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Risks of project financing of infrastructure projects in Serbia

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In the last fifteen years, governments worldwide adopted project financing as a driving power for conducting and improving infrastructure financing. Project financing is generally used in new, autonomous, complex infrastructure projects accompanied by a huge level of risk and high asymmetry among available information. The primary advantage of the project financing concept lies in the manner in which the capital is raised. This is especially important for the countries that have so far failed to develop their own financial markets, Serbia among them, and their only solution is to import the capital for financing infrastructure projects. The aim of the paper is to point out those risks accompanying the project financing of infrastructure projects in Serbia that can be affected, for the purpose of improving infrastructure and create an environment for a more efficient implementation of this modality of infrastructure projects financing.

Key words: Risk, project financing, infrastructure projects, Serbia.

INTRODUCTION

Project financing is based on creating a special purposes entity, one "which acts as the nodal agency for bringing together private investors and concerned Government agencies for the project"(Gupta and Sravat, 1998). In the course of an initial review and structuring, the leading financial institutions that secured loans become the insiders of the project through their cooperation with the project sponsors. They simultaneously take responsibility for external financing through a total syndicated loan that is created by attracting other financial institutions – participants in leveraging a loan (Gatti, 2008). With a higher financial leverage to the project, the operational risk has to be reduced to an acceptable level. This is one of the major advantages of project financing, as it allows for the allocation of specific project risk to those participants that can cope with it in the best manner (Brealey et al., 1996; Milosavljevic and Benkovic, 2010).

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The assets earmarked for project financing are the crucial source of infrastructure project financing as well as an important sustainer of economic development. In comparison with the corporate (direct) financing, the new regulatory framework for the long-term crediting risk, established by the Basel II, assesses risk coefficient in a different way, so that internationally active banks that invest into the projects in the developing countries (Sorge and Gadanecz, 2008) and transition countries are not discouraged. The implementation of weighted coefficients proposed by the Committee specialized in risks of lending financial assets helps get a better insight into the structure of syndicated loans for project financing and draw a conclusion as to the reasons the foreign investors still hesitate to invest in Serbia.

The main goal of this paper is to point out economic, financial and political limits of infrastructure project financing in Serbia. This is particularly important considering the fact that the lack of capital led to under-investments in infrastructure, which was neglected and completely devastated. EBRD analysis suggests that infrastructure development is of strategic importance for the development of national economies (EBRD, 2010). Constructing

new and modern facilities certainly leads to improvement of life quality, and at the same time enables the process of joining the EU. Due to the experiences of neighboring countries which have made the transition and joined the European Union, project financing is considered the most appropriate financing model for infrastructure projects.

Project financing in Serbia is still in its fundamental phase. Initiated projects based on this concept are not yet fully implemented due to lack of understanding of the risks which accompany this mode of financing. The focus of this paper is a profound risk analysis of project financing in Serbia.

Risks of infrastructure project financing

A successful analysis of project financing of infrastructure projects is based on the analysis of all the risks the project has to cope with during its economic life cycle. Risk is one of the basic factors in project financing (Zou et al., 2007) since it is responsible for unexpected changes which endanger the capacity of project managers to achieve previously defined goals, timing and costs of the projects (Kutsch and Hall, 2010). Similarly, the cash flow of infrastructure projects can come under the impact of certain types of risk; hence, if those risks are not adequately anticipated and if an adequate protection from risk is not prepared, the projects are likely to suffer losses. Consequently, the financial plan of the project should be designed in such a way so as to be able to select those options among the available ones that minimize risk, adjusting the financial costs to the prevailing conditions of offer and demand on the global capital market along the way (Farrell, 2003). In this sense, risk management is defined as “an activity that deals with planning actions that will be implemented in order to reduce the exposure to risk“(Ben-David and Raz, 2001). It is for this reason that the major period of time planned for project designing is devoted to the management of project risks that may occur during the project’s life cycle. Besides, project risk management includes”planning, identification, analysis, responses and monitoring and control of a project” (Project Management Institute, 2004). Risk analysis is undertaken before we enter the process of infrastructure project financing.

