DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT

Approved by the Board of Directors on 8 February 2023[1]

SERBIA

EPS 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

AERS	Energy Agency of the Republic of Serbia
CFADS	Cash Flows Available for Debt Service
CFF	Cash Flow from Financing
CFI	Cash Flow from Investments
CFO	Cash Flow from Operations
CO2eq	Carbon dioxide equivalent
CP	Conditions Precedent
CPI	Consumer Prices Index
EBITDA	Earnings Before Interest, Taxes, Depreciation, and Amortization
EIA	Environmental. Impact Assessment
EPS	Javno preduzeće Elektroprivreda Srbije Beograd
ESAP	Environmental and Social Action Plan
ESDD	Environmental and Social Due Diligence
EURIBOR	Euro Interbank Offered Rate
GHG	Greenhouse Gas
GW	Gigawatts
GWh	Gigawatt hours
HPP	Hydro Power Plant
KPI	Key Performance Indicator
NECP	National Energy and Climate Plan
RSD	Serbian Dinar
TC	Technical Cooperation
TPP	Thermal Power Plant
WPP	Wind Power Plant

CURRENCY EQUIVALENTS

Country's Currency Unit 1 Euro =117.3 Serbian Dinar (as at 13 Dec 2022)

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)

PRESIDENT'S RECOMMENDATION

This recommendation and the attached Report concerning an operation in favour of Javno preduzeće Elektroprivreda Srbije Beograd ("EPS," the "Borrower" or the "Company"), the wholly state-owned electricity utility of Serbia, active in the production and supply of electricity, are submitted for consideration by the Board of Directors. The facilities, in the total amount of up to EUR 300 million, will consist of two tranches to the Company in the amounts of EUR 200 million and EUR 100 million. Both tranches will be guaranteed by the Republic of Serbia.

The operation will provide emergency liquidity support to EPS and will result in maintaining the Company's financial stability and maintaining Serbia's critical energy infrastructure in the midst of global energy crisis as result of COVID-19 and further exacerbated by the war on Ukraine and the accumulated effects of past and on-going supply chain disruptions due to COVID-19. The operation will include a robust Action Plan targeting commitments from the Company and the Republic of Serbia in relation to the energy sector decarbonisation agenda, corporate reforms and regulatory context. The loan will be ring-fenced away from any fossil fuel operations and will be used to finance electricity imports, make payment to domestic renewable energy producers, pay for eligible operational expenses, or repay short-term commercial loans falling due.

The Project targets the Resilient and Inclusive transition qualities. The Project will help meet a critical liquidity gap at the Company, therefore increasing energy security and facilitating the Company's longer-term capital investment plans especially in the field of green transition. It also includes ambitious policy dialogue and reform commitments targeting improvements on the corporate level with broader systemic impact (*Resilient TI*). The operation will address the inequality implications of the decarbonisation on human capital thus contributing to a 'just' transition to green energy by helping the 'greening' of national skills systems and defining redeployment and reskilling gaps and opportunities for affected workers (*Inclusive TI*). EPS will also support gender equality by increasing the share of women in top managerial positions and improving the gender-responsiveness of its Human Resources policies and practices (Gender SMART).

TC support for this operation will be provided by donors and/or Shareholder Special Fund and will include: i) de-carbonization strategy and action plan EUR 350,000, ii) implementation of climate risk reporting in accordance with recommendations of the Task Force on Climate-related Financial Disclosures EUR 75,000; iii) EUR 500,000 to help the Borrower design a Corporate Development Programme in line with the reforms commitment and iv) EUR 200,000 to support to address their human capital challenges.

I am satisfied that the operation is consistent with the Bank's Strategy for Serbia, the Energy Sector Strategy, the Green Economy Transition approach, the Equality of Opportunity Strategy 2021-2025, the Strategy for the Promotion of Gender Equality: Promoting human capital development and gender mainstreaming, 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

SERBIA – EPS LIQUIDITY SUPPORT – DTM 54039	
Transaction / Board Decision	Board approval[2] is sought for a sovereign guaranteed loan of up to EUR 300 million to Javno preduzeće Elektroprivreda Srbije Beograd ("EPS," or the "Company"), a corporation registered in Serbia. The loan will provide emergency liquidity support to the Company in order to maintain its financial resilience, enhance energy security for Serbia, and drive the country's decarbonisation agenda. Loan proceeds will be used for liquidity needs and the repayment of maturing commercial loans and will be entirely ring-fenced away from any fossil fuel assets or operations of EPS.
Client	EPS, an existing Bank client, is a vertically integrated power utility 100% owned by the Republic of Serbia. EPS operations consist of the generation and supply of electricity (following a corporate restructuring to spin off its distribution assets in December 2020). The Company usually provides around 95% of the entire domestic production. Average annual production is about 21,537 GWh from the TPPs (installed capacity of 4,079 MW), 630 GWh from the CHPPs (installed capacity 297 MW), and 11,667 GWh from the HPPs (installed capacity 3,015 MW). EPS employs c. 24 thousand people. As of year-end 2021, EPS reported assets of EUR 8,164m, revenues of EUR 2,607m, and EBITDA of EUR 202m.
Main Elements of the Proposal	<u>Transition impact</u>: **1. Resilient -** the Project will improve energy security by allowing the Company to (1) finance critical electricity imports required to keep the electricity market functioning; (2) make payment to renewable energy producers within Serbia under the Feed-in-Tariff system; (3) pay for eligible operating expenses, (4) repay maturing short-term loans. It also includes key reforms on the corporate level with broader systemic impact for energy security and system resilience. **2. Inclusive** – As part of a focus on 'just' transition to green energy, the Project will address the inequality implications of the decarbonisation on human capital by supporting EPS in: i) engaging with the Ministry of Education for 'greening' national skills systems; and ii) creating and implementing strategic workforce management activities by defining redeployment and reskilling gaps and opportunities for affected workers to move within the company or the wider regional and national labour market, in cooperation with relevant authorities. <u>Additionality</u>: **Standard-setting:** EPS will be supported in improving its gender diversity practices and standards by developing an Equal Opportunities Action Plan and increasing the share of women in top management positions. <u>Sound banking:</u> The transaction is a loan guaranteed by the Republic of Serbia, rated BB+ (Stable) by S&P in June 2022 and BB+ (Stable) by Fitch affirmed in August 2022.
Key Risks	<u>Counterparty risk:</u> The Company is currently suffering a liquidity crisis, and its creditworthiness and ability to make debt service out of operational cash flows is questionable. *Mitigant*: the Loan will benefit from a sovereign guarantee. <u>Guarantor risk</u>: the transaction depends significantly on the creditworthiness of the Guarantor to mitigate credit risk. *Mitigant*: the debt capacity of the Republic of Serbia has recently improved, with current sovereign ratings of BB+ stable (improved from BB (stable)) / Ba2 stable (improved from Ba3) / BB+ (improved from BB (stable)) from S&P, Moody's and Fitch, respectively.
Strategic Fit Summary	The Project is aligned with the Bank's Strategy for Serbia, which states that "*the Bank will aim to continue to play a key role in promoting energy efficiency and renewable energy, while assisting with replacing the aging electricity generation capacity and bringing power generation into compliance with the EU environmental standards.*" It is also consistent with the Energy Sector Strategy, the Green Economy Transition approach, the Equality of Opportunity Strategy 2021-2025 and the Strategy for the Promotion of Gender Equality: Promoting human capital development and gender mainstreaming.

