Document of
The World Bank

Report No: 34756

IMPLEMENTATION COMPLETION REPORT
(IDA-40170)

ON A

CREDIT

IN THE AMOUNT OF US$45 MILLION

TO

SERBIA AND MONTENEGRO

(REPUBLIC OF SERBIA)

FOR

SECOND STRUCTURAL ADJUSTMENT CREDIT

December 29, 2005

Macroeconomics 2
Europe and Central Asia

CURRENCY EQUIVALENTS

(Exchange Rate Effective December 13, 2005)

Currency Unit	=	CSD (Serbian Dinar)
CSD1	=	US$ 0.01378
US$ 1	=	CSD72.95

FISCAL YEAR

January 1 - December 31

ABBREVIATIONS AND ACRONYMS

CAS	Country Assistance Strategy
EPS	Electric Company of Serbia
EU	European Union
FIAS	Foreign Investment Advisory Services
GDP	Gross Domestic Product
ICA	Investment Climate Assessment
ICR	Implementation Completion Report
IMF	International Monetary Fund
LDP	Letter of Development Policy
MOP	Material Support to Families Program
MPALSG	Ministry of Public Administration and Local Self-Government
PAR	Public Administration Reforms
PFSAC	Private and Financial Sector Adjustment Credit
PIU	Project Implementation Unit
PPFDPC	Programmatic Private and Financial Sector Development Policy Credit
PPSDPL	Programmatic Public Sector Development Policy Loan
RIA	Regulatory Impact Assessment
SAA	Stabilization and Association Agreement
SAC	Structural Adjustment Credit
SaM	Serbia and Montenegro
SDR	Special Drawing Rights
SOSAC	Social Sector Adjustment Credit
TSS	Transitional Support Strategy
USAID	United States Aid for International Development
ZTP	Serbia Railways

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SERBIA AND MONTENEGRO
Second Structural Adjustment Credit (Republic of Serbia)

CONTENTS

Project ID: P078457	*Project Name:* Structural Adjustment Credit 2 (SAC 2) (Serbia)
Team Leader: Abebe Adugna	*TL Unit:* ECSPE
ICR Type: Core ICR	*Report Date: December 29, 2005*

1. Project Data

Name:	Structural Adjustment Credit 2 (SAC 2) (Serbia)	*L/C/TF Number:*	IDA-40170
Country/Department:	SERBIA AND MONTENEGRO	*Region:*	Europe and Central Asia Region

Sector/subsector: Central government administration (25%); Other social services (25%); General industry and trade sector (25%); Power (25%)

Theme: Legal institutions for a market economy (P); Regulation and competition policy (P); Social safety nets (S); Administrative and civil service reform (S); Corporate governance (S)

KEY DATES			*Original*	*Revised/Actual*
PCD:	11/25/2003	*Effective:*	12/22/2004	12/22/2004
Appraisal:	09/14/2004	*MTR:*		
Approval:	12/16/2004	*Closing:*	06/30/2005	06/30/2005

Borrower/Implementing Agency: Serbia and Montenegro/REPUBLIC OF SERBIA

Other Partners:

STAFF	Current	At Appraisal
Vice President:	Shigeo Katsu	Shigeo Katsu
Country Director:	Orsalia Kalantzopoulos	Orsalia Kalantzopoulos
Sector Director:	Cheryl W. Gray	Cheryl W. Gray
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2. Principal Performance Ratings

(HS=Highly Satisfactory, S=Satisfactory, U=Unsatisfactory, HL=Highly Likely, L=Likely, UN=Unlikely, HUN=Highly Unlikely, HU=Highly Unsatisfactory, H=High, SU=Substantial, M=Modest, N=Negligible)

Outcome:	S
Sustainability:	L
Institutional Development Impact:	M
Bank Performance:	S
Borrower Performance:	S

	QAG (if available)	ICR
Quality at Entry:	S	S
Project at Risk at Any Time:	No	

3. Assessment of Development Objective and Design, and of Quality at Entry

3.1 Original Objective:

Context. The Republic of Serbia embarked on an ambitious economic reform program in January 2001 with the objective of ensuring a rapid transition to an open market economy, normalizing relations with international financial markets, and integrating its economy with the European Union. The reform objectives and measures were outlined in the Government's medium-term Economic Recovery and Transition Program. The government's economic program rested on three pillars: (i) more prudent macroeconomic policies; (ii) market-oriented structural reforms to improve the efficiency and flexibility of the economy; and (iii) the mobilization of significant financial and technical support from donors.

Stabilization policies have focused on aligning fiscal deficits with available sources of non-inflationary financing and reducing quasi-fiscal deficits. Progress in implementing structural reforms has been significant, although uneven across sectors. Notable advances have been made in the following areas: price and foreign exchange liberalization (including early current account convertibility); opening the country to trade and investment; management of public finances; tax policy; privatization; bank resolution; energy; the labor market; pensions and social assistance. In most areas, however, reforms are still incomplete, and in several (e.g., public administration, health care, and the restructuring of major utilities) the reform process remains at an early stage.

The reform program has been supported by the IMF, World Bank, the European Union, and other bilateral development partners. The IMF has, to date, supported the reform program through three successive arrangements--most recently by a three year long Extended Arrangement of SDR 650 million spanning the period through end-December 2005.

The implementation of the economic program was successful in restoring macroeconomic stability and growth. Serbia's retail price inflation declined from 113.5 percent in 2000 to 14.8 percent in 2002 and further to 7.8 percent in 2003. Following the sharp contraction in 1999, SaM's GDP (the Republic of Serbia accounts for about 93 percent of SaM's GDP) grew by 5.5 percent and 4 percent in 2001 and 2002, respectively. By 2003, however, the initially buoyant recovery slowed down due mainly to the political uncertainty created by the assassination of the Serbian Prime Minister Zoran Djindjic in March 2003, and the decision to hold early Serbian parliamentary elections in December 2003. Real GDP growth thus slowed to 3 percent in 2003.

Objectives of SAC 2: Serbia Second Structural Adjustment Credit (SAC 2) was designed to support the Government of the Republic of Serbia to deepen the structural reforms needed to place the economy on a more solid basis for enhanced fiscal discipline, enduring growth, and a move toward European structures. This was to be accomplished through the implementation of structural reforms in four policy areas: (i) reforms of the business enabling environment; (ii) improving performance in the energy sector; (iii) strengthening social protection; and, (iv) improving public administration. These objectives reflected essential priorities for Government of the Republic of Serbia at that time, as identified both by the government's PRSP and by the Bank's Country Assistance Strategy. The Credit was a one-tranche operation, with SDR 30.1 million (US$45 million equivalent) disbursed upon effectiveness in December 2004.

Links with previous operations. The World Bank had supported the Serbian Government's reform agenda since 2001, as outlined in the Bank's Transitional Support Strategy (TSS) produced on June 26, 2001 and updated in August 2002 and February 2004. A multi-sectoral Structural Adjustment Credit (SAC1, approved in January 2002) was designed to enhance fiscal sustainability through reforms of public expenditure management, the energy sector, social protection, labor markets, and health care. A Social Sector Adjustment Credit (SOSAC, approved in April 2003) aimed at supporting reforms in pensions, health and labor, while enhancing the focus on social assistance and poverty monitoring. Two Private and Financial Sector Adjustment Credits (PFSAC1 and PFSAC2, approved in May 2002 and June 2003) aimed at promoting growth through: (i) strengthening the financial system via the liquidation of troubled banks and an improved policy and regulatory environment; (ii) privatizing and restructuring socially-owned enterprises; and (iii) improving the investment and business climate. Therefore, the reform areas supported Serbia SAC 2, with the exception of public administration reform, constituted a continuation and deepening of the reform efforts that had been initiated by the World Bank's previous adjustment operations in Serbia.

3.2 Revised Objective:

The objective was not revised.

3.3 Original Components:

Serbia SAC 2 had five components: (a) maintaining macroeconomic stability; (b) improving the business climate; (c) improving the performance of the energy sector and enhancing institutional development; (d) strengthening social protection; and (e) improving public administration. Each of these components is briefly described below.