Risk identification in project financing and assessment refers to assessment of various ownership rights resulting from complex legal and financial structures of project participants, such as sponsors, construction creditors, standing creditors, contractors, constructors, technology owners, suppliers and exporters (Vinter and Price, 2006). Each participant is assigned a different task in the project execution and, consequently, his engagement assumes a different level of risk. Each participant is free to assess the characteristics and prospects of the project, and hence the risk, subjectively (Woody and Pourian, 1992). Project financing allows for a significantly more efficient allocation of risk and returns in comparison to direct (corporate) financing (Benkovic and Milosavljevic, 2009). Arrangements that include project financing should be created in such a manner that the risks are taken by the partner that can manage them at lowest costs (Milosavljevic and Benkovic, 2010). Thus construction companies encounter the risk related to project execution, suppliers of raw materials are faced exclusively with the risk related to supplies, and customers face the price-related risk, etc. (Fabozzi and Peterson, 2003).

The basic instrument of risk allocation in project financing are project contracts (An and Cheung, 2010) which define the rights and liabilities of each party. The negotiating power of the parties also plays an important part in risk allocation. Leaving too large an amount of risk to the project company which, due to being highly indebted, is not in a position to cope with such a high risk level is a typical error in risk allocation. Similarly, transferring total risk from the project company to other participants in the project is not feasible, since the participants, if they accept higher level of risk, simultaneously expect higher rate of returns on capital, which hardly fits into the financial construction of the project. A systematic process of project financing risk management also means its analysis and classification (Tinsley, 2000; Grimsey and Lewis, 2002; Yescombe, 2002). According to Tinsley (2000), risks are classified as: operative (technology, cost-based and management-based risks), participant risk, project completion risk, material and fuel supply risk, market, infrastructure, environmental, political risk, force majeure, currency, engineering, trade unions, interest and legal risk. Grimsey and Lewis (2002) stress nine risks which all infrastructure projects cope with: technical risk, construction risk, operative risk, income risk, financial risk, force majeure, political risk, environmental risk, and project failure risk which may occur as a result of previous risks.

Yescombe (2002) suggests probably the most considerable risk classification: commercial risks (consideration of appropriateness of the project, project completion risk, environmental risk, operational risk, income risk, supply of raw materials and energy, force majeure risk and project contracts compliance risk), financial risks (inflation risk, interest rate risk and exchange rate risk) and political risks (investment risk, risks of changes in legal system and quasi-political risks). This classification is used in the paper as a basis for project financing risk identification in Serbia.

Infrastructure and infrastructure projects in Serbia

As one of the “key inputs of economy“(Threadgold, 1996), infrastructure allows for economic development and poverty reduction, which is one of the major motives for

Table 1. Infrastructure indicators for Serbia in the 2000 to 2009 period.

Year	Overall Infrastructure	Railways	Electric power	Telecommunications	Roads	Water and waste water
2000	2	2	2	2	2	2
2001	2	2	2	2	2	2
2002	2	2.3	2	2	2.3	2
2003	2	2.3	2.3	2	2.3	2
2004	2	2.3	2.3	2	2.3	2
2005	2	2.3	2.3	2	2.3	2
2006	2	2.3	2.3	2.3	2.7	1.7
2007	2	2.3	2.3	2.3	2.7	1.7
2008	2.3	2.3	2.3	2.7	2.7	1.7
2009	2.3	2.3	2.3	2.7	2.7	1.7

Source: (EBRD, 2000; EBRD, 2008).

attracting investments in infrastructure (Ng and Loosemore, 2007). The East-European countries undertook substantial reforms in the field of infrastructure investments. Reforms and infrastructure restructuring include three aspects – the tariff reform, the commercialization, the legal and institutional development in five infrastructure segments (telecommunications, electrical energy, railways, roads and water supply). Privatization has led to increased presence of privately owned capital in the public sector. With certain legal and regulatory reforms and restructuring, the private capital can largely improve the process of investing into infrastructure.

Improvement and renewal of infrastructure in the entire region requires massive investments. It is certain that regional cooperation, creating a single market and a favorable investment climate are the preconditions for building a modern infrastructure. It is necessary that international financial institutions such as the IMF, the EBRD, the World Bank, and others should give aid and support, in order for all these activities to be conducted and certain advances be accomplished in the period of global crisis and its post period.

