

DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT

Approved by the Board of Directors on 18 November 2020¹

NORTH MACEDONIA

GRCF2: SKOPJE BUS RAPID TRANSIT PROJECT

(UNDER REGIONAL: GREEN CITIES FRAMEWORK II)

[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.

TABLE OF CONTENTS

	Page
TABLE OF CONTENTS	2
ABBREVIATIONS / CURRENCY CONVERSIONS.....	3
PRESIDENT'S RECOMMENDATION.....	4
BOARD DECISION SHEET	5
ADDITIONAL SUMMARY TERMS FACTSHEET	6
INVESTMENT PROPOSAL SUMMARY.....	8
1. STRATEGIC FIT AND KEY ISSUES.....	8
1.1 STRATEGIC CONTEXT.....	8
1.2 TRANSITION IMPACT	10
1.3 ADDITIONALITY	11
1.4 SOUND BANKING - KEY RISKS	12
2. MEASURING / MONITORING SUCCESS.....	13
3. KEY PARTIES	15
3.1 BORROWER.....	15
3.2 THE CITY	16
3.3 JSP	16
4. MARKET CONTEXT	16
5. FINANCIAL / ECONOMIC ANALYSIS	17
5.1 ECONOMIC ANALYSIS.....	17
5.2 SENSITIVITY ANALYSIS	17
5.3 PROJECTED PROFITABILITY FOR THE BANK.....	17
6. OTHER KEY CONSIDERATIONS.....	18
6.1 ENVIRONMENT	18
6.2 INTEGRITY.....	19
ANNEXES TO OPERATION REPORT	20
ANNEX 1 – MAP OF THE BRT	21
ANNEX 2 – IMPLEMENTATION PROGRESS OF GrCF / GrCF2	21
ANNEX 3 – ECONOMIC ANALYSIS SUMMARY	22
ANNEX 4 – PROJECT IMPLEMENTATION	22
ANNEX 5 – JSP FINANCIAL STATEMENTS.....	23

ABBREVIATIONS / CURRENCY CONVERSIONS

AFC	Automatic Fare Collection
BPS	Business Procurement Specialist
BRT	Bus Rapid Transit
BRS	Bus Restructuring Study
CAPEX	Capital Expenditures
CDP	Corporate Development Plan
CO	Carbon Monoxide
CNG	Compressed Natural Gas
EBRD	European Bank for Reconstruction and Development
EC	European Commission
EIRR	Economic Internal Rate of Return
EIA	Environmental Impact Assessment
EHSS	Environment, Health, Safety and Social
ESAP	Environmental and Social Action Plan
EU	European Union
EUR	Euro
EURIBOR	Euro Interbank Offer Rate
FIDIC	Fédération Internationale Des Ingénieurs-Conseils
GCAP	Green City Action Plan
GCF	Green Climate Fund
GET	Green Economy Transition
GHG	Greenhouse Gas
JSP	Javno Soobrakajno Pretprijatje
IMF	International Monetary Fund
MKD	Macedonian Denar
MoEPP	The Ministry of Environment and Physical Planning
MoF	Ministry of Finance
MoTC	Ministry of Transport and Communication
NATO	North Atlantic Treaty Organization
NO _x	Nitrogen Oxide
NPV	Net Present Value
PIU	Project Implementation Unit
PM	Particulate Matter
PPE	Plant, Property and Equipment
PPP	Public-Private Partnership
PP&R	Procurement Policies and Rules
PSC	Public Service Contract
SEP	Stakeholder Engagement Plan
SOE	Sovereign
SSF	Shareholder Special Fund
S&P	Standard & Poor's
SUMP	Sustainable Urban Mobility Plan
TC	Technical Cooperation
TI	Transition Impact
VAT	Value-Added Tax
WWTP	Wastewater Treatment Plant

Currency conversion: EUR 1 = MKD 61.5

PRESIDENT'S RECOMMENDATION

This recommendation and the attached Report concerning an operation in favour of the Republic of North Macedonia (“**North Macedonia**”, the “**Borrower**”) for the benefit of City of Skopje (“**Skopje**”, the “**City**”) are submitted for consideration by the Board of Directors.

The facility consists of a sovereign loan to the Borrower in the amount of up to EUR 70 million to finance the development of a new Bus Rapid Transit (“**BRT**”) system in City of Skopje (the “**Project**”). The loan will be provided in two tranches: Tranche 1 of up to EUR 47.6 million to be committed at signing, and an uncommitted Tranche 2 of up to EUR 22.4 million to be committed at Bank’s discretion after completion of a separate Feasibility Study. The Project is a follow-on investment for the City of Skopje under its Green City Action Plan (“**GCAP**”) where the City has identified emissions from urban transport as a priority to address. The Project will be Skopje’s third investment with the Bank through EBRD Green Cities. This multi-sectoral approach to investing in sustainable infrastructure demonstrates Skopje’s commitment to implementing its now finalised GCAP.

The expected transition impact of the Project is (i) Green and (ii) Well-governed. The operation will introduce a new concept of public transport which will significantly improve the service levels in terms of frequency, capacity and speed for Skopje’s residents. Once implemented, the Project will help reduce air pollution, which is a major environmental concern for the City of Skopje, through investment in a low emission bus fleet using CNG or CNG hybrid technology. It will also support the City’s efforts in addressing urban transport challenges in a more efficient and structured way thanks to the preparation and implementation of a Sustainable Urban Mobility Plan (“**SUMP**”).

The Project will involve TC support totalling EUR 1.5 million provided either from the Bank’s Shareholder Special Fund or by an international donor to assist the City in implementation of Tranches 1 and 2, as well as for a preparation of the Feasibility Study for the Tranche 2.

