

PROJECT INFORMATION DOCUMENT (PID)
APPRAISAL STAGE

Report No.: AB3841

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| Project Name | SOUTH-WEST CORRIDOR ROAD PROJECT |
| Region | EUROPE AND CENTRAL ASIA |
| Sector | Roads and highways (100%) |
| Project ID | P099270 |
| Borrower(s) | Republic of Kazakhstan |
| | |
| Implementing Agency | Committee for Roads |
| | Ministry of Transport and Communications Astana Kazakhstan |
| Environment Category | <input type="checkbox"/> A <input checked="" type="checkbox"/> B <input type="checkbox"/> C <input type="checkbox"/> FI <input type="checkbox"/> TBD (to be determined) |
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1. Country and Sector Background

1. Kazakhstan has enjoyed strong economic performance, with average real GDP growth of 9.2 percent over the past four years (2004–2007). While per capita incomes doubled and exceeded US\$ 7,000 in 2007, the overall budgetary balance remained in healthy surplus (averaging 3.7 percent of GDP over 2003–2007), and the majority of windfall oil revenues have been saved in the National Fund of the Republic of Kazakhstan (NFRK) established in 2000. Nevertheless, signs of overheating were evident before 2007. Inflation accelerated from 6.4 percent in 2003 to 8.6 percent in 2006, and surged to over 18 percent in late 2007. Cumulative appreciation of the real effective exchange rate from 2004 to 2007 was some 18 percent. Overheating was exacerbated by very rapid growth of foreign borrowing and commercial credit expansion, which led to the deterioration of the quality of loan portfolios of Kazakhstan banks. Higher oil prices, slower import growth, and largely responsible macroeconomic policy have stabilized expectations to a large degree since mid-2007, and brought the balance of payments back into surplus. Kazakhstan banks have so far been managing their debt obligations largely on their own, although a few banks remain in difficult positions. The risk of a full blown financial crisis, involving currency depreciation, a very rapid rise in non-performing loans, and a general banking crisis still exists, although it has become much less probable in light of a major strengthening of the current account and continued accumulation by the government of oil and monetary reserves.

2. To achieve the goal of aligning its economy with that of the leading economies in the world by improving the country's competitiveness, Kazakhstan has formulated and adopted comprehensive development strategies. Relevant to the transport sector are the Kazakhstan 2030 Strategy (1997), the National Territorial Development Strategy (NTDS), the Transport Sector

Strategy (2006) and the Road Sector Development Program for 2006-2012 (RSDP). The overall aim of these strategies is to “ensure sustainable development of the country, improve living standards, and increase competitiveness of Kazakhstan in the region and in the world by allocating economic and human resources in an efficient manner”. The Territorial Development Strategy focuses on promoting the development of growth poles and core cities along selected strategic axes. At the core of this would be an efficient network of transport infrastructure required to link the planned growth poles. The Transport Sector Development Strategy 2006-2015 and the RSDP define investment programs that include rehabilitation of the Republican road network and the provision of selective additional infrastructure. The planned investment program gives priority to the reconstruction of six strategic road transport corridors (totaling 8,290 km) that carry the majority of the traffic on the Republican road network.

3. Efficient and safe transport systems are necessary prerequisites for development of the economy and for national cohesion. Kazakhstan has 89,000 km of roads, of which 13,000 km are primary roads. Roads represent the leading mode for short haul transportation in the country. There is little substitute for trucks despite the rather low density of road (3km per 100km square which equals the density in Russian but which is far lower than the density in Uzbekistan – 41km/km²– and in Kyrgyzstan –17km/km²). Additionally, many of the roads that exist are in poor condition, making transport time-consuming, expensive and dangerous. The winter season is an acute problem in the northern regions. The significant travel distances and the poor condition of existing transport infrastructure have been identified as the main reason for the high costs of transport in the region. Nonetheless, Kazakhstan has substantial transit potential by providing trade corridors linking Asian countries with Russia and Europe. In addition to establishing strategic regional transport links within Central Asia, the Government plans to improve transit corridors for trade with China, Russia and Europe, which are Kazakhstan’s main trading partners in non-oil export sectors.

