



Completion Report

Project Number: 42376-012
Technical Assistance Number: 7150
June 2019

Azerbaijan: Railways Sector Development Program

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TA Number, Country, and Name:		Amount Approved: \$1,000,000.00	
TA 7150-AZE: Railways Sector Development Program		Revised Amount: Not applicable	
Executing Agency: Ministry of Transport	Source of Funding: TASF-Others	Amount Undisbursed: \$540,656.10	Amount Utilized: \$459,343.90
TA Approval Date: 17 Oct 2008	TA Signing Date: 11 Nov 2008	Fielding of First Consultants: 24 Apr 2008	TA Completion Date Original: 31 May 2009 Actual: 16 Jul 2010 Account Closing Date Original: 31 May 2009 Actual: 16 Jul 2010
<p>Description</p> <p>Rail transport in Azerbaijan is a major transport mode for transit services for oil and oil products, particularly for spilled-over traffic from the pipeline and for export of goods from Azerbaijan for long-haul traffics. While most crude oil from the Caspian Sea will continue to use the pipeline as primary mode of transportation, the railway across the Caucasus will remain an important alternative transport mode for shippers.</p> <p>Recognizing ADB's experience in the railway sector and the innovative financing modality, the government requested for ADB's assistance to complement and supplement other aid agencies' ongoing efforts to upgrade the railway sector in the country, and ultimately help the government implement the program comprising of physical investment and institutional reforms for the railway sector. This project preparation technical assistance (TA) was prepared to develop a railway investment program for Azerbaijan to be supported through a multitranche financing facility (MFF).</p> <p>Expected Impact, Outcome, and Outputs</p> <p>The expected impact of the ensuing loan project was enhanced railway transport services in Azerbaijan in support of the country's economic and social development as well as increased regional trade. The outcome was efficient railway system operating in Azerbaijan. The TA outputs were: (1) proposed MFF including policy framework, safeguards framework, investment plan, and financing plan and related information such as sector roadmap and strategy context; and (2) feasibility study and related due diligence for technical, commercial, financial, social safeguards, institutional effectiveness, governance, financial management system and project management aspects and preliminary/detailed design for the components of tranche 1 project.</p> <p>Delivery of Inputs and Conduct of Activities</p> <p>The terms of reference (TOR) was adequate and relevant to deliver the TA outputs. The number of experts, required experience and competence were also appropriate. Consultant recruitment started by end of 2008. Evaluation and shortlisting took longer time than planned due to delays in submission of proposals to the reviewing team. The TOR was implemented by a firm, Corporate Solutions Consulting Inc., that was competitively selected using quality-cost based selection method (80:20) with simplified technical proposal.</p> <p>The TA activities were implemented in two phases, in accordance with the planned TA Outputs. The closing date was extended twice: (1) from 31 May 2009 to 31 December 2009 to sufficiently cover the intended work period envisioned in the TOR since the consultant's contract was awarded on 24 April 2009, and (2) 30 April 2010 to accommodate the government delay in determining the scope of the MFF and its first tranche.</p> <p>Four contract variations were processed: (1) increase in translation budget by \$12,000 (approved on 31 May 2009); (2) increase in inputs of two experts and replacement of another two experts, with an effective contract cost increase by \$24,000 (approved on 7 September 2009); (3) termination of the contract effective 13 February 2010 following joint government and ADB decision to discontinue the project preparation work (approved on 13 April 2010); and (4) final contract variation following submission of the Final Statement of Eligible Costs (approved on 23 April 2010).</p> <p>ADB review missions were conducted monthly from April to July 2009 to intensively monitor the work of consultants and facilitate discussion with government. In September 2009, the expected government decision on the scope of the MFF program did not materialize; hence, two review missions were fielded in October 2009 and January 2010 to follow through the pending government actions.</p> <p>Evaluation of Outputs and Achievement of Outcome</p> <p>The first phase of the TA was completed and the first Output was delivered. The consulting firm finished two reports (Inception and Interim reports) and were deemed acceptable. Both reports presented the proposed scope of the MFF program and proposed scope for the first tranche. Twelve (12) candidate projects for the MFF were identified through the consultant's discussions with the Ministry of Transport (MOT) and the Azerbaijan State Railway agency (ADDY) and their research and inspection works. It was agreed that the rehabilitation of the 200 track-kilometers on the East-</p>			

West line, replacement of two bridges over the Kura River and purchase of rehabilitation and maintenance machinery shall be the appropriate scope of the first tranche, with an estimated cost of \$210 million.

A preliminary sector analysis made by the consultant highlights the fundamental shift of the Azeri rail transport environment. The analysis provided valuable information: (i) requirements for rail service quality have tightened considerably, (ii) petroleum products terminal at Batumi Port transformed from an inefficiently operated government-owned facility into a modern commercial operation that relies on efficient and predictable wagon delivery cycles to maximize capacity, and (iii) non-petroleum facilities (including container transfer) in Poti Port have improved significantly that demands efficient rail service.

