DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT

Approved by the Board of Directors on 28 November 2023[1]

KYRGYZ REPUBLIC

ISSYK-KUL RING ROAD IMPROVEMENT PROJECT

[Redacted in line with the EBRD's Access to Information Policy]

[Information considered confidential has been removed from this document in accordance with the EBRD's Access to Information Policy (AIP). Such removed information is considered confidential because it falls under one of the provisions of Section III, paragraph 2 of the AIP]

[1] As per section 1.4.8 of EBRD's Directive on Access to Information (2019), the Bank shall disclose Board reports for State Sector Projects within 30 calendar days of approval of the relevant Project by the Board of Directors. Confidential information has been removed from the Board report.

For the avoidance of any doubt, the information set out here was accurate as at the date of preparation of this document, prior to consideration and approval of the project.

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ABBREVIATIONS / CURRENCY CONVERSIONS

ADB	Asian Development Bank
AADT	Annual Average Daily Traffic
ACG	Arab Coordination Group
AETR	The European Agreement Concerning the Work of Crews of Vehicles Engaged in International Road Transport
AFIR	Alternative Fuels Infrastructure Regulation
BMP	Biodiversity Management Plan
CAREC	Central Asia Regional Economic Co-operation
Capex	Capital Expenditure
CEDAW	The Convention on the Elimination of All Forms of Discrimination against Women
CH	Critical Habitat
CHA	Critical Habitat Assessment
CoC	Code of Conduct
CoO	Countries of Operations
DSSI	Debt Service Suspension Initiative
ECEPP	EBRD Client e-Procurement Portal
E&S	Environmental and Social
EIA	Environmental Impact Assessment
EIRR	Economic Internal Rate of Return
EPG	Economics, Policy and Governance
ESAP	Environmental Social Action Plan
ESD	Environmental and Sustainability Department
ESDD	Environmental and Social Due Diligence
ESIA	Environmental and Social Impact Assessment
ESMP	Environmental and Social Management Plan
ESMS	Environmental and Social Management System
ESP	Environmental and Social Policy
ETI	Expected Transition Impact
EUR	Euro
EURIBOR	Euro Interbank Offer Rate
FY	Full Year
GBVH	Gender-based Violence and Harassment
GDP	Gross Domestic Product
GEI	Gender and Economic Inclusion
GET	Green Economy Transition
GoK	Government of Kyrgyz Republic
IBA	Important Bird and Biodiversity Areas
IMF	International Monetary Fund
j-MDB	Joint Multilateral Development Bank
KAZH	KyrgyzAutoZhol
KGS	Kyrgyz som
KPI	Key Performance Indicators
KR	Kyrgyz Republic
LARF	Land Acquisition and Resettlement Framework
LCP	Low-carbon Pathway
LTS	Long-term Strategy
MoF	Ministry of Finance
MoTC	Ministry of Transport and Communications

NDC	Nationally Determined Contribution
NPV	Net Present Value
NSDS	National Sustainable Development Strategy
NTS	Non-Technical Summary
PA	Paris Alignment
PBF	Priority Biodiversity Features
PBMC	Performance Based Maintenance Contracting
PCU	Passenger Car Units
PD	Probability of Default
PIS	Project Implementation Support
PIU	Project Implementation Unit
PMP	Project Management Plan
PPAD	Procurement Policy and Advisory Department
PPR	EBRD's Procurement Policies and Rules
PR	Performance Requirements
RAD	Road Administration Department
RAROC	Risk-adjusted return on capital
RCP	Representative Concentration Pathway
RF	Road Fund
RP	Resettlement Plan
RS	Road Safety
SEP	Stakeholder Engagement Plan
SIF	Sustainable Infrastructure Fund
SMA	Stone Mastic Asphalt
SOE	State Owned Enterprise
SPI	Strategic Performance Indicator
SSF	EBRD Shareholder Special Fund
STEM	Science, Technology, Engineering, and Math
TC	Technical Cooperation
VAT	Value Added Tax
VOC	Vehicle Operating Costs
VOT	Value of Time
WB	World Bank

CURRENCY CONVERSION

(as of 26 October 2023)

EUR 1 = KGS 94.1

PRESIDENT'S RECOMMENDATION

This recommendation and the attached Report regarding an operation in favour of the Kyrgyz Republic (the "KR") are submitted for consideration by the Board of Directors.

