Eurasian Development Bank
Manager of the EurAsEC Anti-Crisis Fund Resources

EVALUATION REPORT

on Application
of Kyrgyz Republic
for Investment Loan
Financed with Resources of the EurAsEC Anti-Crisis Fund for the project
“Rehabilitation of Bishkek-Osh Road Section, Phase IV”.

in the amount of US$ 60 million

November 2013

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Kyrgyz Republic  
Fiscal year: 1 January - 31 December  

National Currency Exchange Rate  
as of 01/11/2013  

<table>
<thead>
<tr>
<th>Currency</th>
<th>KGS</th>
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<td>1 RUR</td>
<td>1.5121</td>
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<tr>
<td>1 KZT</td>
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<tr>
<td>1 US$</td>
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<tr>
<td>1 EUR</td>
<td>66.4980</td>
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Acronyms and Abbreviations  

AADT – Average Annual Daily Traffic  
AASHTO – American Association of State Highway and Transportation Officials  
ACF, Fund – Anti-Crisis Fund of the Eurasian Economic Community  
ADB – Asian Development Bank  
CAREC – Central Asian Regional Economic Cooperation  
CIS – Commonwealth of Independent States  
EDB – Eurasian Development Bank  
EIRR – Economic Internal Rate of Return  
EurAsEC – Eurasian Economic Community  
FS – Feasibility Study  
GDP – Gross Domestic Product  
HDM – Highway Development and Management Model  
IDB – International Development Bank  
IFI – International Financial Institutions  
IRI – International Roughness Index  
KR – Kyrgyz Republic  
MTC – Ministry of Transport and Communications of KR  
TMC – Transport Maintenance Costs  
VAT – Value Added Tax  
WB – The World Bank

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1. BASELINE PARAMETERS OF LOAN RECOMMENDED BY RESOURCES MANAGER

<table>
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<tr>
<th>Project</th>
<th>&quot;Rehabilitation of Bishkek-Osh Road Section, Phase IV&quot;</th>
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<tr>
<td>Borrower</td>
<td>Kyrgyz Republic</td>
</tr>
<tr>
<td>Project Implementation Agency of Beneficiary</td>
<td>Ministry of Transport and Communications of Kyrgyz Republic</td>
</tr>
</tbody>
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**Amount and financial conditions**

- Requested amount of ACF loan: US$ 60 million
- Total amount of funding of Phase IV of the Program “Rehabilitation of Bishkek-Osh Road" is equal to: US$ 203.8 million
- Interest rate: 1% per annum.
- Interest Margin: n/a.
- Risk premium: n/a.
- Front-end fee: 0.5%
- Commitment fee: n/a.
- Loan maturity, including grace period: up to 20 years
- Grace period for principal repayment: 8 years.
- Date of Termination of Loan Availability: 31 December 2016.
- Grant-element level: 41.6% (consistent with ADB lending terms).
- Co-financing due from Borrower: US$ 12 million (20% of ACF loan amount).

**Type of operation**

Investment loan provided on the basis of co-financing agreement with Asian Development Bank.

**Procedure for disbursement of Fund resources**

ACF loan funds are disbursed to the Borrower as the Borrower signs contracts in the process of Project implementation in accordance with the schedule of payments provided in the contracts.

**ACF loan repayment schedule**

On 30th day of the last month of each calendar quarter beginning from 30 March 2022 and up to 30 December 2033, inclusive, in equal installments. The amount of each such quarterly payment is equal to one million two hundred fifty thousand US dollars (US$ 1,250,000).

**Sector**

Motor roads

**Authorized use of loan**

Payment of reasonable prices under contracts signed by the Beneficiary in the course of the Project implementation funded by the Investment Loan.

**Key performance indicators**

Reduced travel time, lower vehicle operation costs, increased throughput capacity of road sections after rehabilitation and improved road safety.

**Main objective**

Creation of the necessary conditions for cost-effective passenger and freight traffic between the northern and southern regions of KR with concurrent reduction of risks, drivers and transport companies are exposed to during such traffic operations.

**Project Company**

Participation of a Project Company (Final Borrower) is not envisaged. Rights and obligations of the Project Company (Final Borrower), as specified in the relevant ACF documents, are assigned to the Borrower. The provisions of ACF’s relevant regulatory documents on investment funding of ACF member states via a Project Company (Final Borrower) do not apply.
| Principal risks and mitigation techniques | The Project contains design-specific risks, construction risks, operating risks, supplier risks, social risks, environmental risks, social, as well as legal and fiduciary risks (see Risk Matrix). The Manager recommends mitigating the above risks in the course of Project implementation by applying the ADB policies on compliance review and occupational safety, on environmental safeguards, resettlement and compensations. In procurement operations the Manager recommends to rely on the procurement policies of ACF and the World Bank. Also, in order to reduce reputation, corruption and construction risks, the Manager believes the Government of KR should invite a consultant specializing in supervision of construction activities on the site whose services would be paid with the funds of the Investment Loan. |
This Evaluation Report is presented on the basis of evaluation of the application of the Kyrgyz Republic (hereinafter - the Applicant) for an ACF investment loan (hereinafter - the Loan) in the amount of US$ 60 million, which was received by the Bank 18/11/2013 in the letter # 12181 (hereinafter - the Application). The principal declared objective pursued in applying for this Loan is to provide co-financing support to Phase IV of the program “Rehabilitation of Bishkek-Osh Road Section” (on the basis of concurrent funding together with the Asian Development Bank in accordance with the Framework Co-financing Agreement signed on 3 May 2013 in Delhi and endorsed by the Fund Council on 10 June 2013 (hereinafter - the Project). On 7 December the ACF Council endorsed the Project concept and the Manager’s Evaluation Report on the Preliminary Application (the Preliminary Application was received on 20 November 2012).

Section 3 of this document contains rationale for the ACF Resources Manager's Evaluation Report on the Application (hereinafter - the Manager).

Having examined the Application, the Manager requests the ACF Council to consider the following recommendations and conclusions:

The Application is executed in full compliance with the requirements of the Fund. The depth of elaboration of the Application in terms of availability of data required for the approval of the project funding is deemed satisfactory.

The Application conforms to the mission of the Fund, its funding objectives, lending policy and conditionality, as defined by the Treaty on Establishment of the Fund, Statute of the Fund, Regulation on ACF Investment Loans and relevant decisions of the ACF Council.

The Project is consistent with the ACF mission. The implementation of the Project will contribute to economic sustainability of the Kyrgyz Republic. Preservation of the transport infrastructure in the context of extremely limited budget funds allocated for its maintenance, constitutes an indispensable prerequisite for sustainable economic growth in the country, increased standards of living of the population, more opportunities for participation of KR in integration processes, including with the ACF member states.

Kyrgyz Republic is in compliance with all the requirements defined by the Treaty on the Establishment of the Fund, Statute of the Fund and decisions of the ACF Council. The requirements to make an initial contribution in cash and in the form of a bill of exchange have been met in full, and there are no outstanding liabilities. According to the information available to the Manager, Kyrgyz Republic has no outstanding debts either to Fund member states, or to any international financial institutions. The Manager is in receipt of the relevant supporting letters from the International Monetary Fund and the World Bank. Up till now the Kyrgyz Republic has never been granted ACF loans, and the requested amount is within the qualification limit for KR. The level of debt sustainability of the Kyrgyz Republic enables us to make a positive conclusion about financial solvency of the Borrower.

In accordance with para 12 and Appendix 1 of the Regulation on the Use of ACF Funds for Providing Investment Loans the Manager recommends to define financial conditions for the Investment Loan with due account of the requirement of the IMF Program on the size of the grant-element of at least 35%, as well as the need for compliance with the funding terms and conditions tendered by the other Project participant (ADB).

Since the Project structure makes no provision for a Project Company (Final Borrower), and the implementation process will be managed directly by the Borrower which is the Ministry of Transport and Communications of KR (MTC), the Manager recommends to assign to the Borrower the rights and obligations of the Final Borrower as defined by the Regulation on ACF Investment Loans.
To ensure due quality of the Project documentation and proper use of the Loan funds the Manager will work closely with the Asian Development Bank, which has provided technical assistance to the Government of KR in preparation of the Feasibility Study on the program “Rehabilitation of Bishkek-Osh Road Section, Phase IV” for the road section to be funded by ACF.

As defined by the Agreement on the Management of Fund Resources, the Manager is required to control procurement of goods, services and work funded by ACF in compliance with its own procurement policies and regulations, and ensure compliance therewith by making relevant provisions in ACF lending agreements. In June 2013 the Fund Council approved the ACF Procurement Policy. The Policy makes provision for using procurement procedures of other IDBs in working on ACF-funded projects. To ensure competitiveness and transparency of the proposed policies, the Manager recommends application of the World Bank rules in the course of implementation of the Project with appropriate supervision by the World Bank procurement experts. For WB expert assistance the Manager will need up to US$ 250,000 to be provided from the Fund Resources.

All procurement operations funded by the Investment Loan must be carried out by the Borrower in accordance with the ACF Procurement Policy and the IBRD Procurement Guidelines, insofar as they are not at variance with the ACF Procurement Policy. One applicable procurement method in respect of construction work is International Competitive Bidding, whereas for contracts with technical consultants Quality- and Cost-Based selection should prevail. The bidding should be conducted by the Borrower in accordance with the IBRD Procurement Guidelines and based on the IBRD standard bidding documents, regardless of the number of contracts that will be signed - one or several interrelated contracts - and of the price of each of such contracts.

Monitoring and evaluation of the Project will be performed by the Manager in accordance with the EDB monitoring procedures. The above monitoring procedures will require continuous collection of data on Project implementation progress, Project risk assessment to be carried out by the Manager on an on-going basis and regular field missions of the Manager's staff to the Project sites.

The Investment Loan will be disbursed in compliance with the relevant World Bank procedures. The above procedures require disbursement of funds upon receipt by the Manager of all the necessary approvals as provided by the relevant procurement procedure and of all the supporting documents certifying the proper purpose of the proposed payment (agreements, proforma invoices and other documents). The Manager transfers funds on the basis of the Borrower’s Disbursement Requests directly to the vendors contracted in compliance with the IBRD procurement procedures.

The environmental and social policy of the Manager allows additional requirements to be imposed on ACF projects, including compliance with safeguards policies of other IFIs. In particular, as required by the Framework Co-financing Agreement between the Asian Development Bank and the Eurasian Development Bank, endorsed by the ACF Council, the Manager in project implementation will rely on the safeguards policies of the Asian Development Bank. Preliminary review of the Project showed that its implementation might generate a number of social impacts. ADB has sufficient experience and expertise in mitigating such impacts.

In order to reduce reputation, corruption and construction risks, the Manager believes the Government of KR should invite a consultant to carry out supervision over construction activities on the site, and his services should be paid with the Investment Loan funds.
3. RATIONALE OF EVALUATION REPORT

3.1. Overview of Social and Economic Status of Kyrgyz Republic

Kyrgyz Republic is a low-income country. In 2012 its nominal GDP was equal to about US$6.08 billion. In 2012 trend toward shrinking positions of KR on the global competitiveness scale (WEF) continued. Since 2006 Kyrgyzstan has slid 17 points down to position 127. Quality of business environment is the only indicator out of the commonly known development indexes, which rates KR in the midrange and not at the bottom amongst the CIS countries, though in recent years KR has been going down its rating curve according to the World Bank’s “Doing Business” Report (68th in 2013). Moreover, quality of public institutions is poor, and according to the World Bank the level of control of corruption and the current status of the rule of law place the country among the 15% of problem nations. Given all the ambiguity of ratings, their low values are indicative of the lack of progress in the last decade. The poor condition of business environment constitutes a serious constraint for the inflow of foreign investments and thus suppresses opportunities for diversification and modernization of the national economy.