In the beginning of transition Serbia had poor, old and inadequate infrastructure for market economy, as there were no significant investments in this field. In almost each infrastructure sector there was one large monopolistic state-owned company that did not follow the trends on the national and international markets. Doing business with relatively obsolete technology and constrained access to citizens and firms, these companies operated with losses. The railway infrastructure was adjusted to machine tool industry and raw material transportation. The roads were bad, the water supply and sewerage systems were of poor quality and environmentally hostile (EBRD, 2004). Besides, with the prices of infrastructural services at the time, it was impossible to earn an income that would allow further investments in the renewal and construction of new infrastructural facilities. The prices of electric power and water supply, for example, were not calculated on the basis of market movements, or on the basis of cost coverage, but were created as a social category.

The reforms in the field of infrastructure commenced in the 1990s, however, the early 2000s witnessed a slow economic growth on the international markets of telecommunications and electric power, which was in turn reflected upon the Southeastern-European countries, consequently upon Serbia, too. Hence it is important to point out that the countries of the Southeast-European region strive to establish a single market for these industries, especially for the electric power supply, which is a primary condition of the European Union. Small, individual markets that serve a total of about 29 million customers will have to get incorporated into the market of 495 million inhabitants (EBRD, 2008). Creating a single market would develop and increase these industries.

According to the infrastructure development strategy of Serbia, major investments are oriented towards the transportation sector, that is, towards building and development of modern lines of communication, highways and railways on the Corridor 10. Furthermore, there are projects oriented towards development of trough traffic, but also towards construction of other communication lines in order to disburden traffic between larger cities, as well as the construction of the Corridor 7 (the Danube corridor), one of the most important European waterways. Finally comes the building of electric power sector through commercialization and increased participation of private capital in its development (EBRD, 2007). In accordance with this strategy and its implementation, indicators of the infrastructure sector can be identified. Table 1 shows the EBRD infrastructure indicators for Serbia in the 2000 to 2009 period.

Serbia achieved the best outcomes in telecommunication and road sectors. In 2009, the best results and the highest values were those of telecommunications (2.7) and

transportation (2.7), followed by electric power industry (2.3) and railways (2.3), whereas the poorest results were characteristic of water supply and sewerage systems (1.7). The values of these indicators are still low; however, some steps have been made towards adjusting the regulations of telecommunication sector to those of the European Union; electric power industry has become autonomous, railway infrastructure has been separated from other segments of transportation infrastructure, and the Serbian Roads Directorate has also been granted autonomy (EBRD, 2008).

According to the World Economic Forum (2010), Serbia has improved its rank in the infrastructure sector, from the 107th position in 2009, to the 93rd position, out of 139 countries. Its lowest rank is in the water infrastructure domain. Electric power generation and telecommunication sectors remained at almost the same positions. The quality of the electric power supply sector has enhanced in 2010 and moved one position up – Position 74, whereas the quality of telecommunications is slightly lower and hence fell by two positions, to Position 41.

The reforms carried out particularly in sectors such as tele-communications are conditioned by the relative movements on the market, rather than government inter-ventions. In telecommunications sector, demand for mobile phones was greater than that for land phones. Change in technology and its availability resulted in increased demand and attracted new operators into the sector. Initially, tariffs and prices of services were regulated; however, with the emergence of new operators competition is fierce, so the prices were determined on the basis of market laws. These changes led to the introduction of private ownership in this type of companies. Nowadays, the number of mobile phone users is far larger than land phone users; consequently the services of mobile telephony are getting better and more attractive from the point of view of both quality and price (Statistical Office of the Republic of Serbia, 2009).

In August 2006 Telenor Company (Norway) won the auction for Mobi 63; thereby Serbia obtained the second mobile network operator; the offer being €1.51 billion for the company and an operating license for a ten-year period. The Mobilkom (Austria) is the third mobile network operator that came to the Serbian market in December 2006, being granted the operating license as the only applicant on a bid and submitting a deposit of €30 million. Serbian authorities are still in a dilemma whether and how to privatize Telecom Serbia as the chief land telecommunication network operator and introduce other mobile network licenses into the market.

