



Report and Recommendation of the President to the Board of Directors

Project Number: 49026-002
November 2017

Proposed Loan Socialist Republic of Viet Nam: Basic Infrastructure for Inclusive Growth in the Northeastern Provinces Sector Project

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Asian Development Bank

CURRENCY EQUIVALENTS

(As of 2 November 2017)

| | | |
|---------------|---|------------|
| Currency unit | – | dong (D) |
| D1.00 | = | \$0.000044 |
| \$1.00 | = | D22,466 |

ABBREVIATIONS

| | | |
|------|---|---|
| ADB | – | Asian Development Bank |
| ARVC | – | agriculture and rural value chain |
| EIRR | – | economic internal rate of return |
| IFAD | – | International Fund for Agricultural Development |
| O&M | – | operation and maintenance |
| PAM | – | project administration manual |
| PMU | – | project management unit |
| PPC | – | provincial people's committee |
| PRC | – | People's Republic of China |
| RDWS | – | rural domestic water supply |
| SMEs | – | small and medium-sized enterprises |

NOTE

In this report, "\$" refers to United States dollars.

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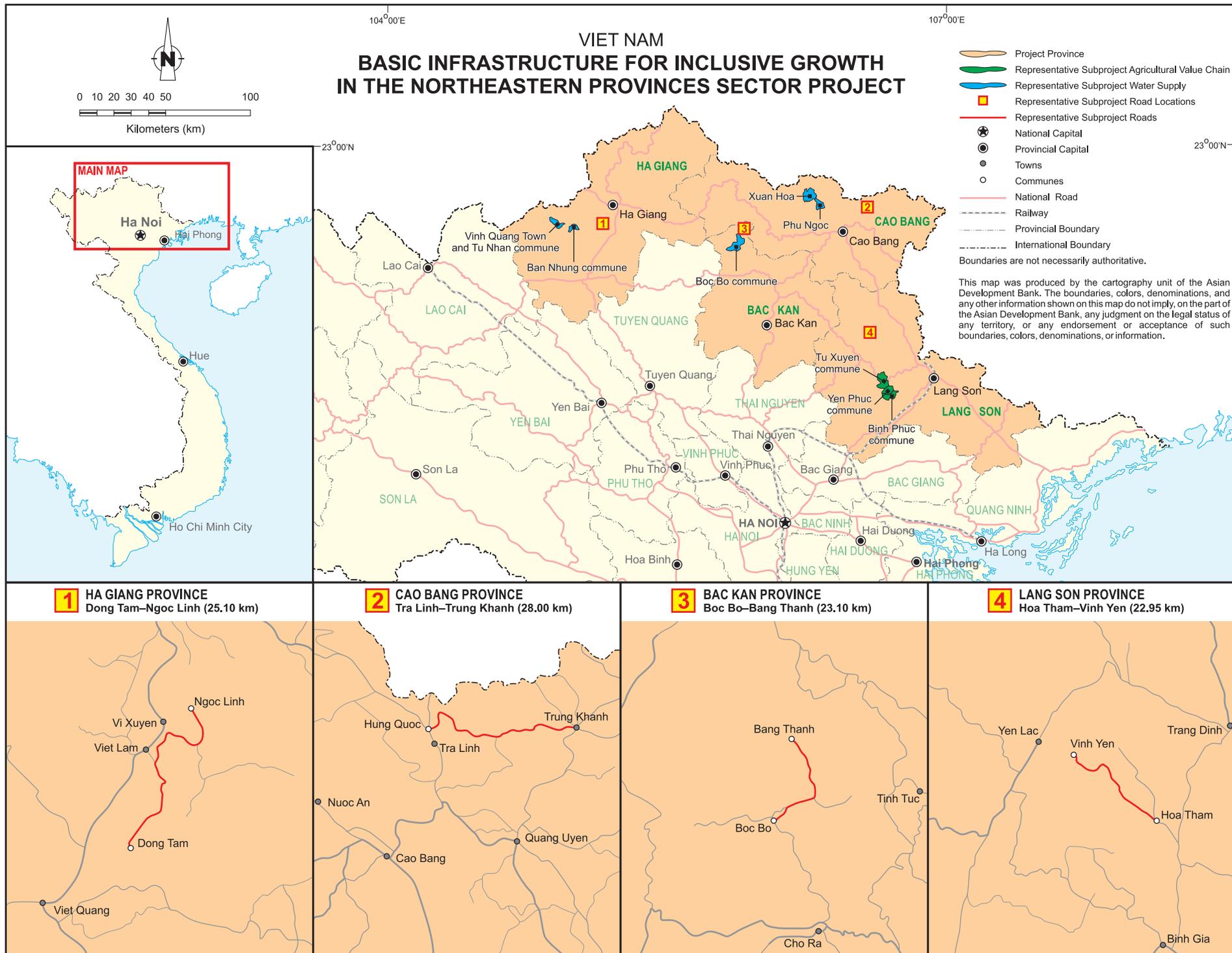
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PROJECT AT A GLANCE

