

**DOCUMENT OF THE EUROPEAN BANK  
FOR RECONSTRUCTION AND DEVELOPMENT**

Approved by the Board of Directors on 7 April 2021<sup>1</sup>

**KOSOVO**

**PRIZREN PUBLIC BUILDINGS ENERGY  
EFFICIENCY PROGRAMME**

*[Redacted in line with the EBRD's Access to Information Policy]*

*[Information considered confidential has been removed from this document in accordance with the EBRD's Access to Information Policy (AIP). Such removed information is considered confidential because it falls under one of the provisions of Section III, paragraph 2 of the AIP]*

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<sup>1</sup> As per section 1.4.8 of EBRD's Directive on Access to Information (2019), the Bank shall disclose Board reports for State Sector Projects within 30 calendar days of approval of the relevant Project by the Board of Directors. Confidential information has been removed from the Board report.

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## ABBREVIATIONS

DSCR	Debt Service Cover Ratio
EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortisation
EBRD	European Bank for Reconstruction and Development
EPC	Engineering, Procurement and Construction Contract
ESAP	Environmental and Social Action Plan
ESCO	Energy Service Company
EE	Energy Efficiency
EH&S	Environmental, Health and Safety
EIRR	Economic Internal Rate of Return
E&S	Environmental and Social
EUR	Euro
FDI	Foreign Direct Investment
GET	Green Economy Transition
GHC	Greenhouse Gas Emissions
GoK	Government of Kosovo
IFI	International Financial Institution
MEI	Municipal and Environmental Infrastructure
MoEE	Ministry of Economy and Environment
MoF	Ministry of Finance
NPV	Net Present Value
NTS	Non-Technical Summary
OSR	Own Source Revenue
PIU	Project Implementation Unit
PP&R	Procurement Policies and Rules
PR	Performance Requirements
PSA	Project Support Agreement
REEP	Regional Efficiency Programme for the Western Balkans
SEP	Stakeholder Engagement Plan
SPP	Stakeholder Participation Programme
SSF	Shareholder Special Fund
TC	Technical Cooperation
VAT	Value-Added Tax

## PRESIDENT'S RECOMMENDATION

This recommendation and the attached Report concerning an operation in favour of Municipality of Prizren (the “City”), a Municipality in Kosovo, are submitted for consideration by the Board of Directors.

The facility will consist of a sub-sovereign loan to the City in the amount of up to EUR 5 million to co-finance energy efficiency, structural and comfort measures in municipally-owned buildings, including kindergartens, schools, and primary healthcare centres. The loan is structured as one tranche, for the Bank’s own account. The Project will be co-financed with an investment grant in the amount of EUR 1 million from the EU Regional Efficiency Programme for the Western Balkans (“REEP”).

The Project will improve energy performance and environmental sustainability of the renovated buildings, improve damaged structures as well as their comfort level and quality, which is very important for buildings of this nature. Moreover, the Project will introduce new standards in the management of the municipally-owned buildings, including Energy Audits and preparation of energy performance certificates. The expected transition impact of the project is *Green* as it introduces high quality, innovative EE technologies in buildings that will have a strong demonstration effect and support the “renovation wave” in buildings across the country and the region; and *Resilient* as the financing structure, being the first direct borrowing by the City and the first or second municipal project/borrowing in Kosovo, expands the range of available financing instruments in the country.

The Project is in line with the Green Economy Transition (“GET”) Approach 2021-2025 , and qualifies as 100 per cent GET as implementing new EE technologies in buildings will reduce demand for carbon-intensive electricity and fossil fuels, and thereby reduce GHG emissions in the City and countrywide.

Post-signing TC support for this operation is expected to be provided for Project Implementation Support. [REDACTED]

I am satisfied that the operation is consistent with the GET Approach 2021-2025 , the Bank’s Strategy for Kosovo and with the Agreement Establishing the Bank.

I recommend that the Board approve, on a no-objection basis, the proposed loan substantially on the terms of the attached Report.