The facility will consist of a sovereign loan to the Kyrgyz Republic of up to EUR 44.2 million to finance the reconstruction of an estimated 30 km section (the "Project") out of the 440 km ring-road around Issyk-Kul Lake.

The Project is of a strategic priority for the Kyrgyz Republic as it is within the catchment area of the Trans-Caspian Route (the "TCR") and forms part of key international transport axis - Central Asia Regional Economic Co-operation ("CAREC") Corridor 1. The Project will facilitate the transit potential of the country and its regional integration via an improved transport linkage with neighbouring Kazakhstan.

The Project's expected transition impact stems from the introduction of enhanced connectivity in the region strengthened adopting road safety standards in line with international standards (*Integrated quality*). The Project also targets improving the efficiency of road maintenance operations (*Resilient quality*) by introducing a performance-based maintenance contracting ("PBMC") approach and general improvement of contracting practices.

Pre-signing technical cooperation ("TC") is comprised of: (i) Technical and Economic due diligence funded by the Turkiye - EBRD Cooperation Fund; (ii) Environmental and Social due diligence funded by the EBRD's Shareholder Special Fund ("SSF"); (iii) Detailed Design funded by the Turkiye - EBRD Cooperation Fund; and (iv) Advance Procurement, funded by the Turkiye - EBRD Cooperation Fund. The post-signing TC package will comprise of: (i) Project Implementation Support, including Construction Supervision, (ii) Institutional Development Support; (iii) Lender's Monitoring Support; (iv) Road Safety; and (v) PIU support, all proposed to be financed by the Sustainable Infrastructure Fund ("SIF") and the SSF.

I am satisfied that the operation is consistent with the Bank's Strategy for Kyrgyz Republic, the Transport Sector Strategy, the Green Economy Transition Approach, the Strategy for the Promotion of Gender Equality, and with the Agreement Establishing the Bank.

I recommend that the Board approve the proposed loan and SSF TC grant from SSF Work Plan 2023-2024 substantially on the terms of the attached Report.

Odile Renaud-Basso

BOARD DECISION SHEET

KYRGYZ REPUBLIC – ISSYK-KUL RING ROAD IMPROVEMENT PROJECT: DTM 52367	
Transaction / Board Decision	Board approval[2] is sought for a sovereign loan of up to EUR 44.2 million in favour of the Kyrgyz Republic for the reconstruction of an estimated 30 km section of the 440 km Issyk-Kul Lake ring-road. Board approval is also sought for EUR 2 million from the EBRD Shareholder Special Fund ("SSF") Work Plan 2023-2024 in support of a technical cooperation for Project Implementation Support, including Construction Supervision ("PIS") TC assignment as part of the Project.
Client	**Borrower:** the Kyrgyz Republic represented by the Ministry of Finance (the "MoF"). **Implementing agency:** the Ministry of Transport and Communications (the "MoTC") which has overall responsibility for the organisation and management of the transport sector in the Kyrgyz Republic.
Main Elements of the Proposal	<u>Transition impact</u> • *Primary Quality – Integrated*. The Project will promote enhanced connectivity and seamless integration within the region as well as introduce improved road safety standards in line with international standards. • *Secondary Quality – Resilient*. The Project will support institutional development through sector regulation reform aimed to improve/establish contractual arrangements for relevant agencies; road sector regulation reform supporting the introduction of the updated PBMC; and road sector reform capacity building. <u>Additionality</u> • The Bank will provide long-term financing, which is presently not available from local commercial banks. It will also support the MoTC to achieve higher standards through its conditionalities (e.g. PP&R and ESAP) as well as support institutional and regulatory changes in the sector. <u>Sound banking</u> • The Bank is focused on improving the effectiveness of road sector institutions and policies, bringing high environmental and social standards, procurement policies and rules.
Key Risks	• <u>Implementation risk</u>. The risk [REDACTED] will be mitigated by the involvement of a PIS consultant.
Strategic Fit Summary	The Project is in line with the Bank's Strategy for the Kyrgyz Republic, which highlights the need to "support development of key regional infrastructure, promoting integration and sectoral reforms". The Project complies with the Bank's Transport Sector Strategy which promotes improved quality and connectivity of network infrastructure via "supporting corridors and network plans such as TEN-T, WBCN, CAREC…", as well as facilitates "policy dialogue on sustainable funding of road maintenance and performance-based maintenance…".