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

ADDITIONAL SUMMARY TERMS FACTSHEET

EBRD Transaction	EUR 300 million sovereign guaranteed loan will be used to meet critical liquidity needs, including (i) paying for electricity imports to meet critical demand and ensure system stability; (ii) purchasing renewable energy from domestic producers operating under the Serbian feed-in-tariff support scheme; (iii) meeting eligible operating expenses (ring fenced from any coal-related assets); and (iv) repaying short-term debt coming due from local commercial banks. The loan will be split into Tranche I (EUR 200 million) and Tranche II (EUR 100 million) [REDACTED].
Existing Exposure	Direct Exposure: EUR 130.9 million **DTM / Signed / Amount / Operating / Description** 41923 / 2011 / EUR 79 / [REDACTED] / Kolubara mining basin and power plan efficiency upgrades 42421 / 2011 / EUR 33 / [REDACTED] / EPS Hydropower Plants 47318 / 2015 / EUR 200 / [REDACTED] / EPS Restructuring loan Sovereign Exposure: Sovereign portfolio: EUR 902 million Sovereign operating assets: [REDACTED].
Maturity / Repayment	Term loan: Tenor of up to 5 years [REDACTED].
AMI eligible financing	n/a
Use of Proceeds	Disbursements of the Loan will be used for (i) paying for electricity imports to meet critical demand and ensure system stability; (ii) purchasing renewable energy from domestic producers operating under the Serbian feed-in-tariff support scheme; (iii) meeting eligible operating expenses (ring fenced from any coal-related assets); and (iv) repaying short-term debt from local commercial banks. See section 6.3 on ring fencing of use of proceeds.
Investment Plan	n/a
Financing Plan	[REDACTED]
Key Parties Involved	• Javno preduzeće "Elektroprivreda Srbije" Beograd (Borrower) • The Republic of Serbia (Guarantor)
Conditions to disbursement	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 with the Eligible Expenditure definition in the Loan Agreement. Additional CPs to Tranche 1: • Government of Serbia to announce coal exit date no later than 2050; • Regulatory framework to allow renewable energy auctions to be adopted; • At least 1,000 MW of wind quotas to be announced for upcoming 3 years; • Initial 400 MW wind auction to be launched; • EPS to commit to implement TCFD reporting standards from 2024; • EPS to agree the TOR for a decarbonisation strategy and action plan; • EPS to agree the TOR for a corporate development programme; • EPS to begin work on agreed gender and economic inclusion activities. Additional CPs to Tranche 2:

	• Government to adopt a National Energy and Climate Plan (NECP) committing to increase the share of renewables in the generation mix from 30% to 45% by 2030; • Government of the Republic of Serbia to define thermal power plant decommissioning milestones by 2030; • At least 50% of the initial 400 MW wind auction to be awarded.
Key Covenants	[REDACTED]
Security	Sovereign guaranteed – Republic of Serbia (Fitch: BB+/S&P: BB+).
Technical Cooperation (TC)	Technical cooperation ("**TC**") to be made available by the EBRD to assist the Borrower in project implementation to be completed by 31 December 2025. Donor fund raising is ongoing and TC activities will be either funded by an international donor or the SSF. Activities include: 1. TC will be mobilized in the estimated amount of EUR [350,000] to support the Borrower with preparation of a Paris-aligned **de-carbonization strategy and action plan**, aligned with the **National Energy and Climate Plan** ("**NECP**") and other strategic documents, that would ensure security of supply and facilitate green energy sector transition, including no new coal; 2. TC will be mobilized in the estimated amount of EUR [75,000] to help EPS with the implementation of climate risk reporting in accordance with recommendations of the **Task Force on Climate- related Financial Disclosures** ("**TCFD**"), meeting disclosure requirements initially focusing on qualitative aspects related to governance, strategy, and climate-related risk management, with incorporation of quantitative aspects of climate-related financial risks and opportunities; and 3. TC will be mobilized in the estimated amount of EUR [500,000] to help the Borrower design a **Corporate Development Programme** in line with the reforms commitment. 4. TC will be mobilized in the estimated amount of EUR [200,000] to support the client address their human capital challenges: in Serbia through the engagement with the Ministry of Mining and Energy and Ministry of Education for 'greening' national skills systems for the energy sector by contributing to the development of the National Action Plan; and in the company itself through the development of a **Strategic workforce management assessment and action plan**, reflecting both the Company's decarbonisation action plan; EBRD's **Just Transition Diagnostic and Action Plan** and regional economic development planning processes. The TC will also support the development of training programmes to address the up-skilling and re-skilling needs of the workforce, as well as the challenge of attracting high-skilled talent and promoting equal opportunities for women.

[REDACTED]

INVESTMENT PROPOSAL SUMMARY

1. STRATEGIC FIT AND KEY ISSUES

1.1 STRATEGIC CONTEXT

Having only recently achieved a partial recovery from the impacts of the COVID-19 pandemic, the Serbian energy sector has been significantly impacted by the unprecedented surge in electricity prices caused by Russia's war on Ukraine. Serbia's state-owned electricity generation company, EPS, is currently experiencing an unprecedented liquidity squeeze due to a 'perfect storm' of internal and external crises. It has been simultaneously affected by multiple serious issues, including problems with TPP operations, shortages of quality coal, poor hydrology, in addition to a large discrepancy between sales and purchase price of electricity which it had to import at a higher level than expected. The proposed loan addresses this emergency liquidity needs, providing support to EPS to retain a healthy liquidity position amid operational difficulties, limited tariffs, and the spike in electricity import prices.

While EPS' immediate liquidity needs and near-term problems are significant, its medium- and long-term challenges are even larger. The Company faces major challenges transitioning away from its existing reliance on legacy lignite-fired infrastructure for power generation. Over the past years, the share of renewable energy in gross final electricity consumption has remained below 30%, with less than 3% of production generated by intermittent wind and solar which well below the 38% target for 2030 established in the National Renewable Energy Action Plan (NREAP).

This liquidity crisis may impact EPS's ability to meet its fundamental obligations and provide electricity to the population if it is unable to pay staff and suppliers (including RES producers under the feed-in-tariff). It will also undermine EPS's ability to continue its decarbonisation path, delaying the roll-out of its renewable energy investment programme including the Morava and Kolubara PV projects, the Kostolac wind farm, and the significant HPP rehabilitation project to be implemented including at Vlasinske HPP. Hydro rehabilitation projects are particularly important due to their potential to increase EPS's balancing capacity, allowing the national grid to absorb additional quantities of intermittent renewable energy.

The Project will support decarbonisation of Serbia's energy sector through holistic approach at national and corporate levels in line with the commitments under the Paris Agreement, while accounting for energy crisis context. Serbia has adopted its enhanced National Determined Contributions (NDC) with a net greenhouse gas emissions reduction target of 33.3% by 2030 compared to 1990. As part of the transaction, the Government will further commit to adoption of the first National Energy and Climate Plan (NECP) by end 2023 and to announcing coal phase out date as soon as possible and before 2050 for the first time. The advanced draft NECP 2030 targets include: (1) emission reduction of 40.4% compared to 1990, (2) net 25% decommissioning (1GW) of coal-fired capacity, (3) circa 4GW of new intermittent RES capacity (from current 400MW). The transaction will also facilitate adoption of regulatory framework, lead to announcement of over 1,000MW RE capacity to be auctioned, and enable the launch Serbia's first renewable energy auction with the help of EBRD's parallel policy engagement, including on development of RES law.