In 2000-2011 the average annual growth rate of the economy was around 4%. Moreover, in 2009-2012 the rate of growth was equal to about 2%. In 2012 the GDP dropped by 0.9%. The key sectors, as of the year-end of 2012, are agriculture - 18%, manufacturing industry – 15% with a 40% share in it of the gold mining company "Kumtor", as well as trade - 16% and transport – 9%. In 2012 significant reduction of gold mining activities at Kumtor resulted in a deep decline (over 27%) in the manufacturing industry. Positive development trends observed in other sectors were not sufficient to offset the above drop, and as a result, overall decline in the GDP in 2012 was registered at the level of 0.9%. The low GDP growth rate in recent years has significantly limited the capacity of companies to fund investments. Their share in investments did not reach the pre-crisis level.

Kyrgyzstan is characterized by a chronic budget deficit averaging at around 4% of the GDP in 2000-2011, and in 2012 as a result of the drop in the GDP, the deficit grew to 6.6%. It is estimated that the deficit in 2013 will go down to 4.8% of the GDP. Prior to 2009 the national external debt was controlled at the level of 33-37% of the GDP. The need for borrowed funds, which emerged in the post-2008 crisis period, the sluggish GDP growth and weakening of the national currency exchange rate increased the external debt service burden to the level of 47.5% of the GDP at the year-end in 2011. In 2012 the situation was aggravated by a drop in the GDP, which, as a consequence, affected the taxable base, and by the year-end the external debt reached 47.9%. 85% of the deficit is funded from external sources of finance.

The current budget condition is far better than last year, despite the reduction in revenue coming from Kumtor (around 1% of the GDP). The national budget deficit in the first six months of 2013 amounted to 1% of the GDP compared to 3.3% one year ago. The Government is taking steps to consolidate its budget position, which will have a limiting impact on investment funding capacity of the budget.

Despite the macroeconomic improvement trends, the current economic status of the Kyrgyz Republic demonstrates its inability to provide financial support for infrastructure projects by mobilizing its domestic resources, and the capacity to attract FDIs for these purposes is also extremely limited.

High poverty level of the population constitutes one of the key social and economic development problems of Kyrgyzstan. According to the Ministry of Economics of KR, as of 2012 the

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The share of the population living below the poverty line was equal to 38%. Over the last five years a trend to steady growth of this indicator has been registered (in 2007 it was 31.7%, see Figure 1).

**Figure 1. Trends in Average Poverty Level in KR**

![Trends in Average Poverty Level in KR](image)

Source: National Statistical Committee of KR

In addition to the overall negative trend in the average poverty level there are serious regional imbalances in this indicator. The average poverty level in the least prosperous area (Djalal-Abad region) in 2012 was 55.7%, whereas the same indicator for the most problem-free territory (Chuy region) was equal to 16.6%.

**Figure 2. Regional Average Poverty Levels in KR, 2012**

![Regional Average Poverty Levels in KR, 2012](image)

Source: Ministry of Economics of KR

There is also a significant gap between urban and rural areas: the average share of urban dwellers living below the poverty line in 2012 was equal to 35.4%, and that of rural population - 39.6%. Over the last five years a trend to closing this gap has emerged, which, however, was actually due to a higher rate of growth of poverty among the urban population.
One of the drivers of poverty in KR is high unemployment. It is noteworthy that a substantial proportion of the active population in KR work in neighboring countries (RF and RK), and economic slowdown in these states may have a significant negative impact on employment rates in KR.

The current economic situation in the Republic of Kyrgyzstan is indicative of its inability to provide financing for infrastructure projects from its own domestic sources.

3.2. **Status of Motor Transport Sector**

Kyrgyzstan is located in the eastern part of Central Asia and has surface borders in the Northern and North-Western areas with the Republic of Kazakhstan, in the Western part - with the Republic of Uzbekistan, in the South-West - with the Republic of Tajikistan and in the South-East - with People’s Republic of China. KR is a land-locked country, and all of its foreign trade operations are carried out by land transport. Rugged terrain in most regions prevents any attempts to develop rail transport infrastructure, which is why the road network continues to play the key role in organizing domestic and cross-border traffic. According to the National Statistical Committee of KR in 2012 over 96.8% of freight and 99.8% of passengers were carried by motor transport vehicles.

The key trading partners of Kyrgyz Republic are Russia, Kazakhstan and China. In 2012 they accounted in total for 65.3% of import and 36.2% of export flows of KR. The economy of KR is heavily dependent on foreign trade supplies, the share of imports in the GDP (import quota) in 2012 amounted to 83%.

The motor traffic connection in KR is established with 37 foreign states. Bilateral intergovernmental agreements on motor traffic connection have been signed with 21 countries (Russia, Ukraine, Belarus, Kazakhstan, Uzbekistan, Turkmenistan, Tajikistan, Azerbaijan, Moldova, Armenia, Latvia, Turkey, Iran, Pakistan, China, Germany, Poland, Mongolia, Georgia, Austria and France).

In 2012 the transport system of the Kyrgyz Republic carried 39.4 million tons of freight and 603.1 million passengers. In 2006 to 2011 the volume of motor road freight traffic was steadily building up, and the average growth rate of this indicator for the above period was equal to 9.3%. The share of the road transport in the total volume of freight flows increased from 90% in 2006 to 96.4% at the end of 2012.

The total length of public motor roads in Kyrgyz Republic is 18,810 km, of which 4,163 km are roads for international traffic, 5,778 km are national roads, and 8,969 km are local roads. The share of hard surface roads at the end of 2010 was equal to 91.5%. The average density of coverage of road pavement on the territory of Kyrgyz Republic is 17 km/km². Since 2006 the length of the road network has not changed, and no new roads have been put into service.

Freight and passenger traffic in the Kyrgyz Republic runs on six main road corridors: Bishkek-Osh, Bishkek-Naryn-Torugart, Osh-Batken-Isfana, Osh-Sarytash-Irkeshtam, Suusamyr-Talas-Taraz, Sarytash-Karamyk.

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2 Statistical Book “Kyrgyzstan in Numbers 2007-2011”
3 Ministry of Transport and Communications of Kyrgyz Republic
4 World Bank Databank
The transport sector of Kyrgyz Republic is very inefficient in terms of availability of logistics infrastructure. Most of the land transport infrastructure was built during Soviet times and wasn’t designed for cross-border traffic to and from neighboring countries. After the dissolution of the Soviet Union some portions of the road network previously used for domestic traffic within Kyrgyz SSR, were cut off by the newly established state borders, which considerably increased the overheads and transit time for domestic freight and passenger traffic. Now for carriage of goods and passengers from the southwestern part of Kyrgyzstan to its central and northern areas the transport vehicles have to cross twice the border with Uzbekistan.

One of the problems of the transport sector of Kyrgyzstan is the poor quality of the motor road infrastructure. According to the Global Competitiveness Index 2012-2013, the overall condition of the infrastructure rates KR as the 103th of 144 (3.4 points out of 7), and in terms of the quality of the motor road infrastructure Kyrgyz Republic ranks 133rd, by the railroad and airport infrastructure - 79th and 135th, respectively. Among the ACF member states based on this indicator (quality of infrastructure) Kyrgyz Republic shows the worst rating\(^5\).

\(^5\) The Republic of Belarus is not rated on the basis of this indicator
By LPI (Logistics Performance Index) the transport and logistical system of KR has a less negative rating: in 2012 the quality parameters of the infrastructure of KR were superior to those of Tajikistan and Armenia and matched the quality level of Russia.

Figure 5. Comparative Analysis of Transport Infrastructure of KR (LPI)


These data provide the basis for evaluation of the logistical system overall and offer just rough indication of the road infrastructure condition. An unbiased assessment of the road network infrastructure can be provided by IRI\(^6\) (International Roughness Index) measured on the main road corridors of the country.

According to the Asian Development Bank the minimum level of IRI on the national and transnational roads that have not been rehabilitated for the last 8 years is equal to 5, with a maximum at 10. The IRI of local roads may reach 15. The above parameters exceed by far the optimum level of IRI, which is 2, and are indicative of extremely worn down condition of the road infrastructure in KR. Moreover, the existing motor road network was built more than 20 years ago and was designed to accommodate transport vehicles of lower capacity and size. The existing bridges, overpasses and tunnels no longer conform to the modern maximum load and safety standards.

It should be noted that routine maintenance of international and national roads, including the Bishkek-Osh road corridor, is funded by the Kyrgyz Government from its national budget. Financing of such road maintenance activities has grown in recent years to a considerable extent (in 2005 - 2011 it increased more than 5-fold\(^7\), from US$ 5.4 to 28.7 million). It should be noted, however, that routine maintenance of regional and local community roads is chronically underfunded.

According to the “Sustainable Development Strategy of Kyrgyz Republic for 2013-2017” the key road infrastructure projects are: rehabilitation and development of road corridors Suusamyr-Talas-Taraz (199 km), Bishkek-Naryn-Torugart (539 km), Osh-Batken-Isfana (385 km), Karakol-Tup-Kegen (76 km), Batken-Isfana-Sulukta (120 km) (3 of the 6 main road corridors are in need of rehabilitation). One more extremely important project is the continuation of rehabilitation of the main motorway of KR Bishkek-Osh on its Bishkek - Kara-Balta and Madaniyat - Jalal-Abad sections. It appears full-scale budget funding of these projects is not possible, and, therefore, participation of IFIs will be required for their implementation.

\(^6\) International Roughness Index. This ratio characterizes the extent of the negative impact of the road pavement on the motor vehicles (ranging from 2 to 16, the higher the level, the stronger the negative impact). The target level is assumed to be equal to 2 m/km, the index value below 4 m/km is accepted to be admissible according to international practices, and IRI for soil road sections may vary within 10 to 16 m/km.

\(^7\) Draft Feasibility Report ‘Bishkek-Osh Road’, 2013
The proposed implementation of Kyrgyz motor road infrastructure rehabilitation projects will bring substantial economic benefits: According to the Asian Development Bank, the first of the three phases of the Bishkek-Osh road corridor rehabilitation project has reduced the average travel time on this road by 41%, and on some sections the average speed increased by 50%. The Economic Internal Rate of Return (EIRR) for phases I, II and III is estimated at 12.9%, 15% and 31%, respectively, which is above the minimum required rate of 12%.

It is noteworthy that the economic efficiency data for the first two phases of the project, published in the ADB’s Performance Evaluation Report upon project completion, differ only slightly from the original indicators, analyzed in the Project Appraisal. The performance indicators for Phase III in the Performance Evaluation Report are well above the forecasts contained in the Project Appraisal Report (EIRR was estimated in PAR at 19.3%).

As shown by IFI practices, implementation of road rehabilitation projects in the Kyrgyz Republic runs up against a number of problems. For example, the difficult terrain causes delays in project preparation schedules. Moreover, in most cases implementation of road rehabilitation projects carries serious social implications associated with resettlement, land acquisition and compensation for construction-related damages.