| | | | |
|--|--|--|---|
| 1. Basic Data | | Project Number: 49026-002 | |
| Project Name | Basic Infrastructure for Inclusive Growth in the Northeastern Provinces Sector Project | Department /Division | SERD/SEER |
| Country Borrower | Viet Nam, Socialist Republic of Viet Nam, Socialist Republic of | Executing Agency | Provincial People's Committee of Bac Kan Province, Provincial People's Committee of Cao Bang Province, Provincial People's Committee of Ha Giang Province, Provincial People's Committee of Lang Son Province |
| 2. Sector | Subsector(s) | ADB Financing (\$ million) | |
| ✓ Agriculture, natural resources and rural development | Agricultural production | | 5.00 |
| | Rural market infrastructure | | 10.00 |
| | Rural water supply services | | 20.00 |
| Transport | Road transport (non-urban) | | 115.00 |
| | | Total | 150.00 |
| 3. Strategic Agenda | Subcomponents | Climate Change Information | |
| Inclusive economic growth (IEG) | Pillar 2: Access to economic opportunities, including jobs, made more inclusive | Adaptation (\$ million) | 33.00 |
| Environmentally sustainable growth (ESG) | Eco-efficiency | Mitigation (\$ million) | 3.00 |
| | Global and regional transboundary environmental concerns | CO ₂ reduction (tons per annum) | 2,692 |
| Regional integration (RCI) | Pillar 1: Cross-border infrastructure | Climate Change impact on the Project | Medium |
| 4. Drivers of Change | Components | Gender Equity and Mainstreaming | |
| Governance and capacity development (GCD) | Civil society participation | Effective gender mainstreaming (EGM) | ✓ |
| Knowledge solutions (KNS) | Knowledge sharing activities | | |
| | Pilot-testing innovation and learning | | |
| Partnerships (PAR) | Civil society organizations | | |
| | Implementation | | |
| Private sector development (PSD) | Public sector goods and services essential for private sector development | | |
| 5. Poverty and SDG Targeting | | Location Impact | |
| Geographic Targeting | Yes | Rural | High |
| Household Targeting | No | Urban | Low |
| SDG Targeting | Yes | | |
| SDG Goals | SDG1, SDG6, SDG8, SDG9, SDG10, SDG13 | | |
| 6. Risk Categorization: | Low | | |
| 7. Safeguard Categorization | Environment: B | Involuntary Resettlement: B | Indigenous Peoples: B |
| 8. Financing | | | |
| Modality and Sources | | Amount (\$ million) | |
| ADB | | 150.00 | |
| Sovereign Sector (Concessional Loan): Ordinary capital resources | | 150.00 | |
| Cofinancing | | 0.00 | |
| None | | 0.00 | |
| Counterpart | | 40.30 | |
| Government | | 40.30 | |
| Total | | 190.30 | |



I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed loan to the Socialist Republic of Viet Nam for the Basic Infrastructure for Inclusive Growth in the Northeastern Provinces Sector Project.

2. The four northeastern provinces of Bac Kan, Cao Bang, Ha Giang, and Lang Son with an area of 27,801 square kilometers include some of the remotest communities in Viet Nam. In 2015, the provinces had a total population of 2.36 million consisting largely of ethnic minorities with high poverty levels. Under the proposed provincially managed multisector project, locally prioritized basic infrastructure subprojects will be implemented. The subprojects will support economic connectivity among the provinces and improve the rural living standards of over 212,000 people through better (i) interprovincial commerce and rural accessibility by upgrading provincial and district roads, (ii) health through the construction of rural domestic water supply (RDWS) systems, (iii) incomes and livelihoods through strengthened agriculture and rural value chains (ARVCs), and (iv) sustainability of provincially owned infrastructure through the establishment of asset management systems.¹

II. THE PROJECT

A. Rationale

3. The overriding comparative advantage of the four provinces is the northeast geographic location, particularly with Cao Bang, Ha Giang, and Lang Son having extensive borders with the People's Republic of China (PRC). The provinces are at the nexus of the PRC, with its vast market and high demand for Vietnamese products; the Red River Delta, with Hanoi and its strong domestic market; and with the Hai Phong port link to world markets. The area is adjacent to the Asian Development Bank (ADB)-supported Greater Mekong Subregion North–South Economic Corridor, including both the central and eastern subcorridors.² In 2015, total PRC–Viet Nam trade was \$96 billion, an increase of 15% over 2014, imports from the PRC to Viet Nam grew at 4%, while exports to the PRC grew at 49%.³ Viet Nam continues to expand trade with PRC by developing additional international gateways and auxiliary border crossings.⁴

4. The full economic potential of the four northeastern provinces is not yet realized. Viet Nam's gross domestic product grew at an average rate of 6% per year during 2012–2016, with gross domestic product per capita reaching \$2,108, however in the project area it remains about half the national average, at \$1,160. The 2015 nationwide poverty level was 7.0% but the levels were 17.1% in Bac Kan, 24.4% in Cao Bang, 24.2% in Ha Giang and 16.2% in Lang Son.⁵ Most rural communities in the provinces are weakly integrated into the mainstream economy and social services. They remain highly vulnerable to changing circumstances through external shocks such as commodity price fluctuations and extreme climatic events, amplified by climate change trends.

5. The underlying causes of low income and poverty in the northeastern provinces include:

¹ ADB. 2015. *Technical Assistance to the Socialist Republic of Viet Nam for the Basic Infrastructure for Inclusive Growth in the Northeast Provinces Sector Project*. Manila.

² The two subcorridor sections are (i) Kunming (PRC) to Hanoi or Hai Phong, and (ii) Nanning (PRC) to Hanoi.

³ Viet Nam to Become China's Biggest ASEAN Trader in 2016. <http://m.english.vietnam.net/fms/business/152210>.

⁴ Government of Viet Nam and Government of People's Republic of China. 2011. *Master Plan on Vietnam – China Economic and Trade Cooperation for the 2012-2016 period* 2011. Beijing.

⁵ Government of Viet Nam, General Statistics Office. 2015. *Statistical Yearbook of Vietnam*. Hanoi.

- (i) **Poor road connectivity.** The mountainous terrain makes road development expensive. The road density averages 70% of the national average, with only 32% of provincial roads and 26% of district roads in good condition. The provinces are poorly linked to each other and to many rural communities; local enterprises are less competitive due to high input and output costs; and travel on the roads is long, arduous, and dangerous. The national arterial road network's south–north axis is mostly established, but much work remains to be done on the east–west axis.
- (ii) **Limited clean water supply.** Only 16% of rural households have access to clean water, in contrast to the national average of 45%. The generally steep, mountainous terrain complicates water storage and distribution management.
- (iii) **Limited value addition to agriculture and rural production.** The provinces already produce and could greatly expand the production of many high-value crops such as oranges and star anise, but inadequate basic infrastructure, weak production organization, and limited access to finance, hampers local value addition from farm to consumer, constraining profits and private investment.
- (iv) **Weak infrastructure asset management.** The piecemeal development of provincial infrastructure assets, without proper management systems, has resulted in substandard public infrastructure condition, coverage and sustainability.

