DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT

Approved by the Board of Directors on 25 June 2024[1]

MONTENEGRO

MONTENEGRIN RAILWAYS PASSENGER TRAINS PROJECT

[Redacted in line with the EBRD's Access to Information Policy]

[Information considered confidential has been removed from this document in accordance with the EBRD's Access to Information Policy (AIP). Such removed information is considered confidential because it falls under one of the provisions of Section III, paragraph 2 of the AIP]

1 As per section 1.4.8 of EBRD's Directive on Access to Information (2019), the Bank shall disclose Board reports for State Sector Projects within 30 calendar days of approval of the relevant Project by the Board of Directors. Confidential information has been removed from the Board report.

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

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ABBREVIATIONS / CURRENCY CONVERSIONS

DSCR	Debt Service Coverage Ratio
EBITDA	Earnings before Interest, Taxes, Depreciation and Amortisation
EE	Energy Efficiency
E&S	Environmental and Social
ESAP	Environmental and Social Action Plan
ESDD	Environmental and Social Due Diligence
ESIA	Environmental and Social Impact Assessment
EU	European Union
EUR	Euro
EUROFIMA	European Company for the Financing of Railroad Rolling Stock
EMU	Electric Multiple Unit
GBVH	Gender Based Violence and Harassment
GDP	Gross Domestic Product
GoM	Government of Montenegro
HR	Human Resources
IFRS	International Financial Reporting Standards
IMS	Integrated Management System
IPA	Instrument for Pre-accession Assistance
MoF	Ministry of Finance
MoTMA	Ministry of Transport and Maritime Affairs
OHS	Occupational Health and Safety
OZVS	Održavanje Željezničkih Voznih Sredstava
PSC	Public Service Contract
PSD	Project Summary Document
PP&R	EBRD Procurement Policies and Rules
SEP	Stakeholder Engagement Plan
SMS	Safety Management System
SOE	State-Owned Enterprise
SSF	Shareholders Special Fund
VAT	Value Added Tax
ZCG	Željeznica Crne Gore a.d. Podgorica
ZICG	Željeznička Infrastruktura Crne Gore a.d. Podgorica
ZPCG	Željeznički Prevoz Crne Gore a.d. Podgorica

PRESIDENT'S RECOMMENDATION

This recommendation and the attached Report concerning an operation in favour of Željeznički Prevoz Crne Gore a.d. Podgorica (the **"Company", "ZPCG"**, or the **"Borrower"**), the majority state owned national passenger rail operator of Montenegro, are submitted for consideration by the Board of Directors.

The facility will consist of a sovereign loan to the Company in the amount of up to EUR 30 million to help the Company enhance the efficiency and quality of its services through the acquisition of electric multiple unit ("EMU") trains to replace old and energy inefficient loco-hauled train sets (the "**Project**"). The loan will be fully guaranteed by the State of Montenegro (the **"Guarantor"**).

The expected transition impact of the Project derives primarily from the *Well-Governed* quality through enhancement of the Company's corporate governance standards and practices. The secondary transition quality is *Green* through reduction of CO_2 emissions as a result of the purchase of new energy efficient rolling stock. The Project is 100% GET eligible.

TC support for this operation will be provided by the European Union ("EU") Instrument for Pre-accession Assistance ("IPA") for corporate governance and the EBRD Shareholder Special Fund ("SSF") for project preparation.

I am satisfied that the operation is consistent with the Bank's Strategy for Montenegro 2021-2026, the Transport Sector Strategy 2019-2024, the Green Economy Transition (GET) approach 2021-2025, the Strategy for the Promotion of the Gender Equality 2021-2025 and with the Agreement Establishing the Bank.