I am satisfied that the operation is consistent with the Green Economy Transition (“**GET**”), which promotes investments that bring environmental benefits and mitigate the effect of climate change and other forms of environmental degradation, resulting in 100 per cent GET attribution to the Project. The operation is also consistent with the Bank’s Country Strategy for North Macedonia, the Municipal and Environmental Sector Strategy and with the Agreement Establishing the Bank.

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

Jürgen Rigterink
Acting President

BOARD DECISION SHEET

NORTH MACEDONIA – Skopje Bus Rapid Transit Project – DTM 51752 Framework: REGIONAL - Green Cities 2, Window 2 – DTM 50674	
Transaction / Board Decision	Board approval ² is sought for a senior loan of up to EUR 70 million in favour of the Republic of North Macedonia (the “ Borrower ”) to finance the development of two lines of a Bus Rapid Transit (“ BRT ”) system in the City of Skopje (the “ City ”, or “ Skopje ”). The Loan comprises two tranches: up to EUR 47.6 million to finance line 1 and to be committed at signing (“ Tranche 1 ”), and EUR 22.4 million to finance line 2 and to be committed at the sole discretion of the Bank following separate due diligence (“ Tranche 2 ”). It is proposed that the decision to commit Tranche 2 be delegated to Management.
Client	The Borrower is the Republic of North Macedonia, represented by the Ministry of Finance (“ MoF ”). Loan proceeds will be on-granted to the City which will implement the Project. The Bank’s existing sovereign exposure is EUR 633 million and private sector portfolio is EUR 137 million.
Main Elements of the Proposal	<p><u>Transition impact</u></p> <p><i>Primary Quality – Green.</i> The Project is Skopje’s third investment under EBRD Green Cities and will address the air pollution challenges identified in its GCAP. The investment will support a modal shift to public transport through dedicated traffic lanes using new CNG or CNG/hybrid buses and will contribute to improved local air quality.</p> <p><i>Secondary Quality – Well-governed.</i> The Project will support the City’s ongoing efforts in to improve urban transport in an efficient and structured way through the preparation and implementation of a Sustainable Urban Mobility Plan (“SUMP”).</p> <p><u>Additionality</u></p> <p>(i) Financing structure: The Bank will provide long term financing that is not available in the current market; (ii) Policy, sector, institutional, or regulatory change through strengthening the City’s urban transport planning policy; (iii) Risk mitigation: EBRD helps the City to mitigate carbon transition risk by supporting investment in a low emission urban transport bus fleet; and (iv) Standard-setting: The Bank will help the City to implement a complex BRT project by providing implementation support using best international practices.</p> <p><u>Sound banking</u></p> <p>The Project satisfies sound banking criteria due to the acceptable quality of North Macedonia sovereign risk.</p>
Key Risks	<p><u>Implementation risk:</u> The City will implement the Project in close cooperation with JSP, the City-owned public transport company. The City has limited previous experience in implementing projects of this scale or type. Implementation risk is mitigated by: (i) engagement of TC consultants to support project implementation, (ii) tendering of the BRT corridor under the Yellow FIDIC where an experienced contractor will be responsible for design and execution of works monitored by a Supervision Engineer, and (iii) establishment of adequately staffed PIU.</p> <p><u>Sovereign risk:</u> North Macedonia’s measures to mitigate the impact of the Covid-19 pandemic and to support its economic recovery is expected to result in a higher deficit and an increase in public debt in 2020. Financing of the deficit is supported by the utilisation of different financing packages from IFIs and the EU as well as from the recently issued euro bond. As of October 2020, North Macedonia’s public debt reached 60.3 per cent of GDP. Despite this increase, S&P confirmed North Macedonia’s credit rating as BB- with a stable outlook.</p>
Strategic Fit Summary	The Project is fully consistent with: (i) the Municipal and Environmental Infrastructure Sector Strategy 2019-2024, (ii) Strategy for North Macedonia, (iii) Green Economy Transition (“ GET ”) objectives and (iv) with the Agreement Establishing the Bank.

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

ADDITIONAL SUMMARY TERMS FACTSHEET

EBRD Transaction	Sovereign loan of up to EUR 70 million to be provided in two tranches: Tranche 1 of up to EUR 47.6 million to be committed at signing, and Tranche 2 of up to EUR 22.4 million to be committed at the Bank's discretion after separate due diligence and not later than 2 years following declaration of effectiveness of the Tranche 1.
Existing Exposure	The Bank's total sovereign exposure to the Republic of North Macedonia is EUR 633 million, including operating assets of EUR 244 million.
Maturity / Repayment	15 years tenor [REDACTED]
Potential AMI eligible financing	None
Use of Proceeds	Development of a BRT system in Skopje in two phases including development of two BRT lines, construction of a new bus depo and upgrade of an existing one, procurement of low-floor BRT vehicles, and upgrade of the ticketing, bus information and traffic control systems.
Investment Plan	[REDACTED]
Financing Plan	[REDACTED]
Key Parties Involved	<ul style="list-style-type: none"> • Republic of North Macedonia represented by the MoF as Borrower. • The Ministry of Transport and Communication ("MoTC") as the Borrower's authorised representative for disbursements. • City of Skopje (the "City") which will be the implementing agency and contracting party of the Project Agreement.
Conditions to effectiveness and disbursement	<p><u>Conditions to effectiveness (Tranche 1 and 2):</u></p> <ul style="list-style-type: none"> • Project Agreement signed and effective. [REDACTED] <p><u>Conditions to first disbursement (Tranche 1 and 2):</u></p> <ul style="list-style-type: none"> • Establishment of a PIU with adequate resources and suitably qualified personnel. [REDACTED]
Key Covenants	[REDACTED] Satisfactory implementation of the Environmental and Social Action Plan ("ESAP") and compliance with EBRD's E&S Policy.
Security / Guarantees	Sovereign loan
Pricing	Standard sovereign loan pricing
Other material agreements	N/A
Associated Donor Funded TC and co-investment grants/concessional finance	<p><i>Pre-signing</i></p> <ul style="list-style-type: none"> • TC 1: Technical and Environmental Due Diligence Study. [REDACTED] <p><i>Post-signing</i></p> <ul style="list-style-type: none"> • TC 2: PIU support for Tranche 1. The assignment will include review of designs and technical specifications, tender preparation and procurement, implementation of works and supply contracts. [REDACTED]