**Odile Renaud-Basso**

## BOARD DECISION SHEET

KOSOVO - PRIZREN PUBLIC BUILDINGS ENERGY EFFICIENCY PROJECT - DTM 51898	
<b>Transaction / Board Decision</b>	<p>Board approval<sup>2</sup> is sought for a senior sub-sovereign loan of up to EUR 5 million in favour of the Municipality of Prizren, to co-finance energy efficiency (“EE”), structural and comfort measures in municipally-owned buildings, including kindergartens, schools, and primary healthcare centres in the city (the “<b>Project</b>”).</p> <p>Approval is also sought for an investment grant co-financing in the amount of EUR 1 million from the EU Regional Efficiency Programme for the Western Balkans (“REEP”), of which EUR 0.73 million have been allocated, while the remaining EUR 0.27 million will be requested from the donor after the replenishment of REEP, [REDACTED], and in the event this is not available, funding from EBRD Shareholder Special Fund (“SSF”) will be sought.</p>
<b>Client</b>	<p>The client and the borrower is the Municipality of Prizren (the “<b>Borrower</b>”, the “<b>City</b>” or “<b>Prizren</b>”). Prizren is the second largest municipality in Kosovo with a population of approximately 180 thousand. [REDACTED]</p>
<b>Main Elements of the Proposal</b>	<p><b><u>Transition impact</u></b></p> <ul style="list-style-type: none"> <li>• <b>Primary Quality – Green:</b> The Project will introduce high quality, innovative EE technologies in buildings resulting in [REDACTED] avoided CO2 emissions annually. The project will have a strong demonstration effect and support a “renovation wave” in buildings across the country and the region.</li> <li>• <b>Secondary Quality – Resilient:</b> The financing structure, as the first direct borrowing by the City and the first or second municipal project/borrowing in Kosovo, expands the range of available financing instruments in the country.</li> </ul> <p><b><u>Additionality</u></b></p> <p><b>Financing Structure</b>– Commercial funding is not yet available for municipalities in Kosovo. The proposed loan will be one of the first to be lent directly to a municipality in Kosovo.</p> <p><b>Risk Mitigation</b>– EBRD technical assistance will help mitigate implementation risk. EE measures will result in energy savings and lower GHG emissions, thereby reducing carbon transition risks.</p> <p><b>Standard setting:</b> The Project includes Energy Audits and preparation of energy performance certificates (“EPCs”) for the renovated buildings. Procurement will be carried out in accordance with EBRD PP&amp;Rs.</p> <p><b>Capacity building</b> - Project Implementation Support TC is also aimed at strengthening the capacities of the Client.</p> <p><b><u>Sound banking</u></b></p> <p>Prizren has an acceptable credit profile and operating performance, with no debts outstanding. The City’s budget projections show a comfortable level of debt servicing capacity. While the COVID-19 crisis has affected its own source revenue (“OSR”), the City has managed its budget through lower capex spending.</p>
<b>Key Risks</b>	<p><b>Political stability:</b> Municipal elections are scheduled in October 2021. The Project has been approved by Prizren’s Municipal Assembly and is supported by all political parties due to its widely recognised public benefits.</p> <p><b>Contingent liabilities:</b> Contingent liabilities may limit the City’s capacity to implement capital projects. The capex budget projected for the next 10 years provides a reasonable buffer to absorb their potential payment.</p> <p><b>Implementation capacity:</b> This is the City’s first loan from an IFI. A Project Implementation Support TC will mitigate implementation risk and will help raise capacity.</p>
<b>Strategic Fit Summary</b>	<p>The Project is consistent with the Bank’s Strategy for Kosovo and the Green Economy Transition (“GET”) Approach 2021-2025 by promoting EE investments and applying the GET approach across all sectors and operations where this is relevant. The operation is also in line with the Municipal and Environmental Infrastructure Sector Strategy, by aiming to lower GHG emissions driven by EE, including a strategic priority to scale up high GET-impact investments in EE sectors, including EE measures in public buildings.</p>

<sup>2</sup> Article 27 of the AEB provides the basis for this decision.

## ADDITIONAL SUMMARY TERMS FACTSHEET

<b>EBRD Transaction</b>	A senior loan of up to EUR 5 million to the City, structured as a direct municipal obligation. The Project is expected to be co-financed with an investment grant in the amount of EUR 1 million, which will be sought from REEP.
<b>Existing Exposure</b>	None to the Municipality of Prizren. Total Bank's exposure to the sovereign as at 31 December 2020 was EUR 193 million in 7 projects, [REDACTED]
<b>Maturity / Repayment</b>	Tenor of 10 years, [REDACTED]
<b>Potential AMI eligible financing</b>	None.
<b>Use of Proceeds</b>	The loan and grant proceeds, which will be blended, will finance the implementation of EE, structural and comfort measures in up to 100 public buildings owned by the Municipality, such as kindergartens, schools and healthcare centres. The proposed EE measures include installation of variable speed pumps in heating systems and replacement of the heating source, thermal insulation of facades, thermal insulation of roofs and installation of new windows and doors made of PVC five-chamber profiles reinforced with stainless steel profiles. Structural measures include improvements of structures damaged in 1999, sewerage/drainage systems, waterproofing, asbestos removal etc. Comfort measures include improvement of insulation, heating/ventilation etc.
<b>Investment Plan</b>	Reconstruction, rehabilitation or refurbishment of public buildings to improve their structure, comfort and energy efficiency. [REDACTED]
<b>Financing Plan</b>	[REDACTED]
<b>Key Parties Involved</b>	Municipality of Prizren
<b>Conditions to subscription / disbursement</b>	<ul style="list-style-type: none"> <li>• The Loan Agreement is in full force and valid;</li> <li>• [REDACTED]</li> <li>• Compliance with the ESAP;</li> <li>• The Project Implementation Unit ("PIU") of the Borrower has been duly created, and the implementation support Consultant has been mobilised;</li> <li>• Satisfactory legal opinions.</li> </ul>
<b>Key Covenants</b>	<ul style="list-style-type: none"> <li>• [REDACTED] Establishing and maintaining a PIU with adequate resources;</li> <li>• Procurement under the Project according to EBRD Procurement Policies and Rules (the "PP&amp;R").</li> </ul>
<b>Security / Guarantees</b>	<ul style="list-style-type: none"> <li>• [REDACTED]</li> </ul>
<b>Other material agreements</b>	<ul style="list-style-type: none"> <li>• Pledge Agreements providing for the Security listed above</li> </ul>
<b>Associated Donor Funded TC and co-investment grants/concessional finance</b>	<p><b>A. Technical Cooperation (TC)</b></p> <p><i>Pre-signing</i></p> <p>1. <b>TC1: Feasibility Study</b> of the Project. [REDACTED]  <b>TC2: Environmental and social due diligence</b> of the Project - [REDACTED]</p> <p><i>Post-signing</i></p> <p><b>TC3: Project Implementation Support</b> including engineering design, procurement, preparation and evaluation of tenders, contract award and administration, supervision of works, financial control, project management and reporting. [REDACTED]  <b>TC4: Advanced Procurement Support for selection of PIU consultant</b>, including preparation of RfP, procurement support and contracting support [REDACTED]</p> <p><b>B. Co-investment grants / Concessional Finance (Non-TC)</b></p> <p>The Project will benefit from an investment grant in the amount of up to EUR 1 million from REEP.</p>

	<p><i>Cost sharing:</i> The Client will be responsible for paying all VAT and other indirect taxes that are applied to the donor-funded TC assignment where they are the contracting party as a parallel cost sharing contribution to the project (VAT is levied at 18 per cent in Kosovo). Lastly, the Client will also provide in-kind support in the form of office space, communication connections, etc., for the consultants to work, presumed to amount to 3 per cent of the total TC budget.</p>
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[REDACTED]

## INVESTMENT PROPOSAL SUMMARY

### 1. STRATEGIC FIT AND KEY ISSUES

#### 1.1 STRATEGIC CONTEXT

The Project involves financing of EE retrofitting, structural and other measures to improve comfort in approximately 100 municipally-owned buildings, comprising kindergartens, schools and primary healthcare centres, in Prizren, Kosovo's second largest city. The Project will improve the energy performance and environmental sustainability of the renovated buildings, rehabilitate damaged structures and improve comfort levels, critical for buildings of this nature.

