ADB

Report and Recommendation of the President to the Board of Directors

Project Number: 44483
August 2011

Proposed Multitranche Financing Facility Republic of Uzbekistan: Second Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program

Asian Development Bank

CURRENCY EQUIVALENTS
(as of 26 July 2011)

Currency Unit	–	sum (SUM)
SUM1.00	=	$0.00058
$1.00	=	SUM1,722.20

ABBREVIATIONS

ADB	–	Asian Development Bank
CAREC	–	Central Asia Regional Economic Cooperation
EIRR	–	economic internal rate of return
FAM	–	facility administration manual
km	–	Kilometer
MFF	–	multitranche financing facility
MOF	–	Ministry of Finance
PMU	–	program management unit
PRC	–	People's Republic of China
RRF	–	Republican Road Fund

GLOSSARY

CAREC Transport Corridor 2	–	Southern Europe–the People's Republic of China International Transit Corridor with a section in Uzbekistan from Alyat at the border with Turkmenistan and Karakalpakya (Daut Ata) at the border with Kazakhstan, running through Bukhara, Navoi, and Tashkent, to the eastern border with the Kyrgyz Republic at Andjan (Karasu)
oblast	–	an administrative unit in Uzbekistan

NOTE

In this report, "$" refers to US dollars.

Vice-President	X. Zhao, Operations 1
Director General	J. Miranda, Central and West Asia Department (CWRD)
Director	H. Wang, Transport and Communications Division, CWRD
Team leader	S. Khan, Principal Portfolio Management Specialist, CWRD
Team members	N. Bustamante, Senior Operations Assistant, CWRD
	M. Khudayberdiyeva, Senior Social Development Officer (Gender), CWRD
	R. Nadyrshin, Portfolio Management Officer, CWRD
	K. Nam, Economist, Economics and Research Department
	L. Nazarbekova, Senior Counsel, Office of the General Counsel
	S. Roth, Social Development Specialist (Gender and Development), CWRD
	D. Utami, Principal Safeguards Specialist, CWRD
Peer reviewer	J. Miller, Principal Transport Specialist, Southeast Asia Department

CONTENTS

PROJECT AT A GLANCE

1. Project Name: MFF - Second CAREC Corridor 2 Road Investment Program

2. Project Number: 44483-024

3. Country: Uzbekistan

4. Department/Division: Central and West Asia Department/Transport and Communications Division

5. Sector Classification:

Sectors	Primary	Subsectors
Transport, and information and communication technology	√	Road transport

6. Thematic Classification:

Themes	Primary	Subthemes
Economic growth		Widening access to markets and economic opportunities
Regional cooperation and integration	√	Trade and investments
Capacity development		Institutional development

6a. Climate Change Impact

No Climate Change Indicator available.

6b. Gender Mainstreaming

Gender equity theme (GEN)	
Effective gender mainstreaming (EGM)	√
Some gender benefits (SGB)	
No gender elements (NGE)	

7. Targeting Classification:

General Intervention	Targeted Intervention		
	Geographic dimensions of inclusive growth	Millennium development goals	Income poverty at household level
√			

8. Location Impact:

National	High
Regional	High
Rural	Low
Urban	Low

9. Project Risk Categorization: Complex

10. Safeguards Categorization:

No Safeguards Categorization available.

11. ADB Financing:

Sovereign/Nonsovereign	Modality	Source	Amount ($ Million)
Sovereign	MFF-Facility (Loan)	Asian Development Fund	up to 180.0
Sovereign	MFF-Facility (Loan)	Ordinary capital resources	320.0
Total			500.0

