

**PROJECT INFORMATION DOCUMENT (PID)
APPRAISAL STAGE**

Report No.: PIDA4898

Project Name	Kosovo Energy Efficiency and Renewable Energy Project (P143055)
Region	EUROPE AND CENTRAL ASIA
Country	Kosovo
Sector(s)	Energy efficiency in Heat and Power (80%), Other Renewable Energy (20%)
Theme(s)	Other public sector governance (20%), Climate change (80%)
Lending Instrument	Specific Investment Loan
Project ID	P143055
Borrower(s)	Republic of Kosovo
Implementing Agency	Kosovo Energy Efficiency Agency, Energy Regulatory Office (ERO)
Environmental Category	B-Partial Assessment
Date PID Prepared/Updated	09-Apr-2014
Date PID Approved/Disclosed	21-Apr-2014
Estimated Date of Appraisal Completion	15-Apr-2014
Estimated Date of Board Approval	18-Jun-2014
Decision	The decision to proceed with project appraisal was obtained.

I. Project Context

Country Context

A potential candidate for European Union (EU) membership, the Republic of Kosovo is the youngest country in Europe and a lower-middle-income country with a solid economic growth performance since the end of the war in 1999. On February 17, 2008, Kosovo unilaterally declared its independence and, by January 2014, was recognized by 105 United Nation member states and 23 out of 28 EU members. Kosovo is a landlocked country in South East Europe with about 1.8 million inhabitants, and a large migrant population mainly based in Western European countries. It is one of only four countries in Europe that recorded positive growth rates in every year during the crisis period 2008–12, averaging 4.3 percent. Medium-term growth beyond 2013 is expected to remain around 4 percent. The resilience of Kosovo’s economy reflects: (i) limited international integration into the global economy; (ii) the success of its diaspora in the labor markets of, especially, the German-speaking countries of Central Europe, resulting in a steady reflux of remittances; (iii) a generally pro-growth composition of the budget, allowing for about 40 percent of public expenditures to be spent on public investments; and (iv) a steady influx of donor support.

Efforts aimed at strengthening domestic productivity—particularly critical in a euroized country—will need to remain the pivotal policy anchor, as Kosovo continues to struggle with high rates of unemployment and poverty. Joblessness in particular—estimated at about 30.9 percent in 2012—remains a central economic-policy challenge. With the difficult labor market conditions affecting youth and women disproportionately, these conditions risk undermining the country’s social fabric. Largely reflecting historical legacies, Kosovo remains one of the poorest countries in Europe, with a per-capita gross domestic product (GDP) of about €2,858 in 2013 and 29.7 percent of the population living below the poverty line—and 10.2 percent in extreme poverty, according to 2011 estimates.

The energy sector is a potential key source for future economic growth. Utilization of lignite resources by attracting strategic foreign investment could turn the energy sector into an engine of growth rather than a drain on public resources and major constraint to doing business. According to the Doing Business Report 2014, unreliable electricity supply is among the top constraints to businesses in Kosovo, together with dealing with construction permits, enforcing contracts, and trading across borders. Frequent power cuts are a major obstacle to day-to-day operations and a constraint both to investment in new equipment and business expansion, in turn affecting job and employment creation and investments.

Sectoral and institutional Context

Kosovo’s electricity system cannot meet current demand. Most of Kosovo’s domestic electricity generation comes from two, unreliable lignite-fired power plants (50-year-old Kosovo A, 30-year-old Kosovo B) with net operating capacity of about 900-950 MW. Both plants are poorly maintained and operate well below their installed capacity. After the planned decommissioning of Kosovo A at the end of 2017, there will be a considerable supply shortfall, requiring new generation capacity to address this shortage of supply. The 2013 electricity annual demand in Kosovo was 5,520 gigawatt-hours (GWh) by the power distribution utility (KEDS) and the balance between supply and demand is being met by expensive electricity imports (annually around 10 percent of demand, or 625 GWh, at a cost of about €45 million in 2012).

