



Periodic Financing Request Report

Project Number: 44483-027
MFF Number: 0059
December 2015

Republic of Uzbekistan: Second Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program (Tranche 3)

This document is being disclosed to the public in accordance with ADB's Public Communications Policy 2011.

CURRENCY EQUIVALENTS

(as of 20 November 2015)

| | | |
|---------------|---|-----------------|
| Currency Unit | – | Uzbek sum (SUM) |
| SUM1.00 | = | \$0.000368 |
| \$1.00 | = | SUM2,712.130000 |

ABBREVIATIONS

| | | |
|-------|---|--|
| ADB | – | Asian Development Bank |
| CAREC | – | Central Asia Regional Economic Cooperation |
| FAM | – | facility administration manual |
| FFA | – | framework financing agreement |
| IEE | – | initial environmental examination |
| km | – | kilometer |
| LARP | – | land acquisition and resettlement plan |
| MFF | – | multitranche financing facility |
| OCR | – | ordinary capital resources |
| PFR | – | periodic financing request |
| PMU | – | program management unit |
| RAMS | – | road asset management system |
| RRF | – | Republican Road Fund |
| SPS | – | Safeguard Policy Statement |

NOTES

- (i) The fiscal year (FY) of the Government of Uzbekistan and its agencies ends on 31 December. FY before a calendar year denotes the year in which the fiscal year ends, e.g., FY2008 ends on 31 December 2008.
- (ii) In this report, "\$" refers to US dollars.

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10. Summary Feasibility Study and Detailed Engineering Design
11. Climate Risk Assessment and Management Report

TRANCHE AT A GLANCE

| 1. Basic Data | | Project Number: 44483-027 | |
|--|--|--------------------------------------|----------------------|
| Project Name | Second Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program (Tranche 3) | Department /Division | CWRD/CWTC |
| Country Borrower | Uzbekistan Republic of Uzbekistan | Executing Agency | Republican Road Fund |
| 2. Sector | Subsector(s) | ADB Financing (\$ million) | |
| ✔ Transport | Road transport (non-urban) | | 150.00 |
| | | Total | 150.00 |
| 3. Strategic Agenda | Subcomponents | Climate Change Information | |
| Inclusive economic growth (IEG) | Pillar 1: Economic opportunities, including jobs, created and expanded | Climate Change impact on the Project | Medium |
| Regional integration (RCI) | Pillar 4: Other regional public goods | | |
| 4. Drivers of Change | Components | Gender Equity and Mainstreaming | |
| Governance and capacity development (GCD) | Institutional development | No gender elements (NGE) | ✔ |
| Knowledge solutions (KNS) | Application and use of new knowledge solutions in key operational areas | | |
| Private sector development (PSD) | Public sector goods and services essential for private sector development | | |
| 5. Poverty Targeting | | Location Impact | |
| Project directly targets poverty | No | Regional | High |
| 6. Risk Categorization: Low | | | |
| 7. Safeguard Categorization Environment: B Involuntary Resettlement: B Indigenous Peoples: C | | | |
| 8. Financing | | | |
| Modality and Sources | | Amount (\$ million) | |
| ADB | | 150.00 | |
| Sovereign MFF-Tranche (Loan): Ordinary capital resources | | 150.00 | |
| Cofinancing | | 0.00 | |
| None | | 0.00 | |
| Counterpart | | 80.00 | |
| Government | | 80.00 | |
| Total | | 230.00 | |
| 9. Effective Development Cooperation | | | |
| Use of country procurement systems | | No | |
| Use of country public financial management systems | | No | |

TRANCHE AT A GLANCE

Date of Receipt by ADB of PFR: 18 July 2014

Tranche Number: 3

10. Country Operations Business Plan

CPS

<http://www.adb.org/documents/uzbekistan-country-partnership-strategy-2012-2016>

COBP

<http://www.adb.org/documents/uzbekistan-country-operations-business-plan-2012-2014>

11. Tranche Summary

The proposed Tranche 3 will lead to improved road connectivity, efficient transport system, and effective management for the Uzbekistan sections of the CAREC Corridor 2 Road. The outcome will be improved travel time and efficiency on the reconstructed A380 highway section. The outputs of Tranche 3 will be (i) approximately 87 km of reconstructed Uzbekistan section of CAREC Corridor 2 Road (between Km 228-Km 315 of A380 highway); and (ii) nonphysical components for supporting the implementation of the civil works and for continued capacity development. Nonphysical components for this tranche include continued capacity development for implementing and updating road asset management system, and project implementation support.

Impact and Outcome: The impact will be better connectivity, efficient transport system, and effective management for the Uzbekistan sections of CAREC Corridor 2 Road (Program-defined [approved MFF Facility Outcome statement, 21 April 2010]) The outcome will be improved travel efficiency on the reconstructed A380 highway section.

Outputs: (i) Km 228-Km 315 road section in A380 highway reconstructed, and (ii) Capacity for road asset management improved.

Implementation Arrangements: Republican Road Fund will be the executing agency.

Project Readiness: The government had completed the detailed design for the civil works component in 2012. In 2014, the government updated the bills of quantities to reflect the current prices. The bid documents for the component are being developed and will be ready by December 2015.

