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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

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# APPRAISAL OF

# THE BABIN KUK TOURISM PROJECT

# YUGOSLAVIA

June 2, 1971

Tourism Projects Department

## CURRENCY EQUIVALENTS

| | | |
|---|---|---|
| Currency Unit | = | Dinar |
| US$1.00 | = | Dinar 15.00 |
| Dinar 1.00 | = | US$0.07 |
| Dinar 1,000,000 | = | US$70,000 |

## UNITS OF WEIGHTS AND MEASURES: Metric

Metric: British/US Equivalents

| | | |
|---|---|---|
| 1 m | = | 3.28 ft |
| 1 $m^2$ | = | 10.76 sq ft |
| 1 km | = | 0.62 mi |
| 1 $km^2$ | = | 0.386 sq mi |
| 1 ha | = | 2.5 acres |
| 1 m ton | = | 0.98 lg ton |
| | | 1.1 US sh ton |

## FISCAL YEAR

January 1 - December 31

YUGOSLAVIA

# APPRAISAL OF THE BABIN KUK TOURISM PROJECT

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This report is based on the findings of a project appraisal mission consisting of Mr. D.T. Scarisbrick, Mr. J.G. Boyd, Mr. A. Odone, Mr. J.E. Kulski (Consultant) and Mr. R. Calkins. The main report was written by Mr. J.A. Simmons.

# YUGOSLAVIA

## APPRAISAL OF THE BABIN KUK TOURISM PROJECT

### SUMMARY


i. This report appraises a project to establish a large integrated tourism complex at Dubrovnik on Yugoslavia's south Adriatic coast. The complex would provide accommodations in nine hotels for 5,000 persons together with facilities for sports and recreation, restaurants, shops and entertainment. The proposed project is one of several recommended in the Physical Development Plan for the South Adriatic Region prepared over the past five years with assistance from the UNDP.

ii. International tourism in Yugoslavia has developed rapidly in the past decade, with foreign exchange earnings from tourism rising from US$22.0 million to US$310.0 million equivalent. The principal destinations of foreign visitors are resorts on the Adriatic coast where about 80% of foreign visitor nights are spent and almost two thirds of all hotel capacity is located. Most visitors to the northern coastal resorts arrive by road. With the greater distances to the southern Adriatic coast, air traffic is important. In consequence this is a higher priced market, catering for a more select clientele, for whom Dubrovnik has been the principal destination.

iii. Yugoslavia's draft Development Plan for 1971-75 sets targets for the tourism sector including a near doubling of hotel capacity and foreign exchange earnings of US$900.0 million in 1975. These targets are ambitious, but Yugoslavia's share of Mediterranean tourism is still small, and prices there are still lower than in competing countries, on average by 20-25%. Provided this competitive advantage can be maintained, there is little doubt that with vigorous development policies Yugoslavia can attract many more foreign visitors than heretofore.

iv. The site for the proposed project is a small peninsula, about 4 km to the north of the old walled city of Dubrovnik. Besides the great scenic beauty of the mountainous coastline, the palaces, churches and monasteries of the old city are tourism assets in themselves and provide a setting for a summer festival offering music, drama, opera and dance which has been a major attraction for tourists in recent years.

v. The project is one of the largest so far developed in Yugoslavia or abroad. The scale of the project offers considerable potential economies in construction and operation. To realize this potential will require the development of new management systems to identify and provide solutions to problems which have not yet been met in the industry. It will also require the selection and training of a management team. Qualified management consultants will be engaged by the borrower to develop and implement the management systems and to select and train the senior management personnel.

vi. The project is estimated to cost US$45.5 million equivalent, including contingencies. Interest during construction would amount to an additional US$4.4 million equivalent. The project would be constructed and operated by a new entity to be established for the purpose. The proposed Bank loan of US$20.0 million would cover 38% of the total project cost and US$2.8 million of interest during construction. The balance of the required financing would be provided by Minceta, a trading enterprise in Dubrovnik and the sponsor of the project, as equity capital (19%) and by Privredna Banka, Zagreb, the largest investment bank in Croatia, as a loan to Minceta for onward lending to the new entity. Financial forecasts show that the new entity should be able to meet all project costs and service its debt satisfactorily.

vii. The successful operation of the project would require investment in external infrastructure, namely extensions to water and sewerage systems in Dubrovnik and to the Dubrovnik airport, and short road connections. Assurances have been received from the appropriate Yugoslav authorities that these investments will be made. The share of the cost of such investments which can properly be charged to the project is estimated at about US$1.0 million equivalent.

viii. Contracts for construction and equipment would be awarded after international competitive bidding. Depending on whether local or foreign contractors would carry out the project and the extent to which foreign equipment would be used, the foreign exchange component in the total project costs would range from 24% to 38%. On the quite probable assumptions that Yugoslav bidders would win construction contracts and that the bulk of equipment would be imported, the foreign exchange component would be about 30%, or US$13.8 million.

ix. The benefits of the project would be measured by expenditures of guests staying at the complex, of whom the large majority would be foreign visitors. At the recently established official exchange rate of D 15.0 = US$1.0, the internal economic return of the investment would be 12.3%. On varying assumptions about occupancy, the exchange rate and the opening date of the complex, the internal economic return would range from 10-18%. When the proposed project is in full operation, the annual net foreign exchange earnings are estimated at US$14.7 million.

x. The project is suitable for a Bank loan of US$20.0 million equivalent for a term of 22 years including a grace period of 5 years. The amount of the loan is approximately equal to the maximum estimated foreign exchange component. To the extent that local currency financing may be involved, it would be justified on country economic grounds. The borrower would be the new entity, referred to in vi above.

# YUGOSLAVIA

## APPRAISAL OF THE BABIN KUK TOURISM PROJECT

## 1. INTRODUCTION

1.01 Early in 1969 the Government of the Socialist Federal Republic of Yugoslavia requested assistance from the Bank in developing tourism along the country's Adriatic coast and subsequently submitted three large scale tourism projects for detailed consideration, located at Portoroz on the northern Adriatic coast in Slovenia, at Dubrovnik in Croatia and at Budva on the southern coast in Montenegro.

1.02 The project at Dubrovnik is one of those recommended in the Physical Development Plan for the South Adriatic Region which was prepared in the past five years by an international team of Yugoslav and foreign planners with assistance from the UNDP.

1.03 The Dubrovnik project is an integrated tourism complex of 5,000 beds in nine hotels together with restaurants, shops, guest services and recreational facilities. It is one of the largest tourism complexes so far developed in Yugoslavia or abroad.

1.04 A project identification mission from the Bank visited Yugoslavia in November 1969. In the course of project preparation missions during 1970, the project was substantially modified. The appraisal mission consisting of Messrs. Scarisbrick, Boyd, Odone, Kulski (Consultant) and Calkins (Young Professional) completed its field work in November, 1970.

1.05 The loan for the Babin Kuk project would be the first Bank loan for tourism in Yugoslavia.

## 2. BACKGROUND

### A. The Economy

2.01 Yugoslavia is a Socialist Federal State comprising six republics, about the size of the United Kingdom. Its population of about 20 million is growing at the rate of 1% per annum. The gross national product at current market prices was estimated at US$12.0 billion equivalent in 1969 and per capita income at US$600 equivalent.

2.02 In 1965 the Yugoslav Government initiated basic economic reforms designed to de-centralize economic management and establish a market oriented economy. Following a period of adjustment and slow growth, real output

increased more rapidly from the middle of 1968 and grew by 9% in 1969. Increased investment, particularly in industrial expansion and diversification, and rising consumption generated sharp pressures on the balance of payments. The expansion of commodity exports did not keep pace with the growth of imports and earnings from "invisibles" became an increasingly important element in the balance of payments, particularly those from tourism which more than doubled during the four years to 1969 to become second in volume only to remittances from workers living abroad.

2.03 Since 1965 unemployment in Yugoslavia has steadily increased. In 1970 it was estimated to be 8% of the labor force in the socialized sector. Much of this increase reflects the gains in labor productivity stimulated by the reorganization of production after 1965. It also reflects a continuous migration of under-employed workers from rural to urban areas. A regional imbalance in unemployment levels is accompanied by a longstanding disparity in levels of income between the less and the more developed areas of the country. In recognition of this problem the Government has stressed the need for greater balance in the regional distribution of employment and income and the development of tourism, particularly on the southern Adriatic coast, will contribute to this objective.

2.04 The prospects for Yugoslavia's further economic development are, on the whole, favorable. The industriousness of her people, her sizable natural resources and proximity to European industrial nations provide the basis for continued expansion. Growth will, however, largely depend on the increase of earnings of foreign exchange, particularly of convertible currencies. Tourism is a sector where Yugoslavia has a comparative advantage and where the major part of foreign exchange earnings is in convertible currencies.

## B. The Tourism Sector

2.05 Yugoslavia, with over 2,000 kms of mountainous coastline of great scenic beauty, warm, dry summers and picturesque old coastal towns and villages, of which Dubrovnik is the most famous, possesses tourist attractions which compare favorably with any in the Mediterranean. These attractions together with the country's relative proximity to the major tourist generating centers of Europe constitute an important potential for the industry.

2.06 The fast growth of foreign tourism to Yugoslavia has been mainly a phenomenon of the past decade. Growing prosperity in Europe and more liberal entry policies to Yugoslavia brought a rising demand for travel to the country, while the implementation of certain key investments, particularly the construction of the Adriatic highway (partly finance by Loan 344-YU of 1963) and the rapid expansion of hotel capacity, made it possible to go far in meeting this demand. Foreign visitor nights spent in Yugoslavia increased more than five-fold over the decade to reach 22.4 million in 1969,

while estimated excursion traffic (those not staying overnight) increased from 1 million in 1960 to 30 million visitors in 1969.

2.07 Gross foreign exchange earnings from tourism including those arising from tourist transportation are officially estimated to have risen from US$22 million in 1960 to US$310 million in 1969, an average annual growth rate of 35%. As a proportion of total receipts from exports of goods and services, tourism receipts rose from 3% to 13% over this period.

2.08 Statistics of the impact of the growth of the sector on employment are incomplete. Between 1960 and 1969, 50,000 new jobs were created in tourism and catering in the socialized sector, which at present absorbs about 130,000 workers (3.5% of the total in employment). In addition small private ventures have developed (restaurants, pensions, etc.) particularly along the Adriatic coast, but statistics on these are not available.

2.09 The principal destinations of holiday visitors to Yugoslavia are resorts on the Adriatic coast where about 80% of foreign visitor nights are spent and almost two thirds of all hotel capacity is located. Most visitors to the northern coastal resorts arrive by road, particularly those from Italy, Germany and Austria, who together account for more than 50% of all stopover visitors. With the greater distances involved in reaching the southern Adriatic coast, air traffic plays a greater role. In consequence this is a higher priced market catering for a more select clientele, for whom Dubrovnik has been the principal destination.

2.10 As in other Mediterranean countries, Yugoslavia's foreign tourist traffic is rather seasonal with peaks in July and August. Domestic tourism in certain favored locations offsets to some extent the sharp seasonal fluctuations in foreign visitor traffic, and particular locations, for climatic and other reasons, have a longer season than the average for the coast. Dubrovnik is one of these, with annual bed-occupancies well above the average in Yugoslavia.

2.11 Recognizing the important contribution that tourism could make to earnings of foreign exchange, particularly of convertible currencies, the Federal and Republican Governments have taken a series of measures to assist the growth of the sector. Important among these were:

(i) the implementation of various tourism oriented infrastructure projects such as the Adriatic highway;

(ii) liberalization of restrictions on entry of foreign visitors;

(iii) the introduction of incentives for development of tourist facilities, including subsidies on bank funds lent for tourism investments, (Annex 1) higher foreign currency retention quotas for tourist enterprises than for other export industries, and exemption from the 3% Federal tax on salaries for personal incomes paid in the tourist industry;

(iv) the promotion of comprehensive regional plans with particular emphasis on tourism, such as the Physical Development Plan for the South Adriatic Region, undertaken in the past five years with assistance from the UNDP.

2.12 The various incentives to development have helped to bring about a major expansion of hotel capacity in the industry. From 1960-69 accommodation in hotels alone quadrupled, rising from 33,000 to 130,000 beds. Investment is continuing. The 1971-75 Draft Plan for the industry envisages a total investment exceeding $500 million, and additions to capacity of 100,000 to 120,000 hotel beds over this period. It also estimates foreign exchange earnings of US$900 million in 1975. These targets are ambitious. Nevertheless, Yugoslavia's present share of Mediterranean tourism is still modest; hotel capacity is only 6% of the total in OECD Mediterranean countries, and a slightly lower proportion of capacity in all Mediterranean countries. Despite the price increases which have occurred in the past decade, hotel and other tariffs in Yugoslavia are still 20-25% lower than in competing countries of the region. Assuming that this competitive advantage can be maintained, with vigorous development policies Yugoslavia should be able to achieve an increase in her share of Mediterranean tourism.

## 3. THE PROJECT

### A. Background

3.01 The town of Dubrovnik on Yugoslavia's southern Adriatic coast is at about the same latitude as Elba and Barcelona. Sheltered by high mountains from cold winds in winter, the climate compares favorably with other well-known Mediterranean resorts such as Nice and Monte Carlo, with warm dry summers and mild winters. (Table 1) The natural setting of coastal mountains, subtropical vegetation, a rocky and indented shoreline, pine-clad islands offshore and intensely blue sea, form a landscape both beautiful and dramatic. In this setting lies the old city of Dubrovnik, the capital of the ancient republic of Ragusa. Largely rebuilt after a great earthquake in 1667, the old city, encircled by massive walls and fortifications has been carefully preserved since that time. Romanesque, Gothic, Renaissance and Baroque monuments harmoniously coexist, and within the many churches, monasteries and palaces are important works of art, including paintings by Titian and Vasari. A summer festival of high artistic standards offering music, ballet, theatre and opera as well as a flourishing school of local painters and sculptors provides additional attractions for the tourist.

3.02 Until the 1960's Dubrovnik was accessible for foreign visitors only by sea. The opening of the Adriatic highway, and the expansion of Dubrovnik airport, now capable of handling planes up to the Boeing 707,

have made possible the great expansion of tourism to the area in the last decade. Regular direct year-round flights link Dubrovnik with Belgrade, Sarajevo, Zagreb and Rome. During the season from May to September regular direct flights also operate twice-weekly to a number of European cities including Athens, Venice, Vienna, Munich, Frankfurt, Zurich, Copenhagen, Amsterdam, Paris and London. The area is served also by charter flights from Scandinavia, the United Kingdom, Holland and Germany. Passenger and car-ferry services operate between Dubrovnik and other Adriatic and Ionian ports such as Split, Rijeka, Trieste, Bari and Piraeus.

The Project Site

3.03 The site for the project is a small peninsula within the town boundaries, approximately 4 km north of the old city. Partly pine-covered, the area slopes gently from a high point (altitude 100 m) to the sea. It has about 1.5 km of indented rocky coastline and about 0.5 km to the northeast is the small island of Daksa which has sandy beaches and dense woods. Because of its topography the site offers panoramic views of the sea and surrounding islands, and it has a slightly more favorable climate than the old city. It is the last large tract of undeveloped land fronting the sea within Dubrovnik's town boundaries (see map 1). During negotiations the sponsors of the project agreed that a condition of effectiveness of the proposed loan would be the acquisition of 73 ha of the project site. It was also agreed that the remaining 6 ha of the project site will be acquired by June 30, 1972 and that no construction contracts would be awarded until the whole 79 ha has been acquired.

The Concept

3.04 The concept of the project is that of an integrated tourist resort large enough to support a variety of facilities for sports and entertainment, restaurants, shops and services. The project is designed to cater for the resident guests and the substantial numbers of non-resident daily visitors who will be attracted by the variety and proximity of facilities available. The concept of the Babin Kuk tourism complex was conceived within the larger framework of the Master Plan for Dubrovnik, itself an integral part of the Physical Development Plan for the South Adriatic Region.

3.05 The project will include 9 hotels operated individually but participating in certain common services under the general direction of the project management. This will leave most day-to-day operations in units of easily manageable size. It will at the same time provide substantial operating economies from joint advertising and promotion, training and the purchase of supplies and from the provision of services such as heating and laundry which will be operated for the complex as a whole. There will also be a common computerized reservations system which will ease the handling of large groups, increasingly characteristic of modern tourism.

3.06 The concept of individual hotels under a single ownership operating under one overall direction permits the flexibility of opening and

closing units as required by seasonal fluctuations in traffic with consequential economies in operating and maintenance costs. There will also be economies in investment costs from providing project infrastructure including roads and parking spaces, marinas, swimming pools, shopping and entertainment centers on an integrated basis.

3.07 With so large a complex, careful consideration was given to the question of whether the project should be developed in stages. Demand is expected to be adequate by the mid 1970's, when the project will open to support the complex as a whole, and there would be serious disadvantages in a phased development. Important among these would be the unfavorable impact on visitor traffic caused by the disturbance resulting from construction over an extended period and the likelihood of additional costs arising from staged construction.

## B. Description

3.08 The project comprises a 5,000 bed hotel complex and communal centers with shops, restaurants, recreation facilities together with the necessary stores, service and other ancillary buildings. The beds would be distributed among a luxury class hotel (300 beds), four class A hotels (1,700 beds) and four class B hotels (3,000 beds). The class B hotels would remain open only during April-October.

3.09 The architectural concept is of multi-story hotels with extensive terraces and balconies. The complex will be placed on the higher parts of the sloping terrain, separated from the shore recreational facilities by an open green zone. The Dubrovnik Master Plan requires that this green zone containing rare tree specimens be conserved, and that the land be used only for recreational purposes which would not disturb the existing ecology of the area.

3.10 The varying ground conditions, landscape and micro-climate on different parts of the peninsula are factors which have defined the most suitable site for the various tourist facilities. The north western part of the Babin Kuk peninsula will contain the luxury and class A hotels for all year-round use. Class B hotels will be located to the northeast. (Map 2) The approximate total area of buildings is about 130,000 $m^2$ divided as follows: Luxury hotel 7.3%; class A hotels 34.2%; class B hotels 44.6%; shops and restaurants 4.5%; agencies and offices 1.5%; service center 7.8%.

3.11 There will be two commercial centers, one serving the year-round hotels and the other the class B hotels. These centers will contain shops, speciality restaurants, coffee shops, bars, as well as travel and tourist agencies, a bank, a post office and other public services.

3.12 Initially, parking for 1,100 cars will be built with a possible future expansion to about 1,700. This would be ample on the assumption

that about 25% of the guests will arrive by car resulting in about 85 parking spaces per 1,000 hotel beds. The complex is expected to serve mainly air-borne tourists who will travel from the airport by bus. To enable the tourists to travel by boat to the old city and neighboring islands, a harbor will be provided at the western end of the site.

3.13 The project includes staff housing because of the critical housing shortage in Dubrovnik and because the hotel complex will draw part of its staff from other parts of Yugoslavia. Fifty apartments and hostels with accommodations for 350 seasonal workers, approximately 18% of the estimated total staff, will be provided.

## C. Design and Planning

3.14 Architectural and city planning controls under the approved Master Plan of Dubrovnik are being strictly enforced by the municipal authorities with professional assistance from the Zagreb Urban Institute. The proposed project must conform to these regulations, which not only govern the use of the land but also the height, bulk and materials of buildings. The generalized land use plan, has already been approved as being in conformance with existing zoning regulations. Before the building permit is granted the detailed architectural studies of the hotel complex will also have to be approved by the municipality. In order to ensure that the final detailed architectural designs meet the operating requirements of the complex, the architects' brief will be developed with the assistance of the management consultants. The final site plan and architectural designs would be submitted to the Bank for approval.

## D. Cost Estimates

3.15 The estimated total cost and foreign exchange component of the project are summarized in the following table:

## Cost Estimate

(millions)

| | Dinars | | | US$ Equivalent | | | % of |
|---|---|---|---|---|---|---|---|
| | Local | Foreign | Total | Local | Foreign | Total | Project Cost |
| i. Land | 22.5 | - | 22.5 | 1.50 | - | 1.50 | 3.3 |
| ii. Construction | | | | | | | |
| Site Development | 40.3 | 11.1 | 51.4 | 2.69 | 0.74 | 3.43 | |
| Buildings | 224.3 | 61.9 | 286.2 | 14.95 | 4.13 | 19.08 | |
| Professional Fees* | 18.0 | 30.0 | 48.0 | 1.20 | 2.00 | 3.20 | |
| Sub-Total | 282.6 | 103.0 | 385.6 | 18.84 | 6.87 | 25.71 | 56.5 |
| iii. Equipment | 21.8 | 48.2 | 70.0 | 1.45 | 3.21 | 4.66 | 10.2 |
| iv. Housing | 6.9 | 2.0 | 8.9 | 0.46 | 0.13 | 0.59 | 1.3 |
| v. Staff Training and Pre-opening Expenses | 4.0 | 1.2 | 5.2 | 0.27 | 0.08 | 0.35 | 0.8 |
| vi. Management Assistance | 1.1 | 7.6 | 8.7 | 0.07 | 0.51 | 0.58 | 1.3 |
| vii. Project Administration | 4.9 | 1.5 | 6.4 | 0.33 | 0.10 | 0.43 | 0.9 |
| viii. Working Capital | 17.0 | - | 17.0 | 1.13 | - | 1.13 | 2.5 |
| Total before Contingency | 360.8 | 163.5 | 524.3 | 24.05 | 10.90 | 34.95 | |
| ix. Contingency | | | | | | | |
| Physical Increase | 31.8 | 15.0 | 46.8 | 2.12 | 1.00 | 3.12 | |
| Price Increase | 84.0 | 27.9 | 111.9 | 5.60 | 1.86 | 7.46 | |
| Sub-Total | 115.8 | 42.9 | 158.7 | 7.72 | 2.86 | 10.58 | 23.2 |
| TOTAL PROJECT COST | 476.6 | 206.4 | 683.0 | 31.77 | 13.76 | 45.53 | 100.0 |

* Includes cost of sewerage and traffic studies.

