COMPARISON OF FINANCING MODALITY AND APPROACH TO TIME-SLICE FINANCING

A. Introduction

1. Large stand-alone projects are often implemented through a few long-term contract packages. To help development member countries finance such projects, Asian Development Bank (ADB) needs to commit or indicate the willingness to provide large amounts of loan(s) and to allow a longer period of implementation than other projects. In such a situation, ADB's financing instrument, the multitranche financing facility (MFF), has the comparative advantage of providing large amounts of loan(s) with minimized financing charges. However, the modality often faces difficulties, such as slow start-up, and uncertainties in the subsequent tranches.

2. ADB's Operations Manual D14, paragraph 8, last sentence, provides that the "MFF can also finance slices of long-term contract packages in such investment programs or large stand-alone projects."

3. Through such a provision, the MFF modality can provide time-slice financing to long-term contract packages if ADB completes the due diligence for the entire project scope. The tranche schedule is based on (i) the disbursement progress and projection to improve the disbursement ratio and minimize financing charges, and (ii) the achievements and needs for capacity development to allow a flexible and incremental approach. The preconstruction activities, such as land acquisition, resettlement, and procurement, will all be advanced for the first 2–3 years of the project to ensure implementation readiness and minimize the uncertainties of subsequent tranches.

4. This note provides a scope of analysis by comparing the financing modalities for the South Asia Subregional Economic Cooperation (SASEC) Dhaka–Northwest Corridor Road Project in Bangladesh, Phase 2, and explains how the approach of time-slice financing will be used.

B. Comparison of Financing Modality

5. A comparison of the MFF in relation to other financing modalities is presented in Table 1.

Table 1: Comparison of the Multitranche Financing Facility to Other Financing Modalities

Issues	Comparison		Remarks
	Multitranche Financing Facility	**Other Financing Modalities**	
1. A total of $1,672.6 million required for the project	MFF enables ADB to offer financial resources to the client in a series of separate financing tranches.	The possible size of project loan is significantly less than the requirement.	MFF modality is preferred. The tranche plan will be based on disbursement progress and projection.
2. Long-term support and engagement in the development of subregional trade corridor	MFF allows ADB to provide assistance programmatically and aligned with long-term needs of the client. The investment program is aligned with the CPS, the COBP and the government's 7th Five Year Plan. Sector roadmap will be updated with the government and DPs during the MFF implementation.	The needs of the client are mainly assessed during the country programming, which may be inefficient. Furthermore, a standalone project limits its support to short-term intervention and policy implementation.	MFF modality is preferred. A sector roadmap has been developed. This could be adjusted for the MFF implementation period, considering that the MFF implementation period has overlaps with the maintenance period.

Issues	Comparison		Remarks
	Multitranche Financing Facility	Other Financing Modalities	
3. Capacity development of the road agencies for planning, road asset management, road safety, and overloading control	MFF allows ADB to enter into a sustained partnership for supporting the capacity development plan. In addition, a phased approach with tranches will allow the EA to improve institutional capacity of the sector/program management.	The support provided by a project loan is limited to the size and term of the loan. A standalone project's interventions are not often institutionalized in terms of capacity building.	MFF modality is preferred. The progress of capacity development and the emerging needs will be assessed during the preparation of new tranches.
4. Policy dialogue and coordination in the transport sector	MFF provides an opportunity to have a platform for policy dialogue with the government and sector coordination with other DPs on a longer term basis.	Possible, but a standalone project loan can be affected by other development partners' support, while MFF will allow the government and ADB to adjust the approach based on the coordination with other partners.	MFF modality is preferred. An MFF modality will provide the necessary flexibility in handling institutional and coordination challenges.
5. Strategic-phased intervention in the transport sector	The MFF allows supporting the government to adjust implementation based on experiences and lessons to be learned in Tranche 1. Development of innovative approaches and rolling-out is possible. Sustainability will be ensured along with capacity development during the phased interventions.	Only short-time intervention is feasible.	MFF modality is preferred. RHD is implementing an institutional development action plan to improve its operational efficiency. Such initiatives could be adjusted for better roll-out for subsequent tranches.
6. Operational flexibility	MFF allows having more opportunities to review and adjust implementation plans during the implementation. New trends and innovations can also be applied to the subsequent tranches, particularly with respect to safeguards and climate change initiatives.	No flexibility is given, compared to the MFF.	MFF modality is preferred. Flexibility is needed for long-term sector development, to assist in coordinating with other DP programs.
7. Transaction costs and financial charges	MFF modality potentially reduces the transaction cost more than a standalone project in preparation for subsequent tranches and implementation.	A standalone project loan will usually incur higher commitment charges if such a large-scale project is to be financed.	MFF modality is preferred. The government will use its own resources to prepare the subsequent projects.