6. The project will help unlock the development binding constraints by improving basic infrastructure across key sectors following with the Overall Development Plan of Mountainous Northeastern Provinces 2015.⁶ Stronger provincial integration into the national economy will be achieved by: (i) upgrading the road network to interconnect: provincial centers; the PRC border gates; the east–west network with the main road corridors to Hanoi and ports on the east coast; and remote rural communities;⁷ (ii) developing clean, dependable RDWSs to improve health and to support enterprise; (iii) increasing ARVC profitability by using modern technologies, building up small and medium-sized enterprises (SMEs), and improving farmer capacity through (a) the use of funds awarded through competitive processes for SME development, (b) increased use of trade promotion, (c) developing producer–market links, and (d) establishing larger commercial-scale production units; and (iv) effective provincial asset management to improve the performance, returns, and sustainability of infrastructure investment.

7. The project is aligned with important government policies and strategies as expressed in (i) the 2016 Socio-Economic Development Plan 2016–2020, which aims to expand and promote exports and sustain trading surpluses;⁸ (ii) the 2013 Master Plan for Socio-Economic Development of Northern Midland and Mountainous Areas towards 2020, which stresses the benefits, economic opportunities, and social services to rural communities by increasing multisector public and private investments;⁹ (iii) the 2009 government transport strategy, which emphasizes corridor development and inclusive rural connectivity;¹⁰ (iv) the 2011 National Target Program on New Rural Development with targets for rural access, RDWSs, and ARVCs;¹¹ (v)

⁶ Government of Viet Nam. 2015. *Overall Development Plan of Mountainous Northeastern Provinces of Viet Nam to 2020*. Hanoi.

⁷ ADB. 2011. *Greater Mekong Subregion Economic Cooperation Program Strategic Framework, 2012–2022*. Manila.

⁸ Government of Viet Nam, National Assembly of Viet Nam. 2016. *Five-Year Socio-Economic Development Plan from 2016–2020*. Resolution No. 142/2016/QH13. Hanoi.

⁹ Approved by Prime Minister's Decision No. 1064 / QĐ-TTg, 8 July 2013.

¹⁰ Government of Viet Nam. 2009. *Decision No. 35/QĐ-TTg. Approval of Adjustments to Viet Nam Transport Development Strategy up to 2020 with a Vision toward 2030*. Hanoi.

¹¹ Government of Viet Nam. 2011. *Prime Minister's Decision No. 2406/QĐ-TTg on Issuing the National Target Programs for Period 2012-2015 dated 18 December 2011*. Hanoi.

decentralization policy for increased provincial responsibility for local development;¹² and (vi) commitment to the Sustainable Development Goals.

8. The project supports the three pillars of ADB's country partnership strategy, 2016–2020 for Viet Nam:¹³ (i) job creation and competitiveness, through improving physical connectivity, supporting commerce and employment creation, enhancing the business environment, and increasing productivity; (ii) inclusive basic infrastructure and service delivery, through diversifying economic opportunities, broadening access to social services, creating livelihood opportunities for remote northeastern rural people, who have disproportionately high numbers of poor and predominantly belong to ethnic minorities, and working with provincial governments to improve the management of provincially owned infrastructure assets; and (iii) improved environmental sustainability and climate change response, with climate-proofing measures in investments.

9. **Value added by ADB assistance.** ADB's experience is central in guiding the decisions to support decentralized government in defining inclusive development through feasible multisector investments with the key features of: (i) provincial responsibility for project execution and financing - by borrowing on ADB loan proceeds. ADB inputs reduce risks in provincial governance, financial management and sustainability; and (ii) locally integrated multisector investments support inclusive local development needs and economic opportunities. ADB has drawn upon specialists across its operations to ensure project viability and due diligence. Greater synergies will be achieved with ADB technical assistance by integrating their activities directly into the project, such as agriculture competitiveness, decentralized public asset management and road safety.¹⁴ The project will coordinate with the International Fund for Agricultural Development (IFAD) on ARVCs.¹⁵ ADB's Viet Nam Resident Mission backed-up by ADB's technical divisions, has experience and capacity to assist the government to overcome implementation challenges having recently administered in the project area projects such as Sustainable Rural Infrastructure Development Project in Northern Mountain Provinces and Transport Connections in the Northern Mountainous Provinces Project.¹⁶

10. **Lessons from ADB's experience.** The project draws on lessons learned from ADB operations, including the need to improve: (i) basic infrastructure and connectivity for economic growth, business competitiveness and integration of rapidly developing areas with disadvantaged regions; (ii) provincial government ownership through early engagement in project design and management; (iii) sustainability by including operation and maintenance (O&M) and climate change considerations into investment strategies; (iv) promoting a more inclusive growth path by enhancing ADB support for SMEs through direct capital financing; and (v) project readiness through the preparation of additional feasibility studies, master bidding documents, and consultant support during the start-up phase to prevent delays and increase implementation efficiency.

¹² Government of Viet Nam. 2017. *State Budget Law 2017*.

¹³ ADB. 2016. *Country Partnership Strategy: Viet Nam, 2016–2020—Fostering More Inclusive and Environmentally Sustainable Growth*. Manila.

¹⁴ ADB. 2017. *Technical Assistance to the Socialist Republic of Viet Nam for Enhancing Agricultural Competitiveness in Viet Nam*. Manila; ADB. 2015. *Technical Assistance to the Socialist Republic of Viet Nam for Capacity Building for Project Management Unit Professionalization*. Manila; and ADB. 2015. *Technical Assistance for Unlocking Innovation in Development-Scaling Up Innovative Road Safety Operations*. Manila.

¹⁵ Development Coordination (accessible from the list of linked documents in Appendix 2).