12. Significant Developments in the MFF and Previous Tranches

ADB approved a MFF for the Second CAREC Corridor 2 Road Investment Program on 23 August 2011 for an aggregate amount not exceeding \$500 million. The MFF aims to reconstruct Uzbekistan sections of the CAREC Corridor 2 on the A373 and A373/4R112 highways in the Fergana region, and A380 highway in the Bukhara region.

Tranche 1 amounting to \$130 million (OCR) was approved in September 2011 for rehabilitating 58 km of four lanes of the A373 highway. The implementation of the civil works contract under Project 1 is currently underway. As of 15 November 2015, implementation progress of the entire project is 67%. Contract awards are \$111.07 million (86%) and disbursements are \$82.05 million (63%). As of October 2015, the contractor completed about 49 km of one side of road, out of the 58 km of both sides. Due to several continued unresolved disputes, the civil works contractor applied for arbitration and issued a notice of termination of contract. Despite ADB's efforts at resolving the disputes, it appears that the contract will be terminated in December 2015 and alternative ways of completing the project will need to be explored.

Tranche 2 amounting to \$220 million (OCR) was approved in December 2012. The contract for construction supervision services has been awarded. The procurement of the civil works contract was delayed owing to rebidding caused by a substantial change in the scope of the works. In response to the government's request, ADB approved limited rebidding in October 2015. The RRF submitted draft bidding documents for limited rebidding in November 2015.

The requirements of the Framework Financing Agreement (FFA) and covenants of the loan agreement are being complied with. Under tranche 1, out of the 18 loan covenants, one has been complied, and the remaining 17 covenants are being complied. Under tranche 2, out of the 21 covenants, 15 are being complied, and the remaining six covenants are not yet due.

The RRF has assured that the issues faced by Project 1 and Project 2 will not affect the implementation of the proposed Project 3 since they are located in different geographic areas.

