

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

Approved by the Board of Directors on 20 July 2022¹

NORTH MACEDONIA

ESM Energy Crisis Liquidity Support

[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.

For the avoidance of any doubt, the information set out here was accurate as at the date of preparation of this document, prior to consideration and approval of the project.

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ABBREVIATIONS / CURRENCY CONVERSIONS

bps	Basis points
CAGR	Compounded Annual Growth Rate
CAPEX	Capital Expenditures
CFADS	Cash Flows Available for Debt Service
CFE	Cash Flow from Financing
CFI	Cash Flow from Investments
CFO	Cash Flow from Operations
CO ₂	Carbon Dioxide
CHP	Combined Heat and Power
COD	Commercial Operation Date
CP	Conditions Precedent
DSCR	Debt Service Coverage Ratio
DSRA	Debt Service Reserve Account
EBIT	Earnings Before Interest and Tax
EBITDA	Earnings Before Interest Tax and Depreciation
ESM	JSC Elektrani na Severna Makedonija
EPC	Engineering, Procurement and Construction
ERC	Energy Regulatory Commission
ESAP	Environmental and Social Action Plan
ESDD	Environmental and Social Due Diligence
EUR	Euro
EURIBOR	European Inter-Bank Offer Rate
FiT	Feed in Tariff
FiP	Feed in Premium
FX	Foreign Exchange
GDP	Gross Domestic Product
HPP	Hydro Power Plant
IFRS	International Financial Reporting Standard
IFC	International Finance Corporation
IPP	Independent Power Producer
LCOE	Levelized Cost of Energy
MKD	Macedonian Denar
MEPSO	Makedonski Elektroprenosen Sistem Operator
NECP	National Energy and Climate Plan
O&M	Operations and Maintenance
PV	Photovoltaic
PPA	Power Purchase Agreement
SSF	Shareholder Special Fund
TC	Technical Cooperation
TPP	Thermal Power Plant

CURRENCY EQUIVALENTS

Country's Currency Unit 1 Euro = 61.5 Macedonian Denar (as at 04 Feb 2021)

WEIGHTS AND MEASURES

1 kilowatt (kW)	=	1,000 watts (10 ³ W)
1 Megawatt (MW)	=	1,000 kilowatts (10 ³ kW)
1 Gigawatt (GW)	=	1 million kilowatts (10 ⁶ kW)
1 kilowatt-hour (kWh)	=	1,000 watt-hours (10 ³ Wh)
1 Megawatt-hour (MWh)	=	1,000 kilowatt-hours (10 ³ kWh)
1 Gigawatt-hour (GWh)	=	1 million kilowatt-hours (10 ⁶ kWh)
1 kilovolt (kV)	=	1,000 volts

PRESIDENT’S RECOMMENDATION

This recommendation and the attached Report concerning an operation in favour of JSC Elektrani na Severna Makedonija (the “Borrower”, “Company”, or “ESM”), a state-owned enterprise incorporated in the Republic of North Macedonia, are submitted for consideration by the Board of Directors.

The facility will consist of a loan to the Company in the amount of up to EUR 100 million. The loan will be guaranteed by the Republic of North Macedonia.

The operation will provide emergency liquidity support to ESM and will result in maintaining the Company’s financial stability, allowing it to continue to provide its essential services in the midst of global energy crisis as result of COVID-19 and further exacerbated by the war on Ukraine. Furthermore, the liquidity support will release additional resources to be used for its long-term capital expenditure programme for decarbonisation and development of renewable energy. The operation will include a robust Action Plan targeting commitments from the Company and the Republic of North Macedonia in relation to the energy sector decarbonisation agenda. The loan will be ring-fenced from any fossil fuel operations of ESM and will target financing electricity imports and working capital needs of ESM’s renewables and headquarter operations.

The Project transition impact stems from *Resilient* quality through a loan sized to cover critical operating costs coupled with an ambitious reform package which will support ESM navigate the current pan-European energy crisis, strengthen energy security in North Macedonia, and help deliver key structural reforms. The Project will also promote human capital development and capacity building for young female and male workers by introducing two new certified training programmes on key project management and energy trading skills (*Inclusive* quality).

As part of the Project, TC support will be provided for (i) the development of a decarbonisation plan for ESM in accordance with North Macedonia’s National Energy and Climate Plan (“NECP”), and (ii) the development of gender-responsive skills training programmes for ESM. [REDACTED].

I am satisfied that the operation is consistent with the Bank’s Strategy Republic of North Macedonia, the Energy Sector Strategy, the Green Economy Transition approach, the Equality of Opportunity Strategy 2021-2025, the Strategy for the Promotion of Gender Equality and with the Agreement Establishing the Bank.

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

Odile Renaud-Basso

BOARD DECISION SHEET

North Macedonia - ESM Energy Crisis Liquidity Support - DTM 53692	
Transaction / Board Decision	Board approval ² is sought for a sovereign guaranteed loan of up to EUR 100 million in favour of JSC Elektrani na Severna Makedonija (the “Borrower”, “Company”, or “ESM”). The loan will provide emergency liquidity support to the Company in order to maintain its financial resilience in order to continue to provide its essential services, enhance energy security for North Macedonia, and drive its decarbonisation agenda by freeing up additional resources to be used for long-term capital expenditure in renewable energy. The loan proceeds will be used for working capital and will be entirely ring-fenced away from any fossil fuel assets or operations of ESM.
Client	ESM is a public electricity generation utility, fully owned by the Government of North Macedonia (Fitch: BB+/S&P: BB-), that employs c. 4,600 people. The Company provides around 90% of the domestic production with installed capacity of c. 1,478 MW (comprising 56% Thermal power plants, 37% hydro plants, 2% Combined Heat and Power (“CHP”) and 2% wind). In 2021, ESM generated c.3,287 GWh of electricity, which led to revenues of EUR 259m, EBITDA of EUR 19m, net loss of EUR 28m and equity book value of EUR 550m.
Main Elements of the Proposal	<p>Transition impact: <i>Resilient:</i> Support ESM navigate the current pan-European energy crisis, strengthen energy security in North Macedonia as a whole, and help deliver key structural reforms; <i>Inclusive:</i> promote human capital development and capacity building for young workers across ESM’s operations in the key fields of project management and energy trading.</p> <p>Additionality: (i) Financing structure – EBRD offers financing that is not available in the market from commercial sources and other IFIs on reasonable terms and conditions; (ii) Climate risk mitigation and regulatory changes – EBRD will assist ESM to develop a decarbonisation strategy fully aligned with the Country’s NECP; and (iii) Standard-setting – Gender SMART – ESM will make use of EBRD expertise for the promotion of equal opportunities in its operations.</p> <p>Sound banking: The transaction is a loan guaranteed by the Republic of North Macedonia, rated BB- (Stable) by S&P on 18 February 2022 and BB+ (Negative) by Fitch on 19 May 2022.</p>
Key Risks	<p>Counterparty risk: Although ESM historically has had robust financial performance, during FY2021-FY2022, a combination of the need to cushion the impact on end users as a result of the energy crisis, weaker hydrology and lingering effects of the Covid-19 pandemic have caused weaker operating performance, leading to a liquidity gap. The government of North Macedonia has already provided fiscal policy support of ~EUR 169m during FY2021 and 1H2022, and the proposed sovereign guaranteed loan will help the company bridge the expected liquidity gap in 2022 and enable a financial turnaround that will support ESM’s capital investment plan much needed for its decarbonisation commitments.</p> <p>Reputation risk arising from ESM exposure to fossil fuel. The Bank has agreed an action plan with ESM and the Republic of North Macedonia targeting clear decarbonisation commitments [REDACTED]</p>
Strategic Fit Summary	The Project is aligned with the Bank’s Strategy for the Republic of North Macedonia, that promotes decarbonisation efforts including increased renewable energy capacity and enhanced access to quality employment and skills for youth, women and populations living in underserved area. It is also consistent with the Energy Sector Strategy, the Green Economy Transition approach, the Equality of Opportunity Strategy 2021-2025, the Strategy for the Promotion of Gender Equality and with the Agreement Establishing the Bank.