Major problems were identified in addressing the shifted needs: (i) weak institutional capacity, (ii) poor railway infrastructure and operating equipment, and (iii) problems with international connections (only 25% of the traffic is domestic). ADB's intervention through the MFF can address these concerns particularly the infrastructure issue. With keen attention to designing the program, capacity development initiatives can be strategically added as investment components especially the activities that will improve institutional capabilities in repair and maintenance techniques for the facilities.

However, in January 2010, the government informed that the first phase of the rail rehabilitation project already completed its financing arrangement with the World Bank and other bilateral donor agencies; and there was no longer need for ADB financing. The government's investment program for railway sector development was also considerably scaled down and eventually disapproved due to declining oil revenue and the country's economic slowdown. As such, the second phase of TA implementation had to be stopped. Project preparation work undertaken by the consulting firm was to be discontinued, the contract to be terminated and the TA to be closed by end of February 2010. Therefore, the second Output cannot be achieved.

Overall Assessment and Rating

The design of the TA was highly relevant; the sector analysis provided valuable assessment of recent developments and established the need for sector interventions. The completed first Output presented the investment options for government's consideration in making a decision for MFF financing. However, TA implementation was stopped because of the change in Government's decision not to pursue ADB financing for railway sector development in Azerbaijan as triggered by the country's economic slowdown. The TA did not progress into the ensuing MFF program as planned. Considering this, the TA was partly successful.

Major Lessons

In 2007 the government selected the World Bank (WB) as a partner of choice in developing the first investment project (East-West railway corridor). These reasons: (i) WB has wider sources of procurement, and (ii) from Czech Eximbank to procure rails for the entire East-West line were major factors for such a decision. Subsequently, by the start of this TA implementation in April 2009, the government had already secured a sufficient external funding, and main focus was shifted to the actual implementation of the East-West railway corridor project with available funds. During the TA processing stage, the Ministry of Finance (MOF) should have been consulted as the key stakeholder in charge of the sovereign borrowing. Not involving MOF during the TA processing stage proved to be a critical omission. Under the first phase of the ADB's stronger and deeper in-country sector analysis and expertise could help to stay engaged with the government and corporate. However, the second phase of TA wasn't materialized as planned. Due to significant reduction of the Government's revenue base during 2008-2009 and serious corporate governance issues in the railway sector, MOF took extremely cautious approach to any new external borrowing in the sector and advised ADB of no scope for the proposed new ADB lending shortly after the start of TA implementation. The analysis made under this TA provided a scope to continue the dialogue with government in exploring financing possibilities in the railway sector in Azerbaijan via various ADB lending modalities. The work undertaken by the TA helped to tailor a sector development program (SDP) into the needs of the railway sector especially in addressing weak institutional capacities. It is the attractiveness of ADB financing package that encouraged government to favorably consider ADB as key investment player and financing partner in railway sector development. This led to the development of the Railway SDP that was approved on 6 December 2017.

The learned lessons helped ADB to undertake broader consultations and avoid omissions made by other IFIs in designing and implementing their projects in the railway sector. Since then ADB has managed to gradually build much stronger relations with the clients. Eventually, the lessons learned resulted with ADB's defined creative innovations to enter in the railway sector in Azerbaijan with a sizable ADB operation.

Azerbaijan government's borrowing ceiling significantly limits possibilities for the new sovereign loan approvals, which negatively affects ADB and other multilateral and bilateral financing institutions operating in the country. The economic downturn diminished the possibility for ADB to enter the investment environment for the railway sector. Forging

stronger business relations with the government and deepening the country analysis can help define creative innovations to sustain and expand ADB operations in Azerbaijan, especially in the railway sector.

Recommendations and Follow-Up Actions

The analysis made under this TA provided scope to continue the dialogue with government in exploring financing possibilities in the railway sector in Azerbaijan. The follow-on analysis shall be to study the fit of various ADB lending modalities into the needs of the railway sector especially in addressing weak institutional capacities. It is the attractiveness of ADB financing package that will encourage government to favorably consider ADB as key investment player and financing partner in railway sector development in Azerbaijan.

ADB used its knowledge and lessons learned under this TA to develop a new transaction technical assistance project that developed ADB's first investment in Azerbaijan's railway sector. The approval of two loans in December 2017 totaling \$400 million for the Railway Sector Development Program (SDP) proved ADB's credibility as a key development partner to support innovations for the railway sector in the country. The SDP was designed with two components: (i) the policy-based loan is needed to take out the railway company from financial distress, while (ii) the project loan will finance the rehabilitation of the 166 km Sumgayit-Yalama rail line, a key link in the North-South Railway Corridor within the Central Asia Regional Economic Cooperation network.

Prepared by: Carmina O. Luna

Designation and Division: Senior Project Officer, CWTC