	<ul style="list-style-type: none">• TC 3: Feasibility Study and Concept Design for Line 2. The Study will appraise construction of the second BRT line, junctions, traffic control, etc. [REDACTED]• TC 4: PIU support for Tranche 2. Support for review of designs and technical specifications, tender preparation, procurement, and other implementation support of the second phase. [REDACTED]
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[REDACTED]

INVESTMENT PROPOSAL SUMMARY

1. STRATEGIC FIT AND KEY ISSUES

1.1 STRATEGIC CONTEXT

Skopje is the capital of North Macedonia and the largest and fastest growing city in the country. As a political, cultural, economic and academic centre, Skopje accounts for about 25 per cent of the population and contributes around 45.6 per cent of the country's GDP. Due to a significant daily migration into the capital from all parts of the country, the number of functional residents exceeds 550,000. Skopje's role as a population and economic hub is expected to grow over the coming decades, with the proportion of North Macedonia's citizens living in urban areas growing to over 70 per cent by 2050.³ To prevent urban sprawl and congestion, while addressing the current challenge of air pollution, Skopje needs to invest in public transport infrastructure that promotes a shift away from private vehicle use and increases connectivity across the City.

As an EBRD Green City (one of twelve in the Western Balkans), Skopje has developed a Green City Action Plan ("GCAP") to identify its most pressing environmental challenges and develop targeted investment and policy actions to address those issues. The GCAP has been finalised and is expected to be adopted by the City Council by the end of 2020. As noted in Skopje's GCAP, the City is one of the most polluted cities in Europe, with pollution concentrations far exceeding World Health Organisation limits. According to official statistics, air pollution causes more than 1,600 premature deaths per year in North Macedonia. Transport is one of the main sources of air pollution in Skopje, with a transport modal split dominated by fossil-fuelled private vehicles. To address this challenge, the City, through its GCAP, identified the need to continue renewing its existing, aged bus fleet with the Project's proposed cleaner vehicles and BRT infrastructure.

The proposed Project will introduce a BRT system in the City in two phases, the first of its kind in the Western Balkans. The City will select either CNG or CNG hybrid buses based on the results of a competitive procurement process. Once implemented, the BRT will provide a high-quality transit system that delivers fast, comfortable and cost-effective services on dedicated lanes. Busways and stations will be aligned to the centre of the road. The system will also be characterised by an off-board fare collection, and fast and frequent operations. It will feature high-level service standards with an extension of the existing systems such as an e-ticketing system, real time passenger information systems at the stops and dynamic service regulation based on the Traffic Management Centre developed under the Bank's first Skopje Urban Transport Project with the City of Skopje.

Through both phases of the Project, Skopje will significantly reduce emissions of harmful air pollutants. The Project envisages a reduction in the City's public transport generated carbon monoxide ("CO") emissions [REDACTED], particulate matter (PM)

³ United Nations, Department of Economic and Social Affairs, Population Division (2018). World Urbanization Prospects: The 2018 Revision, Online Edition.

[REDACTED], and nitrogen oxide (“NO_x”) [REDACTED]. These benefits, along with the Project’s alignment with Skopje’s GCAP priorities, make it eligible to be an EBRD Green Cities investment. Additionally, should the City select CNG hybrid buses, the Project has the potential to have further climate mitigation benefits by reducing greenhouse gas emissions [REDACTED] compared to the current scenario. Given the potential to promote hybrid vehicles, Phase 2 of the Project could benefit from support from the Green Climate Fund’s (“GCF”) dedicated concessional instruments for EBRD Green Cities. The Bank will explore this support with the City in the second phase should the opportunity arise in line with the Bank's concessionality policy.

The Project is Skopje’s third investment under EBRD Green Cities after GrCF: Skopje Bus Project (Opid 50185) and GrCF2: WWTP Skopje Project (Opid 50376). The proposed Project builds upon the previous bus transaction signed with the city public transport operator Javno Soobrakajno Pretprijatie (“JSP”) in 2019. This project has been fully disbursed and implemented and all of the 33 CNG buses have been deployed on Skopje streets since July 2020.

The Project is consistent with the Municipal and Environmental Infrastructure Sector Strategy which aims for “*Increased access to essential municipal infrastructure focused on quality, resource efficiency, reduced environmental impact*”. It is also aligned with the Bank’s Country Strategy for North Macedonia which points to “*Improved environmental infrastructure at the local and municipal level*” as one of the key areas of focus, and aims for “*support municipal mobility with a focus on urban transport systems and traffic control*”. The Project is also fully in line with the GET approach as it will have significant environmental benefits.

[REDACTED] Continuing efforts have been made to increase the support extended to the private sector with key focus areas being (i) working with small and medium enterprises both directly and via commercial banks; (ii) attracting private investors in the energy sector through Public-Private Partnership (“PPP”) schemes (renewables - auctions- and gas), and (iii) exploring expansion of PPP scheme in the healthcare sector.

Current transport operations have been significantly affected by Covid-19 due to restrictions on travel and use of public transport imposed by the government since April 2020. Whilst most of the restrictions have already been lifted, public transport services are expected to be affected through 2021 due to ongoing social distancing requirements and travel patterns. For the BRT system, the impact of any work or travel restrictions may have a limited impact on the Project implementation timeline. However, no impact on BRT operations is expected as a result of Covid-19 since by the time BRT is fully operational the pandemic is expected to be over.