3.16 The total cost of the project is estimated at US$45.5 million. Unit construction costs of US$135.0 equivalent per $m^2$ were used in project

cost estimates, reflecting up-to-date construction costs of similar types of accommodation in Yugoslavia. Construction costs in Yugoslavia have increased at an average rate of about 12-1/2% annually since 1965 and this trend has recently accelerated. The dinar was devalued in January 1971 from D 12.5 to D 15.0 per U.S. dollar. It is very difficult, so soon after devaluation, to gauge its likely impact on domestic costs. In arriving at the price contingency, an 8% per annum increase has been assumed during the construction period for domestic costs and a 6% per annum increase for foreign costs. The 8% estimate of yearly domestic cost increases is based on construction price trends in Yugoslavia in the four years following the 1965 devaluation; the price contingency allowances can be regarded as prudently adequate. In addition a 10% physical contingency allowance for construction has been made, since final designs for the project have not yet been completed. For site development and equipment, a contingency allowance of 15% has been included to cover undefined soil conditions and unforeseen equipment needs. The details of the allowances provided for other components of the project are shown in Table 3. The overall provision for contingencies would amount to 23.2% of total project costs.

3.17 The standards of hotel accommodation under the proposed project are economical. The sizes of bedrooms and public areas have been based upon standards of similar hotels in Yugoslavia and abroad. Estimated unit costs of construction and equipment for different classes of hotels are shown below:

Project Hotels Unit Costs (US$)

| Hotel Category | Unit | Site Development | Building | Equipment | Total |
|---|---|---|---|---|---|
| Luxury | Bed Cost | 1,227 | 5,333 | 1,333 | 7,893 |
| Class "A" | Bed Cost | 566 | 3,294 | 647 | 4,507 |
| Class "B" | Bed Cost | 416 | 2,500 | 566 | 3,482 |

These costs are reasonable.

3.18 The foreign exchange component of the total project cost would depend upon the outcome of international bidding. The size of construction contracts would be large enough to attract foreign bids. Were such bids successful, and were the bulk of equipment to be imported, the foreign exchange component could be as high as 38% of total project cost. Should Yugoslav contractors win the bids and the bulk of equipment be obtained from domestic firms, the foreign exchange component would be about 24%. On the assumption that all construction contracts would be won by Yugoslav contractors and the bulk of equipment would be imported, as is probable, the foreign exchange component would be 30% of total project costs or US$13.8 million.

Amount of the Loan

3.19 The proposed loan of US$20 million would amount to 40% of the estimated total costs of the project of US$49.9 million including interest during construction. It would cover the foreign exchange costs of the project, estimated at US$13.8 million equivalent, interest and other charges on the Bank loan during construction, amounting to US$2.8 million and would provide about US$3.4 million equivalent for local currency financing. If all construction and equipment contracts were won by foreigners, the loan would approximate the full foreign exchange component of the project.

Disbursements

3.20 The loan would be disbursed on the basis of (a) identifiable foreign exchange costs of all imported equipment and professional services, (b) interest and other charges during construction and (c) an appropriate percentage of civil works and locally procured equipment. The estimated schedule of disbursements of the loan is shown in Table 4.

Procurement

3.21 Civil works contracts and contracts for equipment and furniture would be awarded under international competitive bidding. Items would be grouped to the extent practicable to encourage such competitive bidding. The proposed project is well within the capacity of the Yugoslav construction industry to implement, but it is expected that foreign contractors would submit bids. In evaluating bids, local equipment manufacturers would be allowed a preferential margin of 15% of the c.i.f. costs of competing imports or the level of customs duties generally applicable, whichever is the lower. During the loan negotiations, assurances have been obtained that a pre-qualification system, prepared by the consulting architects and engineers and acceptable to the Bank, is to be employed to ensure that only qualified contractors will be allowed to submit bids for construction.

## E. Execution

3.22 Consultant architects and engineers would be commissioned to design the project, including interior design and landscaping. They would be responsible for the preparation of master plans, specifications and working drawings. They would also supervise tendering, construction, and installation of equipment, and would approve payments. The conclusion of a contract between the borrower and the consultant architects, acceptable to the Bank, has been agreed as a condition of effectiveness of the proposed loan. This contract will include detailed project implementation programs.

3.23 A construction office headed by a full-time manager will be established for the construction of the project. The construction manager

will be directly responsible to the Director of Babin Kuk and will be appointed subject to approval by the Bank. It has been agreed that the construction manager will be appointed as a condition of effectiveness. The construction office will include on a full-time basis, architects, engineers, an equipment specialist, a procurement officer and an accountant, all with terms of reference acceptable to the Bank. The borrower has provided assurances that the construction office will be provided with sufficient supporting staff, office space, equipment, transportation and finance to enable it to function effectively. It has been agreed that the establishment of the construction office will be a condition of effectiveness of the proposed loan.

3.24 The consultant architects and engineers will prepare a manual of maintenance. During negotiations it was agreed that the borrower will provide assurances that adequate provision for maintenance as recommended in this manual would be made.

## 4. EXTERNAL INFRASTRUCTURE

4.01 The recent expansion of tourism in the Dubrovnik area has strained the commune's infrastructure facilities. There is need for more expenditious handling of the flow of aircraft, passengers and baggage passing through the airport; the access roads linking the Adriatic Highway with the area south east of the old city and the main streets leading from the new harbor area to the old city are subject to severe traffic congestion during the peak tourist season; while Dubrovnik's sewage system has been extended to service new hotel and commercial facilities, the system discharges untreated sewage into the sea at various points, resulting in heavy pollution in the port area and significant contamination along some parts of the coastline used for bathing and other recreational purposes. It is evident that the planned rapid expansion of tourism facilities, of which the Babin Kuk complex will be the major component, will aggravate these problems. (Annex 2).

4.02 It is estimated that by 1980 peak hour aircraft movements and passenger arrivals at the Dubrovnik airport will be more than three times those in the 1970 tourist season. The Airport Enterprise has developed with the help of consultants, a comprehensive program for staged expansion of the airport facilities. The Federal Government as guarantor has agreed to provide assurances that a first phase of the airport expansion program covering improvements and extension of the terminal, construction of a taxiway and an apron and the installation of additional lighting and other equipment, will be completed no later than December 31, 1974.

4.03 Based on present and projected demand, the present source of water for Dubrovnik will be adequate for many years to come, but additional transmission and pumping capacity will be needed by mid 1975. The cost of these additions is estimated at about US$1.0 million. To safeguard Dubrovnik as a prime tourism area, the city's entire sewerage system needs to be extended

and improved as soon as possible. The Federal Government has agreed to provide assurances that the municipality of Dubrovnik and the Dubrovnik Water and Sewerage Enterprise will: (i) complete the engineering studies for extending and improving the water supply and sewer-age systems; (ii) take action to ensure that the sections of the systems affecting the project will be completed in time for the opening of the proposed project; and (iii) endeavor to complete the full program by 1975, and in any case complete it within a few years thereafter. The proposed Bank loan includes US$150,000 to provide the foreign exchange component required in carrying out the engineering studies for extending and improving the water supply and sewerage systems. During negotiations it was agreed that this amount would be relent by the borrower to either the Municipality of Dubrovnik or the Dubrovnik Water and Sewerage Enterprise for the purpose of the studies.

4.04 Relatively minor improvements in the road system will be required to give better access to Babin Kuk from the rest of Dubrovnik, and from the Adriatic highway. The project would, however, intensify traffic congestion on Dubrovnik's main streets during the peak tourist season (except in the old city which is closed to general traffic). Solutions proposed so far for this problem would be expensive and of doubtful effectiveness. A different approach seems necessary, which may involve banning private vehicles from most of the town. The Federal Government has agreed to provide assurances that the municipality of Dubrovnik will: (i) complete the minor road improvements required for the project no later than December 31, 1974; (ii) commission a study by consultants of alternative solutions to the problem of peak season traffic congestion in Dubrovnik, with the consultants and their terms of reference being approved by the Bank. The proposed Bank loan includes US$150,000 to provide the foreign exchange component required in carrying out the traffic study. During negotiations it was agreed that this amount would be relent by the borrower to the Municipality of Dubrovnik for the purpose of the study. The borrower has agreed to present, before the start of operations, a plan for review by the Bank for transportation of guests between the complex and the old city.

4.05 The guarantor has asked the Bank for its assistance in financing the Dubrovnik infrastructure programs discussed above.

## 5. JUSTIFICATION

### A. Market Demand

5.01 With a slow recovery of tourist traffic to Dubrovnik in the aftermath of World War II and during the 1950's, it was not until 1959 that traffic caught up with the pre-war level. With improved transportation links, traffic in the 1960's expanded rapidly. Foreign tourist nights rose by 19% annually from 1961 to 1969 reaching 895,000 in the latter year. This fast growth was not matched by a comparable growth in capacity and the consequent rise in prices caused domestic tourists to seek cheaper accommodations else-

where. Hence domestic tourist nights spent in Dubrovnik almost halved between 1961 and 1967 but this trend was reversed in the next two years with a general expansion in Yugoslav domestic tourism. The overall annual growth in tourist nights from 1961-69 was 10.3%. (Table 5). This growth rate would have been faster had more capacity existed; substantial numbers of potential visitors were unable to secure accommodation during the peak season in recent years.

5.02 Though the four months, June to September are the months of highest foreign demand, substantial numbers of foreign visitors come also in March, April, May and October, and occupancies in class A hotels especially are high during these months. Many domestic tourists visit Dubrovnik in the off season, encouraged by large seasonal price reductions. These favorable factors have meant average annual bed occupanies in Dubrovnik's hotels (62% in 1969) much above the average for other Adriatic resorts: for example, the Slovenian coast (35%), Venice (36%) and Rimini (25%). Moreover occupancies in class A hotels have consistently been higher (74% in 1969) than in class B (57% in 1969) and class C hotels (46% in 1969), although the increase in capacity in class A hotels was much faster than in the lower categories over the past five years. The proportion of class A capacity to total hotel capacity is much greater in Dubrovnik than in most Yugoslav coastal resorts. These various factors point to the special characteristics of the foreign tourist market for Dubrovnik. It is mainly a richer clientele, whose interests are sight-seeing and culture as well as climate and the beach, and also one which is not entirely restricted to holidays in the peak summer season.

5.03 The growth in hotel capacity in the past five years has been wholly in classes A and B. Approximately 1,000 beds have been added, almost 800 in class A and about 250 in class B. There was a slight decline in class C hotel capacity and in supplementary accommodation. (Table 6) Total capacity amounted to almost 10,700 beds in 1969.

5.04 The expansion of hotel capacity envisaged for the next five years including the Babin Kuk project would add about 8,000 beds in higher class hotels - Luxury, A and B. There are no plans for expanding capacity in C class hotels or in supplementary accommodation. Of the 8,000 beds, 5,000 would be in Luxury and class A hotels and 3,000 in class B hotels. This proportion is approximately in line with past growth in traffic to the different classes of accommodation, but also provides for a substantial growth in middle level capacity which could appeal especially to larger groups travelling on charter flights.

5.05 In Dubrovnik the growth of traffic is mainly dependent on the growth of capacity. With adequate promotion and satisfactory service at competitive prices, a large increase in capacity there, amounting to only a small fraction of capacity in all comparable (competitive) destinations, can be sold.

5.06 A holiday in Dubrovnik is within reach of a small but rapidly growing section of the tourist market in western Europe, which supplies the bulk

of foreign visitors to Yugoslavia. Germany, the U.K. and the Netherlands accounted for about half of total visitors nights in recent years. For destinations comparable in price with Dubrovnik, vacation visitor arrivals have risen considerably in recent years, and the growth rate may well increase as European incomes rise. The recent rise in domestic visitor traffic to Dubrovnik also seems likely to continue.

5.07 An analysis of the likely growth in the different categories of visitor traffic to Dubrovnik and of hotel occupancies as new capacity is added in the next five years shows that with a growth in visitor nights equivalent to an average of 12.4% annually from 1969 to 1977, and no change in seasonality, average hotel occupanies will decline in 1975 with the large additions to capacity projected for that year, but should be almost back to current high levels by 1977-78. (Annex 3). These assumptions appear reasonable in that the growth and pattern of traffic they imply are not out of line with Dubrovnik's past development trends or the likely developments in originating markets. Moreover the new hotels will cater for both new traffic and previously unsatisfied demand.

## B. Economic Justification

### Economic Return

5.08 The quantifiable net benefits from the project consist of visitors' expenditures in the complex less the costs (excluding depreciation, taxes and interest payments) of operating the project. The investment is the capital cost of the project itself plus the share of the cost of external infrastructure properly chargeable to the project, which is estimated at approximately US$1.0 million.

5.09 Additional benefits would be derived from visitors' expenditures outside the project to the extent that these do not require additional investments but enable a fuller utilization of existing capacity to be made. It has not been possible to quantify such benefits with much precision. Sample studies indicate, however, that up to 38% of tourists' total daily expenditures in Dubrovnik are for goods and services other than accommodation and food. This high proportion is attributable to the sophisticated clientele visiting Dubrovnik and the comprehensive range of opportunities available for such expenditures ranging from the traditional souvenir trade through to the famous Dubrovnik festival of arts and music. These external effects are therefore quite sizable and are not reflected in the measure of the overall economic benefits which the Yugoslav economy is likely to derive from the operation of the project.

5.10 With an estimated economic life of the project of 25 years and at the present rate of exchange of D 15.0 to US$1.0, the internal economic return on the project would be 12.3%. As approximately 90% of visitor expenditures would represent receipts of foreign exchange, the rate of return would be highly sensitive to any change in the foreign exchange rate.

The results of sensitivity testing indicate that the rate of return would also be highly sensitive to changes in occupancy levels and a delay in opening (Annex 4). At the time of appraisal, the rates for the dinar in various grey markets ranged from D 15.0 to D 18.0 = US$1.0. Taking also into account varying assumptions about occupancy levels and the opening date, the internal economic return could range from 9% with the worst combination of variables to almost 18% with the best combination. The best estimate of the economic rate of return is 16.9%.

Foreign Exchange Earnings

5.11 When the proposed project is fully operational the annual net foreign exchange earnings are estimated at US$14.7 million equivalent. This compares with the estimated foreign component in total investment costs plus interest during construction of US$16.6 million.

## 6. ORGANIZATION AND MANAGEMENT

### A. The Sponsor - Minceta

6.01 The project sponsor - the enterprise Minceta - is a wholesale and retail business formed by amalgamation of several small enterprises in 1962, trading in general merchandise mainly in the Dubrovnik area. Minceta has a record of successful sales growth, accompanied by an even faster rise in profitability and reinvestment of funds. The rapid growth and a heavy build-up of inventories as an inflation hedge, has resulted in a continuing problem of illiquidity, which could prove serious were economic conditions to change. Minceta's top management is dynamic and flexible, though the management structure is thin, and net worth (almost US$2.0 million equivalent at the end of 1969) very small in relation to the project. Tables summarizing Minceta's financial growth are attached (Tables 7 and 8).

6.02 Minceta's management originally proposed that the Babin Kuk project should be an integral part of the Minceta enterprise, operated as a division. In addition to the Babin Kuk project, however, Minceta has plans for further expansion both by entering new business activities and by absorption of other enterprises. Acceptance of this proposal would have meant the exposure of the project to the risk entailed in all future activities of Minceta as well as a potential liability for all Minceta's future debts. It would have required extensive supervision of all Minceta's activities by the Bank, almost all unrelated to the tourism project. It has, therefore, been agreed with Minceta that a legal separate unit should be formed to construct Babin Kuk and operate it subsequently.

## B. The Borrower

6.03 The borrower of the Bank loan would be the new entity to be called "Babin Kuk" Hotel Tourist Center, Dubrovnik (hereinafter referred to as BKHTC). BKHTC would be somewhat analogous, in Western terms, to a subsidiary company whose sole shareholder would be Minceta. The detailed provisions of the relationship between the two entities will be covered in a joint venture contract. During negotiations agreement was reached on a definitive version of the contract.

6.04 This contract is designed to provide for the assets of the project to be protected from any future creditors of Minceta, for the introduction of Minceta's equity investment and for the rights, duties, obligations and undertakings governing the relationship between Minceta and BKHTC, including a formula providing that 45% of annual net profits or losses is attributable to Minceta.

6.05 During negotiations it has been agreed that prior to the presentation of the loan to the Executive Directors the separate legal entity BKHTC will be formed and that the contract regulating the relationship between Minceta and BKHTC will be signed. Changes in the terms of this contract or in the relationship between Minceta and BKHTC will be subject to approval by the Bank.

## C. Organizational Structure

6.06 The operational management of the complex would be exercised by the Director of BKHTC over whose appointment the Bank would have the right of approval initially and for the first three years of operation of the project. The Director would be a member of a "Business Committee", consisting in addition to himself, of 3 representatives of Minceta and 1 representative of BKHTC. This committee would be responsible for the determination of overall policy. The appointment of the Director of BKHTC is a condition of effectiveness of the proposed loan.

6.07 Subject to modifications which may be suggested by the management consultants referred to below, the Director of BKHTC should have three operational assistants reporting to him. One would be responsible for the operations of the hotels, restaurants and bars. The managers of the 9 individual hotels would report to him. The second would be responsible for entertainment, recreation and guest service functions, and the third would be responsible for the centralized services of hotel reservations, food pre-preparation, laundry, heating, transportation, storage and repairs and maintenance. In addition, those responsible for Public Relations and General Administration covering the functions of central purchasing, accounting and internal audit, personnel and information, would report to the Director. A chart of the proposed management organization is attached (Chart 2).

## D. Management Consultants

6.08 The creation of a successful management structure for the complex may be divided into two distinct but inter-dependent phases. The first or pre-opening phase would be concerned with developing and coordinating the systems and procedures and with recruiting and training the key personnel required to achieve the operating standards set for the project. The second or "post-opening" phase would be concerned with operating the complex using the systems, procedures and staff developed in the pre-opening phase and introducing changes indicated by actual operating experience.

6.09 To realize fully the economies of scale presented by the project, problems and difficulties, most of which have not generally faced the tourism industry before, will have to be successfully identified and overcome. To provide sufficient resources both to identify these problems and devise and implement the solutions, Minceta has agreed to retain qualified consultants.

6.10 It is true that, because of the uniqueness of the project, no organization or consultant can have had actual experience of the problems that will be posed by Babin Kuk. The solution must be to blend the knowledge and experience of the best management consultants, the expertise available in the international hotel industry and local Yugoslav resources to create a team which is capable of developing the management systems prior to opening the complex and has the ability to adapt and amend them during the operational life of the project after the consultants have departed. Minceta has decided to seek the help of foreign management consultants in this task.

6.11 The consultants' assignment would last for at least the 4 years of construction and the first 18 months of operation. They would be responsible to BKHTC for the development, coordination and implementation of the management and operational systems and for the selection and training of top and middle management personnel. Before rejecting any of the consultants' proposals, BKHTC would seek the approval of the Bank which will need to maintain close contact and supervision of the pre-opening and post-opening phases of the project.

6.12 The firm of management consultants selected and the detailed contract and terms of reference will all be subject to Bank approval. It is a condition of effectiveness of the proposed loan that the contract between the borrower and the management consultants be signed.

# 7. FINANCE

## A. Financing Plan

7.01 The total estimated financial requirements of the project together with interest during construction are expected to be provided as follows:

Financing Plan
(US$ million)

| | Estimated Project Cost | Interest During Construction | Total | % of Total |
|---|---|---|---|---|
| Equity - Minceta | 9.50 | | 9.50 | 19.0 |
| Long-Term Debt | | | | |
| Privredna Banka Zagreb (via Minceta) | 17.70 | 1.58 | 19.28 | 38.6 |
| IBRD | 17.20 | 2.80 | 20.00 | 40.1 |
| | 44.40 | 4.38 | 48.78 | |
| Working Capital - Minceta | 1.13 | | 1.13 | 2.3 |
| | 45.53 | 4.38 | 49.91 | 100.0 |

7.02 Minceta's equity contribution of US$9.50 million equivalent will include cash in the amount of US$8.00 million, and land valued at US$1.50 million. Most of this land has already been acquired by Minceta. As a condition of effectiveness, however, acquisition of the 73 ha of site area must be verified. Minceta's cash equity contribution (US$8.0 million) is to be obtained from a loan to Minceta from the Privredna Banka of Zagreb, the largest investment bank of Croatia. The working capital of US$1.13 million will be provided by Minceta.

7.03 It should be noted that the usual concept of equity and its relationship to risk is not fully applicable in the Yugoslav context. The workers of BKHTC will have the assets of the enterprise assigned to them by the state, rights over its income and bear some of the commercial risk, since their income would be reduced to some extent in the event of losses. They will give up a percentage of net profits to Minceta for a specified time under a joint venture contract. Outside the terms of this contract, Minceta will not legally have rights of equity in the usual sense. Only a portion of the benefits of the high leverage in this loan will accrue to the sponsor, Minceta; the major share will go to BKHTC's workers and to build up BKHTC's financial position. As is usual in Yugoslavia and as noted below, the bulk of the dinar financing will be provided by a local bank on terms so favorable as to constitute quasi-equity. The proposed financial structure is acceptable in the light of these considerations.