Selection of construction contractors for implementing road projects in Kyrgyzstan (including with support provided by the Asian Development Bank and the Japan Bank for International Cooperation) is normally carried out on the basis of International Competitive Bidding. In Kyrgyzstan the following international consultants and construction companies were involved in road rehabilitation projects: Carl Bro International, Central Consultant Inc., Kayson Engineering Company, Kocks Consult GmbH. Construction work is mostly performed by local contractors.

After the dissolution of the Soviet Union over 2,000 local government contractors of various sizes have been privatized. Currently they operate as subcontractors for road rehabilitation projects under sponsored funding schemes and as contractors for road construction projects. Private contractors supply materials such as road concrete mix and crushed aggregate for scheduled routine maintenance, but the maintenance departments carry out construction work on their own without any private contractors.

3.3. Current Condition of Bishkek-Osh Road Corridor

The Bishkek-Osh road is a strategic transport corridor providing an interregional link to North-South destinations. This motor road provides the only land-based route linking the Northern and Southern regions. The length of the entire corridor is 672 km. A significant part of the road runs across hillside with terrain that is challenging for drivers both in terms of road safety and ambient temperature conditions. During extreme temperature periods the road is closed for transport vehicles, and the risk of shutdown may continue throughout wintertime.

The Bishkek-Osh motor road passes across 4 out of the 7 Kyrgyz regions and provides transportation services to more than 2 million citizens of Kyrgyzstan. The road accounts for running about one third of the total international traffic of KR.

The most recent rehabilitation undertaken on this road corridor dates back to 1996-2007 when remedial work was carried out on 463 km of the road. At this point 69% of the route is in relatively good condition: according to ADB experts in the second half of 2010 IRI on these road sections averaged 3.5 m/km, which means the condition of the road was satisfactory. No rehabilitation was carried out on 31% of the road, including on sections Madaniyat – Jalal-Abad and Bishkek - Kara-Balta. According to the latest assessment provided by a consultant in 2013, the average IRI measured on the section Madaniyat - Jalal-Abad was about 7.5 m/km, and on the section Bishkek - Kara-Balta
about 6. These data are indicative of poor condition of the above road sections. In the consultant's opinion IRI close to 8 m/km puts road sections into the category of worn out roads.

Figure 6. Condition of Bishkek-Osh Road Corridor

At the end of 2010 the average travel time for a trip by motor vehicle from Bishkek to Osh was equal to 10 hours. Prior to implementation of the first three road rehabilitation phases it had been 17 hours.

No statistical analyses of the structure of freight flows channeled through the Bishkek-Osh road corridor have been conducted. Yet, it should be noted that this motor road plays a key role in domestic and international transit of petroleum and farming products.

3.4. Project Description

3.4.1. Objectives

The Project makes provision for allocation of funds by the Anti-Crisis Fund in the form of an investment loan for rehabilitation of the road section Madaniyat - Jalal-Abad as part of the implementation of Phase IV of the Investment Program “Rehabilitation of Bishkek-Osh Road” in the Kyrgyz Republic.

The program "Rehabilitation of Bishkek-Osh Road” is a component of CAREC, and the Bishkek-Osh road corridor is part of the CAREC-3 corridor. This corridor includes 6,900 km of roads and 4,800 km of railways, which extend from western and southern parts of Siberia (Russian Federation) and run across Afghanistan, Kazakhstan, Kyrgyz Republic, Tajikistan, Turkmenistan and Uzbekistan to Middle East and South Asia.
This Project\(^9\) pursues several objectives, primarily, creation of the necessary conditions for cost-effective passenger and freight traffic between the Northern and Southern regions of KR and concurrent reduction of risks, drivers and transport companies are exposed to during such traffic operations. This objective will be achieved by means of reduced operating overheads of transport vehicles and driving time required for covering the road section under rehabilitation, as well as by increasing its throughput capacity. Risk reduction will be ensured, primarily, by improved road traffic safety, and, secondly, by diminished influence of weather on time and overhead costs required for completing the trip.

In addition to the above primary objective the Project also has some secondary tasks to accomplish. Rehabilitation of the road corridor should become an added driver for poverty reduction in some Kyrgyz regions, should increase competitiveness of farming production in southern Kyrgyzstan by reducing transportation overheads, and ensure unhindered access of rural population to health-care centers and educational institutions.

Phase IV of the Comprehensive Project "Rehabilitation of Bishkek-Osh Road" consists of rehabilitation of two road sections: Bishkek - Kara-Balta (53 km) and Madaniat - Jalal-Abad (67 km). Funding of work on the above two sections will be performed in the form of parallel co-financing provided by the Asian Development Bank (ADB) and the Anti-Crisis Fund. The total funding of Phase IV of the Project is expected to be provided by ADB and ACF in the amount of US$ 203.8 million.

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\(^9\) Hereinafter the Project means funding of rehabilitation activities on the section Madaniyat - Jala-Abad provided by ACF as part of Phase IV. Comprehensive Project consists of 4 phases of rehabilitation of the Bishkek-Osh road.
The financial resources of the Anti-Crisis Fund in the amount of US$ 60 million will be provided for the rehabilitation of the Madaniyat - Jalal-Abad road section.

The road section Madaniyat - Jalal-Abad, 67 km in length, is located in the South of the Kyrgyz Republic. This segment of the route was not rehabilitated during the first three phases of the project "Rehabilitation of Bishkek-Osh Road", and in mid-2013 its pavement was in the worst condition (average IRI - 7.5 m/km). The proposed implementation of the Project will help eliminate the “bottleneck” which hampers development of traffic throughout the Bishkek-Osh road corridor. The strategic importance of the Project is due to the fact that Phase IV is the final component of the entire comprehensive project.

Figure 8. Project Map

3.4.2. Current Status of the Project

At this point ADB has already implemented three phases of the program "Rehabilitation of Bishkek-Osh Road", and the rehabilitation job is 69% complete. In addition to ADB other IFIs, such as the Islamic Development Bank, Japan International Cooperation Agency and Japan Bank for International Cooperation, also participate in the Project funding.

The key parameters of the first three phases of the project are presented in the table below:

Table 1. Key Parameters of Three Phases of Program Implementation

<table>
<thead>
<tr>
<th>Parameter</th>
<th>Phase I</th>
<th>Phase II</th>
<th>Phase III</th>
</tr>
</thead>
<tbody>
<tr>
<td>Endorsement of Project</td>
<td>1996</td>
<td>1997</td>
<td>2001</td>
</tr>
<tr>
<td>Completion of Project</td>
<td>2001</td>
<td>2005</td>
<td>2007</td>
</tr>
<tr>
<td>Project Total</td>
<td>US$ 76 M</td>
<td>US$ 110.9 M</td>
<td>US$ 57.1 M</td>
</tr>
<tr>
<td>EIRR</td>
<td>12.4%</td>
<td>14.8%</td>
<td>31.5%</td>
</tr>
</tbody>
</table>

Source: ADB Performance Evaluation Report. Kyrgyz Republic: Road Rehabilitation Project, Second Road Rehabilitation Project and Third Road Rehabilitation Project, 2010

Implementation of the three phases of the Project has been accepted by the Asian Development Bank and rated ‘successful’. It should be noted, however, that in the course of implementation of the first three phases the Asian Development Bank encountered a number of problems. The problems that
arose in the process of rehabilitation of road sections (lack of operational capacity of contractors and suppliers, adverse weather conditions) led to delays in completion of the first three phases by 17, 46 and 33 months, respectively. Moreover, the program staff failed to establish a road fund for financial support of road cloth maintenance because of the limitations imposed by the IMF program in KR.

The implementation of the three phases of the Project contributed to promotion of farming production activities in the Kyrgyz region of Fergana Valley, as well as to cutting down the price of agricultural products in Bishkek by reducing transport costs. Observers took note of an upward trend in value of property in the Project areas, and higher inter-regional labor mobility in Kyrgyzstan.

On 20 November 2012 the Manager received a preliminary application of the Ministry of Finance of KR for funding rehabilitation of a road section in accordance with Phase IV of the above program. On 7 December the Fund Council endorsed the Project Concept and the Manager’s Appraisal of the Preliminary Application.

On 18 November 2013 the Manager received Kyrgyzstan’s formal application requesting ACF funding of the Project with an Investment Application and Project Feasibility Study. Also the Government of KR issued an executive order establishing a panel of experts authorized to conduct negotiations on the draft loan agreement.

On 5 November 2013 the Asian Development Bank approved commitment of US$ 100 million for funding Phase IV of the Project (road section Bishkek - Kara-Balta), of which amount US$ 65 million would be allocated as a loan, and US$ 35 million would be provided in the form of a grant of the Asian Development Fund.

3.4.3. Technical Parameters

The Project Feasibility Report and Business Plan submitted by the Ministry of Transport and Communications of the Kyrgyz Republic contain the analysis of the current condition of the above road section, as well as a proposed design solution for rehabilitation of the road section and its rationale. The Feasibility Report has been prepared by a leading international consultancy group, Kocks Consult GmbH (hereinafter – the Consultant).

The Project Business Plan provides the following assessment of the Consultant of the road pavement condition and the proposed solution:

- Visual inspection and evaluation of the road revealed the origin and serious defects of the existing asphalt pavement.
- Taking into account the current pavement load capacity measured by the Consultant and the estimated traffic flow intensity, the existing road pavement requires increased strengthening. The strength of the existing road pavement structure, provided in certain locations by a single thin layer of asphalt, does not ensure the required load carrying capacity.
- Based on the results of the conducted tests and surveys, the existing base layer does not provide sufficient support for the pavement layers.
- In the course of rehabilitation work it is necessary to improve the drainage system.
- Most locations of the road pavement are characterized by severe roughness, deep rutting and cracks. If necessary, asphalt reinforcement can be laid and will require ground ballast and roller-flattening of the undulated road surfaces, as well as setting up of geogrids to minimize cracking and other measures to repair existing asphalt pavement.
- Laying reinforcement mat on relatively short-length asphalted road segments in between locations that will be newly paved is not the right solution.
- More than 90% of the Madaniyat - Jalal-Abad road section show high IRI
measurements (over 5.0 m/km), and the depth of rutting on 50% of the road exceeds 30 mm. Along the entire length of the road there are potholes, and on 80% of the total stretch of the road severe cracking has emerged. The pavement is also in need of urgent strengthening to support potential traffic flow intensity. It is unreasonable to resort to low-cost patchwork and postpone full-scale rehabilitation.

- In view of the current condition of the road pavement, comprehensive rehabilitation of the pavement is the preferred solution. Rehabilitation is considered to be the only appropriate plan of action to ensure the required strength by laying new groundwork and asphalt on supporting underlying granular material that will not be removed and will be used as sub-base.

Based on the presented rationale the Consultant recommended the following measures to perform rehabilitation of the above road corridor section:

- Removal of the old asphalt (the material should be re-utilized);
- Alignment and padding of the existing natural gravel (thickness - at least 210 mm), elimination of the deficiencies detected in the layer;
- Laying of road metal sub-base (240 mm);
- Laying bitumen base groundwork (90 mm);
- Laying surface asphalt coat (50 mm).