Kosovo is one of the most energy intensive countries in the region, exceeding the EU-28 by over 4.3 times (in nominal GDP). With a high dependency on coal-powered energy sources, Kosovo's carbon intensity is also significantly higher at 7.2 times EU-28 average. Municipal buildings in Prizren, characterised by low thermal insulation and high average energy consumption, are no exception. In comparison with efficient public buildings in Western European countries, public buildings in Prizren are consuming 1.5 – 4.5 times more energy and emitting 1.1 – 2.5 times higher GHG. The City's EE Action Plan estimated that the annual energy saving potential is around 58 per cent in buildings for education, 32 per cent in administration and 57 per cent in buildings for healthcare services.

The Municipality of Prizren, with the support of UNDP, developed a Cross-Sectoral Intervention Plan on Climate Change in line with Kosovo's Climate Change Strategy (2019-2028), and thereafter approached the EBRD with a request to finance EE investments in eligible municipal buildings. The feasibility study found that the proposed Project generates significant economic and social benefits, thus generating a positive economic NPV, and Economic Internal Rate of Return ("EIRR") [REDACTED].

The Project is in line with the GET Approach 2021-2025, as implementing new EE technologies in buildings will reduce demand for carbon-intensive electricity and fossil fuels, and thereby reduce GHG emissions in the City and countrywide. The Project will introduce new standards in the management of municipally-owned buildings in Prizren by carrying out Energy Audits and preparation of EPC. The EE investments are aimed to improve energy performance of the renovated buildings by at least two EPC classes. Moreover, the Project and the associated TC will support the municipality of Prizren to develop an Asset Management Conceptual Framework and strengthen institutional capacity for sustainable and efficient building management.

Similarly, the Project is in line with the Municipal and Environmental Infrastructure Sector ("MEI") Strategy 2019-2024, which promotes climate resilience solutions and scaling up high GET-impact investments, including EE measures in public buildings. The Project will involve the private sector in designing and implementing EE measures based on energy audits, and EE certification of renovated buildings, in line with the MEI Strategy to facilitate project models that increase private sector participation.

Finally, the Project is consistent with the Bank's Strategy for Kosovo, which prioritises energy efficiency and application of the GET Approach. The Project builds on the Bank's policy engagement in Kosovo to implement EU directives concerning EE and renewable energy, including transposing the EPBD, which defines minimum energy performance requirements for new and renovated buildings, and drafting a long-term Building Renovation Strategy to



comply with the EE Directive (Art. 4). As the first or second sub-sovereign financing in Kosovo and the first direct borrowing by the City, the Project will have an important demonstration effect and expand the range of available financing instruments.

The COVID-19 pandemic did not have any direct effect on the Project, other than causing delays with its preparation. The financial impact of the COVID-19 crisis on the Municipality of Prizren was analysed by outside consultants as part of the TC for Municipal Budget COVID-19 Impact Analysis in Kosovo, and is presented in Annex 5.

## 1.2 TRANSITION IMPACT

### Primary Quality: Green

Obj. No.	Objective	Details
1.1	<i>The percentage of EBRD use of proceeds allocated to the project that qualifies as GET is 50% or higher.</i>	<p>The GET share, EE measures under the Project, are estimated at 100 per cent. Approximately 100 municipally owned buildings will benefit from EE retrofitting, structural and comfort improvement measures under the Project. The Feasibility Study estimated that the EE measures will generate [REDACTED] annual energy savings and [REDACTED] annual avoided CO2 emissions. The Project will go beyond local regulatory standards and practices and will aim to achieve implementation of high quality, new EE technologies in buildings is expected to have a strong demonstration effect across the country and the region.</p> <p>The Project will build on the Bank's policy support for the development of a building renovation strategy, in line with Kosovo's obligations under the EU Energy Efficiency Directive (Directive 2012/27/EU).</p>
1.2	<i>As a result of the project the client will introduce environmental management practices or standards, which fulfils the following three conditions: a) It is internationally accredited; b) It is novel (first or second of its kind) in the relevant market; and c) It is replicable by other market participants.</i>	<p>The Project includes energy audits and preparation of EPCs for the renovated buildings, which is a relatively new practice in Kosovo. The EE measures aim to improve energy performance of the renovated buildings by at least two EPC classes.</p>

**Secondary Quality: Resilient**

Obj. No.	Objective	Details
2.1	<i>The project introduces sub-sovereign project financing (municipal loan) as one of the first five times in the country.</i>	The financing structure, as the first direct borrowing by the Municipality of Prizren and the first or second sub-sovereign public sector project/borrowing in Kosovo, will expand the range of available financing instruments in the country.
2.2	<i>The project and associated TC support will help building necessary institutional capacity and procedures for sustainable and efficient infrastructure asset management where such capacity and procedures are widespread in the country or sector.</i>	The Feasibility Study consultant has also prepared an asset management conceptual framework for the City, which aims to commercialise the management of municipally-owned buildings. The City is expected to develop an asset management plan for its buildings.

**Delivery Risks to the achievement of transition impact:** The main risk is associated with the limited implementation capacities of the Municipality. This risk will be mitigated by providing project implementation support consultants to assist the Client in carrying out the Project, including engineering design, procurement, preparation and evaluation of tenders, contract award, financial control, monitoring and verification of energy performance requirements, including energy audit and EE certificates for all the renovated buildings, project management and reporting.

