

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

Approved by the Board of Directors on 22 July 2020¹

KOSOVO

**VISP: VITAL INFRASTRUCTURE EMERGENCY
LIQUIDITY LOAN**

[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]

¹ 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

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|------------------------|--|
| AEB | Agreement Establishing the Bank |
| CEB | Council of Europe Bank |
| DH | District Heating |
| EIB | European Investment Bank |
| Eligible Sub Borrowers | Vital infrastructure providers - state and municipally owned companies, and municipalities in respect of vital infrastructure services |
| EPPs | Enforcement Policy Procedures |
| E&S | Environmental and Social |
| ESAP | Environmental and Social Action Plan |
| ESDD | Environmental and Social due Diligence |
| GIP | Good International Practice |
| GoK | Government of Kosovo |
| HSE | Environment, Health and Safety |
| ICT | Information and Communication Technology |
| KP | Kosovo Post |
| KPST | Kosovo Pension and Savings Fund |
| KT | Kosovo Telecom |
| MoF | Ministry of Finance |
| POEs | Publicly Owned Enterprises |
| PIMA | Public Investment Management Assessment |
| PSCs | Public Service Contracts |
| RWC | Regional Water Companies |
| WB | World Bank |
| VISP | Vital Infrastructure Solidarity Package |
| W&WW | Water and Wastewater |
| WWS | Wholesale Water Suppliers |

PRESIDENT'S RECOMMENDATION

This recommendation and the attached Report concerning an operation in favour of the Republic of Kosovo are submitted for consideration by the Board of Directors.

The facility will consist of a sovereign loan in the amount of up to EUR 30 million, to be on-lent to vital infrastructure providers in the context of a temporary shortfall in revenues following the economic disruption caused by the COVID-19 crisis. The Project is proposed under Window 2 of the Vital Infrastructure Support Programme (“**VISP**”) under the EBRD COVID-19 Solidarity Package. The loan will be divided into two tranches, one committed and one uncommitted: i) Tranche A in the amount of up to EUR 14 million to finance the Government’s immediate emergency liquidity support to vital infrastructure providers; and ii) Tranche B in the amount of up to EUR 16 million to finance further liquidity support to the same or other vital infrastructure providers on an as-needed basis during the rest of the year until their revenues/collections are restored.

The operation will enable the country’s vital infrastructure providers to guarantee satisfactory essential service levels and ensure sufficient on-going infrastructure maintenance, without being affected by the temporary decrease in bill collection levels. The expected transition impact of the project is *Resilient* contributing to the reliability of essential infrastructure services; and *Well-Governed* through support to the Government on developing a state ownership policy for publicly owned enterprises (“**POEs**”) and adoption and implementation of a draft law on POEs that aligns its corporate governance-related provisions with international best practices.

Post-signing TC support for this operation is expected to be provided for Environmental and Social capacity building to the Eligible Sub-Borrowers, and for support to the POE Monitoring Unit in developing and implementing a monitoring system that satisfies EBRD standards. The budget for the assignment is EUR 40 thousand and the donor remains to be confirmed.

I am satisfied that the operation is consistent with the EBRD COVID-19 Solidarity Package, the Bank’s Strategy for Kosovo and with the Agreement Establishing the Bank.

I recommend that the Board approve the proposed loan substantially on the terms of the attached Report.

Jürgen Rigterink
First Vice President, Acting President

BOARD DECISION SHEET

| Kosovo – VISP: Vital Infrastructure emergency Loan - DTM 52167 | |
|--|---|
| Transaction / Board Decision | <p>Board approval² is sought for a senior sovereign loan of up to EUR 30 million in favour of the Republic of Kosovo to be on-lent to vital infrastructure providers, divided into two tranches as follows:</p> <p>A. <u>Tranche A</u>: up to EUR 14 million to finance the Government’s immediate emergency liquidity support to vital infrastructure providers; and</p> <p>B. <u>Tranche B</u>: up to EUR 16 million to finance as required the Government’s liquidity support to vital infrastructure providers during the rest of the year until their collections are restored. Commitment of Tranche B is subject to Board approval.</p> |
| Client | <ul style="list-style-type: none"> The Borrower is the Republic of Kosovo represented by the Ministry of Finance. The Eligible Sub-Borrowers include vital infrastructure providers such as water and waste water companies, ICT, postal services, railway and bus transport, solid waste management and district heating as set forth in Annex 2. |
| Main Elements of the Proposal | <ul style="list-style-type: none"> <u>Transition impact</u> <i>Primary Quality - Resilient</i>, through stabilisation facilities for key infrastructure provides, which will benefit private sector by ensuring the reliability and viability of vital infrastructure throughout and beyond the COVID-19 crisis. <i>Secondary Quality - Well-Governed</i>, through: (i) support to the Government on developing a state ownership policy for publicly owned enterprises (“POEs”); and (ii) support for the adoption and implementation of a draft law on POEs that aligns its corporate governance-related provisions with international best practices. <u>Additionality</u> COVID-19 crisis response - Financing Structure: EBRD financing effectively bridges liquidity gap due to adverse market conditions. <u>Sound banking</u> Kosovo has low public debt levels and has the capacity to increase sovereign borrowing. Kosovo’s economy has shown resilience in the last years and is expected to recover rapidly after the crisis. |
| Key Risks | <ul style="list-style-type: none"> Kosovo’s economy grew robustly over the last years and its fiscal policy remained prudent. However, due to the current pandemic crisis, the economy is expected to be hit hard and government revenues to drop. Due to the crisis response fiscal measures, the budget deficit is expected to widen and the debt levels likely to increase. However, the risk is mitigated by low public debt levels (end-2019: 17.5 per cent of GDP), which even under the pessimistic scenario are expected to remain at an acceptable levels, under 40 per cent of GDP. Integrity and Control of Use of Proceeds: As the Bank’s PP&Rs, which are the principal safeguards and controls for the Bank’s operations in the public sector, will not apply and the use of proceeds will funnel through certain unknown counterparties (contractor and subcontractors) equivalent controls (e.g. integrity due diligence, EPP provisions) need to be in place. [REDACTED] |
| Strategic Fit Summary | <p>The Project is consistent with the Bank’s Country Strategy for Kosovo, which emphasises the need for restructuring of POEs to make them more efficient, sustainable improvements in quality of urban and rail transport services, and proposes financing in water and wastewater sector, and solid waste management. The Project is also consistent with Vital Infrastructure Support Programme presented under the COVID-19 Solidarity Package and with the Agreement Establishing the Bank.</p> |