7.04 Minceta's loan to BKHTC of US$17.70 million equivalent is to be financed also from a loan from the Privredna Banka, Zagreb. Under an agreement dated July 17, 1969, the Privredna Banka agreed to lend Minceta up to D 320.0

million (US$21.34 million equivalent) for BKHTC. It has been agreed that D 120 million (US$8.0 million equivalent) of this total is to be invested by Minceta as equity in BKHTC. Privredna Banka has confirmed that in accordance with its normal practice an additional amount will be provided to cover interest during construction. The agreement of July 17, 1969, was made prior to investment costs being revised, and Privredna Banka has agreed to provide all the additional funds required plus interest during construction. In addition assurances were obtained during negotiations that Minceta and the Privredna Banka would be jointly and severally liable to cover possible cost over-runs. The loan from Privredna Banka would be for thirty years including a grace period of five years. The loan from Minceta to BKHTC would be for the same period and it would be subordinated to the proposed loan from the Bank.

7.05 Both the Federal and the Croatian Governments subsidize the interest rates payable on long-term loans made by the banks for tourism projects. These subsidies will apply to the loans provided by the Privredna Banka. The Bank's loan would not be eligible for either subsidy. The Federal subsidy effectively reduces the interest rate charged to the project by the Privredna Banka to 4%. The subsidy of 1% from the Republic of Croatia is paid direct and reduces the effective interest rate paid by the project to 3% on the local loan. It has been agreed that the Republic of Croatia interest subsidy received by Minceta in respect of the loan capital provided by Privredna Banka and relent to Babin Kuk will be passed on to Babin Kuk in full at least until the end of the first three full years of the operation of the project. At the conclusion of this period one-half of the Republic subsidy will be passed on by Minceta for a further three full years of operation. Thereafter Minceta may retain the subsidy in full or in part unless the financial condition or profitability of Babin Kuk warrants otherwise. A table showing the effect of the subsidies is included in Annex 5.

7.06 The Yugoslav interest rate subsidy system for investments in the enlargement of tourist accommodation facilities is similar to that used by other major Mediterranean tourism countries, including France, Italy, Spain, Greece and Morocco. The area is the center of European mass tourism, which requires low-cost facilities and where non-commercial accommodation influences the prices that can be charged by hotels. The subsidy system is based on the justification that success in attracting additional foreign tourists and thus achieving a significant increase in net foreign exchange earnings is of much broader benefit to the economy as a whole than indicated by the financial return to the project itself. The subsidies are thus a means of creating financial conditions favorable enough to attract investments for projects which have a relatively modest financial, but a satisfactory economic return and give rise to sizable external economic benefits. As already noted, the use of these subsidies is now widespread throughout the Mediterranean basin and cannot be abandoned by any one country without running the risk that some of its new hotels will be unable to compete successfully. These considerations apply to the competitive position of the Babin Kuk project vis-a-vis both its local and foreign competitors.

7.07 It is proposed that the IBRD loan be made directly to BKHTC for a term of 22 years, including a grace period of five years to cover the construction period and the first operating year. Minceta has agreed to guarantee the loan.

## B. Financial Forecasts

7.08 Forecasts of annual earnings, financial position and cash flow for the first 20 years of the project are presented in Annex 5, together with details of operating assumptions. Projected earnings are summarized below:

Projected Annual Earnings
(US$ Million)

| Year Ending December 31: | 1975 | 1976 | 1977 | 1980 | 1990 |
|---|---|---|---|---|---|
| Operating Year | 1 | 2 | 3 | 6 | 16 |
| Average Annual Hotel Occupancy (%) | 47 | 54 | 57 | 57 | 57 |
| Total Sales | 17.7 | 21.3 | 22.4 | 22.4 | 22.4 |
| Net Profit before Interest | 0.9 | 3.0 | 3.4 | 3.7 | 3.7 |
| As % of Original Investment /1 | 1.9 | 6.0 | 6.9 | 7.4 | 7.4 |

/1 Operating profit before interest but after depreciation and deferred expenses as % of invested capital of US$49.91 million.

7.09 A detailed financial analysis was made by Kienbaum-Steigenberger, consultants to Minceta, on the basis of local cost and revenue estimates prepared by the Institute of Economics and Planning, Dubrovnik. This has been revised by the Bank. The assumptions and estimates used are consistent with both local and international experience. The tariffs are approximately the same as the 1970 rates charged in comparable Dubrovnik hotels adjusted to reflect the price increases expected by 1975 when the project opens. The 1975 full pension tariff would range from about US$10.0 to US$24.0 depending on hotel class and season. The operating costs have been estimated on a conservative basis.

7.10 The financial rate of return on the project, estimated on a discounted cash flow basis for the first 25 years of operation, would be 9.93% In the event that the project opening were to be delayed by one year, the financial rate of return would be reduced to 8.93%. Assuming an occupancy level of 54% instead of 57% in the typical year, (i.e., from 1977 onward) the financial rate of return would be 9.1%. The impact of these alternate assumptions on the projected cash flow indicates that the project should be able without difficulty to meet its debt service obligations.

7.11 A forecast of Balance Sheets and financial ratios is summarized below:

Projected Balance Sheets and Financial Ratios
(US$ million)

| Year Ending December 31: | 1975 | 1976 | 1977 | 1980 | 1990 |
|---|---|---|---|---|---|
| Operating Year: | 1 | 2 | 3 | 6 | 16 |
| Current Assets | 6.05 | 8.52 | 8.99 | 7.62 | 5.40 |
| Current Liabilities | 4.31 | 5.16 | 4.95 | 4.98 | 6.16 |
| Net Working Capital | 1.74 | 3.36 | 4.04 | 2.64 | (0.76) |
| Total Net Assets | 47.99 | 47.08 | 46.04 | 42.71 | 29.13 |
| Long Term Debt | 38.20 | 36.78 | 35.31 | 30.57 | 9.84 |
| Original Equity & Retained Earnings | 9.79 | 10.30 | 10.73 | 12.14 | 19.29 |
| Long-Term Debt Service Coverage | - | 2.3:1 | 1.7:1 | 1.7:1 | 1.7:1 |
| Long-Term Debt/Equity Ratio | 80:20 | 78:22 | 77:23 | 72:28 | 34:66 |

7.12 Equity capital and loan capital from Minceta will be provided equally until the cash equity capital reaches the agreed figure of US$8 million equivalent. It has been agreed that Minceta will receive 45% of the net profits after providing for interest payments and depreciation. BKHTC will not be liable for taxes on profits. The balance of net profits would under Yugoslav law be available for retention in the business or for distribution to the workers in the enterprise.

7.13 In view of the heavy reliance on loan financing normal in the case of new enterprises in Yugoslavia, the build-up of equity from retained earnings is desirable. During negotiations agreement has been reached that not less than 20% of the net profits would be retained in the business.

7.14 With the build-up of retained earnings, BKHTC may find opportunities for profitable investment elsewhere. It has been agreed that capital expenditures, other than for replacement, in excess of US$100,000 equivalent will be made only after consultation with the Bank.

7.15 Accounts and financial statements will be kept by BKHTC in a form acceptable to the Bank. Audited financial statements in a form acceptable to the Bank will be presented to the Bank within four months of the close of the financial year.

## 8. RECOMMENDATIONS

8.01 During loan negotiations, the terms of the contract between Minceta and BKTHC were agreed and assurances were obtained that:

(i) any change in the relationship between Minceta and BKHTC or in the terms of the contract between them would be subject to approval by the Bank (para. 6.05);

(ii) a pre-qualification system prepared by the consulting architects and engineers and acceptable to the Bank would be employed to ensure that only qualified contractors would submit bids for construction contracts (para. 3.21);

(iii) architects and engineers, acceptable to the Bank, would be appointed to design the project and supervise its execution, with terms of reference and on conditions approved by the Bank (para. 3.22);

(iv) a construction office would be set up, headed by a full-time construction manager acceptable to the Bank, and with adequate supporting staff for the execution of the project (para. 3.23);

(v) before the start of operations, a plan would be prepared for review by the Bank for the transport of guests between Babin Kuk and the old city (para. 4.04);

(vi) the appointment of the Director of BKHTC would be subject to the approval of the Bank (para. 6.06);

(vii) Management consultants acceptable to the Bank would be employed by the borrower with terms of reference and on conditions approved by the Bank (para. 6.12);

(viii) Minceta and/or Privredna Banka would provide funds needed to meet cost over-runs (para. 7.04);

(ix) the equity capital due from Minceta to BKHTC would be provided equally with loan capital until the agreed US$8.0 million equivalent of equity has been provided by Minceta (para. 7.12);

(x) not less than 20% of the net profits would be added to retained earnings annually (para. 7.13);

(xi) capital expenditures, except for replacement, in excess of US$100,000 equivalent would be committed only after consultation with the Bank (para. 7.14).

8.02 During loan negotiations, the guarantor has agreed to provide assurances that:

(i) the first stage of the expansion program for Dubrovnik airport would be completed not later than December 31, 1974 (para. 4.02);

(ii) the extension and improvement of those sectors of Dubrovnik's water and sewerage systems affecting Babin Kuk would be completed in time for the opening of the project (para. 4.03);

(iii) the road improvements in Dubrovnik required to improve access to Babin Kuk from the rest of Dubrovnik and the Adriatic highway would be completed not later than December 31, 1974 (para. 4.04);

(iv) a study to propose solutions to the problem of peak season traffic congestion in Dubrovnik would be commissioned, the consultants and their terms of reference to be approved by the Bank (para. 4.04);

8.03 During negotiations the following conditions of effectiveness of the proposed loan have been agreed:

(i) the Director of BKHTC shall have been appointed (para. 6.06);

(ii) staff members of the construction office shall have been employed and have taken up their duties (para. 3.23);

(iii) conclusion of contracts between the borrower and the architectural and engineering consultants and the management consultants (para. 3.22 and 6.12);

(iv) confirmation of the borrower's clear title to 73 ha of the project site (para. 3.03).

8.04 It has also been agreed that the borrower's failure to acquire the remaining 6 ha of the project site by June 30, 1972 can lead to the proposed loan being suspended and that no contracts for construction will be awarded until all the land has been acquired.

8.05 With the indicated assurances, the proposed project provides a suitable basis for a Bank loan of US$20.0 million for a term of 22 years including a 5 year grace period.

Table 1

YUGOSLAVIA: Babin Kuk Tourism Project

AVERAGE MONTHLY TEMPERATURES IN SELECTED MEDITERRANEAN RESORTS
(in degrees fahrenheit)

| Month | Barcelona | S.Remo | Nice | Venice | Rijeka | Dubrovnik |
|---|---|---|---|---|---|---|
| January | 49.0 | 48.0 | 48.5 | 39.5 | 41.5 | 48.4 |
| February | 51.5 | 48.5 | 49.0 | 42.0 | 43.1 | 48.4 |
| March | 55.0 | 51.5 | 52.5 | 47.5 | 46.9 | 51.4 |
| April | 58.5 | 58.5 | 57.5 | 57.5 | 53.6 | 57.2 |
| May | 64.5 | 62.5 | 63.0 | 64.0 | 62.1 | 64.0 |
| June | 71.0 | 69.0 | 69.0 | 71.0 | 68.9 | 71.8 |
| July | 76.0 | 75.0 | 75.5 | 75.0 | 72.7 | 75.9 |
| August | 76.0 | 74.0 | 74.5 | 74.0 | 72.5 | 76.3 |
| September | 69.5 | 70.5 | 70.0 | 69.5 | 66.9 | 70.9 |
| October | 63.0 | 63.0 | 62.5 | 57.5 | 58.5 | 63.9 |
| November | 55.0 | 55.5 | 55.0 | 48.5 | 49.8 | 56.8 |
| December | 50.5 | 50.5 | 49.5 | 42.0 | 45.5 | 52.0 |

Source: Meteorological Office, Great Britain.
(Air Ministry)

December, 1970

YUGOSLAVIA: BABIN KUK TOURISM PROJECT

BREAKDOWN OF COST *

| No. of Units | Type of Accommodation | Area (in $m^2$) | Cost of Site Development (in US$'000) | Cost of Construction (in US$'000) | Cost of Equipment (in US$'000) | Cost of Professional Services (in US$'000) | Cost of Physical Facilities (in US$'000) | Cost of Physical Facilities (in Yug. Din'000) | Cost of Project Administration (in US$'000) | Cost of Management and Staff Training (in US$'000) | TOTAL * (in US$'000) | TOTAL * (in Yug. Din.'000) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | HOTELS | | | | | | | | | | | |
| 1 | Luxury Class Hotel (300 beds) | 9,500 | 368 | 1,600 | 400 | 300 | 2,668 | | | | | |
| 4 | Class A Hotel (1700 beds) | 44,500 | 963 | 5,600 | 1,100 | 1,000 | 8,663 | | | | | |
| 4 | Class B Hotel (3000 beds) | 58,000 | 1,249 | 7,500 | 1,700 | 1,200 | 11,649 | | | | | |
| | Sub-Total | 112,000 | 2,580 | 14,700 | 3,200 | 2,500 | 22,980 | 344,700 | | | | |
| | HOUSING | | | | | | | | | | | |
| 50 | Dwelling Units (150 beds) | | | 450 | | | 450 | | | | | |
| 1 | Hostel (350 beds) | | | 140 | | | 140 | | | | | |
| | Sub-Total | | | 590 | | | 590 | 8,850 | | | | |
| | ANCILLARY FACILITIES | | | | | | | | | | | |
| 14 | Restaurants | 2,500 | 110 | 600 | 360 | 100 | 1,170 | | | | | |
| 22 | Shops | 2,500 | 120 | 700 | 120 | 100 | 1,040 | | | | | |
| | Public Facilities | 2,000 | 90 | 500 | 120 | 100 | 810 | | | | | |
| | Service Facilities | 11,000 | 530 | 2,580 | 860 | 400 | 4,370 | | | | | |
| | Sub-Total | 18,000 | 850 | 4,380 | 1,460 | 700 | 7,390 | 110,850 | | | | |
| | Total before Contingencies | 130,000 | 3,430 | 19,670 | 4,660 | 3,200 | 30,960 | 464,400 | 430 | 930 | 32,320 | 484,800 |
| | Physical Increase | | 510 | 1,910 | 700 | | 3,120 | | | | 3,120 | |
| | Price Increase | | 630 | 5,280 | 1,130 | | 7,040 | | 150 | 270 | 7,460 | |
| | Total Contingencies | | 1,140 | 7,190 | 1,830 | | 10,160 | 152,400 | 150 | 270 | 10,580 | 158,700 |
| | CUMULATIVE TOTAL | | 4,570 | 26,860 | 6,490 | 3,200 | 41,120 | 616,800 | 580 | 1,200 | 42,900 * | 643,500 |
| | Foreign Exchange Component % | | 20.7% | 20.7% | 67.6% | 62.5% | 31.3% | | 22.4% | 61.7% | 32.1% | |
| | Total Foreign Exchange | | 950 | 5,550 | 4,390 | 2,000 | 12,890 | 193,350 | 130 | 740 | 13,760 | 206,400 |
| | Estimated Disbursement of Loan by Sector, % | | 31.6% | 31.6% | 67.6% | 62.5% | 39.7% | | 22.4% | 61.7% | 40.1% | |
| | Total Disbursement | | 1,445 | 8,495 | 4,390 | 2,000 | 16,330 | 244,950 | 130 | 740 | 17,200 | 258,000 |
| | Interest and Other Charges during Construction | | | | | | | | | | 2,300 | 42,000 |
| | TOTAL LOAN | | | | | | | | | | 20,000 | 300,000 |

* Excluding land and working capital

Table 2

February, 1971

## YUGOSLAVIA: BABIN KUK TOURISM PROJECT

## CONTINGENCY ALLOWANCES

| | Site Development | | Buildings | | Professional Fees | | Equipment | | Housing | | Project Administration | | Management and Staff Training Assistance | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Local | Foreign | Local | Foreign | Local | Foreign | Local | Foreign | Local | Foreign | Local | Foreign | Local | Foreign | Total |
| Allowances for Physical Increase | 15% | | 10% | | - | | 15% | | - | | - | | - | | |
| Allowances for Price Increase | 17% | 12% | 26% | 19% | - | | 26% | 19% | 26% | 19% | 36% | 26% | 36% | 26% | |
| Total Cost Before Contingencies (US$ millions) | 2.69 | .74 | 14.95 | 4.13 | 1.20 | 2.00 | 1.45 | 3.21 | .46 | .13 | .33 | .10 | .34 | .59 | 32.32 |
| Allowances for Physical Increase (US$ millions) | .40 | .11 | 1.50 | .41 | - | - | .22 | .48 | - | - | - | - | - | - | 3.12 |
| Sub-total (US$ millions) | 3.09 | .85 | 16.45 | 4.54 | 1.20 | 2.00 | 1.67 | 3.69 | .46 | .13 | .33 | .10 | .34 | .59 | 35.44 |
| Allowances for Price Increase (US$ millions) | .53 | .10 | 4.28 | .86 | - | - | .43 | .70 | .12 | .02 | .12 | .03 | .12 | .15 | 7.46 |
| Total, Including Contingencies (US$ millions) | 3.62 | .95 | 20.73 | 5.40 | 1.20 | 2.00 | 2.10 | 4.39 | .58 | .15 | .45 | .13 | .46 | .74 | 42.90 |

January 1971

Table 3

Table 4

YUGOSLAVIA: Babin Kuk Tourism Project

ESTIMATED SCHEDULE OF DISBURSEMENTS
(including interest on construction and other charges)

| IBRD Fiscal Year and Quarter | Cumulative Disbursement at end of Quarter |
|---|---|
| | US$ '000 |
| 1971-1972 | |
| December 31, 1971 | 30 |
| March 31, 1972 | 386 |
| June 30, 1972 | 927 |
| 1972-1973 | |
| September 30, 1972 | 1,548 |
| December 31, 1972 | 2,179 |
| March 31, 1973 | 3,822 |
| June 30, 1973 | 4,595 |
| 1973-1974 | |
| September 30, 1973 | 5,298 |
| December 31, 1973 | 6,011 |
| March 31, 1974 | 7,193 |
| June 30, 1974 | 9,284 |
| 1974-1975 | |
| September 30, 1974 | 11,878 |
| December 31, 1974 | 13,594 |
| March 31, 1975 | 15,430 |
| June 30, 1975 | 16,512 |
| 1975-1976 | |
| September 30, 1975 | 18,221 |
| December 31, 1975 | 20,000 |

January, 1971

Table 5

YUGOSLAVIA: Babin Kuk Tourism Project

Growth of Tourist Traffic to Dubrovnik, 1961-1969
('000 bednights)

| | - 1961 - | | - 1967 - | | - 1969 - | |
|---|---|---|---|---|---|---|
| | Number | Percent | Number | Percent | Number | Percent |
| Domestic | 310.6 | 58.6 | 185.6 | 19.5 | 262.6 | 22.7 |
| Foreign | 219.0 | 41.4 | 763.8 | 80.5 | 895.2 | 77.3 |
| Total | 530.0 | 100.0 | 949.4 | 100.0 | 1157.8 | 100.0 |

Table 6

Development of Dubrovnik's Accommodation Capacity, 1965-1969
(Number of Beds)

| | - 1965 - | - 1966 - | - 1967 - | - 1968 - | - 1969 - |
|---|---|---|---|---|---|
| Hotel Class A | 505 | 889 | 889 | 1,016 | 1,295 |
| Hotel Class B | 1,171 | 1,253 | 1,365 | 1,385 | 1,425 |
| Hotel Class C | 600 | 637 | 591 | 631 | 504 |
| Total | 2,276 | 2,779 | 2,845 | 3,032 | 3,224 |
| Supplementary Accommodation | | | | | |
| Private Rooms | n.a. | 6,642 | n.a. | n.a. | 7,040 |
| Other | n.a. | 4,152 | n.a. | n.a. | 3,633 |
| Total | | 10,794 | | | 10,673 |

December 9, 1970

YUGOSLAVIA: Babin Kuk Tourism Project

MINCETA'S FINANCIAL RECORD OF GROWTH 1962-9

(Income Statements)
(Din Million)

| | 1962 | % | 1963 | % | 1964 | % | 1965 | % | 1966 | % | 1967 | % | 1968 | % | 1969 1/ | % | Trend Index 1962 = 100 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Gross Sales (after rebates) | 26.7 | 100 | 33.0 | 100 | 43.7 | 100 | 62.5 | 102.3 | 80.1 | 113.5 | 100.7 | 109.7 | 136.1 | 108.5 | 160.4 | 110.9 | 601 |
| Less Sales Tax 2/ | - | - | - | - | - | | 1.4 | 2.3 | 9.5 | 13.5 | 8.9 | 9.7 | 10.7 | 8.5 | 15.7 | 10.9 | - |
| Net Sales | 26.7 | 100 | 33.0 | 100 | 43.7 | 100 | 61.1 | 100.0 | 70.6 | 100.0 | 91.8 | 100.0 | 125.4 | 100.0 | 144.7 | 100.0 | 542 |
| Cost of Sales | 22.1 | 82.8 | 27.1 | 82.1 | 35.6 | 81.5 | 51.8 | 84.8 | 56.9 | 80.6 | 70.6 | 76.9 | 103.8 | 82.8 | 119.8 | 82.8 | 542 |
| Gross Margin | 4.6 | 17.2 | 5.9 | 17.9 | 8.1 | 18.5 | 9.3 | 15.2 | 13.7 | 19.4 | 21.2 | 23.1 | 21.6 | 17.2 | 24.9 | 17.2 | 541 |
| Operating Costs | 2.8 | 10.5 | 2.8 | 8.5 | 4.4 | 10.1 | 6.7 | 11.0 | 9.5 | 13.5 | 13.1 | 14.3 | 14.4 | 11.5 | 17.8 | 12.3 | 636 |
| Net Operating Income | 1.8 | 6.7 | 3.1 | 9.4 | 3.7 | 8.4 | 2.6 | 4.2 | 4.2 | 5.9 | 8.1 | 8.8 | 7.2 | 5.7 | 7.1 | 4.9 | 394 |
| Extraordinary Income | 0.5 | 1.9 | 0.2 | 0.6 | 0.4 | 0.9 | 0.4 | 0.7 | 0.5 | 0.7 | 0.9 | 1.0 | 2.1 | 1.7 | 5.2 | 3.6 | 1,040 |
| Total Net Income | 2.3 | 8.6 | 3.3 | 10.0 | 4.1 | 9.3 | 3.0 | 4.9 | 4.7 | 6.6 | 9.0 | 9.8 | 9.3 | 7.4 | 12.3 | 8.5 | 535 |
| Less: Interest | 0.3 | 1.1 | 0.3 | 0.9 | 0.3 | 0.7 | 1.0 | 1.6 | 1.5 | 2.1 | 2.5 | 2.7 | 3.1 | 2.5 | 4.0 | 2.8 | 1,333 |
| Depreciation | 0.1 | 0.4 | 0.1 | 0.3 | 0.1 | 0.2 | 0.2 | 0.3 | 0.3 | 0.4 | 0.8 | 0.9 | 1.0 | 0.8 | 1.1 | 0.7 | 1,100 |
| Net Income before Taxes | 1.9 | 7.1 | 2.9 | 8.8 | 3.7 | 8.4 | 1.8 | 3.0 | 2.9 | 4.1 | 5.7 | 6.2 | 5.2 | 4.1 | 7.2 | 5.0 | 379 |
| Taxes and Contributions 2/ | 1.6 | 6.0 | 2.4 | 7.3 | 2.9 | 6.6 | 0.3 | 0.5 | 0.5 | 0.7 | 1.8 | 2.0 | 1.6 | 1.3 | 1.5 | 1.0 | 94 |
| Net Profit | 0.3 | 1.1 | 0.5 | 1.5 | 0.8 | 1.8 | 1.5 | 2.5 | 2.4 | 3.4 | 3.9 | 4.2 | 3.6 | 2.8 | 5.7 | 4.0 | 1,900 |

1/ In 1969 the accounting basis was changed from invoices paid to invoices including receivables, so that 1969 is not strictly comparable.
2/ In 1965 the basis of laxation was changed with the introduction of the retail sales tax which is passed on to customers.

