

**MANAGEMENT RESPONSE TO THE PROJECT PERFORMANCE AUDIT REPORT
ON THE SECOND INDUSTRIAL ENERGY EFFICIENCY AND ENVIRONMENT
IMPROVEMENT PROJECT IN PEOPLE'S REPUBLIC OF CHINA
(Loan 1436-PRC)**

On 9 August 2005, the Director General, Operations Evaluation Department, received the following response from the Managing Director General on behalf of Management:

1. Management finds the report well prepared. The overall project rating is "successful," which is the same as the assessment presented in the Project Completion Report circulated on 17 October 2003. It is also noted that no follow-up action is recommended by OED. However, we would like to offer the following specific comments.
2. The key issues for the future, as described in the report, are (i) PRC's high energy intensity and (ii) the need for ADB to contribute to the country's pursuit of building an energy efficient economy. The report also suggests that ADB needs to increase its involvement in the improvement of energy efficiency in industries. Management recognizes the importance of reducing the energy intensity of PRC's economy. ADB's Regional and Sustainable Development Department has launched an energy efficiency initiative, wherein an interdepartmental steering committee and a task force have been established to do a study and prepare a medium-term action plan to increase ADB's interventions related to energy efficiency in the DMCs. Further, East and Central Asia Department is also preparing an advisory TA that will examine ways to overcome the barriers and provide the opportunity to prepare an investment project for energy conservation and resource management in PRC. To increase ADB's involvement in the improvement of energy efficiency in industries poses a challenge because the private sector accounts for over a third of the economy.
3. The PPAR has pointed out the importance of timely and effective monitoring of project progress reports and financial statements. Monitoring and evaluation of industrial subprojects present a special challenge because they function in a competitive environment, which require their management to follow a shorter planning horizon and face considerable volatility in prices of resources, raw materials, and products. To a certain extent, these factors have guided the current ADB operational strategy of requiring industrial units to seek commercial financing. However, considering the importance of energy conservation, discussions are proceeding with the Government of PRC to find ways to extend support to all energy consumers. When such projects are prepared, suitable monitoring and evaluation framework will also be prepared.