¹⁶ ADB. 2010. *Report and Recommendation of the President to the Board of Directors: Proposed Loans to the Socialist Republic of Viet Nam for the Sustainable Rural Infrastructure Development Project in Northern Mountain Provinces*. Manila; ADB. 2011. *Report and Recommendation of the President to the Board of Directors: Proposed Loan to the Socialist Republic of Viet Nam for the Transport Connections in the Northern Mountainous Provinces Project*. Manila.

B. Impact and Outcome

11. The project is aligned with the following impact: subregional competitiveness of the four northeastern provinces enhanced (footnote 6). The project will have the following outcome: production, service delivery, and movement of goods and passengers sustainably increased.¹⁷

C. Outputs

12. **Output 1: Road network connectivity improved.** The output will upgrade about 121 kilometers of provincial and 144 kilometers of district roads, which will improve overall network efficiency by integrating interprovincial travel, transport, and commerce, as well as improve connectivity with PRC border crossings. Many isolated, poor rural communities will be able to access the transport network at lower cost, leading to both economic and social benefits. Reduced transport costs and improved rural access will make SMEs more competitive, and enhance rural development initiatives. The improved network connectivity addresses significant barriers to the development of tourism circuits. Road safety will be included in subproject design, with about 44 traffic calming measures forcing reductions in vehicular speeds at critical points, such as schools, and 13 safety awareness trainings carried out for vulnerable road users. Output 1 will benefit approximately 44 rural communities, comprising about 160,000 people in 27,411 households.

13. **Output 2: Rural water supply improved.** About ten RDWS subprojects will be constructed to meet the 2030 forecasted demand. Clean water will (i) improve public health, which is particularly important for communities located far from medical facilities; (ii) help develop ARVCs, as clean water is needed to wash produce, and for creating sanitary conditions at an early stage of value addition at farm and throughout the ARVC; and (iii) increase the tourism demand through more attractive facilities. Output 2 will serve about 22 communes, comprising 42,300 people in 10,000 households.

14. **Output 3: Agriculture and rural value chain infrastructure in Lang Son province improved.** The viability and incomes of local rural producers and SMEs will be increased by supplying high-quality food, spices, and flowers to (i) international markets, (ii) northern Vietnamese urban centers, and (iii) local tourist sites. IFAD will continue its established program of ARVC support in the Bac Kan, Cao Bang and Ha Giang. While in Lang Son, the project will replicate proven IFAD models to support horticultural trade and marketing organizations for at least five commodities. It will introduce market-based business plans, provide viability gap grants to at least 30 existing value chain enterprises to leverage investment into value-adding technology and infrastructure, support 80 producer groups for investing in market-linked quality control, production, and post-harvest infrastructure. Better transport (output 1) and clean water (output 2) will lead to competitive ARVCs in all four provinces. Output 3 will directly benefit about three communes comprising about 10,400 people in 3,000 households.

15. **Output 4: Decentralized public asset management processes established.** ADB is supporting the national decentralized public asset management program.¹⁸ The provinces will procure asset management hardware and systems, and carry out associated staff training. The systems will include indicators and tools to allow monitoring of annual maintenance budgets and

¹⁷ The design and monitoring framework is in Appendix 1.

¹⁸ ADB. 2016. *Report and Recommendation of the President to the Board of Directors: Proposed Programmatic Approach, Policy-Based Loans, and Technical Assistance Grant for Subprogram 1 to the Socialist Republic of Viet Nam for the Improving Public Expenditure Quality Program*. Manila

their funding, as well as moving to life-cycle-based investment decisions for future O&M, and asset procurement and sustainability.

D. Summary Cost Estimates and Financing Plan

16. The project is estimated to cost \$190.3 million (Table 1). Detailed cost estimates by expenditure category and by financier are included in the project administration manual (PAM).¹⁹ Project investments includes civil works, detailed design, construction supervision and project management, safeguard measures and feasibility studies for additional subprojects.²⁰

Table 1: Summary Cost Estimates
(\$ million)

| Item | Amount ^a |
|--|---------------------|
| A. Base Cost^b | |
| 1. Road network connectivity improved | 122.6 |
| 2. Rural water supply improved | 19.5 |
| 3. ARVC infrastructure in Lang Son province improved | 15.6 |
| 4. Decentralized public asset management processes established | 2.0 |
| 5. Project management | 5.2 |
| Subtotal (A) | 164.9 |
| B. Contingencies^c | 21.7 |
| C. Financial Charges During Implementation^d | 3.7 |
| Total (A+B+C) | 190.3 |

ARVC = agriculture and rural value chain.

^a The Government of Viet Nam will finance taxes and duties estimated at \$16.1 million.

^b In Q3 2017 prices; exchange rate as of 15 October 2017.

^c Physical contingencies computed at 10% for civil works, 10% for equipment, and 0% for consulting services. Price contingencies computed at average of 1.5% on foreign exchange costs and 5.0% on local currency costs; includes provision for potential exchange rate fluctuation under assumption of a purchasing power parity exchange rate.

^d Interest during project implementation for the concessional ordinary capital resources loan has been computed at the rate of 2% per annum.

Source: Asian Development Bank estimates.

17. The government has requested a concessional loan of \$150 million from ADB's ordinary capital resources to help finance the project. The loan will have a 25-year term, including a grace period of 5 years; an interest rate of 2.0% per year during the grace period and thereafter; and such other terms and conditions set forth in the loan and project agreements. The government will (i) make portions of the loan proceeds available to the participating provinces through budget allocation, and (ii) relend the balance of the loan proceeds to the provinces under respective onlending agreements, all upon terms and conditions satisfactory to ADB.²¹ The loan will finance infrastructure works, detailed design, construction supervision, and independent audit.

18. The government will fund \$40.30 million to assist project implementation, including detailed design, project management, land acquisition and resettlement costs, loan implementation consulting services, and all taxes and duties.

19. The project's sector modality meets ADB's criteria of (i) supporting the implementation of multisector development plans, notably the Overall Development Plan of Mountainous Northeastern Provinces 2015 (footnote 6); (ii) the provinces are assessed to have the institutional

¹⁹ Project Administration Manual (accessible from the list of linked documents in Appendix 2).