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

Odile Renaud-Basso

BOARD DECISION SHEET

MONTENEGRO – Montenegrin Railways Passenger Trains Project – DTM 55258	
Transaction / Board Decision	Board approval[2] is sought for a senior loan of up to EUR 30 million in favour of Željeznički Prevoz Crne Gore a.d. Podgorica **("ZPCG",** the **"Company"**, or the **"Borrower"**), to finance the acquisition of three new EMU trains to replace existing old, energy inefficient loco-hauled train sets (the **"Project"**). The loan will be guaranteed by the State of Montenegro (the **"Guarantor"**).
Client	ZPCG is a majority state-owned company and is the sole passenger train operator in Montenegro. The state owns 90.79% of the Company shares, while the remainder is owned by investment funds (4.55%), individual investors (4.58%) and others (0.08%). In 2022, the Company reported EUR 10.3 million revenues and EBITDA of EUR 3.5 million.
Main Elements of the Proposal	Transition impact: - **Well Governed (primary)** through the Company's and the Guarantor's (where applicable) undertaking to implement a corporate governance action plan addressing the Company's deficiencies. - **Green (secondary)** through the renewal of the rolling stock fleet resulting in estimated average savings of 18,145 tonnes of CO_2 over the evaluation period from 2026 to 2037, which represents savings at the level of 53%. The Project is 100% GET eligible. Additionality: The EBRD loan offers a tenor that is longer than the market average. The Bank will support the Company to enhance its governance standards as well as to amend the Public Service Contract ("PSC") in line with EU standards, which will help improve its financial sustainability. The Project will utilise EBRD's expertise for the adoption of gender standards. Sound banking: The transaction is structured as a sovereign-guaranteed loan.
Key Risks	Sovereign risk: Montenegro's economy grew by 6% in 2023 and is projected to slow down to 3.7% in 2024 due to moderation of tourism growth which reached record levels in 2023. [REDACTED]. The risks are mitigated by ongoing fiscal consolidation underpinned by a medium-term fiscal strategy and other structural reforms as the country progresses with the EU accession. Implementation Risk: [REDACTED]. The risk will be mitigated by appointing an international consultant, acceptable to the Bank, to assist the Company with project preparation, procurement, and implementation of the Project.
Strategic Fit Summary	The Project is consistent with: the Bank's **Strategy for Montenegro 2021-2026** which focuses among others on deepening Montenegro's Green Economy Transition through increased energy and resource efficiency and climate resilience as well as improved performance, service delivery and sustainability of infrastructure, the **Transport Sector Strategy 2019-2024** by scaling-up high GET investments in the transport sector through investments supporting the green agenda, the **Green Economy Transition (GET) approach 2021-2025** by supporting a more efficient and greener mode of transport to achieve significant environmental benefits and **the Strategy for the Promotion of the Gender Equality 2021-2025,** which recognises Gender Based Violence and Harassment **("GBVH")** as an obstacle for women equal participation in the economy and public life.

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

ADDITIONAL SUMMARY TERMS FACTSHEET

EBRD Transaction	A senior loan of up to EUR 30 million to the Company guaranteed by the State of Montenegro (the **"Guarantor"**) to finance the purchase of three new four-car EMU train sets to be used for operations throughout the whole railway network of Montenegro (the **"Project")**. The new rolling stock will replace the existing old, energy inefficient loco-hauled train sets resulting in estimated average savings of 18,145 tonnes of CO_2 over the evaluation period from 2026 to 2037, which represents savings at the level of 53%. The Project is 100% GET eligible.
Existing Exposure	[REDACTED]. The Bank's total sovereign portfolio in Montenegro as of 20 March 2024 was EUR 192 million [REDACTED]. This includes sovereign loans of EUR 34.6 million under the Local Roads Reconstruction Project (DTM 43060, DTM 48169 and DTM 51798), EUR 26.2 million under the Main Roads Reconstruction Project (DTM 49075), while the remaining exposure relates to sovereign guaranteed loans.
Maturity / Repayment	15 years [REDACTED].
Potential AMI eligible financing	None.
Use of Proceeds	The Bank's loan will be used to finance acquisition of three new four-car passenger EMU trains to be procured in accordance with the Bank's Procurement Policies and Rules ("**PP&R**") provisions on the "Open Tendering".
Investment Plan	[REDACTED]
Financing Plan	[REDACTED]
Key Parties Involved	- The Company (as the Borrower) - Ministry of Finance (as the representative of the Guarantor)
Conditions precedent to effectiveness	[REDACTED]
Conditions to disbursement	[REDACTED]
Key Covenants	[REDACTED]
Security / Guarantees	Sovereign-guaranteed loan
Other material agreements	Guarantee Agreement between the Bank and Montenegro.
Associated Donor Funded TC and co-investment grants/concessional finance	*Pre-signing* • **TC 1: Technical Due Diligence for** the overall technical assessment of the Project (note: this assignment also supported the Railways Maintenance Equipment Renewal Project (OPID 51806)). The cost of this assignment was EUR 65,000 and was supported by the SSF. *Completed.* • **TC 2: Economic Due Diligence** for the economic assessment of the Project (note: this assignment also supported the Railways Maintenance Equipment Renewal Project (OPID 51806)). The cost of this assignment was EUR 55,000 and was supported by the SSF. *Completed.* *Post-signing* • **TC 3: Project Implementation Support,** a PIU support consultant will support the Client in all aspects of implementation and in meeting the requirements of the Bank's financing documents. The support will include, in particular, project preparation, preparation of the tender documents (including technical specifications), contract administration, financial control, project management and reporting. The assignment will include an independent pre-shipment inspection with the Company. The estimated cost of the assignment [REDACTED]is expected to be funded by an international donor or the SSF. • **TC 4: Procurement Support,** an individual consultant to assist the Client with the procurement of the PIU support consultant, on-the-job training for the preparation of the procurement documents, workshops on the Bank's PP&R and best procurement practices. The estimated cost of the assignment