December, 1970

Table 7

## YUGOSLAVIA: Babin Kuk Tourism Project

### Mincetas Balance Sheet 1962-69

(Din million)

| | 1962 | % | 1963 | % | 1964 | % | 1965 | % | 1966 | % | 1967 | % | 1968 | % | 1969 | % | Trend Index 1962 = 100 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| ASSETS | | | | | | | | | | | | | | | | | |
| Current Assets | 10.3 | 92.0 | 12.5 | 89.3 | 17.5 | 80.6 | 28.9 | 82.8 | 40.1 | 71.0 | 62.2 | 79.2 | 82.5 | 82.3 | 81.8 | 74.4 | 794 |
| Long Term Assets | 0.5 | 4.5 | 0.8 | 5.7 | 0.8 | 3.7 | 0.3 | 0.9 | 0.3 | 0.5 | 0.6 | 0.8 | 1.4 | 1.4 | 7.7 | 7.0 | 1,540 |
| Fixed Assets | 0.4 | 3.5 | 0.7 | 5.0 | 3.4 | 15.7 | 5.7 | 16.3 | 16.1 | 28.5 | 15.7 | 20.0 | 16.4 | 16.3 | 20.4 | 18.6 | 5,100 |
| Total Assets | 11.2 | 100.0 | 14.0 | 100.0 | 21.7 | 100.0 | 34.9 | 100.0 | 56.5 | 100.0 | 78.5 | 100.0 | 100.3 | 100.0 | 109.9 | 100.0 | 981 |
| LIABILITIES | | | | | | | | | | | | | | | | | |
| Current Liabilities | 5.1 | 45.5 | 7.3 | 52.1 | 11.5 | 53.0 | 21.5 | 61.6 | 31.8 | 56.3 | 48.8 | 62.2 | 68.1 | 67.9 | 63.1 | 57.4 | 1,237 |
| Long Term Debt | 4.8 | 42.9 | 4.8 | 34.3 | 8.0 | 36.9 | 9.7 | 27.8 | 11.2 | 19.8 | 12.6 | 16.0 | 12.1 | 12.1 | 22.6 | 20.6 | 471 |
| Equity | 1.3 | 11.6 | 1.9 | 13.6 | 2.2 | 10.1 | 3.7 | 10.6 | 13.5 | 23.9 | 17.1 | 21.8 | 20.1 | 20.0 | 24.2 | 22.0 | 1,862 |
| | 11.2 | 100.0 | 14.0 | 100.0 | 21.7 | 100.0 | 34.9 | 100.0 | 56.5 | 100.0 | 78.5 | 100.0 | 100.3 | 100.0 | 109.9 | 100.0 | 981 |

Table 8

December, 1970

# YUGOSLAVIA: Babin Kuk Tourism Project

## HOTEL SUBSIDIES

1. From the end of World War II, a number of European countries, endowed with tourism potential and favorably situated vis-a-vis the tourist originating markets, initiated a series of incentive schemes designed to direct private investment towards the enlargement of accommodation capacity. Table 1 presents a summary of tourism incentives provided by selected European countries, grouped into the following basic categories: loans at favorable interest rates, loan guarantees, subsidies (grants) and fiscal incentives.

2. Subsidies to the tourist industry reflect the desire of the Governments concerned to net more foreign exchange than would accrue if the industry's capacities and prices were determined only by market forces. The Yugoslav authorities have followed the example of other European countries in providing such incentives for investment in tourism, and the rapid expansion of hotel capacity in Yugoslavia during the last decade has been powerfully assisted by this incentive system. Under the system the Federal Government provides a subsidy to the banks of 2½% in the case of loans for tourist facilities with a term of 10-15 years and 3% for loans of 16-25 years maturity, on condition that they do not charge interest rates in excess of 6%. This subsidy is made available from a Federal tourism subsidy fund as a lump sum advance. In the case of 25 year loans this means that a sum equivalent to about one-third the principal is paid to the banks prior to disbursement. This subsidy has reportedly been sufficient during most of the last few years to permit some of Yugoslavia's larger banks to secure sizeable medium term loans in the Eurodollar market for relending for hotel construction. In addition to these Federal Government subsidies to the Banks, the enterprises sponsoring and investing in hotel development receive subsidies from the Republic governments, 1% in the case of Croatia and 2½% in Slovenia. The net result is that long term loans by Yugoslav banks for hotel construction carry an effective interest rate of 2½% and 3% as contrasted with 8%, the official interest rate limit applicable to most industrial medium and long term loans. Effective interest rates on these latter loans are reportedly substantially higher, since in many cases compensating deposit balances have to be maintained. The Yugoslav tourism subsidy system is thus based on the same justification used in many countries to defend the adoption of bonuses for other "non-traditional" exports, i.e., that the extra foreign exchange resulting from their production and sale abroad is of greater value to the economy as a whole than the financial return to the investor (at least in the short and medium run). In principle, the subsidy system should serve to equate the private and national returns on the investment.

3. In the case of Yugoslavia, the country's accommodation capacity needed to be enlarged at costs which would permit it to compete successfully in the rapidly expanding European mass tourism market. Its main competitors - Italy, Greece, Spain and some of the North African countries - had already greatly increased their hotel capacity or were rapidly doing so.

4. The widespread use of interest subsidies - and even outright grants - to lower the cost of construction of new hotels reflects the fact that there is a limit to the rates new hotels can charge since they have to compete with older facilities often constructed at lower real costs and which have already depreciated a good part of their original plant. This consideration applies with special force to a relative latecomer in the expansion of accommodation for European mass tourism like Yugoslavia.

5. There is room for discussion whether the form and extent of the present Yugoslav system to encourage the construction of new hotels is the most appropriate or whether a more limited and selective form of subsidization might be preferable. For example, the system subsidizes interest rates heavily during the entire repayment period of long term loans, even though it is not clear that this is necessary after, say, the first ten years of operation. It may also be argued that interest rates of 2½% and 3% on loans which are mostly denominated in Dinars and thus are not readjustable with prices or exchange rates, are excessively low - resulting in negative real interest rates and an unnecessarily heavy burden on the Federal and Republic Governments. The Federal Government and the Republics are reportedly studying possible modifications of the system in the light of experience. It is important that in carrying out these studies and in any discussion between the Bank and Yugoslavia concerning the subsidies the following be carefully considered: (i) the key role which the subsidies have played and are playing in the expansion of hotel accommodation and (ii) the need to consider the Yugoslav system in relation to the arrangements in competing Mediterranean tourist countries - including such old-established ones as France and Italy - for subsidizing the construction of new tourist facilities.

Table 1

YUGOSLAVIA: Babin Kuk Tourism Project

Government Aid to Hotels in Various European Countries in 1969

| Country | Loans at Fav. Interest Rates | Guarantee of Loans | Subsidies (Grants) | Fiscal Incentives |
|---|---|---|---|---|
| Austria | x | x | x1) | x |
| France | x | - | 1) | x |
| Greece | x | .. | .. | x |
| Italy | x | - | x1) | x |
| Portugal | x | x | x | x |
| Spain | x | .. | - | - |
| Turkey | x | .. | - | x |
| Yugoslavia | x | .. | x1) | x |

Source: Information supplied by OECD Member countries and Yugoslavia in reply to the annual questionnaire of the OECD Tourism Committee.

(x) = existing
(-) = non existing
(..) = no information available
(1) = a subsidy to help cover interest charges is granted

# YUGOSLAVIA: Babin Kuk Tourism Project

## EXTERNAL INFRASTRUCTURE

1. The recent expansion of tourism in the Dubrovnik area has tended to strain the commune's infrastructure facilities. There is need for more expeditious handling of the flow of passengers and baggage passing through the air terminal; the access roads linking the Adriatic Highway with the area south east of the old city and the main streets leading from the new harbor area to the old city are subject to severe traffic congestion during the peak tourist season; at the same time, while Dubrovnik's centuries old sewerage system has been expanded to service new hotel and commercial facilities, the system discharges untreated sewerage into the sea at various points, resulting in heavy pollution in the port area and significant contamination even along some parts of the coast line used for bathing and other recreational purposes.

2. It is evident that the planned rapid expansion of tourism facilities, of which the Babin Kuk complex will be a key component, cannot help but aggravate some of these problems. Indeed, the success of Babin Kuk as a project and the preservation of Dubrovnik as Yugoslavia's most valuable tourism asset requires timely action on the part of the local authorities to expand and improve the area's infrastructure facilities.

### Airport Facilities

3. On the basis of reasonable traffic forecasts, it is estimated that by 1980, peak hour aircraft movement and passenger arrivals will be more than three times those experienced during the 1970 tourist season. "Airport Dubrovnik", the autonomous, financially self-supporting municipal enterprise in charge of the airport, is developing a comprehensive program for staged expansion of the airport facilities with the help of competent consultants. The first phase of this program, designed to accommodate expected traffic flows until at least 1980, envisages alteration and expansion of the existing terminal, increasing the number of aircraft apron parking positions, and lengthening the runway. Except for the runway extension, the need for which is debatable and should be further reviewed, this program, estimated to cost about US$8.0 million, seems well conceived.

### Water Supply

4. Based on present and projected demand, it appears that while the present source of water will be adequate for many years to come, additional transmission and pumping capacity with limited treatment will be needed by mid-1975. The cost of these facilities, for which the engineering studies are near completion, is estimated at US$1.0 million. It is likely that at most a two year period will be required for construction.

Sewerage System

5. For the success of the Babin Kuk tourism project, taken by itself, it is essential that the waters along the northern coastline of the Babin Kuk peninsula, where swimming areas are to be located, be free from contamination. To ensure this, the section of the municipal sewerage system which discharges untreated sewerage into the city's new harbor area will have to be reconstructed to provide for adequate treatment and an appropriate marine outfall. To safeguard Dubrovnik as a prime tourism area, the city's entire sewerage system needs to be extended and improved as soon as possible. The Bank has indicated to the Yugoslav authorities that it might be willing to finance in part Dubrovnik's sewerage improvement program, the total cost of which is estimated to be about US$8.0 million. Technical studies by Yugoslav consultants are nearing completion. They will have to be reviewed for completeness. Further studies of coastal currents and ocean stratification factors may prove necessary, prior to project appraisal, which may involve retaining additional outside consultants.

Access to Babin Kuk and Urban Transportation

6. A careful review of the road system in the immediate vicinity of the proposed tourism complex at Babin Kuk carried out by consultants, indicates that the existing roads will be able to handle the additional traffic likely to be generated for many years to come. Access to the construction site is now possible over a good, paved road and the proposed internal circulation and parking pattern for Babin Kuk is well designed. A second access route to the site and improved access from Babin Kuk to the old city can be provided by carrying out relatively minor reconstruction and resurfacing of part of the Republic, Marshall Tito and Iva Vajnovica streets, the construction of a short ramp connecting Vladimira Nazora and Marshall Tito streets and through provision of off-street parking facilities for the residential area adjacent to the boulevard entrance to Babin Kuk. These improvements would involve an estimated cost of less than US$1.0 million equivalent.

7. The prospective guests of Babin Kuk, of whom about 75% are expected to arrive by air, will be able to travel to and from the airport by bus in reasonable time even during periods of relative congestion during the peak tourist season, since it is possible to bypass most of the urban area by using the northern access road between the city and the Adriatic highway. The terrain between the built-up area of Dubrovnik and that highway is difficult and steep and any widening of the access roads will be quite expensive. Such improvements are much more important for the existing hotels south east of the old city than for Babin Kuk.

8. The existing peak tourist season congestion on Dubrovnik's main streets (except in the old fortress city, which is closed to general traffic) is bound to be intensified once Babin Kuk is opened. The 5,000 guests will want to visit the rest of the city and especially the old city for

shopping, sightseeing and to participate in the cultural events during the summer festival. Most of its 2,000 employees will live in the rest of Dubrovnik. Their daily trips to and from Babin Kuk, those by visitors and service vehicles will further increase the traffic flow. Existing plans to deal with this problem call for costly widening and reconstruction of main traffic arteries, construction of increased parking facilities in the very heart of the urban area adjacent to the entrances to the old city and a very limited increase of the area where private vehicles are to be banned. This approach would at best prevent present congestion from getting even more unmanageable while endangering the unique character of the city and throwing a heavy financial burden on the municipality since even the top priority improvements would cost in excess of US$7.0 million equivalent. Moreover, it would not ensure the guests of Babin Kuk of reasonably satisfactory access to the old city.

9. Under these circumstances, a different approach to the problem of peak season traffic congestion is needed which would envisage the banning of most outside private vehicles from a major part of the urbanized area, the development of special, convenient transportation services in the form of buses, mini-buses and motor boats and the siting and construction of major parking facilities near the entrances to the urban area from the Adriatic highway. In developing such an approach, the closest cooperation between the hotel industry and the municipality, and the assistance of urban transportation experts will be required.

# YUGOSLAVIA: Babin Kuk Tourism Project

## THE MARKET

### Dubrovnik's Position in Yugoslavian Tourism

1. The uniqueness of its scenic, recreational and cultural resources places Dubrovnik in a special category with respect to Yugoslav tourism.

2. Dubrovnik is one of the oldest Yugoslav tourist resorts. Its reputation as an international tourist destination dates back to the very origin of modern tourism, in the last decades of the nineteenth century. Its first "tourist" hotels, such as Petka, de la Ville and Imperial were built during that period for a wealthy international clientele attracted to the area, particularly in the winter time. About 60 hotels were operating in the area by 1938. In the same year, tourist bed-nights in Dubrovnik stood at 413,000, two-thirds of which were accounted for by foreign visitors. At the present time Dubrovnik is among the leading sea resorts in Yugoslavia, being surpassed in terms of tourist bed-nights only by Porec, on the Istrian coast.

3. Dubrovnik is a select tourist center. The participation of foreign visitors - wealthier on the average than domestic visitors - in the total traffic is far higher in Dubrovnik than in most other Yugoslav tourist resorts. Furthermore, the nationality structure of foreign visitors to Dubrovnik appears to be affected more by the economic conditions of the originating countries than by their geographical proximity to Yugoslavia.1/ Dubrovnik's supply matches this special type of demand. The ratio of A class hotel capacity to total hotel capacity is far higher in Dubrovnik than in the average Yugoslav seaside resort. Because of the selectivity of its supply and demand, Dubrovnik ranks in top position among Yugoslav seaside resorts in terms of average daily expenditure by tourists.

4. Despite Dubrovnik's relatively high prices, and the process of "democratization" currently affecting international tourism, not only has its tourism demand grown faster than in most other Yugoslav seaside resorts during the 'sixties but it has recently been ahead of supply.

5. The fact that Dubrovnik's "tourist season" is longer than that of the average tourist resort along the Adriatic coast contributes to the comparatively better utilization of its accommodation capacity. In 1969 Dubrovnik's hotels experienced an average rate of bed occupancy of about 62%, well above that of hotels on the Slovenian coast (35%), in Venice (36%) and in Rimini (25%). Although Dubrovnik's hotels reach occupancy levels of above 100% in the "peak" months of the summer season, the lack of additional accommodation thwarts the demand of a considerable number of potential tourists - 5,000 in 1969 according to the records of a single travel agency.

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1/ Italy and Austria, the major suppliers of Dubrovnik's foreign traffic from among neighboring countries, actually rank after West Germany, the U.K., the Netherlands and the U.S.A.

6. Dubrovnik's tourist industry is outstanding not only by national standards but even when compared with the tourist industries of the other resorts existing in the locality. Given the substantial differences which exist between Dubrovnik's tourist market and that of the other resorts in the locality with regard to type, rates and utilization of accommodation, as well as in the nationality composition and average daily expenditure of visitors (see Table 1), the two markets are, in fact, completely distinct.

Development of Dubrovnik's Tourist Industry

7. For political reasons, the recovery of the tourist trade was slow in the aftermath of World War II and through the 'fifties. On the whole, not until 1959 was Dubrovnik able to catch up with its pre-war level of bed-nights. In the 'sixties, however, the rapid general expansion of the international tourist market, and the improved relations between Yugoslavia and the bulk of western countries, caused a remarkable revival of Dubrovnik's tourist industry.

Development of Supply

8. No information is available on the development of Dubrovnik's tourist supply in the first part of the 'sixties. During the period 1965-69, hotel beds increased from 2.276 to 3.224 while supplementary accommodation capacity remained about the same (see Table 2).

9. The entire increase in hotel capacity took place in A and B class hotels, the capacity of C hotels having declined slightly. This fact, and the increasingly greater proportion of hotel capacity to total accommodation capacity, clearly shows that Dubrovnik is in the process of accentuating its "exclusive" character.

10. It is worth noting that during this period the increase in hotel capacity in the town area (+42%) was much slower than in the other resorts of the Commune (+292%). Despite the comparatively better utilization rate enjoyed by the town hotels (see para. 20 ahead), many entrepreneurs were probably discouraged from building new hotels in the town area because of the increasing scarcity of land and beach space.

11. The table herebelow describes the present (1969) distribution of Dubrovnik's accommodation capacity by type and class:

| | No. of Rooms | No. of Beds | No. of Beds as a Percentage of Total |
|---|---|---|---|
| "A" Class | 816 | 1,295 | 40.2 |
| "B" Class | 779 | 1,425 | 44.2 |
| "C" Class | 232 | 504 | 15.6 |
| Sub-Total | 1,827 | 3,224 | 100.0 |
| Other Accommodation | | | |
| Private Rooms | 3,492 | 7,040 | 65.9 |
| Other | - | 3,633 | 34.1 |
| Sub-Total | 3,492 | 10,673 | 100.0 |

12. The length of the operating period of Dubrovnik's accommodations is affected by their type and class. "A" hotels are open year-round, while most of B accommodations close during two or three months in winter. The operating period of both C hotels and supplementary accommodations is generally limited to seven months, from April to October. Thanks to its longer operating period and better utilization rate, the hotel industry has the lion's share of total traffic (83% in terms of bed-nights in 1969) despite its smaller capacity as compared with supplementary accommodation.

13. The fluctuation of hotel rates during the year defines, if only broadly, three seasons in Dubrovnik: a high season which goes from the beginning of July to the end of September; a mid-season including June and October; a low season covering the remaining seven months of the year. The difference in hotel rates from one season to the other is remarkable. In fact, mid-season and low season tariffs are respectively about 25% and 50% off those in the high season. Given the high occupancy levels at present enjoyed in the months of April and May (see para. 21 following) the "shift" of these two months from low to mid-season appears advisable as regards the future.

14. A sharp difference in standards of quality[1/], tariffs, length of operating period and development trends leads to the identification of two distinct markets of supply - the first composed of A and B class hotels and the second of C hotels and supplementary accommodation.

The Development of Demand

15. Because of the prompt response of the market to such favorable events as the increase in accommodation capacity, the completion of an

1/ Supplementary accommodation and C hotels, for instance, do not generally have heating facilities.

international airport[1/] (1962) and the opening of the South-Adriatic highway (1965), the development pace of foreign traffic to Dubrovnik stepped up considerably starting at the beginning of the 'sixties. Over the period 1961-69 the number of foreign visitor bed-nights in all kinds of accommodations rose from 219,000 to 895,000, at an average annual growth rate of 19%.