Short of capital required to conduct infrastructural reforms, Serbia accepted financial aid and applied for loans from international institutions. One of the major investors in Serbia is the EBRD. This bank commenced financing projects in 2000. Since then, 130 projects have been signed, whose net value amounts to €2,029.3 million and their total value is € 4,780.0 million, with gross expenditure of €1,326.9 million. The current portfolio is worth € 1,660.1 million, 24% of which is the portfolio share in the private sector. In 2009, 14 projects were signed, worth € 423 million (EBRD, 2010). The basic forms of direct financing granted by the EBRD are loans, equity and guarantees. The projects financed by the EBRD in the field of infrastructure in Serbia are presented in Table 2.

The engagement of the World Bank on the Serbian market is also important. Current World Bank portfolio, IDA, IBRD and GEF, consists of 12 projects which are under way and whose worth amounts to $845.8 million. In July 2009 the World Bank granted a $388 million loan to Serbia to build the main highway – Corridor 10. Serbia also signed several projects with the IFI (International Financial Institutions) for the reconstruction of Serbian Railways (EBRD, 2009).

Issues concerned with power supply and electric power industry refer to the restructuring and privatization of companies in this sector, and finally to creating a single energy market. The establishment of single energy market of Southeastern Europe makes way for the integration into the European Union energy market. These conditions fulfilled, the economies of this region could need a shorter period of time to become part of the European Union. Different countries have, however, achieved different results; hence this market is not developed well enough yet. Certain investment projects are provided for by the operations plan for the defined strategy of the reform and development of the Electric Power industry of Serbia until 2015.

Execution of the Electric Power Industry of Serbia plan requires € 9.2 billion. This amount could be partly supplied from the Electric Power Industry of Serbia's own incomes, partly by strategic partners, and partly from loans and credits. The plan is to build two new thermal power plants – Kolubara B, two blocks of 350 megawatt each and Nikola Tesla B, the power of which will be 700 megawatts. This requires investments into coal production, and then into modernization of CHP Novi Sad. The plan also includes revitalization of hydroelectric power plant Djerdap 1, worth approximately $ 167 million. Also planned is cooperation with the Republic of Srpska and construction of four hydroelectric power plants on the Drina as a joint venture with the Republic of Srpska. Serbia also plans to build a plant on the Tara, jointly with Montenegro (Jednak and Kragulj, 2009).

Risk impact upon project financing in Serbia

Infrastructure projects realization assumes major financial investments followed by high level of risk – commercial, financial and political.

Serbia commenced its transition process in 2000 and it is still in progress. Economic problems are still Serbian reality. The reforms include an economic and financial

Table 2. Infrastructure projects in Serbia in 2005-2009 (EBRD, 2010).

Date	ID of the project	Project title	Sector	Ownership State / Private	Project status	Project value (€ million)	EBRD financing/loan and other investors (€ million)
16/03/2010	41125	Railway Corridor 10	Transport	State	Pending approval	296.4	250.0
02/03/2010	10379	(EPI) EPS measuring	Electric power industry	State	Pending signing	80.0	80.0
16/09/2009	40760	Srbija Gas	Natural resources	State	Signed	150.0	150.0
08/05/2009	40280	K10	Transport	State	Signed	786.0	EBRD 150.0; WB 156.0; EIB 300.0;
04/04/2008	38711	Railway EMU	Transport	State	Signed	221.0	100.0
15/11/2006	37033	Duboko - solid waste	Infrastructure	State	Signed	11.9	5.0
26/09/2006	37198	Pančevo waste water system	Infrastructure	State	Signed	16.1	9.3
11/06/2006	36651	Belgrade highway and interchanges	Transport	State	Signed	290.4	EBRD 80.0; EIB 80.0; Belgrade city 7.5; Putevi Srbije 112.0;
08/08/2005	35414	Railways: railway lines	Transport	State	Signed	162.0	EBRD 60.0; EIB 80.0;
22/09/2005	34913	The Sava river, crossing	Infrastructure	State	Signed	343.2	EBRD 69.6 + 60.0 (for bridge project 41055); EIB 70.0;

recovery of Serbian economy, due to political normalization of international relations and the country's economic openness. Public debt is reduced, banking sector is consolidated, and skilled labor force has become more competitive. However, high level of current account balance deficit is still present, as are the increase in foreign debt and public sector burden. Present business environment is the consequence of commercial risks which influence investments in Serbia. Bad transportation lines and electric power supply are some of them. Serbia makes efforts to improve its road network and it has obtained certain advances in the state railways restructuring.