12. Cofinancing:

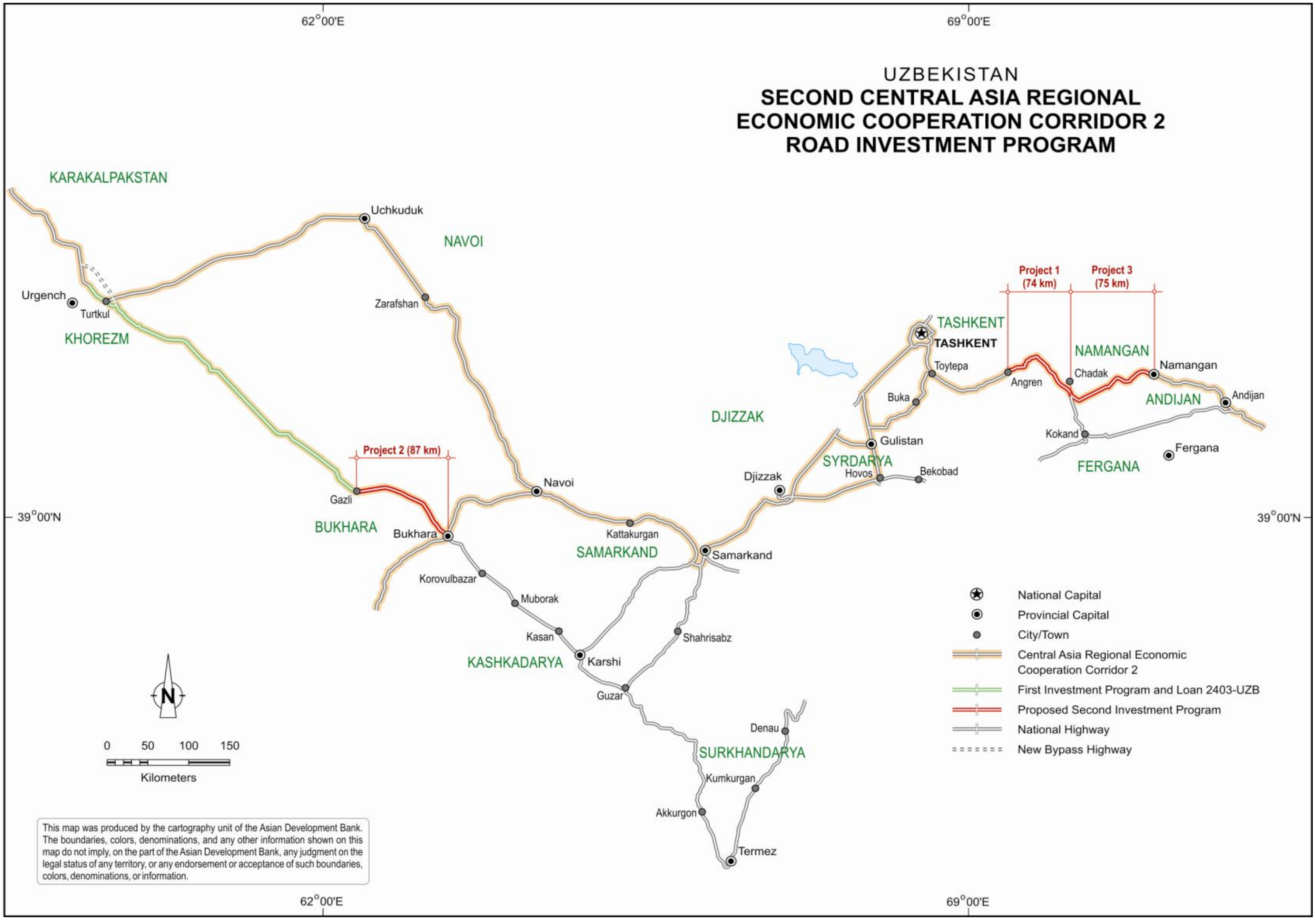
No Cofinancing available.

13. Counterpart Financing:

Source	Amount ($ Million)
Government	100.0
Total	100.0

14. Aid Effectiveness:

Parallel project implementation unit	No
Program-based approach	No



UZBEKISTAN
SECOND CENTRAL ASIA REGIONAL ECONOMIC COOPERATION CORRIDOR 2 ROAD INVESTMENT PROGRAM
62°00'E
69°00'E
39°00'N
KARAKALPAKSTAN
KHOREZM
NAVOI
BUKHARA
SAMARKAND
KASHKADARYA
SURKHANDARYA
DJIZZAK
SYRDARYA
TASHKENT
NAMANGAN
ANDIJAN
FERGANA
Urgench
Turtkul
Uchkuduk
Zarafshan
Navoi
Gazli
Bukhara
Korovulbazar
Muborak
Kasan
Karshi
Guzar
Kattakurgan
Samarkand
Shahrisabz
Denau
Kumkurgan
Akkurgon
Termez
Djizzak
Gulistan
Hovos
Bekobad
Buka
Toytepa
TASHKENT
Angren
Chadak
Namangan
Andijan
Kokand
Fergana
Project 1 (74 km)
Project 2 (87 km)
Project 3 (75 km)
National Capital
Provincial Capital
City/Town
Central Asia Regional Economic Cooperation Corridor 2
First Investment Program and Loan 2403-UZB
Proposed Second Investment Program
National Highway
New Bypass Highway
N
0 50 100 150
Kilometers
This map was produced by the cartography unit of the Asian Development Bank. The boundaries, colors, denominations, and any other information shown on this map do not imply, on the part of the Asian Development Bank, any judgment on the legal status of any territory, or any endorsement or acceptance of such boundaries, colors, denominations, or information.

11-2178 HR

I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed multitranche financing facility (MFF) to the Republic of Uzbekistan for the Second Central Asia Regional Economic Cooperation (CAREC) Corridor 2 Road Investment Program.[1]

II. THE INVESTMENT PROGRAM

A. Rationale

2. Uzbekistan is a key transit country for trade in Central Asia as well as between Central Asia and the rest of Asia and Europe. Transport is crucial in promoting regional and domestic trade.[2] The second investment program[3] will finance the reconstruction of the Uzbekistan section of CAREC Corridor 2, which connects Uzbekistan to Afghanistan, Kazakhstan, the Kyrgyz Republic, Tajikistan, and Turkmenistan. This reconstruction will improve connectivity and road safety, and boost domestic and international trade. The second investment program fits with Strategy 2020[4] of the Asian Development Bank (ADB), is included in the country operations business plan (2011–2013), and is aligned with the United Nations Decade of Action for Road Safety 2011–2020.[5] The proposal is in line with the proposed Uzbekistan Transport Sector Strategy (2006–2020)[6] and road map, as well as the CAREC Transport and Trade Facilitation Strategy and Action Plan (footnote 2).

3. **Regional context**. CAREC Corridor 2 connects the Caucasus and Mediterranean to East Asia. The route covers Azerbaijan, Kazakhstan, the Kyrgyz Republic, Tajikistan, Turkmenistan, Uzbekistan, and the People's Republic of China (PRC). With the rapid economic expansion of the PRC to the east, the Russian Federation and Kazakhstan to the north, and Azerbaijan to the west, Uzbekistan has an unprecedented opportunity to emerge as a center for trade and commerce and to achieve rapid economic growth.

