**PROJECT INFORMATION DOCUMENT (PID)**
**APPRAISAL STAGE**

Report No.: AB1112

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|---|---|
| **Project Name** | Inner Mongolia Transport (and Trade Facilitation) |
| **Region** | EAST ASIA AND PACIFIC |
| **Sector** | Roads and highways (90%); Sub-national government administration (10%) |
| **Project ID** | P068752 |
| **Borrower(s)** | PEOPLE'S REPUBLIC OF CHINA |
| **Implementing Agency** | Inner Mongolia Communications Department |
| **Environment Category** | [X] A [ ] B [ ] C [ ] FI [ ] TBD (to be determined) |
| **Safeguard Classification** | [ ] $S_1$ [X] $S_2$ [ ] $S_3$ [ ] $S_F$ [ ] TBD (to be determined) |
| **Date PID Prepared** | September 14, 2004 |
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| **Date of Board Approval** | December 16, 2004 |

## 1. Country and Sector Background

The strategic objectives for China according to the World Bank's Country Assistance Strategy (CAS) of November 2002 are to:

- Improve the investment climate;
- Accelerate the transition to a market economy;
- Address the needs of disadvantaged groups and underdeveloped regions; and
- Facilitate a more sustainable development process.

In this strategic context, the CAS recommends Bank intervention in the following areas of the transportation sector:

- Financing economic infrastructure in key growth corridors, including seaport and external trade corridors and corridors serving western provinces; and to reduce inter- and intra-regional development disparities.

- Financing infrastructure to serve poorer communities, thereby improving productivity in rural areas; and

- Facilitating the development of institutions necessary for managing the infrastructure network and planning in China's rapidly growing market economy.

Exports have played an important role in China's strong economic growth in recent years. However, because internal transport costs are high, coastal provinces have benefited more from this growth than have inland provinces. Costs are high in part because of distance, but also because of inefficient or inappropriate pricing and weak intermodal logistics. If inland provinces are to have a meaningful share of China's booming export trade, access to these provinces must improve, and constraints on the transportation of goods must be overcome.

## 2. Objectives

*Development objective*. The main objective of the project is to promote and sustain the development of China's cross-border trade between China on one hand and Russia and Mongolia on the other by improving transport infrastructure and logistics. These improvements, in turn, will lower transport costs, increase income from external trade, and raise incomes in Inner Mongolia, the country's third-largest province and one of the poorest provinces of the western region.

*Key performance indicators*. The principal outcome or impact indicators selected for monitoring progress in achieving the project development objective are:

- *For the Hailar-Manzhouli Highway (HMH) and the Border Roads for Trade (BRFT) components*:

— Traffic time (projected to be reduced by at least 50% after HMH completion)
— Traffic volume, especially of trade cargo (projected to increae by 100% after HMH completion)
— Cargo diversion rate from the overburdened rail mode of transport (projected at at least 10%)

- *For the Cargo Transfer Terminal (CTT)* - volume of cargo passing through the CTT (projected to increase by factor of four by 2008).

- *For the Institutional Strengthening and Training (IST) component* - improvement in efficiency and capacity of local governments to manage the HMH and BRFT infrastructure facilities and promote border trade, measured in numbers of staff trained who remain in the jobs for which they received training (projected at at least half those trained).

Besides investment in transport links to Russia and Mongolia and expanding highway network capacity in the relatively poor northeastern corridor of Inner Mongolia, the main challenge of the project is to strengthen institutional capacity and policy development capability in logistics for trade between China on one hand and Russia and Mongolia on the other. Technical assistance will be provided to help setting a foundation for further capacity improvement of Inner Mongolia, particularly Hulunbeier League, to plan, facilitate, and expand international trade.

The proposed project is designed with the clear objective of maximizing the use of transport infrastructure to promote international trade through Inner Mongolia in general and Hulunbeier League in particular. It will help accelerate the general development of Hulunbeier League, preparing it to cope with the increasingly important role the central government has assigned to it to be the country's main contact point for trading with Russia. In so doing, the project aims to: (i) improve the capacity of transport infrastructure and network planning to handle the significant increase in the volume of international freight traffic along China's northeastern border; (ii) develop a freight transfer and trade facilitation program to meet the growing demand for cross-border trade; and (iii) provide technical assistance to the Inner Mongolia Communications Department (IMCD) and Hulunbeier to build their capacity to plan, facilitate, and manage increasing demand for transportation of international trade traffic.

## 3. Rationale for Bank Involvement

The roles of the cities of Manzhouli and Hailar have increased in importance as trade between China and its neighbors expands in this era of trade liberalization and globalization. Border trade between China and Russia has been growing at about 20 percent per year for the past 4–5 years, although from a relatively low base. Trade statistics in 2002 showed about 10 million tons of freight moved between the two countries—9 million by rail and 1 million by road. At estimated growth rates of 20 percent for the next five years and 10 percent for the subsequent five years, the trade volume is expected to reach 30 million tons by 2009 and 42 million tons by 2013. With such a significant increase in trade volume expected,

serious consideration must be given now to investment in transport links and facilities to move and handle cargo in Hulunbeier.