Project completion risk should be mentioned. It is related to construction phase and includes monetary and technical aspects of project. The monetary part considers two options: a) is the risk higher than the one anticipated by inflation rate, or b) the risk is lower than expected price related to product (services) compared to anticipated rate of return. High inflation rate is a serious barrier to an increase in economic activities. Declined trust in business activities, prospects of an increase in investments, as well as in the increase in the number of newly-established firms are some of the consequences. Other risks stem from the lack of capital.

Environmental risk is a consequence of lack of laws and regulations on environmental protection, which should be harmonized with the regulations of international organizations such as the World Bank and EBRD.

In addition to these, unemployment is one of the biggest problems in Serbia. This problem becomes bigger and more complex due to the impact of the global crisis. Large scale unemployment is the result of further restructuring of state-owned companies, dismissal of employees in the state administration, poor development of small and medium-sized enterprise sector, low level of production scope and nearly completed privatization of companies. The unemployment rate is high due to the economic crisis and in 2009 it amounted to 20%, yet estimates are that it will fall in the near future, due to stabilization of market conditions. Serbian labor market failures have impact at the appearance of risks such as operation costs risk, revenue risk and force majeure risks.

The major financial risk which the Serbian economy is faced with is decrease of capital inflow and fall in foreign loans, which can be explained by global financial crisis and significantly low rating due to the ruling of the International Court of Justice and the anti corruption laws.

The exchange rate risk in Serbian banking sector is relatively high, as about three fourths of outstanding loans are indexed in Euros. The share of irrecoverable loans in Serbian banks amounted to only 10% of the total of credit lines issued in 2008 and 2009. The share of the insurance sector and stock exchange capitalization is

Table 3. Risk rating for Serbia (Economist Intelligence Unit, 2009).

Risk category	Currency risk	Currency score	Previous rating	Previous score
Certainty risk	C	57	C	57
Political stability risk	C	60	C	60
Government efficiency risk	D	68	D	68
Legal and regulatory risk	C	60	C	60
Macroeconomic risk	D	80	80	D
Foreign trade and payment risk	C	50	C	50
Tax policy risk	B	25	B	25
Labor force risk	C	46	C	46
Financial risk	E	83	E	83
Infrastructure risk	C	44	C	44
General assessment of risk	C	57	C	57

Risk rating for Serbia; (E=highest risk level; 100=highest risk level).

relatively low and poorly developed, although these financial institutions operate on the interbank monetary market. There is no national market of corporate bonds yet, nor a secondary market of treasury bills. According to Fitch and Standard & Poor's credit rating of Serbia is BB-. In December 2009, the S&P ranked the outlook of Serbia as stable, not negative, while Moody's has not ranked Serbia at all yet (Gatti, 2008; Gatti et al., 2008). According to the official Business Eastern Europe report of 19th October 2009, the overall climate for investing in Serbia was somewhat more favorable than in 2008, that is, it has not changed significantly since as early as 2000.

Until the second half of 2007, Serbia had relatively high economic growth rate. The growth of domestic demand was conditioned by expansion of national loans to the private sector as well as by net exports, which helped achieve this high economic growth rate. Until the end of 2008, loan market operated normally and financial sector developed fast. The progressive loan growth, however, was characterized by unfavorable interest rates, while bond transactions and loans to Serbia subsided with the global crisis becoming deeper and more severe. The reduction of loans led to the reduction in investments and in domestic demand, while an overvalued exchange rate of the dinar largely contributed to the fall in exports. All these negative trends resulted in slowdown of economic activities, first in 2008, and then in 2009, too. (Jednak et al, 2009).

In the past, inflation was a serious problem in Serbia. The inflation rate was increased by liberalization of prices and trade. This was due to administrative prices, exchange rate and wages/salaries in the private sector. High investments and a relatively slow productivity growth are also mirrored in high inflation rate and the current account deficit. The net inflow of foreign capital and the domestic savings can increase investments and growth, trigger monetary expansion and increased competition and they may trigger inflation. (EBRD, 2004, 2008).