In respect of the selection of the geometric design standards the Consultant recommends to rely mainly on the Kyrgyz Building Code standards 32-01:2004, and in some cases, apply international standards (AASHTO or similar). Application of international standards is recommended to avoid the deficiencies of any specific Kyrgyz standard. It should be noted that in his Feasibility Study the Consultant proceeds from the assumption that most of the rehabilitated road sections will run along the existing route. Rerouting is an undesirable solution because of the risks of adverse social impacts associated with potential resettlement.

Based on the assessment of the current and projected future traffic flows, the Consultant concluded that the design of the road section should be classified as category II. Category II roads in accordance with the Kyrgyz standards are international and national roads with estimated traffic of 3,000 to 7,000 transport vehicles per day. The Kyrgyz Building Code (SNIP) 32-01:2004 requires category II roads to have two lanes in each direction, an overall width of the driveway of 7 or 7.5 m, a width of the hard shoulder of 0.75 m or 0.5 m, a shoulder width of 3.25, 3.5 or 3.75 m and no median strip. As required by the Kyrgyz standards the maximum permissible speed on category II roads is 120 km/h. The Consultant believes that over-sized speed limits may have an adverse impact on road safety and performance parameters of the Project. To reduce this risk it is recommended to consider turning to the relevant international speed limit standards.

In FS the Consultant evaluates preliminary parameters for configuring crossings, exits, road signs, driveway markings and roadside facilities. In most cases the Consultant recommends to rely on the Kyrgyz national design planning standards. In respect of the arrangement of sidewalks the Consultant recommends to consider the requirements of the Americans with Disabilities Act (ADA).

The Project also makes provision for rehabilitation of bridges located along the road section Madaniat - Jalal-Abad. The Consultant has identified the following deficiencies in the condition of bridges and spans:
- High wear rate and poor quality of concrete construction work;
- Cracks and disintegration (splitting) of beams/plates, exposure and corrosion of bare reinforcement elements;
- Flaws on the expansion joints and drainage culverts;
- Corroded and damaged bearing supports / in most cases bearing supports are missing;
- Cracks in bank abutments / bridge piles.

It is recommended to carry out rehabilitation work on 9 bridges.

The Consultant conducted a preliminary research of potential suppliers of construction materials for the Project. The FS indicates that the Kyrgyz Republic has facilities for the production of principal classes of cement, whereas special types of cement (sulfate-resistant, high-grade cements) are usually imported from the Russian Federation. Kyrgyzstan has no bitumen production plants of its own, and therefore, bitumen will be imported from neighboring countries. In the process of preparation of the Project procurement plan the Manager recommends to examine possibilities for providing preferences to producers of bitumen in the ACF member countries. A similar arrangement is recommended by the Consultant in the case of mineral aggregate production facilities.

3.4.4. Project Funding Requirements

The Project Funding Requirements are determined based on projected costs of rehabilitation of the above road corridor, as estimated by Kocks Consult GmbH. In the process of preparation of the FS the Consultant produced cost estimates for the Madaniyat - Jalal-Abad road section rehabilitation project. The total amount of funds required for the Project, including contingency expenses and estimated costs of consulting services on engineering and construction supervision under the Project, is equal to $60 million net of VAT.

In his Appraisal of the Preliminary Loan Application for this Project the Manager made provision for allocation of financial resources for funding the Project in the amount of US$ 50 million. Detailed cost estimates for the Project implementation provided by the Consultant in his FS demonstrated that this amount would be insufficient to complete the Project. The analysis revealed the need for additional funds in the amount of US$ 10 million. The Manager recommends increasing the amount of funding of the Project by ACF to US$ 60 million.

The structure of expenses is shown in the table below:

<table>
<thead>
<tr>
<th>Expense Item</th>
<th>Preliminary Estimated Expenses, USD</th>
<th>Total, USD</th>
</tr>
</thead>
<tbody>
<tr>
<td>General</td>
<td>436,733.60</td>
<td>1,674,437.60</td>
</tr>
<tr>
<td>Work distribution</td>
<td>7,896.00</td>
<td>187,340.40</td>
</tr>
<tr>
<td>Earth works</td>
<td>6,649,069.00</td>
<td></td>
</tr>
<tr>
<td>Drainage systems</td>
<td>4,413,456.00</td>
<td></td>
</tr>
<tr>
<td>Road pavement</td>
<td>28,134,300.00</td>
<td></td>
</tr>
<tr>
<td>Roadside facilities</td>
<td>3,355,728.19</td>
<td></td>
</tr>
<tr>
<td>Bridges</td>
<td>1,969,810.45</td>
<td></td>
</tr>
<tr>
<td>Other works</td>
<td>993,735.00</td>
<td></td>
</tr>
</tbody>
</table>
The above estimated costs do not include rehabilitation work on feeder roads, for which FS also provides cost estimates. Commitment of ACF funds for rehabilitation of the feeder roads is not envisaged by the Project.

Based on the above cost estimates the Manager recommends ACF to commit US$ 60 million for this Project, of which amount up to US$ 58 million to be allocated for design planning and construction work and up to US$ 2 million to be provided as payment for Project engineering and construction supervision consulting services to reduce reputation, corruption and construction risks.

The Beneficiary should be required to ensure Project co-financing in an amount about US$ 12 million, including US$ 9.5 million in the form of exemption from taxes (VAT) and other statutory charges imposed on contracts funded by the Investment Loan, and to allocate US$ 2.5 million of budget funds for land acquisition and resettlement for the purposes of the Project.

### 3.5. Economic Benefits

The Business Plan (BP), submitted by the Ministry of Transport and Communications of KR, highlights the principal economic and social benefits associated with implementation of the Project. The Business Plan focuses on the following general benefits: improved efficiency of the transport system, growth of inter-regional contacts, growth of employment and poverty reduction in the Project regions, as well as enhanced competitiveness of local producers.

Efficiency of the transport system will be improved due to reduction in logistics costs associated with traffic of goods and passengers, as well as shorter transit time. From this perspective, the efficiency of the Project can be evaluated by cost-benefit analysis of its implementation results. The analysis provided by the Consultant assumes as benefits the potential reduction of vehicle operating costs, shorter road transit time, as well as lower maintenance costs on the Project road section; and it assumes as costs - the capital investment for the roadway rehabilitation.

The economic assessment was carried out by the Consultant on the basis of comparison of the "project" and "no project" scenarios. According to the "no project" scenario the roads will be subjected to basic maintenance (for the project road it will involve patching, sealing of cracks and periodic surface repairs), whereas structural damages of the pavement will not be fixed, and the road condition...
will continue to deteriorate. The "project" scenario requires rehabilitation of the project road and selected feeder roads, followed by scheduled and routine maintenance.

The economic assessment of the Project provided in the BP was carried out by the Consultant based on the aggregated data collected from two road sections of Phase IV and on the following assumptions:

**Table 3. Economic Assessment Assumptions for Phase IV**

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Evaluation period</td>
<td>2014 – 2036</td>
</tr>
<tr>
<td>Discount factor</td>
<td>12%</td>
</tr>
<tr>
<td>Passenger traffic growth rate since 2014</td>
<td>7%</td>
</tr>
<tr>
<td>Freight traffic growth rate since 2014</td>
<td>4%</td>
</tr>
<tr>
<td>Maintenance costs (scheduled and winter-time maintenance)</td>
<td>US$ 1,126/km</td>
</tr>
<tr>
<td>Maintenance costs (pothole patching and sealing of cracks)</td>
<td>US$ 16/m²</td>
</tr>
<tr>
<td>Current IRI on project roads</td>
<td>6.0 – 8.0</td>
</tr>
<tr>
<td>Estimated IRI for “no project” scenario in 2017</td>
<td>10.0 – 16.0</td>
</tr>
<tr>
<td>Estimated IRI for “project” scenario in 2017</td>
<td>1.5</td>
</tr>
<tr>
<td>Estimated IRI for “project” scenario in 2026</td>
<td>4 – 6</td>
</tr>
<tr>
<td>Cost of working hours for drivers</td>
<td>US$ 1/h</td>
</tr>
<tr>
<td>Cost of non-working hours for passengers</td>
<td>US$ 0.25</td>
</tr>
</tbody>
</table>

Source: FS of Project “Rehabilitation of Bishkek-Osh Road Section, Phase IV”.

The Economic Internal Rate of Return (EIRR) for the entire Phase IV is estimated at 24.68%. This value exceeds by far the threshold of 12.0%, which is indication of efficiency of road construction and rehabilitation projects.

It is noteworthy that BP evaluates cost-effectiveness of the Project in the context of the whole Phase IV project implementation package.

For detailed analysis of the Project performance indicators (Madaniyat - Jalal-Abad road section) the Manager requested MTC to submit a detailed economic assessment report prepared by the Consultant. EIRR of the rehabilitation work to be carried out on the above road section, as estimated by the Consultant, will amount to 22.4%, which is also significantly higher than the threshold of 12%. The Net Present Value (NPV) of the Project is estimated at **US$ 42,36 million**. This indicator represents the net benefits KR will accrue from the Project in monetary terms, i.e. the total amount of cost savings for the transport companies and reduced budget operating expenditures net of capital invested into the rehabilitation of the road corridor, discounted to the current period.

The sensitivity analysis shows strong resilience of efficiency parameters of the Project to variations in the key inputs, such as increase in construction costs, changing traffic flow growth ratios, post-project vehicle maintenance overheads. The sensitivity analysis data are shown in Table 4.
### Table 4. Sensitivity Analysis of Efficiency Parameters (for 2 road sections)

<table>
<thead>
<tr>
<th>Scenarios</th>
<th>EIRR</th>
<th>NPV (US$ M)</th>
<th>Switching Threshold</th>
</tr>
</thead>
<tbody>
<tr>
<td>Baseline scenario</td>
<td>22.68%</td>
<td>162.42</td>
<td></td>
</tr>
<tr>
<td>Growth of capital costs by 40%</td>
<td>19.10%</td>
<td>126.72</td>
<td>182%</td>
</tr>
<tr>
<td>Growth of VOC by 40%</td>
<td>20.00%</td>
<td>104.3</td>
<td>112%</td>
</tr>
<tr>
<td>Road transit time is not reduced</td>
<td>16.50%</td>
<td>53.30</td>
<td>149%</td>
</tr>
<tr>
<td>Reduction in traffic flow by na 40%</td>
<td>13.60%</td>
<td>18.53</td>
<td>45%</td>
</tr>
<tr>
<td>No growth in traffic flow</td>
<td>19.90%</td>
<td>90.95</td>
<td>n/a</td>
</tr>
<tr>
<td>Costs +40%, benefits –40%</td>
<td>16.50%</td>
<td>54.09</td>
<td>60%</td>
</tr>
</tbody>
</table>

Source: FS of Project “Rehabilitation of Bishkek-Osh Road Section, Phase IV”.

3.6. **Project Social, Economic and Anti-Crisis Effects**

The Project will facilitate addressing one of the most important structural problems - traffic isolation of southern regions. Lower cost of freight transportation and, as a consequence, diminished overheads of foreign and domestic trade operations, will have a positive impact on the economic structure by reducing the balance of payments deficit. This process will evolve along two vectors: by reducing the cost of the transport component in the price of imports and by cutting overheads incurred in export operations, which improves competitiveness of exported goods on external markets.