4. The Uzbekistan sections of CAREC Corridor 2 comprise the A373, A373/4R112, and A380 highways. The 404-kilometer (km) A373 from Tashkent to Osh in the Kyrgyz Republic is the only link between Fergana valley and the rest of the country, and is an important road transport link between the PRC and Central and West Asia. The A373/4R112 extends the A373 from Kamchik to Namangan. Fergana valley, with a third of the country's population, exports fertilizer, cotton yarn and textile, chemical products, fruits, and vegetables. To increase domestic and international trade and accommodate heavy traffic, these highways will need to be reconstructed and expanded. In June 2010 the government passed resolution 126[7] to reconstruct the A373. The 1,204 km A380 primarily carries fuel, agricultural commodities, and industrial consumer goods. Another ongoing highway investment in Kazakhstan (supported by

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[1] The design and monitoring framework is in Appendix 1.

[2] ADB. 2008. *CAREC Transport and Trade Facilitation Strategy and Action Plan*. Manila.

[3] The second investment program is an extension of the ongoing investment program (ADB. 2010. *Report and Recommendation of the President to the Board of Directors: Proposed Multitranche Financing Facility to the Republic of Uzbekistan for the Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program.* Manila).

[4] ADB. 2008. *Strategy 2020: The Long-Term Strategic Framework of the Asian Development Bank, 2008–2020*. Manila.

[5] United Nations. 2011. *Decade of Action for Road Safety 2011–2020.* New York.

[6] ADB. 2006. *Technical Assistance to the Republic of Uzbekistan for Transport Sector Strategy (2006–2020).* Manila. (TA 4659-UZB, consultant's final report).

[7] Republic of Uzbekistan. 2010. *Resolution No. 126 of the Cabinet of Ministers, Additional measure to ensure sustainable transport communication via mountain pass Kamchik.* Tashkent (26 June).

ADB)[8] will connect Beyneu (a town on Uzbekistan's border) with Uzbekistan's A380 and the port of Aktau on the Caspian Sea. All these highways, when completed, will provide Uzbekistan and other Central Asian countries with direct access to the Caspian Sea, South Asia, and the Black Sea (via road corridors being built in Armenia, Azerbaijan, and Georgia). The second investment program links with CAREC Corridor 6, which reaches the ring road in Afghanistan and Pakistan's main ports.

5. **Overview of roads**. The country has more than 183,000 km of roads; 42,530 km of these are highways. Roads are classified as international (3,626 km), regional (21,995 km), and national (16,909 km). While the road network is adequate, providing access throughout the country, it has a backlog of road rehabilitation work. The existing road map prioritizes the A380 and the A373.

6. In 2010, roads accounted for 32% of Uzbekistan's freight by ton-km and 88% of its passengers by passenger-km. More vehicles and private road-hauling companies, and shorter transport hauls of manufactured goods have increased road freight. This market share growth is likely to continue, especially for general cargo. With the country's high rates of economic growth, vehicle fleets are projected to double every 5 years. This growth needs to be sustainable, effective, and cost-efficient, and requires improved road safety.

7. **Road funding and sustainability**. Uzbekistan spends 1% of its gross domestic product on roads. While low by international standards, this has been gradually increasing.[9] The goal is to bring funding to international levels or higher. The Republican Road Fund (RRF) was established under the Ministry of Finance (MOF) for this purpose, particularly to deal with capital investment in, and maintenance of, common-use roads.[10] The fund is responsible for up to 25% of all financing of all networks. Although RRF income increased by about 23% annually in the last 5 years, investment needs are higher. Alternative financing sources must be tapped, and partnerships established with the private sector. Road-user charges must be introduced.

8. The government prepared the Accelerated Development Program (2011–2015)[11] by updating the National Road Development Program (2010–2014). Investments mainly involve reconstruction of existing networks, although some greenfield projects are envisaged. Other "softer" infrastructure investments are part of the plan, including improving institutional effectiveness, planning, project management, and road safety. Uzbekistan has a policy framework for roads that supports good governance and accountability, improved road sustainability, seamless transport logistics, greater private sector investment, and sound road maintenance. Since 2003, the government has pursued several policy and sector reforms, including (i) separating road transport operations from road construction, (ii) creating RRF as a quasi-independent body, (iii) promoting competitive bidding for all road construction works, and (iv) establishing an external quality control mechanism. The government has also restructured Uzavtoyul (the sole nationwide road agency), converting it to a state joint stock company with

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8 ADB. 2010. *Report and Recommendation of the President to the Board of Directors: Proposed Multitranche Financing Facility to the Republic of Kazakhstan for the Central Asia Regional Economic Cooperation Corridor 2 (Mangystau Oblast Sections) Investment Program.* Manila.

9 The estimate of 1% is based on the average expenditure per km for the network under the purview of the Republican Road Fund. The corresponding expenditures are 2.5% in Viet Nam (2008); 2.3% in the PRC (2006); 1.8% in Thailand (2006); and below 1.0% in the Philippines (2008), lower than the share of Uzbekistan.

10 RRF, established in 2003, is a quasi-independent agency under the auspices of MOF and responsible for programming, planning, and budgeting of common-use roads comprising international, national, and local roads.

11 Resolution of the President of the Republic of Uzbekistan No 1446 on Accelerated Development of Infrastructure, and Construction in Transport and Communications (2011–2015). Tashkent (21 December 2010).

clear performance and accountability targets.[12] The government is now considering separating several road construction companies from the Uzavtoyul structure to a more commercial ownership structure. A law on roads for vehicular traffic enacted in 2007 allows the private sector to finance highway construction. A state-owned road equipment pool company created under the ADB loan for the CAREC Regional Road Project[13] services all contractors. The second investment program will contribute to Uzbekistan's Accelerated Development Program and policy framework for roads.