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

ADDITIONAL SUMMARY TERMS FACTSHEET

EBRD Transaction	Loan of up to EUR 100 million to ESM, with a sovereign guarantee from the Republic of North Macedonia.
Existing Exposure	<p><u>Direct Exposure:</u> DTM 50415: Loan signed on 4 January 2019, in the amount of EUR 5.9m for the financing of 10MW solar PV plant “Oslomej”. Disbursing and repaying [REDACTED].</p> <p>DTM 52320: Board approved on 12 October 2021, EBRD sovereign guaranteed loan of EUR 25m for the financing of 30MW solar PV plants in Oslomej (10MW extension) and Bitola (20MW) [REDACTED].</p> <p><u>Sovereign Exposure</u> Sovereign portfolio: EUR 656 million Sovereign operating assets: EUR 247 million</p>
Maturity / Exit / Repayment	Term Loan: Tenor of up to 5 years [REDACTED].
Potential AMI eligible financing	N/A
Use of Proceeds	<p>The loan proceeds will be used for working capital needs of ESM and will be entirely ring-fenced away from any fossil fuel assets or operations. [REDACTED].</p> <p>The Borrower will establish a special account to receive loan proceeds from the Bank. [REDACTED].</p>
Investment Plan	[REDACTED]
Financing Plan	[REDACTED]
Key Parties Involved	<ul style="list-style-type: none"> • ESM – Borrower; • Republic of North Macedonia represented by the Ministry of Finance – Guarantor.
Conditions to subscription / disbursement	<ul style="list-style-type: none"> • Standard for sovereign guaranteed loans including corporate documents, financing documents, guarantee agreement and compliance with ESAP for project preparation activities; • Declaration of use of proceeds by the Borrower prior to any disbursement stating that the purposes of each disbursement shall be used by the Borrower for the purposes of the Project and in accordance to the Eligible Expenditures definition in the Loan Agreement.
Key Covenants	[REDACTED]
Security / Guarantees	Sovereign guaranteed – Republic of North Macedonia (Fitch: BB+/S&P: BB-).
Other material agreements	None.
Associated Donor Funded TC and co-investment grants/concessional finance	TC 1: Decarbonisation strategy for ESM. The assignment will support ESM to develop and adopt a decarbonisation strategy aligned with the revised NECP. The strategy will contain i) time bound actions needed for the achievement of coal phase out and Just Transition considerations and ii) greenhouse gas emissions (GHG) reductions targets for 2030 and 2050 (aligned with the NECP), iii) required actions and investment plan associated with the Company’s decarbonisation plan, and iv) suggested Climate Corporate Governance (CCG) and Monitoring Reporting and Verification (MRV) considerations. The EBRD

	<p>will review, approve the deliverables, and monitor the implementation progress. [REDACTED].</p> <p>TC 2: Capacity building for the engagement of an external consultant to build project management and electricity trading capacity within ESM. Two certified training programmes will be introduced for young workers to gain market-relevant skills on electricity trading and on project management. [REDACTED] [E]mployees will benefit from the initiative, with [REDACTED] female participation, and including a cooperation with a specialised national or international college. [REDACTED].</p>
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[REDACTED]

INVESTMENT PROPOSAL SUMMARY

1. STRATEGIC FIT AND KEY ISSUES

1.1 STRATEGIC CONTEXT

North Macedonia's energy mix is dominated by domestic lignite coal-fired units and relies heavily on imports mainly in the form of gas and oil products. Coal is the main source of electricity and accounted for 49% of total generation capacity and 40% of electricity generation in 2021, one of the highest levels in Europe. This level of coal dependence thus represents a major social and economic challenge in the context of the country's pledge to follow the European Union's decarbonisation path towards a carbon neutral economy by 2050 as a signatory to the Sofia Declaration on the Green Agenda for the Western Balkans. It is a particular challenge for ESM, the public utility, that accounts for 90% of the entire domestic production and that owns around 80% of the lignite-fired capacity.

ESM is the state-owned electricity generation utility of North Macedonia. The Company has a total installed capacity of 1,448MW, primarily comprising lignite and large hydro. Domestic generation varies significantly due to hydrological conditions (e.g. FY2021 generation of 3,287 vs 4,339 GWh in FY2020, -24% y-o-y), but is on average sufficient to meet around 70% of domestic demand. ESM, via a subsidiary, is responsible for sourcing the remaining electricity on regional markets via auctions, since the country does not yet have an organised day-ahead power market. Auction prices are highly correlated with the Hungarian market (HUPX) price which have averaged approximately 50 EUR/MWh before the energy crises.

While the retail market in North Macedonia is technically fully liberalised, in line with the country's energy community obligations to implement the EU's Third Energy Package, ESM was compelled by the Government to sell around 90-100% of its electricity to the Universal Service Provider (USP) at tariff substantially below the market price, in order to mitigate the energy price shock and not transfer high prices to retail consumers.

Throughout 2021, a wide range of factors including the rapid recovery from COVID-19, extreme weather, and widespread recent underinvestment in production, pushed energy commodity prices to unprecedented highs. Spot prices for natural gas in Europe reached record levels, exacerbated by Russia's refusal to increase pipeline exports beyond contractual levels and concerns about stocking levels leading up to the winter heating season. Following the Russian invasion in Ukraine, European gas prices have surged to an average of 124.4 EUR/MWh in March 2022, with the highest ever daily price was recorded on March 7th, at 227.2 EUR/MWh. High commodity prices have fed directly through to power prices, with HUPX prices averaging over 200 EUR/MWh (four times increase compared to prior crisis levels) and reaching 700 EUR/MWh in March (fourteen times increase compared to prior crisis levels).

While North Macedonia does not use gas for power generation, the country's heavy dependence on regional electricity imports means that ESM has been forced to buy very significant volumes at these record prices. Similarly to other Western Balkan countries, end user prices in North Macedonia are still de-facto regulated via the USP and well below EU levels, especially for households.