At the company level, EPS will commit to: (a) developing credible Paris-aligned decarbonisation and action plan, aligned with NECP [REDACTED], (b) enhancing Corporate Climate Governance by implementing recommendations from the Task Force on Climate-related Financial Disclosures (TCFD) [REDACTED], including integrating climate change considerations into corporate practices. The transaction is determined as Paris Aligned and is consistent with the Bank's Fossil Fuels approach (2021), subject to implementation of the ambitious action plan. The project is consistent with NDC and has low risk of lock-in, as it does not entail any capital expenditures or investments in physical assets. The use of proceeds will be ring-fenced away from any fossil fuel operations including salaries payable to workers in mining or coal-related business units. At the counterparty level, the commitments of EPS and the Government of Serbia demonstrate the alignment of financial flows with the Paris Agreement for mitigation, in spite of EPS's current involvement in coal mining and generation. The Project is aligned with adaptation goals due to absence of capex, and at the counterparty level as well via actions to address flooding and hydrological variability risks in the ESAP (for large HPPs) and as part of Corporate Climate Governance. Furthermore, reduced reliance on coal as part of decarbonisation targets will lower physical climate risks to mines and power plants.

The Project will be implemented within the context of the Bank's multi-layer involvement on energy sector transition in Serbia, and will be part of a broader holistic engagement covering policy development, institutional capacity building, and support for green and resilient investments. The Bank has been actively supporting the development of renewable energy projects and engaging in policy dialogue starting from 2020, supporting the implementation of a regulatory scheme to support private sector auctions for renewable energy and advising on broader renewable energy mechanism. The Bank's leadership in this space has been recognized by other IFIs, and EBRD is closely working together with the IMF, EU, and World Bank on energy sector loan conditionalities and policy reforms. This has been especially recognized in the current Project, where the German development bank KfW shares EBRD's desire to promote private sector renewable auctions and intends to provide a follow-on EUR 100-200 million loan to EPS on identical terms as negotiated by EBRD alongside the Bank.

Within the broader sector, the Bank has been engaged on providing support to Serbia to improve its regulatory environment and remove barriers for investments in energy efficiency. Under flagship REEP/REEP Plus projects, it has supported the development of legislation governing energy efficiency and the energy performance of buildings, effectively stimulating energy efficiency investments and supporting achievement of national sustainable targets. It has responded to the need to decarbonize the friable and fossil fuel dependent district heating sector to achieve energy savings and reduction of air pollution [REDACTED]. This will entail innovative technologies such as solar thermal, geothermal, heat pumps and waste heat. Further significant activities are carried out to improve energy efficiency in residential and public sector. [REDACTED]. The EBRD is also supporting the Ministry of Mining and Energy and EPS in development of a comprehensive Just Transition Diagnostic and Action Plan to address the effects of decarbonisation on coal-reliant communities and workers and enable them to benefit from green economy opportunities. The transaction will therefore directly support the identification of opportunities and re-skilling of affected workers.

Within the context of this transaction, TC support will be provided for the development of (i) a decarbonisation plan for EPS in accordance with Serbia's National Energy and Climate Plan ("NECP"), (ii) climate risk reporting in accordance with recommendations of the Task Force on Climate- related Financial Disclosures ("TCFD"), (iii) Corporate Development Programme and (iv) a strategic workforce management assessment and action plan to define redeployment and reskilling gaps and opportunities and training for [REDACTED] affected workers within the company as well as in the wider regional and national labour market in cooperation with the authorities of the affected municipalities, the Ministry of Labour, the National Employment Service (NES), its local employment centres and training providers and in line with the company's decarbonisation action plan, EBRD's Just Transition Diagnostic and Action Plan and regional economic development planning processes.

The Corporate Development Programme in particular will focus on key improvements at the EPS corporate level which also have broader systemic significance for Serbia's energy security and overall system resilience. It includes strengthening EPS's corporate governance and independence; improving its operational efficiency, risk management structures and practices and addressing procurement underperformance; and enhancing market liquidity and regional integration, both key contributors to energy security and transition towards more open market structures. The Programme will be deployed under the Bank's new SOEs Management Assistance Reform and Transformation (SMART) programme. In addition to corporate-level improvements, the project also includes conditionality for the state as the owner with respect to the following governance measures [REDACTED]. These measures aim to build on corporate governance improvements implemented by EPS under a Corporate Governance Action Plan developed in the context of the previous EBRD investment and are in line with new legal framework being developed pursuant to the Strategy of State Ownership and Management of Business Entities Owned by the Republic of Serbia for the Period from 2021 to 2027 (Serbia's State Ownership Policy).

The Project is aligned with the Bank's Strategy for Serbia, supporting green economy by fostering energy efficiency, enhancing renewable energy, and promoting sustainable practices, as well as promoting inclusive and gender-equal growth. 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

Given its nature, the Project has been rated manually. The rating strikes a balance between the level of ambition under these two qualities, as well as the conditions precedent and covenants that have been embedded in the agreement on the areas of green and governance, but also the significant delivery risk considering previous projects with the same Client. This leads to a final ETI score of 62.

Impact acknowledges the level of ambition of the transaction on the green transition of EPS and, more generally Serbia, through several TCs and commitments from the Client. Impact also welcomes the SOE reform package that is part of the transaction which is expected to improve investment planning and strengthen oversight and governance in EPS.

Primary Quality: Resilient

Obj.No	Objective	Details
1.1	*The Project targets the Resilient quality through the provision of energy security measures.*	The Project will improve Serbia's energy security by providing the Company with the liquidity needed to (1) finance critical electricity imports required to keep the electricity market functioning; (2) make payment to renewable energy producers within Serbia under the Feed-in-Tariff system; (3) pay for mandatory operating expenses required to keep the Company running, (4) repaying maturing short-term loans. The project also includes ambitious policy dialogue and reform commitments targeting improvements on the corporate level with broader systemic impact.

Secondary Quality: Inclusive

Obj. No	Objective	Details
2.1	*The Project will significantly improve policy practices and standards.*	The Project will enhance the capacity of EPS to actively contribute to a 'just' transition by supporting the formulation and delivery of an action plan for greening skills systems at the national level and by strengthening the human capital development aspect of regional economic development planning processes in the affected municipalities. EBRD has been supporting the Ministry of Mining and Energy (MoME) of Serbia in the development of a Just Transition Diagnostic and Action Plan (TCRS ID: 14896, financed by the Climate Investment Funds),, in line with NECP projections. This engagement focuses on ensuring that the benefits of the green economy transition are shared, while protecting vulnerable communities, regions (i.e. Kolubara, Kostolac and Rembas areas) and workers directly and indirectly affected from falling behind. Building on the Just Transition Diagnostic and Action Plan, the Project will support the coordination between EPS, the Ministry of Mining and Energy, the Ministry of Education, Science and Technological Development, the