9. **Financing modality**. An MFF is proposed to finance the second investment program. This follows the recommendations from past operations to engage with the government over a longer time horizon, and allows ADB to enter into a partnership with the government.[14] All the prerequisites for the use of an MFF are in place—a coherent strategy and sector road map, a policy framework, an investment plan, and a financing plan. The MFF modality will allow the government (i) a greater degree of certainty on the financing plan, and (ii) to borrow according to project readiness. The MFF will also contribute to establishing a long-term partnership between ADB and Uzbekistan.

10. **Lessons**. Implementation of the ongoing ADB-assisted investment program is on track. With advance contracting, physical execution commenced on time and is proceeding smoothly. Implementation of the sector road map and policy framework is also on track in line with the government's Accelerated Development Program. Implementation is smooth because (i) the program is among the government's high priorities, and so government commitment is high; it is consistently monitoring physical and nonphysical outputs; and (ii) the executing agency is strong and capable. The program management unit (PMU) has become a source of knowledge and advice for project units of other ADB-financed projects in Uzbekistan. The lessons of the first investment program are that project design should be needs-based and be among the government's highest priorities, and that a strong PMU can lay the foundation for projects and systematically take advance procurement actions. The second investment program incorporates these lessons. The PMU is in place, the detailed design for the first project is complete, and advance procurement contracting has resulted in the timely start of the tendering process and recruitment of consultants. An aid coordination group has been constituted at ADB's initiative to ensure coordinated assistance for integrated transport sector development and focused institutional capacity development for optimum and sustained development impacts.

B. Impact and Outcome

11. The second investment program will increase domestic and international trade. The outcome will be improved road connectivity, safety, and effective management of the Uzbekistan section of CAREC Corridor 2.

C. Outputs

12. The outputs will be (i) about 236 km of the reconstructed road section of CAREC Corridor 2; and (ii) implemented road system sustainability plans, which relate to road safety and asset management. The investment program will finance three separate projects. The outputs under each project will be as follows.

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[12] Decree of the President of the Republic of Uzbekistan UP-3292 on improvement of the management system for construction and operation of common-use roads (19 August 2003).

[13] ADB. 2007. *Report and Recommendation of the President to the Board of Directors: Proposed Loan to the Republic of Uzbekistan for the CAREC Regional Road Project.* Manila (Loan 2403-UZB, approved on 19 December, for $75.3 million).

[14] ADB. 2009. *Project Completion Report: Road Rehabilitation Project in Uzbekistan*. Manila.

13. **Project 1.** Outputs are categorized under the following:

(i) **Road development**. The output will be about 74 km of the reconstructed road section of the A373 (between Km 116 and Km 190). The investment will upgrade the existing four-lane section with an international design within the existing right-of-way. The cost includes civil works and specialized consulting services, including experts to help with construction supervision and due diligence for, and preparation of, subsequent tranches.

(ii) **Road system sustainability**. The output will be improved road safety management, including (a) a developed national road infrastructure safety strategy and road safety checklist, guidelines, and measures improving road safety management; (b) a developed road safety action plan for all road sections under the first and second investment programs; (c) installed solar road signs for the A373 Kamchik Pass section; and (d) a developed and implemented road safety capacity development program for RRF and Uzavtoyul; and public awareness programs.

14. **Project 2**. The outputs will be the reconstructed section of about 87 km of the A380 highway (between Km 228 and Km 315), strengthened capacity of RRF to manage road assets, the piloting of the introduction of road-user charges on the reconstructed road section of project 1, and implementation of a road safety action plan for projects 1 and 2 of the second investment program.

15. **Project 3**. The outputs will be the reconstructed section of about 75 km of the A373/4R112 highway (between Km 0 and Km 75), updated road asset management plans, and an implemented road safety action plan. Improvement of cross-border facilities to shorten the processing time at Osh at the Kyrgyz Republic border is covered under the Japan Bank for International Cooperation funding.

D. Investment and Financing Plans

16. The second investment program is estimated to cost $600 million equivalent (Table 1).

Table 1: Investment Program
($ million)

	Projects[a]			
Item	**1**	**2**	**3**	**Total**
A. Base Cost				
1. Road development component	110.4	154.3	163.2	427.9
2. Road sustainability component	2.3	3.2	2.0	7.5
3. Recurrent costs[b]	0.3	0.4	0.4	1.1
4. Taxes and duties	25.8	38.0	24.9	88.7
Subtotal (A)	**138.8**	**195.9**	**190.5**	**525.2**
B. Physical and price contingencies[c]	**17.0**	**22.1**	**24.4**	**63.5**
C. Financing charges during implementation[d]	**4.2**	**2.0**	**5.1**	**11.3**
Total (A+B+C)	**160.0**	**220.0**	**220.0**	**600.0**

[a] In end of 2010 prices. Amounts for tranche 2 and 3 projects are based on preliminary estimates.
[b] Program management unit expenses related to the investment program, including program management unit staff salary, operating expenses, travel, training, and other eligible expenditures.
[c] Physical contingencies are estimated at about 10% of the total base cost. Price contingencies estimated at about 5% include provision for potential exchange rate fluctuation under the assumption of a purchasing power parity exchange rate.
[d] Includes interest and commitment charges as appropriate.
Source: Asian Development Bank estimates.