13. Milestones

Estimated Approval
30 November 2015

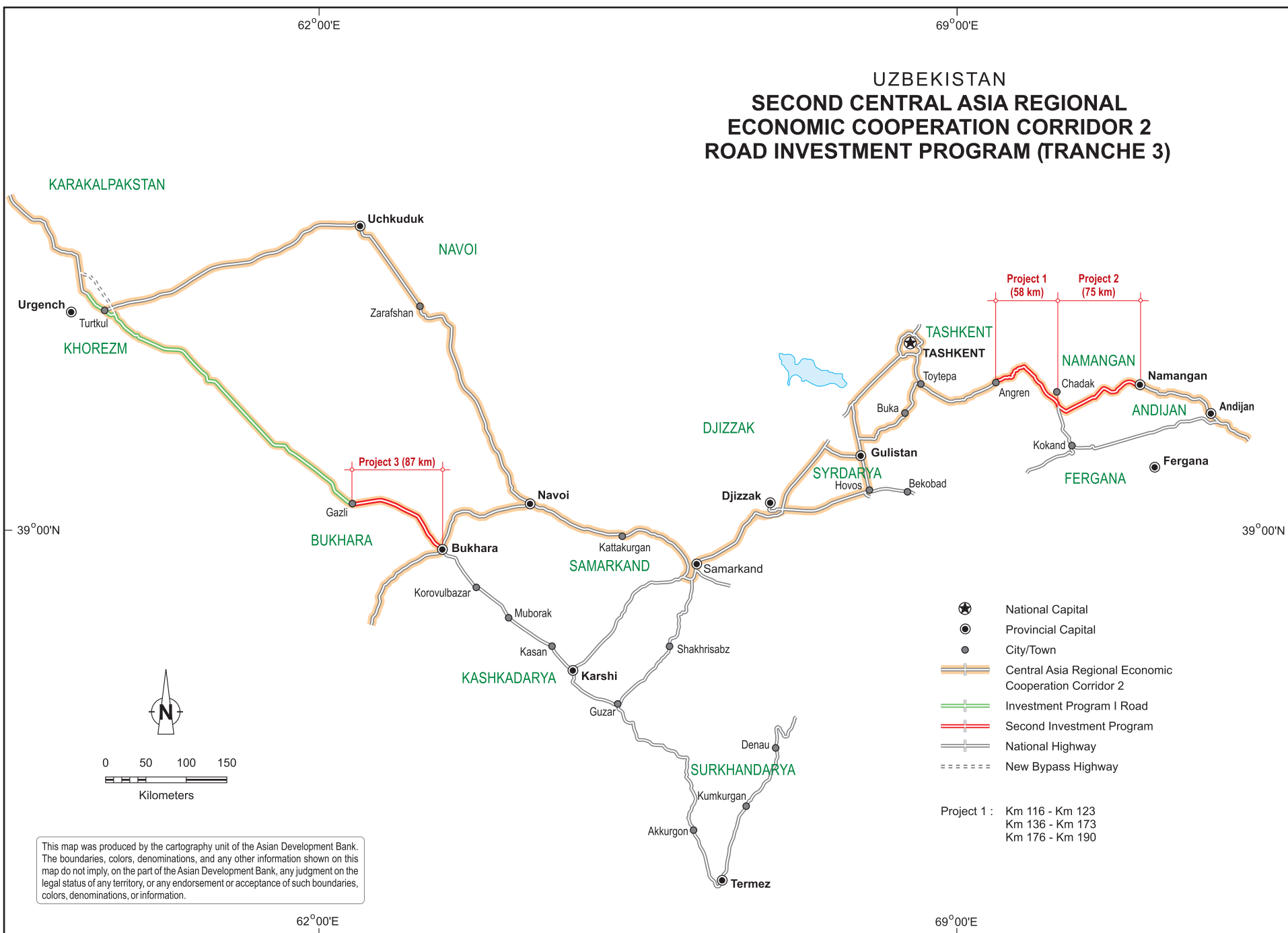
Estimated Effectiveness
30 January 2016

Estimated Completion^a
31 December 2017

14. Linked Documents

| | Required Document | Disclosure Date |
|-------------------------------|---|-----------------|
| (i) Environment | IEE - Initial Environment Examination | |
| Weblink: | http://www.adb.org/projects/documents/uzb-carec-corridor2-road-investment-progrm2-tranche3-may-2014-iee | 30 October 2014 |
| (ii) Involuntary resettlement | RP - Resettlement Plan | |
| Weblink: | http://www.adb.org/projects/documents/uzb-carec-corridor2-road-investment-progrm-p3-oct-2014-rp | 3 November 2014 |
| (iii) Indigenous peoples | | |
| Weblink: | | |

^a For Tranches, this refers to the financial closing date.



I. BACKGROUND

1. The Central Asia Regional Economic Cooperation (CAREC) promotes trade and the movement of people across Central and West Asia. Located in the middle of Central Asia, the Republic of Uzbekistan provides transit access across the region. The CAREC Transport and Trade Facilitation Strategy 2020 program includes priority investments for Uzbekistan amounting to \$4.2 billion.¹ On 23 August 2011, the Asian Development Bank (ADB) approved a multitranche financing facility (MFF) for the Second CAREC Corridor 2 Road Investment Program for a total of not more than \$500 million.² The CAREC Corridor 2 road connects Uzbekistan to Afghanistan, Kazakhstan, the Kyrgyz Republic, Tajikistan, and Turkmenistan.

2. The Republic of Uzbekistan and ADB signed a framework financing agreement (FFA) for the program on 4 July 2011. The Republican Road Fund (RRF) under the Ministry of Finance is implementing the program as the executing agency. The government submitted a periodic financing request (PFR) to ADB for a loan of \$150 million for the third project on 11 July 2014.³ The proposed project for the reconstruction of approximately 87 km of the A380 highway will provide the last mile connectivity between the two major urban economic centers of Urgench and Bukhara. In addition to regional cooperation benefits, this project will improve domestic trade and economic development by increasing the volume of traffic in the Bukhara region. It is also aligned with the country partnership strategy 2012–2016.

II. ASSESSMENT OF IMPLEMENTATION

A. Sector Policy, Strategy, and Road Map

3. The government's long-term vision for road development is to foster economic growth by (i) extending access to regional and world markets, (ii) improving exports with expansion of marketing outlets for sale of national products, (iii) increasing transit transportation, and (iv) ensuring the sustainability of the road subsector.⁴ Implementation of the sector roadmap and policy framework for the program is on track and in line with the government's infrastructure and road construction program (2015–2019).⁵ The policy framework, developed at the MFF approval stage, covers several actions for improving governance and accountability, road subsector sustainability, road safety and transport logistics.

4. Road reforms have progressed significantly since 2003, with the result that the subsector is more functional and rational, with improvements in areas of competence and responsibilities. Reforms include (i) unbundling by separating road transport operations and road construction, and creation of the RRF; (ii) restructuring Uzavtoyul, the road agency, and

¹ ADB. 2014. *CAREC Transport and Trade Facilitation Strategy 2020*. Manila.

² ADB. 2011. *Report and Recommendation of the President to the Board of Directors: Proposed Multitranchise Financing Facility to the Republic of Uzbekistan for the Second Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program*. Manila.

³ Processing of the PFR was delayed to enable the resolution of implementation issues related to the ongoing projects.

⁴ Republic of Uzbekistan. 2010. *Resolution No. 1446 of the President: "Accelerated Development of Infrastructure, Transport and Communication (2011–2015)"*. Tashkent. The construction program was extended from 2015 to 2019, by Resolution No. 2313 of the President of Uzbekistan dated 6 March 2015.