	[REDACTED] is expected to be funded by an international donor or the SSF. • **TC 5: Revisions of the Public Service Contract,** to assist in amendment of the PSC aligning it with the EU regulations and best international practice while enabling the implementation of the new Law on Railway Transport that is to be adopted in 2024 in the field of public service obligation. The estimated cost of this assignment [REDACTED] to be funded by the EU IPA, under the EU reform Facility. • **TC 6: Enhancements of the Company's corporate governance standards and practices** through the adoption of the corporate governance action plan ("CGAP"). The estimated cost of this assignment is [REDACTED] to be funded from the EU IPA, under the EU reform Facility. **Reimbursement:** The above assignments are non-reimbursable transactional TCs required to evaluate the investments and assist the Client with project preparation and implementation as well as enhancement of corporate governance. **Cost sharing:** The Borrower will be responsible for paying all VAT and other indirect taxes that are applied to the post-signing TC assignments, thus providing a parallel cost sharing contribution to the Project (VAT is levied at 21% in Montenegro).

[REDACTED]

INVESTMENT PROPOSAL SUMMARY

1. STRATEGIC FIT AND KEY ISSUES

1.1 STRATEGIC CONTEXT

The Western Balkans region is one of the most affected by climate change in Europe with **estimated temperature increases of 1.7 – 4.0°C,** and even expected to exceed 5.0°C by the end of the century, depending on the global effort to reduce greenhouse gases emissions. The region has already seen severe consequences of climate change[3]. Reducing the emissions of air pollutants and greenhouse gases (GHG) has become a priority, which is strongly interlinked with energy, transport, and health policies, among others. **The transport sector is the second largest contributor of the GHG emissions in the region representing 12% share of these emissions in 1990 and reporting increase to 16% in 2018.** The usage of rail transport over long distances in the region is not on a satisfactory level. **The passenger modal split in the region is far behind the EU-28 average because of several influencing factors such as** reliability of timetable, quality of service or lack of financial sustainability of the operator being some of them. To decarbonise transport, improvement of the rail infrastructure is crucial. In Montenegro specifically, 96.4% of the overall passenger transport on land is undertaken by personal cars (comparing to 81.8% in the EU-28) with railways share being at the level of 1.3% only (7.9% in the EU-28)[4].

The railway sector in Montenegro underwent extensive reforms between 2007-2012 driven by a strong political will of the Montenegrin Government to introduce liberalisation and commercialisation of the sector. In this context, in 2008, the then Montenegro Railways Company (**"ZCG"**) was unbundled into four separate companies: (i) Zeljeznicka Infrastruktura Crne Gore (**"ZICG"**) responsible for the railway track, (ii) MonteCargo – a freight operator, (iii) Rolling Stock Maintenance company (**"OZVS"**)[5] and (iv) ZPCG – a passenger operator. All companies remain majority-owned by the State.

The Project will finance the acquisition of three new passenger EMU train sets to replace existing, nearly 40-year-old trains still operating on the rail network. The manufacturers of the existing train sets have ceased production and spare parts are only obtainable from third party manufacturers or from other scrapped sets. Either of these alternatives is a short-term measure while, in order to upgrade and modernise the passenger rail fleet, ZPCG needs to acquire replacement rollingstock. Apart from the renewal of the passenger rail fleet, the Project will bring significant benefits both for the Company as well as for the users of the public transport and infrastructure in general, such as:

- improved reliability, punctuality and comfort of the users resulting in diversion of the negative trends such as very low and declining usage of the railway transportation; and
- reduction of the maintenance and operational costs of ZPCG due to: (a) much easier access to the spare parts in case of new rolling stock; (b) reduction of manpower required for the operation of the new rolling stock (single driver required for the operation of the new EMUs comparing to two needed for the old locos); and (c) significantly lower consumption of the electricity due to the lighter weight of the new rolling stock with more energy efficient trains and the ability in the future years to take advantage of electricity regeneration.

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2 Those include floods in Bosnia & Herzegovina and Serbia in 2004, 2010 and 2014, heavy snowfalls causing avalanche in Kosovo in 2012 and resulting in ten fatalities, wildfires in Bosnia & Herzegovina in 2017 or droughts in 2000, 2003, 2007 & 2008 in the same country and in Kosovo and depending on the year destroying between 40-70% of agricultural production

4 GAP Analysis – Strategy for Sustainable and smart mobility in the Western Balkans.

5 For economic benefits there are recent plans to merge OZVS with ZPCG by the end of 2024.

The Project is estimated to result in average savings of 18,145 tonnes of CO_2 over the evaluation period from 2026 to 2037, which represents a reduction in CO_2 emissions of 53%. The Project is 100% GET eligible.

In addition, the Project will help the Company improve its corporate governance through the Company's undertaking to implement the CGAP, as well as to align the PSC with the EU regulations and the new Law on Railway Transport which is to be adopted in 2024.