17. The government has requested an MFF in an amount up to $500 million, comprising loans from ADB's ordinary capital resources (OCR) and Special Funds resources (ADF) to help finance part of the second investment program. The MFF will consist of approximately 3 tranches, subject to the government's submission of related periodic financing requests, execution of the related loan agreements for each tranche, and fulfillment of terms and conditions and undertakings set forth in the framework financing agreement. The government has also requested ADB to consider providing an amount up to $180 million equivalent from its Special Funds resources for the second tranche under the MFF. Any such ADF financing will be accompanied by a corresponding reduction in the OCR financing available, so that in any event the total available amount under the MFF will not exceed $500 million equivalent. This will be subject to (i) the general availability of ADF resources, (ii) Uzbekistan's access to such resources pursuant to ADB's Graduation Policy and the requirements of the ADF donors, and (iii) the availability of such resources to Uzbekistan pursuant to ADB's Policy on Performance Based allocation for ADF Resources. In other words, depending on the availability of ADF resources for Uzbekistan, the second tranche may comprise of OCR and ADF financing.

18. For project 1, the government has requested financing of $130 million equivalent from ADB's ordinary capital resources and will submit the periodic financing request to ADB. The government will provide counterpart financing of $30 million equivalent for the balance of the cost, including for the financing of local taxes and duties. The first tranche of the MFF will have a 24-year term, including a grace period of 4 years, an annual interest rate determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility, a commitment charge of 0.15% per year (the interest and other charges during construction will not be capitalized in the loan), and such other terms and conditions set forth in the draft loan agreement. Table 2 summarizes the financing plan for the investment program and the expected three tranches.

Table 2: Summary Financing Plan—Investment Program
($ million)

Source	Tranche 1	Tranche 2	Tranche 3	Total
ADB[a]	130	180	190	500
Government	30	40	30	100
Total	**160**	**220**	**220**	**600**

ADB = Asian Development Bank.
[a] Source of ADB financing: tranches 1 and 3—ordinary capital resources, and tranche 2—Special Funds resources.
Source: Asian Development Bank estimates.

Table 3: Summary Financing Plan—Project 1[a]
($ million)

Item	ADB	Government	Total
Road Development			
Civil works	107.4	0.0	107.4
Consulting services	3.0	0.0	3.0
Road Sustainability			
Road safety equipment	0.5	0.0	0.5
Road safety consultancy services	1.8	0.0	1.8
Recurrent costs[b]	0.3	0.0	0.3
Taxes and duties	0.0	25.8	25.8
Total Base Cost	**113.0**	**25.8**	**138.8**
Physical and price contingencies[c]	17.0	0.0	17.0
Financing charges during implementation[d]	0.0	4.2	4.2
Total	**130.0**	**30.0**	**160.0**

ADB = Asian Development Bank.
[a] In end of 2010 prices.
[b] Program management unit expenses related to the investment program, including program management unit staff salary, operating expenses, travel, training, and other eligible expenditures.
[c] Physical contingencies are estimated at about 10% of the total base cost. Price contingencies estimated at about 5% include provision for potential exchange rate fluctuation under the assumption of a purchasing power parity exchange rate.
[d] Includes interest and commitment charges.
Source: Asian Development Bank estimates.

19. ADB will consider financing subsequent tranches if the government adheres to the general agreement for the MFF as set forth in the framework financing agreement, which includes undertakings for the MFF. The government should also comply with specific assurances for project 1. Progress in achieving the outputs and expected outcomes in the design and monitoring frameworks for the investment program and project 1 will also be decision-making criteria for financing subsequent tranches under the MFF.

E. Implementation Arrangements

1. Management

20. RRF will be the executing agency. It has established a PMU and appointed a director and a team of nine professional and support staff to implement the first investment program and to undertake advance contracting for tranche 1 of the second investment program. The PMU is structured with a specific mandate: technical; legal; procurement; monitoring, reporting, and evaluation; safeguards; and gender development. For the second investment program, RRF will add seven more professionals (deputy project director, two road engineers, financial management specialist, results monitoring specialist, procurement specialist, and accountant) to the PMU. The implementation arrangements are summarized in Table 4 and described in detail in the facility administration manual (FAM).[15]

[15] Facility Administration Manual (accessible from the list of linked documents in Appendix 2).

Table 4: Implementation Arrangements

Aspects	Arrangements		
Implementation period	July 2011–September 2017		
Estimated completion date	31 March 2017		
Management			
(i) Oversight body	Ministry of Finance		
(ii) Executing agency	Republican Road Fund		
(iii) Program management unit	Tashkent, 17 staff		
Procurement	ICB	3 contract (works)	$420 million
	ICB	1 contract (goods)	$500,000
Consulting services	QCBS	916 person-months (engineering and construction supervision, capacity development, and road asset management) – 4 contracts	$13 million
	QCBS	98 person-months (road safety)	$1.8 million
Retroactive financing and advance contracting	Yes. Advance contracting for civil works and consulting services, and retroactive financing for the civil works and consulting services for up to 20% of the loan amount, provided that procurement is in line with ADB Procurement Guidelines and expenditures are incurred during the 12 months before the signing of the loan agreement.		
Disbursement	The loan proceeds will be disbursed in accordance with ADB's *Loan Disbursement Handbook* (2007, as amended from time to time) and detailed arrangements agreed to by the government and ADB.		

ADB = Asian Development Bank, ICB = international competitive bidding, QCBS = quality- and cost-based selection.
Source: Asian Development Bank.

21. Project 1 readiness is high. Design work is complete and advance procurement actions have been taken. Bids for the major international competitive bidding civil works contract have been invited and consultant selection is under way.