For Kyrgyzstan improved transport infrastructure constitutes a significant driver for creating a better business environment to attract foreign investments.

The Project will have a significant positive impact on one more critical development-related problem of the Kyrgyz Republic, i.e. its high level of poverty. As shown in the social and economic review, at this point the average poverty rate is 38%, and Jalal-Abad is the most disadvantaged region, which is one of the Project sites (poverty rate is 55.7%). The current situation is further exacerbated by a rampant growth rate of poverty in Jalal-Abad: in 2011 it was 45.3%, whereas in 2010 - 44.7% (growth by 11 percentage points over the last two years). One of the causes of social problems in the southern part of KR, apart from the deteriorating general economic situation in the country, is the unstable political environment in this specific area. Southern regions due to severe social hardships experienced by the population are a major source of political instability in Kyrgyzstan.

Rehabilitation of the above road section in Jalal-Abad region construction on the basis of the experience gained in implementing the preceding phases of the Program will promote creating new jobs for the local population up to 5,000 man-months\(^{11}\). Given the estimated average time of employment for two months, the Project will provide temporary jobs to **2,500 persons**. Such a number of temporary jobs created for the Project implementation period (2014 - 2016), will help mitigate the social and economic crisis in the region.

Upon completion of the road rehabilitation activities the estimated growth in passenger and freight traffic will improve opportunities for the local communities to start and develop small and medium-size businesses in roadside areas, which will generate long-term employment and may have a positive impact on poverty reduction.

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\(^{10}\) Value of indicators in the first column, when EIRR goes down below 12%, and NPV is less than 0, i.e. when the project is no longer cost-effective.

\(^{11}\) Man-month. The evaluation is based on «Performance Evaluation Report. Kyrgyz Republic: Road Rehabilitation Project, Second Road Rehabilitation Project and Third Road Rehabilitation Project, ADB,2010»
In addition to creation of new jobs and development of roadside businesses, the proposed rehabilitation of the Madaniyat - Jalal-Abad road section will improve access to basic social and education services in the north of Kyrgyzstan (major health-care and education centers) both for the population of the Project area, and for all southern regions of the country.

Furthermore, availability of high-quality transportation to North-South destinations will open new markets for farming products of KR, will reduce losses in transit and may also contribute to reduction of the level and volatility of prices for agricultural products.

Project Impact on Macroeconomic Development Prospects

The proposed ACF Loan for the modernization of the road corridor will help ensure adequate investments into infrastructure. Given the relatively significant share of transport in the structure of GDP, development of the road infrastructure should promote economic diversification and diminish exposure of the economy to external shocks. In addition, construction projects will enable creation of new jobs and will promote growth of the GDP.

The proposed Project will help reduce budget expenditures for routine maintenance of the above road section, and thus, allocate such budget resources for maintenance and rehabilitation of other road sections on the transport network of KR. The figure below shows operating expenses based on the “project” and “no project” scenarios for a 22-years horizon.

As estimated by the Consultant, in 22 years the total amount of routine maintenance budget savings in KR will amount to US$ 17.2 million. The annual maintenance savings for the above road section will range from US$ 0.35 to 3.05 million (from 1.2 to 10.6% of the budget expenditures allocated for repairs of the road network in 2012).

The impact on debt sustainability is estimated as negligible. According to the IMF Kyrgyzstan has no problem of external debt service burden. Provided Kumtor restores its business performance, and given continued conservative external borrowing policies, the budget and debt positions will be rated as sustainable. Acceptance of the ACF Loan in the amount of US$ 60 million (about 1% of the GDP) on the proposed terms and conditions will not increase significantly the total national debt service burden.
3.7. Project Compliance with ACF Mission

According to the Manager the Project is fully consistent with the objectives of the Anti-Crisis Fund. The Project will contribute to improvement of economic and social stability of the Kyrgyz Republic, will help mitigate the aftermath of the social crisis in the southern part of KR and build the basis for further sustainable development of the region.

As indicated in one of the preceding sections (on social and economic benefits), the Project will improve the efficiency of the Kyrgyz transport system, will strengthen inter-regional relations, increase employment and reduce poverty. The above benefits are integral components of one of the ACF objectives: sustainable development of ACF member countries.

The Project will be implemented in a depression-stricken area of KR, Jalal-Abad region, where the poverty level in the last two years has grown by 11 percentage points. Creation of new jobs for construction work on the above road section in this region is fully in line with the anti-crisis objectives of the Fund operations. It is also noteworthy that in addition to the potential short-term positive impact (estimated duration of the Project is 3 years) the implementation activities will contribute to preventing further crises.

The Project possesses a strong integration potential, since the proposed road rehabilitation will not only promote traffic flows between Kyrgyz regions, but will also improve delivery of goods from southern regions of the country to Kazakhstan and Russia, as well as increase transit from Tajikistan. The Project is a very important component of CAREC: it is part of the CAREC 2 road corridor. This corridor extends from western and southern Siberia (Russian Federation) and runs across Afghanistan, Kazakhstan, Kyrgyz Republic, Tajikistan, Turkmenistan and Uzbekistan to destinations in the Middle East and South Asia.

As shown on the Matrix of Project Compliance with Fund Mission, developed by the Manager (Appendix 1), the Project is consistent with the Fund's objectives (compliance criteria are highlighted).

The arguments of the MTC of Kyrgyzstan in support of compliance of the Project with the ACF objectives, laid out in the Investment Application are accepted by the Manager as non-biased and sufficient.

3.8. Proposed Plan and Conditions for Project Funding

Kyrgyz Republic will act as the Investment Loan Beneficiary, and the Ministry of Transport and Communications of KR - as the Project implementation agency, which will establish a special group - Project Implementation Unit. Since the Project structure makes no provision for a Project Company, and the implementation management responsibilities are assigned to the Ministry of Transport and Communications of KR, the Manager recommends assigning to the Kyrgyz Republic the rights and obligations of the Ultimate Beneficiary as defined by the Regulation on ACF Investment Loans.

The funds borrowed from ACF constitute a sovereign loan and are an integral part of the sovereign liabilities of the Kyrgyz Republic. The Kyrgyz Republic will allocate the funds, borrowed from ACF, in its national budget as a source of funding of the budget deficit and as a budget expenditure item for financing the National Investment Project; it will also enter into its national budget the funds allocated for repayment and service of the ACF Loan. The above funding scheme conforms to the Regulation on the Use of ACF Resources for Providing Investment Loans.

In the context of the IMF program currently running in KR, a zero limit for non-preferential lending was agreed upon for the total portfolio of external sovereign and government-guaranteed
loans. KR has assumed the commitment to refrain from borrowing and issuance of guarantees for loans that may reduce the average grant-element for the above portfolio to a level below 35%.

In view of the above and given the need to qualify for the size of the grant-element of at least 35%, as well as for compliance with the funding terms and conditions tendered by the other Project participant (ADB), the Manager recommends to set the following financial conditions for the requested Loan:

- Interest rate: 1% per annum;
- Interest Margin: n/a;
- Risk Premium: n/a;
- Front-end fee - 0.5% of Investment Loan amount;
- Commitment Fee: n/a;
- Loan maturity, up to 20 years, including grace period 8 years;
- Co-financing amount due from Beneficiary - US$ 12 million (20% of ACF loan)
- Grant-element – 41.6%

3.9. Government Support

The Kyrgyz Republic will provide US$ 12 million out of its national budget in the form of exemption from taxes and other mandatory charges related to the Project implementation and by allocating funds for land acquisition in the area of the proposed road corridor rehabilitation in an amount equivalent to 20% of the ACF Investment Loan amount.

This Project is a component of the CAREC program, which is actively supported by the Government of the Kyrgyz Republic.

According to the "Sustainable Development Strategy of Kyrgyz Republic" the development of the transport sector is one of its top priorities. Transport and road networks are part of the 5 sectors of strategic importance according to this document.

3.10. Environmental Impact Assessment


The Investment Application submitted by MTC of KR indicates that the environmental impact of the Project implementation work on rehabilitation of the above road section will be minimized by the fact that most of construction operations are expected to be carried out within the boundaries of the existing right-of-way.

In accordance with the Agreement between the Manager and ADB, endorsed by the ACF Council, the ADB Safeguard Policies will apply to the Project. The Investment Application also makes reference to the Kyrgyz Government's readiness to comply with the ADB safeguards in carrying out project implementation operations, which will mitigate negative environmental impact risks.
Implementation of the Project will be carried out in strict compliance with the Environmental and Social Safeguards Policy of EDB, which classifies the Project as category "B", i.e. a project with potentially hazardous local environmental and social implications, which can be eliminated and/or prevented.

The Project has also been assigned category "B" in accordance with the ADB Safeguards, which means that the environmental impact of the Project will be limited by the boundaries of the right-of-way, that it will be of short duration and can be mitigated in the process of implementation.

According to the minutes of the meeting of the MTC representative with ADB and EDB (Appendix 3) the responsibility for monitoring the Project for compliance with ADB safeguard policies and for putting the Project parameters into conformity therewith, insofar as they are not inconsistent with the Environmental and Social Safeguards Policy of EDB, is assigned to the Kyrgyz MTC.

3.11. **Social Impact Assessment**

According to the Resettlement Plan prepared by the MTC of KR, the total number of households that will be affected by the Project is 110 (488 persons). As estimated by the MTC 4 houses will suffer considerably from the above impact (they will no longer be fit for residence), 6 more houses will be exposed to minor impacts. In total 10 shops will be subjected to significant impacts, and 2 more - to minor impacts.

Implementation of the Project will be carried out in strict compliance with the Environmental and Social Safeguards Policy of EDB, which classifies the Project as category "B", i.e. a project with potentially hazardous local environmental and social implications, which can be eliminated and/or prevented.

Phase IV of the program "Rehabilitation of Bishkek-Osh Road Section", which includes the proposed Project, has also been assigned category "B" by the Asian Development Bank. Category "B" is assigned to projects which carry social impacts that may require resettlement, but they are regarded as negligible.