⁵ Republic of Uzbekistan. 2015. *Resolution No. 2313 of the President: "On the program of development and modernization of the engineering-communication and road and transport infrastructure for the period 2015-2019"*. Tashkent.

converting it to a state joint stock company⁶ with clear accountability targets; (iii) promoting competitive bidding for all road construction works; and (iv) establishing an independent quality control mechanism. A law on vehicular roads enacted in 2007 allows private sector financing for highway construction. ADB has promoted private road contracting industries with access to road equipment provided by the state-owned road equipment pool company created under the loan for ADB's CAREC Regional Road Project.⁷ A road asset management system (RAMS) development component was completed in July 2014 under Loan 2635.⁸

B. Assessment of Investment Program Implementation

5. **Tranche 1 (Loan 2772).** The loan agreement for tranche 1 amounting to \$130 million of ordinary capital resources (OCR) was signed on 1 December 2011 and became effective on 13 January 2012. In March 2014, ADB approved the government's request to extend the loan closing date from 31 March 2014 to 31 March 2015. In March 2015, ADB approved the government's request to extend the loan closing date further to 30 June 2016 to allow for the completion of the civil works. This first project comprises: (i) road development, or the reconstruction of approximately 58 km of the A373 highway; and (ii) road system sustainability comprising road safety management. Currently, the overall implementation progress of Project 1 is at 67%, across all the components of the project. As of 15 November 2015, \$82.05 million has been disbursed representing 63% of the loan amount. Disbursements were delayed by the poor performance of the civil works contractor. In December 2014, construction works were halted due to contractual disputes. In July 2015, the contractor and the RRF agreed that the subcontractor, Alliance Capital K/S, would complete the remaining works and construction resumed. As of October 2015, about 49 km of one side of road has been completed, out of the 58 km of both sides. Due to several continued unresolved disputes, ADB insisted that the contractor and the RRF establish a Dispute Board to provide an independent decision. However, the Dispute Board was not established. In October 2015, the RRF received a notification from the Secretariat of the International Court of Arbitration of the International Chamber of Commerce informing that the Secretariat had received a request for arbitration from the contractor and such arbitration is considered to have commenced on 1 April 2015. In November 2015, the contractor issued a notice of contract termination. ADB has made all efforts to bring the contractor and the RRF together in order to settle their disputes so that the project can be completed. Despite these efforts, it appears that the contract will be terminated in December 2015 and alternative ways of completing the project will need to be explored. The RRF has assured that the disputes on Project 1 will not affect the implementation of the subsequent tranches since they are located in different geographic areas.

6. Nonphysical investments under the program include a road safety component, comprising a consultancy services contract awarded in December 2013 and completed in October 2015. The MFF outcome indicators for road safety are likely to be achieved.

7. **Tranche 2 (Loan 2965).** The loan agreement for tranche 2 amounting to \$220 million of

⁶ Decree of the President of the Republic of Uzbekistan UP-3292 dated 19 August 2003 on improvement of the management system for construction and operation of common use roads.

⁷ 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).

⁸ ADB. 2010. *Periodic Financing Request Report for the Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program—Tranche 1*. Manila.

OCR was signed on 16 April 2013 and became effective on 15 August 2013. The outputs⁹ of tranche 2 will be (i) completion of the A373 highway section begun under tranche 1 (approximately 58 km)¹⁰ using additional financing for civil works, and (ii) reconstruction of approximately 75 km of the CAREC Corridor 2 road on the A373/4R112 highway. A substantial change in the scope of the road works caused by the construction of a new railway in the vicinity of the project delayed the procurement of the civil works contract, since the estimated cost increased significantly, the contract terms were changed, earlier bid documents no longer accurately described the actual situation, the bids that were received did not respond substantially to the modified contract scope, the final bills of quantities were inconsistent with those submitted by the bidders, and there was a risk of serious claims for cost and time overruns from the bidders. In November 2015, the government agreed to ADB's recommendation to rebid the civil works package, and the RRF submitted to ADB the draft bidding documents. The increased costs of civil works will be funded from unallocated loan funds and government counterpart funding. The construction supervision consultancy contract has been awarded. However, since the construction work has not started yet, the project completion will be delayed. The delayed procurement has resulted in this project being rated as an "actual problem." The government has indicated that it will request for an extension of the MFF availability period and the loan closing date to ensure project is completed. The project is expected to be on track after the contract is awarded and civil works implementation begins.

8. The RRF has assured that the issues faced under tranche 1 and tranche 2 will not impact the implementation of the proposed tranche 3 since (i) the projects are located in different regions; (ii) the capacity of the RRF is sufficiently strong to implement the new project in parallel to resolving the issues on the previous tranches; and (iii) the RRF has a sound track record of completing the CAREC Regional Road Project (footnote 8) and the first project under CAREC Corridor 2 Road Investment Program (footnote 9).

C. Compliance

9. **Compliance with the framework financing agreement undertakings and loan covenants.** The requirements of the FFA are being complied with, including (i) a sector roadmap, policy framework, road investment program, and road safety component; (ii) design and monitoring framework targets; (iii) an implementation framework; (iv) selection criteria and an approval process for subsequent tranches; (v) safeguard requirements and social development policies; and (vi) the loan agreement undertakings and covenants. All ten of the undertakings mentioned in Schedule 6 of the FFA are being complied with, and the individual loan covenants are either already complied with or not yet due. Details of these covenants are provided in the PFR submitted by the government. The compliance with loan covenants is satisfactory. Under tranche 1, out of the 18 loan covenants, one has been complied, and the remaining 17 covenants are being complied. Under tranche 2, out of the 21 covenants, 15 are being complied, and the remaining six covenants are not yet due.