4. Kazakhstan’s increasing link with its neighboring countries in Central Asia, but also China, Russia and Europe will have an impact on the directions of trade flows and create new opportunities for road transport. Kazakhstan’s trade flows were previously dominated by the north - south corridor because of its links with Russia and the rest of Central Asia, and these flows were served mainly by rail. Kazakhstan’s geographic position makes transport road and rail infrastructure potentially attractive for transit transport to and from other countries. Based on the Statistical Yearbook of Kazakhstan (2005), rail freight transport dominated the market in 2005, accounting for more than 75 percent of the combined ton-kilometer carried by rail and road in Kazakhstan. But a closer look at the trends over time shows that road freight in terms of ton-kilometers has increased by some 10 percent each year since 2002 and investment in road corridor are now at the core of the government’s strategy for transport.

2. Objectives

5. The overall objective of the Western Europe to Western China corridor development program is to improve transport efficiency and safety, and promote development along one of Kazakhstan’s main strategic road transport corridors. Transport and trade efficiency will be improved through provision of better infrastructure and services along the entire corridor to reduce transport costs, and through gradual reform of the entities responsible for all categories of

roads. The proposed South West Corridor Road Development Program would be an Adaptable Program Loan (APL) comprising three phases that are designed to take into account the pace of institutional reforms, the readiness for implementation, and the capacity of the Committee for Roads.

6. The development objective for Phase-I of the proposed Program is to increase transport efficiency along the South West Corridor between Kyzylorda to Aktobe Oblast border, and initiate reforms to improve road management and traffic safety in Kazakhstan.

3. Rationale for Bank Involvement

7. Reforming the administrative structure for managing roads in Kazakhstan will require careful planning and implementation. The experience of the Bank from several countries shows that reforms cannot be imposed from outside; they must be home grown taking into account the experiences of other similar countries. This proposed Program will initiate the dialogue with the government on the extent and type of institutional reforms in the roads sector that would be sustainable in the context of Kazakhstan. The Government's RSDP recognizes the need for reforms in: good governance and accountability; sustainable financing; policy and regulatory framework; institutional reform and capacity development; road safety; road sector sustainability; and road transport operations. The Bank has significant experience in implementing similar institutional reforms in several countries, and this will guide the development of policy reforms tailored to Kazakhstan.

8. The Bank is well placed to play the convening role to coordinate the participation of the IFIs in undertaking the massive investment required to develop the WE-WC corridor. The Bank's role would be to ensure that parallel financing for the entire corridor will be synchronized, that uniform technical standards will be applied, and the technical assistance components will complement the investments and the reform program. The very large program of proposed investments for the corridor will take several years to implement and will require the integration of the fiduciary and safeguards requirements of all IFIs and of Kazakhstan. This will require an effective oversight of the entire program, which the Bank can provide through joint supervision with other IFIs.

9. Also, the Bank together with the World Health Organization (WHO) have taken a leading role internationally to improve road safety. The Bank hosts the Global Road Safety Facility (GRSF) that helps conducting road safety management capacity reviews. The GRSF is financing a road safety capacity review in Kazakhstan, the findings of which will be implemented under the project.

4. Description

10. The Project constitutes Phase I of the SWC development program. The implementation of the works are expected to start in early 2009. The Project focuses on the 564km long section from Aktobe Oblast border to Kyzylorda that consists of an upgrading of the existing carriageway. The remaining sections of the Bank financed SWC Program will finance the 461 km from Kyzylorda to Shymkent.