According to the minutes of the meeting of the MTC representative with ADB and EDB (Appendix 3) the responsibility for monitoring the Project for compliance with ADB safeguard policies and for putting the Project parameters into conformity therewith, insofar as they are not inconsistent with the Environmental and Social Safeguards Policy of EDB, is assigned to the Kyrgyz MTC. The Project Implementation Unit possesses adequate expertise and resources to enable and carry out the proposed monitoring of the Resettlement Plan.
<table>
<thead>
<tr>
<th>Risk group</th>
<th>Description</th>
<th>Assessment of risk level</th>
<th>Impact on Project performance</th>
<th>Risk reduction measures</th>
<th>Risk assessment following reduction measures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Design risks</td>
<td>Risks of design errors and poor quality of design documentation</td>
<td>Medium</td>
<td>High</td>
<td>These risks can be reduced if the Manager participates in negotiations on the terms and conditions of the construction contract and in the process of preparation of the Project detail design by the Consultant, responsible for Project supervision.</td>
<td>Low</td>
</tr>
<tr>
<td>Construction risks</td>
<td>Risks of inflated cost of Project as compared with relevant parameters of FS.</td>
<td>High</td>
<td>Medium</td>
<td>Participation of the Manager in negotiating the terms and conditions of the General Contract. International Competitive Bidding according to IBRD procedures. Introduction into the agreement of penalties for increase in cost estimates of construction. Building sufficient contingency reserve funds.</td>
<td>Medium</td>
</tr>
<tr>
<td></td>
<td>Risks of inflated cost of Project as compared with relevant parameters of FS.</td>
<td>High</td>
<td>Medium</td>
<td>Participation of the Manager in negotiating the terms and conditions of the General Contract. Introduction into the agreement of penalties for delays in the schedule of construction. Continuous monitoring of Project progress.</td>
<td>Medium-High</td>
</tr>
<tr>
<td>Operating risks</td>
<td>Risks of insufficient funding of regular maintenance of the road section.</td>
<td>High</td>
<td>High</td>
<td>Monitoring by the Beneficiary of the operation performance of the road corridor, including on the basis of IRI, flow capacity measurements, etc., and updating the plan of funding maintenance operations in case of departure from the pre-set parameters.</td>
<td>Medium</td>
</tr>
<tr>
<td>Technological risks</td>
<td>Risks of non-compliance of proposed engineering solution with regulatory requirements imposed on the road corridor.</td>
<td>Medium</td>
<td>Medium</td>
<td>Flexible approach to selection of engineering standards for design planning. Normally such as the Building Code (SNIP) of KR, and in the event of any deficiencies found in it, turn to AASHTO or other international standards.</td>
<td>Low</td>
</tr>
<tr>
<td>Supplier risks</td>
<td>Risks arising from inadequate capacity of suppliers of construction materials and problems of delivery to construction site.</td>
<td>High</td>
<td>High</td>
<td>Detailed analysis of available capacity of construction materials suppliers and transport companies and due consideration of collected data in design planning. Introduction of quality requirements into bidding documents. Introduction of penalties into the contract agreement.</td>
<td>Medium</td>
</tr>
<tr>
<td>Financial risks</td>
<td>Risks of Borrower's insolvency</td>
<td>Low-Medium</td>
<td>High</td>
<td>The key factor of reduction of this risk lies in the provision of cross-default conditions in the draft Agreement. Similar conditions are practiced in KR in arrangements with other leading IDBs.</td>
<td>Low</td>
</tr>
<tr>
<td>Environmental risks</td>
<td>Risks of Project’s adverse impact on environment.</td>
<td>Medium</td>
<td>High</td>
<td>In order to reduce such risks environmental assessment will be carried out in accordance with the ADB safeguards. According to the minutes of the meeting of the MTC representative with ADB and EDB (Appendix 3) the responsibility for monitoring the Project for compliance with ADB safeguard policies and for putting the Project parameters into conformity therewith, is assigned to the MTC of KR</td>
<td>Low</td>
</tr>
<tr>
<td>Social risks</td>
<td>Risks of Project’s adverse impact on social structure of local communities living in the vicinity of road corridor.</td>
<td>Medium</td>
<td>High</td>
<td>Wherever possible rehabilitation operations must be carried out on the existing road, and rerouting should be considered only on accident-prone sections. In order to reduce such risks social assessment will be conducted in</td>
<td>Low</td>
</tr>
</tbody>
</table>
accordance with the ADB safeguards. According to the minutes of the meeting of the MTC representative with ADB and EDB (Appendix 3) the responsibility for monitoring the Project for compliance with ADB resettlement policies and for putting the Project parameters into conformity therewith, is assigned to the MTC of KR

| Legal risks | Risks related to inappropriate interpretation and, as a consequence, non-performance (delayed performance) under the Investment Loan Agreement and related documents, other than legal provisions of KR. Risks associated with the need of suppliers to obtain permits, licenses and other documents as required by Kyrgyz legislation or relevant international treaties. | High | Medium | The principal risk reduction factors are:  
- Signing by the Manager of the Investment Loan Agreement directly with KR and its ratification in due process, which will enhance its status as an international agreement and will thus ensure its precedence over national legislation of KR;  
- Introduction into the Agreement of penalties, which may be applied in case of breach by the Borrower of any provision thereof. |

| Corruption and fiduciary risks | Corruption Perception Index, estimated for Kyrgyzstan by Transparency International, is deteriorating: in 2012 Kyrgyz Republic was rated 154th of 183 countries; compare with 150th in 2007. In the process of funding Project potentially corruption and fiduciary risks may arise in connection with alleged inappropriate use of funds. | High | High | In the process of Project implementation IBRD procurement and disbursement policies and procedures will be used, which provide for financial penalties for violations thereof. For purposes of procurement monitoring provision is made for services if IBRD experts. Compliance review will be performed in accordance with the relevant recommendations of EAG and FATF. |
## Appendix 1. Matrix of Project Compliance with ACF Mission

### Objectives

<table>
<thead>
<tr>
<th>Anti-crisis</th>
<th>Integration</th>
<th>Sustainable development</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Criteria</strong></td>
<td><strong>Social Stability:</strong></td>
<td><strong>Economic Sustainability:</strong></td>
</tr>
<tr>
<td><em>Project implementation in depression-stricken sector</em></td>
<td><em>Creation of new jobs</em></td>
<td><em>Growth of tax revenue (both directly from project implementation, and indirectly, from creating conditions for development of other sectors and businesses)</em></td>
</tr>
<tr>
<td><em>Project implementation in sector exposed to crises</em></td>
<td><em>Creation of new jobs for disadvantaged groups of population</em></td>
<td><em>Promotion of export-driven sectors</em></td>
</tr>
<tr>
<td><em>Funding of project, whose failure may produce adverse social and economic impacts (threat to food security, energy security, environmental sustainability, sanitary conditions, agricultural production capacity)</em></td>
<td><em>Improvement of food security</em></td>
<td><em>Growth of share of value added, produced in country</em></td>
</tr>
<tr>
<td><em>Implementation of project of strategic importance in the context of increasing budget constraints</em></td>
<td><em>Reduction of volatility of prices for food and basic services</em></td>
<td><em>Support of stability of operation of national power supply systems</em></td>
</tr>
<tr>
<td><em>Restoration of sector in the aftermath of armed conflicts, mass riots, etc.</em></td>
<td><em>Increase availability of basic services (education, health care, etc.)</em></td>
<td><em>Reduction of logistics overheads</em></td>
</tr>
<tr>
<td><em>Creation of new jobs in the context of growing unemployment</em></td>
<td><em>Improve access to higher quality water resources</em></td>
<td><em>Diversification of economy and/or exports</em></td>
</tr>
</tbody>
</table>

### Notes

12 Investment project taken into consideration should match to one or more criterion from each column of the matrix. The project meets criteria which are highlighted in yellow.
Управляющему средствами
Антикризисного фонда Евразийского
экономического сообщества -
Евразийскому банку развития
Республика Казахстан, 050051
г. Алматы, пр. Достык, д.220
Тел: +7 (727) 244 40 44
Факс: +7 (727) 244 65 70
e-mail: info@eabr.org

В соответствии с Договором об учреждении Антикризисного фонда Евразийского экономического сообщества (далее — Фонд) настоящим направляем Вам Заявку на предоставление из средств Фонда Инвестиционного кредита в сумме 60 млн. долларов США для рассмотрения и подготовки заключения Управляющего средствами Фонда в соответствии с Порядком предоставления инвестиционного финансирования из средств Фонда, утвержденным Советом Фонда.

Запрашиваемые средства Фонда будут направлены на финансирование проекта «Реконструкция автомобильной дороги «Бишкек-Ош», Фаза IV», реализация которого будет осуществляться сформированной в Министерстве транспорта и коммуникаций Кыргызской Республики группой реализации проекта.
В соответствии с условиями предоставления Инвестиционного финансирования предполагается, что Кыргызская Республика выступит Получателем средств Фонда.

Выделенные из Фонда средства предполагается израсходовать в течение 3 лет, начиная с 2014 года, в соответствии с Руководством Всемирного банка по предоставлению средств на реализацию проектов от 1 мая 2006 года (World Bank Disbursement Guidelines for Projects, dated May 1, 2006).

Возврат средств Фонда предполагается производить в течение 20 лет, льготный период - 8 лет. В соответствии с утвержденными Советом Фонда параметрами, предлагаются следующие условия предоставления Инвестиционного кредита:

- ставка процентов, начисляемых на использованную и непогашенную сумму Инвестиционного кредита – 1% годовых;
- Премия за риск – 0%, начисляемая на снятую и непогашенную сумму Инвестиционного кредита сверх Процентов;
- комиссия за резервирование – не применяется;
- единовременная комиссия – 0,5% от суммы Инвестиционного кредита.

Для проведения оценки Проекта в приложении к настоящей заявке направляем Инвестиционную заявку, содержащую информацию о проектной компании и о Проекте. Настоящим удостоверяем, что указанная в прилагаемой Инвестиционной заявке информация является полной и достоверной и может быть подтверждена в случае необходимости документально. Выражаем согласие на полную проверку достоверности указанных в Инвестиционной заявке данных. Обязуемся своевременно информировать Управляющего средствами Фонда обо всех изменениях данной информации и представлять по Вашему запросу все необходимые для подтверждения представленной информации документы, а также любую обоснованно запрошенную дополнительную информацию.

Приложения:
Инвестиционная заявка на 49 л.
Отчет о технико-экономическом обосновании Проекта на 255 л.
Экономический отчет по Проекту на 31 л.
План переселения Проекта на 99 л.
Рамочная программа экологической оценки и экологического обзора 54 л.
Документы, удостоверяющие полномочия лиц, подписавших Заявку и Инвестиционную заявку на 2 л.

Министр

О. Лаврова
Appendix 3. Minutes of Meeting of MTC, ADB and EDB

MINISTRY OF TRANSPORT AND COMMUNICATIONS (MOTC)

ASIAN DEVELOPMENT BANK (ADB)

And

EURASIAN DEVELOPMENT BANK (EDB)

with respect to the

CAREC Corridor 3 (Bishkek-Osh Road) Improvement Project, Phase 4
in
Kyrgyz Republic

A. Introduction

1. A joint ADB - EDB mission visited the Kyrgyz Republic on 12 November 2013 to firm up implementation arrangement of the CAREC Corridor 3 (Bishkek-Osh Road) Improvement Project, Phase 4 (the Project). On 4 June 2013, in the Kyrgyz Republic, ADB and EDB signed a Memorandum of Understanding (MOU) in accordance with the Framework Cofinancing Agreement between ADB and EDB signed on 3 May 2013 in Delhi. The MOU summarized the findings of the mission and records the understandings reached between ADB and EDB acting as the EurAsEC Anti-Crisis Fund (ACF) Resource Manager (collectively referred to as the Cofinancers and individually as a Cofinancier).

2. As stated in the MOU, for the purposes of EDB-financed section, ADB and EDB agree that a single process for social and environmental assessment and planning, safeguard documentation, consultation, and disclosure requirements shall be conducted to satisfy both the ADB's Safeguard Policy Statement (2009) (SPS) and the safeguard requirements of EDB. During project preparation and implementation, ADB shall be responsible for conducting due diligence, reviewing documents and supervising project activities in accordance with ADB's SPS. EDB will be responsible for conducting due diligence, reviewing documents and supervising other activities that are not required by ADB's SPS but may be required by EDB.