Although previously robust, ESM's financial performance suffered in 2020 due to the impact of COVID-19 on electricity demand in addition to poor hydrology forcing most profitable hydro generation assets offline. The requirement to supply 90-100% of the USP demand and the large increases in wholesale electricity costs through 2021/22, which ESM has been unable to pass onto end users in order to avoid exposing households to record-high market prices, has however caused the Company's free cash flow and its cash position to rapidly deteriorate.

In November 2021, the Government declared a state of emergency in the energy sector and provided ESM with EUR 89 million of direct fiscal support which meant that for YE2021, ESM's cash position was still marginally positive. The government provided a further EUR 21 million in January 2022 and EUR 59 million in February 2022. In addition, North Macedonia's Energy and Water Services

Regulatory Commission (ERC) increased prices for electricity used by households by 9.48% in January 2022.

However, despite the government fiscal support and electricity price increases, ESM's free cash flows and the cash position of the Company were at historic low in January 2022. [REDACTED].

In this context, the proposed Project will ensure that ESM remains solvent throughout 2022 and enable it to continue to provide its essential services to meet the electricity demand of North Macedonia. Furthermore, it will allow ESM sufficient financial resilience and free up additional resources needed for its long-term capex programme focused on renewable energy development. Through the development of an Action Plan, the Project will create a platform to (i) push market reforms and developments designed to ensure competitive wholesale prices, (ii) support ESM to improve its project management and electricity trading capacities to more effectively manage risks and hedge against future price increases, and most importantly (iii) ensure that the Company and country continues with the ambitions decarbonisation plans that will provide a long-term and sustainable avenue to the current energy price crisis. The Action Plan will impose a set of legally binding obligations on i) the Government to enact key market reform and adopt a revised NECP and ii) ESM to align its decarbonisation strategy with the new NECP, including legally binding timeline for the decommissioning of its coal-fired capacity, development of new renewable energy capacity and implementation of the TCFD requirements on climate disclosures.

North Macedonia has adopted its enhanced National Determined Contributions (NDC) and is the first country in the Western Balkan to adopt a National Energy and Climate Plan (NECP) for the 2021- 2030 period, which sets out a complete coal phase-out by 2027, emission reduction target of 82% and RES deployment of 1.7 GW by 2030. EBRD has already provided technical assistance to establish an auctioning scheme for solar PV projects and supported ESM and the government to run a 100MW solar PV auction at the Oslomej coal mine. The Bank, in close cooperation with the local EU Delegation is also providing technical assistance to develop a Just Transition Plan and a national reskilling strategy covering the two coal regions at Oslomej and Bitola.

The transaction is determined as Paris Aligned and is consistent with the Bank's Fossil Fuels approach (2021). This is based on the commitment for the development and adoption of corporate decarbonisation strategy by ESM, with time bound actions for coal phase out, increased renewable energy capacity, decarbonisation ambition aligned with the NECP and Measurement Reporting and Verification (MRV) provisions. The Project does not invest in physical assets (capex), is consistent with the NDC and does not have carbon lock in risk.

TC support will be provided for (i) the development of a decarbonisation plan for ESM in accordance with North Macedonia's National Energy and Climate Plan ("NECP"), and (ii) the development of gender-responsive skills training programmes for ESM to develop capacities for electricity training and for project management.

The Project is aligned with the Bank's Strategy for the Republic of North Macedonia that promotes decarbonisation efforts including increased renewable energy capacity and enhanced access to quality employment and skills for youth, women and populations living in underserved area. It is also consistent with the Energy Sector Strategy, the Green Economy Transition approach, the Equality of Opportunity Strategy 2021-2025, the Strategy for the Promotion of Gender Equality and with the Agreement Establishing the Bank.

1.2 TRANSITION IMPACT

Primary Quality: Resilient

Obj. No.	Objective	Details
1.1	The project entails addressing current liquidity shortages of the company resulting from a sudden, significant change in economic activity due to a crisis event.	<p>The significant increases in wholesale electricity costs through 2021/22, which ESM has not been able to pass through to end users, combined with the requirement to supply 90-100% of the needs of the Universal Supplier, have caused the Company's cash position to rapidly deteriorate. Throughout 2021, the government provided ESM with EUR 89 million of direct fiscal support which meant that at YE2021, the cash position of ESM was still marginally positive. The government provided a further EUR 21 million in January 2022 and EUR 59 million in February 2022. However, despite the government fiscal support, cash position of the company remained very weak. [REDACTED].</p> <p>The sovereign guaranteed EBRD emergency liquidity loan is designed and sized to cover operating costs, including electricity imports and worker salaries, to ensure energy system stability at a time of crisis for local consumers.</p>
1.2	The project entails a policy dialogue initiative that has been assessed as Strong Good by the sector economist.	<p>The Project features a comprehensive policy dialogue package, including technical cooperation programmes, CPs and [REDACTED] commitments by both ESM and the Government of North Macedonia; aimed at supporting ESM navigate the current pan-European energy crisis, strengthen energy security in the country as a whole, and help deliver key structural reforms. The following are included in the Action Plan:</p> <ul style="list-style-type: none"> • Change of the electricity supply tariff methodology by introduction of tariff bands [REDACTED] • Approval by the Government of amendments to the Energy Law [REDACTED] • National Electricity Market Operator (MEMO) to appoint service provider for market coupling with Bulgaria, and establishment of working groups for market coupling with Greece [REDACTED] • Signing of the merger agreement between AD GA-MA and AD NER [REDACTED] • Capacity building to ESM to help boost the Company's power trading capabilities [REDACTED]

Secondary Quality: Inclusive

Obj. No.	Objective	Details
2.1	The project will introduce a new, replicable and accredited training programme improving skills for [REDACTED] people from the inclusion target group in partnership with (local)	ESM will also promote human capital development and capacity building for young workers across its operations in North Macedonia. This will be achieved by introducing two new certified training programmes that will allow young local workers to gain market-relevant skills on energy trading (i.e. analysis of market conditions, regulatory environment, development of financial instruments) and project management (i.e. procurement standards, supply chain management, risk management).

	vocational schools or universities	<p>The initiative will upskill [REDACTED] employees, including [REDACTED] female participants, and entail cooperation with a specialised national or international college. It will follow the principles of work-based learning and be designed with a gender lens. About a dozen of participants will be trained in key electricity trading skills, which are largely lacking across North Macedonia and the Western Balkans. Another [REDACTED] participants will be trained in project management skills, to enhance the capacity of the Company to manage the challenges and uncertainties that the energy security crisis entails.</p> <p>The delivery of this training programme will be delivered with the help of a TC consultant [REDACTED].</p>
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Risks to TI delivery:

Key risks to the realisation of the project TI relate primarily to potential non-implementation of the ambitious climate and energy market reform agenda. This is partially mitigated by the fact that (i) proposed reforms are included [REDACTED] in the loan agreement; (ii) they are fully aligned with North Macedonia's Energy Community conditionality; and (iii) they have been extensively discussed with relevant authorities, are accepted as valid drivers for bringing ESM back to financial sustainability and the Action plan was considered and approved by the Government.