A. Macroeconomic Performance. As with all structural adjustment operations, SAC 2 required satisfactory macroeconomic performance, although there were no tranche conditions linked specifically to macroeconomic outcomes.

B. Investment Climate. Serbia's weak business environment limited the development of a strong private sector capable of generating growth and employment. Serbia SAC 2 sought to support the government to improve business entry and corporate governance, contract enforcement, and regulatory capacity, mainly through supporting legislative changes.

C. Energy Sector. The energy sector reforms under SAC 2 aimed to improve financial and operational sustainability of the power company, *Elektroprivreda Srbije* (EPS), on a stand alone (off budget) basis; support power sector commercialization; and ensure that risks associated with potential adverse impacts of increased electricity tariffs on the poor were mitigated.

D. Social Protection. Serbia's PRSP and Serbia Poverty Assessment (2004) highlighted that the key priorities in social protection were enhancing effectiveness of the safety net through expanded coverage, greater adequacy of benefits and improved targeting; mitigating the adverse impact of changes in the level and structure of electricity tariffs on the poor; and, strengthening coordination between social protection programs and energy-related subsidies. SAC 2 focused on supporting the Government to: (i) improve the effectiveness of Serbia's safety net; and (ii) put in place a program to mitigate the adverse impact of increases in electricity tariffs on the poor.

E. Public Administration. Serbia had inherited a legacy of politicized and fragmented public administration, ill-suited to performing its expected role in a modern market economy and democratic system. After the change of regime in 2000, the new Government of Serbia expressed strong interest in the reform and modernization of its public administration. The Government established the Civil Service Council (CSC) to design the reform process, and later the Ministry of Public Administration and Local Self-Government (MPALSG), with the responsibility to unify and coordinate all public sector reform activities. Reform goals supported under SAC 2 aimed at setting the stage for the implementation of a medium-term Public Administration Reform (PAR) agenda, including (i) the formulation and adoption of a

PAR strategy and action plan; (ii) creation of effective PAR management structures; and (iii) design of pay reform for the civil service.

Linkages of Component Design to Objectives. Design of the Credit's components was well linked to the general objectives described above. By improving the investment climate and introducing energy sector reforms that promote cost recovery price and commercialization, the Credit sought to directly support higher growth and fiscal discipline, although no assessment was done of the total fiscal impact of the operation. By supporting the implementation of the new social welfare law and the electricity price subsidy scheme for the poor, the Credit sought to mitigate the social impact of reforms on the poor and vulnerable. By introducing the long-haul public administration reforms, the Credit sought to support Serbia's efforts in moving its public administration system towards European structures and standards.

3.4 Revised Components:

The components were not revised.

3.5 Quality at Entry:

Quality at entry is rated satisfactory based on: (i) the Credit's consistency with Government priorities, and Bank priorities; (ii) the Credit's solid analytical basis that informed the policy areas to be supported; and, (iii) the close coordination with other donors, including the IMF, and the common goals shared by the donor community in Serbia. Each of these is briefly discussed below.

Consistency with Government priorities. SAC 2 aimed to support the Government's structural and institutional reform agenda in four policy areas, as outlined in the Letter of Development Policy and Policy Action Matrix. The tranche conditions listed in the Development Credit Agreement were cross-referenced with specific paragraphs in the LDP, reflecting the close mutuality of purpose between the Credit and the Government's program. SAC 2 was also consistent with the objectives of Serbia's PRSP, developed in 2004, which aimed to create dynamic and sustainable growth, with emphasis on job creation, as well as an efficient and transparent public administration system. The structural reforms were also fully consistent with, and indeed supportive of, the overarching aspiration of Serbia to join the European Union, and the Stabilization and Association Process (SAP) framework that guided Serbia's harmonization efforts with European structures.

Consistency with Bank priorities. Serbia SAC 2 was an integral part of the first joint Bank-IFC FY05-07 CAS for Serbia and Montenegro, which was presented to the Board in parallel with SAC 2. Consistent with the overall economic objectives set in the Stabilization and Association Process (SAP), which contains the framework for Serbia's eventual joining of the EU, and Serbia's PRSP, the CAS rested on three pillars (i) creating a smaller, more sustainable, more efficient public sector; (ii) creating a larger, more dynamic, private sector; and (iii) reducing poverty, and improving social protection and access to social services, particularly for poor and vulnerable populations. SAC 2 supported the continuation of structural reforms that had been initiated under the World Bank's previous adjustment operations in Serbia and represented a bridge between the Bank's earlier support and the programmatic loans envisaged in the new CAS. The reform measures in SAC 2 were designed to support the policy goals of the new CAS by enhancing fiscal discipline, encouraging a strong private sector response as well as employment creation, and setting the stage for deeper reforms aimed at improving public administration. Measures in SAC 2 were also essential to strengthen social protection and to mitigate the adverse impact of the energy sector reform measures on the poor.

Analytical basis for program design. The focus on the four key policy areas supported by SAC 2 was underpinned by the Bank's economic sector work and intensive dialogue with relevant counterparts. The

World Bank's analytical background work included: Recent Progress on Structural Reforms (2003), which took stock of the status of structural reforms; Serbia Investment Climate Assessment (2004), which guided the business environment reform component; Serbian Energy Sector: Status, Key Issues and an Agenda for Action (2003), which supported the reform design in the energy sector; Serbia and Montenegro Poverty Assessment (2003), which, among other areas, highlighted the priorities within the social protection and impact mitigation; and Serbia and Montenegro Public Administration Development: Creating the Conditions for Effective Economic and Social Reform Policy Note(2004), which constituted the basis for the design of the public administration reforms.

Donor coordination. Both the IMF and the Bank along with the donor community shared the goals of achieving a credible fiscal adjustment and macroeconomic stability, and placing the Serbian economy on a sustainable growth path. During the preparation of this operation, Fund and Bank staff as well as the key donors such as EU and USAID cooperated closely to ensure consistency between not only the stabilization and structural adjustment measures but also between the reforms that were supported by different donors. SAC 2 complemented the IMF macroeconomic program in Serbia, and supported Serbia's objective of bringing its economic structure in line with the EU standards.

4. Achievement of Objective and Outputs

4.1 Outcome/achievement of objective:

The outcome is rated satisfactory as the Credit achieved its objectives with respect to all components (see below).

4.2 Outputs by components:

The Credit's outcome for each component is discussed below.

A. Macroeconomic performance. This component is rated satisfactory. The satisfactory macroeconomic rating reflects a balance between some overperformance relative to projections in the Project Document in growth and fiscal policy, and some underperformance in reducing inflation and the current account deficit (Table 1). The macroeconomic scenario supported by SAC 2 has been consistent with that of the IMF, and the IMF program has been on track.

Table 1. Republic of Serbia: Key Macroeconomic Outcomes: Projected vs. Actual, 2002-2005

	2004		2005	
	Projected	Actual	Projected	Actual/ Current Projection
Real GDP Growth	6	8.6	4.6	4.6
Inflation	12.6	13.4	9.6	12.3
General Government Deficit (before grants)	-2	-0.3	0.7	1.2
Current Account Balance	-10.7	-13.1	-10.2	-9.5
External Indebtedness	57.8	62	56.4	57.1
Investment/ GDP	16.5	17.6	17.8	18.4

The actual 8.6 percent growth of real GDP in 2004 exceeded the 6 percent growth rate projected under the Credit. Similarly, the general government deficit for 2004 (0.3 percent of GDP) was significantly lower than projected under the Credit (2 percent of GDP), mainly because fiscal policy was tightened beyond program targets to contain the external imbalance and inflation. The tight fiscal policy stance is expected to continue in 2005, leading to a surplus of about 1.2 percent of GDP, again higher than the surplus of 0.7 percent of GDP projected under the Credit. On the other hand, inflation at about 13.4 percent in 2004, was slightly above the originally projected target of 12.6 percent under the Credit, owing mainly to one-off factors including the introduction of the VAT, increases in tariffs for municipal services, and rising oil prices. Also, the current account deficit was higher than programmed under the Credit in 2004 due mainly to higher than projected trade deficit. The current inflation projection for 2005 is also higher than the original projection—12.3 percent vs. 9.6 percent—on account of demand pressures and rising oil prices. Some exogenous factors such as high oil prices contributed to the unexpectedly high inflation and current account deficit. The IMF's extended arrangement with SaM has continued to focus on reducing Serbia's relatively high inflation and current account deficit.