² Article 27 of the AEB provides the basis for this decision.

ADDITIONAL SUMMARY TERMS FACTSHEET

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| EBRD Transaction | <p>The transaction consists of a sovereign loan of up to EUR 30 million to the Republic of Kosovo to be on-lent to vital infrastructure providers - state and municipally owned companies, and municipalities in respect of vital infrastructure services - (the “Eligible Sub-Borrowers”) affected by the COVID-19 pandemic crisis (the “Project”).</p> <p>The Loan will be divided in two tranches as follows:</p> <p>A. Tranche A: up to EUR 14 million to finance the Government’s immediate emergency liquidity support to vital infrastructure providers; and</p> <p>B. Tranche B: up to EUR 16 million to finance as required the Government’s liquidity support to vital infrastructure providers until their revenues/collections are restored.</p> <p>The availability of Tranche B is subject to fulfilment of conditions to commitment and Board approval.</p> |
| Existing Exposure | EUR 176 million to the Republic of Kosovo [REDACTED]. |
| Maturity / Exit / Repayment | Tenor of 3 years [REDACTED]. |
| Potential AMI eligible financing | N/A. |
| Use of Proceeds | <p>The proceeds of the Bank's loan will be used by the Government to provide emergency liquidity loans to vital infrastructure providers to compensate for immediate and temporary revenue losses due to COVID-19 related issues, until their revenues/collections are restored. No capital expenditure will be financed with this Project.</p> <p>Eligibility Criteria for the use of Loan funds:</p> <ul style="list-style-type: none"> - All Eligible Sub-Borrowers must be able to demonstrate loss of revenue due to the COVID-19 pandemic, and due to measures put in place by the Government to respond to the crisis, and confirmed as going concerns prior to the COVID-19 crisis; [REDACTED] - EBRD will assess and approve all Eligible Sub-Borrowers and ultimate beneficiaries if required under the structure in Annex 1 subject to EBRD integrity standards. <p>Monitoring:</p> <ul style="list-style-type: none"> - The Borrower, through the POE monitoring unit of the Ministry of Economic Development will furnish to the Bank semi-annual reports on the use of Loan proceeds, among other confirming compliance with the Eligibility Criteria for the use of Loan funds for every loan allocated to the Eligible Sub-Borrowers; - The Borrower will furnish to the Bank within 90 days after the end of each Financial Year a report, in form and substance satisfactory to the Bank, on Environmental and Social Matters arising in relation to the Borrower or the Project during such Financial Year. <p>Disbursement Approach:</p> <p>Due to the urgency nature of the Loan, the Borrower will provide emergency bridge liquidity to Eligible Sub-borrowers before Tranche A of the Loan becomes available, to be reimbursed when all the Loan conditions are met. The Bank will review the documentation with the assistance of an independent auditor to ensure that the use of proceeds and the eligibility criteria has been met prior to releasing any funding.</p> |