As the Covid-19 pandemic has emerged, several links between the pandemic and air pollution have been observed. According to the recent World Bank Group report, the spatial, temporal, and sectoral structure of air pollution matters in Skopje, among other Western Balkans environmental hot spots, can translate into highly toxic pollution

peaks in the winter season⁴. Ambient air pollution is one of the main environmental death and disability risk in North Macedonia with 1,600 deaths every year. More and more people exposed to severe air pollution suffer from diseases identified as heightening vulnerability to Covid-19. Therefore, being a medium-term phased investment in clean bus technology, the Project contributes to an overall air improvement quality in Skopje and reduction of health vulnerability of its citizens.

1.2 TRANSITION IMPACT

The GrCF2 is a strategic and multi-project approach targeting environmental issues in cities in the Bank's countries of operation. Its primary goal is to achieve significant environmental improvements and promote the green transition quality in participating cities. The GrCF2 also aims to build the necessary capacity and facilitate better coordination and buy-in among various stakeholders within participating cities in order to improve the governance, operational efficiency and financial sustainability of the targeted investments and initiatives. These objectives are supported by the development and implementation of a city-specific GCAP identifying and prioritising environmental challenges and ways to address them through targeted investments, services and policy instruments.

This Project will contribute to achieving the Framework's objectives through the following TI qualities:

- **Green** (primary quality): The Project is the third investment under EBRD Green Cities, and will address air pollution as one of the most critical challenges identified by Skopje's GCAP. The investment is also in line with the GET approach. Prioritisation of public transport along these lines in dedicated traffic lanes in new CNG or CNG/hybrid engine technology will contribute to improved local air quality by reducing air pollution emissions (NOx and particulate matters) [REDACTED] for CO, [REDACTED]for PM, and [REDACTED] for NOx once both BRT lines are fully functional. The Project also has the potential to reduce GHG emissions [REDACTED] compared to baseline should the City opt for CNG hybrid buses.
- **Well-governed** (secondary quality): Beyond an ongoing support for the development and implementation of the Skopje GCAP's priorities, the Bank will carry on supporting the City in promoting better planning and regulatory capacity for green urban transportation and strengthening the financial sustainability of the municipal transport company. The preparation of the first critical documents towards meeting this objective (Corporate Development Plan ("CDP"), Public Service Contract ("PSC") and Bus Restructuring Strategy ("BRS")) is either ongoing or expected to be launched soon. With this Project, the Bank will further support City's efforts to tackle urban transport problems in a more efficient and structured process through a SUMP. While the BRS ensures operational performance and connectivity to all current population

⁴ The Economic and Social Impact of COVID-19, Western Balkans Regular Economic Report No.17; World Bank Group, Spring 2020

centres and facilities, the SUMP is focusing on developing a complete public transport network, including local connectivity and bus stop locations. The Bank partnered up with the EU Delegation in Skopje which secured financing for preparation of the SUMP by covenanting implementation of its most critical milestones in the Project's financing agreements.

The Transition Impact objectives and the relevance for this sub-project are detailed in Section 2. The transition qualities will be monitored at the Framework level aggregating data on each transition benchmark for all sub-projects.

Delivery risks: The main risks to delivery of the transition impact are related to implementation risks and final approval and implementation of Skopje's GCAP. Implementation risks are mitigated by City's and JSP's recent experience on procurement of CNG buses under *GrCF: Skopje Bus Project*. The City has demonstrated strong commitment in the course of the GCAP development, as it is recognised as one of the key strategic initiatives and priorities for the City.

1.3 ADDITIONALITY

Identified triggers	Description
A subsequent/consecutive transaction with the same client/group either with the same use of proceeds or in the same country (repeat transaction).	Bank's involvement is justified as continuation of its support to the City in development its urban transport system, one of the top priorities in Skopje's GCAP.

Additionality sources	Evidence of additionality sources
<p>Financing structure</p> <p>EBRD offers financing for infrastructure projects that is not available in the market from commercial sources on reasonable terms and conditions, e.g. a longer grace period restricted foreign currency financing etc. Such financing is necessary to structure the project. EBRD offers a tenor, which is above the market average and is necessary to structure the project of this nature.</p>	<p>The Bank provides long-term financing of 15 years [REDACTED], which is not readily available in North Macedonia from local commercial banks for projects of this nature. The proposed tenor is above the market average, and is justified by the long project implementation of the first in the Western Balkan region BRT system.</p>
<p>Policy, sector, institutional, or regulatory change</p> <p>EBRD's involvement in a project is considered additional when it is designed to trigger a change in the policy, sector, institutional or regulatory framework, or enhance practices at the sector or country level.</p>	<p>The Bank's long standing experience in the infrastructure sector in North Macedonia and unique ability to structure a GCAP, coupled with strengthening of transport planning policy of the City through development of the SUMP.</p> <p>Also, the development of the CDP, PSC and BRS, which will take into consideration the new BRT system will further support City's efforts to improve the overall urban transport system.</p>
<p>Risk mitigation</p>	<p>The Project will contribute to reduction of air pollution which is one of most pressing</p>

EBRD helps the client to mitigate carbon transition risks and take climate action, such as to move along a low carbon transition pathway.	environmental challenges in the City. Thus, investment in improved and low emission urban transport system will not only improve the air quality, but will also offer better quality services to Skopje citizens.
Standard-setting: helping projects and clients achieve higher standards Client seeks/makes use of EBRD expertise on corporate governance improvements, including for climate risk management.	The Bank's engagement is additional due to its experience in financing similar projects, existing client relationship and long-lasting policy dialogue and support in the urban transport sector in Skopje. The City lacks expertise and know-how in implementing projects of this magnitude which is the first of a kind in the country. Therefore, the Bank will support implementation of the Project by mobilising finance for high-qualified consultants to work closely with the PIU in all aspects of project implementation to ensure the Bank's standards are met and best sector practices applied.