16. During the period 1961-67, the rise in prices caused by the pressure of foreign demand on Dubrovnik's supply induced an increasing proportion of comparatively poorer Yugoslav tourists to seek cheaper accommodation elsewhere. Hence, a decline in the number of domestic visitor bed-nights (from 311,000 to 185,000) and a dramatic change in the relative importance of domestic and foreign visitors in the composition of Dubrovnik's traffic were observed during this period. More recently, however, the trend shown by domestic traffic in the years 1961-67 has inverted itself, possibly as a result of improved economic conditions in Yugoslavia (see para. 48 ahead). In the last two years the number of national visitor bed-nights rose from 185,000 to 263,000 and their ratio to total visitor bed-nights increased slightly.

| | - 1 9 6 1 - | | - 1 9 6 7 - | | - 1 9 6 9 - | |
|---|---|---|---|---|---|---|
| | No. of Bed-nights ('000) | % | No. of Bed-nights ('000) | % | No. of Bed-nights ('000) | % |
| Domestic | 310.6 | 58.6 | 185.6 | 19.5 | 262.6 | 22.7 |
| Foreign | 219.4 | 41.4 | 763.8 | 80.5 | 895.2 | 77.3 |
| Total | 530.0 | 100.0 | 949.4 | 100.0 | 1,157.8 | 100.0 |

17. If the present analysis is restricted to hotel traffic, and foreign and domestic components of said traffic are considered separately, one can see that these two components had in 1969 an inverse seasonality pattern. In five months of the year (January, February, March, October and November), the number of domestic bed-nights is higher than that of foreign. Conversely, foreign visitor bed-nights outnumber domestic in the remaining part of the year (see Table 3).

18. One of the salient results of the faster growth of domestic tourist traffic as compared with that of foreign in the years 1967-69, was an improvement of the seasonality pattern of traffic to Dubrovnik during that period:

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1/ Located at Cilipi, about 20 km. from the town.

| | Percent of Total Yearly Traffic in Terms of Bed-Nights | |
|---|---|---|
| | 1967 | 1969 |
| High Season | 57.4 | 53.5 |
| Mid Season | 21.9 | 21.6 |
| Low Season | 20.7 | 24.9 |
| Total | 100.0 | 100.0 |

Although it is difficult to make any accurate forecasts, it appears that any further shift of the seasonality pattern in favor of the low season is unlikely owing to a variety of traditional social "institutions" current in the originating markets (e.g., school and certain industrial vacations restricted to summer).

19. As a whole, traffic to Dubrovnik increased between 1961 and 1969 from 530,000 to 1,158,000 bed-nights, at an annual growth rate of 10.3%. As for hotel traffic in particular, bed-nights rose from 417,000 to 729,000 during the period 1965-69 - a total increase of 75%.

Comparison of Supply with Demand:
Dubrovnik's Accommodation Rate of Occupancy

20. The table below indicates that as a result of the greater increase of demand (+75%) vis-a-vis that of supply (+42%), the occupancy rate of Dubrovnik's hotel accommodations improved considerably from 1965 to 1969, rising from a level of 50% to a level of about 62%. During that period, A class hotels constantly showed a better occupancy rate than B hotels, and the occupancy rate of B hotels was better than that of C hotels. The fact that higher class hotels have maintained their level of occupancy well over that of lower class hotels indicates that the upgrading process of Dubrovnik's tourist supply was met by a similar process on the demand side.

(Percentages)

| | A Hotels | B Hotels | C Hotels | All Hotels |
|---|---|---|---|---|
| 1965 | 68.5 | 44.1 | 44.7 | 50.1 |
| 1966 | 57.3 | 53.2 | 44.9 | 52.9 |
| 1967 | 53.4 | 49.9 | 49.9 | 51.0 |
| 1968 | 58.9 | 52.3 | 44.1 | 52.9 |
| 1969 | 73.7 | 56.6 | 46.3 | 61.9 |

21. The table below, which relates to 1969 monthly data on selected[1/] Dubrovnik hotels, describes (i) the different rate of utilization of A and B class hotel accommodation and (ii) the relative contribution of foreign and domestic traffic to said utilization.

(Percentages)

| | A Class Hotels | | | B Class Hotels | | |
|---|---|---|---|---|---|---|
| | Occupancy Ascribable to Foreign Traffic | Occupancy Ascribable to Domestic Traffic | Total | Occupancy Ascribable to Foreign Traffic | Occupancy Ascribable to Domestic Traffic | Total |
| January | 13.0 | 52.9 | 65.9 | 0.3 | 10.6 | 10.9 |
| February | 16.8 | 32.5 | 49.3 | 0.2 | 11.1 | 11.3 |
| March | 34.5 | 22.5 | 57.0 | 2.6 | 13.3 | 15.9 |
| April | 58.3 | 12.3 | 70.6 | 38.7 | 13.1 | 51.8 |
| May | 79.6 | 8.4 | 88.0 | 73.3 | 10.8 | 84.1 |
| June | 85.5 | 3.4 | 88.9 | 96.6 | 2.3 | 98.9 |
| July | 90.3 | 3.8 | 94.1 | 93.7 | 3.0 | 96.7 |
| August | 100.1 | 2.6 | 102.7 | 100.4 | 3.1 | 103.5 |
| September | 92.5 | 3.2 | 95.7 | 96.2 | 2.8 | 99.0 |
| October | 75.1 | 8.1 | 83.2 | 41.9 | 12.6 | 54.5 |
| November | 20.7 | 13.8 | 34.5 | 0.5 | 12.0 | 12.5 |
| December | 17.7 | 15.0 | 32.7 | 0.1 | 12.5 | 12.6 |
| Year | 57.3 | 14.8 | 72.1[2/] | 45.4 | 8.9 | 54.3[2/] |

In as much as its seasonal pattern is inverted with respect to that of foreign tourism, domestic tourism plays a determinant role in the extension of Dubrovnik's tourism season to the winter months, even though it accounts for a relatively small share of the total yearly traffic.

22. From the figures presented in the preceding paragraph, the following seasonal occupancy[3/] levels may be derived for A and B class hotels:

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1/ The A class hotel sample includes three hotels for a total of 838 beds, or 65% of total A class hotel accommodation capacity. The B class hotel sample includes five hotels for a total of 933 beds, or 65% of total B class hotel accommodation.

2/ Yearly occupancy of both A and B class sample hotels is somewhat lower than that of the "universe" (see table under para. 20 preceding).

3/ The seasons have been defined according to the new classification proposed under para. 13 above).

(Percentages)

| | A Class Hotels 1/ | B Class Hotels 1/ |
|---|---|---|
| High Season | 99.6 | 103.8 |
| Mid Season | 83.9 | 74.7 |
| Low Season | 49.4 | 13.1 |
| Year | 73.7 | 56.6 |

23. It should be noted that the occupancy levels indicated in the preceding paragraph for B hotels relate to B hotels as a whole, irrespective of their opening period. If, however, consideration is given only to B hotels operating part of the year, the yearly occupancy levels arrived at would be 51.3%.

The Composition of Demand by Originating Geographic Areas

24. As indicated in paragraph 16 above, foreign and domestic visitors at present account (in terms of bed-nights) for 23% and 77% respectively of Dubrovnik's total traffic.

25. No substantial change has occurred in the nationality composition of foreign visitors to Dubrovnik in recent times. Western Europe retains its post World War II position as Dubrovnik's major foreign traffic supplier. In terms of bed-nights, its participation in this traffic was 87% in 1965 and 83% in 1969. For many years in the past, West Germany, the U.K. and the Netherlands have ranked in first, second and third positions respectively, among Western European countries. The "nights" spent in Dubrovnik by the nationals of these three countries combined accounted for 56% of total bed-nights in 1965 and for 46% in 1969. North America has increased its share in Dubrovnik's foreign visitor bed-nights from 5.4% in 1965 to 9.5% in 1969. The remaining 17% of Dubrovnik's 1969 foreign traffic is split between Eastern European countries and non-European countries (U.S.A. and Canada excluded).

26. Quite naturally, both demographic and geographical factors bear an influence on the composition, by Republic of origin, of Dubrovnik's domestic traffic. Tourists from Serbia, the most populous among Yugoslav republics, account for nearly 39% of Dubrovnik's domestic visitor bed-nights. The second position (25%), however, is held by visitors from the Bosna-Hercegovina Republic whose territory, although less populous than that of Croatia, is on the average closer to Dubrovnik. Croatia comes third, with a 24% share of Dubrovnik's "domestic" bed-night market. The remainder of this market (22%) is accounted for by visitors from Slovenia, Macedonia and Montenegro.

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1/ Figures have been slightly adjusted to reflect the yearly occupancy of the "universe" - i.e. the occupancy observed in 1969 in all A and B class hotels existing in Dubrovnik (see footnote 2 on preceding page).

## THE CHARACTERISTICS OF DEMAND

### Major Demand Motivations: Business and Pleasure

27. No adequate data is available for the calculation of the exact breakdown between the pleasure and business-motivated components of Dubrovnik's tourist traffic - a breakdown which is most important for the purpose of the present analysis. The statement may, however, be made that in 1969 business traffic is unlikely to have surpassed the level of 85,000 bed-nights, i.e. 7.3% of total traffic, or 10.9% of total hotel traffic, or 12.7% of A and B hotel traffic. This maximum value is arrived at by:

(a) adding (i) the monthly average of foreign visitors' bed-nights registered in A and B class hotels 1/ in the months of January and February 2/ (among the lows for foreign traffic), and (ii) the monthly average of domestic visitors' bed-nights registered at the same hotels in the months of July and September 2/ (among the lows for domestic traffic);

(b) considering the sum total under (a) above as representative of the maximum value attained by business-motivated tourism (both foreign and domestic) in each month of the year.

28. On the basis of information released directly by hotel managers in Dubrovnik, the Mission has formed the opinion that the actual share of business-motivated visitors in total A and B hotel traffic can, within the limit indicated in the preceding paragraph (12.7%), be set at 7.5%.

### Other Characteristics of the Demand

29. Some up-to-date information on other traffic characteristics is provided by two recent surveys conducted by Dubrovnik's Institute for Economics and Planning. Carried out in the period August 15 to September 15, 1969, the first deals with foreign tourism alone. The second survey taken between December 15, 1969 and January 15, 1970 includes domestic tourism as well. Given the period of the year in which they were carried out, these surveys may be regarded as indicative only as far as peak and low season traffic characteristics are concerned.

30. A comparative analysis of these characteristics with respect to both foreign and domestic traffic is presented herebelow:

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1/ C class hotel traffic has been omitted from this calculation as businessmen, for different reasons, tend to use almost exclusively, high standard accommodation.

2/ The implicit assumption is made that business-motivated traffic tends to distribute itself evenly throughout the year with the possible exceptions of December, July and August, when a number of business people become vacationers.

| | Peak Season | Low Season | |
|---|---|---|---|
| | Foreign | Foreign | Domestic |
| (1) Distribution of Visitors by Profession of Household Head: | | | |
| Workers | 10.2 | | 7.5 |
| Employers | 25.7 | | 37.5 |
| Professional People and Artists | 25.1 | | 42.5 |
| Students | 6.8 | | - |
| Retired People | 3.7 | | 10.0 |
| Other 1/ | 28.5 | | 2.5 |
| Total | 100.0 | | 100.0 |
| (2) Distribution of Visitors by Mode of Travel | | | |
| Organized Tours (Charters and IT) | 30.0 | 10.9 | 10.0 |
| Other Modes | 70.0 | 89.1 | 90.0 |
| Total | 100.0 | 100.0 | 100.0 |
| (3) Distribution of Visitors by Way of Access | | | |
| Air | 65.9 | 65.4 | 17.5 |
| Road | 22.6 | 18.1 | 32.5 |
| Sea | 9.6 | 12.7 | - |
| Rail | 1.9 | 3.8 | 50.0 |
| Total | 100.0 | 100.0 | 100.0 |
| (4) Distribution of Visitors by Length of Stay | | | |
| 1-10 Days | 37.8 | 47.2 | 50.0 |
| 10-15 Days | 43.3 | 41.2 | 50.0 |
| 16 and more | 18.9 | 11.6 | - |
| Total | 100.0 | 100.0 | 100.0 |
| (5) Average Daily Expenditure by Type of Accommodation (US$) | | | |
| Hotel A | 15.2 | - | - |
| Hotel B | 11.2 | - | - |
| Hotel C | 7.6 | - | - |
| Average all types of hotels | 12.7 | - | - |
| Camping | 4.5 | - | - |
| Private Rooms | 5.5 | - | - |
| Average all types of accommodation | 11.1 | 8.6 | 6.2 |

1/ Including an "unknown" 10.2%.

## TYPES OF MARKETS

31. The information provided in the preceding sections indicates that Dubrovnik's tourist industry is based on two primary types of market: a winter market, characterized by the prevalence of domestic visitors and a summer market of predominantly foreign composition.

### Winter Market

32. Because of the distance from their countries to Dubrovnik, the majority of foreign tourists consider a trip to Dubrovnik worth while only if they can stay there a minimum length of time - hence their tendency to visit Dubrovnik during the period of their "main" vacation - a period which for Europeans and North Americans generally runs from April to October. Yugoslavs, on the other hand, may plan a trip to Dubrovnik for even a relatively short stay.

33. Aside from businessmen, the winter domestic market appears to be composed of:

(i) climate-seekers looking for a "spell" from the severe Yugoslav winters; Dubrovnik's mild climate and the fact that it is closer to some of the major Yugoslav centers (including Belgrade, Sarajevo and Titograd) lead to the assumption of a heavy participation of said type of tourist in Dubrovnik's winter traffic.

(ii) culture-motivated visitors and sightseers in general; given their relative degree of indifference to season, this type of visitor tends to go to Dubrovnik in the "off season", when good accommodation is available at moderate rates.

34. The prevailing motivations (climate, sightseeing and culture), and a definite preference for the very best type of accommodation available indicate that the domestic winter demand is, in social if not economic terms,[1/] an elite and status-conscious demand. This fact is also proven by the high share accounted for by the "professional" group (45%) in the socio-economic composition of the aforesaid demand.

### Summer Market

35. Both the foreign and the domestic components of the summer market are highly heterogeneous in motivation. Climatic conditions, cultural interests and beaches all contribute to make Dubrovnik attractive to this market. However, while sightseers and climate-seekers are more heavily represented in the "fringe" months (April, May and October) beach-based tourists predominate in the peak months. The difference in motivations also reflects on the visitor's average length-of-stay, which in summer tends to be longer than in winter.

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1/ In purely economic terms the foreign-dominated summer market is superior than the winter market, as indicated by the difference in average daily expenditure (see para. 27 above).

36. A further division can be made in the summer market between the wealthier market for A and B hotels on the one hand and the poorer market for C hotels and supplementary accommodation on the other. Thus far, this distinction has not been very clear on the demand side; because of insufficient room in A and B class hotels a number of A and B class potential visitors have had to redirect their demand towards the lower type of accommodation - particularly in the peak months of the season. The distinction will, however, become increasingly apparent parallel to the large increase in first-class accommodation (L-A and B class hotels) scheduled for the next five years (see para. 38 following).

37. As a whole, the summer market can also be considered an elite market, at least by European standards. The average distance of the major tourist supplier markets and the considerable resultant proportion of airborne tourists support this particular classification.

## MARKET PROSPECTS FOR THE BABIN KUK PROJECT

### Planned Development of Dubrovnik's Accommodation Capacity

38. There are no plans for expanding either the capacity of Dubrovnik's existing supplementary accommodation or that of C class hotels. On the other hand, based on projects at various stages of advancement, current estimates indicate that Dubrovnik's L-A and B hotel capacity will develop over the next five years as follows:

| | - Number of Beds - | | | |
|---|---|---|---|---|
| | Class L | Class A | Class B | Total |
| 1969 | - | 1,295 | 1,425 | 2,720 |
| 1970 | - | 1,295 | 1,425 | 2,720 |
| 1971 | - | 1,795 | 1,425 | 3,220 |
| 1972 | - | 2,295 | 1,425 | 3,720 |
| 1973 | - | 2,295 | 1,425 | 3,720 |
| 1974 | 800 | 2,295 | 1,425 | 4,520 |
| 1975 1/ | 1,600 | 4,695 | 4,425 | 10,720 |

39. Consistent with past supply and demand trends, Dubrovnik will continue to upgrade the quality of its accommodations. By 1975 the number of hotel beds will reach approximately that of supplementary accommodation. As for the hotel industry proper, the L class will appear for the first time on Dubrovnik's supply market in 1974. It should be mentioned, incidentally, that this further improvement of the quality of accommodation appears to be most appropriate in the case of Dubrovnik, where the scarcity of land and beach space will most probably prevent any substantial increase in accommodation capacity beyond the expected 1975 level.

1/ Includes Babin Kuk complex.

Babin Kuk Physical and Economic Competitiveness

40. Because of its location within the town boundaries and yet near the sea, the projected complex will be attractive to all kinds of tourists: climate-seekers, sightseers, beach-motivated visitors and businessmen.

41. Babin Kuk will be the first tourist complex to be built in Dubrovnik, with the numerous financial and promotional advantages that this will imply. From the market standpoint this will also have a favorable impact. Given the size of its public facilities, Babin Kuk will be the most suitable site in the Dubrovnik area for conventions, conferences and meetings - a specialized segment of the market which has constantly been growing in importance.

42. Another specific advantage of Babin Kuk over other existing and planned accommodations is that of offering a great deal of space in general, and beach space in particular. The resultant favorable balance between man-made and environmental conditions will assure resident visitors of a relaxed atmosphere in unspoiled natural surroundings - a combination appreciated by an ever-increasing proportion of tourists, irrespective of their primary motivations.

43. The above-mentioned advantages of Babin Kuk over the competition should, at the very least, balance out the disadvantage of its being located farther from the old town. Given similar tariffs and lengths of operating periods, Babin Kuk's rate of occupancy should not, therefore, fall short of that of its direct competitors.

44. Based on the hotel tariffs currently prevailing in Dubrovnik,1/ the table herebelow shows the rates (in 1970 prices) which the Babin Kuk complex should offer in order to be competitive.

| Class of Babin Kuk's Different Sections | Full Board per Person in Double Room (US$) | | |
|---|---|---|---|
| | High Season | Mid Season | Low Season |
| "L" Class | 20.00 | 15.00 | 10.00 |
| "A" Class | 15.00 | 11.00 | 7.50 |
| "B" Class | 10.00 | 7.50 | - |

The Outlook for the Expansion of Dubrovnik's Tourist Markets

Foreign Market

45. The data provided in paragraphs 25 and 28 above indicate that by far the bulk of Dubrovnik's foreign traffic is composed of Western European holidaymakers.

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1/ The "L" hotel tariffs have been estimated on the basis of those of "L" class hotels existing in other Yugoslav towns.

46. A vacation in Dubrovnik is rather expensive for most Western Europeans on account of both Dubrovnik's geographical position and its level of prices. As also indicated by prevailing tariffs for package tours originating in Western Europe, the total expenditure for a 14 day vacation in Dubrovnik is unlikely to be less than $250. If this minimum is compared with (i) the per capita incomes and income distributions current in Western Europe, and (ii) the average tourist expenditure propensities observed in Western European countries,[1/] the conclusion may be drawn that Western Europeans earning annual incomes compatible with a vacation to Dubrovnik or other comparable[2/] tourist destinations (i.e. Dubrovnik's potential market) are, at present, only a small share of Western Europe's total population.

47. The development of the actual tourist demand deriving from the above-mentioned potential market has been very dynamic in recent years. Table 4 shows that between 1964 and 1969 in a number of Mediterranean regions[3/] total foreign tourist arrivals - more than 80% of which originated in Western Europe - increased at an annual average rate of 12.6%.[4/] There is strong evidence that this rate of development will improve, or at least remain the same, in the coming years as well:

(i) Despite past development trends, the number of Western Europeans who can afford the costs implied by a vacation in Dubrovnik or similar tourist centers remains small. The potential market has thus plenty of "room" for expanding as per capita incomes rise. It should be noted, furthermore, that the typical "shape" of income distributions current in Western Europe is such that each additional increase in the potential market is bound to be greater than the previous.

(ii) The proportion of actual long haul travellers to the potential market (i.e., all people who can afford such travels) will continue to rise in future in relation to the constantly increasing propensity for travel in general and for air travel in particular.

Domestic Market

48. Although from 1960 to 1967 per capita income in Yugoslavia developed at a considerable growth rate (approximately 5% growth rate in constant prices) domestic pleasure-motivated traffic as measured by national visitors' overnights in all Yugoslav seaside resorts was about stagnant. With some fluctuations,

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1/ Tourist expenditure as a percentage of total private consumption expenditures in Western Europe varied from 3.7% in Italy to 7.4% in Switzerland.

2/ i.e. in terms of prices and distances.

3/ They have been selected, within the limits of available statistical data, from among those more closely reflecting Dubrovnik's situation.

4/ The range varies from 6.2% (Morocco) to 22% (Tunisia) and 41% (Cyprus).

domestic tourist bed-nights in these resorts passed from 9,231,000 in 1960 to 10,242,000 in 1967. More recently, however, domestic pleasure-motivated tourism to seaside resorts has shown a sudden upsurge, with the number of bed-nights rising to 12,650 in 1969 from the 1967 level (at an average growth-rate for the two years of over 12%). Although it is too soon to draw any definite conclusions, this trend might be related to the fact that per capita income in Yugoslavia has reached the threshold at which pleasure-motivated domestic tourist demand becomes increasingly "income-sensitive".

49. Even assuming that this threshold has not yet been reached, and the 1967-69 upsurge proves to be fortuitous, it is likely to be attained within the next seven or eight years, as per capita income climbs from the present level of $570 to $850 in 1975. Accordingly the time has either come, or it will soon come, when domestic Yugoslav tourism will develop rapidly.

Underlying Assumptions for Projection of Traffic and Occupancy Levels

Pleasure-Motivated Traffic

50. The development of Dubrovnik holidaymaker traffic has been forecast on the main assumption that this traffic will tend to grow - within every hotel category - in proportion to supply.[1/] As far as foreign tourism is concerned, the demand requirements for the period 1969-77 implied by this assumption (see para. 62 following) do not seem to exceed, to any large extent, either past development trends of foreign traffic to Dubrovnik or the likely pace of development of Western European pleasure-motivated traffic to comparable Mediterranean tourist destinations. The more so as part of these requirements will be met not by "new" traffic but by frustrated demand (see para. 54 following). Similar considerations are applicable to the demand requirements of pleasure-motivated domestic traffic. Consequently there is no serious constraint for Dubrovnik's further tourism development on the part of the market.