Manzhouli, as a result of the blossoming of trade between China and Russia, has become the second-largest international land port in China after Shenzhen (near Hong Kong). Despite its importance, it is essentially a border checkpoint and has no cargo terminal except for some private facilities belonging to large importers and exporters. Small shippers and traders that do not have their own premises need common loading and unloading facilities.

Furthermore, Russian trucks, which carry about 90 percent of cargo crossing the border by road, are not permitted in Chinese territory beyond Hailar; cargo for destinations beyond Hailar has to be carried by Chinese trucks. A terminal for transferring cargo between Russian and Chinese trucks and between modes (road and rail), and for distributing and consolidating cargo in the Hulunbeier area, is necessary for promoting trade.

**Trade and Transport in Hulunbeier, Inner Mongolia**

Hulunbeier has a total land area of 253,000 sq. km (80 percent the size of Vietnam), but with a population of only 2.7 million, it is one of the most thinly populated areas of China. However, it is strategically important because of its long border with Russia (1,048 km) and Mongolia (676 km). It has five border crossings with Russia and two with Mongolia. All but one of the border crossings are seasonally open with bilateral arrangement. The exception, the Manzhouli crossing, was upgraded in 1996 to function as an international land port. Currently about 60 percent of trade between China and Russia passes through the land port of Manzhouli. Russian trucks are allowed to travel about 200 km into China from Manzhouli to Hailar (capital of Hulunbeier League), while Chinese trucks are allowed to travel 500 km into Russia from the Zabaykal'sk checkpoint across from Manzhouli. The Russians and the Chinese recently have negotiated a reciprocal deal and the Chinese have agreed to prepare road and freight transfer facilities in the next 1–2 years so that Russian trucks can travel 500 km into China. Imports from Russia to China consist of mainly raw materials— timber and minerals—while exports to Russia are agricultural and consumer goods. Hulunbeier's economy relies heavily on this foreign trade, which makes up about 40 percent of Inner Mongolia's foreign trade. The following table summarizes a few key features of Hulunbeier's economy.

| | China | Inner Mongolia | Hulunbeier | Inner Mongolia Compared to China | Hulunbeier Compared to Inner Mongolia |
|---|---|---|---|---|---|
| Land area (1,000 km2) | 9,600 | 1,183 | 253 | 12% (country's third-largest) | 21% |
| Population (million) | 1,285 | 23.78 | 2.68 | 2% of total (ranks 23rd) | 11% |
| Population density (pop/km2) | 134 | 20 | 11 | Ranks 28th | |
| GDP per capita (RMB in 2002) | 8,184 | 7,230 | 7,051 | Ranks 15th (12% below national average) | Close to Inner Mongolia average |
| Highway network (km) | 1,820,000 | 72,673 | | Has 4% of country's network | |
| Road density (km/1,000km2) | 190 | 61.4 | | One-third national average | |
| Total import and export (RMB billion) | | 24.64 | 10.68 | | Contributes 43% of foreign trade of Inner Mongolia |
| Proportion of import and export to GDP | | 14.3% | 56.6% | | Economy relies heavily on foreign trade. |

The CAS identifies the strengthening of regional integration and competitiveness through a well-functioning transportation system as a key objective in the transport sector. The project will help meet the sector-related CAS objectives of facilitating trade (domestic and international), improving regional and market integration, and fostering the development of western regions, whose development lags behind that of coastal areas. One of the critical features of the proposed project is the expansion of the transport route between China and Russia. As a multilateral organization, the Bank has the unique capacity to liaise with other countries across the border and is in a good position to advise China on this critical undertaking.

## 4. Description

The project includes the following components:

- *Component 1—Hailar–Manzhouli Highway.* Expansion of highway capacity by upgrading or constructing about 177 km of HMH. The component is estimated to cost about US$172 million, of which US$70 million will be financed by the World Bank;

- *Component 2—Border Roads for Trade.* Upgrading and rehabilitation of about 413 km of the highway network, sections identified either as key links for international trade facilitation at smaller border crossings with Russia and Mongolia, or as critical missing links in the highway network. The component aims to improve transport access to four other seasonal land ports between China and Russia and China and Mongolia. The component is estimated to cost about US$51 million, of which US$18 million will be financed by the Bank.

- *Component 3—Cargo transfer terminal and trade facilitation program.* Development of facilities and trade regime designed mainly for China's import and export trade with Russia and Mongolia, but also meeting the requirements of potential trade in transit shipped through Chinese seaports to other countries. The primary purpose of the CTT is to facilitate the consolidation, distribution, and trucking of cargo. The component is composed of: (i) construction of a transfer station in Hailar housing facilities for transferring cargo between transportation modes (rail and road) and between Chinese and Russian trucks as well as for warehousing; and (ii) carrying out of a diagnostic study on measures to promote cross-border trade between China and its land-locked neighbors. The study could later form a foundation to further improve a process for the quick and convenient inspection and clearance of cargo by customs and quarantine authorities; and to develop an internationally accepted trade documentation and practices for importers and exporters, transportation carriers, banks, and insurance companies. The component is estimated to cost about US$26 million, and will be financed locally.