1.4 SOUND BANKING - KEY RISKS

Risks	Probability / Effect	Comments
Project management/ implementation risk	Medium/ Medium	<ul style="list-style-type: none"> As with any large-scale construction project, there is a risk of cost overruns and delays. The cost overrun risk is mitigated by incorporating adequate contingency for all Project components. The City has limited experience in implementing large scale projects, therefore implementation risk is mitigated by: (i) engagement of TC consultants supporting Project preparation and implementation; (ii) tendering the works component on the basis of a Yellow FIDIC whereas an experienced contractor will design and build work's components monitored by a Supervision Engineer; (iii) creation of the PIU composed of representatives from the City and JSP. The City has already set up a PIU composed of experienced staff of the City and JSP. In addition, the Project will benefit from JSP acquired experience in the course of implementation of Skopje Bus project; 33 CNG busses have already arrived in Skopje in spite of the Covid-19 pandemic outbreak.
Sovereign risk	Medium/ Medium	<ul style="list-style-type: none"> In May 2020, Fitch affirmed North Macedonia's sovereign rating at BB+ with negative outlook due to the global pandemic. As of October 2020, the state debt and debt of state owned enterprises guaranteed by the government reached 60.3 per cent of GDP. Despite the increase in public debt, the latest credit rating as of September 2020, S&P confirmed its credit rating of BB- with a stable outlook. [REDACTED] Although the government will continue to take fiscal measures while the Covid-19 pandemic is ongoing (IMF expects the general government deficit to

		decline to 3.1 per cent of GDP in 2021), the rise in the debt level is to be only temporary. [REDACTED]
Macroeconomic risk	Medium/ High	<ul style="list-style-type: none"> [REDACTED] A recovery which started in 2018 with 2.7 per cent GDP growth continued in 2019 when GDP grew by additional 3.6 per cent. The growth was helped by political stability and the impact of the rising minimum wage and other social protection measures on private consumption. As a result of the Covid-19 pandemic, GDP is currently projected to fall by 5.0 per cent in 2020, rebounding by 3.0 per cent in 2021.

2. MEASURING / MONITORING SUCCESS

Project Monitoring Indicators for BRT Line 1 (Tranche 1):

Indicator	Projected Impact	Implementation Timing
Green		
Total Population benefitting from access to BRT system (individuals)	[REDACTED]	[REDACTED]
Annual reduction in tonnes of CO ₂ equivalent savings (tonnes CO ₂ eq / year)	[REDACTED]	[REDACTED]
Annual reduction in NO _x emissions (tonne / year)	[REDACTED]	[REDACTED]
Annual reduction in PM emissions (tonne / year)	[REDACTED]	[REDACTED]
Well-Governed		
Recommended policy or strategy agreed by relevant stakeholder(s)	<ul style="list-style-type: none"> - Prepared SUMP; - Adopted SUMP; - Implemented key SUMP recommendations. 	[REDACTED]

GrCF2 Framework Monitoring Indicators:

Obj. No.	Framework Objective	Transition Indicators	Contribution of Operation to Framework Objectives	Baselines	Target Values	Implementation Timeline
Primary TI Quality: Green						
1.1	Multiple green investments: Each participating city makes on average at least 3 investments that address priority environmental challenges identified by the GCAP, where all EBRD	Implementing an eligible Green Cities project	The Project will be the second follow-on investment under the GrCF2 and the third in the City after Skopje Bus Project (OpID 50185) and Skopje	[REDACTED]	[REDACTED]	[REDACTED]

	financed projects reduce emissions or improve resource efficiency by minimum 20 per cent or promote climate change resilience.		Wastewater Project (OpID 50376). It will result in reduction of air pollution emissions by minimum 20 per cent.			
1.2	Environmental impact: To achieve significant environmental improvements for at least one priority environmental challenge, i.e. the promotion or protection of certain performance levels (colour codes) for critical environmental challenges as specified in the GCAPs, for more than 50 per cent of the Green Cities.	Achieving significant environmental impact in a priority environmental challenge identified in the GCAP	The Project will address Skopje's air quality challenge as identified through the GCAP.	[REDACTED]	[REDACTED]	[REDACTED]
1.3	Effective GCAP implementation: To achieve the overall objective, the Framework will also have an implementation objective of achieving at least 50 per cent of all verifiable targets, set in all GCAPs, within 5 years after the respective GCAP finalisation (including both investments and well defined policy measures).	Implementing a project identified as a target for the GCAP	The Project was identified as a priority investment under the Skopje GCAP.	[REDACTED]	[REDACTED]	[REDACTED]
1.4	Strong follow-on support: At least 50 per cent of transactions and investment volume under GrCF2 being follow-on investments addressing critical environmental challenges identified in the GCAPs.	Implementing a follow-on project	The Project is a follow-on investment from the GCAP that addresses the priority challenge of air pollution.	[REDACTED]	[REDACTED]	[REDACTED]
Secondary TI Quality: Well-governed						
2.1	New GCAPs: 10 additional GCAPs finalised and approved where all GCAPs include priority actions and a monitoring strategy.	GCAP developed and submitted for approval	Development of GCAP by the City has been covenanted as part of the Skopje Bus Project. The GCAP has been finalised and is expected to be adopted by the City Council by the end 2020.	[REDACTED]	[REDACTED]	[REDACTED]
2.2	PSCs and tariff increases: PSCs and effective tariff increases in line with the respective PSCs, aimed at	Public service contract signed and	A PSC was covenanted under the Skopje Bus Project. It is currently under preparation.	[REDACTED]	[REDACTED]	[REDACTED]

	cost-recovery or improved fare-box ratio, for the majority of all sub-projects benefitting revenue-generating operators.	implemented				
		Tariffs reached the target level	Tariff increases in line with the PSCs aimed at cost-recovery or improved fare-box ratio are also covenanted under the Skopje Bus Project.	[REDACTED]	[REDACTED]	[REDACTED]
2.3	Access to financial markets: Develop green finance roadmaps in 4 cities to address the key elements required to access green finance markets, including green bonds.	A green finance roadmap finalised	N/A	[REDACTED]	[REDACTED]	[REDACTED]