The Women, Business and the Law 2024[6] (**"WBL"**) report published by the World Bank Group assesses the supportive frameworks in Montenegro at a score of 50.8 out of 100.0 which is lower than the Europe & Central Asia regional average score (51.3). Despite a modest gap in scores, violence against women remains a problem in many developing countries and the perpetrators often go unpunished. According to WBL, one of the lowest scores for Montenegro is on the indicator measuring supportive frameworks affecting women's safety. Safety is a major concern for women choosing among public and private transport options. Women are at greater risk of violence, sexual harassment, and sexual assault from strangers on public transportation and walking to and from transportation. High levels of harassment and other abuse in public transportation can also limit women's willingness to travel, reducing their earning options (woman might forgo a well-paying job for one paying less that is closer to her home, or women's absenteeism might increase and productivity decrease because of the psychological effects of sexual harassment). Therefore, violence against women and girls (VAWG) in transport and related public spaces can limit the success of infrastructure programs aimed at improving access to resources and services (jobs, health, and education). The Project will help the Company introduce appropriate measures and procedures to minimize the risk of GBVH in the railway system, contributing to the safety of women and girls, hence increasing their access to employment opportunities.

The Project is consistent with the following strategies:

- **Strategy for Montenegro (2021-2026) (BDS/MT/21-01)**, which includes a focus on deepening Montenegro's Green Economy Transition through increased energy and resource efficiency and climate resilience as well as improved performance, service delivery and sustainability of infrastructure;
- **Transport Sector Strategy 2019-2024 (BDS19-172 (F))** which concentrates on scaling-up high GET-impact investments in the transport sector through investments supporting the green agenda;
- **Green Economy Transition (GET) approach 2021-2025 (BDS20-082/F),** which recognises the benefits of EBRD lending to public sector entities to achieve significant environmental benefits in the form of CO2 emission reduction and reduction of air pollution.
- **Strategy for the Promotion of the Gender Equality 2021-2025 (BDS21-133(F))** recognises Gender Based Violence and Harassment **("GBVH")** as an obstacle for women equal participation in the economy and public life while supporting clients to introduce measures to eliminate the risk of GBVH in infrastructure projects became one of the strategic directions of that Strategy. The Project will help the Company undertake several measures such as developing the procedure for: (i) establishing of Internal Security Service aiming to protect the property and passengers on the train; (ii) establishing the operational centre for quick interventions and reporting; (iii) training the personnel on how to deal with passengers affected by GBVH; and (iv) introducing an information campaign on the relevant procedure being implemented.

[6] https://wbl.worldbank.org/content/dam/documents/wbl/2024/pilot/WBL24-2-0-Montenegro.pdf

1.2 TRANSITION IMPACT

The Project's transition qualities include *Well-Governed* (primary) and *Green* (secondary) as follows:

- **Well-Governed (primary)** through the Company's and the Guarantor's (where applicable) undertakings to implement a corporate governance action plan; and
- **Green (secondary)** through the renewal of the rolling stock fleet resulting in estimated average savings of 18,145 tonnes of CO_2 over the evaluation period from 2026 to 2037, which represents savings at the level of 53%. The Project is 100% GET eligible.

Primary Quality: Well-Governed

Obj. No.	Objective	Details
1.1	*The Company will improve its CG from a base level that on par with the average in the country and sector.* *The CGAP will have a very likely and significant impact on the country/sector because of the client's large size or because of the high visibility of the project.* *The CGAP addresses all CG issues identified in the company.* *[REDACTED]*	[REDACTED]. The Bank undertook an in-house corporate governance review (initially in 2021 with an update in 2024) which revealed several areas for improvement. [REDACTED]. In order to address identified deficiencies, a CGAP was prepared aiming at improvements on both the state-level and company-level practices and processes. Due to the Company's size and the national coverage, the corporate governance improvements are very likely to become the benchmark for the other SOEs in the country. The EBRD Corporate Governance country assessment for Montenegro also highlights a number of key corporate governance challenges [REDACTED]. All of these issues have been addressed in the proposed CGAP which will be implemented as part of the Project. Apart from them, the Bank will provide the TC to amend the PSC aligning it with the EU regulations and best international practices while enabling the implementation of the new Law on Railway Transport that is to be adopted in 2024, in the area of public service obligation. Therefore, the Project will include implementation of a CGAP in order to assist the Company and the State (as its shareholder) in addressing the issues identified and improve the Company's corporate governance. [REDACTED] The Project will also aim to support the Company in implementing the CGAP through a dedicated TC aimed at providing expertise and knowledge not readily available in the Company and providing related capacity building where relevant.

Secondary Quality: Green

Obj. No.	Objective	Details
2.1	The percentage of EBRD use of proceeds allocated to the project that qualifies as GET is equal to or exceeds the sectoral threshold agreed in the GET TI assessment methodology.	The Project is 100% GET eligible. The Project is estimated to result in average savings of 18,145 tonnes of CO_2 over the evaluation period from 2026 to 2037, which represents a reduction at the level of 53%.

