

**MANAGEMENT RESPONSE ON THE PROJECT PERFORMANCE AUDIT REPORT
ON THE TANGSHAN AND CHENGDE ENVIRONMENTAL IMPROVEMENT PROJECT
IN PEOPLE'S REPUBLIC OF CHINA (Loan 1270-PRC)**

On 7 February 2005, the Director General, Operations Evaluation Department, received the following response from the Managing Director General on behalf of Management:

1. Management and staff have reviewed the Project Performance Audit Report (PPAR) for Loan 1270-PRC: Tangshan and Chengde Environmental Improvement Project (the Project), and would like to provide the following comments.

2. The Project included seven components of varying scope and thereby different costs and benefits. The Project Completion Report (PCR) circulated on 9 October 2002, rated the project as "successful".¹ OED reviewed the PCR and validated the methodology used, and the rating. The PPAR has now adopted a different methodology and rated the Project as partly successful.

3. Due to the multi-component feature of the Project, the PPAR has identified the limitation of applying the current "*Guidelines for the Preparation of Project Performance Audit Report*" to determine the overall project rating, and explained the new approach that it used. However, the new approach does not provide a direct link between the ratings of individual components and that of the overall project. In our view, the overall Project rating in the PPAR is conservative, because it does not take into account the overall weighted average (OWA), or the overall EIRR and FIRR.

4. A lack of clarity regarding the methodology for determining overall rating in multi-component projects will lead to inconsistencies in project evaluation. We suggest that OED augment the guidelines for evaluating multi-component projects.

5. We have taken note of the key lessons and follow-up actions stated in the PPAR and will take them into account for the design of similar future ADB projects, as outlined below:

- (i) The low rating of some subprojects highlights the importance of (a) more rigorous analysis of assumptions in the case of linked subprojects, and (b) technical recommendations of consultants being verified by in-house experts, and where in-house capacity is lacking, avoidance of investments in such subprojects.
- (ii) The PPAR supports the current operational strategy in PRC that focuses on achieving public goods through public utilities and staying away from supporting industrial projects. Similarly,

¹ "With the achievement of the main objective of air improvement despite the about 1.3% increase in the city population in the last 10 years and an annual economic growth rate of about 10% per annum, the Project is rated as successful."

integrating subprojects in selected cities will enhance the impact of environmental improvement projects.

- (iii) Choice of appropriate technologies is considered important, particularly because of the rapid technological developments in environmental engineering and cleaner production. Further, sustainability of subprojects and environmental benefits must be given equal emphasis.
- (iv) Staff review of project implementation has been strengthened to help identify potential contractual problems and seek alternate solutions for successfully commissioning equipment.