		National Employment Service (NES), its local employment centres, relevant municipal authorities and sectoral associations, such as the Renewables and Environmental Regulatory Institute. The aim of this collaboration will be to assess how existing competency standards and curricula could be revised to respond to the changes in the labour market driven by the green energy transition. To this end, EPS recently formed a "Scientific Council" to strengthen collaboration with academics, heads of technical faculties, engineers and scientific institutes such as the SANU's (Serbian Academy of Sciences and Arts) Energy branch. At the same time, EPS re-launched and expanded its "Expert Council", with the idea that these two councils will represent permanent advisory bodies. Going forward, the Company wants to focus more on interdisciplinary approaches that consider mining, decarbonisation and renewable energy sources as interconnected key issues in the energy transition. This initiative will also rely on a collaboration with the International Labour Organisation (ILO) and follow the methodology established by ILO for greening Technical and Vocational Education and Training (TVET) systems. Such an assessment will identify both outdated competences and emerging ones and will guide the development of an action plan for greening national and local skills systems. This will ensure that the reskilling programme can be designed in response to the upcoming needs of the national and local economies.
2.2	*The Project will introduce a new and replicable training programme improving skills for [REDACTED] people from the inclusion target group in partnership with (local) vocational schools or universities.*	The Project will enhance access to market-relevant skills and employment opportunities for local workers affected by the green economy transition and support the development of a strategic vision for EPS's HR function. According to most recent (end of September 2022) data, EPS employs c. 24.4 thousand workers. [REDACTED]. About half of EPS workforce is located in the Kolubara district, where the effects of the green economy transition might be felt [REDACTED]. As a response to the challenges that the decarbonisation process will bring, the Project will develop a retraining initiative in line with market relevance and best-practice standards, which will target [REDACTED] affected workers [REDACTED]. EPS is also committed to continue supporting the implementation of this initiative after EBRD's intervention, providing further re-skilling opportunities for affected workers in the years to come through long-term partnerships with relevant training providers. To decide on the list of the most relevant courses to include, the Bank's support will focus as a first step on a strategic workforce planning exercise to identify skill gaps and related training needs at EPS level and to introduce forward-looking workforce management measures based on EPS's business strategy for the next decade, as well as on the results of the national assessment on greening skills systems. The retraining programme will be developed in collaboration with suitable TVET institutes, as well as with the local employment centres of the NES and will be open to both EPS employees and other indirectly affected workers. Gender implications of the programme will be considered throughout (e.g. the need to design gender-sensitive trainings).

1.3 ADDITIONALITY

Identified triggers	**Description**
A significant share [REDACTED] of the project is to finance liquidity	Bank proceeds will be used to finance liquidity needs.
Additionality sources	**Evidence of additionality sources**

Financing structure Crisis response: EBRD financing **effectively bridges a financing gap** due to adverse market conditions. EBRD offers a **tenor**, which is longer than available to the client in the market on reasonable terms and conditions.	The recent energy crisis has resulted in the unprecedented spike in energy costs-- in many European markets, wholesale power prices in the first half of 2022 were three to more than four times as high as the average in the first half of 2016 to 2021, primarily due to gas prices increasing to more than five times the value of the reference period. EPS has traditionally depended on imports to meet peak winter demand, and its recent mechanical and production failures have exacerbated the situation EPS has [REDACTED] a significant financing gap which can only be met by international financial institutions. In addition, the Bank's liquidity facility tenor is currently not available on the market where local banks are providing liquidity lines for up to 1-2 years. The longer-term nature of the current electricity market disruption, coupled with the Company's inability to fully pass on costs to end-users, but a premium on longer tenor liquidity facilities.
Risk mitigation EBRD provides comfort to clients and investors, financial or strategic, by **mitigating non-financial risks**, such as country, regulatory, project, economic cycle, or political risks.	The current energy crisis continues to be exacerbated by the ongoing geopolitical conflict stemming from Russia's invasion of Ukraine and the disruption to significant imports of Russian gas by the continent. The Company is seeking the Bank's support to address the energy security issue.
Standard-setting: helping projects and clients achieve higher standards Client seeks/makes use of EBRD expertise on **higher environmental standards**, above 'business as usual' (e.g. adoption of emissions standards, climate-related ISO standards etc.).	As part of the proposed transaction, the Bank will support EPS to enhance its climate corporate governance and develop a decarbonisation roadmap by: 1) preparing a decarbonisation roadmap, including the development of an action plan, aligned with the NECP [REDACTED] and other strategic documents, that would ensure the Company's green energy sector transition; and 2) enhancing corporate climate governance by implementing climate risk reporting in accordance with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD): disclosure requirements initially to focus on qualitative aspects related to governance, strategy, and climate-related risk/opportunities management, with incorporation of quantitative aspects of climate-related financial risks and opportunities [REDACTED].
Gender SMART **Standard-setting: helping projects and clients achieve higher standards** Client seeks/makes use of EBRD expertise on **gender standards or equal opportunities action plans**.	EPS will promote gender equality across its operations in Serbia and will commit to increase the share of women in top managerial positions [REDACTED], in line with the national sectoral average. To achieve this, EPS will be supported in the review and improvement of its HR policies and practices, including the development of an Equal Opportunity Action Plan. This will help EPS identify new ways to introduce gender inclusion measures and foster women's access to economic opportunities across all its operations, including in relation to (i) attraction, (ii) recruitment, (iii) retention, (iv) development, (v) retrenchment, and (vi) promotion to managerial positions of women. The Company also committed to focus on promoting the role of women in Science, Technology, Engineering, and Maths (STEM) occupations by developing a tailored campaign to attract more female engineers.

1.4 SOUND BANKING - KEY RISKS

Risks	Probability / Effect	Comments
Project risks		
Counterparty Creditworthiness	**High/ Medium**	The Company's performance has suffered over the past year due to production issues (e.g. poor hydrology, low quality of coal) which resulted in higher reliance on electricity imports at very high prices resulting in losses and deterioration in liquidity. At the same time sales prices to end users were capped. This was partly addressed by state support similarly to other countries. **Mitigants:** • Recovery is planned over the coming years with stabilisation of production and steady increase of sales prices. While the repayment if the proposed loan will rely on Company's performance which is projected to steadily improve, ultimately the risk is mitigated by the sovereign guarantee which ensures debt service for sovereign guaranteed loans. • The Bank will engage consultants to work on improvements in Company's risk management and procurement as well as decarbonisation strategy all with the aim to support improvement operational structure and strategic positioning.
Guarantor Creditworthiness	**Low/ High**	Serbia is rated at BB+ (Stable) by S&P, Ba2 (Stable) by Moody's and BB+ (Stable) by Fitch. Serbia's rating is underpinned by a track record of macroeconomic stability and credible policy framework. The Serbian economy has demonstrated resilience in the face of the recent shocks. Following a mild 0.9% GDP contraction in 2020, GDP grew by 7.4% in 2021, outperforming the expectations, and is set to expand in 2022 albeit at more moderate rate in the face of worsening environment. Exchange rate vis-a-vis EUR is managed very tightly, supported by the adequate level of international reserves and robust FDI inflows. IMF assesses the public debt to be sustainable with high probability and projects it to decline over the medium term, supported by the authorities' commitment to fiscal consolidation and continuation of economic growth.

2. MEASURING / MONITORING SUCCESS

Overall objectives of project	*Monitoring benchmarks*	*Implementation timing*
- Good financial and operational performance - On-time project implementation	- Stable financial position and compliance with financial covenants - Completion according to the timeline - Implementation of TCFD, corporate programme including decarbonisation plan in line with NECP, inclusion programme within a set timeframe.	[REDACTED]

Primary Quality: Resilience

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date	TC[3]
1.1	Improved financial standards	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

[3] Select "Y" if this project has an associated TC and this indicator is related to that TC.

1.2	Improved financial standards	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
1.3	Improved financial standards	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
1.4	Improved financial standards	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Secondary Quality: Inclusive

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date	Donor
2.1	Recommended policy or strategy agreed by relevant stakeholder(s)	The Project will enhance the capacity of EPS to actively contribute to the just transition process ongoing in the country, and engage in the preparation of an action plan for greening skills systems, in collaboration with MoME.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
2.2	Tailored training programme developed and implemented	With Bank's support and in collaboration with partner TVET institutes and local employment centres, EPS will develop and introducing a comprehensive reskilling and upskilling programme.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
2.3	Number of local population enhancing their skills as a result of training	Number of local workers that will be retrained [REDACTED], enabling them to acquire market-relevant skills to be redeployed within EPS or the broader regional and national labour market.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Additional Indicators: Gender SMART and Conditions Precedent/Covenants in the Loan Agreement on the fields of Green Transition including energy market strengthening and better EPS Governance.