1.3 ADDITIONALITY

Identified triggers*	**Description**
*A subsequent/consecutive transaction with the same client/group either with the same use of proceeds or in the same country (**repeat transaction**)*	The Bank provides long-term financing, which is not readily available in Montenegro from local or international commercial banks. The proposed tenor and grace period are longer than the market average, and are necessary to structure the Project given its use of proceeds. The Bank's experience in financing similar projects, existing long-term client relationships and on-going policy dialogue on sector reform process is highly appreciated by the Client and Government.
Additionality sources	
Financing Structure - *EBRD offers a **tenor**, which is above the market average and is necessary to structure the project*	As mentioned above, the Bank provides long-term financing, which is not readily available in Montenegro from local or international commercial banks. The proposed tenor and grace period are above the market average, and are necessary to structure the Project given its use of proceeds.
Standard-setting: helping projects and clients achieve higher standards. *Client seeks/makes use of EBRD expertise on **corporate governance** improvements, including for climate risk management.* *Client seeks/makes use of EBRD expertise on **best international procurement standards**.*	The Bank's experience in financing similar projects, existing long-term relationship with both the Company and the Government and on-going policy dialogue on sector reform process is highly appreciated by Montenegrin side. The Company will also comply with the Bank's environmental and social policies. As part of the Project, the Company and the Guarantor will undertake to sign the PSC in line with best market practices and EU regulations. In addition, the Company will implement a CGAP with the aim to improve its corporate governance. Provision of the loan to finance the Project is also supplemented by the TC to build the Company's procurement and project management capacity and procure the trains in line with the Bank's PP&R.
Gender SMART: *Client seeks/makes use of EBRD expertise for the adoption of gender standards and/or equal opportunities action plans (e.g. improving women's access to safe transport and/or women-led businesses participation in the client supply chain).*	The Client plans to set up an operational centre for quick and urgent interventions in the protection of persons and property. This will include the: - Set-up of emergency calls, emergency sms, anonymous reports for potential victims of violence. This will also allow the Company to collect the data on such incidents currently not reported on. - Training for employees to act adequately in given situations. - Development of a campaign through social networks and in trains and stations using flyers, videos, visuals, which would inform passengers on prevention and the procedure for reporting such cases. - Additional training of personnel in direct contact with passengers (conductors, cashiers, information workers, train drivers) to implement the procedure, provide information and recognize and adequately deal with victims of violence. The Company also plans to cooperate with international and national organizations and institutions for staff training in respect to GBVH.

1.4 SOUND BANKING - KEY RISKS

Risks	Probability / Effect	Comments
Sovereign risk	*Low/ Medium*	- As of March 2024, Standard & Poor's credit rating for Montenegro stands at B with a positive outlook. Moody's credit rating for Montenegro was last set at B1 with stable outlook as of September 2023. - Strong economic growth continued in 2023 with GDP growth at 6.1 per cent in 2022 and 6 per cent in 2023, boosted by robust household consumption (fuelled by immigration wave from Ukraine and Russia) and a strong performance of the hospitality sector. - Growth is projected to slow down, but risks are tilted towards the upside. After higher-than-expected growth in 2023, deceleration to 3.7 per cent is projected for 2024, due to moderation of tourism growth after a record season in 2023.
Dependence on state subsidies	*Low/High*	- The Company is highly dependent on state subsidies (79% of total revenues in 2022, down from 83% in 2020). [REDACTED]. - The risk is mitigated by the revision of the PSC between ZPCG and GoM, which will ensure an adequate methodology to support cost recovery and will allow ZPCG to better plan its investments and budget. The EU regulations allow the PSC to be concluded for up to 15 years (in exceptional cases the tenor might be extended up to 22 years), therefore the new PSC between ZPCG and GoM will be aligned with the EU regulations.
Operating costs	*Low / Low*	- The Company has a relatively high cost base with operating expenses representing approx. 77% of operating revenues. The Project will help the Company benefit from some cost savings in terms of lower maintenance costs, electricity consumption and personnel costs starting from year 2027.
Financial risk	*Low/Low*	- [REDACTED]. The risk is mitigated by: (i) improved PSC supporting a compensation level adequate to achieve costs coverage, including debt service and (iii) by the sovereign guarantee.
Implementation Capacity	*Low / High*	- [REDACTED]. The Project includes a TC for procurement capacity building to support the Company with the selection of the PIU support consultant in line with the Bank's PP&R; - An international consultant will support the PIU throughout project implementation;

2. MEASURING / MONITORING SUCCESS

Overall objectives of project	*Monitoring benchmarks*	*Implementation timing*
- Good financial and operational performance of the Company - On-time Project implementation i.e. procurement and delivery of the trains in line with the timeframe envisaged	[REDACTED]	[REDACTED]

Integrated Results Matrix

TI indicators, primary Quality: Well-Governed

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date
1.1	Corporate governance improved: Commitment to Corporate Governance	CGAP implemented.	No	Yes	[REDACTED]