3. KEY PARTIES

3.1 BORROWER

The Borrower is the Republic of North Macedonia, represented by MoF. Growth in North Macedonia accelerated to 3.6 per cent in 2019, from 2.7 per cent in 2018, driven by domestic demand, primarily the recovery of investment. The resolution of the country's name helped to strengthen investor confidence, as reflected in the June 2019 upgrade and affirmed in May 2020 country's sovereign rating to BB+ by Fitch, a rating agency. In March 2020, the country received a green light for the launch of the EU accession talks and became a NATO member. The framework for North Macedonia's EU accession negotiations is currently being prepared and the opening of the first chapter is expected to be conducted by 2020 year-end.

Vulnerabilities to the COVID-19 pandemic in North Macedonia are moderate and GDP is projected to fall by 5.0 per cent in 2020, rebounding by 3.0 per cent in 2021. The fall in GDP this year is to be the consequence of a fall in both domestic and external demand. The crisis has created an urgent balance of payments need to address, for which the authorities have requested and received financing from the IMF under the Rapid Financing Instrument worth EUR 176.5 million. In addition, the EC provided EUR 160 million under macro-financial assistance and the World Bank provided EUR 140 million in relief funds (out of which EUR 50 million is reallocation from exiting financing road programme). In May 2020, the country issued a six-year euro bond in the amount of EUR 700 million. Given financing obtained to address the pandemic, the sovereign finances remained stable.

As of October 2020, public debt increased to 60.3 per cent of GDP compared to 48.5 per cent as of 2019 year-end and is expected to increase further due to the funding required as a respond to COVID-19 outbreak. GDP declined by 6.3 per cent year-on-year in the first half of 2020, with sharp contractions in industry, trade, transport and tourism. On the expenditure side, government consumption recorded growth, while private consumption, investments, exports and imports all contracted strongly. The general government deficit increased marginally in 2019 (to 2.1 per cent of GDP, from

1.8 per cent in 2018). However, the government measures to mitigate the impact of the pandemic and support the recovery of the economy are expected to result in a higher deficit this year and an increase in the public debt. Despite the increase in public debt, Standard and Poor's affirmed its BB- long-term sovereign credit rating on North Macedonia with stable outlook. The rating is supported by the potential upside from strengthening institutional arrangements and structural reform implementation as part of EU accession negotiations as well as stronger expected growth beyond 2020.

3.2 THE CITY

The loan will be on-granted to the City, which has no borrowing capacity to be the Bank's borrower due to local legislation restrictions. The maximum new additional debt the City can incur in 2020 is EUR 47.7 million, of which EUR 26.3 million has already been utilised. Skopje is an existing client of the Bank and will be the party to the Project Agreement as the implementing entity under this Project.

3.3 JSP

JSP is a public transport company 100 per cent owned by the City. It employs 1,300 people. In 2019, the company realised 44 million passenger trips and produced 18 million vehicle-kilometres. JSP is an existing client of the Bank (OpID: 50185) with current exposure EUR 6.1 million. Under this project, the Bank is supporting key pillars of the current urban transport system structure through the PSC and BRS (contract to be awarded at the end of 2020).

Upon BRT Project completion, new buses and dedicated BRT bus stops will be handed over to JSP for operation and maintenance. The current draft of the PSC structure takes into account the effective costs incurred with the provision of the urban transport services and will also include BRT services as they become operational. The draft PSC also envisages a program of maintenance and repair of bus depots to be fully embodied in the PSC which cost will be latter on accepted as a base for a calculation of the performance-based subsidies that the City would be contractually bound to provide. JSP financial statements are presented in Annex 5.

4. MARKET CONTEXT

The public transport system in Skopje currently lacks a basic level of service. The bus route network is outdated and operated with old amortised buses which emit significant quantities of pollutants. Moreover, the low service level has caused a shift from public transport to private car usage in the past two decades, which increased traffic congestion leading to increased air pollution.

As with most other public transport systems, Skopje's public transport system does not presently generate enough revenue to cover its annual operating expenditure. Therefore, the City of Skopje currently provides an annual operating subsidy of c. EUR 10 million to the public transport operators.

The organisation of public transport in Skopje (regulation of bus routes, taxi services, parking, traffic safety and management) is under the responsibility of the City. Three companies currently operate buses on all routes in the City:

- JSP - a public transport operator wholly owned by the City, which provides 73 per cent of urban transport services (42 urban bus routes) and 71 per cent of suburban bus routes (49 bus routes). JSP currently has only an agreement on the provision of subsidies. The bus fleet inventory is composed of 401 bus of which 319 are operational. The average age of the fleet is 15 years but over 20 per cent is older than 27 years.
- Mak Express and Sloboda Prevoz – two associations of several private operators running on urban and suburban line networks, which provide the remaining 27 per cent of urban transport services (7 routes) and 29 per cent of suburban bus routes (9 bus routes). Mak Express operates on 5 lines with 41 vehicles and Sloboda Prevoz covering 11 lines on which it runs 71 vehicles. The activities of those two private operators are regulated by 5-year contracts with the City (based on number of kilometers ridden with no specific service quality requirement) signed in 2015.