Heating of buildings is not financially or environmentally sustainable. The main energy sources for both space and water heating in buildings in Kosovo are biomass (mainly firewood) and electricity (from lignite), together accounting for over 80 percent of heating consumption. The high consumption of unmanaged and unregulated firewood can lead to forest degradation, giving rise to adverse environmental, economic and health impacts. Heating with electricity is highly inefficient, and exacerbates power supply interruptions while creating the need for electricity imports, especially during the heating (winter) season. Kosovo has two isolated operating district heating (DH) systems (Pristina and Gjakova), which are facing serious problems as the heat demand exceeds supply, collection rates are low, fuel costs are high, and thermal losses exceed 18 percent. The total installed capacity of 183.5 MW only produces 130 GWh/p.a. (thermal) or about 3 percent of Kosovo’s heating demand.

Energy efficiency and renewable energy can help mitigate projected shortfalls. The World Bank Power Supply Options Study (December 2011) forecasts that electricity demand will increase by 4.6 percent a year to about 8,800 GWh by 2020. The Study shows that the rising demand can be met by adding about 600 MW of new (replacement) thermal generation capacity, with an additional 402 MW of renewable energy (RE) generation by 2025 and parallel progress in loss reduction

(halving technical losses to 8 percent by 2025 and non-technical losses to 5 percent) and end-use energy efficiency (EE). This is consistent with the Government's National Energy Efficiency and Renewable Energy Action Plans (NEEAP, NREAP), which call for a cumulative energy savings of 9 percent by 2018 (based on 2010 levels) and 25 percent RE target (of gross final energy consumption) by 2020, respectively. Such targets are in line with the EU energy acquis, as committed under the Energy Community Treaty, in areas of climate change and environmental protection, which will require strengthening the existing regulatory frameworks and institutional capacity in support of EE and RE investments.

Kosovo has high EE potential. Energy efficiency can help address issues related to energy security (current deficits and reduced imports), while reducing public expenditures on energy and environmental impacts of energy use. A 2013 World Bank Institute (WBI) preliminary market assessment showed the building sector (e.g. public, commercial, and residential) accounts for 47.5 percent of final energy consumption and has been rising steadily, at an average annual rate of 3.6 percent, over period 2003-2011. The energy savings potential across the building sector was estimated at more than 44 percent. Of particular note were the high savings potential for public buildings. For municipal buildings, health buildings could save 47 percent, schools 38 percent and other municipal buildings 46 percent, even with modest improvements in current comfort levels to meet national norms. For central government buildings, the energy savings are estimated to be about 49 percent. Such savings offer substantial budgetary savings—estimates indicate that GOK spends some €1 million per year for energy in its buildings and could save as much as €18.85 million annually through cost-effective EE measures. The Government has recognized this potential and, thus, the 1st NEEAP included EE measures in the buildings sector (residential, commercial and public buildings) totaling 70 percent (21.7 ktoe) of the 3% target (2010-2012). The 2nd NEEAP, adopted in June 2013, reported that the initial 3% target was achieved (3.1% energy savings reported), all of which was in the buildings sector. In addition, the report targeted an additional 6.4% (65.9 ktoe) of energy savings from the buildings sector by 2018.

There is also moderate RE potential. The Bank's Power Supply Options Study estimated the percentage of installed RE and hydro capacity to increase from the current 2 percent (primarily hydro) to 32 percent by 2025 (60 MW small hydro, 257 MW wind, 18 MG biomass and 67 MG biogas). This is slightly higher than Kosovo's NREAP, adopted in November 2013, which includes a voluntary target of just over 29 percent, with sub-targets in three sectors: electricity generation (26 percent), transport (10 percent) and thermal energy for heating and cooling (46 percent). With regard to the electricity sector, the NREAP projects an increase in RE generation from 240 MW of small hydro, 305 MW of large hydro (HPP Zhur), 150 MW from wind, 14 MW from biomass and 10 MW from solar photovoltaic (PV). The target for heating and cooling would be met by 95.2 percent solid biomass, 4.3 percent solar water heating and 0.4 percent from geothermal heat pumps.