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| Investment Plan | The proceeds of the Loan will be used for short-term obligations [REDACTED] |
| Financing Plan | [REDACTED] |
| Key Parties Involved | Ministry of Finance; Ministry of Economy and Development; Municipalities; and Eligible Sub-Borrowers (vital infrastructure providers). |
| Conditions to subscription / disbursement | <p>Conditions Precedent to all Drawdowns:</p> <ul style="list-style-type: none"> - On-lending Agreement(s) between the Borrower and the Eligible Sub-Borrower(s) in form and substance acceptable to the Bank, including EPP/Audit/Inspection provisions, shall have been signed for the relevant disbursement amount. - Satisfactory supporting documentation for the use of Loan funds by the Eligible Sub-Borrowers for the relevant disbursed amount evidencing compliance with the Eligibility Criteria. - The Bank's approval of the relevant Eligible Sub-Borrower (and ultimate beneficiaries if required under the structure in Annex 1) following a full integrity assessment in line with the Bank's integrity standards. <p>Conditions Precedent to Commitment of Tranche B:</p> <ul style="list-style-type: none"> - Satisfactory assessment by the Bank of the Borrower's compliance with the Eligibility Criteria for the use of Loan funds under Tranche A; - Satisfactory assessment by the Bank of the Borrower's compliance with the Banks's Designated Performance Requirements under Tranche A. - Approval by the Bank of a TC assignment for the development of a state ownership policy on POEs. |
| Key Covenants | <ul style="list-style-type: none"> - Minimum tenor of sub-loans of 1 year; - Make progress on the revision of the draft Law on Publicly Owned Enterprises and seek parliamentary ratification for the revised Law as soon as conditions allow, but not later than the final repayment date of the Loan; - Implement a set of Environmental and Social procedures to achieve alignment with EBRD Performance Requirements 1 to 8 and 10. - Have proportionate controls in place and close oversight on each sub-loans provided under this project. No EBRD funding will be provided for contracts with an entity: that is owned or controlled by a PEP (as defined by FATF); is a related party (as defined by International Accounting Standard (IAS) 24; debarred or sanctioned (UN Chapter 7) or where there is an actual or apparent conflict of interest between the contracting parties. |
| Security / Guarantees | Sovereign loan |
| Other material agreements | On-lending Agreement(s) between the Borrower and the Eligible Sub-Borrower(s). |
| Associated Donor Funded TC | <p>A. Technical Cooperation (TC)</p> <ul style="list-style-type: none"> - Environmental and Social capacity building programme for the Eligible Sub-Borrowers, and support to the POE Monitoring Unit in developing and implementing a monitoring system that satisfies EBRD standards. [REDACTED] - Independent Auditor to validate compliance with the eligibility criteria for the use of Loan proceeds prior to any disbursement. [REDACTED]. <p>Additional TC for the development of State Ownership Policy for POEs to be approved prior to seeking approval for commitment of the 2nd tranche. [REDACTED]</p> |

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| | <p><u>Cost sharing:</u></p> <p>The Government will be responsible for paying all VAT and other indirect taxes that are applied to the post-signing TC assignments as a parallel cost sharing contribution to the project. Additionally, the Government and the Sub-Borrowers will also provide “in-kind” contributions 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 transaction consists of a sovereign loan of up to EUR 30 million to the Republic of Kosovo, to be on-lent to vital infrastructure providers (state and municipally owned companies, and municipalities in respect of vital infrastructure services) affected by the COVID-19 pandemic crisis (the “**Project**”). The Project is proposed under Window 2 of the Vital Infrastructure Support Programme (“**VISP**”), Solidarity Package 2.0.

Kosovo is suffering from severe negative social and economic impacts of the COVID-19 crisis. The economy is forecast to contract by 5 per cent in 2020, as tourism revenues, remittances (16 per cent of GDP), exports of goods, and FDI are all expected to decrease due to travel restrictions and the effect of the pandemic on its trading partners and remittance-originating countries. Moreover, the measures aimed at containing the pandemic heightened uncertainty affecting demand. The economy is expected to recover rapidly [REDACTED]. However, if the crisis prolongs, an economic contraction [REDACTED] is projected [REDACTED]. The deteriorating economic outlook is expected to result in external and financing gaps due to decreased tax revenues and necessary budget reallocations to fund the crisis emergency response.

The Government of Kosovo (“**GoK**”) introduced a country wide lockdown on March 16, which was in effect for roughly three months. In addition to restricting movement and curtailed travel between cities, it deferred utility payments amongst a raft of measures announced in response to the COVID-19 crisis. This has severely affected infrastructure service providers causing a temporary loss of revenues. Other companies such as those in the transport sector have had their operations suspended altogether. Given that POEs tend to operate on a breakeven basis with very low buffer, these companies are now in urgent need of liquidity to be able to continue to provide vital services to people and businesses and weather the crisis. Accordingly, the GoK has announced its intention to earmark up to EUR 30 million to support vital infrastructure providers as part of an ambitious emergency package [REDACTED]

The proceeds of the Bank's loan will be used by the GoK to provide emergency liquidity loans to vital infrastructure providers experiencing temporary loss of revenues due the current pandemic crisis and related government actions until their revenue collections are restored or services resumed. The Bank's loan will make available financing to vital infrastructure providers [REDACTED]. The Project ensures the continuity of vital infrastructure and sustainability of infrastructure services needed for the private sector. [REDACTED]

The loan will be provided in two equal tranches. Tranche A of EUR 14 million is envisaged to finance the Government's immediate emergency liquidity support to vital infrastructure providers. Tranche B of EUR 16 million is envisaged to finance as required the Government's liquidity support to vital infrastructure providers during the rest of the year until their revenues/collections are restored, and/or if there is a second wave of COVID-19 pandemic. Commitment of Tranche B is subject to Board approval.

The Eligible Sub-Borrowers include vital infrastructure providers such as regional water and wastewater (“**W&WW**”) companies, Information and Communication Technology (“**ICT**”) companies, postal services, railway and bus transport, solid waste management and district heating. The telecom, postal services, W&WW and railway transport services fall under the remit of the central government. The respective infrastructure providers are mainly POEs owned by the central

government, represented by the Ministry of Economic Development. The bus transport sector, solid waste collection and district heating fall under municipal jurisdiction.