²⁰ A long list of candidate subprojects, which are eligible for feasibility studies, is presented in the PAM.

²¹ The breakdown of financing by province is detailed in the PAM.

capacity to implement the relevant sector development plans; and (iii) the relevant policies for infrastructure sustainability will be strengthened.

20. The summary financing plan is presented in Table 2.

Table 2: Summary Financing Plan

| Source | Amount (\$ million) | Share of Total (%) |
|--|------------------------|-----------------------|
| Asian Development Bank | | |
| Ordinary capital resources (concessional loan) | 150.00 | 79 |
| Government | 40.30 | 21 |
| Total | 190.30 | 100 |

Source: Asian Development Bank.

21. Subproject design will include adaptations to reduce climatic change effects from a high to a medium risk level.²² The climatic adaptation measures are aligned with the government's construction procedures. Climate mitigation is estimated to cost \$3 million and climate adaptation is estimated to cost \$33 million with ADB financing 100% of the costs.

E. Implementation Arrangements

22. The implementation arrangements are summarized in Table 3 and detailed in the PAM.

Table 3: Implementation Arrangements

| Aspects | Arrangements | | |
|---------------------------------|--|--------------------------------------|-----------------|
| Implementation period | March 2018–March 2023 | | |
| Estimated completion date | 31 March 2023 | | |
| Estimated loan closing date | 30 September 2023 | | |
| Management | | | |
| (i) Oversight body | Each province will have a provincial steering committee | | |
| (ii) Executing agency | Each province's provincial people's committee | | |
| (iii) Key implementing agencies | Each province's department of planning and investment | | |
| (iv) Implementation unit | Each province's project management unit (each with 16–23 staff) with support from the interprovincial coordination unit | | |
| Procurement | NCB | 24 contracts | \$126.9 million |
| | GOV procedures | 24 contracts (GOV financed) | \$3.0 million |
| Consulting services | QCBS | 8 contracts, 2,000 p-m | \$9.9 million |
| | CQS | 3 contracts, 25 p-m | \$0.6 million |
| | FBS | 4 contracts, 20 p-m | \$0.2 million |
| | GOV procedures | 50 contracts, 600 p-m (GOV financed) | \$20.3 million |
| Advance contracting | Preparation: (i) of 11 subproject feasibility studies, (ii) of the project performance management system, (iii) for recruitment of detailed design consultants and loan implementation consultants, and (iv) for procurement of government financed equipment and goods. | | |
| Disbursement | The loan proceeds will be disbursed following ADB's <i>Loan Disbursement Handbook</i> (2017, as amended from time to time) and detailed arrangements agreed between the government and ADB. | | |

ADB = Asian Development Bank, CQS = consultant quality selection, FBS = fixed budget selection, GOV = Government of Viet Nam, NCB = national competitive bidding, p-m = person-months, QCBS = quality- and cost-based selection.

Source: Asian Development Bank.

²² Climate Risk and Vulnerability Assessment (accessible from the list of linked documents in Appendix 2).

23. Each Provincial People's Committees (PPC) will be an executing agency and shall chair their respective provincial steering committees to address project coordination, negotiations, and discussions.²³ Each Provincial Department of Planning and Investment will be an implementing agency and will establish project management units (PMU) for day to day operations. The PMUs will be legally registered entities able to sign contracts with consultants, contractors, and suppliers, and will be assisted by the loan implementation consultants. The Lang Son PMU will establish a small unit for aggregating reports for, and to coordinate with, ADB. At the commune level, the PMUs will coordinate with local administrations, and liaise with commune people's committees.

24. Project readiness will be enhanced by the: (i) preparation of 11 subproject feasibility studies, a screened and prioritized list of 17 potential additional subprojects and master bidding documents;²⁴ (ii) contract signing for detailed design and loan implementation consultant upon loan effectiveness;²⁵ and (iii) intensive training to the PMUs for key operational tasks.

III. DUE DILIGENCE

A. Technical

25. Viet Nam's private sector has the skills for subproject implementation. Of the 11 subproject feasibility studies prepared following the relevant Viet Nam design standards, nine were used as representative subprojects.²⁶ Detailed demand forecasts and preliminary engineering designs informed the road and RDWS subproject feasibility studies. For the ARVC subprojects, market demand was confirmed, value addition constraints were identified, indicative investment packages specified and quality control standards and procedures were defined. Technical guidelines were prepared for integrating climate change risk into detailed designs for more resilient infrastructure through increased flood elevations, improved cross drainage, and the use of bioengineering for erosion protection. For ARVC's the movement into safe food systems and standards, drip and spray irrigation with organic fertilizer and backward linked supply contracting will enable producers to adapt to climate and market risks.²⁷

B. Economic and Financial

26. The economic and financial analysis was carried out following ADB's Guidelines for the Economic Analysis of Projects, comparing with- and without-project scenarios.²⁸ Financial analysis of the feasibility studies validate the financial and fiscal sustainability of all nine representative subprojects.²⁹ O&M was estimated for the economic life of each road subproject and is less than 1% of current provincial O&M budgets.³⁰ The RDWS subprojects will be professionally managed by water supply companies without incremental increases in fiscal resources and do not require a subsidy increase. The financial internal rates of return for RDWS subprojects range from 2% to 3%, all above the weighted cost of capital. The ARVCs are fiscally positive requiring no operational subsidy while generating increased tax revenues through enterprise growth. The financial internal rate of return is 14% for the safe vegetable and 25% for

²³ Project Agreement (accessible from the list of linked documents in Appendix 2).

²⁴ Additional Subprojects Screening Report (accessible from the list of linked documents in Appendix 2).

²⁵ Using loan proceeds from ADB. 2012. *Report and Recommendation of the President to the Board of Directors: Project Preparation and Start-Up Support Facility, Socialist Republic of Viet Nam*. Manila.

