Accessing New Financial Markets and Improving Borrowing Terms in Serbia

Background

After transition-related declines in GDP and armed conflict in the 1990s, Serbia has restored macroeconomic stability in the last decade and achieved high growth. Aided by stabilization measures and structural reforms in public and financial sectors, Serbia is today on sound footing and taking steps to improve its debt management capacity.

Despite high financing requirements, Serbia has accessed the international markets only once, as Serbia and Montenegro. After the 20-year Eurobond issue in 2005, which raised USD 1 billion, Serbia did not return to the global capital market independently, tapping instead the local capital market and domestic banking sector. Diversifying sources of funding could help Serbia reduce cost over time and avoid crowding out private sector financing.

Supporting the government's efforts to promote private sector-led growth and strengthening the Serbian financial sector through a series of development policy operations was an important element of the World Bank’s Country Partnership Strategy for Serbia in FY 2008-2011. In this context, Serbia requested an IBRD Policy-Based Guarantee (PBG) rather than an IBRD loan to help access the international loan market to fund one of these operations.

Financing Objectives

Serbia needed sound financing to further advance its strong track record in structural reforms and improve its business environment, strengthen financial discipline in the non-private enterprise sector, and build a stable and more efficient financial sector. It also faced large liabilities from maturing debt in the next five years and was therefore seeking funding with a tenor longer than the 3-year average life possible in the local market. Furthermore, Serbia’s debt management strategy for 2011-2013 aimed to access new sources of financing in global markets and reduce roll-over risk in the public debt portfolio.

IBRD Financial Solution

On February 14, 2011, the World Bank Board of Directors approved a PBG to help Serbia access international markets, and support its reform program. The PBG covers the principal repayment risk of a 6-year commercial bank loan of EUR292.6 million (approximately USD 400 million) with bullet maturity, on a non-accelerable basis. The PBG does not guarantee interest payments.

Outcome

The transaction punctuated Serbia’s return to the international financial market and helped mobilize EUR292.6 million. The PBG allowed the Government to double the average life of market borrowing at a markedly reduced cost of funding as the result of financial bidding by a number of international banks. Figure 1 provides a comparison of Serbia’s access to financing in the local market without a guarantee to access to an international commercial bank loan with an IBRD guarantee. The longer maturity is expected to strengthen Serbia’s debt portfolio by reducing refinancing risks, particularly given uncertainty in the financial markets in the near term. At a borrowing spread of 100 basis points above EURIBOR, the transaction has resulted in roughly USD 80 million in net present value savings for Serbia.

Another important benefit of this transaction for Serbia was the experience gained through engagement with global lenders. International banks had the opportunity to familiarize themselves with the Serbian credit story through due diligence activities. Ten banks submitted proposals for the transaction. With the PBG, Serbia re-established itself as a global borrower, which could help create context for better terms for future market borrowings. This transaction has also provided positive signals to financial markets about Serbia’s access to diversified sources of capital, which may reduce perceived credit risk over time.

Highlights

- Despite high financing requirements, Serbia has accessed the international markets only once, as Serbia and Montenegro.
- A Policy-Based Guarantee from IBRD helped Serbia raise EUR 292.6 million from a global lender.
- This transaction signals to markets about Serbia’s access to diversified sources of capital, which may reduce perceived credit risk over time.
## Summary of Terms: Serbia PBG

<table>
<thead>
<tr>
<th>Closing Date</th>
<th>April, 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Type of Guarantee</strong></td>
<td>IBRD Policy-Based Guarantee (PBG)</td>
</tr>
<tr>
<td><strong>Coverage</strong></td>
<td>100% of principal at maturity on a non-accelerable basis</td>
</tr>
<tr>
<td><strong>Amount</strong></td>
<td>EUR 292.6 million</td>
</tr>
<tr>
<td><strong>Term</strong></td>
<td>6 years</td>
</tr>
<tr>
<td><strong>Structure</strong></td>
<td>Bullet payment</td>
</tr>
</tbody>
</table>

### Figure 1: Cost comparison: Serbia borrowing with and without IBRD guarantee

- Govt. borrowing from local banks with no IBRD guarantee
  
  EURIBOR + Spread for 6y* 6-8%**

- Govt. borrowing from global lender with IBRD guarantee
  
  EURIBOR + Commercial loan spread 1%*

* Excludes arrangement fees and IBRD fees; actual interest rate was fixed for the loan.

** These indicative spreads were extrapolated from the Serbian Government’s last borrowing at an average life of 3 years around the time period of the transaction.

---

For more information, please contact:
Miguel Navarro-Martin, Head of Banking Products, [mnavarromartin@worldbank.org](mailto:mnavarromartin@worldbank.org), +1 (202) 458-4722
Pankaj Gupta, Manager of Financial Solutions Unit, [pgupta2@worldbank.org](mailto:pgupta2@worldbank.org), +1 (202) 473-6188