The proposed Project is consistent with the Agreement Establishing the Bank as it ultimately aims to protect the delivery and viability of vital infrastructure for the private sector. Without EBRD support, [REDACTED] long-term transition to sustainable provision would be compromised. The Bank's support is targeted to ensure that essential infrastructure services are maintained despite shortfalls in infrastructure service revenues as a result of the COVID-19 crisis. The proposed emergency loan will enable critical infrastructure service providers to develop effective responses to the pandemic crisis. As such, it will not have a distortionary effect on market functioning. Sustainable operations of these public infrastructure services are necessary for private sector development and also essential for public health and environmental standards.

The Project is consistent with the Bank's Country Strategy for Kosovo, which in terms of transition challenges emphasises the need for restructuring of POEs to make them more efficient, the need for sustainable improvements in quality of bus and rail transport services, and proposes financing in water and wastewater sector, and solid waste management.

1.2 TRANSITION IMPACT

Primary Quality: Resilient

| Obj. No. | Objective | Details |
|----------|--|---|
| 1.1 | <i>Stabilisation facilities for key infrastructure providers</i> | The operation is part of the Bank's COVID-19 Solidarity Package and is presented under the VISIP. The Bank's loan will be used to support the immediate working capital needs of the Eligible Sub-Borrowers to compensate for temporary cash shortfall due to COVID-19 related issues (whether government action, consumer constraints or temporary reduction in demand), ensuring vital infrastructure services are preserved throughout and beyond the COVID-19 pandemic. The Project will support the sustainability of infrastructure providers, help them recover financially and operationally to pre-crisis levels and will benefit the local residents and the private sector |

Secondary Quality: Well-Governed

| Obj. No. | Objective | Details |
|----------|---|--|
| 2.1 | Commitment to improvement of Corporate Governance of POEs | The Bank's Legal Transition Team has assisted the GoK, via Technical Cooperation, with revising the law on POEs and align its corporate governance-related provisions with international best practices. The team has obtained commitments from the Government, which will form an affirmative covenant in the loan agreement, to make progress on the revision of the draft law on POEs and seek Parliamentary ratification as soon as conditions allow, and before final repayment under the Loan. The revised draft law foresees establishment of an independent Agency for oversight and monitoring of POEs. Moreover, after the revised law is adopted, the Bank's TC will continue with a pilot project with two POEs to assist them with the development and drafting of their business strategy. |
| 2.2 | <i>TC for State-owned Policy on POE's</i> | The Project also envisages TC support to the Government on developing a state ownership policy on POEs, which will set out clearly the Government's principles of active management and good governance of |

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| | | POEs. The dialogue in respect of this policy reform is still ongoing with the new government, which was only appointed on 3 June 2020. It is anticipated that details on this proposed TC will be clarified prior to Commitment of Tranche B. |
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1.3 ADDITIONALITY

| Identified triggers | Description |
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| A significant share (at least 30%) of the project is to finance working capital | Notwithstanding the identified triggers the proposed liquidity facility is necessary to help the Eligible Sub-Borrowers to mitigate the effects of the COVID-19 crisis, including, inter alia, collapse in service provision. By bridging the liquidity gap and alleviating financial pressure, Eligible Sub-Borrowers will be able to maintain operations and continue to provide vital services needed by the private sector. |
| Financing structure – Crisis response: EBRD financing bridges a financing gap due to adverse market conditions and fills a market funding gap | Kosovo does not have access to international capital markets for funding. The domestic commercial market has limited capacity to absorb higher government debt, especially during the current crisis. In addition, Kosovo has limited monetary policy as it has unilaterally adopted the Euro without being in the Eurozone. Therefore, Kosovo's borrowing potential is limited to IFIs/MDBs. The IMF and EU are providing general budget support loans, whereas the WB is financing through the budget the Government's crisis response in the health and social sectors. The Project is additional to other IFI financing for the crisis response as it will be channelled to vital infrastructure providers, which are not being financed by other IFIs, with the aim of protecting the delivery and viability vital infrastructure services in the economy. |
| Knowledge, innovation and capacity building- EBRD provides expertise, innovation, knowledge and/or capabilities that are material to the timely realisation of the project's objectives, including support to strengthen the capacity of the client. | The Bank through relevant TC provides support to strengthen capacity of GOK with respect to developing a policy for POE's and strengthening corporate governance |

1.4 SOUND BANKING - KEY RISKS

| Risks | Probability / Effect | Comments |
|-----------------------|----------------------|--|
| Sovereign credit risk | Medium / High | <ul style="list-style-type: none"> Kosovo is not risk rated by any of the main credit rating agencies. Kosovo has low public debt 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 [REDACTED]. However, in a stress test assuming that COVID-19 crisis prolongs beyond Q3 2020, [REDACTED] sovereign debt levels are expected to increase further, but will remain within sustainable levels, under 40% of GDP by the year 2023. In addition to the sovereign debt, the IMF also flags implicit contingent |