ADB = Asian Development Bank, CPS = country partnership strategy, COBP = country operations business plan, DP = development partner, EA = executing agency, MFF = multitranche financing facility, RHD = Roads and Highways Department.

Source: Asian Development Bank.

C. Approach of Time-Slice Financing

6. **Rationale**. The project will involve long-term contract packages for civil works, which includes a construction period of about 3 years, a defect-liability period of 1 year, and a performance-based maintenance period of 6 years. The contract model will require long-term engagement of contractors to ensure that the required level of services is provided by the project road. The contracts are packaged in relatively large size to invite adequate competition during procurement processes, and to engage qualified contractors in their specialized areas. Related consulting services will also be required for a longer term than the conventional construction contracts. ADB's financing approach needs to accommodate the longer contract period, and the financial resources should be used more efficiently.

7. **Time-slice financing.** It is proposed that a works package or a consulting services package will be contracted with ADB financing commitment provided on the demand basis by MFF tranches. For example, for a $100 million contract which is fully covered under the MFF including government financing, ADB provides $5 million commitment under the first periodic financing request (PFR), which will be followed further by ADB commitment on a series of subsequent PFRs in line with project implementation. The civil works will be packaged according to three principles:

(i) Civil works will be packaged according to the geographical areas to cover a section of 20 km to 30 km to utilize the capacity of qualified contractors on programming and coordinating the civil works.
(ii) Each contract will be at a reasonably large size, taking into account local and international markets, e.g., works could be referred to the past international competitive bidding contracts in the country.
(iii) Neighboring packages will be procured at the same time to allow large contractors to pursue economy of scale in implementation.

8. **Disbursement-based tranching.** The tranching schedule is based on the disbursement projection, which will minimize financing charges and improve the disbursement ratio under the investment program. Each tranche will finance slices of a group of contracts for civil works or consulting services. Each contract is sliced according to the indicative tranche schedule. The government has completed the preparation and due diligence for the entire project scope. The project cost is estimated at $1,672.6 million. Following the disbursement-based tranche plan, the government intends to request Tranche 1 of $300 million together with the facility to finance the first slice of the project. The amount of each tranche will be requested according to the disbursement progress and projection.

9. **Advantages.** The approach of time-slice financing and disbursement-based tranching will have the following advantages:

(i) More competition from contractors with high qualification and adequate capacity is expected due to larger contract packages.
(ii) Contract prices may decrease due to large contract size.
(iii) Quality of works will increase, as more experienced and larger international contractors participate.
(iv) Delays in project implementation can be reduced, as the contract for the overall section was awarded upfront and no additional procurement is required for further sections when processing subsequent PFRs.
(v) ADB's review for procurement can concentrate on large contracts upfront and less subsequent review of procurement activities is required, thus reducing the risk of delays during project implementation.

(vi) The Government of Bangladesh and the executing agency or implementing agency can avail of ADB financing when it is required according to the project schedule and actual progress, improving certainty of annual disbursement.

(vii) ADB can better plan allocation of scarce financial resources in accordance with the project progress rather than allocating a huge loan in the country program for 1 year at the time of approval of the project. The disbursement ratio will also be improved according to disbursement projection-based commitment.

(viii) Time-slicing allows better integration of cofinancing, as cofinancing agreements can be reached for any tranche individually. Other products such as grants or guarantees may be included for individual tranches as appropriate.

10. **Risks and measures.** Possible risks can be managed under the following measures shown in Table 2:

Table 2: Management of Risks

Risks	Mitigation Measures
Coordination of the follow-on financing	After the first submission of the IPC, annual disbursement will become predictable. Frequent review missions involving contractors will help plan preparation of the subsequent PFRs. A risk of delay in PFR approval can be mitigated by government counterpart financing.
Assurance of the follow-on financing	ADB board approval will have been provided for the overall facility with commitment of government financing. It is a matter of management consideration to provide the next PFR based on the performance of the ongoing PFR. This could provide more control on the ongoing PFR. A very marginal risk of ADB non-financing can be mitigated by provisions of the government commitment to the financing beyond ADB financing commitment.
Control of the size and the number of PFRs per contract	Each PFR will cover the financing at least for 1 year for all contracts appraised in the past PFR.

ADB = Asian Development Bank, IPC = interim payment certificate, PFR = periodic financing request.

D. Conclusion

11. A multitranche financing facility using the time-slice financing approach will be the most appropriate financing modality for the Bangladesh SASEC Dhaka–Northwest Corridor Road Project, Phase 2.