Political risk is relatively lower because of the forming of a pro-European government; however, relatively high risk remains due to the Kosovo proclamation of independence in February 2004, due to the uncertainty and delays in the negotiations on the Serbian accession to the EU, as well as due to increasing dissatisfaction of citizens with low standard of living which is a result of the omnipresent economic crisis.

Alongside a relatively fast rise of nominal pays and bank loans in recent years, there has been an increase of deficit in the current account balance. Such a large deficit is an indicator of a lack of international competitiveness and of the need for new investments, especially foreign direct investments, as well as the need for solving structural problems. All the above mentioned factors create unfavorable business environment for the investors, and this in turn has an impact upon the risks accompanying project financing of infrastructure projects in Serbia.

The efficiency of the Government is constrained by the lack of capacities in the public administration, while the level of legal and regulatory risk fell. At the same time, financial risk indicates that domestic capital is not well placed, whereas the money market is to a large extent constrained with the elements of negative fall, due to the global credit crisis. Tax risk is relatively low, due to more favorable tax rates in comparison with the countries in the region. Risk rating for Serbia is shown in Table 3.

In the past, there were several attempts in Serbia to build large infrastructure and industrial projects implementing project financing methodology and overcome the impacts of risks. Such is the example of forming the RAST consortium in 1999 from Borovica Transport, the PIM and the Beogradska Banka. The consortium was granted concession for building the left lane of Belgrade – Novi Sad highway. The works have never commenced, and the concession was cancelled three years after.

Initially, Horgos – Pozega highway was to be the first large infrastructure project built by implementing project financing concept in Serbia. On 30th March, 2007, the Government of Serbia signed the agreement on granting the concession to a Spanish-Austrian consortium that included the Spanish Fomento de Construcciones y Contratas and the Austrian Alpine-Mayreder, for the period of 25 years, to build and maintain 350 kilometers of the highway. The investment value amounted to €800 million. The agreement stipulated the construction of a 106 km long stretch of highway from Novi Sad to Horgos, the maintenance of 68 km of the highway between Novi Sad and Belgrade and the construction of 148 km of highway between Belgrade and Pozega. The deadline was set to be the year 2012; however, the project was contested from the beginning, there was no political consensus, and there were also problems with raising capital. The commencement of works was postponed several times, until, after parliamentary elections in May 2008, the new Government decided that it was not the time for giving concessions for this project and that it was not the priority interest of the state. Accusations of corruption ensued, there was public pressure that the agreement should be cancelled, and finally the Austrian-Spanish consortium cancelled the bid in December 2008 as they failed to raise funds for the project. The government of Serbia won the dispute before the Arbitration tribunal and the consortium is now obliged to pay the guarantee the amount of €10 million.

The contract between Russian Gazprom and Serbian company Srbijagas on forming a joint venture, the South Stream, a project company that was to execute the project of building a stretch of 450 km long pipeline through Serbia, was signed on 17th November, 2009. The value of the project was estimated at €700 million. The project is to be executed implementing project financing model and crediting the Juzni tok Srbija (South Stream Serbia) joint venture. The contract states that the Russian company has a 51% share in the joint venture created for the construction of the pipeline. In addition to this document, and within the Serbian-Russian energy arrangement, 51% of shares of the Oil Industry of Serbia were sold for €400 million, and a contract was signed on the construction of an underground storage facility at Banatski dvor. The feasibility study is planned to be completed not later than June 2010, and the works are to commence not later than 2011, while the deadline is set to be 31st December, 2015.

DISCUSSION AND RECOMMENDATIONS

The conclusion that arises from the experiences of EU member countries and countries of the region in the implementation of infrastructure projects using the concept of project financing, is that they are, in the financial sense, certainly the most extensive and comprehensive financial projects. It particularly refers to transportation, energy, environmental and water supply projects. Due to limitations and risks immanent to the Serbian market, in the closing we draw a number of conclusions.

Firstly, Serbia is still dependent on foreign financial aid, donations and loans. Those factors led to both current account and fiscal deficits. Foreign direct investments (FDI) have an important role in reducing deficits as well as in the development of Serbian economy. However, the FDI inflows are not as high as they were, but there are signs they would be enhanced. Financing of infrastructure by applying the concept of project financing in relation to loans means that the funding sources are book-kept as off-balance sheet debt of public sector. Therefore, it significantly relieves the public sector in terms of reducing public debt, which is certainly an important factor for countries in transition such as Serbia. Hence, it is the advantage of this mode of financing infrastructure projects in Serbia since it reduces the financial risk.

