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| 1. Project Data: | | Date Posted : 06/04/2004 | |
| PROJ ID: P067223 | | Appraisal | Actual |
| Project Name: Sal | Project Costs (US\$M) | 202 | 202 |
| Country: Croatia | Loan/Credit (US\$M) | 202 | 202 |
| Sector(s): Board: EP - General industry and trade sector (40%), Central government administration (24%), Compulsory pension and unemployment insurance (18%), Other social services (16%), Health insurance (2%) | Cofinancing (US\$M) | | |
| L/C Number: L4641 | | | |
| | Board Approval (FY) | | 02 |
| Partners involved : | Closing Date | 03/31/2003 | 10/31/2003 |
| Prepared by : | Reviewed by : | Group Manager : | Group: |
| Michael R. Lav | Emily S. Andrews | Ajay Chhibber | OEDCR |
| 2. Project Objectives and Components a. Objectives To support the Government in the implementation of a structural reform program that aims to place the economy on a path of rapid and sustainable growth through improving coordination and management in economic policy making; enhancing fiscal discipline; strengthening market institutions and the competitiveness of the economy; enhancing flexibility in the labor market; and strengthening social protection . b. Components 1. Improving coordination and management in economic policy through high level policy committee . 2. Improve overall budget processes and strengthen fiscal discipline by, in particular, improving health care and pensions systems. 3. Strengthen Market Institutions and the competitiveness of the economy by : (a) settling arrears and accounts payable/receivables between public enterprises and between public enterprises and the Government, (b) facilitating the bankruptcy processes, (c) strengthening the framework for inter-enterprise competition, (d) enhancing the entry of new businesses, and (e) reducing barriers to domestic and foreign direct investment . 4. Enhance labor market flexibility by making it less expensive to hire and fire workers . 5. Strengthen Social Protection by developing a national strategy for poverty reduction and improving the effectiveness of social assistance . c. Comments on Project Cost, Financing and Dates The project cost US\$202 million financed by an IBRD loan in two tranches . The project was appraised in April, 2001, approved by the Board on December 4, 2001, made effective on February 8, 2002, and closed on October 31, 2003, 7 months behind schedule. | | | |
| 3. Achievement of Relevant Objectives: 1. A high level policy committee chaired by the Deputy Prime Minister improved coordination . 2. To improve budget processes (a) a consolidated government budget was introduced and a modern and comprehensive Budget Law was adopted which improved the accuracy of budgeting . Fiscal discipline was strengthened with the passage of the health and pension laws and amendments . Health care co-payments increased and co-payment exemptions were restricted to 50 percent of the population . For pensions, the minimum accrual rate of contributions was decreased and non-wage income was made subject to a pension levy . Pension accruals are now based only on paid contributions, although this was partially reversed when a law was amended to re-establish the wage indexation of pensions. 3. To Strengthen Market Institutions and the Competitiveness of the Economy : (a) arrears and accounts receivable/payable between PEs and between PEs and the Government were substantially settled (although new arrears are emerging), (b) a new bankruptcy law was passed to increase court capacity and improve the quality of bankruptcy professionals (although the outcome will be dependent on implementation by the judiciary), (c) A new Competition Law was enacted and the Anti-Monopoly Commission was given greater economic and legal expertise, | | | |

(d) to enhance new entry of businesses, licensing and registration were streamlined, and (e) to reduce the barriers to domestic and foreign investment, many of the recommendations of the FIAS study were implemented, although more remains to be done. 4. To enhance labor market flexibility, worker severance benefits were reduced, as were mass layoff's provisions, notification periods and other benefits such as maternity leave which had been excessive. 5. To Strengthen Social Protection, the National Poverty Reduction Program was finalized, arrears were eliminated for social protection, and the effectiveness of targeting is now being monitored.

4. Significant Outcomes/Impacts:

Reforms have improved Croatia's economic performance and brought it closer to negotiations for admission to the EU. GDP has grown by more than 4 percent since 2001 when the SAL-supported program was initiated.

5. Significant Shortcomings (including non-compliance with safeguard policies):

1. The wage indexation of pensions may lead to financial problems over time. 2. Enterprise arrears are re-emerging as a problem, and more fundamental reforms of the largest enterprises (responsible for most of the arrears problem) are called for.

| 6. Ratings : | ICR | OED Review | Reason for Disagreement /Comments |
|-----------------------------|--------------|--------------|--|
| Outcome : | Satisfactory | Satisfactory | |
| Institutional Dev .: | Modest | Substantial | Institutional reforms in private sector development, labor markets, and government management of its resources all indicate that IDI should be rated "substantial". The ICR rating for IDI was upgraded because the reforms supported by the SAL should have a substantial impact on the way that Croatia uses its resources both initially and over time, in view of the agreed "likely" rating for sustainability. |
| Sustainability : | Likely | Likely | |
| Bank Performance : | Satisfactory | Satisfactory | |
| Borrower Perf .: | Satisfactory | Satisfactory | |
| Quality of ICR : | | Satisfactory | |

NOTE: ICR rating values flagged with '*' don't comply with OP/BP 13.55, but are listed for completeness.

7. Lessons of Broad Applicability:

1. SALs should focus on a few key reforms essential for improved economic performance. This SAL focussed on key reforms in 5 sectors and achieved almost all of its objectives. 2. Interagency coordination is essential. In the case, the Deputy Prime Minister and the committee that he chaired played a constructive role in fostering ownership of the reforms in the line ministries and agencies, and adhering to implementation schedules.

8. Assessment Recommended? ☐ Yes ☒ No

9. Comments on Quality of ICR:

The ICR covers the wide horizon of the project concisely and with clarity.