[2] Article 27 of the AEB provides the basis for this decision.

ADDITIONAL SUMMARY TERMS FACTSHEET

EBRD Transaction	A sovereign loan of up to EUR 44.2 million (the "Loan") to finance reconstruction of an estimated 30 km section ("Balbay Batyr-Karakol") of Issyk-Kul Lake ring-road ("Balykchy-Karakol-Balykchy") (the "Project"). Issyk-Kul Lake ring-road or the Balykchy-Karakol-Balykchy road is divided into five sections: (1) Balykchy-Korumdu of c. 104 km (Section 1); (ii) Korumdu-Balbay Batyr of c.80.5 km (Section 2); (iii) Balbay Batyr – Tyup – Karakol of an estimated 30 km, excluding 3 km road section within Tyup village financed from state budget (Section 3); (iv) Karakol – Barskoon of c. 79 km (Section 4); and (v) Barskoon – Balykchy of c. 141 km. These sections are financed by different sources and thus correspond to five contract packages that will be procured separately. For more details of the road map please refer to Annex 1**.**
Existing Exposure	EUR 127 million sovereign portfolio, EUR 48 million operating assets.
Maturity / Exit / Repayment	20 years [REDACTED].
Potential AMI eligible financing	None.
Use of Proceeds	The Loan proceeds will be used to finance the Project in accordance with the Investment Plan below. [REDACTED]
Investment Plan	[REDACTED]
Financing Plan	[REDACTED]
Key Parties Involved	• The Borrower: the Government of the Kyrgyz Republic, represented by the MoF. • The Implementing Agency: the MoTC.
Conditions to disbursement	[REDACTED]
Key Covenants	[REDACTED]
Security / Guarantees	Sovereign loan
Other material agreements	The Loan Agreement between the EBRD and the Kyrgyz Republic.
Associated Donor Funded TC and co-investment grants/concessional finance	**A. Technical Cooperation (TC)** *Pre-signing:* – **TC 1: Technical and economic due diligence** with a cost of EUR 75,000 was financed by the Turkiye - EBRD Cooperation Fund. – **TC 2: Environmental and social due diligence** with a cost of EUR 289,000 was financed by the SSF. – **TC 3: Detailed design** with a cost of EUR 74,800 was financed by the Turkiye - EBRD Cooperation Fund. – **TC 4: Advance procurement** with a cost of up to EUR 50,000 is funded by the Turkiye - EBRD Cooperation Fund. *Post signing:* – **TC 5: Project Implementation Support including Construction Supervision ("PIS")** with a cost of up to EUR 2,300,000 is proposed to be financed by the SIF (EUR 300,000) and the SSF (EUR 2,000,000). – **TC 6: Institutional Development Support** with a cost of up to EUR 400,000 is proposed to be financed by the SIF. – **TC 7: Lender's Monitoring Consultant** with a cost of up to EUR 74,900 is proposed to be financed by the SIF. – **TC 8: Road Safety Programme** with a cost of up to EUR 200,000 is proposed to be financed by the SIF.

	– **TC 9: PIU Support** with a cost of up to EUR 225,000 is proposed to be financed by the SIF or the SSF. **B. Concessional Finance** None. **Cost-sharing** In line with the Bank's client contributions policy, dated 1 January 2021, cash contributions will not be provided considering the client's public ownership, as well as its inability to make a financial contribution due to lack of funding in public budget.

[REDACTED] INVESTMENT PROPOSAL SUMMARY

1. STRATEGIC FIT AND KEY ISSUES

1.1 STRATEGIC CONTEXT

The Project will close the financing gap of the 440 km long ring-road rehabilitation programme around Issyk-Kul Lake (within the catchment area of the Trans-Caspian Route ("TCR")[3] and part of CAREC 1 corridor), to foster the Kyrgyz Republic's economic development and connectivity, as well as strengthen the country's integration into regional markets.

As a land-locked country, the KR is heavily dependent on its road network to ensure smooth and reliable international transit and domestic traffic. With its rugged mountainous terrain and poor road network quality, the Government of the KR (the "GoK") experiences serious challenges maintaining its transport corridors which are essential for effective regional trade and sustainable economic growth.