²⁶ The representative subprojects included: (i) four roads; (ii) three RDWS; and (iii) two ARVC preliminary designs.

²⁷ ADB. 2016. *Project Readiness Improvement Trust Fund*. Manila.

²⁸ ADB. 2017. *Guidelines for the Economic Analysis of Projects*. Manila.

²⁹ Economic and Financial Analysis (accessible from the list of linked documents in Appendix 2).

³⁰ Excludes additional VAT collected from economic output generated by improved transport infrastructure.

the star anise value chain subprojects. The provinces are heavily dependent on transfers from the central government and the establishment of the asset management systems will improve the sustainability of provincial infrastructure assets, and the loan agreement includes a covenant committing the government to provide adequate O&M for subproject investments.

27. The economic internal rates of return (EIRRs) for the road representative subprojects, are above 10%, based on vehicle operating cost and time savings. For RDWS subprojects, the EIRRs are above 9% based on the willingness to pay by domestic, industrial, and institutional users, and the time savings and health benefits for households. All subproject EIRRs exceed the social discount rate of 9%, which is taken as the threshold rate. The EIRRs are estimated to be 25% for the safe vegetable value chain and 15% for the star anise subprojects. Sensitivity analysis considers: (i) cost overruns on investment and O&M; (ii) reductions in forecasted demand for produce or services; and (iii) reduction in project benefits such as vehicle operating and time cost savings, health benefits, and agricultural produce prices. Economic viability is robust against risks.

C. Governance

28. The financial management assessment identified a high risk for the executing and implementing agencies because of capacity and systems constraints in existing accounting, staffing, auditing, and controls systems.³¹ Mitigation measures have been captured in the financial management action plan, to implement training, accounting systems, and external audit arrangements, and are supported by a covenant in the loan agreement. All procurement of goods and civil works and recruitment of consultants to be financed by the ADB loan will follow ADB's Procurement Guidelines (2015, as amended from time to time) and Guidelines on the Use of Consultants (2013, as amended from time to time) and have been arranged considering the limited capacity for managing externally funded projects in the four northeastern provinces. The government's public procurement regulations, as acceptable to ADB, will be applied for packages procured using national competitive bidding and shopping procedures.

29. ADB's Anticorruption Policy (1998, as amended to date) was explained to, and discussed with, the government and the PPCs. The specific policy requirements and supplementary measures are described in the PAM.

D. Poverty, Social, and Gender

30. The four northeastern provinces have high rural populations (80%), of whom 88% belong to ethnic minorities, and have rural poverty rates ranging from 28% to 57%, being roughly equal for men and women.³² The rural people often have limited access to markets, with low labor productivity associated with smallholder farming. Paid employment accounts for limited lengths of time, ranging from 25% in Bac Kan to 41% in Lang Son. Rural migration to urban areas is accelerating, leaving an aging population and constraining future rural economic growth potential.

31. **Gender.** The project is categorized as effective gender mainstreaming. A gender analysis revealed that women are disadvantaged in participating in public decision making, access to information, training, and employment, while often carrying a disproportionate work load.³³ The project gender action plan will promote (i) equal access to project benefits and opportunity sharing; (ii) reduction in gender inequalities and social risks; (iii) increased representation of

³¹ Financial Management Assessment (accessible from the list of linked documents in Appendix 2).

³² Summary Poverty Reduction and Social Strategy (accessible from the list of linked documents in Appendix 2).

³³ Gender Action Plan (accessible from the list of linked documents in Appendix 2).

women in decision making, (iv) collection of sex-disaggregated data for benefit monitoring and evaluation; and (v) the role of women in ARVCs, which often exceeds 50% and requires proportionately inclusive measures.

E. Safeguards

32. In compliance with national requirements and ADB's Safeguard Policy Statement (2009), all PPCs and ADB have agreed on the project's safeguard categories and mitigating measures. ADB's safeguard due diligence, gender action plan, appropriate community consultations and implementation resources, are included in all representative subproject feasibility studies, which serve as models for succeeding subproject feasibility studies. ADB will only finance subprojects that are classified *category B* or *category C* for all safeguards concerns.

33. **Environment (category B).** PPCs and ADB have agreed upon an environmental assessment and review framework.³⁴ The road works are limited to upgrades within the existing or newly established right-of-way and environmental impacts will be minor and temporary. They will not infringe on protected or environmentally sensitive areas and will require only simple mitigation measures such as proper management of construction camps or storage of building materials. Each initial environmental examination prepared for the nine representative subprojects includes an environmental management plan with appropriate mitigation measures and have been publicly disclosed.³⁵

34. **Involuntary resettlement (category B).** PPCs and ADB have agreed on a combined resettlement and ethnic minorities development framework.³⁶ Resettlement and ethnic minority development plans were prepared for all representative subprojects. They are supported by public consultation and information disclosure, which will be continued during implementation. The only impacts will be minor land acquisition and compensation for roadside trees, crops, or small structures within the rights-of-way, for which compensation, allowances, operation and administration, surveys, monitoring, and reporting will be financed from government counterpart funds. The internal monitor will ensure that any impacts are evaluated properly and reported to ADB semiannually through the PPCs.

35. **Indigenous peoples (category B).** Impacts on indigenous peoples, referred to as ethnic minorities in Viet Nam, are overwhelmingly positive and will enhance economic and social improvement. The project will neither cause displacement from traditional or customary lands nor negatively impact the identity, culture, or customary livelihood systems. The resettlement and ethnic minorities development framework will ensure the inclusion of ethnic minorities within project benefits and provide the basis to prepare subproject resettlement and ethnic minority development plans with impact mitigation measures, capacity development, a grievance redress mechanism, and compliance with ADB information disclosure and consultation requirements.

F. Summary of Risk Assessment and Risk Management Plan

36. Significant risks and mitigating measures are summarized in Table 4 and described in detail in the risk assessment and risk management plan.³⁷

³⁴ Environmental Assessment and Review Framework (accessible from the list of linked documents in Appendix 2).