**1.3 ADDITIONALITY****Financial additionality**

Sources	Description of additionality sources
<b>Financing Structure:</b> <ul style="list-style-type: none"> <li>EBRD offers financing that is not available in the market from commercial sources on reasonable terms and conditions, e.g. a longer grace period. Such financing is necessary to structure the project.</li> <li>Public sector: EBRD investment is needed to close the funding gap. At the same time, EBRD does not crowd out other sources, such as from IFIs, government, commercial banks and/or complements them.</li> </ul>	<ul style="list-style-type: none"> <li>The loan tenor of 10 years [REDACTED] is above the market average, which is an appropriate structure for the Project.</li> <li>Commercial funding is not yet available for municipalities in Kosovo. The Bank's loan will be first direct municipal borrowing in Kosovo, thereby expanding the range of available financing instruments in the country.</li> </ul>

## Non-Financial additionality

Sources	Description of additionality sources
<p><b>Risk mitigation:</b></p> <p>EBRD provides comfort to clients and investors, financial or strategic, by mitigating non-financial risks, such as country, regulatory, project, economic cycle, or political risks.</p> <ul style="list-style-type: none"> <li>EBRD helps the client to mitigate carbon transition risks and take climate action, such as to move along a low carbon transition pathway.</li> </ul>	<ul style="list-style-type: none"> <li>The Municipality's administration has experienced difficulties in securing the majority votes at the Municipal Assembly, including for the COVID-19 economic recovery package and passing the 2021 Budget. Nonetheless, the Project received support from all parties due to its widely recognised public benefit, and due to the support during project preparation and implementation as well as application of EBRD's environmental and social standards.</li> <li>The Project will implement EE measures in around 100 municipal buildings which will result in energy saving and reduction of GHG emissions.</li> </ul>
<p><b>Standard-setting - helping projects and clients achieve higher standards:</b></p> <ul style="list-style-type: none"> <li>Client seeks/makes use of EBRD expertise over <b>energy and resource efficiency and climate resilience</b> financing via provision of energy and climate audits, minimum performance standards of technologies, climate-related strategies and policies, monitoring, reporting and verification (MRV) systems etc.</li> <li>Client seeks/makes use of EBRD expertise on <b>best international procurement standards</b>.</li> </ul>	<ul style="list-style-type: none"> <li>The Project through energy audits and preparation of EPCs for the renovated buildings, as well as EE measures aimed at improving energy performance by at least two EPC classes enhances the practices and sets new standards in the EE sector.</li> <li>Procurement under the Project will be carried out in accordance with EBRD Procurement Policies and Rules. Moreover, EBRD will provide Project Implementation Support TC which will include procurement, preparation of tenders and contract award and administration.</li> </ul>
<p><b>Knowledge, innovation, and capacity building:</b></p> <ul style="list-style-type: none"> <li>EBRD provides expertise, innovation, knowledge and/or capabilities that are material to the timely realisation of the project's objectives, including support to <b>strengthen the capacity of the client</b>.</li> </ul>	<ul style="list-style-type: none"> <li>The City has consistently underspent its capital budget due to its weak implementation capacities. The Project includes project implementation support by international consultants which is aimed at strengthening the Client's capacities.</li> </ul>

#### 1.4 SOUND BANKING - KEY RISKS

<b>Risks of Borrower</b>	<b>Probability / Effect</b>	<b>Comments</b>
Sovereign, and Prizren sub-sovereign Credit Risk	<i>Low/High</i>	<ul style="list-style-type: none"> <li>Kosovo has low public debt levels by regional standards and has capacity to increase sovereign borrowing. The level of sovereign debt was only 17.5 per cent of GDP as of end-2019, jumping to 24.5 per cent at end-2020 due to COVID-19 related crisis response measures. [REDACTED]. Hence, the sovereign credit risk is considered acceptable.</li> <li>Prizren currently has no debts outstanding [REDACTED]</li> </ul>
Political stability	<i>Medium/High</i>	<ul style="list-style-type: none"> <li>The next municipal elections will be held in October 2021. The mayors are selected directly therefore no changes are expected in the City's administration until next elections. The Mayor's party won the last central elections held in February, winning around 50 per cent of the votes. The project has broad political support.</li> </ul>
Financial balance strength / debt burden	<i>Low/ Medium</i>	<ul style="list-style-type: none"> <li>The City's financial performance is strong, with total revenues of EUR 50.1 million in 2019, up from EUR 40.7 million in 2017 [REDACTED].</li> <li>The City has generated consistent annual current surplus above EUR 16 million.</li> <li>The City currently has no debt outstanding.</li> </ul>
Contingent liabilities	<i>Medium/ Medium</i>	<ul style="list-style-type: none"> <li>[REDACTED]Contingent liabilities may limit the City's capacity to implement capital projects in the coming years.</li> <li>However, the projected capital budget for the next 10 years provides a reasonable buffer to absorb them.</li> </ul>
Implementation capacity	<i>Medium / Medium</i>	<ul style="list-style-type: none"> <li>[REDACTED]</li> <li>The Project will be implemented by a dedicated PIU established within the Municipality.</li> <li>TC will be provided to support the PIU in implementing the Project, including for engineering design, procurement, preparation and evaluation of tenders, contract award and administration, supervision of works, financial control, project management and reporting.</li> <li>The TCs will also help the client to speed up the implementation process by allowing faster mobilisation of the required consultants.</li> <li>The Feasibility Study provides the basis for defining the procurement packages, assessing associated contractual risks and accordingly for structuring the TC for project implementation support.</li> </ul>

## 2. MEASURING / MONITORING SUCCESS

<i>Overall objectives of project</i>	<i>Monitoring benchmarks</i>	<i>Implementation timing</i>
<ul style="list-style-type: none"> <li>- Population of Prizren benefiting from EE measures in public buildings (individuals)</li> <li>- Annual reduction in tonnes of CO<sub>2</sub> equivalent savings (tonnes CO<sub>2</sub> eq / yr)</li> <li>- Annual energy savings (GWh/yr)</li> </ul>	[REDACTED]	[REDACTED]