As a key output of the EU's Global Gateway strategy, the Bank has prepared an EU-funded study to identify to identify and prioritize actions towards developing the most sustainable transport connections between Europe and Central Asia. The Project is within the catchment area of the TCR covered by the study. The Project will contribute to the strategic goal of sustainable connectivity between the KR and Kazakhstan with the potential to further support establishing and developing a regional trade value chain and economic integration.

The strategic importance of the Issyk-Kul Lake ring-road is reinforced by its position on the Central Asia Regional Economic Co-operation ("CAREC") Corridor 1. On a larger scale, the road remains an important corridor between Europe and East Asia. The Project is in line with the CAREC Programme. This aims to expand trade and improve competitiveness through focused action from all multilateral partners (i.e. ADB, EBRD, IMF, IDF, WB and UN) on transport initiatives, trade facilitation, energy, trade policy, and economic corridor development.

The Project is expected to: (i) bring the current road to motorway standards; (ii) increase transport volume of freight and passengers between the countries of the region, and (iii) consequently, generate positive social impacts in terms of employment through regional value chain development, enhanced connectivity and seamless integration within the region.

The Project is consistent with the Bank's Country Strategy for the Kyrgyz Republic. Fostering regional infrastructure connectivity and integration into the wider regional economy is one of the strategic orientations of the Kyrgyz Republic's Country Strategy. It notes that critical infrastructure (roads, cross-border logistics) needs to be enhanced

[3] Often referred to as the Middle Corridor.

to facilitate cross-border trade. The road sector remains largely unreformed in all aspects, including institutions, financing and private sector participation. While some road construction has been undertaken by the private sector under IFI-funded contracts, there is little competition in the sector generally. In line with the KR Country Strategy, the Bank will focus on promoting road maintenance and a financially sustainable approach to road maintenance operations.

The Project is also fully consistent with the Transport Sector Strategy, notably with Strategic Direction 1 ("Connected Networks") which states that the Bank will "complement co-financing partners with investment in constructing, upgrading and modernising of …regional…cross border road infrastructure to improve access to markets and services, and create linkages to key transport networks and corridors" as well as "support corridors and network plans such as TEN-T, WBCN, CAREC…" coupled with facilitating "policy dialogue on sustainable funding of road maintenance and performance-based maintenance…". The Project will contribute to improving the resilience of roads in the KR to the impacts of climate change in line with the Green Economy Transition ("GET") approach. Moreover, the Project is assessed as positively aligned for both mitigation and adaptation goals of the Paris Agreement ("PA"). There is a decrease in Scope 3 emission of approximately 7ktCO2e in the first year of the project (2027) and of 16ktCO2e in 2050 as a result of the improved roughness of the road, increased speed, and associated reduced fuel consumption.

In addition there is a credible pathway for decarbonisation of the fleets responsible for those emissions via electrification. A detailed climate risk assessment was undertaken, and adaptation measures introduced to address rockfalls, flooding, and temperature increase and extreme heat events. The Project is expected to deliver climate resilience outcomes of reduced weather-related damage to the road assets and reduced weather-related disruption on the road network. This results in a GET attribution of 16 per cent, in line with the GET Handbook and the j-MDB methodology for attribution of climate adaptation finance. Further details of the Green assessment results can be found in Annex 2.

The Project is in line with Recommendation 3 – "…increase regional connectivity despite the challenging political economy in ETCs, such as through transport linkages…" - from the recent Evaluation study of the EBRD's approach to Early Transition Countries (2017–2022), performed by the EBRD Evaluation department.

1.2 Transition Impact

Primary Quality: Integrated

Obj. No.	Objective	Details
1.1	*The Project delivers material quality improvements of the current infrastructure between or within regions that are currently inadequately integrated.*	The Project is expected to: (i) bring the current Category III road to Category II motorway standards; (ii) increase transport volume of freight and passengers by boosting transit and economic exchanges between the countries of the region, and (iii) consequently, generate positive social impacts in terms of employment by developing regional value chains, enhanced connectivity and seamless integration within the region. This will result in travel time cost savings from the reduction in travel distance, in congestion, or from faster road speeds

		[REDACTED] and benefit both passengers and cargo in transit. The Project supports the development of the most sustainable transport connections between Europe and Central Asia. It is within the catchment area of the TraTCR, identified in the EBRD-led, EU-funded study, as part of the EU's Global Gateway Strategy.
1.2	*Specific soft measures to improve or expand infrastructure will be introduced and capacity increases will be benchmarked.*	The Project envisages improvement of road safety ("RS") management through improved RS planning in road designs by supporting the introduction of road safety auditing into national law and establishing a formal road safety training award for road safety auditing. In addition, the Project will support the implementation of the AETR Agreement related to driving hours. This is expected to result in a decrease in collisions associated with the transport of passengers and freight across the KR.