TI indicators, secondary Quality: Green

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date
2.1	Annual amount of CO2 emissions reduced	The amount of CO2 emissions reduced due to vehicle-km performed by EMUs (based on 2.6kgr CO2 per vehicle-km)	No	1,300 tonnes	[REDACTED]

Additional Indicators

Indicator type	Monitoring indicator	Details	Baseline	Target	Due date
1.1	New public service contract signed and implemented	PSC signed and implemented.	No	Yes	[REDACTED]

3. KEY PARTIES

3.1 BORROWER

ZPCG was established in 2008 as a state-owned company responsible for the operation of passenger railway services in Montenegro, following the unbundling of ZCG, a reform supported by EBRD. The Company operates both EMU and loco-hauled services. It is responsible for the maintenance of the EMUs, with the loco-hauled rolling stock being maintained under a contract by the specialist maintenance company, OZVS. According to the latest information, there is a plan to merge OZVS with ZPCG by end-2024. ZPCG employed 382 staff as for the end of December 2023.

Domestic passenger railway services are operated over the Bar-Bijelo Polje mainline, and between Niksic and Podgorica. ZPCG also operates up to two return services daily to Belgrade, in conjunction with Serbia Voz. No passenger services are operated on the branch towards Albania.

The state owns 94.52% of the Company shares, while the remainder is owned by investment funds (2.79%), individual investors (2.53%) and other (0.15%). The Company is managed by a CEO and has a Board of Directors comprising five members, out of which four are appointed by the Government. The Company's organisational scheme is presented in Annex 2.

3.2 GUARANTOR

The Guarantor is the State of Montenegro represented by the Ministry of Finance ("MoF"). According to EBRD macro projections, Montenegro's economic growth is expected to slow down in 2024 to 3.7% following robust growth of 6% in 2023, fuelled by significant domestic consumption elevated by the migration from Ukraine and Russia. After a peak in 2020, general government debt moderated to 71% of GDP by YE 2022 on the back of strong economic growth and public debt repayments. IMF expects general government debt to decline to around 62 per cent in end-2023, before gradually increasing to 77% of GDP by 2028 due to the anticipated fiscal impact of the planned reform package. Given the better-than-expected GDP outcome, the general government debt to GDP ratio may have been lower in 2023 than the IMF expectation of 62% of GDP (it was around 60% of GDP as for the end of September 2023) and S&P expects general government debt at 54% of GDP for 2023.

After annual inflation peak in November 2022 (17.5%), inflation decelerated to 4.4% in January 2024. Net nominal wages maintained strong annual growth rates in the meanwhile, at 11% in 2023. A set of tax changes was introduced in July 2023 with the aim of boosting budget revenues, and the government brought in lower excise duties on fuel for farmers, fishermen and some transport companies. An extraordinary adjustment in the minimum pension, set to benefit a third of Montenegrin pensioners, was enacted from September 2023.

4. MARKET CONTEXT

Montenegro's main railway line is 167 km long and links Port of Bar on the Adriatic coast with Serbian capital city of Belgrade passing through the Montenegrin capital city of Podgorica which is the country's main rail hub. From Podgorica, there are two other main lines, north-west to Nikšić (57 km) and east to the Albanian border (25 km).

The railway sector in Montenegro is regulated by the Railways Administration located within the Ministry of Transport and Maritime Affairs ("**MoTMA**"). The scope of the rail regulator activities covers the necessary regulation and supervision of transport safety, allocating routes and usage of railway infrastructure, approving the timetable, and issuing of relevant licences.

The restructuring of Montenegro's rail sector was completed in 2008 following the unbundling of former ZCG, which was responsible for all railway operations, into four companies: (i) ZPCG; (ii) Railways Freight ("**MonteCargo**"); (iii) OZVS and (iv) ZICG. In February 2024, the Government of Montenegro decided to merge ZPCG and OZVS to achieve some costs savings and reflect the organisation of the companies widely applied in the other Western Balkan countries. As ZPCG is significantly larger, there will be no changes in its business apart from adding additional work on the trains' maintenance. The Government will, most likely, pay out minority shareholders and increase its ownership to 100%.

[REDACTED]. The existing contractual relationship between the Company and the Government of Montenegro is based on an annually negotiated contract, and therefore not ensuring long-term financial viability of the Company. [REDACTED]. The aim of the new PSC is to fix those deficiencies and align the tenor of the PSC with the tenor of the financing.

5. FINANCIAL / ECONOMIC ANALYSIS

5.1 FINANCIAL PROJECTIONS
[REDACTED]

5.2 SENSITIVITY ANALYSIS
[REDACTED]

5.3 ECONOMIC ANALYSIS
[REDACTED]

5.4 PROJECTED PROFITABILITY FOR THE BANK
[REDACTED]

6. OTHER KEY CONSIDERATIONS

6.1 ENVIRONMENT

Categorised B (ESP 2019). The Environmental and Social Due Diligence (**"ESDD"**) for the Project has been undertaken internally and included an environmental and social (**"E&S"**) assessment of the Project, review of the current operations, as well as the E&S management systems and the capacity of ZPCG as it relates to rail operations.