Indicator type	Monitoring indicator	Details	Base-line	Target	Due date	Donor
Advisory & Policy Indicators	Share of female employees in total number of employees	EPS will increase the share of women in top management positions [REDACTED].	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Practices of the relevant stakeholder improved (equal opportunity practices of the client)	EPS will design and implement a comprehensive Equal Opportunities Action Plan, with a focus on promoting the role of women in STEM careers.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Number of local population enhancing	Number of local workers that will be retrained, enabling them to acquire	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

	their skills as a result of training	market-relevant skills to be redeployed within EPS or the broader regional and national labour market.				
Advisory & Policy Indicators	Number of local population enhancing their skills as a result of training	Number of local workers that will be retrained, enabling them to acquire market-relevant skills to be redeployed within EPS or the broader regional and national labour market.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Number of local population enhancing their skills as a result of training	Number of local workers that will be retrained, enabling them to acquire market-relevant skills to be redeployed within EPS or the broader regional and national labour market.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Recommended policy or strategy or regulatory framework/standard agreed by relevant stakeholder(s)	The Project will enhance the capacity of EPS to actively contribute to the just transition process ongoing in the country and contribute to the implementation of an action plan for greening skills systems in collaboration with MoME, which will result in the approval [REDACTED] new education standard on green energy/ energy efficiency	[REDACTED]	[REACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Actions in the climate action plan implemented	Implementation of decarbonisation strategy and action plan	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Recognised climate reporting framework adopted	Implementation of climate risk reporting	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Actions in the Corporate Governance Action Plan Implemented	Implementation of corporate governance programme	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Generic indicator	Conduct and conclude a public process for the selection and appointment of a new general manager ("*direktor*") for a mandate stipulated by applicable legislation.	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Generic indicator	Expand expertise and diversity of the supervisory board and introduce not less than one additional	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

		independent supervisory board member.				
Advisory & Policy Indicators	Generic indicator	Launch of first renewable energy auction [REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Improved reporting standards	Improve compliance and reporting standards in line with REMIT	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Advisory & Policy Indicators	Market-based exchange mechanisms introduced or improved as targeted	Achieve a minimum [REDACTED] trading volume on regional energy exchanges	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

3. KEY PARTIES

3.1 BORROWER

Javno preduzeće Elektroprivreda Srbije Beograd ("EPS," or the "Company"), the fully state-owned incumbent power utility in Serbia. EPS operations consist of the generation and supply of electricity. The Company usually provides around 95% of the entire domestic production. Annual production in 2021 was about 21,537 GWh from the TPPs (installed capacity of 4,079 MW), 630 GWh from the CHPPs (installed capacity 297 MW), and 11,667 GWh from the HPPs (installed capacity 3,015 MW). EPS employs c. 24 thousand people.

Serbia and its state-owned generation company, EPS, face major challenges transitioning away from their existing reliance on legacy lignite-fired infrastructure for power generation. Over the past years, the share of renewable energy in gross final electricity consumption has remained below 30%, with less than 3% of production generated by intermittent wind and solar- well below the 38% target for 2030 established in the National Renewable Energy Action Plan (NREAP) or the more ambitious 45% target for 2030 to be included in the draft National Energy and Climate Plan (NECP).

	Audited financials			*Management account*	
EUR million	**2019**	**2020**	**2021**	[REDACTED]	[REDACTED]
Profit and Loss					
Revenues	2,068	2,156	2,720	[REDACTED]	[REDACTED]
EBITDA	493	597	202		
margin %	*23.8%*	*27.7%*	*7.4%*		
Financial debt	1,855	1,075	1,906		
Cash	176	173	115		
Equity	3,063	3,062	3,066		
Debt/EBITDA (x)	3.77	1.80	9.44		

[REDACTED]. Detailed historic financial accounts are presented in *Annex 2*.

3.2 GUARANTOR

The Guarantor is the Republic of Serbia, represented by the Ministry of Finance. The Serbian economy showed resilience in the face of recent shocks. Following a mild 0.9% GDP contraction in 2020, GDP grew by 7.4% in 2021, outperforming the expectations The expansion reflects a strong expansion of exports and industry due to rebound of the Euro Area, Serbia's main trading partner, robust household consumption on the back of pent up demand and continued investment impulse supported by the sizeable public investments. FDI recovered in 2021 to above the 2019 level, which bodes well for future growth. The GDP growth is expected to moderate closer to 3% in 2022 on the back of worsening macroeconomic environment and external conditions.

Serbia's public debt is elevated, but considered to be sustainable. The main challenge to Serbia's debt sustainability relate to absence of further structural fiscal adjustment and unfavourable internal and external developments due to different shocks. On the positive side, a majority of Serbia's debt is at fixed interest rates (87.2% of the debt), the average maturity of outstanding debt is long, the share of multilateral and institutional creditors in the external debt is high and the level of international reserves adequate. Continued engagement with the IMF helps uphold the confidence and ensure liquidity. IMF team and the Serbian authorities have reached staff-level agreement on replacing a non-financial Policy Coordination Instrument initiated in June 2021 with a 24-month Stand-By Arrangement (SBA) with access amounting to EUR 2.4 billion. This arrangement would help address emerging external and fiscal financing needs given the challenging global economic environment and support the authorities' macroeconomic policies and structural reform efforts, with a focus on the energy sector. Serbia is rated at BB+ (Stable) by S&P, Ba2 (Stable) by Moody's and BB+ (Stable) by Fitch.

4. MARKET CONTEXT

Electricity production in Serbia in 2021 amounted to 35.6 TWh, of which consumption was 36.3 TWh and the final customer consumption was at 30.8 TWh. The remaining was used electricity losses recovery in transmission and distribution, and for the power plants operations. The final customer consumption increased 1.4 TWh YoY. Because of the ongoing energy crisis and the disruptions with EPS' TPPs, the import of electricity dramatically increased in the last quarter of 2021 and the first quarter of 2022. [REDACTED].

Serbia has made considerable progress towards meeting its Energy Community Treaty obligations and in liberalising its energy sector. Generation, transmission and distribution are fully separated.

Distribution has been split off from EPS at end 2020 and is now owned and operated by the state-owned Elektrodistribucija Srbije ("EDS," and EBRD client). The Ministry of Mining and Energy ("MoME") is assigned primary responsibility over the energy sector in the country. The Minister is responsible for the overall energy strategy and is closely overseeing all public investments in the energy sector.

The Energy Agency (AERS) is the single authority regulating the energy sector of Serbia, as required by the Third Energy Package. AERS is headed by a Council consisting of a President and four members with five-year terms, renewable once. The regulator is responsible for issuing the relevant licences, setting tariff methodologies, proposing tariffs for monopoly activities and monitoring the operation of the energy market. AERS has benefited from substantial donor funded capacity building technical assistance, and has, in the ten years since it was set up, developed both its technical capacity, and its reputation as a technically competent and effective regulator within the sector.