³⁵ Initial Environmental Examinations for Representative Subprojects (accessible from the list of linked documents in Appendix 2)

³⁶ Resettlement Framework: Resettlement and Ethnic Minorities Development Framework (accessible from the list of linked documents in Appendix 2).

³⁷ Risk Assessment and Risk Management Plan (accessible from the list of linked documents in Appendix 2).

Table 4: Summary of Risks and Mitigating Measures

| Risks | Mitigation Measures |
|---|---|
| Premature asset deterioration. | DEDs will be based upon robust estimates for traffic increases and other loading stresses. O&M cost will be estimated for each subproject, and each EA will provide an O&M budgetary allocation as committed in the loan agreement. The asset management system will improve sustainability through better O&M. |
| Assets damaged by impacts of intensifying climate change. | All subprojects will be assessed for climate change impacts during FS with appropriate measures to be included in the DED. |
| Weak financial management and procurement systems. | Financial management: Regular financial management capacity training, strong LIC technical support, and the inclusion of a specific financial management covenant in the loan agreement. RDWS management will be assigned to functioning water supply companies which will help increase the capacity to cover the financing of O&M. Asset management systems for efficient resource allocation will be established. Procurement: Procurement plan uses NCB with fewer and larger packages, master bidding documents have been prepared and LIC will provide procurement support. |
| Reduced overall project scope. | Project readiness improved by the preparation of 11 subproject FS and 17 preliminary FS and the utilization of the project preparation start-up support fund for early preparation of DEDs. Risks of delays and price escalations are addressed by a covenant requiring necessary counterpart funding in the loan agreement. |
| Inadequate ADB project implementation experience. | PMUs will be staffed with necessary skill set and supported by LIC. ADB VRM with ADB technical sector back-up will provide proactive implementation administrative and technical support. |
| ARVCs development constrained. | The project will build on successful and established precedence and models with support to strengthen private sector actors in the value chain. |

ADB = Asian Development Bank, ARVC = agriculture and rural value chains, DED = detailed engineering design, EA = executing agency, FS = feasibility study, LIC = loan implementation consultant, NCB = national competitive building, PMUs = project management unit, O&M = operation and maintenance, RDWS = rural domestic water supply, VRM = Viet Nam Resident Mission.

Source: Asian Development Bank.

IV. ASSURANCES AND CONDITIONS

37. The Government of Viet Nam and the PPCs of the four northeastern provinces of Bac Kan, Cao Bang, Ha Giang, and Lang Son have assured ADB that implementation of the project 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 PAM and loan documents. The government and the PPCs of the four northeastern provinces have agreed with ADB on certain covenants, which are set forth in the loan and project agreements, including that no withdrawal shall be made from the loan account until the onlending loan agreements between the government and the PPCs have been duly completed.

V. RECOMMENDATION

38. I am satisfied that the proposed loan would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the loan of \$150,000,000 to the Socialist Republic of Viet Nam for the Basic Infrastructure for Inclusive Growth in the Northeastern Provinces Sector Project, from ADB's ordinary capital resources, in concessional terms, with an interest charge at the rate of 2% per year during the grace period and thereafter; for a term of 25 years, including a grace period of 5 years; and such other terms and conditions as are substantially in accordance with those set forth in the draft loan and project agreements presented to the Board.

Takehiko Nakao
President

24 November 2017

DESIGN AND MONITORING FRAMEWORK

| Impacts the Project is Aligned with | | | |
|--|--|---|--|
| Subregional competitiveness of the four northeastern provinces enhanced. <i>(Overall Development Plan of Mountainous Northeastern Provinces of Viet Nam to 2020, and National Target Program on new rural development for 2016-2020)^a</i> | | | |
| Results Chain | Performance Indicators with Targets and Baselines | Data Sources and Reporting Mechanisms | Risks |
| Outcome Production, service delivery, and movement of goods and passengers sustainably increased | By 2024: a. average annual increase of 5% in passenger car units and movement of goods 10% in ton-km on improved roads (2016 baseline: 468,612 passenger car units and 16.9 ton-km) b. About 44 communities within 2 km of the developed transport network (2016 baseline: 0 commune) c. About 22 communes have year-round reliable access to clean water (2016 baseline: 0) d. Incremental increase in value chain margins by D180 million per ha for star anise in three communes (2016 baseline: D360 million per ha) e. Asset management data to support O&M for provincially owned road and irrigation infrastructure integrated into annual provincial reports and development plans (2016 baseline: 0) | a.–b. PPMS, government and public transport operator statistics, additional subproject feasibility reports c. PPMS, provincial people's committee annual reports d. PPMS, district agriculture statistics e. Provincial annual reports and development plans | Inadequate O&M and climate change impacts lead to premature asset damage and deterioration. Delays in counterpart fund availability leads to price escalation reducing project scope. |
| Outputs 1. Road network connectivity improved | By 2023: 1a. About 121 km of provincial and 144 km of district roads improved (2016 baseline: 0 km) 1b. About 44 traffic calming measures provided to all road sections passing schools, markets, medical facilities, and administrative centers (2016 baseline: 0 measures) 1c. About 13 training programs, one for each road subproject, provided to vulnerable road users on each of the road subprojects, of whom female users account for 50% of trainees (2016 baseline: 0 measures and training) | 1a.–1c. PPMS | Official traffic forecasting systems underestimates loading leading to under-designed roads and premature deterioration. |
| 2. Rural water supply improved | By 2023: 2a. About ten rural domestic water supply schemes comprising | 2a. PPMS and QPR | Weak financial management related to |