### Primary Quality: Green

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date	Donor
1.1	CO <sub>2</sub> e emissions reduced (tonnes/year)	Implementation of EE measures under the Project are estimated to achieve a total CO <sub>2</sub> emission reduction [REDACTED] per year.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
2.1	Improved energy management standards (including building /goods certifications)	Energy Audits and preparation of EPCs for municipally-owned buildings. The EPCs for each building after the implementation will be at least 2 classes above the current level.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

### Secondary Quality: Resilient

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date	Donor
2.1	Practices of the relevant stakeholder improved (operational)	Development of the Asset Management Plan for the Municipality's buildings	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

### 3. KEY PARTIES

#### 3.1 BORROWER

Prizren is the second largest municipality in Kosovo, with a population of around 180 thousand, accounting for 10 per cent of the country's total population. Prizren is the second largest commercial centre and the regional centre of southwest Kosovo, located near the border with Albania. The economy of Prizren municipality is mainly based on agriculture, trade, constructing and food processing, all private enterprises.

The local government is autonomous of the central government. The City is governed by the municipal Assembly and a City mayor, who is elected directly. The current mayor is Mytaher Haskuka, elected for his first term in the 2017 municipal elections.

Prizren's EE Action Plan presents the energy consumption analysis of the public buildings, residential buildings, public lighting and transportation sector, the efficiency potential and lists the projects to be implemented towards EE development. There are over 150 buildings owned and managed by the City. Currently, grid-supplied electricity bills for public heating and public lighting, and bills for motor vehicle fuels, amounts to around 3 per cent of the City's budget. Other materials such as oil, pellets, coal, and wood are also used for energy. A brief summary of the Prizren's financials is shown in table below.

**Table 1. Prizren's Financial Highlights**

[REDACTED]

#### 3.2 KOSOVO: MACROECONOMIC DEVELOPMENTS

Kosovo grew robustly over the last years, averaging at 4 per cent annually. However, due to COVID-19 pandemic, GDP is estimated to have contracted by 6 per cent in 2020, while under large uncertainties, it is expected to be followed by a recovery of 4 per cent in 2021 [REDACTED], mainly due to a more favourable external environment (higher remittances and exports) and an anticipated acceleration of investments, including in public infrastructure.

[REDACTED]. Following the end of its IMF programme in August 2017, the government has stuck to a prudent fiscal path, staying within the fiscal deficit ceiling of 2.0 per cent (rule excludes IFI financed projects). Due to the implementation of pandemic related support measures and recession-induced loss of tax revenues, the authorities allowed a relaxation of the fiscal rule over 2020-21. While fiscal revenues in 2020 declined by about 9 per cent, primary spending increased by more than 6 per cent, because of mitigation and recovery measures that led to a rise in subsidies and transfers of about 40 per cent. The "fiscal rule" deficit (that excludes capital investment financed by IFIs and bilateral sources contracted after 2015) reached 5.8 per cent of GDP during 2020 [REDACTED]. After 2021, the "Fiscal rule" deficit is expected to gradually converge to the below 2 per cent of GDP through the medium-term.

The current account deficit grew from 5.5 per cent in 2019 [REDACTED] to 7.5 per cent in 2020 (despite a decrease in imports and increase in the inflow of remittances. However, the current account deficit is projected to gradually decline [REDACTED].

An assessment of Kosovo's debt capacity is provided in Annex 2.

#### 4. MARKET CONTEXT

Kosovo's demand for energy is expected to increase in line with its economic development. Kosovo has a very low consumption of energy per capita, at ca. 32 per cent of the EU-28 average. While being an indicator of lower level of economic development, this implies that energy consumption will continue to increase in line with the economic growth and convergence of living standards.

Kosovo is a contracting party to the Energy Community Treaty, therefore it has to implement relevant EU directives concerning EE and renewable energy. Accordingly, it has a National EE Action Plan which provides the framework for a strategic approach to EE improvement, specifically setting energy savings targets (9 per cent by end-2018) and proposing concrete measures and actions.

The Government of Kosovo with the support of the World Bank ("WB") has established an Energy Efficiency Fund ("EEF") last year, which was capitalised initially from the government budget, and will also be supported by an EU IPA grant and a loan from the WB. Eligible investments will include rehabilitation of public buildings which cannot be financed through commercial funding. The Bank will consider collaboration with the EEF, initially by sharing experiences, as well as potential financing after a few years of proven record.

The Project will stimulate the EE goods and services market in Kosovo, establishing better access to public and donor funds. On the supply side, which includes provision of EE goods and services, such as installation of efficient heating and cooling systems, thermal insulation of walls / roof / floors, double-glazed windows, the successful implementation of the Project will enable the private sector to be involved in energy saving projects.

[REDACTED] The legal framework for EE is developed, but the secondary legislation required for the development of an ESCO market remains yet to be developed. The Project therefore aims to demonstrate financial viability of EE investments and thus promote bank lending for EE projects in the country and the region.

## **5. FINANCIAL / ECONOMIC ANALYSIS**

### **5.1 PROJECT FINANCIAL AND ECONOMIC ANALYSIS**

[REDACTED]

### **5.2 FINANCIAL PROJECTIONS OF THE CITY**

[REDACTED]

### **5.3 SENSITIVITY ANALYSIS**

[REDACTED]

### **5.4 PROJECTED PROFITABILITY FOR THE BANK**

[REDACTED]



## 6. OTHER KEY CONSIDERATIONS

### 6.1 ENVIRONMENT

Categorised B (2019 ESP). This project will have significant benefits related to high quality energy efficiency measures, including improvement to building insulation and replacement of old heating sources, resulting in improved energy efficiency and reduced emissions in public buildings in the city of Prizren. Environmental and social due diligence (“ESDD”) was comprised of an audit carried out by an independent consultant and included site visit to 11 selected buildings. The findings of the ESDD were that the Municipality has some limited elements of environmental and social management in place and is generally in compliance with national legislation. The ESAP has been prepared and agreed with the Municipality.