Serbia SAC 2 contributed to improved macroeconomic environment, including the high growth rates in 2004 and 2005. Although the Credit did not assess with any specificity the fiscal impact of the energy sector reforms, the introduction of energy sector tariff adjustment in line with cost recovery contributed to reducing the overall fiscal burden imposed by that sector. The business environment reforms had a positive impact on investment as Serbia's investment as percentage of GDP in 2004 increased significantly, from 16.1 percent in 2003 to 17.6 percent in 2004. As a result of these reforms, there has also been a significant increase in the number of limited liability companies registered per annum—from about 6000 new companies in 2004 to about 10,000 new companies in 2005.

B. Business Climate. **This component is rated highly satisfactory.** This rating reflects the fact that medium term outcome indicators have evolved much better than had been anticipated under the Credit (as discussed below). The reforms under SAC 2 focused on introducing new laws essential for improving the business climate. More specifically, with the support of SAC 2, the Republic of Serbia:

- **Enacted a new Company Law.** The new Law introduced several signficant improvements, including consistency with the requirements of EU Company Law Directives. The minimum capital requirement was reduced from USD5,000 per company to 500 euros per company, with no requirement for capital maintenance. Two types of joint stock companies, namely closed and open, were introduced. A new closed company would be free of capital maintenance requirements and would be free to impose restrictions on the transfer of its shares, but could not offer its shares publicly and may not have more than 100 shareholders unless it adopts and agrees to follow the rules and requirements for an open company. The law expanded and clarified a director's legal duty of care and duty of loyalty to the company, introduced the concept of "personal interest", simplified the structure of the board, made the establishment of a supervisory board optional and provided for directors to be elected only by the shareholders and only for one-year terms—all with a view to encourage good corporate governance. Finally, the law provided detailed provisions for merger, division, and conversion of a company from one form to another, imposed new disclosure and other requirements on companies and persons who control a company, and provided new rules for the liquidation of a company outside bankruptcy.

- **Enacted a new Law on Execution Procedures.** With the support of SAC 2 the Government prepared a new Law on Execution Procedures. After consultation with the public and other stakeholders, the new Law was adopted by the Government in October 2004 and was subsequently enacted in November 2004. The most important improvements of the new Law included: new types of injunctions, especially in commercial matters, that will strengthen the position of the creditor; a special regulation and procedure for enforcement in commercial matters; significant changes in legal remedies (introduction of appeals, precise definition of reasons for both legal remedies and short time limits provided for decisions on legal remedies); the possibility to postpone enforcement but for only a narrow set of reasons; and, a clearer regulation of the position and responsibilities of courts.

- **Increased its regulatory impact assessment capacity.** Amendments to the Rules of Operation of the

Government requiring the responsible ministry to prepare a justification statement for a new law, a decree and an order in line with the OECD Regulatory Impact Assessment (RIA) were made in October 2004. Since then RIA is mandatory for all new legislation and decrees, and a *Regulatory Reform Council* and a small technical secretariat have been established to facilitate and guide the process. Since October 2004, an RIA has been carried out for more than 60 draft laws. In some cases, the RIA has led to amendment of laws to reduce the regulatory burden on the private sector. However, the still limited capacity and resources of the technical secretariat need to be further increased to enhance sustainability.

Progress toward medium-term outcomes. The medium-term outcomes of the Credit were stated as: (i) increasing in the number of limited liability companies registered per annum; (ii) a more efficient enforcement of judicial decisions and commercial contracts as measured by the Enforcing Contract Indicators; and, (iii) a steady increase in the use of RIA of legislation. The adoption of the Company Law and Law on Execution Procedures, together with the Business Registration Law in May 2004 and the Bankruptcy Law in July 2004 under PFSAC 2, laid the foundations for an improved entry and exit regime in Serbia. According to the new Doing Business Study of the World Bank (2006), Serbia was rated among the top reformers during 2004-05. Serbia significantly reduced enterprise entry time from 51 days in 2004 to 15 days in 2005; the number of procedures was reduced from 11 in 2004 to 10 in 2005; and the average duration of court cases was reduced from 1028 days in 2004 to about 600 days in 2005. As a result of these reforms, there has been a significant increase in the number of limited liability companies registered per annum—from about 6000 new companies in 2004 to about 10,000 new companies in 2005. Serbia now has a more efficient enforcement of judicial decisions and commercial contracts as measured by the Enforcing Contract Indicator. As mentioned above, there has also been a steady increase in the use of RIA, as over 60 laws have become subjected to RIA since October 2004.

C. Energy Sector. **This component is rated satisfactory.** This rating reflects the fact that all conditions were met and there is good progress towards achieving the medium term outcomes. With the support of SAC 2, the Republic of Serbia:

- **Enacted the Energy Law and set up an independent Energy Regulator.** The new Energy Law is consistent with best practice for the region and entered into force in July 2004. The Law detailed the institutional aspects of the regulatory framework together with broad regulatory rules (e.g. tariffs will be set to cover costs). The Law serves as the basis for further energy sector reforms, including regulatory development, tariff reform, Elektroprivreda Srbije (EPS) restructuring, and energy market liberalization. Following the enactment of this law, an independent energy regulator was established in June 2005. Staffing of the regulatory agency, although not yet complete, is underway, and the agency is expected to be operational by January 2006. In addition, the Government adopted an Energy Strategy that explained the vision behind the Energy Law, and laid a foundation for further energy sector reforms and investment.

- **Helped improve payment discipline and commercialization of the energy sector.** Specific steps taken under the Credit included: (i) offering more than four of EPS' large electricity debtors for sale, with two of them or viable parts thereof sold; (ii) increasing the tariff level to maintain an approximately constant real tariff in July 2004 relative to 2003; (iii) reforming the existing tariff structure by reducing the first block tariff to 350kWh; (iv) maintaining a net hiring freeze at EPS; and (v) adopting a Government decision to separate ownership of power generation and transmission businesses. A separate transmission business (EMS) became legally operational in July 2005.

Progress toward medium-term outcomes. SAC 2 recognized that the reforms supported under the Credit were only near-term steps in a longer-term program with the ultimate objective of attaining a financially sustainable and operationally efficient power industry. The medium term outcomes of the operation were thus cautiously stated as: (i) full staffing of the Energy Regulator and the adoption of business plan; (ii) maintaining ongoing financial viability of EPS defined as positive operating cash flow; and (iii) maintaining residential collections ratio in the range of 92-95 percent. As of the time of this assessment, the Government has made good progress in staffing the regulatory agency, with about 10 of the 35 total positions filled. The regulatory agency is on course to become fully operational in the first half of 2006, and among its immediate priorities is the develoment of a tariff schedule for cost recovery. In terms of improving financial viability, the tariff adjustment for 2004 was fully in line with what was agreed under the Credit, while in 2005 there has been an average increase in the electricity tariff of 9.5 percent. Collection rate for residential consumers has been in line with benchmarks, rising from 91-92 percent in 2004, to 93 percent in 2005. Improving collections from industrial consumers, however, remains a big challenge. Despite some progress under the Credit in tackling the biggest industrial debtors of EPS through offering them for sale, a continued effort is needed. In 2005, the Ministry of Mines and Energy has submitted an additional list of the 15 largest non-payers of electricity to the privatization agency for action, but progress with privatization has been slow. The challenge in the future is to have a regulatory framework that allows for cost recovery, while providing incentives for EPS (or its successor companies) to perform efficiently in comparison with other participants in the evolving regional energy market. A recently approved, follow-on Bank operation, the first programmatic Private and Financial Development Policy Credit (PPFDPL1), directly builds on the SAC 2 reforms by introducing measures to minimize supply disruptions and improve the operating cash flows of EPS.