10. **Safeguards Compliance.** The civil works under Project 1 do not involve land acquisition or involuntary resettlement, or affect ethnic minority groups. The project is category C for

⁹ As per the Report and Recommendation of the President to the Board of Directors for the Second CAREC Corridor 2 Road Investment Program, Tranche 2 will cover the reconstruction of 87 km of the A380 highway (between Km 228 and Km 315). However, due to the change in the government's priorities, the project's implementation was postponed. The government had prioritized the reconstruction of the A373/4R112 highway, having moved it from tranche 3 to tranche 2. Hence, the A373/4R112 was funded under tranche 2.

¹⁰ The 58 km section of the A373 highway comprises Km 116–Km 123 (7 km), Km 136–Km 173 (37 km), and Km 176–Km 190 (14 km).

involuntary resettlement and impact on indigenous people. It is classified as environment category B. The RRF has submitted environmental management plan including a site management plan and will continue monitoring the environment impact. The RRF reported minor environmental issues, which the contractor is in the process of resolving.

11. The Project 2 is category A for involuntary resettlement. The land acquisition and resettlement plan (LARP) was disclosed on 20 November 2012 and is currently being implemented with about 90% of the affected persons having received compensation. The submission of LARP monitoring report has been delayed owing to ongoing replacement of the local social safeguards expert. ADB's safeguards specialist and project team leader are closely monitoring the LARP implementation. No road construction work has been initiated on the project site yet. An External Monitor was appointed in December 2013. The External Monitor's contract was terminated in October 2015 due to health reasons. The RRF is in the process of recruiting a new External Monitor. The project is category B for environment and the draft initial environmental examination (IEE) was posted on ADB's website on 12 November 2012.

III. PERIODIC FINANCING REQUEST

A. Impact and Outcome

12. The proposed tranche 3 will lead to better road connectivity, efficient transport system, and effective management of the Uzbekistan sections of the CAREC Corridor 2 road. The outcome will be improved travel time and efficiency on the reconstructed section of the A380 highway.

B. Outputs

13. The outputs of tranche 3 will be (i) the reconstruction of approximately 87 km of the CAREC Corridor 2 road in Uzbekistan (between Km 228 and Km 315 on the A380 highway); and (ii) nonphysical components to continue capacity development and to support implementation of the civil works. The reconstructed highway section will comprise four lanes of cement concrete road pavement. The continued capacity development activities will include implementation and updating of the RAMS. The costs of auditing the project financial statements will be financed under the proposed loan.

C. Investment and Financing Plans

14. Tranche 3 is estimated to cost \$230 million, inclusive of taxes, physical and price contingencies, and interest charges on the loan during construction (Table 1).

Table 1: Tranche 3 Investment Plan (\$ million)

| Item | Amount ^a |
|---|---------------------|
| A. Base Cost | |
| 1. Reconstruction of 87km of the A380 highway ^b | 212.15 |
| 2. Nonphysical components ^c | 2.60 |
| Subtotal (A) | 214.75 |
| B. Contingencies^d | 11.90 |
| C. Financing Charges during Implementation^e | 3.35 |
| Total (A+B+C) | 230.00 |

km = kilometer.

- ^a In 2014 prices.
- ^b Includes (i) civil works (\$176.00 million), (ii) construction supervision consulting services (\$3.50 million), (iii) land acquisition and resettlement costs (\$1.50 million), and (iv) taxes and duties (\$31.15 million). The government will finance (i) part of the civil works; (ii) land acquisition and resettlement costs, and (iii) taxes and duties.
- ^c Includes (i) consulting services for capacity development for the RAMS component (\$0.4 million); (ii) procurement, safeguards, and contract management (\$0.9 million); (iii) a financial auditor (\$0.1 million); and (iv) recurrent costs (\$1.2 million). Recurrent costs will be financed under tranche 3 and cover expenses related to program management unit (PMU) staff salaries, operational expenses, travel, training, computers, software, office furniture, office equipment and spares, and other eligible expenditures, in line with the Operations Manual, Section H3/OP, para. 10. ADB financing of these costs is justified because the PMU has been set up to manage all of the program tranches.
- ^d Physical contingency is estimated at about 3% of the total base cost. Price contingencies are estimated following ADB's cost escalation factors, including provision for potential exchange rate fluctuation under the assumption of a purchasing power parity exchange rate.
- ^e Includes interest and commitment charges since tranche 3 is funded by an OCR loan. The government has opted not to capitalize interest and other charges during construction.
- Source: Asian Development Bank estimates.

15. The government has requested a loan of \$150 million from ADB's OCR to help finance the project. The loan will have a 24-year term, including a grace period of 4 years, a straight line repayment method, an annual interest rate determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility, and a commitment charge of 0.15% per year (the interest and other charges during construction will not be capitalized in the loan). Based on this, the average loan maturity is 14.25 years and the maturity premium payable to ADB is 0.10% per annum. The loan will have such other terms and conditions as are set forth in the draft loan agreement. The financing plan for tranche 3 is in Table 2.

Table 2: Financing Plan for Tranche 3

| Source | Amount (\$ million) | Share of the Total |
|------------------------------|--------------------------------|-------------------------------|
| Asian Development Bank (OCR) | 150.0 | 65% |
| Government of Uzbekistan | 80.0 | 35% |
| Total | 230.0 | 100% |

OCR = ordinary capital resources.