Given its high legacy dependence on coal and lack of indigenous substitute energy alternatives, Serbia has been slow to adopt a decarbonisation strategy or to set a fixed exit date for coal. Renewable energy remains virtually undeveloped, with only 430 MW of installed wind farm capacity and c. 8 MW of PV capacity. The country's 2022 revised NDC calls for a 33% GHG reduction target by 2030 as compared to 1990 (2017 NDC targets: 13% GHG reduction vs 1990), while NECP is not adopted yet. The escalating operational problems at EPS' legacy thermal assets, coupled with extreme energy prices and the increasing attractiveness of renewables, presents a key potential tipping point for Serbia's decarbonisation path. As a condition to extending the first tranche of EUR 200 million, EBRD will require a number of a unprecedented commitments from the Serbian government, including: (i) a public commitment to exit coal as soon as possible and before 2050 and (ii) adoption of a regulatory framework for renewable energy auctions and the publication of a 1,000 MW auction plan for 2023-2025, cumulating with the launching of Serbia's first renewable energy auction for 400 MW of wind power capacity on terms satisfactory to the Bank. As a condition for Loan 2 facility EBRD will require that the pilot wind auction successfully closes, and that Serbia adopt an ambitious NECP requiring an increase in the share of renewable electricity generation to increase from 30% to 45%.

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

Categorised B (2019 ESP). As liquidity support with a specified use of proceeds, this transaction has limited direct environmental or social impacts. Due diligence was carried out in-house via questionnaires, a review of reporting for previous EPS projects and site visits to monitor the company's health and safety performance. EPS's environmental and social performance is well known to the Bank as, under the existing ESAP, it is required to carry out three-yearly environmental and social audits of all its operations, with the last audit carried out in 2020.

The most recent audits found that EPS continues to face significant environmental challenges related to air emissions (NOx, SOx and particulates) associated with its aging thermal generation fleet. In November 2022 a Serbian court issued a judgment requiring EPS to reduce SO_2 emission in line commitments made in the National Emission Reduction Plan. EPS has undertaken some measures to retrofit pollution abatement technology, but ultimately, consistent compliance with EU air emission standards will require the decommissioning and replacement of existing plants with renewable and non-coal alternatives.

REDACTED] Requirements for the establishment of central environmental, health and safety functions have been included in the ESAP for this transaction, with fixed deadlines for implementation. It also includes a requirement for EPS to assess and address physical climate risks posed to large hydropower plants by water stress, drought and flooding. EPS has also prepared and disclosed a Non-Technical Summary that describes the company's operations, its environmental and social performance, management systems and ESAP commitments. [REDACTED].

6.2 INTEGRITY

In conjunction with OCCO, integrity due diligence was undertaken on EPS, its senior management, and board members. The [REDACTED] Project does not pose an unacceptable integrity or reputational risk to the Bank. [REDACTED]. EPS is an existing client of the Bank via several projects. [REDACTED].

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

6.3 RING FENCING OF PROCEEDS

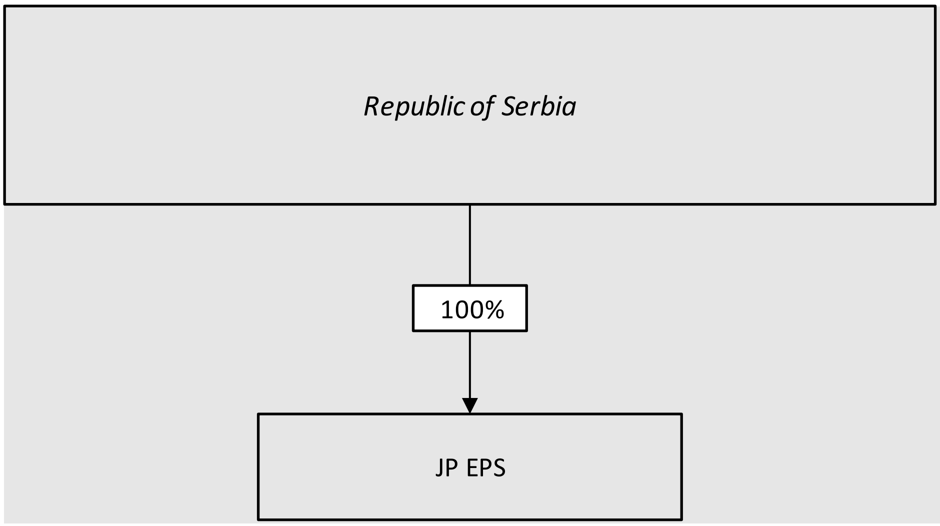
The transaction's use of proceeds will be entirely ring-fenced away from the coal-linked electricity generation of EPS, and will not be used for any investment, maintenance or operating costs (including worker salaries linked to these cost centres) linked with fossil fuels. [REDACTED].

ANNEXES TO OPERATION REPORT

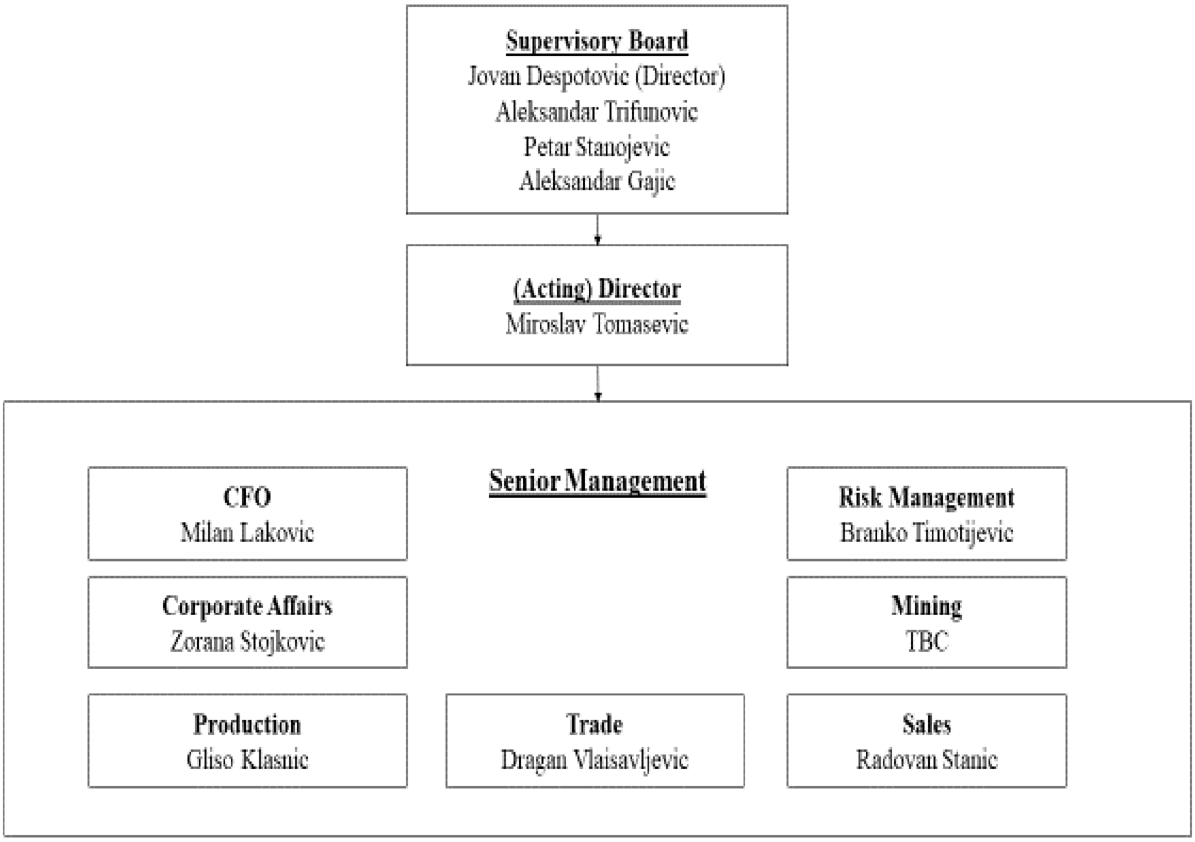
ANNEX 1	Shareholding and Organization Structure
ANNEX 2	Historical Financial Statements
ANNEX 3	Green Assessment
ANNEX 4	Project Implementation

ANNEX 1 – SHAREHOLDING AND ORGANIZATION STRUCTURE

EPS is a public utility 100% directly owned by the Government of Serbia.