D. Social Protection. This component is rated marginally satisfactory. This rating reflects the fact that while all conditions under the Credit were met, the medium term impact has been weaker than expected (see below). With the support of SAC 2, the Republic of Serbia:

- **Ensured full implementation of the Social Welfare Law, which expanded coverage of Serbia's main social safety net program**—the Material Support to Families Program(MOP). The enactment of the Social Welfare Law had been a key condition of another previous Bank operation, the Social Sector Adjustment Credit (SOSAC). The implementation of the Law, however, hinged on the availability of adequate funds in the 2004 and 2005 state budgets. The Credit helped ensure an increase in the budgetary allocation for the implementation of the MOP of about 20 percent (from about 0.1 percent of GDP prior to the Law), allowing a modest expansion in coverage. With the implementation of the Law, the number of recipients of social welfare (cash) assistance was expected to increase from about 43,000 families to about 56,000 families.

- **Helped mitigate the adverse welfare impact of increased electricity tariffs on the poor.** With the support of SAC 2, the Government introduced a new mitigation scheme to support the poor and vulnerable population, whereby recipients of child benefit, minimum pension and MOP were entitled to a discount of 30% of the monthly bill on consumption up to 300 kWh. Also, the Government established an inter-agency group (involving the Ministry of Mines and Energy, EPS, and the Ministry of Labor, Employment and Social Welfare) to oversee the implementation of the mitigation scheme. The program was introduced in the summer of 2004. When it was introduced, it was expected that about 80,000 (and at least 50,000) new poor households would become beneficiaries of the scheme, thereby increasing the total number of families from a previous estimated 20,000 to about 100,000.

Progress toward medium-term outcomes. This was weaker than expected. The stated medium-term outcomes for the Credit were that: (i) 13,000 new beneficiaries would be covered by MOP; and (ii) a minimum of 50,000 new beneficiaries would be protected by the energy sector social safety nets. While the reforms supported by the Credit did bring 8,000 additional poor and vulnerable families into the MOP program, this was less than the expected increase of 13,000 families. This was not due to the inadequacy of budget, but rather to the limited public information campaign about the MOP program, and the weak outreach efforts of the local social welfare centers. As concerns the electricity subsidy program, only 17,000 additional families benefited from the assistance (versus the originally planned 50,000 new households). While the reasons for this shortfall are many, two factors appear especially important. First, many poor families faced 'technical' problems in meeting the eligibility criteria for the scheme, such as not having their own electricity meter or living in illegally constructed buildings. Second, a key condition for accessing the subsidy was that the families remained current on their electricity bills—a rather stringent condition for many poor households to meet. Also, discussions with the authorities during this assessment suggested that this scheme may not be as well targeted as Serbia's MOP program (discussed above). While Serbia's MOP program is well targeted and the actions needed to expand its coverage are clear (increase information campaign and outreach at the local level), a more rigorous evaluation of the electricity subsidy program is warranted going forward.

E. Public Administration. This component is rated satisfactory. This rating reflects the fact that all conditions were met and progress towards medium term outcome has been good, with faster than expected progress in reaching legislative milestones. With the support of SAC 2, the Republic of Serbia:

- **Enacted a Public Administration Reform Strategy and Action Plan.** The Public Administration Reform (PAR) Strategy and the related Action Plan were first endorsed by the PAR council in October 2004, and subsequently adopted by the Government of Serbia in November 2004. The Strategy is anchored in European principles and standards—professionalization, de-politicization, rationalization, decentralization and modernization—and lays the foundation for creation of a merit-based and de-politicized civil service and for the rationalization of administrative structures in the central state administration. The focus of the strategy is on the central state administration and local (self) government and other parts of the public sector are not included. The Action plan elaborates concrete priority activities and the deadlines for their implementation.

- **Introduced a clear horizontal public administration reform management structure**. The development and implementation of the PAR strategy was assigned to the Ministry of Public Administrtaion and Local Self Government (MPALSG), and its capacity was strengthened through an accelerated recruitment effort by the new minister and by the integration of the former Agency for Public Administration Development in the structure of the Ministry. The drafting work on PAR legislation was taken over by the Office for Legislation at the Government, which built up the technical capabilities to ensure that draft laws were of appropriate quality. A small group of experts was assigned responsibility for drafting the legislative framework. A clear structure was put in place, and appropriate resources were allocated to manage the PAR process.

- **Reviewed the Serbian civil service wage system to develop reform proposals**, which was subsequently endorsed by the Public Administration Reform Council, outlining the direction of pay reforms. The proposed elements of wage reform included: (i) a pay and grading system; (ii) development of a performance appraisal system linked to the salary system; (iii) the systematization process; (iv) de-politicization; and (v) integrating staff development with career advancement.

Progress toward medium-term outcomes. It was recognized in SAC2 that the reforms to be supported represented the first steps in a very long reform program. The medium term outcome indicators specified in the Credit were: (i) adoption of basic laws (Law on Government, Law on Civil Service, Law on Public Agencies, Law on State Administration, and Law on Salaries) that would provide the foundation for modern and competitive civil service; (ii) a Law on Salaries that sets a minimum compression ratio in civil service pay of 1:6; and (iii) effective implementation of PAR according to set deadlines. With the exception of the Law on Salaries, all the basic laws have been adopted. On salaries, the Government has introduced interim salary system reforms through the 2005 budget, which have decompressed the wage system. Salaries of high management positions, subject to Government appointment, such as Deputies, Assistants and Secretaries of the Ministry have been increased substantially. In this way, the decompression ratio has been extended from 1:4.9 to 1:8. The next step in the overhaul of the salary system is the adoption of the Law on Salaries in the civil service, which is in a drafting stage and expected to be adopted in the second quarter of 2006. Up to now, the deadlines for finalization of various PAR activities set out by the Action plan have not been fully respected and continued efforts are needed to perform the envisaged tasks in an efficient and effective manner. Full implementation of all PAR laws, including the Civil Service Law, the Law on State Administration, the Law on Salaries and the Law on Ombudsman, is one of the key conditions in the follow-on Bank operation in Serbia currently under preparation, the first Programmatic Public Sector Development Policy Loan (PPSDPL1).

4.3 Net Present Value/Economic rate of return:

Not applicable.

4.4 Financial rate of return:

Not applicable.

4.5 Institutional development impact:

The institutional development impact of the Credit is rated as modest. As a one-tranche adjustment operation, SAC2 was not expected to have significant institutional development impact. Nonetheless, the Credit did have several notable institutional impacts. These include: the establishment of an energy regulatory agency, including partial staffing (energy sector); the establishment of a *Regulatory Reform Council* and a small technical secretariat to facilitate and guide the process of regulatory impact assessment for all new legislation and decrees (business environment); and the creation of clear management and accountability structures to drive the long and difficult reforms in public administration. Since the Credit's objectives and implementation have increased, to a limited extent, Serbia's ability to effectively use its human, financial and natural resources, an overall institutional development impact rating of modest is reasonable.

5. Major Factors Affecting Implementation and Outcome

5.1 Factors outside the control of government or implementing agency:

Major factors outside the control of government, such as changes in world market prices, did not significantly affect or disrupt the implementation of the program, but did impact on the macroeconomic outcome of the program. Most importantly, a significant surge in oil prices towards the closing period of the operation worked to keep inflation and the current account deficit at levels above those projected at the time of project approval.

5.2 Factors generally subject to government control:

Following the Parliamentary elections of December 2003, Serbia formed a fragile but functioning minority coalition in early March 2004. Serbian legislative elections held in June 2004 further bolstered stability. There was some concern that the challenges of ruling as a minority coalition could undermine the Government's cohesiveness and effectiveness in implementation of the reforms supported by SAC 2.

Contrary to the expectation, however, government commitment to the overall program and effectiveness in implementation remained very strong throughout. Business environment, energy sector, social welfare and public administration reforms were all well implemented. As discussed below, good progress has also been made towards attaining the medium term goals of the operation in each area.