| Results Chain | Performance Indicators with Targets and Baselines | Data Sources and Reporting Mechanisms | Risks |
|---|--|---------------------------------------|---|
| | approximately a total of 414 km of pipes laid (2016 baseline: 0 commune) | | user cost recovery reduces the sustainability of RDWS schemes. |
| 3. Agriculture and rural value chain infrastructure in Lang Son province improved | <p>By 2023:</p> <p>3a. Horticulture Lang Son Marketing and Trade Access Association for horticultural commodity groups formed with five commodity associations with proven market demand as members (2016 baseline: 0)</p> <p>3b. About 80 packages of market support for producer group infrastructure implemented (at least 50% female membership) (2016 baseline: 0)</p> <p>3c. About 30 enterprises receive matching grants for value addition and quality control standards with at least 10% of enterprises headed by women^b (2016 baseline: 0)</p> | 3a.–c. PPMS and QPR | Limited adoption of ARVC systems. |
| 4. Decentralized public asset management processes established | <p>By 2023:</p> <p>4a. Asset planning systems producing maintenance management information, including budget needs and timelines, operational in each province (2016 baseline: 0)</p> <p>4b. Water supply asset management planning with supporting databases for business management reporting for 10 rural domestic water supply schemes established (2016 baseline: 0)</p> <p>4c. Decentralized irrigation infrastructure asset planning systems producing management information on maintenance budget needs extended into Ha Giang, Bac Kan, and Cao Bang using the Asian Development Bank-supported Ministry of Finance model (2016 baseline: 0)</p> | 4a.–c. PPMS and QPR | Weak financial management systems do allocate resources for effective asset management. |

| |
|---|
| <p>Key Activities with Milestones^e</p> <p>1. Road network connectivity improved</p> <p>1.1 Prepare feasibility study for additional subprojects by April 2018 (PSD)</p> <p>1.2 Award works contracts for representative subproject by March 2019 (PSD)</p> <p>1.3 Award works contracts for priority additional subprojects by December 2019 (PSD)</p> <p>1.4 Prepare additional subproject detailed design (to use remaining funds) by June 2020 (PSD)</p> <p>1.5 Award works contracts for final additional subprojects by December 2020 (PSD)</p> <p>1.6 Complete construction works by December 2022 (PSD)</p> <p>2. Rural water supply improved</p> <p>2.1 Prepare feasibility study for remaining water supply subprojects by April 2018 (PSD)</p> <p>2.2 Award works contracts for representative subproject by March 2019 (PSD)</p> <p>2.3 Award works contracts for priority additional subprojects by December 2019 (PSD)</p> <p>2.4 Additional subproject detailed design (to use remaining funds) by June 2020 (PSD)</p> <p>2.5 Award works contracts for final additional subprojects by December 2020 (PSD)</p> <p>2.6 Establish water supply operation and maintenance capability by June 2022 (PSD)</p> <p>2.7 Complete construction works by December 2022 (PSD)</p> <p>3. Agriculture and rural value chain infrastructure in Lang Son province improved</p> <p>3.1 Sign contract with value chain service provider for market, trade access, and value chain integration by June 2018</p> <p>3.2 Establish the Horticulture Lang Son Marketing and Trade Access Association board by June 2018 and operational strategic business plan by December 2018 (PSD)</p> <p>3.3 Complete key commodities of safe vegetable and star anise marketing and trade studies by December 2018 (PSD)</p> <p>3.4 Establish commodity associations by December 2018 (PSD)</p> <p>3.5 Establish producer group business plans with infrastructure needs, and submit to HORTLANG SON to review and fund by January 2019 (PSD)</p> <p>3.6 Advertise and award enterprise value addition grants starting October 2018 (PSD)</p> <p>3.7 Train women's groups in agriculture and rural product value addition by March 2022 (PAR)</p> <p>4. Decentralized public asset management processes established</p> <p>4.1 Implement road network asset planning systems by September 2022 (GCD)</p> <p>4.2 Implement rural water supply asset planning by September 2022 (GCD)</p> <p>4.3 Extend decentralized irrigation asset management by September 2022 (GCD)</p> |
| <p>Project Management Activities</p> <p>Establish coordinating office and provincial project management units by December 2017.</p> <p>Complete recruitment of loan implementation consultants by May 2018.</p> <p>PPMS functioning within 30 days of loan effectiveness.</p> |
| <p>Inputs:</p> <p>Asian Development Bank: \$150.00 million concessional loan - ordinary capital resources</p> <p>Government of Viet Nam: \$40.30 million</p> |
| <p>Assumptions for Partner Financing</p> <p>Not applicable</p> |

ARVC = agriculture and rural value chains, D = dong, GCD = government capacity development, ha = hectare, km = kilometer, O&M = operation and maintenance, PAR = partnerships, PPMS = project performance monitoring system, PSD = private sector development, QPR = quarterly progress report, RSP = representative subproject, VND = Viet Nam Dong.

^a Government of Viet Nam. 2015. *Overall Development Plan of Mountainous Northeastern Provinces of Viet Nam to 2020*. Hanoi.; Government of Viet Nam. 2016. *Decision 1600/QD-TTg approving the National Target Program on new rural development for 2016-2020*. Hanoi.

^b In enterprises headed by women, the final decision is led by a woman. Households headed by women are households in which women are the main income earners.

Source: Asian Development Bank.

LIST OF LINKED DOCUMENTS

<http://www.adb.org/Documents/RRPs/?id=49026-002-3>

1. Loan Agreement
2. Project Agreement
3. Sector Assessment (Summary): Transport, Agriculture, Natural Resources and Rural Development
4. Project Administration Manual
5. Contribution to the ADB Results Framework
6. Development Coordination
7. Economic and Financial Analysis
8. Country Economic Indicators
9. Summary Poverty Reduction and Social Strategy
10. Risk Assessment and Risk Management Plan
11. Gender Action Plan
12. Environmental Assessment and Review Framework
13. Resettlement Framework: Resettlement and Ethnic Minority Development Framework

Supplementary Documents

14. Financial Management Assessment
15. Procurement Risk Assessment
16. Climate Risk and Vulnerability Assessment
17. Initial Environmental Examinations for Representative Subprojects
18. Detailed Economic and Financial Analysis: Roads
19. Detailed Economic and Financial Analysis: Water Supply
20. Output 3: Improved ARVC Infrastructure in Lang Son
21. Additional Subproject Screening Report