Source: Asian Development Bank estimates.

D. Implementation Arrangements

16. The RRF will be the executing agency for all the tranches of the program. The RRF has conducted civil works procurements under ADB-assisted projects following ADB's Procurement Guidelines (2015, as amended from time to time). The PMU will help the RRF implement all of the tranches.¹¹ The PMU's procurement capacity will be supplemented by an international individual procurement consultant who will support all procurement-related activities under the program. The construction supervision consultants will assist the RRF and PMU during implementation. The facility administration manual (FAM) as updated periodically will be an integral project document. It includes the administrative and management requirements and procedures necessary to implement the project on time and within budget. It also includes URL links to all available templates and instructions. The loan proceeds will be disbursed in

¹¹ PMU expenses will be financed as recurrent costs. To pay expenses related to recurrent costs, the Road Fund will establish a separate imprest account for the proposed tranche at a commercial bank in accordance with ADB's *Loan Disbursement Handbook*. This is consistent with the arrangements for the previous tranches under the program.

accordance with ADB's *Loan Disbursement Handbook* (2015, as amended from time to time).

17. The current expanded PMU will continue to help the RRF implement the third project efficiently by offering assistance in the areas of (i) project management and procurement; (ii) finance and administration; and (iii) evaluation, monitoring, compliance, and reporting. The PMU will (i) establish a project performance monitoring system within six months from the loan effectiveness date, and (ii) collect baseline data for performance monitoring. The implementation arrangements are summarized in Table 3 and described in detail in the updated FAM. The FAM also provides the procurement plan for goods, works, and consulting services.

Table 3: Implementation Arrangements

| Aspects | | Arrangements | |
|--|-----------------------------------|--|---------------|
| Implementation period | | January 2016–November 2017 | |
| Estimated project completion date | | 30 November 2017 (loan closing date of 31 December 2017 to be extended after extension of MFF availability period) | |
| Management | | | |
| (i) Executing agency | | Republican Road Fund | |
| (ii) Implementation unit | | Program Management Unit, Tashkent (12 staff) | |
| Procurement | International competitive bidding | 1 civil works contract | \$176 million |
| Consulting services | QCBS | 474 person-months | \$3.5 million |
| | Individual | 73 person-months | \$1.3 million |
| | LCS | Lump sum contract (financial audit) | \$0.1 million |
| Retroactive financing and/or advance contracting | | Retroactive financing not exceeding \$1.3 million is requested for consulting services costs incurred before the date of loan effectiveness but not earlier than 12 months before the signing of the legal agreement. Advance contracting for civil works and consulting services is also requested. | |
| Disbursement | | The loan proceeds will be disbursed in accordance with ADB's <i>Loan Disbursement Handbook</i> (2015, as amended from time to time) and detailed arrangements agreed upon between the Government of Uzbekistan and ADB. | |

ADB = Asian Development Bank, LCS = least cost selection, MFF = multitranché financing facility, QCBS = quality- and cost-based selection.

Source: ADB estimates.

18. The proposed tranche 3 loan is currently scheduled to close on 31 December 2017, with the MFF availability period ending on the same date. Since this period could be insufficient during implementation, a separate approval will be requested to extend the MFF availability period and the loan closing date. A confirmation to this effect was provided by the Borrower during loan negotiations and included in the minutes of loan negotiations.

19. About 108 person-months of international and 366 person-months of national consulting services from an international firm are required to supervise civil works construction on ADB-financed road sections. In addition, an international individual procurement consultant (20 person-months), an international individual RAMS specialist (15 person-months), an international individual contract management specialist (18 person-months), and two national individual safeguards specialists (environment–10 person-months and social–10 person-months) will be recruited. All consultants will be recruited and engaged according to ADB's Guidelines on the Use of Consultants (2013, as amended from time to time) and the project procurement plan. Consulting firm will be selected and engaged using the quality- and cost-based selection method (90:10 ratio), and full technical proposals for the construction supervision package will be solicited. Preference for key positions in the consultant team will be

given to the consulting firm's permanent staff. The consultants will be required to report to both the RRF and ADB.

E. Project Readiness

20. The detailed design has been completed and approved by the government, and poses a minimal risk of delay. The PMU is fully functional and comprises technical, procurement, financial, monitoring, reporting, and safeguards specialists. To ensure the smooth implementation of the program, in 2013, the PMU was expanded to include eight new staff: a deputy director, financial management specialist, accountant, engineer, procurement expert, monitoring specialist, office manager, and interpreter. The RRF intends to issue the bid documents for civil works and consulting services in December 2015. Since the project will only impact five households, land acquisition is not expected to be an issue. ADB has reviewed the draft IEE and LARP, and both documents have been disclosed on ADB website.

F. Advance Contracting and Retroactive Financing

21. Retroactive financing not exceeding \$1.3 million is requested for costs of consulting services incurred before the date of loan effectiveness but not earlier than 12 months before the signing of the legal agreement. Retroactive financing will not be applicable to civil works. The government has requested an advance action to procure civil works and services. The RRF has been informed that, by approving the advance action, ADB does not commit to providing financing.