5.3 Factors generally subject to implementing agency control:
There were no implementation delays. However, as discussed above, the monitoring and evaluation of beneficiary participation in the main social welfare assistance scheme, the Material Support to Families program (MOP), and the electricity subsidy scheme for poor households could have been improved by the respective implementing agencies, the Ministry of Labor, Employment and Social Welfare, the electric company of Serbia (EPS), and the Ministry of Mines and Energy.

5.4 Costs and financing:
There were no cost changes or changes in financing, and disbursements were handled promptly without delay.

6. Sustainability

6.1 Rationale for sustainability rating:
Sustainability is rated as likely for the following reasons.

First, many of the reforms undertaken with the support of SAC 2 involved changes in the legal framework and enactment of new laws (new enterprise law, new law on enforcement procedures, new energy law), and development of strategies (new Energy Strategy, new Public Administration Reform Strategy). These laws and strategies are unlikely to be reversed. Indeed, they have continued to take root as implementation has progressed over time.

Second, SAC 2 supported substantial up-front policy actions as a bridge between the first series of adjustment lending initiated under the Transitional Support Strategy and the programmatic development lending envisaged under the new CAS. Three of the components of SAC 2 are directly built upon in the follow-on Bank operations currently under preparation for the Republic of Serbia. The first programmatic private and financial sector loan, approved by the Bank Board in early December 2005, builds on the business environment and energy sector reforms pursued under SAC 2 by accelerating the restructuring and privatization of socially-owned enterprises; improving the financial sector through further privatization of state banks and strengthening the capacity of the bank and insurance regulatory authority; and engaging an international financial advisor for the electric company (EPS) to improve its commercialization. Similarly, the first programmatic public sector reform loan, which is currently under preparation and expected to be presented to the Bank Board in May 2005, builds directly on the public administration reforms initiated under SAC 2, and envisages to complete the legislative agenda (e.g. Law on Salaries) and move swiftly to implementation, including the staff rationalization and establishment of a merit-based civil service agency. Although there is at the moment no clear follow on operation that builds on the social protection reforms undertaken with the support of SAC 2, the monitoring of social impacts of reforms is planned to continue in the context of Bank's regional programmatic poverty assessment work for Serbia.

Third, Serbia and Montenegro aspires to join the European Union, and EU accession remains an important anchor for reforms. Many of the legislative and structural reforms undertaken with the support of SAC 2 –in particular the business environment reforms, energy sector, and public administration reforms--were designed to move Serbia increasingly towards European structures and standards, and as such appear sustainable. Serbia and Montenegro has officially started the negotiations with the European Union on the Stabilization and Association Agreement (SAA) in October 2005, which is expected to last about one year.

These negotiations provide an important extra impetus for maintaining the momentum on economic reforms, including the implementation of several important laws and strategies supported under SAC 2.

6.2 Transition arrangement to regular operations:
Not applicable.

7. Bank and Borrower Performance

Bank
7.1 Lending:
This is rated satisfactory. Credit *identification* and *design* was compatible with the CAS, and SAC 2 was considered by the Bank Board together with the new CAS for Serbia and Montenegro, covering 2005-07. SAC 2 built directly on the outcomes of previous adjustment operations and other sectoral operations. It was consistent with the government's development strategy, in particular the PRSP. The Bank worked closely with other donors—the IMF, European Agency for Reconstruction, DFID, SIDA, UNDP—on the credit's design in all the five main areas of reform. Credit appraisal correctly assessed the government's strong commitment to the reforms, and appropriately focused on helping the government introduce legislative changes and develop strategies in various areas.

Concept meetings effectively tightened loans focus and policy conditionalities prior to Board submission. For example, during the concept review there were proposals to include the restructuring of Serbia's state railways (ZTP) as part of the Credit since the direct budget subsidy to the railways accounted for around 1 percent of GDP. However, the team argued, and the peer reviewers and management concurred, that this would overload the program and divert the main focus from promoting sustainable economic growth. Similarly, at the Regional Operating Committee review, the peer reviewers urged the team to keep the policy conditionalities focused but go beyond process, and to develop measurable indicators. The time elapsed between appraisal and board presentation was about three months, so the Credit met the five-month standard for time elapsed between appraisal and board presentation.

There was good team continuity in this operation. The SAC 2 team leadership was continuous throughout the credit preparation and implementation. The team leader (country economist) left the country unit around the time of closing of the Credit, and a new country economist has come on board to lead, among other things, the follow-on programmatic public sector development policy lending (PSDPL1), currently under preparation.

7.2 Supervision:
Supervision is rated satisfactory. As a one-tranche operation which disbursed in December 2004, and closed in June 2005, SAC 2 did not involve a level of supervision which would normally be associated with a multi-tranche operation, and where supervision could materially affect progress and reform outcomes. SAC 2 supported mostly up-front policy actions, but sectoral missions conducted regular reviews of progress in achieving medium term outcome benchmarks described in the LDP as well as in the Program Document. The final ICR mission took a comprehensive stock of progress in achieving such benchmarks, as reported above.

7.3 Overall Bank performance:
In view of the satisfactory rating for the quality at entry, lending, and supervision, the **overall Bank performance is rated as satisfactory**.

Borrower
7.4 Preparation:

This is rated satisfactory. During program preparation and appraisal (December 2003- October 2004), the Borrower was fully committed to the reform program and showed a high level of ownership, leadership, and commitment to the mutually proposed package of economic reforms. During the appraisal mission (September 23-October 5, 2004), the Government and the Bank team reached a full understanding on all elements of the program, including the policy action matrix, with the Minister of Finance. The fact that the reform measures in the SAC 2 program--except for the public administration reform--constituted a continuation and deepening of the reform efforts that had been started under previous World Bank adjustment credits somewhat eased the preparation process and ensured continued Government commitment. This commitment has been maintained. With the exception of social safety nets, all components of SAC 2—macroeconomic performance, business environment and private sector development, energy sector, and public administration—have also been continued under the subsequent Serbia programmatic private and public sector development policy loans.

7.5 Government implementation performance:

This is rated satisfactory. Following the Parliamentary elections of December 28, 2003, Serbia formed a fragile but functioning minority coalition in early March 2004. There was some concern that the challenges of ruling as a minority coalition could undermine the Government's cohesiveness and effectiveness in reform implementation. Contrary to these expectation, however, government commitment to the overall program and effectiveness in implementation remained very strong. As discussed above, good progress has also been made towards attaining the medium term goals of the operation. Effective inter-ministerial coordination--including effective horizontal communication (between institutions) as well as vertical communication (within a sector)--was one of the critical factors for successful project implementation.

7.6 Implementing Agency:

This is rated as satisfactory. The performance of the implementing agencies was generally good. The reform implementation was rightly decentralized to the competent agencies. The Ministry of Economy was responsible for implementing the business environment reforms, while the Ministry of Mines and Energy was tasked with implementing the energy sector reforms in cooperation with the EPS. The Ministry of Labor, Employment and Social Welfare was responsible for the implementation of the new Social Welfare Law and the MOP program, and the Government established an inter-agency group (involving the Ministry of Mines and Energy, EPS, and the Ministry of Labor, Employment and Social Welfare) to oversee the implementation of the electricity subsidy scheme. The development and implementation of the PAR strategy was assigned to the Ministry of Public Administration and Local Self Government (MPALSG), and the drafting work on PAR legislation to the Office for Legislation at the Government.

However, follow-through has in some cases been weaker than expected. As discussed above, the implementation of both the new Law on Social Welfare and the electricity subsidy scheme for the poor could have been stronger. With a more vigorous public information campaign about the MOP program at the local social welfare centers and other stronger outreach efforts, the medium term impact of the MOP program could have been improved. Similarly, by relaxing the rather stringent criterion to access the subsidy scheme--i.e. that poor households be current on their electricity bill payments--the coverage of the subsidy scheme could have been expanded to benefit more poor households, with greater medium term impact.

7.7 Overall Borrower performance:

In view of the satisfactory ratings for preparation, and govenment implementation performance, the **overall Borrower performance is rated as satisfactory**.