1.3 ADDITIONALITY

Identified triggers	Description
A significant share [REDACTED] of the project is to finance working capital (subject to sector characteristics).	The liquidity facility will provide emergency funding to ESM to be used primarily for working capital consisting of eligible salaries (excl. fossil fuel related operations), taxes, electricity imports, and other operating expenses. These are all ring-fenced from all fossil fuel operations and subsidiaries of ESM.

Additionality sources	Description / Evidence
<p>Financing Structure - EBRD offers financing that is not available in the market from commercial sources on reasonable terms and conditions. Such financing is necessary to structure the project.</p> <p>Public sector: EBRD investment is needed to close the funding gap. At the same time, EBRD does not crowd out other sources, such as from IFIs, government, commercial banks and/or complements them.</p>	<p>EBRD's participation with the proposed emergency liquidity facility is critical to assisting ESM to withstand the financial distress caused by the energy crisis, improving the long-term resilience of its balance sheet, and enabling the envisaged decarbonisation agenda of North Macedonia. ESM is unable to raise financing locally that is sufficient to close the liquidity gap [REDACTED].</p> <p>The proposed loan tenor is longer than available from the local banking sector for this type of financing. Given the substantial liquidity gap, the proposed combination of debt sizing and 5-year tenor is critical to delivering the envisaged turnaround for ESM and its ability to repay the loan from its own cash flows.</p>
<p>Climate Risk Mitigation/Policy sector, institutional, or regulatory change</p> <p>EBRD helps the client to mitigate carbon transition risks and take climate action, such as to move along a low carbon transition pathway.</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 (e.g., an introduction of cost-reflective pricing of energy, water etc.).</p>	<p>In addition to the extensive policy dialogue package, the Action Plan also defines a comprehensive decarbonisation agenda with legally binding obligations for both ESM and the Government of North Macedonia [REDACTED]. Specifically, the Project's Action Plan also includes:</p> <ul style="list-style-type: none"> • Approval of the revised NECP by the Government by end of 2023, which will include comprehensive targets for decarbonisation, new renewable energy capacity and reduction of greenhouse gas emissions. <ul style="list-style-type: none"> ○ [REDACTED] ESM will construct new renewable energy capacity [REDACTED]. ○ Reduction of net greenhouse gas emissions [REDACTED]. • ESM to develop and adopt a Decarbonisation Strategy aligned with the country's NECP. [REDACTED].
<p>Corporate Governance</p> <p>– Client seeks/makes use of EBRD expertise on corporate governance improvements, including for climate risk management.</p>	<p>ESM to join and implement recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). ESM will develop a road map for disclosure of climate-related information as part of annual ESG or integrated financial reporting. This includes public disclosure and reporting of GHG emissions.</p>
<p>Standard-setting: Gender SMART</p> <p>- Client seeks/makes use of EBRD expertise for the adoption of gender standards and/or equal opportunities action plans</p>	<p>To promote equal opportunities across ESM's operations, gender considerations will be integrated throughout the two training programmes. The curricula will be designed with a gender lens and both the programmes will include [REDACTED] female participants (in a company where the share of female workers is 12 percent).</p>

1.4 SOUND BANKING - KEY RISKS

Risks	Probability / Effect	Comments
<i>Project specific risks</i>		
Counterparty Creditworthiness	Medium/High	<p>The repayment of the loan will rely on the Company's performance and capacity to service its debt. Although ESM historically has had robust financial performance, this has worsened during FY2021-2022 with the energy crisis and led to the liquidity gap.</p> <p><i>Mitigation:</i> ESM is the state-owned electricity generation utility that provides 90% of domestic electricity production, and therefore of great systemic importance. The government of North Macedonia has already provided fiscal policy support of ~EUR 169m during FY2021 and 1H2022, and is expected to continue extending support to ESM as a last resort. [REDACTED]. Additionally, the loan will be sovereign guaranteed by the Republic of North Macedonia.</p>
Guarantor Creditworthiness	Low/High	<p>The Bank will also rely on North Macedonia's creditworthiness, as the government will provide a full sovereign guarantee for the liquidity facility.</p> <p><i>Mitigation:</i> North Macedonia's rating (BB+/BB-) is underpinned by a record of historic coherent macroeconomic and financial policy supporting the longstanding exchange-rate peg to the EUR. Whilst the economy is forecasted to have 3.0% GDP growth rate in 2022, and general government debt levels is low at 46.8% of GDP in Q1 2022. North Macedonia has also access to capital markets and can raise Eurobonds accordingly to face any fiscal shock.</p>
<i>External risks</i>		
Interest rate and currency risk	Low/Low	<p>The repayment capacity of the Borrower could be affected if EURIBOR increases over the term of the loan and/or by adverse movements in the FX rate.</p> <p><i>Mitigation:</i> The Company is cash positive under normal operating circumstances and moderately leveraged with sufficient debt service capacity. The currency in North Macedonia (MKD) is pegged to the EUR and fluctuates against the EUR in a very narrow corridor (between 61.5 and 61.7 MKD per EUR, or 0.3% corridor). The electricity prices are denominated in EUR although paid in MKD. Operating expense items are denominated in MKD.</p>

2. MEASURING / MONITORING SUCCESS

<i>Overall objectives of project</i>	<i>Monitoring benchmarks</i>	<i>Implementation timing</i>
- Good financial and operational performance	[REDACTED]	[REDACTED]
- On-time implementation of the Action Plan		

Primary Quality: Resilient

Obj · No.	Monitoring indicator	Details	Baselin e	Target	Due date	TC	Covena nt
1.1	Improved operational performance of the client	Following disbursement of the Bank's loan, ESM to maintain positive cash position with no further Government cash injections to ESM in 2022.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
1.2	Legal, institutional, or regulatory frameworks in targeted areas improved	Approval by the government of amendments to the Energy Law, [REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Legal, institutional, or regulatory frameworks in targeted areas improved	Change of the electricity supply tariff methodology [REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Legal, institutional, or regulatory frameworks in targeted areas improved	Signing of the Merger agreement between AD GA-MA and AD NER	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Legal, institutional, or regulatory frameworks in targeted areas improved	National Electricity Market Operator (MEMO) contracts service provider for market coupling with Bulgaria.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Legal, institutional, or regulatory frameworks in targeted areas improved	Establishment of working groups for preliminary work on market coupling with Greece.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Secondary Quality: Inclusive

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date	TC	Covenant
2.1	Tailored training programme developed and implemented	In partnership with a specialised national or international college, ESM will introduce two certified training programmes on energy trading and project management.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
2.2	Number of individuals enhancing their skills as a result of training	A relevant number of young employees will be benefiting from the new work-based learning programmes.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Additional Indicators:

Indicator type	Monitoring indicator	Details	Baseline	Target	Due date	Donor	Covenant
Advisory & Policy Indicators	Number of women enhancing their skills as a result of training	Both training programmes will take into account gender considerations throughout and aim to reach [REDACTED] female participants.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Additional Indicators	Legal, institutional or regulatory frameworks in target areas improved	Approval of the revised NECP by the Government, which includes the targets for coal plant decommissioning, RES construction and GHG emission reductions	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Renewable energy capacity installed (MW)	New renewable energy capacity constructed and connected to the grid by ESM, or private partners under a PPP agreement with ESM.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Renewable energy capacity installed (MW)	New renewable energy capacity constructed and connected to the grid by ESM, or private partners under a PPP agreement with ESM.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

	Operational restructuring completed	Decommission of existing coal fired TPP Oslomej	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Operational restructuring completed	Decommission of existing coal fired TPP Bitola	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Recommended policy or strategy or regulatory framework/standard agreed by relevant stakeholder(s)	Decarbonisation Strategy aligned with the NECP developed and adopted by ESM.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Corporate Climate Governance (CCG) improved: reporting, metrics and targets	ESM will join and implement the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). ESM will develop a road map for disclosure of climate-related information as part of annual ESG or integrated financial reporting. This includes public disclosure and reporting of GHG emissions. It is expected that ESM will report TCFD data in corporate reports [REDACTED].	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

3. KEY PARTIES

3.1 BORROWER / INVESTEE COMPANY

ESM is a public electricity generation utility, fully owned by the Government of North Macedonia. The Company provides around 90% of the entire domestic production and had 4,589 employees in 2021. The Company has electricity generation licence valid until 1 November 2040. It also has a heat generation, distribution and supply licence for its Energetika branch. ESM has 4 subsidiaries, one of which is electricity trading company (ESM Trade), another subsidiary owns and operates non-generation assets like hotels and ski centres in the Country (ESM Turs) and the remaining two companies are maintenance companies and produce some equipment and spare parts.

As of December 2021, ESM's total installed capacity was 1,448MW of which 557MW (38%) hydro power plants, 824MW (57%) thermal, 60MW (4%) CHP, and 37MW (3%) wind. The Company has a pipeline of 40MW of solar PV capacity equivalent to 3% of total combined capacity.

The hydro assets comprise of 8 operating hydro power plants (HPPs) with an annual generation of 1,250 GWh. The thermal assets comprise of 2 thermal power plants (TPPs) providing the base load to North Macedonia. TPP Bitola has three blocks, each with 225 MW installed capacity and combined production of 3,600 GWh per year. TPP Oslomej has 125 MW installed capacity, but normally operates less than 20 days per year as all nearby lignite deposits are exhausted.

The Combined Heat and Power (CHP) assets comprise of the existing 30 MW Energetika CHP and 30 MW Kogel CHP (acquired in 2018). The CHP output is c.121 GWh per year. These two CHPs are the main source of heat supply to steel factory in Skopje and the nearby households.

The wind assets comprise 36 MW wind farm in Bogdanci with annual production of about 100 GWh. Extension of this wind farm is planned to be operational by end of 2023 and will add 14 MW installed wind capacity and annual output of 37 GWh. ESM is also considering additional wind farm on a nearby location (Miravci) with 14 MW installed capacity and 40 GWh yearly production. [REDACTED]

3.2 GUARANTOR

The Guarantor is the Republic of North Macedonia, represented by the Ministry of Finance. While relatively modest prior to the Covid-19 outbreak (48 per cent of GDP in 2019), the country's public debt increased to an estimated 62 per cent of GDP in 2021 on the back of economic contraction coupled with rising fiscal³ bill to support the economy during the pandemic. Although public debt is still expected to rise and peak at 63 per cent of GDP in 2023, the IMF assessed that the composition of public debt is improving as the average maturity of domestic government securities is increasing and interest payments remain contained (*IMF Country report, February 2022*). Subsequently, the IMF valued the public debt sustainable in February, given no further significant shocks.

In 2021, the country started recovering from the impacts of the Covid-19 pandemic, with a 4 per cent activity expansion driven by both domestic and external demand and a GDP which should be higher than that of 2019. The main risks and uncertainties now come from the war in Ukraine. Although North Macedonia has limited exposure to Russia or Ukraine in terms of direct economic links, the country is impacted through rising commodity prices which have led to an increased fiscal spending above what was initially planned. In addition to ongoing expenditures to uphold the energy sector and maintain subsidised electricity prices for households, authorities adopted a package of measures in the amount of EUR 400 million in March 2022 to protect households from rising food and energy prices and to help firms maintain liquidity. This will derail fiscal consolidation plans as the deficit will surpass the earlier projected 4.3 per cent of GDP in 2022. The authorities [REDACTED] issued a six-year EUR 700 million Eurobond in May 2020 and a seven-year EUR 700 million Eurobond in March 2021 to foster the recovery from the pandemic. The new organic budget law envisaging adoption of a set of fiscal rules (similar to the Eurozone's Maastricht criteria) and the establishment of an independent fiscal council is not yet adopted by the Parliament. In 2022, North Macedonia is rated at BB- (Stable) by S&P and BB+ (Negative) by Fitch.

4. MARKET CONTEXT

North Macedonia is a net importer and domestic electricity is produced almost entirely from ESM's power plants. Electricity imports amount to approximately 30% of the total domestic electricity consumption and are mostly required to meet peak winter demand. The Macedonian electricity system has interconnection with the electricity systems of Serbia, Greece, Kosovo and Bulgaria (DTM 27768). Construction of the interconnection with Albania has started in Q3 2021 (DTM 46274). As a result of

³ It is important to emphasise that General Government Debt levels remain below the level of 60% generally considered problematic. As of Jan 2022: c. 49% of GDP.

these interconnections, the regional grid is expected to be more readily able to accommodate increasing RES penetration.

The country has made considerable progress towards meeting its Energy Community Treaty obligations and in liberalising its energy sector. Generation, transmission and distribution are fully separated. Transmission is owned and operated by Makedonski Elektroprenosen Sistem (MEPSO), an existing EBRD client (DTM 44114 and 46274). The new Energy Law was adopted in May 2018 and fully, unbundled, liberalized the market and incorporated the Third Energy Package. The new law has put in place the legal framework to support competition in electricity supply and generation and ERC sets the tariffs only for transmission and distribution. New amendments to the Energy Law are expected to be introduced for regulation for wholesale energy market integrity and transparency (REMIT), capacity allocation and congestion management (CACM), and cybersecurity provisions.

The Ministry of Economy (“MoE”) is assigned primary responsibility over the energy sector in the Country. The Deputy Prime Minister for economic affairs is responsible for the overall energy strategy and is closely overseeing all public investments in the energy sector.