Secondly, projects funded by the concept of project financing are implemented in countries which have previously developed adequate legal frame and implemented it strictly. There is a clear tendency that this interesting field should be systemized by special legal regulations in Serbia since project finance is a particularly appropriate concept for financing infrastructure. Clear and uncomplicated procedures for contracting projects are a precondition for the implementation of this concept. Otherwise, the very concept of financing just may become unattractive. Serbia is known for its administrative barriers and inefficiencies, which is a risk that is relatively easy to remove. The experiences of other countries in transition have shown that proper legislation and establishment of supporting institutions for project financing is important for significant progress in cooperation between public and private sectors which are financed by domestic and/or foreign capital. Accordingly, this commercial risk which substantially exists in the financing of infrastructure projects in Serbia should be reduced.

Third, together with comprehensively developed regulatory and institutional framework, implementation of project by project financing is impossible if the public sector does not pre-define clear priorities in the sector of infrastructure. This is certainly the duty of central and local governments, which must have a clear concept in which infrastructure sectors project financing may occur as convenient method of financing. A coherent strategic document is required, which will set clear guidelines to potential investors and international financial institutions on what the state sees as a priority in the sector. Unfortunately, by now Serbia does not have a complete document of that type. Considering the fact that the creation of such a strategic document is one of the conditions on the way for further European integration, the Government will certainly, in due course, have to create and adopt a so-called Strategic Coherent Framework (SCF),

which would also include priorities from infrastructure sector which would focus on all the available financial resources and financing mechanisms, including currently available EU funds, funds received from loans and other financing sources. Although it is currently the long run, financial and technical assistance received from the European structural funds can drastically change the economic situation of a country. Therefore, Serbia has to be prepared for them by strengthening the capacity of the public sector, and certainly by strengthening private sector which will find the way to place free resources for investments. This will certainly bring about the reduction of political, as well as commercial risk.

Finally, we will mention an advantage of Serbia compared to surrounding countries. Namely, although Serbia has no projects based on project financing concept, at least there is a possibility to learn from experiences of other countries which have already developed good practice in using this method of financing. Therefore, Croatia should be mentioned as an example where successful implementation of this model of financing went the farthest.

Conclusion

Project financing is a specific form of financing that proves to be a viable option in infrastructure project execution. Risk analysis is conducted prior to entering the project financing process, therefore identification and limitation of risk impact in the project financing of infrastructure projects is considered to be more efficient in comparison with other forms of project financing, which we aimed to point out in this report.

The benefits of such a model of financing are not automatically created. It needs an adequate mechanism and a business environment to minimize the impact of various risks inherent to infrastructure development. It is for this reason that an appropriate management and risk allocation are the key parts of an adequate project financing. They define rights and obligations of partners in each of the project phases, thus ensuring an appropriate quality level and the scope of services at contracted prices, as well as the returns on invested assets at an adequate rate.

This report shows that the basic sources of risk for a faster and a more efficient development of the project financing of infrastructure projects in Serbia are inherited inadequate infrastructure basis, retarded economic development due to the impact of the global economic crisis, inadequately adjusted institutional and regulatory framework, slow inflow of foreign direct investments into the infrastructure sector, as well as relatively unfavorable macroeconomic factors such as exchange rate, relatively high inflation rates and imbalanced foreign trade balance.

The key factor of successful execution of an infrastructure project is appropriate risk management and allocation to those partners in the business operations who can finance, construct and manage the infrastructure at lowest costs. As the signs of larger inflow of foreign capital, support of international financial institutions, incremental improvements in creating an adequate institutional framework and broad support in political circles are evident in Serbia today, it is to be expected that the risk will be reduced and, consequently, that the level of project financing in the infrastructure project execution will be higher.

This research analyzed the risks of project financing of infrastructure projects in Serbia. Considering the myriad of limits in data collection and advantages of implementation of this model in advancement of infrastructure, possibilities occur for further research.

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