.org/sites/default/files/asset/document/2017\\_USAID\\_Climate%20Change%20Risk%20Profile\\_Serbia.pdf](https://www.climatelinks.org/sites/default/files/asset/document/2017_USAID_Climate%20Change%20Risk%20Profile_Serbia.pdf)





promotion of the sector; iii) sustainable management of resources and environment protection; iv) promotion of quality of life in rural areas and poverty reduction; v) efficient management of public policies and promotion of institutional framework for development of agriculture and rural development.

### C. Proposed Development Objective(s)

#### 18. To improve access to markets and information systems for agricultural producers in Serbia.

This will be achieved through a) improving productivity of small and medium scale farmers by strengthening advisory and technical support; b) supporting market access of small and medium scale farmers (including finance and business planning capacity); c) improving government systems to strengthen the enabling environment for all agricultural producers (including capacity building for the Ministry, information systems, data platform).

Key Results (From PCN)

#### 19. The project will achieve the following results:

- (i) *Productivity*<sup>10</sup>: **Increase in gross value added per utilized agricultural area**
- (ii) *Competitiveness*<sup>11</sup>: **Increase in the share of production sold by project beneficiaries**
- (iii) *Financial inclusion*<sup>12</sup>: **Number of beneficiaries accessing commercial bank loans for their productive investments (disaggregated by gender)**
- (iv) *Use of information systems*<sup>13</sup>: **Number of unique users of the integrated information platform (disaggregated by gender)**

### D. Concept Description

#### A. Concept

20. **Scope:** The project will support the Government of Serbia with the implementation of the National Agriculture and Rural Development Program. This will complement Serbia's on-going efforts to align its national programs to the EU CAP programs. In particular, the project will provide financial and technical support to all productive investments in agriculture in Serbia through the national rural development program<sup>14</sup> and will not participate in the financing of direct payments (subsidies). This delimits the scope of project interventions outside of all IPARD measures that the country has been accredited for or plans to be accredited for and puts it in the center of national rural development program.

<sup>10</sup> Improved on-farm productivity (use of better management practices, climate smart agriculture, etc.)

<sup>11</sup> Improved linkages between producers and buyers/markets (volume, quality and uniformity of production, value and volume of sales, market segmentation strategies, etc.; building entrepreneurial capacity of the production units)

<sup>12</sup> Improved access to finance to drive the process of value-addition on and off-farm (enable investments in equipment, small infrastructure, technical assistance, and other services that improve the competitiveness of the production units)

<sup>13</sup> Improved information systems for decision making at the level of the Ministry of Agriculture Forestry and Water Management (MAFWM) and information flow with agricultural producers

<sup>14</sup> In 2018, the program received 8,000 applications from small and medium scale producers.





21. **Beneficiaries:** Small and medium scale agricultural production units (including producers, producer groups, agribusinesses/agro-processors that can provide direct link to smallholder farmers) that have or can have commercial focus and are not covered by accredited IPARD measures. Although large producers will not be directly targeted, the project will also benefit them with the enabling environment it will create through the improvements in information systems and the financial services provided. Small and medium size producers are defined by the economic size of holding expressed in euros of standard output. For the purposes of this project and the context of Serbia, small producers are those with an economic size of up to 8,000 euros; medium producers are those with an economic size between 8,000 and 25,000 euros.

## **Description**

22. The project activities are structured into three Components. Component 1 will focus on improving the productive and entrepreneurial capacity of small and medium farmers by supporting business and financial planning for productive investments, as well as supporting market access and strengthening sector competitiveness. Component 2 will focus on improving the capacity of the Ministry of Agriculture, Forestry and Water Management (MAFWM) to provide core public goods for improving sector performance. This includes establishing an information system aligned with EU CAP requirements to enable evidence-based policy making and monitoring of results, enhance market information for stakeholders and build capacity for regulatory roles aligned with EU CAP. Component 3 will focus on project management.

23. By addressing sector needs at the level of producers (Component 1) and the MAFWM (Component 2), the project will support a broader policy reform process in the agriculture sector through: i) improved targeting of policy instruments to different typologies of producers, ii) strengthened enabling environment for investment for small and medium agricultural producers, by improving the delivery of services to these productive segments (advisory, financial, information, etc.), iii) improving the monitoring of public resources and their utilization, as well as sector performance. It is expected that this will bring about a significant shift in the utilization of public resources in agriculture from subsidies (direct payments) to rural development investments.

### **Component 1: Improving the value-added of agriculture (US\$35 million)**

24. The objective of this component is to improve the economic performance of small and medium agricultural producers in Serbia on- and off-farm. The component will support the building of entrepreneurial capacity of agricultural producers through the integration of production decisions with market requirements and technical and financial services. Activities will focus on improving land and labor productivity, broaden access to productive assets, technology, information, and credit, diversification of agricultural products, and access to markets, including traceability and differentiation strategies. Unlocking agricultural finance for productive investments, strengthening productive and entrepreneurial capacity of producers, developing short value chains and market linkages will stimulate economic activities in rural areas and can lead to the creation of jobs. It will also create capacity for better absorption of IPARD funds for improving the rural development of Serbia, while also strengthening alignment to EU CAP.