The Project consists of implementing energy efficiency (“EE”), structural and comfort measures in up to 100 municipally-owned buildings, such as kindergartens, schools, and primary healthcare centres. The EE measures will generate [REDACTED] annual energy savings and [REDACTED] annual avoided CO2 emissions [REDACTED]. Technical and ESDD findings showed that for some buildings, the water supplied does not meet drinking water standards, the sites are not connected to the sewage system and some schools are not equipped with proper toilets. Essential structural and comfort measures have therefore been added to the project scope; they include improvement of damaged structures, sewage/drainage systems, waterproofing, asbestos removal, sanitary rooms, etc. The Municipality does not have an E&S Policy, nor operate an Environmental, Health, Safety and Social (“EHSS”) Management System. The ESAP requires the client to assign responsibility for EHSS management at the Project Implementation Unit and to appoint a certified EHS Manager full time within the Municipality.

A Construction Phase Environmental, Health, Safety and Social Management Plan (“CESMP”) will be developed and implemented by the Contractor, and approved by the Municipality prior to start of construction. The ESAP requires the Municipality to ensure that in every Project building, i) building users have access to drinking water, ii) building users have access to toilets located within the building and equipped with flushing water, iii) domestic wastewater is collected and treated before discharge to natural environment.

All the contracts are in line with Law on Labour. The Municipality staff is covered by a Collective Labour General Agreement and a high percentage of employees are members of a Trade Union. There is currently no planned major programme of retrenchment across the Municipality. Most of the buildings are heated by central modern pellet boilers or firewood boilers of modern technology (or electricity); for the project-related buildings heated by non-certified individual firewood stoves, the ESAP requires replacement by a less air polluting heating system. Occupational H&S issues at the majority of the sites visited during ESDD need improved management; operational corrective actions have been captured in the ESAP. The ESAP also requires to conduct an intrusive asbestos survey and, where asbestos has been identified, to implement necessary measures to reduce the risks of exposure to asbestos fibres. Asbestos surveys will be conducted together with the Energy Audits in each Project building, and the implementation of an Asbestos Management Plan has been covenanted. The thermal insulation of walls and roofs will be suitably fire-rated by the Supplier, as prescribed in national standards. The ESAP requires that the design engineer submit a fire safety report to the Municipality, and that operational H&S issues are addressed after the end of the works (fire extinguishers, fire safety doors, etc.). All the buildings are owned and managed by the Municipality, however in some cases the land parcels are contested by private owners. The ESAP requires the Municipality to obtain the missing land titles. None of the Project building

is on the list of buildings which are under protection of UNESCO or national law (as confirmed by a provision in the Loan Agreement). The Municipality maintains its own official webpage. An online grievance mechanism is already in place. A Stakeholder Engagement Plan (SEP) has been developed during the ESDD; the Municipality will notify in advance the building users about the planned reconstruction activities including alternative access to disrupted services (e.g. patients to be sent to other health care locations temporarily).

The Bank will monitor the project through annual environmental and social reports provided by the Client, and site visits if necessary.

## **6.2 INTEGRITY**

In conjunction with OCCO, integrity due diligence was undertaken on the Municipality, its shareholders, senior management and other relevant parties. The [REDACTED] project does not pose an unacceptable reputational risk to the Bank.

[REDACTED] All actions required by applicable EBRD procedures relevant to the prevention of money laundering, terrorist financing and other integrity issues have been taken with respect to the Project, and the project files contain the integrity checklists and other required documentation which have been properly and accurately completed to proceed with the Project.

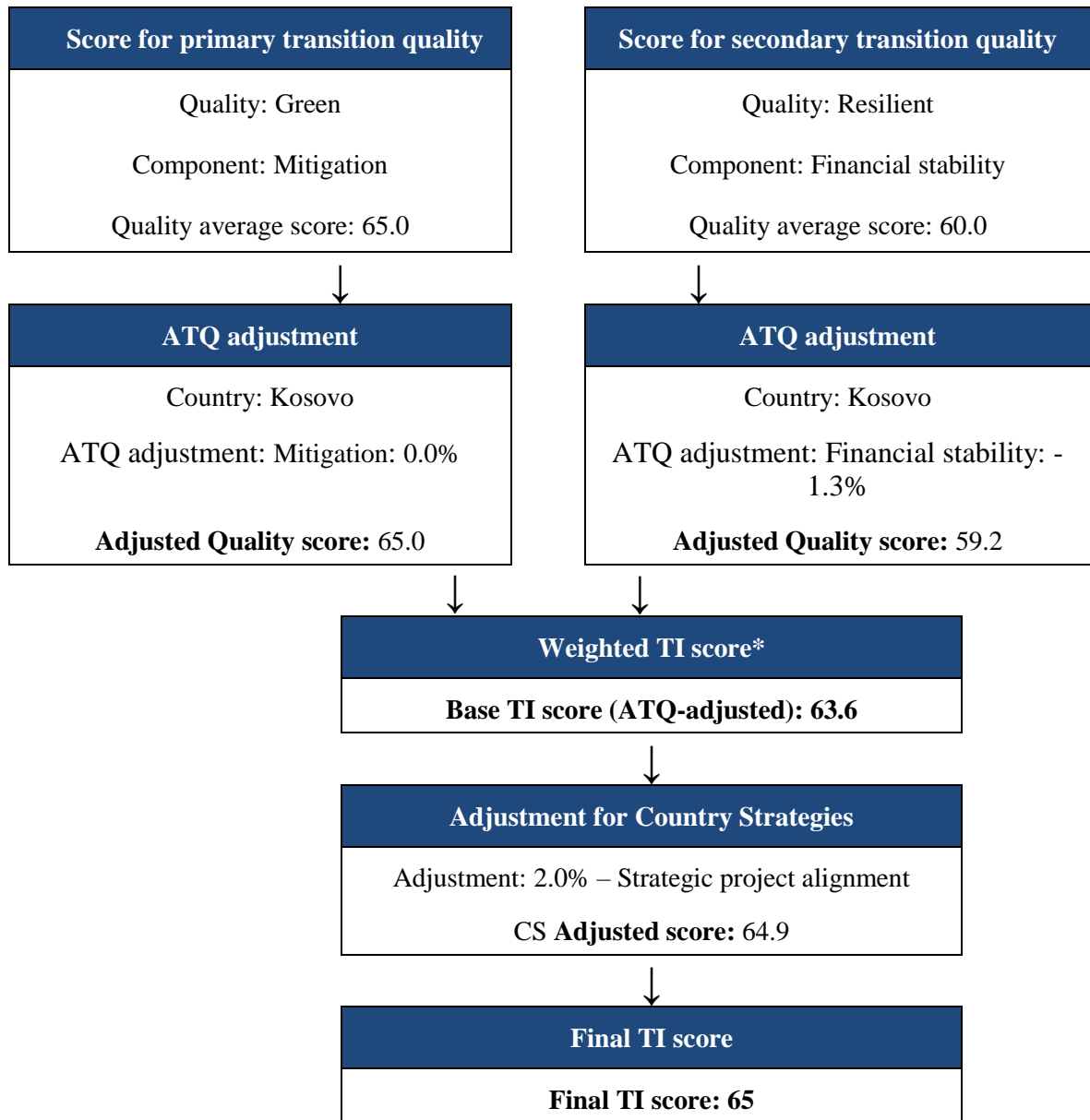
## **6.3 OTHER ISSUES - CONCESSIONAL FINANCE**