Below is the organization structure:



ANNEX 2 – HISTORICAL FINANCIAL STATEMENTS

PROFIT AND LOSS - Consolidated report
EUR '000

	31 Dec 19 Audit	31 Dec 20 Audit	31 Dec 21 Audit	[REDACTED]	[REDACTED]
Income from sales of goods and services	2,025,250	2,093,136	2,607,077		
Other revenues	18,973	40,719	31,782		
Income from premiums, subventions, grants and donation	24,211	21,931	81,437		
Total revenues from operation	**2,068,433**	**2,155,786**	**2,720,297**		
Production materials	(557,178)	(532,766)	(1,606,329)		
Production services	(235,935)	(263,467)	(193,988)		
Personnel cost	(555,163)	(529,664)	(416,034)		
Other operating cost	(227,567)	(233,120)	(301,986)		
EBITDA	**492,590**	**596,768**	**201,961**		
Depreciation	(406,020)	(428,632)	(299,935)		
EBIT	**86,570**	**168,136**	**(97,974)**		
Financial income	68,715	99,784	40,057		
Financial costs	(27,136)	(17,242)	(54,552)		
Interest	(11,606)	(10,508)	(14,218)		
Negative forex costs	(13,222)	(4,118)	(37,913)		
Other financial cost	(2,308)	(2,616)	(2,421)		
Other income	12,638	48,765	50,910		
Other costs	(181,449)	(161,690)	(73,145)		
Income from adjustments of other assets carried at fair value	11,054	6,938	57,684		
Expenses from adjustments of other assets carried at fair value	(89,156)	(107,865)	(50,246)		
Other costs	(103,347)	(60,763)	(80,582)		
EBT	**(40,662)**	**137,752**	**(134,705)**		
Corporate tax	(8,860)	(46,978)	2,936		
Net Income	**(49,522)**	**90,774**	**(131,769)**		

BALANCE SHEET - Consolidated report

EUR '000

	31 Dec 19 Audit	31 Dec 20 Audit	31 Dec 21 Audit	[REDACTED]	[REDACTED]
Assets					
Inventories	322,337	295,834	276,421		
Trade receivables	391,372	483,377	533,219		
Other trade receivables	1,113	2,641	1,076		
Short term financial investments	3,906	1,855	2,112		
Other current assets/accruals	105,981	79,039	144,088		
Cash and cash equivalents	176,091	173,369	114,552		
Total current assets	**1,000,800**	**1,036,114**	**1,071,468**		
Property, plant and equipment	8,714,313	6,587,511	6,954,595		
Intangible assets	109,963	143,839	107,523		
LT financial investments	47,631	42,655	30,735		
Total non current assets	**8,871,908**	**6,774,005**	**7,092,854**		
TOTAL ASSETS	**9,872,708**	**7,810,120**	**8,164,322**		
Liabilities					
Trade payables	277,002	392,785	601,301		
Other trade payables	15,675	16,990	17,858		
Short-term debt	161,592	156,434	462,846		
Other short-term liabilities/accruals	466,468	237,175	195,681		
Total current liabilities	**920,736**	**803,384**	**1,277,686**		
Long term provisions	218,091	346,925	322,881		
Non-current financial debt	1,693,338	1,548,418	1,443,487		
Total non current liabilities	**1,911,430**	**1,895,342**	**1,766,369**		
TOTAL LIABILITIES	**2,832,166**	**2,698,726**	**3,044,054**		
Equity					
Reserves	5,104,676	3,604,900	3,807,653		
Retained earnings	(1,099,987)	(1,530,068)	(1,728,037)		
Other Equity and unrealsed gain/(loss) from securities	(26,767)	(25,205)	(25,568)		
Paid-in capital	3,062,619	3,061,766	3,066,220		
TOTAL EQUITY	**7,040,542**	**5,111,394**	**5,120,268**		
TOTAL EQUITY AND LIABILITIES	**9,872,708**	**7,810,120**	**8,164,322**		
check	-	-	-		

CASH FLOW - Consolidated report

EUR '000

	31 Dec 19 Audit	**31 Dec 20** Audit	**31 Dec 21** Audit	[REDACTED]	[REDACTED]
Operating activities					
Cash inflow sales and advances received	1,567,801	2,299,413	2,327,621		
Other proceeds from operating activities	22,341	23,463	12,410		
Charges for services that qualify as public revenues	(517,218)	(496,555)	(471,897)		
Interest net	11,922	1,449	(1,715)		
Paid tax	(3,192)	(28,269)	(81,247)		
Other operating outflows	(696,086)	(1,399,314)	(1,450,378)		
Cash flow from operating activities	**385,568**	**400,187**	**334,793**		
Investment activities					
CAPEX	(395,113)	(405,899)	(431,257)		
Sale of intangible assets, PPE and biological assets	162	-	110		
Other financial investments (net inflows)	48,868	-	8,257		
Interest received from investing activities	6,766	10,328	3,344		
Other financial outflows (net)	(1)	(35,370)	(10)		
Cash flow from investment activities	**(339,318)**	**(430,941)**	**(419,556)**		
Financial activities					
Inflows/outflows from LT debt	(101,907)	167,454	210,350		
Inflows/outflows from ST debt	9	(138,805)	(157,225)		
Interest net	-	-	-		
Paid dividends	(82)	(3)	(25,516)		
Finance lease	-	(2)	(1,162)		
Other liabilites and increase in share capital	(10)	(488)	(497)		
Cash flow from financial activities	**(101,990)**	**28,155**	**25,949**		
Forex translation adjustment	(51)	(141)	(5)		
Net cash	(55,740)	(2,599)	(58,814)		
Cash balance at the beginning of the year	222,963	167,173	164,432		
Cash balance at the end of the year	**167,173**	**164,432**	**105,613**		

Note 1: Year-end financials have been converted from RSD (as presented in the report) to EUR at FX EUR/RSD of 117.593, 117.580 and 117.582 (31.12.2019, 31.12.2020 and 2021, respectively - applied to balance sheet) and 117.852, 117.578 and 117.573 (average FX for 2019, 2020 and 2021, respectively - applied to Cash flow and Income statement).
Note 3: PwC (unqualified opinion) has audited the report
Note 4: Source for the FX rates - https://nbs.rs/en/indeks/

ANNEX 3 – GREEN ASSESSMENT

Introduction

The project is aligned with the mitigation and adaptation goals of the Paris agreement, subject to implementation of the ambitious action plan. At the transaction level, the project is consistent with NDC and has low risk of lock-in, as the transaction does not invest in physical assets (capex). At the counterparty level, the commitments of EPS and the Government of Serbia demonstrate actions to align financial flows with Paris Agreement for mitigation. The project is aligned with adaptation goals due to the absence of capex, and at counterparty level - reduced reliance on vulnerable coal assets over time due to decarbonisation, as well as actions to address flooding and hydrological variability risks in the ESAP and as part of Corporate Climate Governance.

The transaction meets criteria of the Energy Sector Strategy (Fossil Fuels) approach of the EBRD (2021) [REDACTED].

Paris alignment assessment

Alignment with the mitigation goals of Paris Agreement: general screening

- The project/economic activity is **not included** in the 'aligned list'.
- Regarding project/economic activities, 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.
- However, EPS is engaged in economic activities on ‘non-aligned’ list, including mining of thermal coal and electricity generation from coal.