Kosovo's regulatory regime needs to support RE targets. Kosovo's Energy Regulatory Office (ERO) has put in place feed-in-tariffs (FiTs) for all RE technologies except for geothermal and solar PV systems. With assistance from the IFC, ERO is now in the process of reviewing a proposed design for FiTs applying to solar PV and associated draft contracts (power purchase and grid connection agreements). These enhancements to the regulatory framework have resulted in increased private sector interest in Kosovo's RE sector. To date, ERO has received 24 license applications for hydropower and wind projects totaling just under 360 MW of generation capacity; only five have yet received final authorization and none have yet reached financial closure or become operational. The regulatory regime also includes Certificates of Origin (CoO), but there is

no clarity as to how these certificates will be issued or when and whether they will be applied as premiums in addition to FiT or only as a pre-condition or requirement for RE energy purchase. The policy interaction between FiTs and CoO is also unclear.

Despite the potential, development barriers facing the EE and RE sectors in Kosovo today include economic, institutional, legal and regulatory and financial impediments. Fundamental to the sector is the rationalization of energy prices, which when low, make RE options uncompetitive and EE improvements unattractive to end users. The legal and regulatory framework, while improving, still lack some proper secondary legislations, rulebooks, financing mechanisms and other critical elements for the country to realize its stated goals and targets. Lack of credible and complete information, with respect to RE resource availability, energy use patterns, etc. also hampers greater private sector participation in these sectors. Further, there remains an insufficient enabling environment to support the EE and RE markets—lack of awareness, low technical capacity, no standardized contracts and protocols, underdeveloped financing modalities, etc. which serve to increase individual transaction costs, perceived risks, etc. thus further constraining accelerated sustainable energy investments. The proposed project will help address several of these critical barriers.

II. Proposed Development Objectives

The project development objectives are to: (i) reduce energy consumption and fossil fuel use in public buildings through energy efficiency and renewable energy investments; and (ii) enhance the policy and regulatory environment for renewable energy and energy efficiency.

To achieve these PDOs, the proposed project will provide:

- (i) investment finance for energy efficiency and renewable energy projects in eligible central government-owned buildings;
- (ii) demonstrations on the commercial viability and program models for energy efficiency and renewable energy investments in municipal buildings;
- (iii) support to develop a robust policy and regulatory framework which will help attract investments in and scale-up renewable energy and energy efficiency; and
- (iv) support for project implementation.

III. Project Description

Component Name

Energy efficiency investments in public buildings

Comments (optional)

Component Name

Policy and regulatory support for RE/EE

Comments (optional)

Component Name

Project implementation support

Comments (optional)

IV. Financing (in USD Million)

Total Project Cost:	34.00	Total Bank Financing:	32.50
Financing Gap:	0.00		
For Loans/Credits/Others			Amount
BORROWER/RECIPIENT			1.50
International Development Association (IDA)			32.50
Total			34.00

V. Implementation

The Kosovo Energy Efficiency Agency (KEEA) under the Ministry of Economic Development (MED), will act as the lead implementing agency for the project and maintain fiduciary responsibilities for all components. For this purpose, KEEA's capacity will be strengthened with consultant support for procurement and financial management and technical supervision and oversight. To ensure proper coordination with the various line ministries and subproject beneficiaries under Components 1 and 2, MED would establish a Coordination Group (CG), with invitations to relevant ministries (e.g., Finance, Education, Health, Public Administration, Local Government, Environment and Spatial Planning, Justice, Culture) to participate. The CG would be chaired by KEEA and would discuss issue related to subproject pipelines, inter-ministerial coordination, budgeting and procurement, resolving of implementation issues, etc. For technical issues related to Component 3, KEEA will liaise closely with the concerned agencies (e.g., ERO, MESP, municipal association) on technical oversight of policy and regulatory advice, option papers, assessments and training to ensure proper coordination.

VI. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01	x	
Natural Habitats OP/BP 4.04		x
Forests OP/BP 4.36		x
Pest Management OP 4.09		x
Physical Cultural Resources OP/BP 4.11	x	
Indigenous Peoples OP/BP 4.10		x
Involuntary Resettlement OP/BP 4.12		x
Safety of Dams OP/BP 4.37		x
Projects on International Waterways OP/BP 7.50		x
Projects in Disputed Areas OP/BP 7.60		x

Comments (optional)

VII. Contact point**World Bank**

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