Secondary Quality: Resilient

Obj. No.	Objective	Details
2.1	*First in the country - First management contract/lease/outsourcing (i.e. without private capital investment) in a country where private sector involvement in any infrastructure sector is either not present or minimal [Maximum 1 across all infrastructure sectors].*	The Project will introduce a proper full-scale PBMC concept in the KR by: (i) developing multiyear output/performance based maintenance contracts to cover at least routine, periodic and emergency response maintenance of rehabilitated roads and support KAZH in its introduction; (ii) contracting the PBMCs out to private sector; (iii) supporting the development of the relevant institutional capacity to implement the PBMCs in line with the best practices. [REDACTED].
2.2	*First in the country - The project and associated TC support will help building necessary institutional capacity and procedures for sustainable and efficient infrastructure asset management as one of the first three times in the country.*	The Project will support improving contractual arrangements and practices of the newly established KAZH. The Institutional Development Support TC will include: (i) improvement/establishment of contractual arrangements for KAZH, Road Fund and MoTC (e.g. performance obligation contracts) with clear defined KPIs, responsibilities, obligations, and penalties for each party; (ii) support the introduction of the updated PBMC approach with well-defined performance standards, clear reporting and monitoring arrangements, and a deduction approach in case of non-compliance with performance standards; and (iii) developing KAZH's, the MoTC's and the Road Fund's capacity to implement reforms of contractual arrangements and PBMC.

<u>Delivery Risks</u>

[REDACTED].The Bank-funded TCs will mitigate the risks of the GoK's implementation capacity through consultancy support and providing targeted training

to the beneficiaries' staff. The capex contracts' procurement risk will be mitigated by the PIS consultant and the use of the Bank's PP&Rs. For detailed information on project implementation and procurement plan, please refer to Annex 3.

1.3 ADDITIONALITY

Identified triggers	**Description**
No triggers identified	N/a.
Additionality sources	**Evidence of additionality triggers**
Financing structure	EBRD offers a tenor [REDACTED] above the market average, necessary to structure the project. A 20-year tenor [REDACTED]. EBRD investment is needed to close the funding gap. It does not crowd out other sources, such as from IFIs, government, commercial banks and/or complements them.
Standard-setting: helping projects and clients achieve higher standards	Client seeks EBRD expertise on best international procurement standards. The on-going procurement will follow the EBRD's PP&R to maintain eligibility for EBRD financing. The Bank will also implement ESAP.
Gender SMART:** the MoTC seeks/makes use of EBRD expertise on the adoption of **gender standards and/or equal opportunities action plans** (e.g. improving women's access to economic opportunities)**.	Employment rate of women in the Issyk-Kul Province is lower than men 34 vs 63.9, and lower than the national average 71.9 men vs 42.7 women. Furthermore, there are still strong conservative social norms in the country, where men are traditionally considered as the head of the household whilst wives are stereotypically tasked with households and childcare. The project will build on the Bank's past efforts to include in the National Gender Strategy further efforts on identifying and removing list of banned occupations for women. Under this project, the MoTC will lead on a communication campaign to support the removal of banned occupations for women – in particular a campaign around promoting women's participation in the transport sector outlined in the new National Gender Policy.
Policy, sector, institutional, or regulatory change	The Bank will facilitate better contractual arrangements for KAZH, Road Fund and the MoTC. There will be clear defined KPIs, responsibilities, obligations, and penalties for each party as well as support the introduction of the updated PBMC approach with well-defined performance standards, clear reporting and monitoring arrangements.