51. Under these conditions, the assumption that pleasure-motivated traffic will grow as a linear function of supply appears reasonable. It also closely reflects what has occurred in the past development of many tourist resorts (examples of which are given on both sides of the Adriatic), where the hotel occupancy remained unchanged despite considerable increases in accommodation capacity.

52. At any rate, Dubrovnik appears capable of increasing its share of the above-mentioned traffic. Supporting factors for this assumption are:

Foreign Traffic

(i) pleasure-motivated traffic to Dubrovnik originating in Western Europe is only a small share of total

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1/ Such assumption in regard to B class hotels will only apply to tourist traffic registered from April to October, this being the operating period of the planned additional B class accommodation in Dubrovnik (i.e., Babin Kuk 3,000 beds).

Western European pleasure-motivated traffic to the Mediterranean area, or even Yugoslavia.

(ii) Dubrovnik has a high degree of competitiveness; although Dubrovnik's level of prices is high by general Yugoslav standards, it is lower than that of other resorts in the same geographic area offering comparable types of attractions - say, Venice, Capri, Elba, St. Tropez.

Domestic Traffic

(i) Domestic pleasure-motivated traffic to Dubrovnik is only a small share of total domestic tourist traffic to Yugoslav seaside resorts.1/

(ii) Its past traditions make Dubrovnik more popular among Yugoslavs than any other seaside resort in Yugoslavia.

53. The assumption that pleasure-motivated demand will grow in proportion to supply appears to be applicable for each year from 1969 to 1974 - a period during which Dubrovnik's supply will, according to plan, increase at about the same rate as in the previous five years. In the following period, however, because of the leap in hotel accommodation capacity from 1974 to 1975, the adjustment of demand to supply is unlikely to occur immediately. The mission has formulated the hypothesis that demand will catch up with supply in three years.

54. Aside from the general reasons indicated in the preceding paragraphs, any hypothesis forecasting a longer period of time for the market to meet the 1974-75 increase in accommodation is rendered most unlikely by a consideration of the size of existing frustrated demand.2/ According to the records of Atlas, Dubrovnik's major travel agency, 1,000 Americans, 2,700 French or Italians, 1,300 Germans and 300 British, for a total of 5,000 potential visitors, were turned away from hotels located in the general area of Dubrovnik's commune during the period January/August, 1970. This data naturally reflects the volume of frustrated demand only as far as potential visitors who requested organized group travel are concerned. If data on frustrated demand was also available for potential visitors intending to travel on an individual basis - the majority of the market as shown in paragraph 30 above - this volume would undoubtedly be much greater.

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1/ About 1.4% in terms of bed-nights in 1968.

2/ It should be noted that there are three levels of frustrated demand in the Dubrovnik area (i) that of potential visitors who could not find accommodation anywhere else in the commune's territory, (ii) of potential visitors who could not find accommodation in the town itself and (iii) of potential visitors who could not find rooms in hotels.

55. Due to the relatively slow increase scheduled for Dubrovnik's accommodation capacity from 1970 to 1974, the present situation of frustrated demand will remain unchanged during those years. It will thus cast its full impact on hotel occupancy in the following period.

56. Because of frustrated demand, the increase in pleasure-motivated traffic will not be evenly distributed over the years 1975-77, but will rather tend to be concentrated at the beginning of this period. Accordingly, the mission has assumed that the years 1975, 1976 and 1977 will take up 70%, 20% and 10% respectively of said increase.

Business-Motivated Traffic

57. Unlike holidaymaker traffic, business traffic is scarcely affected by increased accommodation, its growth depending on such factors as economic conditions, expansion of trade and the like. As for Dubrovnik's business traffic, development has been projected at 4% annual growth rate, i.e. the same average rate recorded during the period 1964-68 by 15 Yugoslav commercial centers with very little or no tourist attractions (see Table 5).1/

Projection of Dubrovnik's Yearly Levels of Occupancy

58. According to the assumptions set forth in the proceeding paragraph, the average yearly occupancy of L-A and B class hotels in Dubrovnik will be as follows:2/

| | "L" and "A" Class Hotel 3/ | "B" Class Hotels | |
|---|---|---|---|
| | | On Average | Open from April to October 4/ |
| 1969 | 73.8 | 56.6 | 51.1 |
| 1970 | 74.0 | 56.8 | 51.3 |
| 1971 | 72.6 | 56.9 | 51.4 |
| 1972 | 71.4 | 57.1 | 51.6 |
| 1973 | 71.5 | 57.3 | 51.8 |
| 1974 | 70.7 | 57.5 | 52.0 |
| 1975 | 59.0 | 41.0 | 39.2 |
| 1976 | 65.9 | 47.5 | 45.7 |
| 1977 | 69.4 | 50.8 | 49.0 |

1/ The implicit assumption here is that the factors affecting the growth of the business-motivated component of Yugoslav tourism traffic will continue to develop in the period under consideration as they did in the period 1964-68.

2/ See Tables 6 and 7 for the calculation.

3/ The occupancy level of "L" class hotels when they begin to operate is assumed to be equal to that of "A" hotels.

4/ Includes Babin Kuk.

Seasonal Adjustment of Hotel Occupancy Levels

59. From what has been said in paragraph 18, the seasonal pattern of Dubrovnik's hotel occupancy should be about the same in the typical year 1977 as that prevailing at present. In the years 1975 and 1976, on the other hand, this pattern is likely to be modified substantially. Since frustrated demand is strictly a summer months' phenonemon, it stands to reason that the progressive meeting of this segment of potential demand will cast its ensuing favorable impact on high season alone. It is therefore logical to assume that the hotel occupancy rate for this particular season will immediately (i.e. as of 1975) reach the level forecast for the typical year. This will not be the case for mid and low season rates, which will together bear the brunt of the reduced annual occupancy levels predicted for 1975 and 1976.

60. These considerations have led to the following assumptions:

(i) Throughout the period 1975-77, high season occupancy levels will stand at 98% and 95% for L-A and B hotels, respectively.

(ii) Mid and low season occupancy levels for L-A class hotels will be such as to (a) satisfy the condition set forth under (i) above, (b) be in the same ratio to each other as they were in 1969 and (c) be compatible with the volume of traffic forecast for each single year. As for B class hotels, mid-season occupancy levels will be determined by residual traffic.

61. The occupancy levels (in percentages) for each season and class of hotel during the period 1975 to 1977 will thus be:

| | L-A Hotels | | | B Hotels | | |
|---|---|---|---|---|---|---|
| | 1975 | 1976 | 1977 | 1975 | 1976 | 1977 |
| High Season | 95 | 95 | 95 | 98 | 98 | 98 |
| Mid Season | 61 | 72 | 79 | 37 | 56 | 65 |
| Low Season | 36 | 43 | 46 | | | |

Assessment of Demand Requirements

62. In line with the assumptions laid out in the foregoing sections, the development of Dubrovnik's tourist traffic as a whole is indicated herebelow:

| | ('000 Bed-Nights in all kinds of Accommodations) | Growth Rates |
|---|---|---|
| 1969 | 1,158 | |
| 1970 | 1,160 | Period 1969-77 : 12.4% |
| 1971 | 1,287 | |
| 1972 | 1,410 | Period 1969-74 : 6.9% |
| 1973 | 1,412 | |
| 1974 | 1,613 | Period 1974-77 : 22% |
| 1975 | 2,534 | |
| 1976 | 2,800 | |
| 1977 | 2,934 | |

YUG[redacted]AVIA: Babin Kuk Tourism Project

COMPARISON BETWEEN THE TOURIST MARKET OF DUBROVNIK TOWN AND THAT OF THE OTHER RESORTS WITHIN DUBROVNIK COMMUNE

| 1. Distribution of Hotel Bed Capacity by Category (%) | Dubrovnik Town | Other Resorts |
|---|---|---|
| A Category | 40.2 | 10 .8 |
| B Category | 44.2 | 70.0 |
| C Category | 15.6 | 19.2 |
| Total | 100.0 | 100.0 |

2. High Season, Full Board Hotel Rates for Selected same Category Hotels (U.S.$)

| | Dubrovnik Town | | | Cavtat | | | Lopud | | |
|---|---|---|---|---|---|---|---|---|---|
| | | Min. | Max. | | Min. | Max. | | Min. | Max. |
| A Category | Excelsior | 11.20 | 18.00 | Albatros | 10.10 | | | | |
| | Argentina | 12.20 | 17.00 | | | | | | |
| B Category | Splendid | 8.20 | 8.70 | Adriatic | 7.80 | | Grand Hotel | 5.60 | |
| | Bellevue | 9.00 | | Cavtat | 6.00 | 6.70 | La Fodia | 6.50 | 7.50 |
| | Kompas | 8.48 | 11.00 | Supetar | 5.40 | 6.20 | | | |

| 3. Distribution of Bed Nights by Foreign and Domestic Visitors (%) | Dubrovnik Town | Other Resorts |
|---|---|---|
| Foreign | 77.4 | 69.8 |
| Domestic | 22.6 | 30.2 |
| Total | 100.0 | 100.0 |

| 4. Average Daily Expenditure in High Season by Foreign Visitors (U.S. $) | Dubrovnik Town | Selected Other Resorts | |
|---|---|---|---|
| | | Cavtat | Lopud |
| | 11.1 | 8.9 | 7.4 |

Annex 3
Table 1

Annex 3
Table 2

YUGOSLAVIA: Babin Kuk Tourism Project

DEVELOPMENT OF DUBROVNIK'S ACCOMMODATION CAPACITY DURING THE PERIOD 1965-69

(Number of Beds)

| | - 1965 - | - 1966 - | - 1967 - | - 1968 - | - 1969 - |
|---|---|---|---|---|---|
| **Hotel** | | | | | |
| A Category | 505 | 889 | 889 | 1,016 | 1,295 |
| B Category | 1,171 | 1,253 | 1,365 | 1,385 | 1,425 |
| C Category | 600 | 637 | 591 | 631 | 504 |
| Total | 2,276 | 2,779 | 2,845 | 3,032 | 3,224 |
| **Supplementary Accommodation** | | | | | |
| Private Rooms | n.a. | 6,642 | n.a. | n.a. | 7,040 |
| Other | n.a. | 4,152 | n.a. | n.a. | 3,633 |
| Total | | 10,794 | | | 10,673 |

December, 1970

YUGOSLAVIA: Babin Kuk Tourism Project

RELATIVE IMPORTANCE OF FOREIGN AND DOMESTIC VISITOR HOTEL BEDNIGHTS IN IN 1969 - ON A MONTHLY BASIS

(Percentages)

| | Domestic | Foreign | Total |
|---|---|---|---|
| January | 83.7 | 16.3 | 100.0 |
| February | 73.2 | 26.8 | 100.0 |
| March | 50.4 | 49.6 | 100.0 |
| April | 17.5 | 82.5 | 100.0 |
| May | 10.8 | 89.2 | 100.0 |
| June | 3.7 | 96.3 | 100.0 |
| July | 3.7 | 96.3 | 100.0 |
| August | 3.2 | 96.8 | 100.0 |
| September | 3.6 | 96.4 | 100.0 |
| October | 14.9 | 85.1 | 100.0 |
| November | 57.0 | 43.0 | 100.0 |
| December | 63.4 | 36.6 | 100.0 |
| Total | 14.3 | 85.7 | 100.0 |

December, 1970

Annex 3
Table 4

## YUGOSLAVIA: Babin Kuk Tourism Project

### Foreign Stopover Visitor Arrivals
('000)

| | 1964 | 1969 | Av.Annual Growth Rate |
|---|---|---|---|
| | | | % |
| Lebanon | 963 | 1,587 | 10.5 |
| Malta | 38 | 186 | 37.0 |
| Morocco | 460 | 621 | 6.2 |
| Turkey | 229 | 435 | 13.6 |
| Tunisia | 138 | 373 | 22.0 |
| Cyprus | 16 | 118 | 49.0 |
| Greece | 674 | 1,139 | 11.0 |
| Spain | 12,794 | 21,682 | 11.1 |
| Portugal | 1,008 | 2,759 | 22.0 |
| Yugoslavia | 2,227 | 4,746 | 16.4 |
| Israel | 230 | 385 | 10.9 |
| | 18,777 | 34,031 | 12.6 |

December, 1970

YUGOSLAVIA: Babin Kuk Tourism Project

INCREASE IN HOTEL OVERNIGHTS DURING THE PERIOD 1963-1968 IN 15 YUGOSLAV CENTERS WITH LITTLE OR NO TOURIST ATTRACTIONS

| Town | - 1963 - No. of Over-Nights | - 1968 - No. of Over-Nights |
|---|---|---|
| Bijeljina | 8,125 | 10,083 |
| Brcko | 13,738 | 15,286 |
| Doboj | 11,876 | 17,877 |
| Tuzla | 42,891 | 40,696 |
| Titograd | 62,315 | 61,991 |
| Skoplje | 148,050 | 194,055 |
| Kragujerac | 26,328 | 46,370 |
| Kraljevo | 31,446 | 35,187 |
| Novisad | 95,571 | 118,537 |
| Pec | 36,317 | 39,888 |
| Svetozarevo | 19,242 | 25,485 |
| Valjevo | 15,866 | 20,023 |
| Zrenjanin | 18,723 | 26,294 |
| Cacak | 23,363 | 25,123 |
| Titovo Ozicc | 39,215 | 47,446 |
| TOTAL | 593,066 | 724,341 |

Average Annual Growth-Rate: 4.0 percent

December, 1970

YUGOSLAVIA: Babin Kuk Tourism Project

PROJECTION OF L-A HOTEL CAPACITY, TRAFFIC AND OCCUPANCY LEVELS - (Theoretical Capacity and Traffic in '000 overnights)

| | - Capacity - | | - Traffic - | | | -Occupancy- |
|---|---|---|---|---|---|---|
| Year | Beds 1/ | Theoretical Capacity 2/ | Pleasure Motivated Traffic 3/ | Business Motivated Traffic 4/ | Total Traffic | L - A 5/ % |
| | (a) | (b) | (c) | (d) | (e) | (f) |
| 1969 | 1,295 | 472.7 | 322.8 | 26.1 | 348.9 | 73.8 |
| 1970 | 1,295 | 472.7 | 322.8 | 37.0 | 349.8 | 74.0 |
| 1971 | 1,795 | 655.2 | 447.4 | 28.1 | 475.5 | 72.6 |
| 1972 | 2,295 | 837.7 | 568.6 | 29.2 | 597.8 | 71.4 |
| 1973 | 2,295 | 837.7 | 568.6 | 30.4 | 599.0 | 71.5 |
| 1974 | 3,095 | 1,129.7 | 766.8 | 31.7 | 798.5 | 70.7 |
| 1975 | 6,295 | 2,297.7 | 1,321.7 | 33.0 | 1,354.7 | 59.0 |
| 1976 | 6,295 | 2,297.7 | 1,480.3 | 34.3 | 1,514.6 | 65.9 |
| 1977 | 6,295 | 2,297.7 | 1,559.6 | 35.7 | 1,593.3 | 69.4 |

1/ Actual figure for 1969. Figures as from plans for following years.

2/ Number of beds multiplied by 365.

3/ 1969 figure arrived at by assuming that pleasure-motivated visitors' bednights were 92.5% of total bednights. (see para. 4.01 and 6.20 of the Appendix). Projection based on a growth proportionate to that of supply for the period 1969-74. As for the following period, projection based on the assumption that years 1975, 1976 and 1977 will take up 70%, 20% and 10% respectively, of the increase required for demand to match the 1974-75 increase in supply.

4/ 1969 figure arrived at by assuming that business motivated visitors' bednights were 7.5% of total. As for following period projection based on a 4% annual growth rate.

5/ $\frac{(e)}{(b)}$

December, 1970

Annex 3
Table 6

# YUGOSLAVIA: Babin Kuk Tourism Project

## PROJECTION OF B-HOTEL CAPACITY, TRAFFIC AND OCCUPANCY LEVELS

(Theoretical Capacity and Traffic in '000 Overnights)

| Year | Beds 1/ (a) | Theoretical Capacity 2/ (b) | April to October Traffic: Pleasure Motivated (c) | April to October Traffic: Business Motivated (d) | April to October Traffic: Total (e) | November to March Traffic: Pleasure Motivated (f) | November to March Traffic: Business Motivated (g) | November to March Traffic: Total (h) | Total Yearly Traffic (l) | Occupancy of B-hotels with Opening Period from Apr-Oct. 7/ (m) | Occupancy of all B-hotels on Average 8/ (n) |
|---|---|---|---|---|---|---|---|---|---|---|---|
| 1969 | 1,425 | 520.1 | 246.1 4/ | 19.9 4/ | 266.0 3/ | 26.2 4/ | 2.1 4/ | 28.3 3/ | 294.3 3/ | 51.1 | 56.6 |
| 1970 | 1,425 | 520.1 | 246.1 | 20.7 6/ | 266.8 | 26.2 | 2.2 6/ | 28.4 | 295.2 | 51.3 | 56.8 |
| 1971 | 1,425 | 520.1 | 246.1 | 21.5 6/ | 267.6 | 26.2 | 2.3 6/ | 28.5 | 296.1 | 51.4 | 56.9 |
| 1972 | 1,425 | 520.1 | 246.1 | 22.4 6/ | 268.5 | 26.2 | 2.4 6/ | 28.6 | 297.2 | 51.6 | 57.1 |
| 1973 | 1,425 | 520.1 | 246.1 | 23.3 6/ | 269.4 | 26.2 | 2.5 6/ | 28.7 | 298.1 | 51.8 | 57.3 |
| 1974 | 1,425 | 520.1 | 246.1 | 24.2 6/ | 270.3 | 26.2 | 2.6 6/ | 28.8 | 299.1 | 52.0 | 57.5 |
| 1975 | 4,425 | 1,615.1 | 608.7 5/ | 25.1 6/ | 633.8 | 26.2 | 2.7 6/ | 28.9 | 662.7 | 39.2 | 41.0 |
| 1976 | 4,425 | 1,615.1 | 712.3 5/ | 26.1 6/ | 738.4 | 26.2 | 2.8 6/ | 29.0 | 767.4 | 45.7 | 47.5 |
| 1977 | 4,425 | 1,615.1 | 764.1 5/ | 27.0 6/ | 791.1 | 26.2 | 2.9 6/ | 29.1 | 820.2 | 49.0 | 50.8 |

1/ Actual figure for 1969. Figures as from existing plans for following years.
2/ Number of beds multiplied by 365.
3/ Visitors' bednights in the periods April-October and November-March are estimated to be 90.4% and 9.6% of total yearly bednights, respectively. These percentages are derived from information on a sample of B-hotels (see par. 2.14 of the Appendix).
4/ Pleasure-motivated and business-motivated visitors bednights are estimated to be 92.5% and 7.5% respectively of total nights in the particular period of the year considered (see par. 4.01 of the Appendix).
5/ Based on assumption that years 1975, 1976 and 1977 will take up 70%, 20% and 10% respectively of the increase required for demand to match the 1974-1975 increase in supply.
6/ 1969 figure projected at 4% annual growth rate (see par. 6.20 of Appendix).
7/ $\frac{(e)}{(b)}$
8/ $\frac{(l)}{(b)}$

December, 1970

# YUGOSLAVIA: Babin Kuk Tourism Project

## ECONOMIC JUSTIFICATION

### Introduction

1. The quantifiable net benefits from the project consist primarily of visitors' expenditures within the project complex itself less the costs (excluding depreciation, taxes and interest payments) of operating the project. An important characteristic of the benefits is that 90% of them consist of foreign exchange. The relevant investment is the capital cost of the project itself plus the share of external infrastructure properly chargeable to the project.

2. In addition to the costs and benefits generated within the Babin Kuk complex, the project will produce additional costs and benefits outside the project's physical and accounting boundaries. The treatment of these external effects is explained in paras. 10-15 below.

### Costs, Revenues, and Economic Life of the Project

3. So far as the Babin Kuk complex itself is concerned, the economic benefits and costs are derived from the project's financial accounts (Annex 5). Depreciation, interest and taxes are excluded from economic costs. However, part of the costs of improving external infrastructure is added to the investment costs of the complex.

4. The share of local road costs attributable to the project has been derived as follows (two road projects are involved):

(i) the improvement of short access roads to Babin Kuk, which would also serve other adjoining areas. These are estimated to cost US$700,000;

(ii) the improvement of parking facilities and public transportation to reduce traffic congestion during the peak tourist season. The cost of this project will depend on the solution adopted; it is believed that the cost will not in any case exceed US$2.5 million.

Conservatively, one-half of (i) and one-third of the cost of (ii), amounting in all to a little more than US$1.0 million, are assumed to be properly chargeable to the Babin Kuk complex.

5. The costs and revenues of the project are expected to be distributed over time as follows:

(US$ Million)

| Year | Investment Costs[1/] Babin Kuk Complex | Investment Cost Roads | Total Investment Costs | Operating[2/] Costs | Operating Revenues |
|---|---|---|---|---|---|
| 1 | 1.60 | - | 1.60 | - | - |
| 2 | 7.32 | - | 7.32 | - | - |
| 3 | 8.11 | 0.50 | 8.61 | - | - |
| 4 | 20.95 | 0.50 | 21.45 | - | - |
| 5 | 6.05 | - | 6.05 | 13.75 | 17.71 |
| 6 | - | - | - | 15.17 | 21.27 |
| 7-29 | - | - | - | 15.87 | 22.44 |

Total Investment Cost: US$45.03

6. The project facilities and equipment have varying economic lives, but as a whole it is estimated that the project would have an economic life of about 25 years. The need to make modest provision for some replacement expenditures during this period is considered to be offset by the life of the main assets beyond 25 years.