In 2017, the City put into operation a fully functional single-card Automatic Fare Collection system which is used by both public and private bus operators. The levels of bus fares are set by the decision of the City Council. Students, pensioners and those with disabilities benefit from reduced fares and the cost of the discounts is covered by the subsidies from the City or government. Current levels of fares and subsidies from the City allow JSP and the private operators to cover only their operational costs, with no room for any major maintenance works or investments.

5. FINANCIAL / ECONOMIC ANALYSIS

5.1 ECONOMIC ANALYSIS

[REDACTED]

5.2 SENSITIVITY ANALYSIS

[REDACTED]

5.3 PROJECTED PROFITABILITY FOR THE BANK

[REDACTED]

6. OTHER KEY CONSIDERATIONS

6.1 ENVIRONMENT

Categorised B (2014 Environmental and Social Policy). The environmental and social risks and impacts associated with the construction and operation of a Bus Rapid Transit line can be readily assessed and managed. Due diligence comprised an environmental and social appraisal of the Project, which was carried out by independent consultants. It included an audit of the City of Skopje's and public transport company's environmental and social management policies and systems. Although public consultation has not yet been carried out, a Stakeholder Engagement Plan has been prepared and will be implemented by the City, taking account of COVID-19 restrictions.

The BRT line will be located along existing urban roads. The planned depot site is on a 7 ha plot owned by the City, which is currently used as a recreation and sports area. Some of these amenities will be lost and the ESAP will require the City to engage with local stakeholders to inform them about this and provide alternative recreational facilities. The Project will provide a modern and efficient public transport option for Skopje. The vehicles will be fully accessible, and the use of CNG/CNG hybrid will mean significantly lower emissions of particulates and other pollutants compared with the existing fleet and diesel alternatives.

The City and the transport company will need to put in place additional environmental and social policies and systems for the Project to be constructed and operated in line with EBRD's performance requirements. These additional actions are set out in the ESAP, which has been agreed with the City. The City will have responsibility for ensuring that ESAP actions are implemented by the transport company and contractors as appropriate. Construction and operation EHSS plans will be developed in conjunction with the PIU and the selected contractors. The transport company is EBRD's client and the ESAP for this previous transaction already includes implementation of appropriate E&S and OHS management systems, training of all staff on EHSS issues, provision of PPE equipment, development of a Traffic Management Plan, implementation of good housekeeping measures and development of grievance mechanisms for employees and the public. The company will have to ensure grievance mechanisms for residents potentially affected by the project are implemented for this transaction.

BRT projects fall under annex II of the EIA Directive, which is transposed into North Macedonia law, meaning that an EIA is not mandatory but may be required by the competent national authority. The ESAP includes a requirement for an EIA to be carried out if one is required by the Ministry of Environment and Physical Planning.

The PIU will help to supervise implementation of the ESAP and ensure compliance with national environmental and social requirements and EBRD's Performance Requirements. The Bank will monitor the environmental and social performance of the project through annual reports from the City.

6.2 INTEGRITY

In conjunction with OCCO, integrity due diligence was undertaken on the City, JSP and the senior management including Mayor Petre Shilegov. The review [REDACTED] concluded that [REDACTED] this 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.

ANNEXES TO OPERATION REPORT

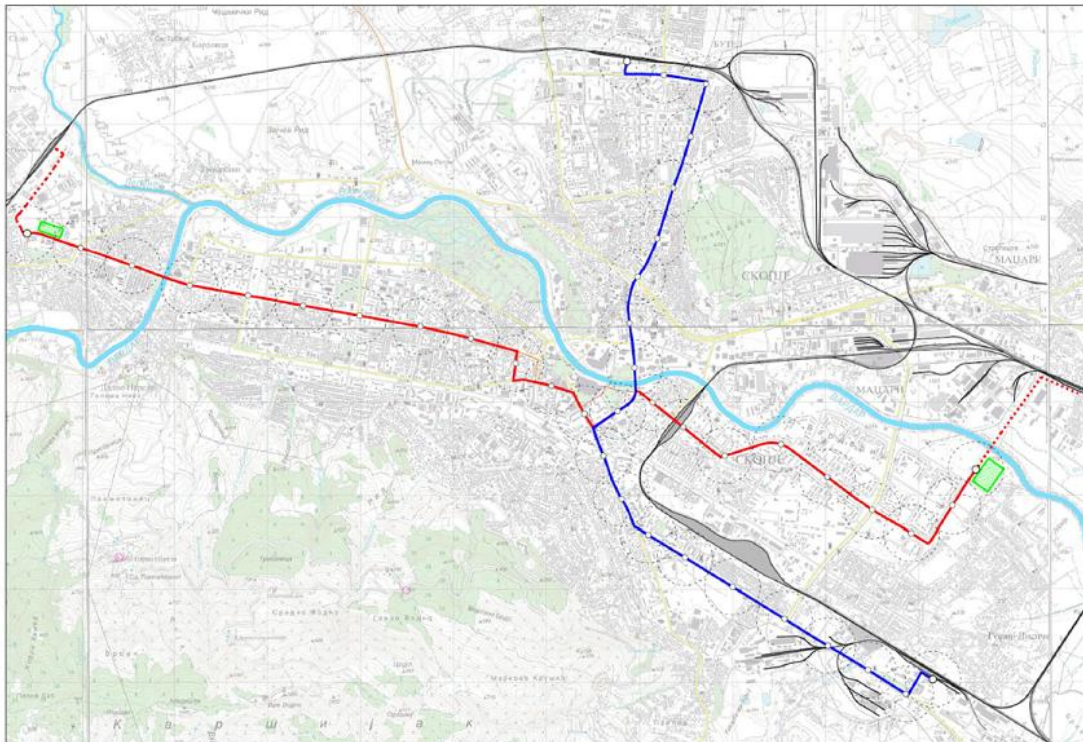
ANNEX 1	MAP OF THE BRT
ANNEX 2	IMPLEMENTATION PROGRESS OF GrCF / GrCF2
ANNEX 3	ECONOMIC ANALYSIS SUMMARY
ANNEX 4	PROJECT IMPLEMENTATION
ANNEX 5	JSP FINANCIAL STATEMENTS