1.4 SOUND BANKING - KEY RISKS

Risks	**Probability / Effect**	**Comments**
Kyrgyz Republic's creditworthiness as the Borrower	Medium / Medium	The share of the KR's public debt at 49.2 per cent of GDP in 2022 (compared with 56.2 per cent in 2021) and 49.7 per cent by 2028. A debt sustainability analysis (please refer to Annex 4) indicates that sovereign debt levels are likely to remain at acceptable levels over the medium term, even under conditions of a number of shocks.
Construction risks and	Medium / Low	The MoTC and its PIU have experience in implementing IFI-financed projects, including the EBRD-financed Osh-

implementation capacity		Isfana Road Upgrading Project. The PIU will be assisted during implementation of the Project by the PIU Support individual consultants. PIU will also be assisted by a PIS consultant to identify quality problems, and cost/time overruns at an early stage.
Demand risk	Medium / Low	According to reputable independent consultants, the Project's Annual Average Daily Traffic ("AADT") is projected to increase [REDACTED], suggesting that a 4-lane road is justified and within the capacity limit of 40 thousand PCU/day as given in GOST 33475-2015.
Environmental & Social risks	Medium	As this is a Category A project, a full environmental and social due diligence was undertaken and the key documents were made publicly available in May 2022. The Environmental and Social Impact Assessment ("ESIA") included Environmental and Social Action Plan ("ESAP"), Stakeholder Engagement Plan ("SEP"), Land Acquisition and Resettlement Framework ("LARF"), Environmental and Social Management Plan ("ESMP"), Non-Technical Summary ("NTS"), Biodiversity Management Plan ("BMP") and Critical Habitat Assessment ("CHA"). It was concluded that the impacts of the Project are manageable, and construction and operation of the Project will not result in irreversible, unacceptable risks to people or the environment with the application of the mitigation measures and supporting TCs.

2. MEASURING / MONITORING SUCCESS

Overall objectives of project	***Monitoring benchmarks***	***Implementation timing***
- Project implemented on time, within budget	- Completion according to the timeline and within the budget	[REDACTED]
- Compliance with the EBRD Environmental and Social Standards	- Timely implementation of ESAP	[REDACTED]

Primary Quality: Integrated

Obj. No.	**Monitoring indicator**	**Details**	**Base line**	**Target**	**Due date**	**TC**
1.1	Improved quality of infrastructure within regions	To be achieved via the following indicators: 1) estimated traffic increase [REDACTED]after road rehabilitation; 2) estimated road users savings during the first, second and third year after the rehabilitation completion [REDACTED]	No	Yes	[REDACTED]	Y
1.2	Operational restructuring completed	Introduction of Road safety auditing and implementation of the AETR agreement.	No	Yes	[REDACTED]	Y

Secondary Quality: Resilient

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date	TC
2.1	Practices of the relevant stakeholder improved (operational)	[REDACTED]	No	Yes	[REDACTED]	Y

3. KEY PARTIES

3.1 BORROWER

The KR will be the Borrower with the Project to be implemented by the MoTC. The Project implementation process is to be managed by the PIU. Having been its authorised agency for managing similar projects funded by IFIs such as the ADB and WB for many years, the PIU has sufficient institutional capacity to implement the Project.

The Road Administration Department ("RAD") was established by the MoTC in 2010 as an entity in charge of policies, norms, and regulations in the road sector. In 2021, it combined all regional road maintenance units and enterprises under KAZH. This is currently in charge of regular road maintenance operations. The MoTC also established a dedicated Road Fund (the "RF") in 2021, which accumulates funds from various sources linked to transport and roads to finance design works, regular maintenance and reconstruction as well as building and development of road networks. According to the ADB's Road Funds and Road User Charges in the CAREC Region Report, prepared in 2022[4], the RF is expected to generate around KGS 4 billion (USD 50 million), covering circa 40 per cent of the USD 125 million maintenance and repair needs in the road sector of the KR.

4. MARKET CONTEXT

Having a population of 7 million, the KR is a small, landlocked, mountainous country with an area of 199,900 square km located in Central Asia. The country shares its borders with Kazakhstan to the north and northwest, Uzbekistan to the southwest, Tajikistan to the south, and the People's Republic of China to the southeast.

Roads provide the dominant transport mode in the country for both freight and passenger transport, but the road density is approximately 96 km per 100 km^2. The rail network's role in transportation of goods and people is limited due to the lack of connection between northern and southern railway tracks. The country's challenging geography makes aviation is a key part of the country's transportation system; however, due to the lack of regular cargo flights and cargo facilities, aviation does not compete with the road transport. Thus, the efficient functioning of the road sector is fundamental for the economic and social development of the KR.