25. The component is structured into two sub-components: (i) Improving entrepreneurial capacity – focusing on capacity building activities required to formulate business plans, investment decisions and financial support, from public and private sources; (ii) Improving productivity and competitiveness – comprising investments in equipment and technical assistance to support their implementation. The detailed description of the sub-components is provided below.



### ***Sub-component 1.1: Improving productive and entrepreneurial capacity (US\$5 million)***

26. This sub-component will focus on technical assistance to producers, producer groups and agri-businesses for the formulation of business plans that normally bundle three key elements: i) investment in equipment, ii) working capital, and iii) technical assistance for productivity improvement and entrepreneurial capacity. The sub-component will finance the preparation and implementation of business plans for proposed investments, including: (i) business skills and organizational training for small-scale producers; (ii) preparation of subprojects, including information on financial cash flow as per bank requirements, including the formulation of matching grants<sup>15</sup> for capital investments in equipment, machinery, processing units<sup>16</sup>, packaging, storage, etc., (iii) specific technical studies and consultancies that would contribute to the implementation and the execution of approved business plans; (iv) a communication strategy designed to raise awareness of and stimulate participation of the SME agribusinesses in the project; (v) support banks with developing methodologies suitable for assessing credit for the types of investments and beneficiaries of the project.

27. The scope of the business plan will depend on the capacity of producers and the complexity of the sought investment. Activities will take place on- and off-farm. To enable greater participation of potential beneficiaries, emphasis will be placed on improving the entrepreneurial capacity of producers by providing technical assistance and seed capital for analysis of investment options. The business plans will also include public good/ compliance elements (environmental and social aspects, food safety compliance, etc.). Strict eligibility criteria will be set forth to enable the participation of small and medium producers. The selection and eligibility criteria and the governance and management aspects of the matching grants will be detailed in a Grant Operational Manual to be formulated during project preparation.

### ***Sub-component 1.2: Improving productivity and competitiveness (US\$30 million)***

28. This sub-component will focus on improving the productivity and competitiveness of project beneficiaries through specific investments, as defined in the business plans and implemented through matching grants (defined in Component 1). The total cost of the business plan depends on the type of investment, the amount of working capital and the scope of the technical assistance. This cost also varies by the productive activity and the typology of the producers. For example, in Montenegro (under the MIDAS project), the total cost for agricultural producers ranges between 10,000 and 70,000 euros, while for agricultural processors it ranges between 50,000 and 250,000 euros. In Kosovo, the range for producers ranges between 10,000 and 100,000 euros, while for processors it is between 30,000 and 400,000 euros. The project will finance only a share of this cost (through a matching grant of typically 50%), as a one time incentive to leverage private investment, including own resources and/or credit.

29. The sub-component will finance i) the use of good environmental and agricultural practices to improve on-farm productivity, ii) in on-farm inputs and equipment required for the optimization of production and/or diversification, as well as technical advice for the use inputs, technologies, alternatives, etc., iii) support digital agriculture approaches to improve productivity on-farm and enhance linkages between producers and markets, iv) support compliance with food safety standards, traceability, geographic denomination of origin and other market-related activities as part of the improvement of the competitive position of beneficiaries; v) carry out market demand assessments to identify differential market potential for products; vi) support beneficiary participation in trade fairs and other events; vii) support the commercialization of agricultural products by improving access to medium-term finance, providing start-up capital for

<sup>15</sup> There is a strong public good argument for using matching grants – stimulate cross compliance (improving environmental outcomes), stimulate use of innovations, new technologies, development of skills, modernization, horizontal integration, financial inclusion. Through the project, capacity for the use of matching grants will be improved in the sector, which can lead to a consecutive better absorption of IPARD grants.

<sup>16</sup> Under IPARD grants, investment grants for processing facilities is only provided for new structures; national rural development program can provide investments for rehabilitation and upgrade of existent facilities.



small- and medium-sized farms involved in productive partnerships, and by ensuring the availability of financing for value chain support. Considering the high risk of lending to small producers, the project will support the enabling environment for de-risking by working with existent public credit guarantee funds. There are various guarantee schemes applicable to Serbian agriculture and, in particular, the EIF and DCA<sup>17</sup>, which the project seeks to leverage as a risk mitigating mechanism for crowing-in private investment through lending by commercial banks.

## **Component 2: Improving the capacity of MAFWM to support modern agriculture (US\$10 million)**

30. The objective of this component is to improve capacity of MAFWM and related agencies to facilitate the enabling environment for improved sector performance through evidence-based policy making and provision of public goods, such as information systems and open data platforms. A digital platform for decision making<sup>18</sup> will benefit all agricultural producers of Serbia, whether they apply for support through IPARD or national program or don't. A unique registry system<sup>19</sup> would be required to support decision making and to also support pension reform efforts in the country.