- *Component 4—Institutional strengthening and training.* Various technical assistance and training aiming to improve the quality of development zone planning, trade promotion, and transportation efficiency, as well as project management, environmental monitoring, and supervision of highway construction. The component is estimated to cost about US$1.2 million and will be financed by the Bank.

## 5. Financing

| Source: | ($m.) |
|---|---|
| BORROWER | 162.66 |
| INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | 100 |
| Total | 262.66 |

## 6. Implementation

Technically, IMCD has overall responsibility for project preparation and implementation. It will be directly responsible for formulating, implementing, and managing the project. However, administratively, the local government of Hulunbeier has responsibility for making local arrangements related to environmental safeguards, land acquisition, and resettlement arrangements for project-affected people. A project management office has been established in the Hulunbeier branch of the IMCD in Hai Man (the HMPMO), headed by a deputy director general of IMCD and co-chaired by the mayor of Hulunbeier. The HMPMO will assume overall implementation and coordination responsibility for all components and every aspect of the project.

The CTT component will be developed and operated in the first instance by the Hulunbeier government. Depending on demand, various facilities in the terminal may be leased and operated by the private sector.

The project will be implemented 2004–2009. Overall direction of the project at the central level rests with MOC in Beijing. The Bank loan will be lent to the borrower, the Ministry of Finance (MOF), which will on-lend the loan proceeds to Inner Mongolia.

## 7. Sustainability

The strong commitment of the central, provincial, and local Hulunbeier governments to the project is the main indication of the sustainability of the project. Furthermore, the project has national importance because it is part of the State Council's plan to expand border trade with Russia through the Hailar–Manzhouli corridor. For their parts, MOC and the government of Inner Mongolia already have approved RMB 790 million and RMB 500 million, respectively, as the state and provincial contributions to the project.

## 8. Lessons Learned from Past Operations in the Country/Sector

OED's recent assessment of the Bank's transport portfolio in China highlights a high level of client satisfaction with investments in the highway sector. The overall performance of the Bank's highway portfolio in China has been satisfactory; nevertheless, a number of issues have arisen during project implementation. These include a lack of coordination among organizations and levels of government that has been detrimental to implementation of the policy agenda, especially for improving road safety, and issues with infrastructure design as well. Two ongoing Bank-financed highway projects in Inner Mongolia, the Inner Mongolia component of the Tri-provincial Highway Project, and the Inner Mongolia Highway Project, have provided relevant lessons, which the design of the proposed project has taken into account:

- *Client ownership and coordination among various levels of government units must improve.* The task team ensured that all relevant government units, including various ministries, Hulunbeier government, IMCD, and other organizations involved, participated in project preparation to foster a sense of ownership as well as create continuity for implementation.
- *Rushing the engineering design without carrying out a thorough geological survey leads to many design variations during implementation.* The proposed project has tried to ensure

that the design institute has enough time to complete a thorough survey and carry out design work properly.

- *A weak local supervision team causes quality control during implementation to suffer.* The project team discussed supervision at length with the Hulunbeier project management office to ensure that the client takes site supervision work seriously and that the local supervision team recruited through national competitive bidding is of good quality.
    - *Rushing through the procurement process in order to start construction quickly does not leave sufficient time for bidders to prepare good bids.* The task team for this project insisted on giving bidders sufficient time to prepare good bids and established procedures that do not allow the client to shorten the bid period without good reason.

9. Safeguard Policies (including public consultation)

| **Safeguard Policies Triggered by the Project** | Yes | No |
|---|---|---|
| Environmental Assessment (OP/BP/GP 4.01) | [X] | [ ] |
| Natural Habitats (OP/BP 4.04) | [X] | [ ] |
| Pest Management (OP 4.09) | [ ] | [X] |
| Cultural Property (OPN 11.03, being revised as OP 4.11) | [ ] | [X] |
| Involuntary Resettlement (OP/BP 4.12) | [X ] | [ ] |
| Indigenous Peoples (OD 4.20, being revised as OP 4.10) | [X ] | [ ] |
| Forests (OP/BP 4.36) | [ ] | [X] |
| Safety of Dams (OP/BP 4.37) | [ ] | [X] |
| Projects in Disputed Areas (OP/BP/GP 7.60)* | [ ] | [X] |
| Projects on International Waterways (OP/BP/GP 7.50) | [ ] | [X] |

10. List of Factual Technical Documents

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* By supporting the proposed project, the Bank does not intend to prejudice the final determination of the parties' claims on the disputed areas