IV. DUE DILIGENCE

A. Technical

22. Technical due diligence was carried out for the project. The feasibility study and detailed design for road improvement is based on similar design parameters developed for the first project using cement concrete road pavement. The original detailed design for the third project was updated in 2014 and has been approved by the State Committee of Architecture and Construction. Bills of quantity have been prepared and included in the bidding documents. The due diligence for the RAMS component was carried out during the implementation of the recently completed CAREC Corridor 2 Road Investment Program–Project 1.¹²

B. Economic and Financial

23. Implementing the project will contribute to the envisaged benefits of the improved transport corridor, including higher travel speeds, lower operating costs, and improved road safety standards. Based on ADB's Guidelines for the Economic Analysis of Projects, the project was evaluated as economically viable with an estimated economic internal rate of return of 14% and a net present value of \$29.4 million, based on a 12% discount rate. A financial analysis concluded that expenditure on routine and periodic road maintenance has been increasing at an average annual rate of 60% since 2010, and currently forms about 22% of the RRF's annual expenditure. Incremental expenditure caused by the proposed project road is expected to average about \$0.8 million per year (in 2013 prices) during 2017–2036. Based on the current increase in the budget allocations, it is highly likely that the government will allocate sufficient funds for overall road maintenance.

¹² ADB. 2015. *Completion Report: Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program (Tranche 1)*. Manila.

C. Governance

24. The RRF has allocated additional staff for financial management, procurement, and technical supervision within the PMU. Regular training workshops will be necessary to ensure that the new staff are trained in good governance practices, especially relating to financial management and procurement. In 2014, a financial management reassessment of the RRF's capacity carried out by ADB found that the RRF and PMU have a satisfactory financial management capability to (i) record required financial transactions and balances, (ii) provide regular and reliable financial statements and monitoring reports, and (iii) safeguard their financial assets. Nevertheless, ADB rated the overall financial management risk as *substantial* and recommended several actions, which are currently being implemented. Inherent risk was assessed as *substantial*, and control risk as *moderate*. In 2014, ADB staff carried out a procurement capacity reassessment, which found the current capacity of the RRF and PMU to be adequate. The overall risk rating was *high*. Recommendations from the assessment are currently being implemented.¹³ These ratings are based on (i) weak public procurement legislation, (ii) the risk of contract changes caused by the contract registration system of the Ministry of Foreign Economic Relations Investment and Trade, and (iii) the need for the Ministry of Finance and RRF level to ensure the timely disbursement of counterpart funds.

25. ADB's Anticorruption Policy (1998, as amended to date) was explained to the government and the RRF. Consistent with its commitment to good governance, accountability, and transparency, ADB reserves the right to investigate, directly or through its agents, any alleged corrupt, fraudulent, collusive, or coercive practices relating to the project. To support these efforts, relevant provisions from ADB's Anticorruption Policy are included in the project loan agreement and bidding documents. In particular, all contracts financed by ADB will include provisions specifying ADB's right to audit and examine the records and accounts of the RRF and all contractors, suppliers, consultants, and other service providers relating to the project. The specific policy requirements and supplementary measures are described in the FAM.

D. Poverty, Social, and Gender Dimensions

26. The project site is located in the Bukhara region in the southern part of the country and traverses four districts: Bukhara, Jondor, Peshku, and Romitan. A socioeconomic survey carried out along the project road section indicated an average household size of five persons. Males and females constitute nearly equal portions of the affected population, with 51% of men and 49% of women found to be educated. Apart from business (small businesses and enterprises) and government employment, agriculture is a key source of income for the affected households. The majority of the households have access to potable water, toilets, bathrooms, electricity, and means of communications such as mobile phones. The program will not directly reduce household poverty or provide specific services that address the geographic determinants of poverty. Since no specific gender intervention is planned, the project is classified as 'no gender elements'.

E. Safeguards

27. **Environment Impact.** The project is category B for environment. The RRF prepared an

¹³ ADB is supporting the capacity development exercise through TA-8665-REG: Strengthening the Capacity and Integrity of Procurement Processes in Central and West Asia. In addition, an International Federation of Consulting Engineers contract management workshop was held in Uzbekistan from 28 to 30 October 2014 on "Enhancing Procurement and Contract Management Capacity" with the participation of the Operations Services and Financial Management Department.

IEE that complies with the requirements of ADB's Safeguard Policy Statement (SPS) 2009. Public consultations, including public hearings in two locations along the road section, were held on 28 May 2014. The English version of the draft IEE was posted on ADB's website on 30 October 2014. The IEE found no major negative potential impacts from the proposed project. The IEE found that (i) no negative environmental impact is associated with the project location; and (ii) environmental impacts associated with construction will be minimized by proper implementation of the proposed mitigation measures. The IEE also found that operational environmental impacts such as noise and vehicle emissions will be mitigated and addressed by the government's existing pollution control program, which will be closely coordinated with and monitored by the State Committee for Nature Protection. Effective implementation of the environmental management plan will minimize and mitigate any adverse impacts during project implementation. The tender and contract documents will contain details of the environmental management and monitoring requirements to be carried out by the contractor. After completion, traffic is likely to increase, causing a rise in greenhouse gas emissions. However, the amount of incremental emissions is not significant as defined in the SPS 2009. A climate risk screening exercise carried out using geographic data concluded that the project faced a medium risk of flooding, which is mitigated in the road design. The government's strong environmental monitoring and mitigation system ensures the sound management of environmental impacts.