8. Lessons Learned

Improve communication with the implementing agencies. A key lesson learnt from this operation is that clear project rationale, description of the objectives of reform to the relevant management tiers of the ministries and state institutions in charge of implementation, and communication between the World Bank teams and the designated focal points in the partner state institutions are all critical for success. While the overall implementation performance under the Credit has been good, the feedback during the implementation completion mission highlighted that there is a need for sustained effort to improve communication with the Borrower, in particular with the implementing agencies. The staff of the Ministry of Mines and Energy, in their comments about the Credit, said: “The conditions were carefully chosen, and the timeline was realistic. However, there is a need to improve communication between the Bank and the Government, especially in engaging the Ministry of Mines and Energy in the policy dialogue from the start”.

Continue to rely on lending instruments that provide maximum flexibility. Within SaM’s complex political economy, past development policy credits, including SAC 2, have proved effective in supporting the Government to undertake difficult policy reforms, in part because they allowed for significant flexibility in terms of the time as well as policy areas to be supported. With the support of these credits, Serbia has developed medium to long-term reform strategies that guide sector reforms, revamped its legislative frameworks in many areas, and embarked on the long road of institutional development. The road ahead requires a strong effort to implement the new strategies and laws, as well as long-term institutional change and development. This suggests that the support to the government should be appropriately paced and focused, while at the same time ensuring continuity over the medium term.

Continue to rely on a strong analytical basis to design effective operation. The four key policy areas supported by SAC 2 were underpinned by extensive Bank economic sector work and intensive dialogue with the Borrower. The Bank’s analytical background work included: Recent Progress on Structural Reforms (2003), which took stock of the status of structural reforms and where Serbia was lagging; Serbia Investment Climate Assessment (2004), which guided the business environment reform component; Serbian Energy Sector: Status, Key Issues and an Agenda for Action (2003), which supported the reform design in the energy sector; Serbia and Montenegro Poverty Assessment (2003), which, among other areas, highlighted the priorities within the social protection and impact mitigation; and Serbia and Montenegro Public Administration Development: Creating the Conditions for Effective Economic and Social Reform Policy Note (2004), which constituted the basis for the design of the public administration reforms. These studies helped crystallize clearly the areas to be supported under SAC 2 , ensuring at the same time a strong government buy-in at the preparation stage and a strong commitment during implementation.

9. Partner Comments

(a) Borrower/implementing agency:

The Government's own evaluation of the credit is included in Annex 8.

To: <aadugna@worldbank.org>
From: "vladimir" <vvukojevic@mfin.sr.gov.yu>
Date: 12/27/2005 01:50AM
cc: <tmitrovickocovic@worldbank.org>
Subject: ICR comments

Dear Mr. Adugna ,

We would like to thank the World Bank for successful cooperation and support to the Government of the Republic of Serbia during Structural Adjustment Credit 2 (SAC 2) project, IDA -40170.

We also would like to thank for the preparation of Implementation Completion Report on a credit in the amount of US$45 million to Serbia and Montenegro (Republic of Serbia), for a Structural Adjustment Credit 2.

We have reviewed the report that you have submitted to us. We find the report well prepared.

We have reviewed the findings and comments presented in the Implementation Completion Report and we fully agree with them.

Best regards,

Vladimir Vukojevic
Assistant Minister
Sector for International Financial
Relations
Ministry of Finance of Serbia
tel +381 11 3614 713

(b) Cofinanciers:

(c) Other partners (NGOs/private sector):

10. Additional Information

Annex 1. Key Performance Indicators/Log Frame Matrix

Reform Areas/Objectives	Output/ Planned Measures	Actual Output	Medium term Outcome Indicators	Actual Outcome as of December 2005
1. MACROECONOMIC STABILITY				
	Continue to maintain a sustainable macroeconomic framework	**Progress was mixed.** IMF program on track. Real GDP growth was 8.6 percent in 2004, much higher than the 6 percent growth projected; inflation was slightly above the originally projected target of 12.6 percent (13.4 percent); general government deficit (0.3 percent) was significantly lower than the projected 2 percent of GDP; current account deficit was higher than programmed; and indebtedness to GDP in 2004 was slightly higher than projected.	Continue to maintain a sustainable macroeconomic framework	**Mixed progress.** IMF program on track; real GDP growth positive and close to the medium-term target of 5%; fiscal policy tightened and sustainable. But inflation still in double digit and needs to be reduced; and current account deficit too high and still not consistent with external sustainability.
2. IMPROVE THE BUSINESS CLIMATE				
Enable easier entry and improve corporate governance	Undertake a wide public consultation process about the New Enterprise Law including relevant stakeholders Enact the new Enterprise Law	**Completed.** A new Company Law was prepared and enacted. A wide public consultation was carried out the Enterprise Law before its enactment.	Increase in the number of limited liability companies registered per annum	**Good progress**. There has been a significant increase in the number of limited liability companies registered per annum—from about 6000 new companies in 2004 to about 10, 000 new companies in 2005.
Improve contract enforcement	Undertake a wide public consultation process about the new Law on Execution Procedures including relevant stakeholders Enact the new Law on Execution Procedures	**Completed.** After consultation with the public and other stakeholders, a new Law on Execution Procedures was adopted by the Government in October 2004 and subsequently enacted by the Parliament of Serbia in November 2004.	More efficient enforcement of judicial decisions and commercial contracts, as measured by the Enforcing Contract Indicators	**Good progress.** According to the new Doing Business Study of the World Bank (2006), Serbia was rated among the top reformers during 2004-05. Serbia significantly reduced enterprise entry time from 51 days in 2004 to 15 days in 2005; the number of procedures was reduced from 11 in 2004 to 10 in 2005; and the average duration of court cases was reduced from 1028 days in 2004 to about 600 days in 2005.
Improve the country's regulatory framework	Prepare amendments to the Rules of Operation of the Government necessary for the introduction of Regulatory Impact Analysis and identify an entity (Regulatory Reform Council) to carry out this function Adopt amendments to the Rules of Operation of the Government requiring responsible ministry to	**Completed.** Amendments to the Rules of Operation of the Government requiring the responsible ministry to prepare a justification statement for a new law, a decree and an order in line with the OECD Regulatory Impact Assessment (RIA) were made in October 2004. A *Regulatory Reform Council* and a small technical secretariat have been established. Since October 2004, the Council has helped carry out for more than 60 draft laws.	Steady increase in the use of RIA	**Good progress.** There has also been a steady increase in the use of RIA: over 60 laws and decrees have become subjected to RIA since October 2004.