North Macedonia currently has multiple small private PV plants (less than 3 MWac) with 24MWac of installed capacity benefiting from feed-in-tariff (FiT) and 21MWac on the market. The 10MW Oslomej PV plant financed by the Bank (50415) is the first utility size plant of this kind in the country not rely on the FiT regime. The bank has also supported the design and implementation of the first competitive auction tenders under feed-in-premium (FiP) for 35MWac private solar PV plants on state-owned land and 27 MWac on private land were concluded at the beginning of 2020 (contracts signed). In April 2021, ESM announced the results of its PPP tender, also supported by the EBRD, for a fully merchant 100 MWac solar PV plant at Oslomej mine site. In addition, a 17MWac project won by Slovenian GEN-I, the largest capacity awarded to a single investor without FiP, under the first competitive auction tender supported by the Bank, is expected to come online in early 2023.

The country has a single operational 36.8 MW wind power plant Bogdanci owned by ESM which benefits from the FiT. A tender for an additional 14 MW of capacity on the same location was relaunched by ESM in August 2020, while the first two private windfarms investment are in development stage.

North Macedonia published Strategy for Energy Development until 2040, adopted the enhanced National Determined Contributions (“NDC”) and the Long Term Strategy, which outline the overall energy sector decarbonisation, modernisation and transformation in line with EU energy trends. The National Energy and Climate Plan (“NECP”) was adopted on 31 May 2022, and envisages a 82% net reduction of GHG by 2030 to be achieved through the gradual decommissioning of the country’s TPP fleet by the end of 2027 whilst simultaneously by adding 2.2GW (incl. hydropower) to the energy mix by 2040.

The 10MWac PV plant of ESM under construction alongside this operation for an additional solar capacity of 30MWac aim to minimise the gap to the RES target and are in line with the decarbonisation strategy of the Country. Overall, ESM’s long-term investment plans envisage the addition of 210MW of RES capacity by 2025.

5. FINANCIAL / ECONOMIC ANALYSIS

5.1 FINANCIAL PROJECTIONS

[REDACTED]

5.2 SENSITIVITY ANALYSIS

[REDACTED]

5.3 PROJECTED PROFITABILITY FOR THE BANK

[REDACTED]

6. OTHER KEY CONSIDERATIONS

6.1 ENVIRONMENT

Category B (2019 ESP). The provision of the liquidity finance will be used as working capital to finance salaries, electricity purchases (imports), debt service and other administrative costs of the client and is not associated with any environmental or social risks or impacts. The company JSC “Elektrani na Severna Makedonija” (ESM) is an existing client of the Bank with good performance record and has proven their ability to comply with the Bank’s requirements during on-going projects under OpID 50415. The Environmental and social due diligence (ESDD) was undertaken in-house by ESD and included the review of environmental and social (E&S) Questionnaires, follow up interviews with the Company’s EHS representatives, review of supporting EHS documentation, review of ESAP progress status, and review of AESR developed under the existing transaction. The Company operates in line with national requirements and has been certified with internationally recognised ISO standards for quality management (9001), environmental management (14001) and occupational health and safety (45001) and has EHS management systems, policies, and operational procedures in place, and is additionally using external resources wherever needed (i.e. for EHS auditing and monitoring of emissions).

Based on the ESDD an ESAP has been developed to structure the corporate EHS management to meet EBRD E&S Policy and Performance requirements. Under PR1, the ESAP stipulates the measures to: (i) maintain and improve existing EHS management system, (ii) undertake ESG and climate related information (i.e. TCFD) reporting in line with the EU Corporate Sustainability Reporting Directive and publishing, and (iii) include gender based violence and harassment (GBVH) awareness raising and prevention into regular EHS training of staff. Issues related to GBVH will be assessed more explicitly in a revision of the Company’s anti-harassment policy, as stipulated by ESAP.

The company has satisfactory HR practices that are aligned with national Law on Labour Relations, as well as a Collective Agreement and a formal grievance mechanism. The Company operates in line with national requirements, which are in line with core ILO conventions and forced labour and child labour are prohibited by local legislation. The Company policy on Objections, Requirements and Complaints is in place for capturing worker complaints. The Company adheres to existing Rules on General Procurement Procedure, however, this procedure will need to be updated to consider supply chain risks, including and explicitly those related to the supplier of solar panels. The ESAP stipulates that, in the case of any future solar projects, the client should inform the contractor or supplier of solar components of the requirement to select products from the [Green Technology Selector](#) (GTS), which is in line with requirements of the PR2 and EBRD’s Management approach for solar.

The waste management practices are regulated by existing waste management programme documents at the level of the two subsidiary companies that are generating the largest quantities of waste, thermal power plants Bitola and Oslomej, and the ESAP stipulates development of the comprehensive Waste Management Plan at the corporate level, targeting both ESM and other subsidiary companies that do not have WMP in place. At TPPs Bitola and Oslomej the Company undertakes continuous monitoring of air emissions which showed occasional exceedances of SO₂ and particulate matter above the limit values. The ESAP includes the measure to develop plan of corrective actions to suggest measures to reduce air emissions in case of exceedances of the limit values. An ambitious decarbonisation Action Plan has been developed in line with national strategy for decarbonisation to align the Project with Paris agreement criterion for mitigation, including decommissioning of the thermal PPs and increase of the electricity produced from renewable energy sources.

The OHS related issues are covered as part of the existing comprehensive OHS management system. The Company is undertaking regular internal and external monitoring of H&S risks and trainings, periodical internal and external examinations of H&S equipment; and has reported adequate response to COVID-19. Specific focal points will be assigned and trained to increase awareness of the issue and to ensure that any allegation or grievances related to gender based violence are handled in an

appropriate manner. The Project does not include any new infrastructure. Therefore, there is no associated risks or impacts related to land acquisition, biodiversity or cultural heritage. A corporate level Stakeholder Engagement Plan (SEP) is to be developed to describe the high level requirements and procedures related to information disclosure at each facility. The SEP will also establish a formal external grievance mechanism that will be consistent across all facilities. The Bank will monitor the implementation of the Project through review of annual reports and site visits when deemed necessary.

The Project is considered aligned with the objectives of the Paris Agreement for adaptation. The Project is also considered aligned with the mitigation objectives of the Paris Agreement based on the commitment for the development and adoption of corporate decarbonisation strategy by ESM, with time bound actions for coal phase out, increased renewable energy capacity, decarbonisation ambition aligned with the NECP and MRV provisions.