III. DUE DILIGENCE

A. Technical

22. Due diligence carried out for project 1 includes assessing the investment plan, design features, cost structure for operations, and maintenance requirements. The investment program roads will carry heavy vehicles—from within and outside Uzbekistan. The approach is to reconstruct four-lane existing asphalt concrete and cement concrete road sections of the A373 (project 1), widen the existing two-lane asphalt concrete road sections of the A380 into a four-lane cement concrete road (project 2), and widen the existing two-lane asphalt concrete road sections of the A373/4R112 into a four-lane asphalt concrete road (project 3), following the existing right-of-way.

23. Road traffic is expected to grow by 10% annually to about 108,300 passenger cars daily by 2030 for project 1. The reconstructed and expanded network can accommodate the traffic, including growing intercity traffic, but requires improved road safety measures. Best-practice standards are, therefore, included in the investment program. Detailed design work for the road section under project 1 is complete. The investment program is ready for implementation.

B. Economic

24. The second investment program will benefit Uzbekistan as well as its neighbors. The major benefits are better, safer, cheaper, and faster connectivity; lower transport costs; a developed logistics center; better access to health and education facilities—all of which translate into more investments and jobs. The main beneficiaries include people and local

businesses, farmer communities, manufacturers, traders, neighboring countries, and Uzbekistan communities living along the corridor. The link to Kazakhstan in the west and to the Kyrgyz Republic in the east, and the construction of a road from Beyneu to Andizhan deliver substantial spillover benefits to all countries. The improved corridor will give Uzbekistan and Central Asia direct access to the Caspian Sea on the west and access to the PRC via the Kyrgyz Republic.

25. Project 1 is economically viable, with an economic internal rate of return (EIRR) of 17.3%. The sensitivity of the EIRR to changes in crucial input assumptions was tested. The EIRR exceeds 12% for the variations to all parameters. Even in the worst case, which combines a 20% increase in capital cost and a 20% reduction in traffic, the EIRR would decrease to 13.3%, which is favorable compared with the assumed hurdle rate of 12%.

C. Financial

26. The due diligence work analyzed the financial management aspects and maintenance requirements and capabilities. Current traffic on the road is 10,000 vehicles/day for project 1, 1,200 for project 2, and 9,200 for project 3. The traffic for projects 1, 2, and 3 is not high enough to attract private investors. However, over time, some sections could be handed over to private operators, especially around big cities and industrial zones like Navoi. A public–private partnership framework will be used to access private sector investment. The due diligence work indicates that RRF has sound financial management systems, sound systems and procedures, and clear accountability lines.

27. RRF has resources for road maintenance. The government has been increasing its budget allocation for RRF every year and will continue to do so in line with national tax collections. In 2010, RRF received 32% more than in 2009. The allocation will be inflation-proof. This will help maintain reasonable revenue to help sustain investments. Generally, countries with road funds spend about 0.3% of their income on road maintenance. Uzbekistan falls below this now but intends to do better. Uzavtoyul will maintain the road.

D. Governance

28. A governance assessment undertaken as part of the due diligence process focused on the legal framework, regulation, strength of enforcement regimes, RRF capacity, human resources, and the risk of corruption. Uzbekistan's performance in governance has progressed steadily. The legal frameworks for managing public finances have been tightened. The Budget System Law and Treasury Law, approved on 17 December 2007, provide additional cover and better practices in this area. The public expenditure reform process for 2007–2018 includes measures to increase efficiency, accountability, and transparency.[16]These reforms are tackling public financial management arrangements, particularly with regard to budget execution. The second investment program will be subjected to international competitive bidding to increase oversight and help mitigate corruption.

29. RRF has improved its systems and transparency by including information on its performance, the status of each contract under the investment program, the specific list of business opportunities, and a summary of the bidding process and its guidelines on its webpage and the MOF website. An international procurement specialist has been hired to assist in procuring civil works, goods, and services; and strengthen RRF capacity. An independent auditor will be appointed.

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[16] ADB. 2007. *Report and Recommendation of the President to the Board of Directors: Proposed Loan and Technical Assistance Grant to the Republic of Uzbekistan for the Public Finance Management Reform Project*. Manila (Loan 2338-UZB) will support the establishment of a single treasury account and improvement of the general financial management information system. The technical assistance grant for Supporting Public Finance Management Reform (TA 4946-UZB) reformed the public financial management system.

30. ADB’s Anticorruption Policy (1998, as amended to date) was explained to and discussed with MOF and RRF. The specific policy requirements and supplementary measures are described in the FAM. The content of the policy, how it needs to be applied, and courses of action in case of any infringement are all clear.

E. Poverty and Social

31. The investment program will not directly reduce household poverty or provide specific services that deal with the geographic determinants of poverty. Poverty and social analysis undertaken as part of the due diligence process demonstrates a female–male unemployment ratio of 6.5:2.5. The poverty rate among households headed by women is 1.5 times higher than those headed by men. Although the second investment program is not a targeted intervention, it will reduce gender inequalities and solve other issues by (i) improving access to health care and education, (ii) creating jobs and developing women’s entrepreneurship skills, and (iii) developing roadside infrastructure such as sanitary facilities for men and women travelers and market spaces for women entrepreneurs. Highway construction and the development of long-term transit routes may increase the risk of sexually transmitted infections. The government takes this risk seriously and has agreed to a mitigation plan with ADB. During the execution phase of the investment program, these actions will be reflected in contractors’ contracts, and the gender action plan will be implemented in close cooperation with women’s committees.