3. Furthermore, during Project implementation, ADB shall be responsible for ensuring project compliance with ADB safeguard requirements and complaints are resolved in relation to the ADB-financed section only; while EDB shall be responsible for ensuring project compliance with safeguard requirements and complaints are resolved in relation to the EDB-financed section only. This meeting minutes is to document the procedure for interaction amongst MOTC, ADB and EDB in related to safeguards during project implementation.

B. Implementation Arrangement

4. The Ministry of Transport and Communications (MOTC) will be the executing agency. The Investment Project Implementation Group (IPIG) in MOTC will be responsible for Project implementation activities and the safeguard team in IPIG will be responsible for the daily supervision and monitoring of the safeguard implementation based on SPS. The safeguard team is to be financed under the project management line item of the section to be financed by the ADB.
B.1. Supervision of Safeguard Implementation

5. MOTC/IPIG will supervise the safeguards compliance for both sections. MOTC/IPIG will review the implementation of the Land and Resettlement Plan (LARP) and Environmental Monitoring Plan (EMP) for both sections.

6. ADB and EDB will conduct the project and safeguards review missions in its own financed section. EDB will inform ADB their annual project review mission schedule and invite ADB to participate in reviewing the safeguards implementation status of the EDB-financed section. ADB will participate in reviewing safeguards implementation of EDB-financed section and provide recommendations for SPS compliance, if necessary.

7. For LARP implementation, resettlement specialists (one international and one national) in the construction supervision consultant to be recruited under each section paid for by each Cofinancier. Any corrective actions or mitigation measures of unanticipated LAR impacts identified in any of the road section shall be the responsibility of the concerned Cofinancier and shall follow the provisions and entitlements set forth in the LARP of the concerned road section.

8. For EMP implementation, the construction supervision consultant to be recruited under each section paid for by each Cofinancier, will assist MOTC/IPIG in environmental monitoring and endorsing site-specific EMPs (SEMPs) to be prepared by the contractors as needed.

B.2. Safeguards Reporting

9. Progress reports: MOTC/IPIG, with the assistance of the construction supervision consultants to be recruited under each section paid for by each Cofinancier, will submit (i) quarterly progress report with a separate section on safeguard implementation for each road section, (ii) semi-annual environmental monitoring report for each road section, and (iii) semi-annual resettlement monitoring report for each road section. On ADB-financed section, the reports submitted to EDB are for information only and are the sole responsibly of ADB. On EDB-financed section, EDB will share the reports to ADB. ADB will provide SPS compliance recommendations for EDB and MOTC/IPIG to incorporate, if needed, and the reports are the sole responsibly of EDB.

10. Completion/Compliance report of Land Acquisition and Resettlement Plan: MOTC/IPIG will prepare completion/compliance report of the LARP for each section with the assistance of the construction supervision consultants to be recruited under each section paid for by each Cofinancier. On ADB-financed section, MOTC/IPIG will request ADB for no objection and send the report to EDB for information only. On EDB-financed section, MOTC/IPIG will request EDB for no objection and EDB will send the report to ADB for information. ADB will provide SPS compliance recommendations for EDB and MOTC/IPIG to incorporate, if required.

B.3. Civil Works Contract and Mobilization

11. MOTC/IPIG will request ADB for no objection in signing the civil works contract and start works on the ADB-financed section once meeting all the safeguards and non-safeguards requirements in the financing agreement with ADB.

12. MOTC/IPIG will request EDB for no objection in signing the civil works contract and start works on the EDB-financed section once meeting all the safeguards and non-safeguards
requirements in the financing agreement with EDB.

B.4. Safeguards Disclosure

13. Until EDB has established its own safeguards policies, updated Initial Environmental Examination (IEE), Environmental Management Plan (EMP), and LARP, as well as semi-annual environmental and resettlement monitoring reports for both sections, if any, will be endorsed and disclosed by ADB at a final stage, with a disclaimer on EDB endorsement, by MOTC/IPIG’s request. After EDB has its safeguard policy established, EDB will follow its safeguard policy requirements in disclosure and in addition to disclosure on ADB website.

B.5. Safeguards Complaints

14. To ensure proper handling and resolution of complaints emanating during project preparation and construction, ADB will ensure all complaints emanating from the ADB-financed section will be handled and resolved based on the Grievance Redress Mechanism (GRM) specified in the IEE/LARP prepared for the ADB-financed road section only; EDB will ensure all complaints emanating from the EDB-financed section will be handled and resolved based on the GRM specified in the IEE/LARP prepared for the EDB-financed road section only. Complaints sent through ADB accountability mechanism will be excluded if they are about actions that are not related to ADB-financed road section. Until EDB has established its accountability mechanism, complaints related to EDB-financed road section will be channeled in accordance with the Kyrgyz Republic legal system.

B.6. Safeguards Knowledge Sharing and Capacity Building

15. ADB will inform EDB of ADB-organized safeguards training program in Manila and EDB will send representatives to ADB Manila to participate in the safeguards training during the first year of project implementation or as appropriate. In addition, EDB staff may opt to participate in the ADB Kyrgyz Resident Mission Office sponsored capacity building activities for environment and social safeguards under various capacity development technical assistance.

Signed in Bishkek on __ November 2013

[Signature]

Kubanychbek Mamaev, Director, IPIG

[Signature]

Susan Lim, Transport Specialist, ADB

[Signature]

Alexey Cherekaev, Head of ACF Project Group, EDB
Appendix 4. Memorandum of Understanding of ADB and EDB on Co-finnancing of Project "Rehabilitation of Bishkek-Osh Road, Phase IV"

MEMORANDUM OF UNDERSTANDING
on COLLABORATIVE COFINANCING
between ASIAN DEVELOPMENT BANK (ADB)
and EURASIAN DEVELOPMENT BANK (EDB)
with respect to the CAREC Corridor 3 (Bishkek-Osh Road) Improvement Project, Phase 4 in Kyrgyz Republic

A. Introduction

1. A joint ADB - EDB mission visited the Kyrgyz Republic from 27 May to 4 June 2013 for fact-finding to firm up the project design, scope, components, and financing of CAREC Corridor 3 (Bishkek-Osh Road) Improvement Project, Phase 4. A record of mission members and persons consulted is in Annex 1.

2. This Memorandum of Understanding (MOU) is signed in accordance with the Framework Cofinancing Agreement between ADB and EDB signed on 3 May 2013 in Delhi and summarizes the findings of the mission and records the understandings reached between ADB and EDB acting as the EurAsEC Anti-Crisis Fund (ACF) Resource Manager (collectively referred to as the Cofinancers and individually as a Cofinancer). Such findings and understandings are subject to confirmation by higher authorities of the Cofinancers.

B. Particulars of the Project

B.1. Project Description

3. The Kyrgyz Republic is a landlocked, mountainous country with formidable geographic barriers that constrain its ability to effectively participate in international trade. Its development efforts are further hampered by inadequate physical infrastructure, which is in need of investment and regular maintenance.

4. Bishkek, the capital of the Kyrgyz Republic, is the country's political and economic hub with a dense population of about one million. The largest city after Bishkek is Osh (population 250,000), located in the Fergana valley in the south, the country's major agricultural area. These two cities' GDP accounts for nearly half of the total for the nation, home to 80% of the country's industry.

5. The Bishkek-Osh road represents about one-third of the core international road corridor network in the Kyrgyz Republic, and links the country to Kazakhstan in the north, Uzbekistan and Tajikistan in the south, and the People's Republic of China in the southeast. It crosses four of the seven provinces of the country and serves about 2 million people. It is the only direct surface link between the southern and northern parts of the country making it crucial for maintaining the country's social, political, and economic integrity. The Bishkek-Osh road forms part of the Central Asia Regional Economic Cooperation (CAREC) Corridor 3, which runs from the west and south Siberian region of the Russian Federation through Kazakhstan, Kyrgyz
Republic, Tajikistan, Afghanistan, and Uzbekistan to the Middle East and South Asia. The Bishkek-Osh road also passes through some of the poorest districts of the area, such as Osh Oblast and Jalalabad, both have over 40% of urban and rural poverty rate.

6. The development of the transport sector is very important for landlocked Kyrgyz Republic as it will help ensure a cost-effective access to regional and domestic markets. It will also help generate employment and provide services throughout the country. The Project will improve the national and regional connectivity by rehabilitating an estimated 120 km of crucial road sections between Bishkek and Osh. The Project is consistent with the government's priority in upgrading key corridors as stated in the National Strategy of Sustainable Development (2013–2017). The Project is in line with the draft Country Partnership Strategy (2013-2017) which has as its priority theme development of a successful and stable democratic [stage] through inclusive growth in addressing regional disparities. By improving the key corridor in the Kyrgyz Republic, the poorest regions in the Kyrgyz Republic will have improved access to regional and domestic economic activities. Improving the road network, especially for connecting rural populations to urban centers for access to services and trade in domestic and regional markets, is critical for inclusive economic growth and social development.

7. The impact of the Project will be enhanced regional connectivity and safer movement of goods on Bishkek-Osh Road. The outcome of the Project will be improved efficiency and sustainability on transport operations on the Bishkek-Osh Road.

8. The Project outputs will be (i) 52.5 km of rehabilitated road from Bishkek to Kara Balta (km 8.5-km 61), (ii) 67 km of rehabilitated road from Madaniyak to Jalalabad (km 507.5 - km 574.5), (iii) 100 km of performance-based maintenance (PBM) contract pilot section from Kara-Balta to km 161, and (iv) road safety enhancement and awareness program.

B.2. Cost Estimates and Financing Plan

9. The Project is estimated to cost $193 million (Table 1). The Government is seeking assistance from ADB and Eurasian Development Bank (EDB) to finance the Project.

10. ADB will provide a grant and a loan totaling $100 million from ADB's Special Funds resources to help finance the Project. The loan will have a 32-year term, including a grace period of 8 years, an interest rate of 1.0% per annum during the grace period and 1.5% per annum thereafter, and such other terms and conditions set forth in the draft financing agreement. ADB will finance 52.5 km of rehabilitated road from Bishkek to Kara Balta (km 8.5 - km 61), 50% PBM contract pilot, and the road safety enhancement and awareness program.

11. The Amount for EDB, preliminary approved for the Project by the ACF Council is US$ 50 million. The Government will request EDB to provide $50 million for civil works to finance 67 km of rehabilitated road from Madaniyak to Jalalabad (km 507.5 - km 574.5) and consulting services for engineering and supervision. Preliminary approved loan terms are 20 years (include 5 years grace period) and 1% interest annum.  