Alignment with the mitigation goals of Paris Agreement: specific assessments

Nationally Determined Contributions (NDC) and decarbonisation context: The project is compatible with Serbia’s updated NDC, targeting a net reduction of greenhouse gas emissions by 33.3% by 2030 compared to 1990. As part of Serbia's Stabilisation and Association Agreement with the EU (2012), the country has committed to aligning its legislation on climate change to the EU acquis, further reinforced by becoming a signatory of Sofia Declaration on the Green Agenda for the Western Balkans (2020) and by endorsing Berlin Declaration on Energy Security and Green Transition in the Western Balkans (November 2022). This confirms a commitment to align with the EU Climate Law once it is adopted with a vision of achieving climate neutrality by 2050.

As part of transaction, the Government commits to adopt a National Energy and Climate Plan (NECP) by 31 December 2023, including KPI of increasing the share of renewables in the energy mix from 30% to over 45% by 2030. The current NECP draft targets 40.3% emissions reduction (47.82 MtCO2eq) compared to 1990, and 1,073 MW coal-fired TPP capacity phaseout by 2030, supporting 2050 climate neutrality trajectory. The Government is also working to finalize the regulatory framework to launch Serbia's first renewable energy auction (expected 400 MW in 1H 2023), as well as announcing an ambitious forthcoming auction quotas of not less than 1,000 MW for the forthcoming three-year period.
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 [REDACTED].

Counterparty-level actions to align financial flows: [REDACTED]. The project and associated TCs will support their development and set the company on a decarbonisation path. needs to demonstrate commitment to working towards aligning their activities with the goals of the Paris Agreement. This includes:

1. Having a credible corporate decarbonisation plan

EPS will adopt and start implementing the plan [REDACTED]. The plan will set out a pathway to phase out coal-related activities on a timeline consistent with the goals of the Paris

Agreement to limit global warming to well below 2, preferably to 1.5 degrees Celsius, compared to pre-industrial levels [REDACTED].

- The plan will include tangible actions, targets and key performance indicators with specific timeframes, including a coal exit strategy and related monitoring, as well as indication of funding sources and affordability. It will also be supplemented by Just transition Diagnostic and Action Plan, supported by the EBRD.
- As an SOE, EPS is obliged to be aligned with national strategies, including NECP. As part of the transaction, the Government will commit to a coal phase-out [REDACTED]. Draft NECP envisages net decommissioning of 1,073 of thermal power plant capacity by 2030, including 239 MW of Kolubara A1, A2, A3, A5, 125 MW of Morava, 210 MW of Kostolac A2, 100MW of Kostolac A1, 210 MW of Nikola Tesla A2, 210MW of Nikola Tesla A1, 329 MW of Nikola Tesla A3 units.
- Furthermore, EPS is pursuing decarbonisation by advancing its first renewables projects and plans roll-out of its renewable energy investment programme including the Morava and Kolubara PV projects, the Kostolac wind farm, and the significant HPP rehabilitation project to be implemented including at Vlasinske HPP. The latter project is of especial importance to Serbia's decarbonisation strategy, as carrying out the hydro rehabilitation will significantly increase EPS' balancing capacity and potentially allow it to absorb [REDACTED]of new intermittent renewables on the Serbian grid.

2.Commitment to no new investments in non-aligned activities:
In November 2022, Serbia endorsed the *Berlin Declaration on Energy Security and Green Transition in the Western Balkans*, confirming the country's determination to "prevent long-term carbon lock-in and stranded assets associated with the construction of new coal-fired power plants". As an SOE, EPS is obliged to fully align its activities with national strategies, including NECP and Energy Development Strategy (currently in draft form, a derivative of NECP). [REDACTED].

3. Corporate Climate Governance
Consistent with Fossil Fuel approach and Paris alignment annex, EPS will also enhance Corporate Climate Governance by implementing recommendations from the Task Force on Climate-related Financial Disclosures (TCFD) [REDACTED], including fully integrating climate change considerations into corporate practices.

Alignment with the adaptation goals of Paris Agreement

The Project is considered aligned with the adaptation goals of the Paris Agreement, given the that use of proceeds is not linked to physical capital (purchases of electricity, debt repayment and meeting critical operating expenses). Furthermore, at counterparty level, EPS's operations are geographically diversified, making it impractical to assess individual assets. At the counterparty level, key climate vulnerability risks include flooding (eg TENT power station, Kolubara and Kostolac coal mining basins), and increased hydrological variability (water stress) for 3,015 MW of HPPs. These will be addressed through: (1) reduced usage of coal-related infrastructure in line with decarbonisation targets, (2) physical climate risk assessment, and actions to address floods and water stress/droughts hazards for installed large hydropower capacity as part of Environmental and Social Action Plan (ESAP) and (3) integration of broader climate risk considerations at corporate level as part of Corporate Climate Governance engagement.

GET attribution: N/A

Green Project Monitoring Plan: [REDACTED].

ANNEX 4 – PROJECT IMPLEMENTATION

Procurement classification – *Public sovereign*

[REDACTED]. This project will be subject to Article 3.25 "Procurement of Commodities" and 3.27 "Procurement by Utilities" of PPR and be implemented by the Client in accordance with their internal procurement procedures. Considering the experience and the volume of similar transaction with those to be financed under the project it is estimated that the Company has a good capacity to implement the project in accordance with their own procedure and at the same time observing the PPR requirements.

Contracts risk assessment - *Low*

The contracts to be financed under the Project are standard energy purchase contracts which are either implemented through commodity exchange mechanism or through standardized framework contract agreement for licensed trading companies with which the Client has long standing blanket purchase agreements.

Project implementation arrangements:

The EBRD loan proceeds will be used for working capital including electricity purchases [REDACTED]. 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 PPR, paragraphs 3.25 and 3.57 i.e. Special Competitive Procedures. As electricity purchase is a common and regular task of the Client there are established procurement arrangements in place as described in below.

Procurement Requirements to be met when applying Special Competitive Procedures

1. **The Bank Operation involves multiple contract awards for partial quantities of Commodities;**

EPS operates a framework contract with over 20 licensed trading companies which are qualified and competent to sell electricity to EPS. EPS also purchases electricity via organized electricity exchanges either i) through its Slovenian based subsidiary EPS Trgovanje which buys electricity on the organized regional electricity exchanges and markets including Hungary, Slovenia, Croatia and ii) directly by EPS through Serbian organized electricity exchange SEEPEX. The electricity is further sold from EPS to the universal supplier and eventually supplied to the households and corporates.

In the case of purchase of electricity through framework agreements the selected bidders sign sales and purchase contracts with EPS. These are multiple small-size contracts (commonly in the range of EUR 1 Mln or higher) with a predefined amount of electricity to be provided including standard terms of contracts (EFET 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 number of days and hence are not long term contract obligations. They are typically daily or weekly contracts but can have maturity of up to 1 year.

2. **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 announced by EPS to all trading companies with which EPS has signed EFET contracts providing an opportunity for them 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 announced to all bidders including number of signed contracts and highest contract price.

In the case of purchase through SEEPEX or another organized electricity exchange this is seen as efficient means to benefit from favourable competitive conditions providing market participants with high-quality and comprehensive services of a liquid, competitive and transparent electricity exchange market, which ensures their security in trading and reduces their risks and costs.

3. This is necessary to secure a timely supply of Commodities.

This requirement is met as EPS 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.

EPS has been requested to make sure that participating tenderers will sign the Bank's template of Covenant of Integrity and for the awarded tenderer to sign the template of Form of Contractor Integrity Undertaking.

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.