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| | | <p>liabilities with respect to debt held by POEs (estimated at around 5 per cent of GDP) and Privatisation Agency financing (about 1.5 per cent of GDP). [REDACTED]</p> <ul style="list-style-type: none"> • Gross financing needs in 2020 are large [REDACTED]. The new GoK is planning a larger economic recovery programme. With no access to international debt market and limited domestic borrowing capacity, Kosovo has to rely on IFI funding to finance the fiscal deficit. [REDACTED] • The EU and IFIs are also currently mobilising funding to support Kosovo's crisis response [REDACTED]. • As an IDA-eligible country, Kosovo has not requested any sovereign restructuring due to the current crisis, and no rescheduling of EBRD sovereign debt service is expected. |
| Macro-economic risk | Medium / Medium | <ul style="list-style-type: none"> • Kosovo's economy has shown resilience and grew robustly in the last years, and was projected to continue to grow by 4.0 per cent in 2020-2021 [REDACTED]. However, if the crisis protracts through the second half of the year, the GDP is projected to contract [REDACTED]. • Due to the COVID-19 crisis, the IMF projects the current account to deteriorate and external financing inflows to be cut by half, creating an urgent balance of payments need. The diaspora-related tourism revenues and remittances are expected to be affected significantly, but also exports of goods will decrease due to the global recession, as Kosovo's foreign sales are largely composed of metals. Although Kosovo will face an urgent financing gap this year, the IMF expects the balance of payments financing gap to be resolved within one year without major policy changes. • The Banking sector is well capitalised, liquid and profitable and able to withstand the impact of COVID-19 outbreak (IMF April 2020). The Central Bank of Kosovo has temporarily suspended loan repayments by borrowers affected by the crisis, and is applying regulatory forbearance on loan provisioning and capital requirements on the reprogrammed loans. However, the banking system is in a position to absorb this measure, as banks' NPLs remain low (2019: 2.0 per cent) and liquidity (27.2 per cent of assets) and capital buffers (CAR 16.6 per cent) comfortably within regulatory limits. |
| Political risk | Medium / Medium | <ul style="list-style-type: none"> • [REDACTED] A new Government has just recently been formed and has a remaining term of more than three years. Despite the tense fluid political situation, the proposed Project as well as other crisis related support from IFIs is expected to receive wide political support. • Internal disagreements about how to advance the dialogue with Serbia pose an additional risk. However, the new government has made strong commitments to continue the dialogue with Serbia. |
| Use of Loan proceeds / allocation risk | Medium / Medium | <ul style="list-style-type: none"> • [REDACTED] Clear and objective eligibility criteria have been established for the use of proceeds. EBRD will assess/approve all final Eligible Sub-Borrowers subject to integrity standards and based on evidence. Eligible Sub-Borrowers are defined as vital infrastructure providers, and must be able to demonstrate loss of revenue due to the crisis (with confirmed going concern prior to the COVID-19 crisis) and a requirement for support, i.e. significant risk of collapse in the service provision. • The process for on-lending and monitoring is well defined. Drawdowns |

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| | | are conditioned on on-lending agreements between the GoK/Borrower and the Eligible Sub-Borrower(s) in form and substance acceptable to the Bank for the relevant disbursed amount. Moreover, furnishing of satisfactory supporting documentation for the use of loan funds by the Sub-Borrowers will need to be in line with the eligibility criteria, and include evidence of loss of revenue and short-term obligations to be financed. Furthermore, commitment of tranche B is conditioned upon satisfactory assessment of compliance with the Eligibility Criteria on the use of loan funds under Tranche A. |
| Integrity Risk | Medium/High | <ul style="list-style-type: none"> The Bank's PP&Rs, which are the principal safeguards and controls for the Bank's operations in the public sector, will not apply and the use of proceeds will funnel through certain unknown counterparties (contractor and subcontractors), therefore equivalent controls need to be in place. The Bank will assess and approve each and every Eligible Sub-Borrower subject to EBRD integrity standards and based on evidence before disbursement. [REDACTED] |
| FX and interest rate risk | Low/Low | The loan will be in EUR, which is the legal tender in Kosovo. The Borrower will be exposed to the base rate risk, however, the short tenor of the loan provides some protection. |

2. MEASURING / MONITORING SUCCESS

Primary Quality: Resilient

| Obj. No. | Monitoring indicator | Details | Base-line | Target | Due date |
|----------|---|--|------------|------------|------------|
| 1.1 | Preserving the provision of vital infrastructure services | Provision of vital infrastructure services without any major disruptions during the COVID-19 pandemic crisis, and preservation of capacities beyond the crisis for 20 infrastructure service providers | [REDACTED] | [REDACTED] | [REDACTED] |
| 1.2 | Operational performance of the clients | Improved financial and operational performance of eligible beneficiaries. Growth in revenues, profitability and cash flows in the recovery period following the COVID-19 crisis to pre-crisis level (2019 operational and financial key performance benchmarks) taking into account GDP growth | [REDACTED] | [REDACTED] | [REDACTED] |

Secondary Quality: Well-Governed

| Obj. No. | Monitoring indicator | Details | Base-line | Target | Due date |
|----------|--|---|------------|------------|------------|
| 2.1 | Legal, institutional or regulatory frameworks in target areas improved | Parliamentary ratification of the revised law on POEs which aligns its corporate governance-related provisions with international best practices. | [REDACTED] | [REDACTED] | [REDACTED] |

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| 2.2 | Recommended policy or strategy agreed by relevant stakeholder(s) | State ownership policy on POEs, among other, setting out Government's principles of active management and good governance of POEs developed and adopted by the GoK. | [REDACTED] | [REDACTED] | [REDACTED] |
|-----|--|---|------------|------------|------------|

Delivery risks are mainly associated with the delay of the Parliamentary ratification of the revised law on POEs due to unforeseen political developments and shift of priorities. However, the improvement of corporate governance of POEs is in the agenda of the government and is expected to remain also for new governments. Moreover, continuity of provision of vital infrastructure services and capacity will be at risk if liquidity is not made available to them to weather the crisis.