12. The Government will provide counterpart funding of $33 million to cover (i) taxes and duties related to all civil works, goods, and consulting services, (ii) 50% PBM contract pilot, and (iii) land acquisition and resettlement and other miscellaneous costs. The summary financing

1 Loan terms are subject to final approval by the ACF Council.
plan is in Table 2.

**Table 1: Project Investment Plan**

<table>
<thead>
<tr>
<th>Item</th>
<th>ADB</th>
<th>EDB</th>
<th>Government</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Investment Costs</td>
<td>($ million)</td>
<td>% of Cost Category</td>
<td>($ million)</td>
<td>% of Cost Category</td>
</tr>
<tr>
<td>1. Rehabilitation of 52.6 km from Bishkek to Karasuu</td>
<td>75.5</td>
<td>100</td>
<td>47.5</td>
<td>100</td>
</tr>
<tr>
<td>2. Rehabilitation of 67 km from Madanyak to Jalalabad</td>
<td>2.5</td>
<td>50</td>
<td>2.5</td>
<td>50</td>
</tr>
<tr>
<td>3. Performance-based maintenance contract pilot</td>
<td>4.8</td>
<td>100</td>
<td>4.8</td>
<td>100</td>
</tr>
<tr>
<td>5. Consulting services for engineering, supervision and project management</td>
<td>2.7</td>
<td>60</td>
<td>2.7</td>
<td>60</td>
</tr>
<tr>
<td>6. Consulting services for engineering and supervision</td>
<td>1.3</td>
<td>100</td>
<td>1.3</td>
<td>100</td>
</tr>
<tr>
<td>7. Project management</td>
<td>2.5</td>
<td>100</td>
<td>2.5</td>
<td>100</td>
</tr>
<tr>
<td>9. Total Base Cost</td>
<td>84.0</td>
<td>50.5</td>
<td>33.0</td>
<td>167.5</td>
</tr>
<tr>
<td>B. Contingencies</td>
<td>16.0</td>
<td>9.5</td>
<td>24.5</td>
<td></td>
</tr>
<tr>
<td>C. Financing Charges During Implementation</td>
<td>1.0</td>
<td>1.0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Project Cost</td>
<td>100.0</td>
<td>60.0</td>
<td>21.0</td>
<td>17.0</td>
</tr>
</tbody>
</table>

In mid-2013 prices
Source: Asian Development Bank Estimates

**Table 2: Financing Plan**

<table>
<thead>
<tr>
<th>Source</th>
<th>Amount ($ million)</th>
<th>Share of Total (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asian Development Bank</td>
<td>100.00</td>
<td>52</td>
</tr>
<tr>
<td>(Asian Development Fund)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Eurasian Development Bank</td>
<td>60.00</td>
<td>31</td>
</tr>
<tr>
<td>Government</td>
<td>33.00</td>
<td>17</td>
</tr>
<tr>
<td>Total</td>
<td>193.00</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Asian Development Bank estimates

1. **Implementation Arrangements**

13. The Ministry of Transport and Communications (MOTC) will be the executing agency. It has implemented all development partner-financed road projects since 1995, and has accumulated considerable experience. The Investment Project Implementation Group (IPIG) in MOTC will be responsible for Project implementation activities.

2. **Processing Schedule**

---

1 The Amount for EDB, preliminary approved for the Project by the ACF Council is US$ 50 million (see paragraph 11).
2 The amount of US$ 60 million is subject to approval by the ACF Council.
3 The Amount for EDB, preliminary approved for the Project by the ACF Council is US$ 50 million (see paragraph 11).

The amount of US$ 60 million is subject to approval by the ACF Council.
14. Provided that the internal review procedures of the Government and the Cofinanciers support the proposal, further Project processing will be according to the following schedule:

<table>
<thead>
<tr>
<th>Loan/Grant Negotiations</th>
<th>ADB</th>
<th>EDB</th>
</tr>
</thead>
<tbody>
<tr>
<td>Board Consideration</td>
<td>Aug 2013</td>
<td>Aug 2013</td>
</tr>
<tr>
<td>Loan/Grant Signing</td>
<td>Sept. 2013</td>
<td>Nov 2013</td>
</tr>
<tr>
<td>Loan/Grant Effectiveness</td>
<td>Oct. 2013</td>
<td>Dec 2013</td>
</tr>
<tr>
<td></td>
<td>Dec. 2013</td>
<td>Feb 2014</td>
</tr>
</tbody>
</table>

C. Understandings Reached between the Cofinanciers

15. The Cofinanciers will promptly inform each other of any event which interferes or threatens to interfere with the successful processing and implementation of the Project.

16. Each Cofinancier will retain its independent right of action and decision under its respective Loan/Grant Agreement to be signed with the Borrower.

17. The Cofinanciers will inform each other sufficiently in advance of any proposed Project mission by its representatives so as to afford a reasonable opportunity to participate in such mission. In case joint missions are not possible, the Cofinanciers will keep each other informed of the progress of the Project, including provision of copies of the findings of any Project missions by its representatives.

18. The following will be in accordance with each Cofinancier’s respective policies and procedures:

   (a) Procurement of goods and services, and the use of consulting services to be financed under the Cofinanciers’ loans/grant;

   (b) Disbursement arrangements and establishment of accounts used for payments from the Cofinanciers’ loans/grant;

   (c) Reporting mechanisms and auditing of Project accounts related to the Cofinanciers’ loans/grant; and

   (d) Measures against money laundering and fight against the financing of terrorism.

19. In the interests of economy and efficiency of the Project, wherever possible, both cofinanciers will determine the procurement and consultant’s selection procedure that ensure:

   a) Satisfactory quality and are compatible with the balance of the Project;

   b) Delivery of and completion in timely fashion; and

   c) Does not affect adversely the economic and financial viability of the Project.

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4 For ADB, procurement of all goods and works financed under the loan/grant will be carried out in accordance with ADB’s Procurement Guidelines dated April 2010, as amended from time to time. The selection and engagement of consultants financed under the Grant will be carried out in accordance with Guidelines on the Use of Consultants by ADB and its Borrowers dated April 2010, as amended from time to time.
20. For the purposes of EDB financed section; the Cofinancers agree that: (a) A single process for social and environmental assessment and planning, safeguard documentation, consultation, and disclosure requirements shall be conducted to satisfy both the ADB’s Safeguard Policy Statement (2009) (SPS) and the safeguard requirements of EDB. During project preparation and implementation, ADB shall be responsible for conducting due diligence, reviewing documents and supervising project activities in accordance with ADB’s SPS. EDB will be responsible for conducting due diligence, reviewing documents and supervising other activities that are not required by ADB’s SPS but may be required by EDB. (b) EDB financed section will be subject to ADB’s Anticorruption Policy (1998) and Integrity Principles and Guidelines (2012), both as amended from time to time. Any party found in breach of ADB’s Anticorruption Policy may be subject to sanctions in accordance with ADB’s Integrity Principles and Guidelines. Any legal entity or individual debarred or cross debarred in accordance with the Integrity Principles and Guidelines shall be ineligible to participate in project cofinanced under this Memorandum.

21. ADB confirms that social and environmental assessment and planning, safeguard documentation, consultation, and disclosure during Project preparation shall be conducted to satisfy ADB’s SPS in relation to the ADB-financed section and the EDB-financed section. EDB confirms that the social and environmental assessment and planning, safeguard documentation, consultation, and disclosure during project preparation shall be undertaken to EDB’s satisfaction in relation to the EDB-financed section.

22. During implementation, ADB shall be responsible for ensuring project compliance with ADB safeguard requirements and complaints are resolved in relation to the ADB-financed section only, while EDB shall be responsible for ensuring project compliance with safeguard requirements and complaints are resolved in relation to the EDB-financed section only. The procedure for interaction between ADB and EDB is to be developed during further negotiations which to be documented in a supplementary MOU to be signed by 15 July 2013.

Signed in Bishkek, Kyrgyz Republic on 4 June 2013

[Signature]
Name: Susan Lim
Title: Transport Specialist

[Signature]
Name: Alexey Cherekaev
Title: Head of ACF Project Group
### Appendix 5. Macroeconomic Performance Indicators of Kyrgyz Republic

<table>
<thead>
<tr>
<th>Indicator</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nominal GDP, cumulative (KGS million)</td>
<td>285,989</td>
<td>304,350</td>
<td>59,011</td>
</tr>
<tr>
<td>Nominal GDP, cumulative (US$ million)</td>
<td>6.198</td>
<td>6.475</td>
<td>1.237</td>
</tr>
<tr>
<td>GDP growth rate in constant prices, compared with previous period, %</td>
<td>6.0</td>
<td>-0.9</td>
<td>7.6</td>
</tr>
<tr>
<td>Consumer price index growth compared with December of previous year, %</td>
<td>5.7</td>
<td>7.5</td>
<td>1.1</td>
</tr>
<tr>
<td>Average nominal wages at year end, KGS</td>
<td>9,352</td>
<td>10,891</td>
<td>10,619</td>
</tr>
<tr>
<td>Average nominal wages at year end, US$</td>
<td>201</td>
<td>230</td>
<td>222</td>
</tr>
<tr>
<td>National budget revenues (% of GDP)*</td>
<td>27.2</td>
<td>28.6</td>
<td>36.5</td>
</tr>
<tr>
<td>National budget expenditures (% of GDP)*</td>
<td>31.9</td>
<td>35.2</td>
<td>31.1</td>
</tr>
<tr>
<td>National budget deficit (-) / surplus (+) (% of GDP)*</td>
<td>-4.7</td>
<td>-6.6</td>
<td>5.4</td>
</tr>
<tr>
<td>Export of products and services (% of GDP)</td>
<td>57.4</td>
<td>49.4</td>
<td>49.6</td>
</tr>
<tr>
<td>Import of products and services (% of GDP)</td>
<td>85.4</td>
<td>100.5</td>
<td>96.2</td>
</tr>
<tr>
<td>Migrants cash remittances (% of GDP)</td>
<td>29.7</td>
<td>31.8</td>
<td>32.3</td>
</tr>
<tr>
<td>Current account transactions</td>
<td>-8.1</td>
<td>-21.8</td>
<td>-22.8</td>
</tr>
<tr>
<td>Reserves in months of future imports (% GDP)</td>
<td>3.4</td>
<td>3.5</td>
<td>3.5</td>
</tr>
<tr>
<td>External debt (USD million)</td>
<td>5.260</td>
<td>5.990</td>
<td>6.155</td>
</tr>
<tr>
<td>External debt (% of GDP)*</td>
<td>80.0</td>
<td>82.0</td>
<td>82.5</td>
</tr>
<tr>
<td>Sovereign debt, US$ million</td>
<td>2,577</td>
<td>3,002</td>
<td>3,060</td>
</tr>
<tr>
<td>Sovereign debt (% of GDP)*</td>
<td>47.5</td>
<td>47.9</td>
<td>48.7</td>
</tr>
<tr>
<td>Sovereign debt service burden to exports of goods and services</td>
<td>2.8</td>
<td>3.0</td>
<td>3.2</td>
</tr>
<tr>
<td>Money base (KGS million)</td>
<td>54,803</td>
<td>64,489</td>
<td>63,699</td>
</tr>
<tr>
<td>Money supply in national currency M2 (KGS million)</td>
<td>62,125</td>
<td>77,461</td>
<td>76,465</td>
</tr>
<tr>
<td>Velocity of money circulation on M2, times</td>
<td>5.11</td>
<td>4.52</td>
<td>4.36</td>
</tr>
<tr>
<td>Rate of discount of NB of KR, % per annum</td>
<td>13.61</td>
<td>2.64</td>
<td>2.98</td>
</tr>
<tr>
<td>Lending interest rate, end of period, % per annum</td>
<td>19.86</td>
<td>19.90</td>
<td>19.54</td>
</tr>
<tr>
<td>KGS/US$ exchange rate, end of period (KGS = US$ 1)</td>
<td>46.48</td>
<td>47.40</td>
<td>47.96</td>
</tr>
<tr>
<td>Real effective exchange rate of KGS, compared with December of previous year, %</td>
<td>1.14</td>
<td>0.07</td>
<td>-0.70</td>
</tr>
</tbody>
</table>

* - Data for 2013 estimated by ACF