## Rates of Return

7. Based on the above estimates, the internal economic return on the project comes out at 12.3%. This is not however, the "best estimate" of the project's true profitability to the economy. Key factors in this calculation are the exchange rate used (i.e., D 15.0 = US$1.0, the recently established official rate) and the cost of the land which does not reflect its full current value. The recent change in the exchange rate was widely regarded in Yugoslavia as moderate in the light of the country's balance of payments position. Accordingly, in order to test the project's sensitivity to changes in the value of certain variables, the rate of return was re-calculated on varying assumptions as is shown below.

1/ Excludes US$4.38 million for interest during construction and US$1.50 million paid to the Municipality in the form of a building fee, but includes US$1.0 million for roads and related investments.

2/ Operating costs before taxes, depreciation, interest and dividends.

Sensitivity Analysis

8. The project's economic return has been subjected to sensitivity tests, with the results shown in the following table:

| | | Resulting Rate of Return % |
|---|---|---|
| i. | Foreign Exchange Rate (instead of US$1.0 = D 15.0) | |
| | (a) US$1.0 = D 18.0 | 17.5 |
| ii. | Valuation of Land (instead of US$1.5 million) | |
| | (a) US$2.50 million | 11.8 |
| | (b) US$4.25 million | 11.2 |
| iii. | Annual Occupancy Rate (instead of 57%) | |
| | (a) 54% | 11.5 |
| iv. | Opening Date (1 year delay, i.e. 1976 not 1975) | 11.0 |
| v. | Most Adverse Combination of above Factors | 9.5 |
| vi. | Most Favorable Combination of above Factors | 17.5 |

It is clear that the rate of return is most sensitive to a change in the value of foreign exchange and, to a lesser extent, to changes in occupancy levels. A combination of the least favorable assumptions yields a rate of return of more than 9%.

9. Assuming a value of US$1.0 = D 18.0 and a value of land of US$2.5 million, the internal economic return comes out at 16.9%. This figure may be considered the "best estimate" (the calculation assumes 1975 as the opening date and an average annual occupancy of 57%).

External or Off-Site Effects

10. The project will have both direct and indirect external effects. The direct effects are defined as expenditures of Babin Kuk guests outside the complex, while the indirect are a result of induced investment, especially in infrastructure, not paid for directly by Babin Kuk guests. These are further described below.

Direct Effects

11. As a result of the proposed investment in Babin Kuk, foreign and Yugoslav airlines and other modes of transportation are expected to increase their activities and their earnings. This will also be the case with retail shops, restaurants and the like outside the Babin Kuk complex and especially in the old city of Dubrovnik. These services will be paid for directly by the tourist in addition to what he spends on food, accommodation, etc. within the complex itself. Total gross earnings of the Yugoslav economy will be substantially greater than those of the complex itself.

12. These additional revenues, however, result not only from the investment in and operation of Babin Kuk, but also from investment in and operation of other facilities. Because of the number of "other facilities" required to serve the needs of the visitor, it has not been possible to estimate the additional capital and operating costs required to generate these extra revenues.

13. However, it is likely that there would be a better utilization of existing capacity as well as an expansion of present facilities and the net benefits of the former would properly be ascribable to the investment in Babin Kuk. To this extent, the benefits of the project in the rate of return analysis are understated.

Indirect Effects

14. Investment in Babin Kuk would result in the need for expansion and improvement of the water supply and sewage systems, the airport and some of the roads (see Annex 2). With regard to water supply and sewage and the airport, the agencies involved are autonomous and financially self-supporting. Any additional capital and operating costs involved, therefore, would be recovered through:

(i) charging the Babin Kuk complex through rates for water supply and sewage services supplied; and

(ii) charging the airlines through landing and other fees for the airport services provided.

Since these agencies are financially self-supporting it is reasonable to assume that the return on the additional investment required would be adequate.

15. With regard to road and related investments the problem is complicated for three reasons:

(i) the road projects involved are not revenue earning;

(ii) the projects are to serve not only the Babin Kuk project but other needs of the area; and

(iii) the projects would be required anyway in the future and the investment in Babin Kuk only accelerates this need.

The share of the estimated investment chargeable to Babin Kuk has been given above (para. 4).

Balance of Payments Impact

16. By the time it is fully operational, the proposed project would increase gross foreign exchange earnings from tourism by US$20.2 million, net of tourist transportation. This compares with the official estimate of US$310.0 million earned by the sector in 1969, but which includes foreign exchange earnings from tourist transportation.

17. Because of the high proportion of foreign tourists, and the low import content of operating costs, the estimated net foreign exchange earnings of the project are relatively high. When the project is fully operational the annual costs in foreign exchange are estimated at US$3.35 million on operating account with US$2.10 million of capital charges. Thus the net foreign exchange earnings in 1977 and subsequent years would be US$14.7 million, which compares with the estimated foreign exchange component in total investment costs of US$16.6 million, including price contingencies.

# YUGOSLAVIA: Babin Kuk Tourism Project

## FINANCIAL ANALYSIS

### Operating Results

1. Table 1 of this annex presents the forecast of Operating Results over the first 16 years of the project. This forecast is based on Revenue and Cost assumptions which are described below.

### Revenue Assumptions

2. Total revenues include income from both hotel and non hotel sources within the Babin Kuk complex. Hotel revenue has been broken down into four categories: rooms, food, beverage and other. Room and food income has been estimated on the basis of full pension tariffs and the projected occupancy in each type of hotel in the complex. The full pension tariffs and expected occupancy levels for a typical year are indicated in the following table:1/

Projected Occupancy and Full Pension Tariffs

| Category | Season | Full Pension2/ Tariffs US$ | Expected Occupancy Rates % |
|---|---|---|---|
| Luxury | High | 24.00 | 95 |
| | Mid | 19.00 | 79 |
| | Low | 13.00 | 46 |
| Class A | High | 20.00 | 95 |
| | Mid | 15.00 | 79 |
| | Low | 10.00 | 46 |
| Class B | High | 15.00 | 98 |
| | Mid | 10.00 | 73 |

3. Income from the sale of beverages and all other goods and services within hotels is estimated on the basis of the number of guests (by category) times the assumed expenditure per guest-night as follows:

1/ The average annual hotel occupancy rate for this typical year is 57%. The annual occupancy rates expected during the first two years of operation are 44% and 54%, respectively. The tariff structure is the same for all years.

2/ These tariffs are dollar equivalents of dinar rates inflated to take account of the price increases expected to occur up to 1975, rounded to the nearest dollar.

| | Beverage US$ | Other |
|---|---|---|
| Luxury Hotel Guests | 2.08 | 1.47 |
| Class A Hotel Guests | 1.6 | .94 |
| Class B Hotel Guests | 1.34 | .75 |

4. Non hotel revenue is derived from the sale of goods and services to both hotel guests and non resident guests (transients). Non hotel revenue sources include catering, shops, guest services and recreation. Daily expenditures by hotel guests for non hotel items is estimated as follows:

Non Hotel Expenditures by Hotel Guests

| Category | Catering (US$) | Shops (US$) | Guest Services (US$) | Recreation (US$) | Total (US$) |
|---|---|---|---|---|---|
| Luxury | 1.20 | 2.95 | 1.14 | .87 | 6.16 |
| Class A | .94 | 2.28 | .80 | .67 | 4.69 |
| Class B | .67 | 1.54 | .54 | .47 | 3.22 |

5. Expected daily expenditure per guest, within the complex is given below:

Expected Daily Expenditure by Hotel Guests
(US$)

| Category | Season | Within Hotels | Non Hotel Items | Within Complex 1/ |
|---|---|---|---|---|
| Luxury | High | 27.66 | 6.16 | 33.84 |
| | Mid | 22.30 | 6.16 | 28.48 |
| | Low | 16.94 | 6.16 | 23.12 |
| Class A | High | 22.65 | 4.69 | 27.34 |
| | Mid | 17.29 | 4.69 | 21.98 |
| | Low | 12.60 | 4.69 | 17.29 |
| Class B | High | 16.83 | 3.22 | 20.05 |
| | Mid | 12.15 | 3.22 | 15.37 |

1/ Hotel guests are expected to spend the following amounts per day outside the complex: Luxury - US$2.29, Class A - US$1.76, and Class B - US$1.22.

6. Non resident guests are expected to number 297,000 in a typical year, with an average daily expenditure of US$3.26 per visit: catering - US$1.41, shops - US$0.80, guest services - US$0.60, and recreation - US$0.46.

Cost Assumptions

7. Total operating costs include the direct and indirect expenses attributable to the three groups of activity within the complex: hotel operations, non hotel operations (catering, shops, guest services, and recreation), and the central service centers.1/

8. Direct material costs for food, beverage and other items within the hotels have been calculated as follows: (a) daily food cost per guest has been estimated at US$2.81 for Luxury and Class A residents, and US$2.61 for Class B residents; (b) beverage costs are estimated to average 30% of sales; (c) the cost of other goods and services averages 60% of sales. Direct material costs for catering, shops, guest services and recreation are estimated at 31%, 56%, 23%, and 21% respectively. For the central service centers, material costs in a typical year are expected to be US$275,000, or 1.7% of total operating costs.

9. Payroll costs for hotels are expected to be 21% of sales in the typical year of operation. For individual hotel categories, the payroll as a percent of sales is: Luxury - 30%, Class A - 21%, and Class B - 19%. These costs reflect the relatively low wages of semi- and unskilled workers in the hotel industry in Yugoslavia. The total number of employees in the high season will be about 2,160, in the off season, about 845. Payroll costs for the non hotel departments include an average of 10% of sales for catering, shops, guest services and recreation, and an estimated US$616,000 for the central service centers in a typical year.

10. Indirect costs include the following items for a typical year:2/

---

1/ Total cost estimates for the first two operating years are reduced, reflecting lower occupancy levels, but decline less than proportionally due to fixed and semi-variable costs.

2/ For the first two years of operation, commissions vary directly with sales, laundry declines with reduced occupancy, and all other indirect costs remain fixed.

| | (US$ '000) |
|---|---|
| Administration and General Costs | 1,545 |
| Travel Agency Commission | 1,186 |
| Heat, Light and Power | 864 |
| Maintenance and Repair | 670 |
| Laundry | 586 |
| Advertising and Sales | 134 |
| | 4,985 |

11. Average depreciation on total assets is about 4.6% per year. Buildings and site development are depreciated over 50 years, heavy and light equipment and miscellaneous supplies over 10, 5 and 3 years, respectively. The professional fees and the project office are both amortized over 25 years. Pre-opening management and staff training expenses are amortized in equal installments over the first five years of operation.

12. Interest is calculated at 3% on the Privredna Banka, Zagreb loan, (reflecting the subsidy from the Croatian Government) and 7-1/4% on the proposed IBRD loan.

13. It has been agreed during negotiations that 45% of the annual net profit of BKHTC will be paid to Minceta as dividend. It has also been agreed that no less than 20% of the annual net profits will be retained within BKHTC to build up equity. The allocation of the balance of 35% of the net profits will be at the discretion of the BKHTC Business Committee. It has been assumed that the Business Committee will retain within BKHTC more than the minimum and that this will, on average, amount to a total of 30% of the annual net profits. This will leave 25% of the net profits to be distributed at the discretion of the Business Committee in other ways. A projected Financial Position Statement and a projected Cash Flow Statement, based on the forecast of operating results, are presented below as Tables 2 and 3 attached.

14. The table below shows the impact on the operating results of the subsidized interest rates. Interest rates without subsidies are 7-1/4% on the IBRD loan and 8% on the Yugoslav loan. The interest charge for 1975 is capitalized. Column (A) in each year shows non-subsidized interest payments; Column (B) shows subsidized interest payments.

## Impact of Subsidized Interest on Operating Results
(US$ '000)

| | 1976 | | 1977 | | 1980 | | 1990 | |
|---|---|---|---|---|---|---|---|---|
| | -A- | -B- | -A- | -B- | -A- | -B- | -A- | -B- |
| Operating Profit | 5.54 | 5.54 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 |
| Less Depreciation and Amortization | 2.53 | 2.53 | 2.53 | 2.53 | 2.29 | 2.29 | 2.29 | 2.29 |
| Interest | 2.52 | 1.33 | 2.47 | 2.02 | 2.25 | 1.87 | 1.20 | 0.84 |
| Net Profit | 0.39 | 1.68 | 0.96 | 1.41 | 1.42 | 1.80 | 2.47 | 2.83 |

YUGOSLAVIA: Babin Kuk Tourism Project

PROJECTED PROFIT AND LOSS STATEMENT
(US$ Millions)

| Year Ending December 31: | 1975 | 1976 | 1977 | 1978 | 1979 | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 | 1990 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Operational Year: | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | 14 | 15 | 16 |
| Gross Revenue: | | | | | | | | | | | | | | | | |
| Hotel Operations | 13.65 | 16.37 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 | 17.25 |
| Non-Hotel Operations | 4.06 | 4.90 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 | 5.19 |
| Total | 17.71 | 21.27 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 | 22.44 |
| Less Operating Costs: | | | | | | | | | | | | | | | | |
| Material | 4.80 | 5.82 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 | 6.17 |
| Payroll | 4.30 | 4.49 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 | 4.71 |
| Indirect Costs | 4.65 | 4.86 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 | 4.99 |
| Turnover Tax | .47 | .56 | .61 | .61 | .61 | .61 | .61 | .61 | .61 | .61 | .61 | .61 | .61 | .61 | .61 | .61 |
| Total | 14.22 | 15.73 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 | 16.48 |
| Operating Profit | 3.49 | 5.54 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 |
| Less: Depreciation and Amortization | 2.53 | 2.53 | 2.53 | 2.53 | 2.53 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 |
| Net Profit Before Interest | 0.96 | 3.01 | 3.43 | 3.43 | 3.43 | 3.67 | 3.67 | 3.67 | 3.67 | 3.67 | 3.67 | 3.67 | 3.67 | 3.67 | 3.67 | 3.67 |
| Less: Interest | - | 1.33 | 2.02 | 1.97 | 1.93 | 1.87 | 1.81 | 1.55 | 1.48 | 1.41 | 1.33 | 1.24 | 1.15 | 1.05 | 0.95 | 0.84 |
| Net Profit | 0.96 | 1.68 | 1.41 | 1.46 | 1.50 | 1.80 | 1.86 | 2.12 | 2.19 | 2.26 | 2.34 | 2.43 | 2.52 | 2.62 | 2.72 | 2.83 |
| Dividends to Minceta (45%) | 0.43 | 0.75 | 0.63 | 0.66 | 0.68 | 0.81 | 0.84 | 0.95 | 0.99 | 1.02 | 1.05 | 1.09 | 1.13 | 1.18 | 1.22 | 1.27 |
| Allocation by Business Committee | 0.24 | 0.42 | 0.35 | 0.37 | 0.38 | 0.45 | 0.47 | 0.53 | 0.55 | 0.57 | 0.59 | 0.61 | 0.63 | 0.66 | 0.68 | 0.71 |
| Total Dividend and Shares | 0.67 | 1.17 | 0.98 | 1.03 | 1.06 | 1.26 | 1.31 | 1.48 | 1.54 | 1.59 | 1.64 | 1.70 | 1.76 | 1.84 | 1.90 | 1.98 |
| Retained Earnings | 0.29 | 0.51 | 0.43 | 0.43 | 0.44 | 0.54 | 0.55 | 0.64 | 0.65 | 0.67 | 0.70 | 0.73 | 0.76 | 0.78 | 0.82 | 0.85 |
| Cummulative Retained Earnings | 0.29 | 0.80 | 1.23 | 1.66 | 2.10 | 2.64 | 3.19 | 3.83 | 4.48 | 5.15 | 5.85 | 6.58 | 7.34 | 8.12 | 8.94 | 9.79 |
| Return on Total Investment (%) 1/ | 1.9 | 6.0 | 6.9 | 6.9 | 6.9 | 7.4 | 7.4 | 7.4 | 7.4 | 7.4 | 7.4 | 7.4 | 7.4 | 7.4 | 7.4 | 7.4 |

1/ Net profit before interest and dividend but after depreciation

April, 1971

Annex 2
Table 1

YUGOSLAVIA: Babin Kuk Tourism Project

PROJECTED FINANCIAL POSITION
(US$ Million)

| Year Ending December 31 | 1974 | 1975 | 1976 | 1977 | 1978 | 1979 | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 | 1990 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Operational Year | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | 14 | 15 | 16 |
| **Current Assets** | | | | | | | | | | | | | | | | | |
| Cash | | 4.46 | 6.60 | 6.97 | 8.37 | 5.10 | 5.60 | 6.71 | 7.97 | 8.25 | 3.74 | 4.86 | 5.13 | 6.15 | 7.11 | 2.57 | 3.38 |
| Receivables | | 0.35 | 0.43 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 |
| Inventories | | 0.89 | 1.06 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 | 1.12 |
| Others | | 0.35 | 0.43 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 | 0.45 |
| Total Current Assets | | 6.05 | 8.52 | 8.99 | 10.39 | 7.12 | 7.62 | 8.73 | 9.99 | 10.27 | 5.76 | 6.88 | 7.15 | 8.17 | 9.13 | 4.59 | 5.40 |
| **Current Liabilities** | | | | | | | | | | | | | | | | | |
| Payables/General | | 0.53 | 0.64 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 | 0.68 |
| Payables/Minceta Credits | | 1.13 | 0.99 | 0.85 | 0.71 | 0.57 | 0.43 | 0.29 | 0.15 | - | - | - | - | - | - | - | - |
| Other | | 0.90 | 0.94 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 | 0.97 |
| Provision for Dividend Payment | | 0.67 | 1.17 | 0.98 | 1.03 | 1.06 | 1.26 | 1.31 | 1.48 | 1.54 | 1.59 | 1.64 | 1.70 | 1.76 | 1.84 | 1.90 | 1.98 |
| Long-Term Debt Maturities | | 1.08 | 1.42 | 1.47 | 1.52 | 1.58 | 1.64 | 1.70 | 1.76 | 1.84 | 1.92 | 2.00 | 2.09 | 2.19 | 2.29 | 2.41 | 2.53 |
| Total Current Liabilities | | 4.31 | 5.16 | 4.95 | 4.91 | 4.86 | 4.98 | 4.95 | 5.04 | 5.03 | 5.16 | 5.29 | 5.44 | 5.60 | 5.78 | 5.96 | 6.16 |
| **Net Working Capital** | | 1.74 | 3.36 | 4.04 | 5.48 | 2.26 | 2.64 | 3.78 | 4.95 | 5.24 | 0.60 | 1.59 | 1.71 | 2.57 | 3.35 | (1.37) | (0.76) |
| **Fixed Assets (Net)** | | | | | | | | | | | | | | | | | |
| Fixed Assets | 40.52 | 45.29 | 43.00 | 41.52 | 39.23 | 41.55 | 40.07 | 37.78 | 35.49 | 34.01 | 37.40 | 35.11 | 33.63 | 31.34 | 29.05 | 32.18 | 29.89 |
| Deferred Charges | 1.05 | 0.96 | 0.72 | 0.48 | 0.24 | - | - | - | - | - | - | - | - | - | - | - | - |
| Total Fixed Assets | 41.57 | 46.25 | 43.72 | 42.00 | 39.47 | 41.55 | 40.07 | 37.78 | 35.49 | 34.01 | 37.40 | 35.11 | 33.63 | 31.34 | 29.05 | 32.18 | 29.89 |
| **Total Net Assets** | 41.57 | 47.99 | 47.08 | 46.04 | 44.95 | 43.81 | 42.71 | 41.56 | 40.44 | 39.25 | 38.00 | 36.70 | 35.34 | 33.91 | 32.40 | 30.81 | 29.13 |
| **Long-Term Liabilities** | | | | | | | | | | | | | | | | | |
| IBRD Loan | 13.59 | 20.00 | 19.69 | 19.04 | 18.34 | 17.59 | 16.78 | 15.91 | 14.98 | 13.99 | 12.92 | 11.77 | 10.54 | 9.22 | 7.80 | 6.28 | 4.64 |
| Yugoslav Loan | 18.48 | 19.28 | 18.51 | 17.74 | 16.97 | 16.20 | 15.43 | 14.66 | 13.89 | 13.12 | 12.35 | 11.58 | 10.81 | 10.04 | 9.27 | 8.50 | 7.73 |
| Total Long-Term Loans | 32.07 | 39.28 | 38.20 | 36.78 | 35.31 | 33.79 | 32.21 | 30.57 | 28.87 | 27.11 | 25.27 | 23.35 | 21.35 | 19.26 | 17.07 | 14.78 | 12.37 |
| (Less: Debt Maturities) | - | 1.08 | 1.42 | 1.47 | 1.52 | 1.58 | 1.64 | 1.70 | 1.76 | 1.84 | 1.92 | 2.00 | 2.09 | 2.19 | 2.29 | 2.41 | 2.53 |
| **Total Long-Term Liabilities** | 32.07 | 38.20 | 36.78 | 35.31 | 33.79 | 32.21 | 30.57 | 28.87 | 27.11 | 25.27 | 23.35 | 21.35 | 19.26 | 17.07 | 14.78 | 12.37 | 9.84 |
| **Equity** | 9.50 | 9.79 | 10.30 | 10.73 | 11.16 | 11.60 | 12.14 | 12.69 | 13.33 | 13.98 | 14.65 | 15.35 | 16.08 | 16.84 | 17.62 | 18.44 | 19.29 |
| Represented by: | | | | | | | | | | | | | | | | | |
| Share Capital | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 |
| Retained Earnings 1/ | - | 0.29 | 0.80 | 1.23 | 1.66 | 2.10 | 2.64 | 3.19 | 3.83 | 4.48 | 5.15 | 5.85 | 6.58 | 7.34 | 8.12 | 8.94 | 9.79 |
| **Total Equity** | 9.50 | 9.79 | 10.30 | 10.73 | 11.16 | 11.60 | 12.14 | 12.69 | 13.33 | 13.98 | 14.65 | 15.35 | 16.08 | 16.84 | 17.62 | 18.44 | 19.29 |
| Current Ratio 2/ | - | 1.4:1 | 1.7:1 | 1.8:1 | 2.1:1 | 1.5:1 | 1.5:1 | 1.8:1 | 2.0:1 | 2.0:1 | 1.1:1 | 1.3:1 | 1.3:1 | 1.5:1 | 1.6:1 | 0.8:1 | 0.9:1 |
| Long-Term Debt/Equity | 77:23 | 80:20 | 78:22 | 77:23 | 75:25 | 74:26 | 72:28 | 69:31 | 67:33 | 64:36 | 61:39 | 58:42 | 54:46 | 50:50 | 46:54 | 40:60 | 34:66 |