11. The project is expected to be implemented in four years. It comprises four components:

- (a) Component 1: Upgrade of road sections between Aktobe/ Kyzylorda Oblast border – Kyzylorda By-pass estimated at US\$987.0 million (Bank financed share US\$839.3 million). This component will finance the upgrade and reconstruction of road sections in the Kyzylorda oblasts (564 km) with a design oriented toward increased road safety, and includes the costs of consultant services for supervision. The list of civil works contracts was agreed with the Ministry of Transport and Communications and accepted by the Bank. Preparation and design costs have been financed by the Borrower's own funds. The proposed reconstruction will improve ride quality leading to lower operating costs for road users, guarantee road structural soundness for a prolonged period, and prevent collapse, leading to lower life-cycle cost for the road asset. Communities living along the Corridor would also benefit from improved access to markets.
- (b) Component 2: Project Management Consultants estimated at US\$4.0 million equivalent (Bank financed share US\$3.4 million). The consultancy service will assist the Committee with the management of all activities associated with the projects (similar arrangements are in place for the implementation of the sections of the Corridor to be financed by the other IFIs, based on the MOU between the Committee, the MOTC and the IFIs). The main beneficiaries will be the Committee as well as the MOTC due to improved efficiency of project implementation, and improved efficiency and effectiveness of the Committee in managing the Republican road network.
- (c) Component 3: Institutional Development estimated at US\$4.0 million equivalent (Bank financed share US\$3.4 million). The component comprises consulting services, technical studies, the provision of equipment, and training to strengthen the internal management and operations of the Committee, particularly to improve road sector planning, programming, budgeting, and implementation, and to improve the efficiency of road maintenance practices (see details under Annex 4). The beneficiaries would be the Committee, Kazakhavtodor, and KazdorNII (the road research organization within MOTC).
- (d) Component 4: Improvements in road safety and road-side services along the corridor estimated at US\$2.0 million equivalent (Bank financed share US\$1.7 million). The first part of this component will include technical assistance targeted at specific road safety improvements. The Bank will finance a Road Safety Management Capacity Review to be completed by December 2008. The study will review road safety management capacity in Kazakhstan and develop a consensus with the government on the need for safety improvements. The main output will be a medium-term action plan for achieving road safety improvements in the form of a qualitative safety investment strategy and appropriate implementation steps. This phase of the Program will finance the “soft” aspects of the road safety action plan, such as; (i) public awareness campaigns, (ii) strengthening regulations to improve road safety, (iii) introduction of new

approaches to enforcement, and (iv) development of new approaches for timely emergency medical services. The “hard” activities agreed upon in the road safety action plan will be financed under Phase II and Phase III of the Program. The second part of this component will finance the preparation of an action plan to develop services along the Corridor in order to facilitate private sector investments in the provision of services to transporters along the corridor. The project will assist in developing incentives to the private sector for investments in road-side services. Phase II and Phase III of the Program would provide funds for public sector investments, such as access roads, bus terminals, road/rail terminals and the like. The main beneficiaries would be road users in general as well as local communities along the SWC.

5. Financing

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|---|--------|
| Source: | (\$m.) |
| Borrower | 149 |
| International Bank for Reconstruction and Development | 848 |
| Total | 997 |

6. Implementation

12. The Government invited the Bank, ADB, IsDB and EBRD, to co-finance in parallel separate sections of the WE-WC corridor. In order to formalize this collaboration, it was agreed that a Memorandum of Understanding (MOU) would be signed by the MOTC and all participating IFIs. The MOU drafted by the Bank incorporates the mechanisms for collaboration, an outline of the financing, joint project implementation arrangements, and the commitment to uniform design standards. The implementing entity for the Project is the Committee for Roads within the Ministry of Transport and Communications (MOTC). The MOTC has requested Bank advice on options for reforming the Committee, including: (i) the re-establishment of a Project Implementation Unit (PIU) within the Committee; (ii) outsourcing to consultants some of the Committee’s functions related to management of the Corridor development program; (iii) transformation of the Committee into a semi-autonomous Road Agency that can hire staff at market remuneration rates; and (iv) transformation of the Committee into a State Owned Enterprise (SOE) or Joint Stock Company with a defined income and full autonomy. The MOTC selected option (ii) above as an initial step, and hence the concept of a Project Management Consultant was developed. The role of the PMC will be to provide technical assistance to the Committee for management and administration of all projects, quality control of road works and oversight of supervising engineers employed under separate consulting services contracts. The proposed project will finance a technical study to review if options (iii) and (iv) would be viable in the context of Kazakhstan with recommendations for the MOTC on how the preferred option could be implemented.