ESDD was carried out by means of questionnaires and a review of previous annual E&S reports submitted to the Bank over the past several years. Other relevant documents were also reviewed including the ISO certifications, the recent annual report on railway transport safety and other labour related documentation. Due to the time that had elapsed since the initial ESDD, further information was requested to confirm any E&S related updates within ZPCG operations. It is estimated that the Project will generate average savings of 18,145 tonnes of CO_2 over the evaluation period from 2026 to 2037.

Previous annual E&S reporting by ZPCG has been satisfactory and ZPCG has well established Human Resources (**"HR"**) policies. A new collective agreement has been effective from August 2023. ZPCG complies with national legislation related to labour and working conditions which are aligned with PR2. Some updates to existing labour arrangements are needed which includes the preparation of an updated retrenchment plan and further development of the worker grievance mechanism. The Bank will require both these documents to be submitted for review prior to any future retrenchment.

ZPCG has a certified integrated management system ("IMS") including ISO 14001 Environmental Management and ISO 45001 Occupational Health and Safety (**"OHS"**) which has been certified since 2016. The last independent audit was carried out in 2020 and included the migration from the OHSAS 18001 to ISO 45001. Annual E&S reports confirmed regular inspections take place annually by the relevant labour and environmental authorities, with no significant issues raised. The existing policy document for the IMS is available on ZPCG website and starting from September 2021 includes also ISO 45001:2018. ZPCG evaluates contractors E&S arrangements prior to selection and appointment although further development on contractor monitoring is needed to confirm implementation. ZPCG has an employee OHS rulebook which is also made available on their website and for operational safety, an formal safety management system (**"SMS"**) has been implemented and is audited annually.

ZPCG has an existing Stakeholder Engagement Plan (**"SEP"**) developed under the previous EBRD project and this requires a review and update to reflect changes since its original development. ZPCG will also develop arrangements on Energy Efficiency (**"EE"**), which include establishing an EE team, establish performance indicators and objectives and produce annual report on energy consumption.

The above requirements have been included in the Environmental and Social Action Plan **("ESAP"**) which has been developed and has been agreed with the ZPCG. The Bank will continue to monitor ZPCG activities through annual E&S monitoring reports and site visits if necessary.

6.2 INTEGRITY

In conjunction with OCCO, integrity due diligence was undertaken on the Borrower, its shareholders, senior management and other relevant parties. [REDACTED]

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

ANNEXES TO OPERATION REPORT

ANNEX 1- TRANSITION IMPACT SCORING CHART

Score for primary transition quality

Quality: Well-Governed
Component: Corporate-level governance
Quality average score: 68.8

ATQ adjustment

Country: Montenegro
ATQ adjustment: Corporate-level governance: -0.9%
Adjusted Quality score: 68.1

Score for secondary transition quality

Quality: Green
Component: Mitigation
Quality average score: 60.0

ATQ adjustment

Country: Montenegro
ATQ adjustment: Mitigation: 0.0%

Adjusted Quality score: 60.0

Weighted TI score

Base TI score (ATQ-adjusted): 66.1

Adjustment for Country Strategies

Adjustment: 0.0% – Not applicable
NA **Adjusted score:** 66.1

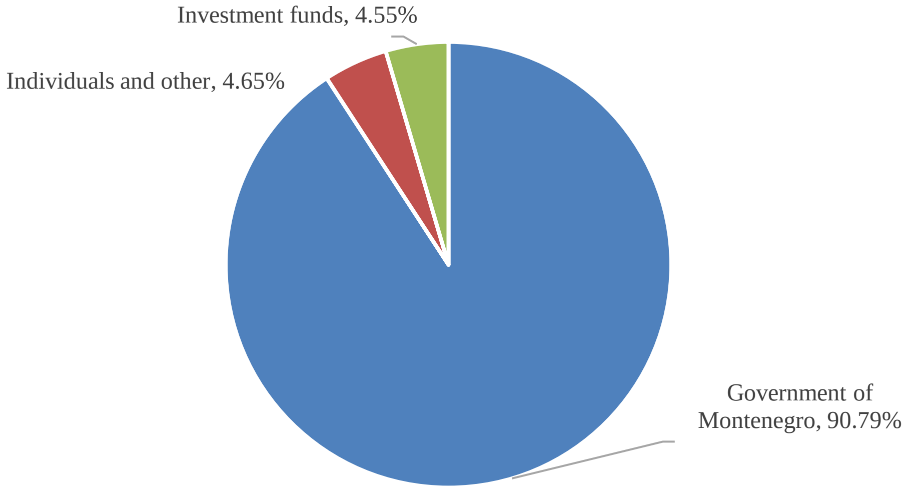
Local currency / Equity uplift

0.0% uplift

Final TI score

Final TI score: 66

ANNEX 2 – SHAREHOLDING STRUCTURE



The largest shareholders of the ZPCG include:

Company name	**Data on stocks / shares**	
	Number of shares	**Share percentage**
Government of Montenegro	6,459,640	90.79%
Individuals	325,692	4.58%
Open Investment Fund "TREND"	169,305	2.38%
Pension and disability insurance fund PIO	69,306	0.97%
Open Investment Fund "MONETA"	48,117	0.68%
Employment Agency of Montenegro	27,635	0.39%
CKB AD/CK Collective custody account 1	4,018	0.06%
UNIPRED - BIJELO POLJE	3,863	0.05%
FOND ZA OBEŠTEĆENJE	1,665	0.02%
Other	5,394	0.08%
Total amount of shares	**7,114,635**	**100.00%**

ANNEX 3 – TIMS DETAILS OF ZPCG FORMER PROJECT (DTM 41899)

[REDACTED]

ANNEX 4 – PROJECT IMPLEMENTATION

Procurement classification – *Public sovereign*

Project risk assessment:

[REDACTED]. The Client's capacity was assessed during a meeting with its representatives in Podgorica. The Client is ZPCG, the company that handles passenger transport within Montenegro, as well as the operation of the Montenegrin rolling stock. ZPCG is an existing client of the Bank. [REDACTED].

ZPCG will establish the PIU for the purpose of implementing the Project. [REDACTED] [T]he PIU will be supported by a PIU support consultant, appointed competitively in accordance with the EBRD PP&R.

Contracts risk assessment - *High/Moderate*

The contract proposed to be financed from the Bank's loan is detailed in the attached Procurement Plan. The support of an experienced consultant will ensure that technical specifications, employer's requirements and tender documents are suitable for open tendering and aligned with the Bank's PP&R.

The nature of the CAPEX contract, which includes the procurement of the trains, is generally considered of high/medium complexity, and has an equivalent degree of implementation risk. The risk will be mitigated by the appointment of an implementation consultant that will assist the Client along the entire project cycle.

Project implementation arrangements:
The Project will be implemented by ZPCG, which oversees the operation and maintenance of the rolling stock in Montenegro. The PIU will be established by ZPCG and will be supported by an international consultant. These arrangements will address the risks and ensure smooth project implementation.

The PIU consultant will assist the PIU in all aspects of implementation and in meeting the requirements of the Bank's financing documents. In particular, the consultant will provide support in the following areas: preparation of the tender documents in accordance with the Bank's latest standard procurement documents (including technical specifications), tendering, contract administration, final independent pre-shipping inspection at the manufacturer's site.

Procurement arrangements:
There will be one goods contract for the procurement of three four-car trains for the transport company. The trains will be procured following open tendering procedures in accordance with the requirements of the Bank's PP&R for public sector operations and will be subject to prior review by the Bank. It is envisaged that the tender documents for the procurement of goods will be based on the latest version of the Bank's standard procurement documents for goods.

The Project also envisages two technical cooperation contracts:

1. A Procurement expert, which will be selected through direct contracting, given the value of the assignment; 2. A PIU support consultant, which will be selected through competitive selection procedure.

The contracts will be tendered via the EBRD Client E-Procurement Portal (ECEPP) and will be subject to prior review. [REDACTED].

ANNEX 5 – GREEN ASSESSMENT

1. Introduction

The Project will involve the acquisition of three, new electric multiple unit ("EMU") for passengers. The Project was assessed for Paris Agreement (PA) alignment, GET and climate related financial risk. The Project is assessed as positively aligned for both mitigation and adaptation goals of the PA and is attributed as 100% GET.

2. Paris alignment assessment

General screening of alignment with the mitigation goals of Paris Agreement
The Project/economic activity is considered to be **included** in the 'aligned list' category of 'Electric Passenger or Freight Transport'.

Alignment with the adaptation goals of Paris Agreement
Step 1: Evaluation of the physical climate risk and vulnerability context:
The Project involves acquisition of moveable assets. Whilst the operation of these assets may be impacted by impact of climate change on other assets of the system (for example extreme heat impacting electric supply, or flooding of the network), the physical climate risk faced by the assets being financed by the Bank are not material.

Step 2: Definition of climate resilience measures:
No specific climate resilience measures have been incorporated, as no material risks to the assets being financed by the Bank were identified.

Step 3: Appraisal of broader climate resilience context:
The Project does not undermine the resilience of wider systems and is not inconsistent with the national policy for context adaptation.

The Project satisfies the three steps of the adaptation approach, and is thus considered aligned with adaptation goals of the Paris Agreement.

3. GET attribution

The Project is 100% GET eligible in line with the GET Handbook A.5.3.1.1. Zero-direct-emissions fleet and related infrastructure for electric rolling stock, as Use of Proceeds specifies purchase of "three new four-car passenger Electric Multiple Units ("EMU") trains". The Project is anticipated to result in CO_2 savings of 1,512 tonnes CO_2 per year on average over the period 2024-2037.