ANNEX 1 – MAP OF THE BRT

The Project will be implemented in two phases:

Phase 1 includes development of the BRT Line 1 (East-West) of 12.8 km and 22 bus stops, construction of a new depot and acquisition of 29 low-floor CNG or CNG hybrid buses (red line one the map);

Phase 2 includes development of the BRT Line 2 (North-South) of 10.4 km and 20 bus stops and acquisition of 24 low-floor CNG or CNG hybrid buses (blue line on the map).



ANNEX 2 – IMPLEMENTATION PROGRESS OF GrCF / GrCF2

The Green Cities Framework (GrCF), approved by the Board in November 2016, set an ambitious agenda for the Bank's municipal business, with the over-arching aim being 'to serve as a sector-wide catalyst for addressing environmental challenges at the City level'. After only 2 years of operation, the Framework proved its ability to act as such a catalyst with the utilisation of the entire EUR 250 million headroom. As a consequence, in October 2018 a new Framework was approved by the Board, Green Cities Framework 2 (GrCF2), with a headroom of EUR 1.1 billion, with EUR 700 million from the Bank's own capital and the remainder from the Green Climate Fund (GCF) and other donors. Given the sizeable amount from the GCF, in the form of concessional loans and grants for both capex and TC and the requirement to confirm to GCF the availability of Bank co-financing, GrCF2 is divided into two windows:

Window I for GCF co-financing and Window II for non GCF co-financing. Since 2016, the GrCF and GrCF2 have mobilised nearly EUR 1.5 billion in EBRD and donor funding. [REDACTED]

ANNEX 3 – ECONOMIC ANALYSIS SUMMARY

[REDACTED]

ANNEX 4 – PROJECT IMPLEMENTATION

Procurement classification – *Public*

[REDACTED] The City established a PIU reporting to the Mayor and the PIU Head. The City has experience in the implementation of previous EBRD funded projects and has some experience of work with other IFIs but needs support to start the Project due to staff turnover.

The Client's capacity assessment related risk: Moderate High

Contracts risk assessment: Moderate High

Project implementation arrangements:

The City PIU is reporting to the Mayor and the PIU Head. In September 2020, the City awarded a consultancy contract to a company which will prepare a conceptual design for BRT Line 1 civil works expected to be completed by end 2020. The contract is funded by City's own funds. The City will also arrange and pay the costs of FIDIC Engineer contract for a project supervision and provide office/working desks for the Consultants and arrange for access to all relevant information, reports, maps, studies, legal documents at no cost to the Consultant.

The assignment of a PIU consultant for the Tranche 1 is split in two phases. The first phase is expected to start on April 2021 and will have a duration of 2 years. Given the complexity and the novelty of the Project, the Bank will assess the best timing for a start of second phase of the assignment, but in any case not earlier than April 2023. The Phase 2 PIU assistance to support Tranche 2 Project implementation will take on board the findings of the Tranche 2 Feasibility Study and will last 2.5 years.

Procurement arrangements:

All goods, works and services, financed from the Bank's loan, will be procured following open tendering procedure in accordance with the requirements of the Bank's Procurement Policies and Rules ("PP&R") for public sector operations.

The standard tender documents based on templates from EBRD Client Electronic Platform (“**ECEPP**”) and contract form will be used by the client.

The following contracts to be awarded under the Project through open tendering:

1. Development of BRT Line 1 (East-West) of 12.8 km and 22 bus stops and BRT Depot at the east end of Line 1 (Novo Lisiche) in a 7-hectare plot owned by the City of Skopje and minor interventions in Gorche Petrov depot to be awarded under two stage works tender process.
2. For Passenger Information and Smart Stops system a two stage goods tendering process will be used.
3. The acquisition of the following system components in vehicles and at the bus stops and the integration of junctions to the Traffic Management Centre (“**TMC**”) will be awarded on a direct contract basis as the City has contracts placed with existing suppliers, based on the review of the documentation provided by the City and carried out by independent expert:
 - Traffic Management System (“**TMS**”) the direct contract with SWARCO – estimated to be up to EUR 400,000 (with contingencies) – justification PPR 3.9 (a), which was awarded through competitive tendering previously under EBRD operation Skopje Urban Transport Project (OpID 41505) as the system is expanded and therefore PPR para 3.9 (c) and (d) will apply. Specifically, under PP&R direct contract considered to be justified “if a product, works or service can only be provided by a single supplier or contractor because of exclusive capabilities, rights or availability of required product and requires standardization with existing equipment is determined to be important and justified”. It was established that the number of new items are generally less than the existing number and compatible goods cannot be provided by other suppliers.
 - Fleet Management System (“**FMS**”) and Automatic Fare Collection (“**AFC**”) – the direct contract with Macedonian Telekom – estimated to be up to EUR 400,000 (with contingencies) - justification PPR 3.9 (c) and (d) as described above.

CNG/hybrid low-floor BRT vehicles (ca. 30 units) will be awarded under two stage open tendering goods contract.

All contracts under Tranche 2 will follow the same procurement strategy unless there is a justification for Direct Contracting. In such case, Board approval will be sought.

ANNEX 5 – JSP FINANCIAL STATEMENTS

[REDACTED]