	prepare justification statement for a new law, a decree and an order in line with the OECD Regulatory Impact Analysis			
3. IMPROVE ENERGY SECTOR PERFORMANCE				
Adopt an enabling framework for energy sector reform	Enact Energy Law that includes the following provisions: establishment of an independent regulator; enabling the restructuring of EPS and the ownership/ operation separation of transmission; strengthening the legal framework for enforcement of payments discipline Adopt Energy Strategy Appoint key personnel for the new Energy Regulator	**Completed.** A new Energy Law, with all the required provisions as set out in the condition, entered into force in July 2004. The Law is consistent with best practice for the region serves as the basis for regulatory development, tariff reform, Elektroprivreda Srbije (EPS) restructuring, and energy market liberalization. Staffing of the regulatory agency, although not yet complete, is underway with about 10 out of 35 total positions filled, and the agency is expected to be operational by January 2006. The Government also adopted an Energy Strategy that explained the vision behind the Energy Law.	Full staffing of the Regulator and adoption of a business plan	**Good progress.** About 10 of the 35 total positions of the regulatory agency have been filled. Full staffing is expected to be completed, and the agency fully operational, in the first half of 2006. Among its immediate priorities would be to develop a business plan and a tariff schedule toward cost recovery.
Adjust tariff level and its structure to maintain cost recovery and improve energy efficiency incentives	Raise power tariffs to yield a revenue increase of the order of 10% for EPS from July 1st; the tariff increase should comprise in part a reduction of the first block in the block tariff structure to 350 kWh	**Completed.** Increased tariff level by 10% to maintain an approximately constant real tariff in July 2004 relative to 2003; reformed the existing tariff structure by reducing the first block tariff to 350 kWh.	Ongoing financial viability of EPS defined as positive operating cash flow	**Limited progress.** Tariff adjustment for 2004 (10 percent) and 2005 (9.5 percent) have helped EPS' financial viability, but full cost recovery schedules are yet to be developed by the regulatory agency.
Improve payments discipline	Keep residential collections—defined as cash collected divided by invoices—for the first six months of 2004 at or above the level for the corresponding period in 2003. Thereafter the six month rolling average should be at least as high as the corresponding period in the previous year Form teams in distribution companies and EPS headquarters, and identify where commercial losses are a problem Offer at least four of EPS' large electricity debtors for sale and sell at least two of them or viable parts thereof—all in a manner and on terms and conditions satisfactory to the Bank	**Completed**. Collection rate for residential consumers was 91-92 percent in 2004, and has slightly improved to 93 percent as of the third quarter of 2005. Improving collections from industrial consumers, however, remains a big challenge. A team was established that identified commercial non-technical losses, but progress in loss reduction has been slow. More than four of EPS' large electricity debtors for sale. In 2005, the Ministry of Mines and Energy submitted an additional list of 15 largest debtors of electricity to the privatization agency for action, but progress with privatization has been slow.	Maintain residential collections ratio in the range of 92-95 percent	**Good progress.** Collection rate for residential consumers has been in line with benchmarks, rising from 91-92 percent in 2004, to 93 percent in 2005. Improving collections from industrial consumers, however, remains a big challenge.
Achieve power industry commercialization	Transfer out of EPS 8 non-core companies and establish within EPS from non core assets 12 new subsidiary companies Adopt a Government Decision to separate ownership of power generation/ distribution and	**Completed.** More than 12 new subsidiary companies were established and more than 8 non-core companies were transferred to these subsidiary companies. A Government decision was adopted to separate ownership of power generation/ distribution and transmission businesses, and transmission company has been separately set up		

	transmission businesses Maintain net hiring freeze at EPS	and operational since July 2005. Net hiring freeze maintained at the Serbia Electric Company, EPS.		
4. STRENGTHENING SOCIAL PROTECTION				
Improve effectiveness of the safety net	Ensure adequate funds within the 2004 State Budget and the draft 2005 State Budget submitted to the Parliament for full implementation of the Social Welfare Law upon its effectiveness	**Completed.** Helped ensure increased budget allocation for the implementation of the new Social Welfare Law: by increasing budget allocation for the MOP by about 20 percent (from about 0.1 percent of GDP prior to the Law), which allowed for a modest expansion in coverage.	13,000 new beneficiaries covered by MOP	**Progress less than expected.** Only 8,000 new beneficiaries have been covered by MOP.
Mitigate the adverse impact of changes in the level and structure of electricity tariffs on the poor	Introduce a new mitigation scheme to support the poor and vulnerable population, whereby recipients of child benefit, minimum pension and MOP are entitled to a discount of no less than 30% of the monthly bill on consumption up to 300 kWh	**Completed.** The Government introduced a new mitigation scheme to support the poor and vulnerable population, whereby recipients of child benefit, minimum pension and Material Support to Families program (MOP) were entitled to a discount of 30% on their monthly electricity bill on consumption up to 300 kWh. The program was introduced in the summer of 2004 and an additional 17,000 families have benefited from the scheme.	A minimum of 50,000 new beneficiaries to be protected by the energy sector social safety net	**Progress less than expected.** Only an additional 17,000 families have benefited from the electricity subsidy scheme to date.
Improve coordination between social protection programs and energy related subsidies as well as monitoring of social impact to achieve better targeting and efficiency	Establish a working group consisting of representatives from MoME, MoSA, and EPS to coordinate and oversee the implementation of energy mitigation schemes Prepare a report on poverty in 2004 based on household survey to monitor the social impact of reform and revise the program publication by RSO to include the production of poverty data on a regular basis	**Completed.** A working group was established consisting of representatives from MoME, MoSA, and EPS to coordinate and oversee the implementation of energy mitigation schemes. This working group is still functional. No poverty report was prepared in 2004, although the Republican Statistical Office has attempted to produce poverty numbers (which are surrounded by considerable debate).		
5. IMPROVING PUBLIC ADMINISTRATION				
Create a policy framework for effective reform of the Public Administration	Complete the preparation of a Strategy and Action Plan on Public Administration Reform Adopt the Public Administration Reform Strategy and related Action Plan	**Completed.** The Public Administration Reform Strategy (PAR) and the related Action Plan were adopted in November 2004. The Strategy is anchored in European principles and standards--professionalization, de-politicization, rationalization, decentralization and modernization—and lays the foundation for creation of a merit-based and de-politicized civil service and for the rationalization of administrative structures in the central state administration.	Adoption of basic laws (Law on Government, Law on Civil Service, Law on Public Agencies, Law on State Administration and Law on Salaries) on public administration	**Good progress.** All the basic laws have been adopted, with the exception of the Law on Salaries which is in draft stage and expected to be adopted in the first half of 2006.
Review the Salary System for the central Civil Service	Finalize an in-depth review of the Civil Service pay system and identify two alternative options for reform that will be fully	**Completed.** The Government reviewed the Serbian civil service wage system to develop reform proposals, which was subsequently endorsed by the Public Administration	The Law on Salaries sets compression ratio in civil service pay at minimum 1:6	**Good progress.** The Government has introduced interim salary system reforms through the 2005 budget, which have

	explored and costed	Reform Council, outlining the direction of pay reforms. The Government has introduced interim salary system reforms through the 2005 budget, which have decompressed the wage and salaries system from 1:4.9 to 1:8.		decompressed the wage system from 1:4.9 to 1:8.
Establish an effective Public Administration Management Structures	Create a management structure for public administration reform and ensure that it has adequate staffing and is fully operational	**Completed.** The Government introduced a clear horizontal public PAR structure. The development and implementation of the PAR strategy was assigned to the MPALSG; the drafting work on PAR legislation was taken over by the Office for Legislation at the Government; and appropriate resources were allocated to manage the PAR process.	Initial steps in public administration reform are effectively implemented according to set deadlines	**Good progress.** The timeline for finalization of various PAR activities set out by the Action plan has not always been fully respected, but the government has carried out all activities albeit with some delays.

Annex 2. Project Costs and Financing

Not Applicable

Annex 3. Economic Costs and Benefits

Not Applicable

Annex 4. Bank Inputs

(a) Missions:

Stage of Project Cycle / Month/Year	No. of Persons and Specialty (e.g. 2 Economists, 1 FMS, etc.) Count	Specialty	Performance Rating: Implementation Progress	Development Objective
Identification/Preparation				
10/17/2003	4	1 Lead Economist; 1 Team Leader (Sr Econ); 1 Sr. Energy Economist; 1 Research Analyst		
12/06/2003	8	1 Team Leader (Sr. Econ); 1 Sr. Public Sector Specialist; 1 Sr. Energy Economist; 1 Lead Specialist; 1 Sr. Economist; 1 Operations Officer; 1 Research Analyst; 1 Consultant		
05/17/2004	7	1 Team Leader (Sr. Econ); 1 Sr. Energy Economist; 1 Lead Specialist; 1 Operations Officer; 1 Research Analyst; 2 Consultants		
Appraisal/Negotiation				
09/23/2004	7	1 Team Leader (Sr. Econ); 1 Sr. Public Sector Specialist; 1 Sr. Energy Economist; 1 Lead Specialist; 1 Research; Analyst; 2 Consultants		
Supervision				
01/01/2005 -06/30/2005	6	1 Team Leader (Sr. Econ); 1 Sr. Public Sector Specialist; 1 Sr. Energy Economist; 1 Lead Specialist; 1 Research Analyst	S	S
ICR				
11/10/2005	2	1 Team Leader (Sr. Econ); 1 Research Analyst	S	S

(b) Staff:

Stage of Project Cycle	Actual/Latest Estimate: No. Staff weeks	US$ ('000)
Identification/Preparation	44.25	178,746.29
Appraisal/Negotiation	20.34	89,631.46
Supervision	2.49	13,240.58
ICR	4	15,000