1/ Net of dividend provision
2/ Current maturities of LT debt as a current liability

April, 1971

Annex 5
Table 2

YUGOSLAVIA: Babin Kuk Tourism Project

PROJECTED CASH FLOW

(US$ Million)

| Year Ending December 31: | 1971 | 1972 | 1973 | 1974 | 1975 | 1976 | 1977 | 1978 | 1979 | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 | 1990 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Operating Year: | - | - | - | - | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | 14 | 15 | 16 |
| **Source:** | | | | | | | | | | | | | | | | | | | | |
| Cash at beginning | - | - | - | - | - | 4.46 | 6.60 | 6.97 | 8.37 | 5.10 | 5.60 | 6.71 | 7.97 | 8.25 | 3.74 | 4.86 | 5.13 | 6.15 | 7.11 | 2.57 |
| Initial equity capital 1/ | 1.50 | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Initial equity investment | 0.35 | 2.65 | 2.48 | 2.52 | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Long-term loan (IBRD) 2/ | 0.03 | 2.14 | 3.84 | 7.58 | 6.41 | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Long-term loan (Yugoslav) 2/ | 0.35 | 2.71 | 2.64 | 12.78 | 0.80 | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| **Sub-Total** | 2.23 | 7.50 | 8.96 | 22.88 | 7.21 | 4.46 | 6.60 | 6.97 | 8.37 | 5.10 | 5.60 | 6.71 | 7.97 | 8.25 | 3.74 | 4.86 | 5.13 | 6.15 | 7.11 | 2.57 |
| Net profit | - | - | - | - | 0.96 | 1.68 | 1.41 | 1.46 | 1.50 | 1.80 | 1.86 | 2.12 | 2.19 | 2.26 | 2.34 | 2.43 | 2.52 | 2.62 | 2.72 | 2.83 |
| Non-cash charges | - | - | - | - | 2.53 | 2.53 | 2.53 | 2.53 | 2.53 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 | 2.29 |
| Sub-Total | - | - | - | - | 3.49 | 4.21 | 3.94 | 3.99 | 4.03 | 4.09 | 4.15 | 4.41 | 4.48 | 4.55 | 4.63 | 4.72 | 4.81 | 4.91 | 5.01 | 5.12 |
| Total cash & initial investment | 2.23 | 7.50 | 8.96 | 22.88 | 10.70 | 8.67 | 10.54 | 10.96 | 12.40 | 9.19 | 9.75 | 11.12 | 12.45 | 12.80 | 8.37 | 9.58 | 9.94 | 11.06 | 12.12 | 7.69 |
| Increase (or decrease) in Minceta Credits | - | - | - | - | 1.13 3/ | (0.14) | (0.14) | (0.14) | (0.14) | (0.14) | (0.14) | (0.14) | (0.15) | - | - | - | - | - | - | - |
| Increase in payables and others | - | - | - | - | 1.43 | 0.15 | 0.07 | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Sub-Total | - | - | - | - | 2.56 | 0.01 | (0.07) | (0.14) | (0.14) | (0.14) | (0.14) | (0.14) | (0.15) | - | - | - | - | - | - | - |
| Total funds provided | 2.23 | 7.50 | 8.96 | 22.88 | 13.26 | 8.68 | 10.47 | 10.82 | 12.26 | 9.05 | 9.61 | 10.98 | 12.30 | 12.80 | 8.37 | 9.58 | 9.94 | 11.06 | 12.12 | 7.69 |
| **Application:** | | | | | | | | | | | | | | | | | | | | |
| Project expenses | | | | | | | | | | | | | | | | | | | | |
| Land | 1.50 | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Building, fixtures and equipment | 0.68 | 7.26 | 8.58 | 22.50 | 7.06 | - | 0.81 | - | 4.61 | 0.81 | - | - | 0.81 | 5.68 | - | 0.81 | - | - | 5.42 | - |
| Sub-Total | 2.18 | 7.26 | 8.58 | 22.50 | 7.06 | - | 0.81 | - | 4.61 | 0.81 | - | - | 0.81 | 5.68 | - | 0.81 | - | - | 5.42 | - |
| Pre-operational expenses | 0.05 | 0.24 | 0.38 | 0.38 | 0.15 | - | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Total project expenses | 2.23 | 7.50 | 8.96 | 22.88 | 7.21 | - | 0.81 | - | 4.61 | 0.81 | - | - | 0.81 | 5.68 | - | 0.81 | - | - | 5.42 | - |
| Long-term repayment (IBRD) | - | - | - | - | - | 0.31 | 0.65 | 0.70 | 0.75 | 0.81 | 0.87 | 0.93 | 0.99 | 1.07 | 1.15 | 1.23 | 1.32 | 1.42 | 1.52 | 1.64 |
| Long-term repayment (Yugoslav) | - | - | - | - | - | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 | 0.77 |
| Total loan repayment | - | - | - | - | - | 1.08 | 1.42 | 1.47 | 1.52 | 1.58 | 1.64 | 1.70 | 1.76 | 1.84 | 1.92 | 2.00 | 2.09 | 2.19 | 2.29 | 2.41 |
| Distribution by Business Committee | - | - | - | - | - | 0.67 | 1.17 | 0.98 | 1.03 | 1.06 | 1.26 | 1.31 | 1.48 | 1.54 | 1.59 | 1.64 | 1.70 | 1.76 | 1.84 | 1.90 |
| Increase in current assets | - | - | - | - | 1.59 | 0.33 | 0.10 | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Total application | 2.23 | 7.50 | 8.96 | 22.88 | 8.80 | 2.08 | 3.50 | 2.45 | 7.16 | 3.45 | 2.90 | 3.01 | 4.05 | 9.06 | 3.51 | 4.45 | 3.79 | 3.95 | 9.55 | 4.31 |
| Cash at end | - | - | - | - | 4.46 | 6.60 | 6.97 | 8.37 | 5.10 | 5.60 | 6.71 | 7.97 | 8.25 | 3.74 | 4.86 | 5.13 | 6.15 | 7.11 | 2.57 | 3.38 |
| Debt Service Coverage: (a) Generated Income plus Interest | | | | | 3.49 | 5.54 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 | 5.96 |
| (b) Maturities plus Interest | | | | | - | 2.41 | 3.44 | 3.44 | 3.45 | 3.45 | 3.45 | 3.25 | 3.24 | 3.25 | 3.25 | 3.24 | 3.24 | 3.24 | 3.24 | 3.25 |
| (c) Debt Service Coverage | | | | | - | 2.3 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 |

1/ Land
2/ Including principal and financial charges capitalized during construction.
3/ Working capital.

Annex 5
Table 3

# YUGOSLAVIA
# BABIN KUK HOTEL COMPLEX
## ESTIMATED CONSTRUCTION AND DISBURSEMENT SCHEDULE

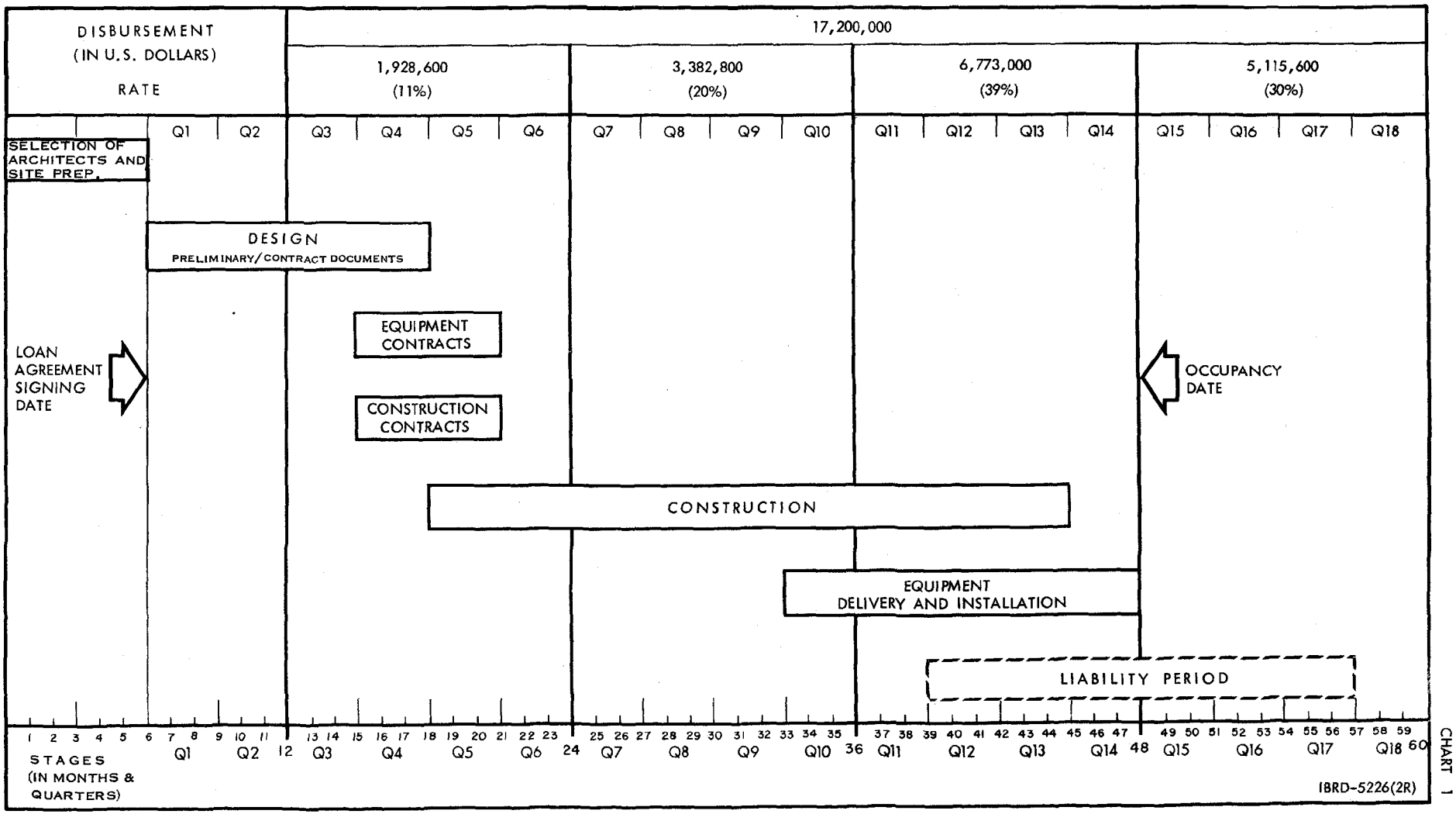
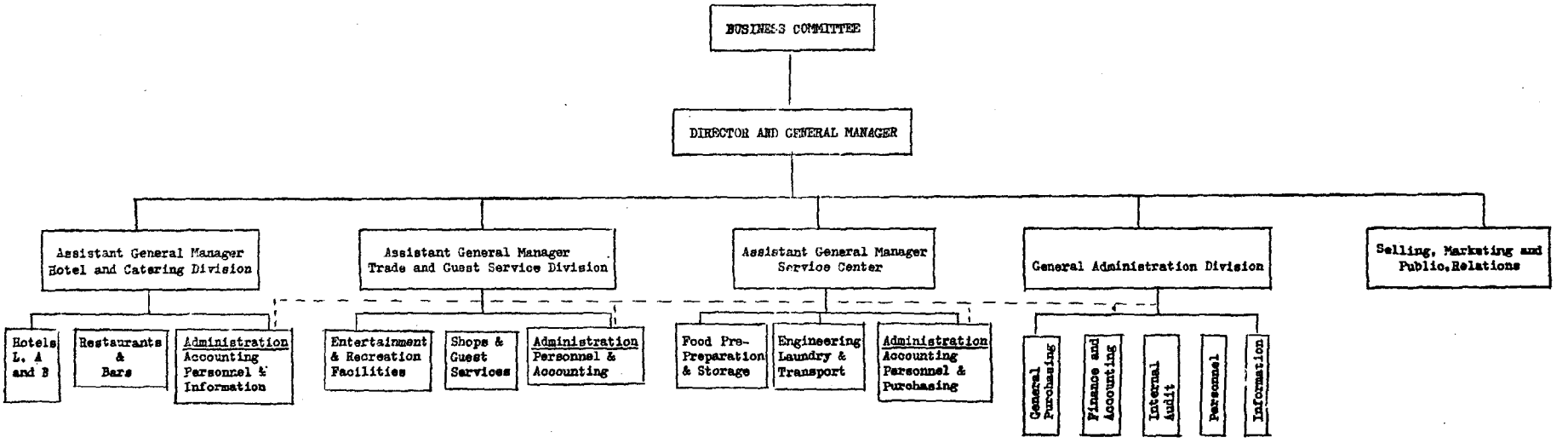



CHART 1

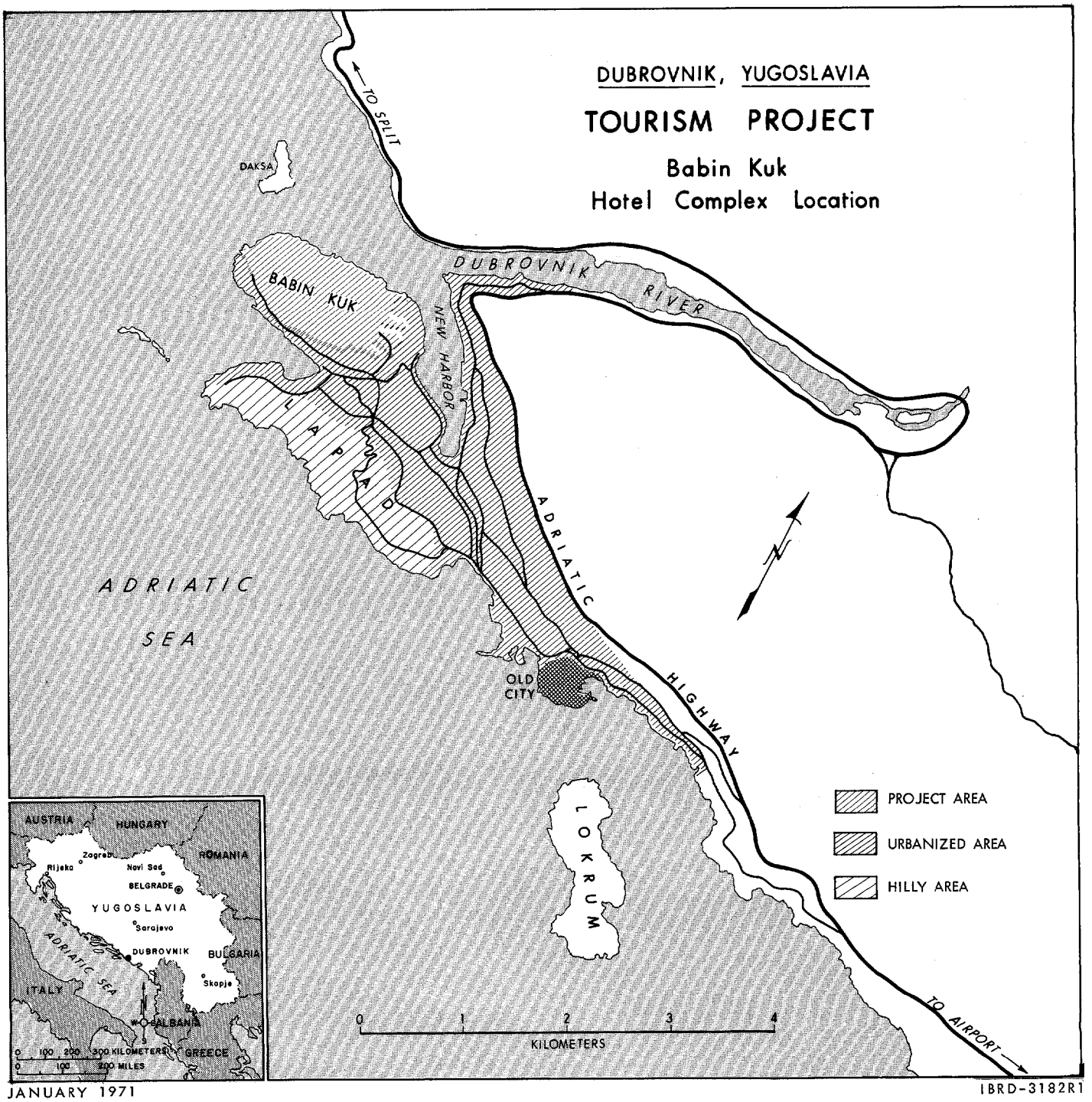
# YUGOSLAVIA: Babin Kuk Tourism Project

## GENERAL ORGANIZATION CHART




NOTES: Unbroken Lines indicate direct reponsibility
Broken Lines indicate indirect responsibility

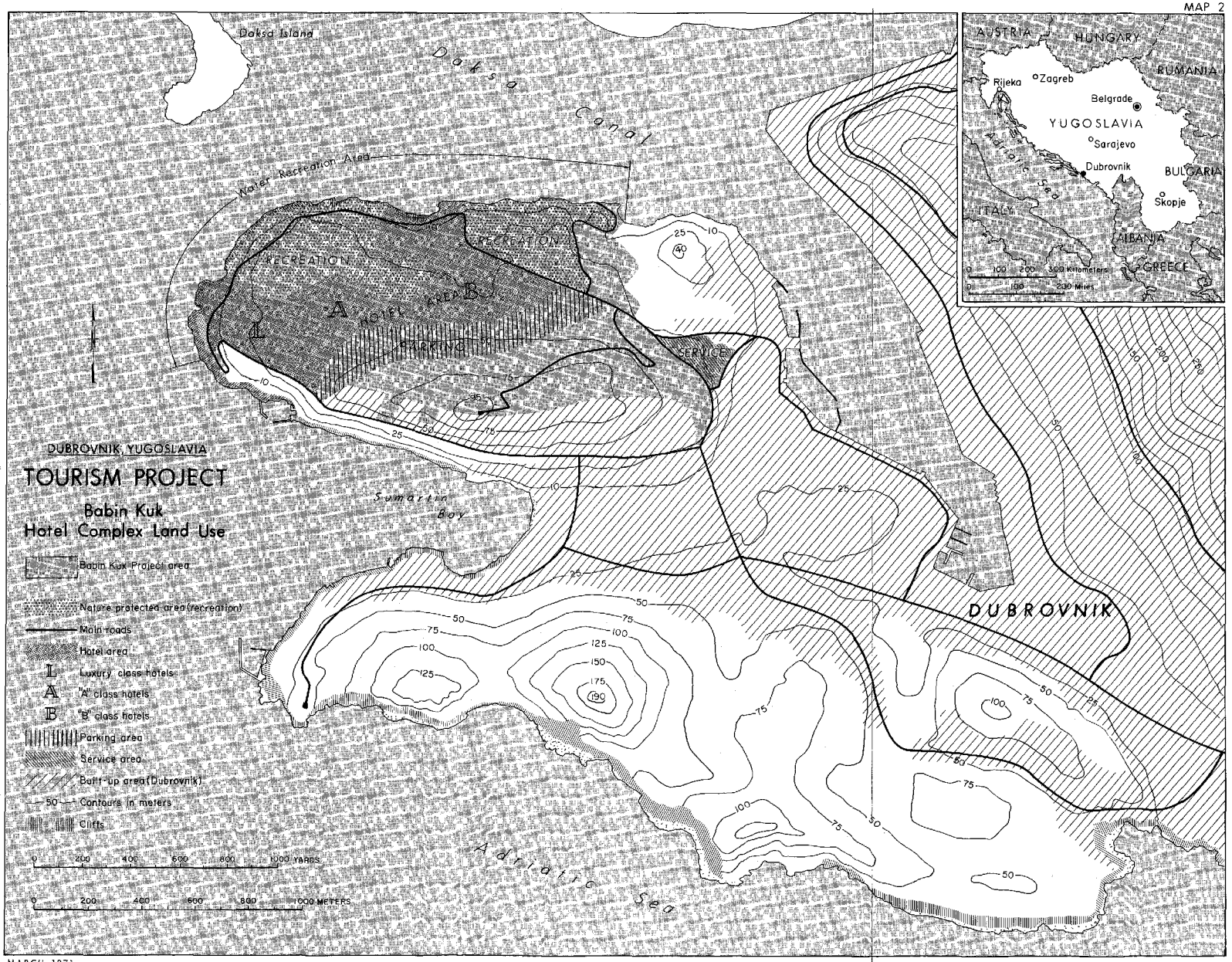
Chart 2




JANUARY 1971

IBRD-3182R1

MAP 2




MARCH 1971

IBRD 3243R