6.2 INTEGRITY

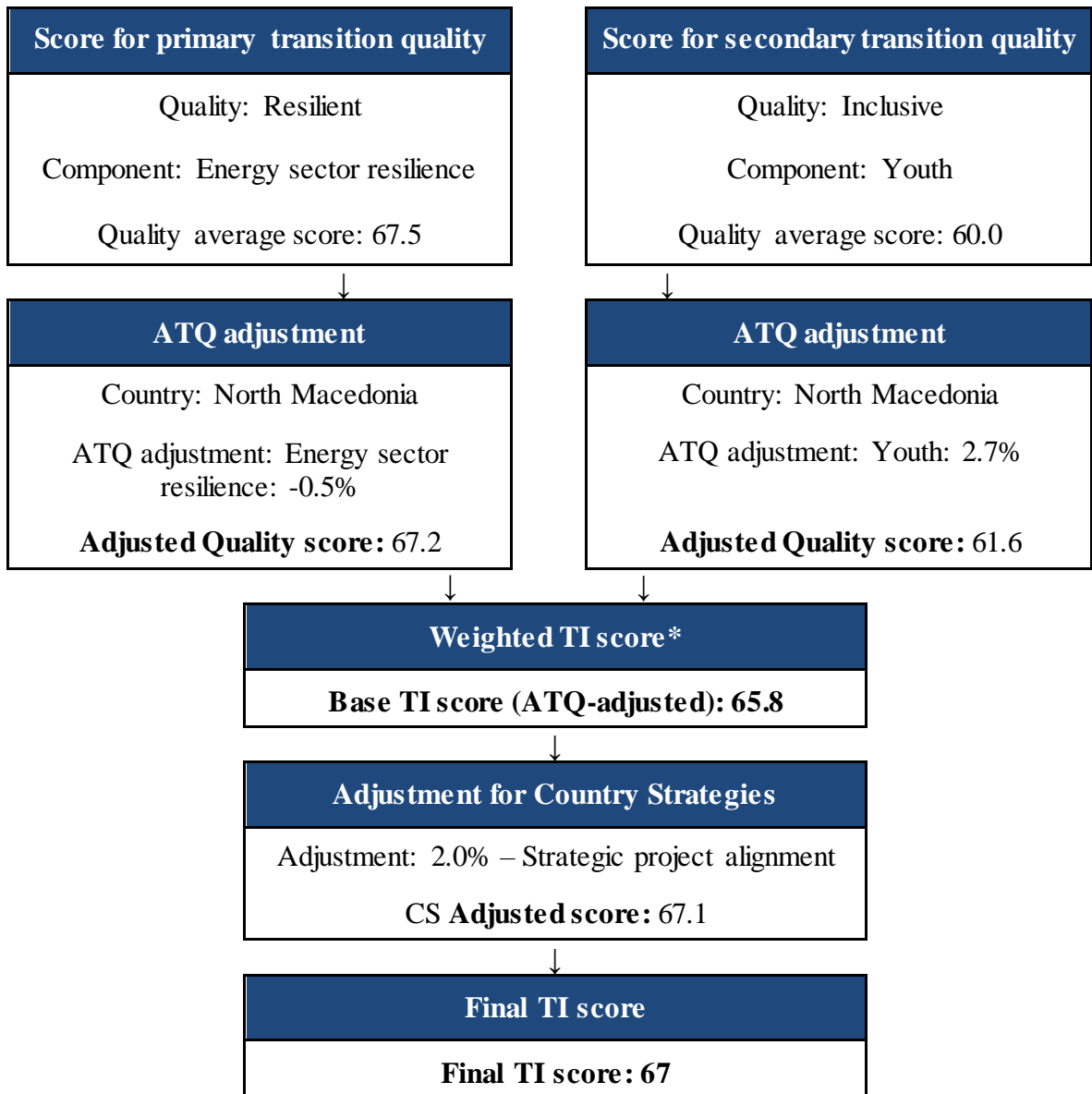
In conjunction with OCCO, integrity due diligence was undertaken on the Company, its senior management, and other relevant parties. The review identified no new material integrity issues since the previous projects involving the same client [REDACTED] and it has therefore been concluded that this Project does not present unacceptable integrity or reputational risks 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

#	Name
ANNEX 1	Transition impact scoring chart
ANNEX 2	Shareholding and organisation structure
ANNEX 3	ESM Action Plan
ANNEX 4	Green Assessment
ANNEX 5	Historical Financials
ANNEX 6	Project Implementation

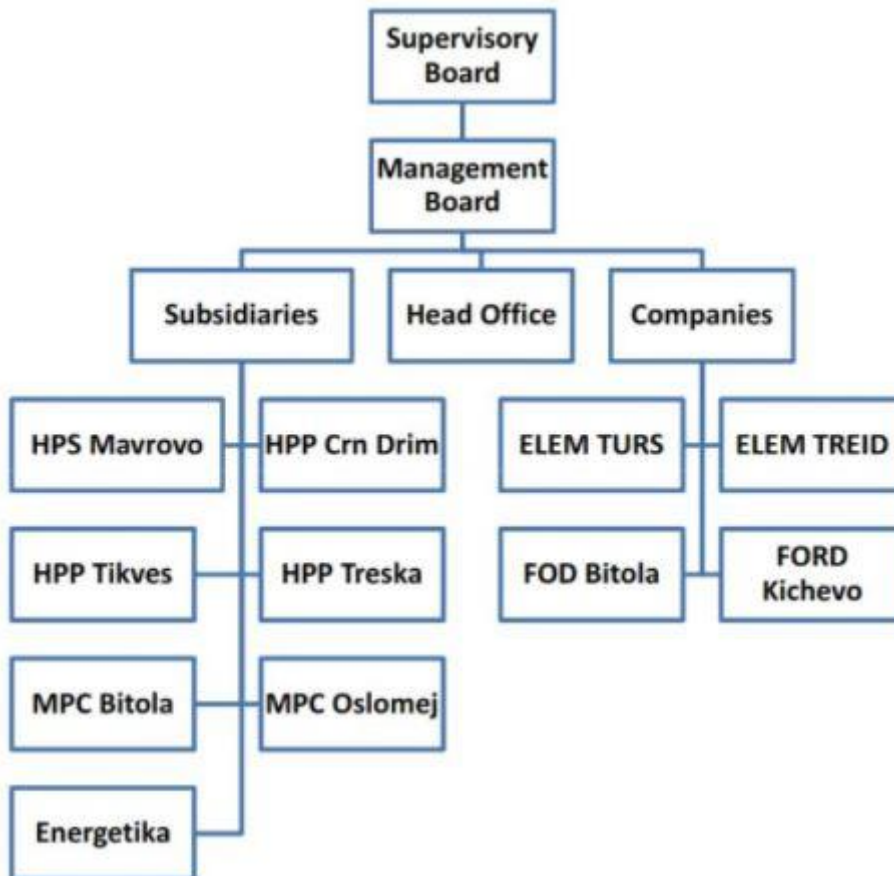
ANNEX 1- TRANSITION IMPACT SCORING CHART



*The Primary Quality score is weighted 75% for the calculation of the Base TI Score. The Secondary Quality is weighted 25%.

ANNEX 2 – SHAREHOLDING AND ORGANISATION STRUCTURE

ESM is 100% owned by the Government of North Macedonia. Below is the organization structure



ANNEX 3 – ESM ACTION PLAN

[REDACTED]

ANNEX 4 – GREEN ASSESSMENT

Paris alignment assessment:

The transaction is Paris Aligned: The project is considered aligned with the mitigation objectives of the Paris Agreement based on the commitment for the development and adoption of corporate decarbonisation strategy by ESM, with time bound actions for coal phase out, increased renewable energy capacity, decarbonisation ambition aligned with the NECP and MRV provisions. The transaction does not invest in physical assets (capex), is consistent with the NDC and does not have carbon lock in risk.