3. KEY PARTIES

3.1 BORROWER

The Borrower is the Republic of Kosovo, represented by the Ministry of Finance, which will then on-lend the loan proceeds to the vital infrastructure providers.

3.2 VITAL INFRASTRUCTURE PROVIDERS

The Bank has undertaken an analysis on main vital infrastructure providers to benefit under the Project to understand the impact of COVID19 related measures on their performance and loss of revenues. [REDACTED]

Since the pandemic outbreak in mid-March until end of May, the selected infrastructure providers have suffered an actual loss of EUR 14 million. Based on management expectations and economic outlook, their loss is expected to increase [REDACTED] by year-end 2020[REDACTED].

Telecommunications:

Kosovo Telecom (“**KT**”) is one of the main beneficiaries under the Project. KT is the largest telecoms company in the country, structured as JSC and wholly owned by the GoK. Its main business is mobile phone services and also provides fixed line and internet services. TK has been suffering financial losses in the last years, mainly due to the market trend of falling telecommunication charges and shift to internet communication applications, but also due to internal operational inefficiencies. Moreover, due to the pandemic crisis, the Company has lost [REDACTED] roaming charges [REDACTED], which represent around 15-20 per cent Company’s revenues. Consequently, their revenues fell by around 15 per cent in March and 20 per cent in April. The management is expecting to restore [REDACTED] revenues slowly by end of 2020. [REDACTED] The Company needs emergency liquidity to maintain its communications infrastructure and continue provision of services.

Postal Services:

Kosovo Post (“**KP**”) is the national postal authority structured as a JSC and wholly owned by the GoK, providing postal and payment services. KP has suffered significant decline in revenues due to the lock-down. Sales went down to 45 per cent in March and 35 per cent in April compared to pre-pandemic levels. Recovery is expected to be slow [REDACTED]. The main reason for the decline is reduced bill payment services to public utilities and overall decrease in postal services. [REDACTED] The

Company needs liquidity to be able to operate and maintain its distribution infrastructure and continue provision of services.

Regional Water Companies:

The water and wastewater sector will be a significant beneficiary under the Project, which are key service providers to beat the virus outbreak. The sector comprises seven regional water and wastewater companies (“**RWC**”) companies and three wholesale water supply companies for irrigation and industrial use.

The RWCs have been severally impacted by the crisis with significant decline in collection rates. After the pandemic outbreak, the average collection rate of all RWCs dropped from historical 92 per cent to 59 per cent in March and 57 per cent in April. According to the management of selected companies, a similar collection trend is expected in May at around 60 per cent, with slight improvement during June-September period at around 67 per cent, and some more tangible improvement expected in the last quarter of the year at around 80 per cent. Recovery to pre-pandemic levels is not expected before early 2021, under the assumption that there will be no second wave of COVID-19 pandemic. [REDACTED] RWCs are among the utilities with the largest losses suffered during the pandemic. RWCs need emergency liquidity to be able to continue to deliver uninterrupted services until their collections are restored.

Wholesale Water Suppliers (“WWS”):

There are three WWS companies structured as JSCs and wholly owned by the GoK, supplying bulk water for industrial use, to water companies and for irrigation. Since WWSs are closely related and dependent to RWCs through supply of drinking water, their collection rates have experienced a similar decline. Thus, in March there was a drop from historical collection rate of 95 per cent to 70 per cent and down further to 64 per cent in April. Their managements are expecting slight improvements in the second quarter to 67 per cent, and further increase to 77 per cent in the last quarter of the year. Similarly, full recovery is not expected before early 2021. Consequently, the three WWSs are expecting to generate [REDACTED] loss of revenue [REDACTED] in 2020.

Railway Transport:

The railway sector beneficiaries include the railway infrastructure company, Infrakos (EBRD client) and the train operator, Trainkos, both POEs.

Infrakos generates around EUR 2 million in revenues per year, half of which is made of track access charges, rentals and other income, whereas the other half comes from annual transfers by the Government to contribute towards the cost of maintaining and operating the infrastructure. [REDACTED] Track access charges and other income fell below 45 per cent in March and April compared to historical levels due to suspension of passenger services, but also due to lower freight transport as mineral exports and oil imports were also affected by the crisis. Moreover, the Company also lost rental income due to suspension of business activities on its premises. The management is expecting slow recovery [REDACTED].

Trainkos is the main national train operator serving both passenger and freight traffic. The Company receives fare subsidy from the Government which makes around 50 per cent of its revenues. The rest of the revenues are made of freight traffic and other income. [REDACTED]. Whilst Trainkos’ freight revenue performance has not been acutely impacted as its passenger revenue (due to Ferronikeli – a large nickel producer; exporting company; EBRD client), there has been a noticeable impact on Trainkos’ operations. [REDACTED]

Bus Transport:

Bus transport potential beneficiaries include the Pristina municipality-owned urban transport company (Trafiku Urban; EBRD client) and the municipally owned inter-city bus stations of the larger cities which provide infrastructure services to inter-city bus operators, all private. The sector has lost revenues due the suspension of public transport by the GoK since 1st of April 2020. Partial services have resumed since 18th of May, and are expected to get back to normal from July 2020 onwards.