F. Safeguards

32. RRF prepared an environmental assessment and review framework for the investment program in accordance with ADB’s Safeguard Policy Statement (2009). The investment program will not have significant irreversible or permanent negative environmental impacts during or after construction. Project 1 does not have major environmental impacts, and is classified under environment category B in line with ADB’s Safeguard Policy Statement. RRF prepared an initial environmental examination for project 1, which includes an environmental management plan. The plan provides measures to minimize and mitigate potential adverse impacts. The environmental assessment and review framework and initial environmental examination were posted on ADB's website on 10 June 2011 and on RRF’s website on 11 June 2011.

33. A land acquisition and resettlement framework and an ethnic minority planning framework were also prepared in accordance with ADB’s Safeguard Policy Statement. These social safeguard documents were disclosed on ADB’s website on 10 June 2011 and on RRF’s website on 11 June 2011. Civil works under project 1 do not involve land acquisition or involuntary resettlement, or affect ethnic minority groups in all forms as described in ADB’s Safeguard Policy Statement. In line with the statement, project 1 is classified as category C for the purposes of social safeguards. RRF will undertake environmental and social due diligence for subsequent tranches according to the agreed frameworks, ADB’s Safeguard Policy Statement, and all relevant laws and regulations in Uzbekistan. The PMU will be supported by a team of environment and social safeguard experts to implement the safeguard requirement for the MFF.

G. Risks and Mitigating Measures

34. Table 5 summarizes major risks and mitigating measures based on lessons from implementation of the ongoing investment program. Risks relating to cross-border performance and remedial measures, including cross-border point investments, are part of the first investment program. Overall mitigation measures, integrated benefits, and impacts are expected to outweigh the program costs.

Table 5: Summary of Risks and Mitigating Measures

Risks	Mitigating Measures
Program implementation delays	Project readiness before approval, including advance contracting No staff changes in the project management unit without ADB approval
Road system sustainability	Annual road maintenance budget inflation-linked Advisory services to review revenues and expenditures, maintenance, and independent quality control systems Cement concrete pavement requiring less maintenance

ADB = Asian Development Bank.
Source: Asian Development Bank.

IV. UNDERTAKINGS AND ASSURANCES

35. The government has assured ADB that implementation of the investment program shall conform to all applicable ADB policies including those concerning anticorruption measures, safeguards, gender, procurement, consulting services, and disbursement as described in detail in the FAM and loan documents.

36. The government has given ADB certain undertakings for the investment program, which are set forth in the framework financing agreement. Specific covenants agreed by the government with respect to individual tranches under the MFF are set forth in the loan agreements for the respective tranches.

V. RECOMMENDATION

37. I am satisfied that the proposed multitranche financing facility would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the provision of loans under the multitranche financing facility in an aggregate principal amount not exceeding $500,000,000 equivalent (the facility amount) to the Republic of Uzbekistan for the Second Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program comprising

(i) a loan in various currencies not exceeding the equivalent of $180,000,000 in Special Drawing Rights from ADB's Special Funds resources, with interest to be determined in accordance with the then applicable policies relating to Special Funds resources and such other terms and conditions set out in paragraph 17 of this report; and

(ii) loans in an aggregate amount not exceeding the balance of the facility amount from ADB's ordinary capital resources, with interest to be determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility;

subject to such other terms and conditions as are substantially in accordance with those set forth in the framework financing agreement presented to the Board.

Haruhiko Kuroda
President

1 August 2011

DESIGN AND MONITORING FRAMEWORK FOR THE INVESTMENT PROGRAM

Design Summary	Performance Targets and Indicators with Baselines	Data Sources and Reporting Mechanisms	Assumptions and Risks
Impact Increased domestic and international trade	**By 2020**: Annual domestic trade with Fergana valley increased to $3.360 billion (2010 baseline: $2.285 billion), and with Bukhara province to $1.134 billion (2010 baseline: $0.772 billion) Annual external trade with the Kyrgyz Republic increased to $300 million (2010 baseline: $177 million), with Tajikistan to $50 million (2010 baseline: $12.6 million), and with Kazakhstan to $1,600 million (2010 baseline: $956 million)	Statistical Review of Uzbekistan (annual publication by the Central Statistics Office) Statistical data of the Ministry for Foreign Economic Relations, Investment and Trade	**Assumption** The government sustains policies conducive to economic growth and remains committed to enhanced policy reforms and regional integration. **Risk** Internal slow decision making delays impetus for policy reforms.
Outcome Improved road connectivity, safety, and effective RRF management of the Uzbekistan sections of CAREC Corridor 2	**By 2017:** Increased average total long-haul traffic volume on the A373 and A373/4R112 highways in Fergana province to 20,000 vpd (2011 baseline: 10,000 vpd), and on the A380 in Bukhara region to 2,500 vpd (2011 baseline: 1,200 vpd) Travel time from Dautata to Bukhara reduced to 8 hours (2011 baseline: 12 hours), and from Tashkent to Osh border reduced to 5 hours (2011 baseline: 7 hours) Accidents on the A373 and A373/4R112 reduced to 120 per year (2009 baseline: 250 accidents/year), and on the A380 to 75 accidents/year. (2009 baseline: 150 accidents/year) Road asset management system and road safety plans approved by the government and implemented in accordance with international standards	Periodic classified traffic reports of Uzavtoyul Periodic classified traffic reports of Uzavtoyul Periodic classified traffic reports of Uzavtoyul RRF biannual asset management reports and Road Safety Commission’s periodic reports	**Assumptions** Increased availability and quality of road transport services (freight and passengers) follows improvement of the investment program roads. RRF continues construction of the remaining sections of the A380 and A373 as scheduled at the same quality as the investment program. **Risk** Inadequate financial resources are available for road maintenance.
Outputs 1. Selected road sections of CAREC Corridor 2 reconstructed by RRF	**By 2017:** With pavement international roughness index of less than 4 meters per km:(i) 74 km of the A373 (between Km 116 and Km 190) reconstructed under project 1; (ii) 87 km of the A380 (between Km 228 and Km 315)	RRF website and periodic road condition reports by RRF and Uzavtoyul	**Assumption** Provision of counterpart resources is timely and support for the investment program continues.