An investment grant co-financing of up to EUR 1.0 million will be sought from REEP to co-finance the Project to stimulate and improve the economic feasibility of the EE investments under the Project. The rationale for the use of co-investment grant is the presence of significant environmental externalities related to high CO<sub>2</sub> emissions generated from City's public buildings due to their energy consumption significantly higher than acceptable levels. The capex grant should also be justified on the merits of introducing and promoting innovative EE technologies and measures in public buildings, which will have a strong demonstration of the viability effect across the country and the region.

**ANNEXES TO OPERATION REPORT**

ANNEX 1	TRANSITION IMPACT SCORING CHART
ANNEX 2	SOVEREIGN DEBT ASSESSMENT
ANNEX 3	MUNICIPAL BORROWING LEGAL FRAMEWORK IN KOSOVO
ANNEX 4	PROJECT IMPLEMENTATION AND PROCUREMENT PLAN

## ANNEX 1- TRANSITION IMPACT SCORING CHART



## ANNEX 2 – SOVEREIGN DEBT ASSESSMENT

Kosovo's sovereign debt remains low relative to regional standards. However, reflecting the sizable fiscal deficits expected over 2020 – 21, public debt is projected to almost double [REDACTED].

The short-term fiscal financing needs arising from the impact of COVID-19 were and will continue to be secured through drawdowns from existing government bank balances, official financing from World Bank and other IFI resources, EU grants, and larger domestic issuance of government bonds. As a result, government debt grew to 24.5 per cent of GDP in 2020 [REDACTED].

Gross financing needs are projected to remain below the sustainability threshold in the medium-term. After peaking at close to 14 per cent of GDP in 2020, gross financing needs are expected to moderate to 9.4 per cent of GDP in 2021 and then decline and situate within the 7 - 8 per cent of GDP range over 2022 – 25. Resorting to the implementation of the fiscal rule beyond 2021 and increasing the average maturity of domestic debt should limit the vulnerabilities arising from the absence of external market access.

**Table 1. Public debt sustainability framework**

	2019	2020	2021	2022	2023	2024	2025
Public Debt (% of GDP)	17.6	24.5	28.7	30.4	31.7	32.9	34.1
<i>Key underlying assumptions for the baseline</i>							
Real GDP growth (%)	4.9	-6.0	4.5	5.5	4.0	4.0	4.0
Inflation (GDP deflator rate, in %)	0.6	2.1	-0.3	1.5	1.8	1.9	1.7
Primary Balance (% of GDP)	-2.5	-9.1	-5.5	-2.4	-2.0	-2.1	-2.0

Source: IMF, February 2021

[REDACTED]

## ANNEX 3 – MUNICIPAL BORROWING LEGAL FRAMEWORK IN KOSOVO

- A Municipality may incur Long-Term Debt to finance capital improvements that are related to education and healthcare.
- Debt may only be issues in the official currency of Kosovo – in EUR.
- Municipal Debt does not comprise a direct or indirect obligation of the Republic of Kosovo unless the Ministry of Finance has issued a written guarantee related to the debt.
- All Municipal Debt shall be secured and accounted as a general obligation of the Municipality, payable as a first claim from all of the Municipality’s lawfully available funds that have not otherwise been pledged to other Lenders.
- Debt may be additionally secured by a pledge on:
  1. A portion of Own Source Revenues
  2. Not more than 25 per cent of the General Grant it receives from the Central Government Budget.
- Intercept Financing: A Municipality may provide for additionally securing its Debt with revenues listed above by entering into written agreements to provide for the payment of Debt upon an Event of Default directly from unconditional transfers that are payable to the Municipality from the Ministry. This written intercept agreement may not provide for acceleration or otherwise vary any of the terms of repayment of the Debt. In the Event of Default, the written agreement must be sent to the Ministry.
- Debt may also secured by the immovable municipal property that is not used in delivering Municipal services.
- The total stock of short-and long-term debt, including guarantees, shall not at any time exceed more than 40 per cent of Collected Own Source Revenues and General Grants (excluding any of such revenues that are non-current) for the Fiscal Year immediately preceding the issuance of Debt.
- The amount of Debt Service owing in any year of a Long-Term Debt shall not exceed ten percent of the Total Collected Revenues (excluding any such revenues that are noncurrent) for the Fiscal Year immediately preceding the issuance of the Long-Term debt.
- In the Event of Default, Lenders of Debt, additionally secured with certain pledged revenues, shall be authorised to immediately take possession of any pledged revenues, which have been pledged to the Debt pursuant to the Resolution, and to use such revenues in accordance with the terms and conditions of the Debt or any Intercept Agreement, until all of the principal and interest on the Debt has been paid in full in accordance with procedures established by the Ministry of Finance.
- Limitation for Total Debt, which includes State Debt and Municipal Debt, as well as State and Municipal Guarantees:

In no event shall the outstanding principal amount of Total Debt exceed 40 per cent of the GDP. In the event that Total Debt would exceed 40 per cent of GDP, the

Government will present to the Assembly a strategy to bring Total Debt back under the threshold of 40 per cent within one year. Such strategy would be included in subsequent yearly budget laws.

The Law on Public Debt in Kosovo has been prepared in consultation and with support of the IMF. Based on the public debt limitations, purpose and security/pledge legally allowed, elaborated above, it can be concluded that the legal framework for public debt in Kosovo is creditor friendly.

Municipal debt structure, secured with a pledge on the state transfer, up to 25 per cent of the general grant it receives from the central government budget, together with the intercept financing clause, it can be considered as a quasi-sovereign credit risk.

As of end-November 2020 Municipalities in Kosovo had no debt outstanding.

## ANNEX 4 - PROJECT IMPLEMENTATION AND PROCUREMENT PLAN

### PROJECT IMPLEMENTATION

#### **Procurement classification – *Public non-sovereign***

[REDACTED]

#### **The Client's Capacity assessment related risk: High**

[REDACTED] The day-to-day procurement activity, which is relatively small, is handled on a needs basis by the City. The City is subject to Kosovo Public Procurement Law.

The main challenge remains the City's capacity to administer the procurement processes in accordance with the EBRD Procurement Policies and Rules and in the English language which represents a moderate risk to efficient procurement and implementation of the expected works and services. An experienced PIU and supervision consultant will guide the City and the PIU through tender preparation, procurement process and contract administration to mitigate this risk.

#### **The Contract's Risk assessment: Low**

The contract proposed to be co-financed from the Bank's loan and EU REEP Grant is detailed in the attached Procurement Plan. The support of an experienced consultant who will conduct the energy audits and detailed designs will ensure that technical specifications, employer's requirements and tender documents are suitable for open tendering and in accordance to the Bank's PP&R, moreover that any procurement and contractual issues that may arise will be addressed in a professional and timely manner.

The nature of the works contract is generally considered of low complexity and has a relatively medium to low degree of implementation risk. This risk is mitigated by appointing an independent consultant to conduct the required energy audits of the selected buildings and prepare the technical specifications and employer's requirements for the expected works, in addition, the consultant will support the client through the entire procurement, supervision, control and monitoring of the project along the entire project cycle. The risk will be mitigated by the appointment of an implementation consultant that will support the Client along the entire project cycle.

#### **Project implementation arrangements:**

The City will delegate the implementation responsibility to the PIU, who will have the overall responsibility for the implementation of the Project.

In terms of implementation risks, the higher risk resides on the potential number of buildings to be rehabilitated which management in parallel may challenge the limited capacity of the PIU and City. To mitigate this risk, the PIU capacity will be strengthened by a donor-funded experienced consultant(s) along the entire project. The advance procurement consultant will assist the PIU during the selection process of the PIU Implementation consultant. It will ensure a faster mobilization of the PIU implementation consultant, hence, faster implementation of the overall project.



The implementation consultant(s) will also assist the City in all aspects of procurement and implementation of the Project in accordance with the Bank's policies and support PIU in meeting requirements of various Financing Documents. When necessary, the consultant(s) will train the City and PIU staff in addressing the project procurement and implementation matters, ultimately, this consultant will assist the client with the preparation and completion of the required Energy Efficiency certificates.

**Procurement arrangements:**

There is envisaged one works contract for the reconstruction, rehabilitation or refurbishment of public buildings in the city of Pristina to improve their energy efficiency. The contract will be co-financed by the proceeds of the Bank's Loan and EU REEP grant. The envisaged works contract will be procured following open tendering procedures in accordance with the requirements of the Bank's PP&R for public sector operations and will be subject to prior review by the Bank. It is envisaged that the tender documents for the procurement of works will be based on the latest version of the Bank's standard tender documents for procurement of works.

The Project also envisages two technical cooperation contracts. An advance procurement consultant that will support the client during the Preparation of RFP and selection and contracting of PIU implementation consultant. The second technical cooperation contract is an implementation consultant who will support the PIU by carrying out energy audits and detailed designs that City will use to obtain the required construction permits for each building and definition of employer's requirements for further preparation of the tender documents. In addition, the implementation consultant will also act as PIU consultant and supervision consultant along the entire project cycle. Lastly, the consultancy services will also cover the preparation and completion of the energy efficiency certificates for each of the involved buildings.

Both consultancy contracts will be procured following the provisions of the Bank's PP&R Section 5 (Procurement of Consultant Services).

The Procurement Plan below provides the procurement strategy and details of planned investment and consultancy assignments.

**Additional information:**

The Contracts will be tendered via the EBRD Client e-Procurement Portal (ECEPP). The team has also investigated, based on market research, the potential benefits of applying national procurement procedures or Simplified Open Tendering procedure. However, limited previous experience in contracts of similar nature have been identified in Kosovo within the last 5 years. Furthermore, the use of national procedures could involve higher implementation risks due to current divergences of the Kosovo National Procurement Law with best procurement practice and in special with procurement complaint review process. Further investigation will be conducted in relation to the use of the Simplified Open Tendering Procedures. [REDACTED]