Trafiku Urban expects loss of revenues [REDACTED] in 2020 due to restricted/reduced operations. However, the Company is compensated gross cost (per bus/km) as per the PSC with the municipality of Pristina, which is structured to ensure cost recovery by adjusting the compensation based on the costs as per audited statements. The Company however will need liquidity to continue its operations until it recovers the costs from the City through the PSC process. Likewise, the Municipality of Pristina may need liquidity to make payments to Trafiku Urban as per the PSC due to a significant drop in ticket sales which would have been netted off from the due compensation.

District Heating:

There are two district heating (“DH”) companies in Kosovo. Termokos JSC (pipeline client) is the DH company serving around 15 thousand customers in Pristina, wholly owned by the Municipality. Gjakova DH is the municipal company providing services in the city of Gjakova. The Company is undergoing significant capital investment therefore not fully in operation. Collections of the two DH companies have declined from historical 95 per cent to around 65-70 per cent in March and 60-65 per cent in April. From May until October the companies do not provide services due to summer season, hence no collection issues during this period. However, the managements are expecting collection issues also in the new season from October 2020 of about 20 per cent decline. Consequently, they expect to lose revenues [REDACTED] in 2020. Both companies will require liquidity to carry out essential maintenance during the summer.

Solid Waste Collection:

The solid waste collection sector has also been hit hard by the pandemic as the people have not been paying the bills, also due to government action. The Loan will provide liquidity either directly to the companies or to municipalities in respect of waste collection services to ensure continuity of services.

The proposed beneficiary entities are in general too small and not credit worthy thus not eligible for direct financing. Therefore, the GoK or the respective Municipality are the only viable source of temporary liquidity.

As part of its ongoing work, the Bank has a technical cooperation project with the municipalities of Pristina, Prizren and Mitrovica to assess and understand the impacts that the COVID-19 virus is likely to have on budgets and finances of the municipality and municipal utility companies, as well as how this impact is reflected on provision of key infrastructure and other key public services under the Municipality’s responsibility.

4. MARKET CONTEXT

Vital infrastructure services (energy, telecom, postal services, railway and bus transport, water supply, sewage and waste) are managed by 17 non-financial central level and 44 local level POEs, which

account for around 5 per cent of GDP in terms of revenue and employ around 11,000 people (3.1 percent of total employment).

The energy sector (other than district energy companies focusing on renewables) is not included in the proposed facility.

The telecom market is liberalised and competitive. However, the mobile market, which is the main business, is a 2-player market [REDACTED]. TK dominates the fixed phone line market.

KP is the only postal services provider in Kosovo. There are also a few international parcel delivery providers operating.

The water and wastewater sector is regulated by an independent regulator, with tariffs set at cost recovery levels. Water losses are high, with non-revenue water above 50 per cent. A form of public service contract (“PSC”) is in place between the RWCs and the municipalities, though not at a level typically endorsed by EBRD. The RWCs currently cover over 90 per cent of the population with water supply services, and 74 per cent with wastewater services. Currently only 2 per cent of wastewater is treated, but the government is implementing a programme for constructing 7 wastewater treatment plans, two of which with co-financing from EBRD and EIB, and the remaining with funding from the Germany (KfW), Switzerland (SECO), France (Afd) and a bilateral sovereign loan from Hungary.

The railway sector is regulated by an independent regulator and is open to competition for train services. However, currently there is only one small private freight train operator. The track access charges are partly subsidised by the government, as well as rail infrastructure rehabilitation and maintenance.

Municipal Services:

There are in total 38 municipalities in Kosovo. Each municipality contracts its own municipal infrastructure services through public tendering or provides them via municipally owned companies. Some municipal infrastructure providers collect their fees directly from customers while others have public service contracts (“PSCs”) with the respective municipalities.

Kosovo has a fiscally centralised system with taxes collected at the central level. The Government allocates a proportion of its revenues to the municipalities in a form of transfers and grants based on population size. Municipal own revenues represent a smaller share of around 20 to 30 per cent their budgets. Accordingly, the Government intends to lend proceeds of the Bank’s loan either directly to vital municipal infrastructure providers or to municipalities in respect of infrastructure services to ensure continuity of service provision during the crisis and beyond.

The urban bus transport sector is very small, mainly functioning in the capital Pristina, which includes the municipal company and many small private operators. Licenses for bus routes and tariffs are set by municipalities. The Bank provided TC to the municipality of Pristina to introduce a PSC between the municipality and the municipal bus operator, and will continue to introduce simplified PSCs to private urban bus operators. The bus stations, which are municipally owned companies, will also benefit under the facility. They lost fee income due to restricted/reduced transport operations.

Solid waste collection companies are a mix of municipal and private providers. The private providers are contracted through open tendering process. The solid waste landfills are state-owned.

District heating (“**DH**”) is very limited in Kosovo. The Bank is currently working with the Pristina DH Company to potentially co-finance together with the KfW the construction of a solar powered district heating plant and a network extension.

The POEs generally suffer from overemployment and wages burden the companies’ balance sheets, while there is significant under-investment. Financial management and oversight of POEs is weak as assessed in the 2016 IMF Public Investment Management Assessment (“**PIMA**”). Weaknesses include lack of strategic documents, managerial accountability and absence of standard procedures for oversight and monitoring of POEs. The envisaged support to the GoK in for the revision of the law on POEs, as well as further support to selected POEs to assist them with the development and drafting of their business strategy aims to address these weaknesses.