### ***Sub-component 2.1: Improving information systems***

31. This sub-component will support the Ministry of Agriculture Forestry and Water Management (MAFWM) to modernize its information systems and strengthen its decision-making capacity, through the improvement of hardware, software and human capacity for information support to the sector. Modernizing the information systems is critical in the process of alignment to EU CAP, including sanitary and phytosanitary (SPS) delivery and monitoring, advisory information, land parceling (LPIS), paying agency data management, etc. In addition, the project will support a digital producer identification card ("one card") to enable the better monitoring of the access to resources, support services and information by all farmers in the country. The project will finance the following: i) technical assistance to improve the coordination within and across existing information systems across Directorates and enhance delivery of information for decision making at different levels; ii) acquisition of hardware and software to improve the scope, functionality and compatibility of information systems and establish digital data collection and processing of current paper-based processes.

32. The project will also assist the Ministry of Agriculture Forestry and Water Management (MAFWM) with technical assistance to develop capacity to assess the demand, structure, and modalities for agricultural Guarantee agency in Serbia, similar to these in other neighboring and EU countries, with the potential of establishing in the medium term such a guarantee agency (state-owned or PPP). Options to capitalize the guarantees would also be part of the assessment.

### ***Sub-component 2.2: Open data platform***

33. This sub-component will establish an open, public information platform where key information is accessible to all agriculture stakeholders. The project will finance the software, hardware and technical assistance required for the set-up

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<sup>17</sup> Two public donor guarantee schemes with agricultural windows are expected to be available in early 2020 – European Investment Fund (EIF) (backed by EU funding) and the DCA (guarantee facility of USAID), still under negotiations with MAFWM – and can be tapped on by commercial banks in the first couple of years of project implementation. IFC is already engaged with the EIF. Although a public guarantee fund exists in Serbia (the Serbian Development Fund, SDF), it is weak and does not cater to agriculture. Hence, a capacity building (through a TA) activity may be warranted under the project to provide guidance on future needs by the public sector for unlocking private investment in agriculture.

<sup>18</sup> A PHRD grant on strengthening M&E capacity of MAFWM, implemented in parallel to this project, will support this platform through capacity building within the Ministry and technical assistance, as needed.

<sup>19</sup> For example, only farm household applying for IPARD grants are registered in the national farm registry (around 335,000), excluding a large number of agricultural producers.



and functionality of the platform. Access to important production and market information, including weather variables, prices of key products, etc. is critical for on and off-farm decisions. This platform can also be a support system for advisory services in Serbia and can link to digital approaches on farm, ensuring a two-way communication on plan and animal health, and other risks that can constrain agricultural competitiveness. Maintaining the content and enabling public access to this platform is a key role that the Ministry can play in the enabling environment for agricultural sector transformation.

34. A digital information platform can play an important role for the spatial tracking and connectivity of production and market demand, thus contributing to improved positioning of products, sales and overall competitiveness. In addition, by including weather and climate information modeling, the project could contribute to early warning systems, helping producers to better prepare and adapt to changing climatic conditions. The project will use existing digital agriculture tools and will collaborate with private sector IT companies for finetuning electronic delivery mechanisms for monitoring production, access to technical information, traceability of goods and identification of market opportunities.

**Component 3: Project Management, Monitoring and Evaluation (US\$5 million)**

35. This component will support the establishment of a project management team (PMT) in the Directorate of Agrarian Payments (DAP) and capacity needs related to project implementation, as well as project monitoring, including a comprehensive baseline, mid-term review and a final impact assessment of project investments.

Legal Operational Policies	Triggered?
Projects on International Waterways OP 7.50	No
Projects in Disputed Areas OP 7.60	No

Summary of Screening of Environmental and Social Risks and Impacts

The project is classified as Moderate Risk taking in account the low risk nature of the interventions, the limitations on implementation capacity, the application of environmentally friendly practices and new technologies, and the difficulty of enforcing workers’ rights in multiple SME agribusinesses. No adverse impacts such as involuntary land acquisition, impacts on community health and safety, on cultural heritage, are expected. Some of the project funded activities may include support to small scale community agriculture that is undertaken within areas under some level of environmental protection. The project will introduce new technologies and support improvement of technical knowledge and skills of beneficiaries on, amongst other, water and energy efficiency, pollution prevention and best practice use of herbicides and pesticides. The project’s anticipated social impacts are predominantly positive, such as increased income and employment in the agricultural sector as well as protection from climate related economic losses for farmers through the introduction of an early warning system. As labor informality is prevalent in the agricultural sector, the Borrower will prepare Labor Management Procedures to manage risks related to workers’ rights in project supported agribusinesses. The environmental and social screening criteria developed for the agricultural grant schemes and the credit guarantee fund will screen for relevant risks and apply mitigation hierarchy.

**Note** To view the Environmental and Social Risks and Impacts, please refer to the Concept Stage ESRS Document.



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