This transaction is consistent with the Energy Sector Strategy (Fossil Fuels) approach of the EBRD (2021). Where the Bank provides finance that is not related to specific capital expenditures to a company with significant fossil fuel assets operating in the energy sector, it will only do so on the condition that the company has in place, or is committed to adopting, high climate governance standards and operates in a regulatory or corporate context which embeds strong commitments to decarbonisation.

The Government will enact policy that facilitates renewables both by ESM and private investors including:

- NDC targets of a net reduction of net greenhouse gas emissions by 82% by 2030. A revised NECP will be developed and approved by the Government [REDACTED].
- Facilitates the development and connection to the grid of new renewable capacity (including hydro) by private investors of 1,500 MW by end of 2030 (this is aligned with the planned 2,200 MW total new renewable energy capacity to be connected to the grid by 2040).

ESM will play a key role in the decarbonisation process in North Macedonia by ensuring that:

- Decommissioning all coal-fired TPP capacity by the end of 2027 in line with NDC. Existing coal fired TPP Oslomej (end of 2023) and TPP Bitola (phase-out by end of 2027) will be replaced by RES capacity (independently or under PPP) by the end of 2025.
- Stops any coal mining operations in related coalmines or further coal exploration, in line with Action Plan for TPP decommissioning.
- Adopting a corporate decarbonisation strategy with binding actions and reporting requirements including specific targets, investment plan and Climate Corporate Governance benchmarking.
- Developing an implement the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).
- Delivering 210 MW of renewable energy capacity [REDACTED].

General screening of alignment with the mitigation goals of Paris Agreement

- The project/economic activity is **not included** in the 'aligned list'.
- Regarding project/economic activity(ies), there are **no** activities included in the 'non-aligned list'.
- Applicable additional or specific conditions associated with the 'aligned' project/economic activity **have** been met.

Specific assessments undertaken

- NDC (Nationally Determined Contributions) reviewed: The enhanced NDC targets of a net reduction of net greenhouse gas emissions by 82% by 2030 and has dates for expected coal phase out (by 2027) aligned with this transaction. A revised NECP will be developed and approved by the Government [REDACTED]. The draft NECP anticipates 2,200 MW total new renewable energy capacity to be connected to the grid by 2040 – NECP Green scenario.
- Low carbon pathway: the company will develop and adopt a decarbonisation strategy and is committed to coal phase out by 2027. These requirements are in the Action Plan attached to this transaction which includes:

- Decommissioning all coal-fired TPP capacity by the end of 2027 in line with NDC. Existing coal fired TPP Oslomej (end of 2023) and TPP Bitola (phase-out by end of 2027) will be replaced by RES capacity (independently or under PPP).
 - Delivering 210 MW of renewable energy capacity [REDACTED].
 - Stops any coal mining operations in related coalmines or further coal exploration, in line with Action Plan for TPP decommissioning.
 - Adopting a corporate decarbonisation strategy with binding actions and reporting requirements including specific targets, investment plan and Climate Corporate Governance benchmarking.
 - Developing an implement the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).
- Carbon lock-in: the transaction does not invest in capex and therefore has limited lock in risk. The use of the liquidity finance is further ring-fenced away from fossil fuels using a special audited account.
 - Economic assessment: N/A

Alignment with the adaptation goals of Paris Agreement

The Project is considered aligned with the objectives of the Paris Agreement as potential climate hazards have been determined to be non-material. Physical climate risk assessment is not applicable to sovereign CARTs.

GET attribution:

There is no GET attribution given the nature of the transaction.

Climate-related financial risk

N/A. The Bank's counterparty in this case is the Republic of North Macedonia, not ESM due to the guarantee. There is no need for either a CT or PC score. Sovereigns are currently not in scope for screening.

ANNEX 5 – HISTORICAL FINANCIALS

[REDACTED]

ANNEX 6 - PROJECT IMPLEMENTATION

Procurement classification – *Public sub-sovereign*

Project risk assessment:

[REDACTED]. This is the third EBRD financed project with Elektrani na Severna Makedonija (ESM). Although this project includes Procurement of Commodities, ESM has earlier proven experience in procuring contracts in line with EBRD's Procurement Policies and Rules (PPR) including the use of ECEPP.

By applying PPAD's capacity assessment toolkit the client's risk on procurement has been assessed as *Low*. All categories i.e. legal framework, organisation of procurement function, support/control systems, staffing, record keeping, procurement planning, procurement cycle, general assessment of the client, and project risk have been assessed.

Contracts risk assessment

Low

Project implementation arrangements:

The EBRD loan proceeds will be used for working capital including electricity purchases and repayment of debt. As agreed with the Client, the project will be subject to the 2022 version of the Bank's PPR which explicitly excludes operating expenses (excluding commodities) from the policy under article 2.6 (d). The purchase of electricity is seen as procurement of commodities in accordance with the provisions set out in the new PP&R, paragraphs 3.25 and 3.57 i.e. Special Competitive Procedures. As electricity purchase is a common and regular task of ESM there are established procurement arrangements in place as described in below.

Procurement Requirements to be met when applying Special Competitive Procedures

(a) The Bank Operation involves multiple contract awards for partial quantities of Commodities;

ESM operates a framework contract with 24 licensed trading companies which are qualified and competent to sell electricity to ESM. The electricity is further sold from ESM to the universal supplier and eventually supplied to the households. The selected bidders sign sales and purchase contracts with ESM. These are multiple small-size contracts (commonly less than EUR 1 Mln) with a predefined amount of electricity to be provided including standard terms of contracts. The volume of electricity in the contracts vary and so is the timing, for instance the majority of these contracts are implemented during a nos. of days and hence are not long term contract obligations.

(b) This is the most economic and efficient approach to benefit from favourable conditions in the spot market;

The procurement process is seen as the most economic and efficient approach as (i) it provides for an open call for electricity purchase published on ESM website providing an opportunity for the licensed companies to place a bid, and (ii) the company offering the lowest price for the electricity to be provided is offered to sign the Contract. This process is repeated until the

amount of electricity in MWh has been fulfilled. The contract award is published and available on ESM website.

(c) This is necessary to secure a timely supply of Commodities.

This requirement is met as ESM is able to timely award the contracts to the licensed companies which in turn is able to promptly supply the households through the Universal supplier with the required volume of electricity. [REDACTED].

In addition, the Bank's right to audit/prohibited practice provisions will be addressed via an External Auditor to be appointed in the project. The Auditor has the obligation to review the use of loan proceeds including provisions of prohibited practices. [REDACTED].

In the event that the loan proceeds are used for the purposes of retroactive financing, the provisions of article 3.77 – Retroactive Financing will be applied.