5. FINANCIAL / ECONOMIC ANALYSIS

5.1 MACROECONOMIC OUTLOOK / FINANCIAL PROJECTIONS

[REDACTED]

5.2 PROJECTED PROFITABILITY FOR THE BANK

[REDACTED]

6. OTHER KEY CONSIDERATIONS

6.1 ENVIRONMENT

Categorised C (ESP 2019). This project is categorised C, since the use of proceeds is related to the provision of working capital to address issues such as office expenses and the payment of salaries (no physical works). The Client (Ministry of Finance) will be required to comply with the Bank’s PRs but since the Project is not expected to have potential adverse environmental and/or social impacts, the need to develop an Environmental and Social Action Plan (“**ESAP**”) was not identified. The Environmental and Social Due Diligence (“**ESDD**”) was conducted in-house, and consisted of raising written questions to the MoF on labour conditions, health and safety, and environmental management procedures. The ESDD concluded that the MoF follows national regulation but does not have environment, health, and safety (“**HSE**”) management system in place.

In addition, since the main E&S risks in this Project are related to the activities of the Eligible Sub-Borrowers (beyond the Bank’s use of proceeds), a post-signing TC assignment towards the Eligible Sub-Borrowers will be implemented in parallel to this Project in order to build their capacity and manage their main environmental and social risks.

The MoF complies with National Law on Labour and employees are free to join a workers’ organisation. Although the MoF does not have an Occupational Health and Safety management system, occupational accidents and diseases are documented, as required by national regulation. There is no procedure in place at MoF level to control and monitor the E&S performance of the Eligible Sub-Borrowers.

With regards to the Eligible Sub-Borrowers (state and municipally owned companies and municipalities in respect of vital infrastructure services), compliance with national standards for HSE will be the baseline which should be expected given they are public entities. The condition that, in making Sub-loans, the Ministry requires in the on-lending agreements that the Eligible Sub-Borrowers conduct their business in accordance with the national regulation related to HSE and Labour Conditions, has been covenanted. Satisfactory assessment by the Bank of the Borrower's compliance with the PRs during Tranche A is a Condition Precedent to disbursement of Tranche B.

The Phase 1 of the transactional TC related to this project has been approved by Grant Review and target two objectives: i) Capacity building of the Eligible Sub-Borrowers on Good International Practice (“GIP”) in relation to environmental and social issues in the sector; ii) Supporting the POE Monitoring Unit in developing and implementing a monitoring system that satisfies EBRD standards, for the duration of the Project. The Phase 1 comprises the scoping of the capacity building program and the development of the monitoring system, and will start after signing.

6.2 INTEGRITY

In conjunction with OCCO, a desktop-based preliminary internal integrity due diligence was undertaken on the potential sub-borrowers for this VISP (thirty-eight municipalities, their mayors, sixteen SOEs and their CEOs) in order to support high-level screening of potential beneficiaries. This will be further supplemented by additional integrity due diligence prior to any disbursement. [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 PROCUREMENT

VISP is designed to help clients continue to provide essential public infrastructure services, strengthen resilience and protect reforms. The use of proceeds for the proposed Loan will be on lent to Eligible sub-Borrowers to enable them to meet short-term obligations payable within 12 months covering inter alia payments to suppliers, employees, or payments to continue essential operations and maintenance under already locally procured contracts.

The proceeds of the Loan cannot be used for capital expenditure. On the basis that the PP&R was specially designed to cover the procurement of capital expenditures it is proposed that the Bank's Procurement Policies and Rules not be applicable. In making this recommendation, the Bank notes that its funds (i) will not support Capex, which will be covenanted both in the Loan Agreement and sub-loan agreements with Eligible Sub-Borrowers; (ii) financing is fungible, and (iii) most contracts benefiting from finance will be of low value and in most cases will only be partly financed by the Bank. In the event contracts are substantial contracts (on or above EUR 75,000 annually), stricter integrity arrangements will apply as described below and in Annex 1.

The TCs envisaged under the Project will be procured by the Bank in line with the Banks PPRs.

ANNEXES TO OPERATION REPORT

| | |
|---------|-------------------------------|
| ANNEX 1 | Integrity Due Diligence Chart |
| ANNEX 2 | Sub-Borrowers |
| ANNEX 3 | Summary of TIMS Analysis |

ANNEX 1- INTEGRITY DUE DILIGENCE AND EPP/AUDIT PROVISIONS CHART

[REDACTED]

ANNEX 2 - SUB-BORROWERS

The below list with potential sub-borrowers and sub-loan amounts for Tranche A has been provided by the Ministry of Finance, based on the applications they received and a dedicated committee assessment/decision for liquidity support. The below list of infrastructure providers, and all the potential sub-borrowers to benefit from the loan, will be assessed for the impact of COVID-19 on loss of their revenue and integrity standards prior to disbursement. All disbursements will be done based on the on-lending agreements signed for the disbursed amount, which will specify the use of proceeds, and supporting documentation provided, including the respective committee decision. The Bank will approve all final sub-borrowers prior to disbursement. The list for Tranche A may be subject to further changes prior to Board submission to ensure that the total amount of sub-loans is equal to EUR 14 million. [REDACTED]

ANNEX 3 - SUMMARY OF TIMS ANALYSIS

[REDACTED]