28. Land Acquisition and Resettlement. The project is category B for involuntary resettlement. Based on the findings of the census carried out along the road section in October 2014, the RRF prepared a draft LARP that includes the information required by the SPS 2009 and follows the land acquisition and resettlement framework. Consultations with the affected persons were carried out in April, May, and August 2014. An estimated total of 0.05 hectares of land will be acquired and five households located in the Bukhara and Romitan districts will be affected. The draft LARP estimates the cost of land acquisition and resettlement at \$188,597.30, which the current land acquisition budget can cover. The draft LARP was disclosed to the affected persons during October–November 2014 and posted on ADB's website on 3 November 2014. The RRF has in-house capacity to implement resettlement plans based on Uzbek law. To develop capacity in implementing ADB's Safeguards Policy, a national social safeguards consultant will be appointed to work closely with the PMU. The ADB safeguards specialist will help PMU staff implement the LARP efficiently.

29. Indigenous Peoples Impact. The project is category C for indigenous peoples, as defined under the SPS 2009.

F. Risks and Mitigating Measures

Table 4: Summary of Risks and Mitigating Measures

| Risks | Mitigating Measures |
|--|---|
| Public financial management. Weak country level public financial management. Inadequate allocation of funds for road maintenance and low capacity for maintenance planning. | ADB is supporting the government in implementing financial reforms through an ongoing loan. ¹⁴ ADB's assistance in improving the RAMS is mitigating this risk. The government has provided assurance in loan agreement that it will prepare a road maintenance plan by 2018 using the RAMS for international road corridors. The budget allocation has been increasing steadily over the last three years. ¹⁵ |

¹⁴ ADB. 2007. *Report and Recommendation of the President to the Board of Directors: Proposed Loan to the Republic of Uzbekistan for the Public Finance Management Reform Project*. Manila. (Loan 2338-UZB for \$20.7 million approved on 28 June).

¹⁵ The road maintenance allocation was 234.4 billion sum (\$86.42 million) in 2011, 452.2 billion sum (\$166.73 million) in 2012, and 720.5 billion sum (\$265.66 million) in 2013. In addition, ADB is working with Uzavtoyul to improve its maintenance planning and allocation system.

| Risks | Mitigating Measures |
|--|--|
| | The Uzbekistan President's Resolution identified adequate maintenance of the road network as one of the main tasks for the development of public roads in Uzbekistan. ¹⁶ |
| Procurement. Delays in procurement caused by contract registration and price verification procedure delay contract effectiveness, and could lead to delays, increased costs, and increased claims from contractors. | The lengthy contract registration process is being mitigated by continuous dialogue at various levels among ADB, the RRF, and the Ministry of Foreign Economic Relations, Investment and Trade. |
| Implementation delays. Poor contractor performance combined with delays by the Road Fund in complying with its obligations. | ADB and the RRF will closely supervise the contractors' performance to minimize delays. The Road Fund will resolve issues contributing to implementation delays, such as customs clearance of equipment and materials, by taking proactive measures such as seeking government permission to import these goods duty free at an early stage. |

ADB = Asian Development Bank, RAMS = road asset management system, RRF = Republican Road Fund

Source: ADB estimates.

30. The integrated benefits and impacts of the project are expected to outweigh the costs.

G. Risk Categorization

31. The project is categorized as *low risk* since (i) the loan amount does not exceed \$200 million, (ii) ADB has a sound record of previous experience in the transport sector in Uzbekistan, (iii) the capacity of the executing agency in terms of externally financed project administration is reasonable, and (iv) the safeguards classification is not category A. The RRF has a good record of successfully completing two projects funded by ADB and is efficiently implementing two more projects currently under the CAREC Corridor 2 Road Investment Program. The issues with tranche 1 and tranche 2 are exceptional in nature and do not necessarily reflect the capacity of the RRF.

V. ASSURANCES

32. The government has assured ADB that the project implementation 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. The government has agreed with ADB on certain covenants for the project, which are set forth in the loan agreement. The government has also affirmed that it will prepare a road maintenance plan by 2018 using the RAMS for international road corridors and will provide for the maintenance of these roads in the 2019 annual budget.

VI. RECOMMENDATION

33. Pursuant to the request of the Republic of Uzbekistan dated 11 July 2014, and on the basis of the approval by ADB's Board of Directors for the provision of loans under the multitranchise financing facility in an aggregate principal amount not exceeding the equivalent of \$500,000,000 to the Republic of Uzbekistan for the Second Central Asia Regional Economic Cooperation Corridor 2 Road Investment Program, it is recommended that the President approve the proposed tranche as described in para. 15 of this report and the draft loan agreement for the proposed tranche in the form attached to this report.

¹⁶ Republic of Uzbekistan. 2006. *Resolution No. 535 of the President dated 20 December 2006*. Tashkent. http://www.lex.uz/pages/GetAct.aspx?lact_id=1097936