Total	71.08	296,618.33

Annex 5. Ratings for Achievement of Objectives/Outputs of Components

(H=High, SU=Substantial, M=Modest, N=Negligible, NA=Not Applicable)

	Rating
☒ *Macro policies*	○ *H* ● *SU* ○ *M* ○ *N* ○ *NA*
☒ *Sector Policies*	○ *H* ● *SU* ○ *M* ○ *N* ○ *NA*
☐ *Physical*	○ *H* ○ *SU* ○ *M* ○ *N* ● *NA*
☐ *Financial*	○ *H* ○ *SU* ○ *M* ○ *N* ● *NA*
☒ *Institutional Development*	○ *H* ○ *SU* ● *M* ○ *N* ○ *NA*
☐ *Environmental*	○ *H* ○ *SU* ○ *M* ○ *N* ● *NA*
Social	
☒ *Poverty Reduction*	○ *H* ○ *SU* ● *M* ○ *N* ○ *NA*
☐ *Gender*	○ *H* ○ *SU* ○ *M* ○ *N* ● *NA*
☐ *Other (Please specify)*	○ *H* ○ *SU* ○ *M* ○ *N* ● *NA*
☒ *Private sector development*	○ *H* ● *SU* ○ *M* ○ *N* ○ *NA*
☒ *Public sector management*	○ *H* ● *SU* ○ *M* ○ *N* ○ *NA*
☐ *Other (Please specify)*	○ *H* ○ *SU* ○ *M* ○ *N* ● *NA*

Annex 6. Ratings of Bank and Borrower Performance

(HS=Highly Satisfactory, S=Satisfactory, U=Unsatisfactory, HU=Highly Unsatisfactory)

6.1 Bank performance	*Rating*
☒ *Lending*	○ *HS* ● *S* ○ *U* ○ *HU*
☒ *Supervision*	○ *HS* ● *S* ○ *U* ○ *HU*
☒ *Overall*	○ *HS* ● *S* ○ *U* ○ *HU*

6.2 Borrower performance	*Rating*
☒ *Preparation*	○ *HS* ● *S* ○ *U* ○ *HU*
☒ *Government implementation performance*	○ *HS* ● *S* ○ *U* ○ *HU*
☒ *Implementation agency performance*	○ *HS* ● *S* ○ *U* ○ *HU*
☒ *Overall*	○ *HS* ● *S* ○ *U* ○ *HU*

Annex 7. List of Supporting Documents

World Bank
Country Assistance Strategy for Serbia and Montenegro, Report No. 30426-YU, November 2004

Program Document on a Proposed Second Structural Adjustment Credit (Republic of Serbia), Report No. 29857-YU, November 2004

"Serbia Structural Adjustment Credit 2 Back to Office Report of Identification Mission", November 10, 2003

"Serbia and Montenegro: Proposed Second Structural Adjustment Credit (SAC 2), Republic of Serbia (P078457) Initiating Concept Memorandum—Review Meeting" November 18, 2003

"Serbia and Montenegro: Proposed Second Structural Adjustment Credit (SAC 2), Republic of Serbia (P078457) – Minutes/summary of the Initiating Concept Memorandum Review Meeting", December 3, 2003

"Serbia Structural Adjustment Credit 2 (P078457) Back-to-Office Report of Technical Preparation Mission", December 30, 2003

"Serbia and Montenegro: (Republic of Serbia) SAC 2 Project, Minutes of Regional Operations Committee (ROC) Review Meeting", September 20, 2004

"Serbia and Montenegro Second Structural Adjustment Credit (Republic of Serbia), Appraisal Mission Aide Memoire", October 2004

"Serbia and Montenegro (Republic of Serbia): Structural Adjustment Credit 2 (P078457) Appraisal Mission Back-to-Office Report", October 7, 2004

"Program Document for Serbia and Montenegro (Republic of Serbia) for the Proposed First Programmatic and Financial Sector Development Policy Credit", October 2005

"Program Document for Serbia and Montenegro (Republic of Serbia) for the Proposed First Programmatic Public Sector Development Policy Loan", Draft, November 2005

"Poverty Reduction Strategy Paper for Serbia", 2003.

Government
Republic of Serbia, Ministry of Finance, "Second Structural Adjustment Credit Completion Report" December 8, 2005

Additional Annex 8. Government Evaluation of the Credit

Republic of Serbia
MINISTRY OF FINANCE
Cabinet of the Minister
Kneza Milosa 20, Belgrade
Tel: +381 11 36 14 214
Belgrade, December 8, 2005

Subject: Second Structural Adjustment Credit Completion Report

The initial transition measures in Serbia in the period 2001-2004 were aimed to provide basic conditions for development of market economy, more efficient state sector, therefore enabling growth in employment, living standards and economic output. The WB has addressed all key areas relevant for the overall macroeconomic goals, through well designed and comprehensive assistance strategy for Serbia.

The Second Structural Adjustment Credit focused on key prerequisites to enable sustainable growth and to provide fundamental institutional reforms leading towards EU integration process. In line with this, we have defined four basic actions: improving the business climate, improving the energy sector performance, enhancing the social protection and public administration reform. The strategy was supported with the detailed activity log-frame including key objectives, stakeholders and timings, providing for easy management and monitoring of the reform process.

This project proved as a very successful one, properly implemented and reaching its objectives. The proper outcome indicator is a steady and continuous economic growth in 2004 and 2005, with the increased efficiency mainly due to the private sector growth. The results enabled further continuation of the reforms started, supported with the First Programmatic Policy Development Credit in 2005, namely paving the way for the energy sector restructuring, support to the social programs for the redundant workers and privatization process. The results in area of public administration reform have provided for momentum for further actions, in line with the Strategy for the Public Administration Reform adopted.

(i) Assessment of the project objective, design, implementation and operational experience

The project objectives design was comprehensive, understandable and easy to monitor and verify. As usual, the specific policy/action matrix was developed to facilitate the project implementation and enable easy monitoring of the project. The matrix was clear and understandable. The objectives design included legislative improvements needed, as well as introduction of new units, procedures and practices (example of the Regulatory Reform Council and Regulatory Impact Analysis). The certain concrete actions were included in order to reach several objectives (to improve payment discipline towards power sector, enhanced tariff structure and more).

Once more the effective inter-ministerial proved as one of the critical factors for the project success. Proper horizontal communication (between institutions) as well as vertical communication (between institution management, experts, PIU and other relevant civil servants) was a key for efficient activity implementation. The one example is rather quick response in urgent activity of initiating Public Administration Reform. After many expert assessments on limitations of the current state administration system, in close cooperation of the civil servants and high management of the Ministry of State Administration and Ministry of Finance, the key priorities were easily identified leading to the issuing of the Joint policy statement signed by both relevant ministers, paving the way for the adoption of the State Administration Reform Strategy.

(ii) Evaluation of the borrower's own performance during the evolution and implementation of the project, with special emphasis on lessons learned that may be relevant in the future

As a consequence of the well prepared project, there were no major obstacles for the implementation. The project goals fitted with overall Government strategy and administration is to good extent already acquainted to WB practices. The lack of administrative and expert capacity in state administration is still present, but with the trend of improvement. The lesson learnt is that it is essential to provide for the institution's commitment in the implementation, including securing adequate human resources to focus both on expertise and management out of the regular institutions administrative activities.

(iii) Evaluation of the performance by the Bank during the evolution and implementation of the project, including the effectiveness of their relationships, with special emphasis on lessons learned

The World Bank has maintained high standards of expertise needed as an external assistance to state administration in process of significant reform, and in cases of capacity shortfalls in state institutions. Besides the expert and strategic support of the visiting World Bank teams, local WB Belgrade office continued to provide adequate support, covering local expertise, communication, strong assistance to project management and coordination.

The lesson learnt is the importance of clear project rationale description/demonstration to relevant high management tiers of the ministries/state institutions, and frequent communication of the WB teams to the designated focal points in the partner state institutions.