13. The Government plans to implement road works along the entire corridor within the four year period 2009 – 2012, which puts significant pressure on the procurement of the works. The detailed design for civil works, preparation of tender documents and the first prequalification for civil works are expected to be completed by December 2008. In order to expedite procurement of the works, the Committee will launch the prequalification process before the detailed design is completed. In addition, as most of the activities on the critical path relate to the procurement of civil works, the packaging of the works has been designed to address this constraint with few

contracts in order to minimize the procurement process, but with several bidding lots in order to ensure a large competition.

7. Sustainability

14. The issuing of the Transport Sector Development Strategy for 2006-2015 and of the Road Sector Development Program for 2006-2012 provides strong evidence of the Government's commitment to the Program. Those strategies include indications of long term financing to the roads sector with the objective of attaining acceptable levels of service along the corridor and throughout the Republican road network. The RSDP specifies the need to improve the condition of the Republican road network. The budget foreseen for this purpose is forecast until the year 2012 incorporating 8–10 percent increase each year, with the maintenance of the six CAREC road corridors assigned the highest priority. During project implementation, strong oversight and supervision of all contracts will be undertaken by the Committee supported by the PMC. The project is designed to support the implementation of the RSDP through Component 3 and the financing of technical improvements (e.g., to increase the durability and reliability of the infrastructure), the introduction of international standards, the protection of environment and the training of staff. The participation of the PMC in the implementation of the Program represents a significant step towards sustainability of project outcomes as it is expected that by the end of the implementation period for all three phases of the Program, most the local staff at the PMC will join the successor organization after the reform of the Committee, ensuring a sustainable transfer of knowledge.

7. Lessons Learned from Past Operations in the Country/Sector

15. Main lessons learned include the following:

- The implementation of large transport investments requires significant institutional capacity and incentives for staff in relevant departments to support project implementation and coordination.
- Weak institutional capacity affects project implementation and jeopardizes fiduciary control. The Committee so far has not been able to attract qualified staff with the necessary experience to manage large projects and to manage the fiduciary processes.
- Supervision of consultants was weak due to the shortage of experienced engineers within the Committee. Supervising engineers need much closer oversight by the Committee. Hence it is proposed that this function should be carried out with the assistance of the PMC. As part of this agenda, it is proposed to introduce longer term defect liability (warranty) periods for road construction from the present 2 years up to 5 years during which the construction company will remain in charge of maintenance activities.
- Road construction costs are very high in Kazakhstan, demonstrating the lack of a competitive construction industry in the country and in the region as a whole. It is therefore important to encourage more effective and efficient contracting practices, including widespread use of international bidding, use of local sub-contractors, and exposing the SOE Kazakhkavtodor to competition. The rapid economic growth in Kazakhstan over the past two decades has resulted in very high traffic growth rates. This should be catered for by longer term planning of development projects and for

improvements in the technical design standards for roads and bridges. The Soviet SNIP¹ standards are inappropriate under such circumstances and the Committee will need to develop appropriate standards for road and bridge design.

- Concerns with poor governance and corruption in the construction industry require that special attention should be paid to fiduciary management of projects.

8. Safeguard Policies (including public consultation)

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

9. List of Factual Technical Documents

16. KDP carried out the study with the assistance of Saty-Invest Ltd (Kazakhstan), Asia Megatransit (Kazakhstan), TASC (Israel) and BCEOM (France)

10. Contact point

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¹ SNIPs are the technical regulations and standards used throughout the Former Soviet Union.

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