Design Summary	Performance Targets and Indicators with Baselines	Data Sources and Reporting Mechanisms	Assumptions and Risks
	reconstructed under project 2; and (iii) 75 km of the A373/4R112 (between Km 0 and Km 75) reconstructed under project 3 Roads with cracks more than 10% and 10 potholes per km reduced to 50% (2009 baseline: 60%)	Periodic road condition reports by RRF and Uzavtoyul	**Risks** High turnover of program management unit mid-level staff disrupts program implementation progress. Internal delays are experienced in the approval of contracts for works, goods, and consultants
2. Road subsector sustainability plans implemented by RRF	**Sector** The independent quality control unit reporting to MOF biannually on road construction and maintenance works Public–private partnership framework in place National road infrastructure safety strategy approved by the government by March 2013 Routine annual road maintenance budget is increased by an amount equal to or greater than the annual inflation rate **Investment program** Road safety action plan for the investment program approved by the government by May 2013 and implemented under projects 2 and 3 150 staff of RRF and Uzavtoyul trained under the road safety capacity development program under projects 2 and 3 Road asset management system updated quarterly by RRF and reported to MOF	Biannual road condition reports by the independent quality control unit and periodic Uzavtoyul reports Periodic reports of "Norma" (a private company maintaining a government legislation database) Road Safety Commission's periodic reports Annual budget reports of RRF and Uzavtoyul Road Safety Commission's periodic reports Periodic Road Safety Commission's periodic reports RRF quarterly road asset management reports	**Assumptions** The government is committed to further reform the road subsector. RRF and Uzavtoyul are committed to continue improving their institutional structures and capacity. **Risk** Delays are experienced in the approval of the national road infrastructure safety strategy

Design Summary	Performance Targets and Indicators with Baselines	Data Sources and Reporting Mechanisms	Assumptions and Risks
	Road user charges piloted on reconstructed Kamchik road section in 2014 under project 2	Periodic reports of “Norma”	
	Specific gender action plan implemented under each project	RRF website and quarterly communication reports	
3. Projects completed as targeted and budgeted	Project 1 completed by 30 September 2013 with no cost overrun	Annual statistical review of Uzbekistan	
	Projects 2 and 3 completed as targeted and budgeted	Annual statistical review of Uzbekistan	

Activities with Key Milestones	Inputs
1. Selected sections of CAREC Corridor 2 reconstructed by RRF 1.1 74 km of the A373 reconstructed under project 1 by 31 March 2014 1.2 87 km of the A380 reconstructed under project 2 by 30 September 2015 1.3 75 km of the A373/4R112 reconstructed under project 3 by 31 March 2017 **2. Road subsector sustainability plans implemented by RRF** 2.1 National road infrastructure safety strategy, road safety checklist, guidelines, and measures that will improve road safety management, developed by September 2012 under project 1 and approved by March 2013 2.2 Specific road safety program for the road sections of the investment program developed by December 2012 under project 1, approved by March 2013, and implemented under projects 2 and 3 2.3 Road safety awareness campaign to selected communities and training for 150 staff of RRF and Uzavtoyul conducted under project 2 as part of the overall road safety and capacity development program 2.4 Road asset management system updated quarterly by RRF effective January 2012 2.5 Under each project, outreach training of entrepreneurial skills development conducted for selected number of women, and HIV/AIDS prevention and traffic safety training conducted for both men and women **3. Projects completed as targeted and budgeted** 3.1 For project 1, construction supervision consultants recruited by 30 September 2011, civil works contract awarded by 15 October 2011 and completed by 30 September 2013 with no cost overrun 3.2 Due diligence for projects 2 and 3 completed by December 2012, focusing on effective road management and road safety in planning, design, construction, and operation	1. ADB MFF not exceeding $500 million, comprising up to $180 million from Special Funds resources and balance OCR 2. Government counterpart budget: $100 million

ADB = Asian Development Bank, CAREC = Central Asia Regional Economic Cooperation, km = kilometer, OCR = ordinary capital resources, MFF = multitranche financing facility, MOF = Ministry of Finance, RRF = Republican Road Fund, vpd = vehicles per day.
Source: Asian Development Bank.

LIST OF LINKED DOCUMENTS

http://adb.org/Documents/RRPs/?id=44483-024-3

1. Loan Agreement
2. Framework Financing Agreement and Periodic Financing Request for Project 1
3. Sector Assessment (Summary): Road
4. Facility Administration Manual
5. Contribution to the ADB Results Framework
6. Development Coordination
7. Summary Economic and Financial Sustainability Analysis for Project 1
8. Country Economic Indicators
9. Summary Poverty Reduction and Social Strategy
10. Gender Action Plan for Project 1
11. Initial Environmental Examination for Project 1
12. Environmental Assessment and Review Framework
13. Resettlement Framework
14. Ethnic Minority Planning Framework
15. Risk Assessment and Risk Management Plan