To date, 98 per cent of passenger and 96 per cent of freight traffic is carried by automotive transport. Over 60 per cent of the national road network requires either a full overhaul or partial maintenance. The government's main concern is not expansion of, or major upgrades to, the national road network, but rather the rehabilitation of key sections to keep transport connectivity stable, reliable and safe. The country's transport

[4] https://www.adb.org/sites/default/files/publication/861456/road-funds-road-user-charges-carec.pdf

sector development policy is reflected in its National Sustainable Development Strategy 2018-2040 ("NSDS") and Forecast of Socio-Economic Development of the KR for 2023–2027, which prioritise rehabilitation of strategic road corridors.

Out of around 34,000 km of the KR's road network, the MoTC is responsible for almost 19,000 km, which includes 5,700 km of international roads, 5,100 km of national roads, and 8,100 km of local roads. The remaining 15,000 km comprise mainly urban and rural roads in cities and villages.

The KR's international transit roads are part of four CAREC corridors, and have been largely improved through assistance from international financial institutions. This enables the country to be an important transit player in the Central Asia region.

There is already a competitive environment for road transport services in the KR. All investment, including new construction and overhaul, are systematically tendered. About half of all asphalt resurfacing work is contracted to the private sector. Foreign (mainly Turkish and Chinese) contractors are contributing to the significant advancement of the road construction industry, building its capacity mainly on the internationally financed road network rehabilitation programme. The recently established KAZH carries out maintenance and current repairs works in public roads through annual contracts with the RAD.

5. FINANCIAL / ECONOMIC ANALYSIS

5.1 Financial Projections

[REDACTED]

5.2 Economic Internal Rate of Return

[REDACTED]

5.3 Sensitivity Analysis

[REDACTED]

5.4 Projected Profitability for the Bank

[REDACTED]

6. OTHER KEY CONSIDERATIONS

6.1 Environment

Category A (ESP 2019). The project comprises the rehabilitation of an estimated 30 km section of the Balykchy-Karakol road, namely the Balbay Batyr-Karakol road section, located in the eastern part of the KR along the northern shore of Issyk-Kul Lake. The Project proposes the road widening from a 2-lane to a 4-lane carriageway.

The Tyup Karakol ESIA documentation which covers the Balbay Batyr-Karakol road section, was published on the EBRD web site on 12 May 2022 and includes the following documents: ESIA Report and NTS, ESMP, ESAP, SEP, LARF and BMP. Consultation meetings were undertaken in November-December 2022 and a consultation report is being prepared and will be disclosed prior to Final review.

The route for this project is largely based on the current road alignment. Therefore, the area required for clearance falls is almost entirely within the current road right of way and roadside, with only the footprint and temporary works areas to be cleared for the widening of the road. ESAP stipulates the measures to develop a national

Environmental Impact Assessment (“EIA”) in line with national legislation and obtain environmental and construction related permits.

A multi-criteria analysis incorporating environmental and social criteria and consideration of stakeholder feedback was prepared and assessed whether or not to include a potential bypass around Tyup village. The ‘Preferred Option’ selected was upgrading the road on its current alignment though with a reduced width. Rehabilitation works within the village have been undertaken recently requiring additional mitigation measures relating to road and public safety which have been included in ESAP.

A key risk associated with this Project will be to ensure that the contractors are aware of their responsibilities and that they implement adequate actions to avoid, minimise, mitigate and manage these risks as identified in ESIA and associated management plans. An Environmental and Social Management System (“ESMS”) is required as part of ESAP to ensure the contractors adequately address the environmental and social impacts and risks. Contractors are required to develop construction management plans to provide management/mitigation procedures to cover air emissions, water quality, land restoration, topsoil, health and safety, waste management and emergency response, labour, worker accommodation, Code of Conduct (“CoC”) and stakeholder engagement. The MoTC will be required to have effective contractor monitoring in place.

The biodiversity features have been assessed as part of ESIA report and a CHA, in line with EBRD’s PR6. Extensive baseline data collection and biodiversity field surveys of both terrestrial and riverine ecosystems concluded that the majority of the habitat within the vicinity of the Project road is cultivated ground, with natural and semi-natural areas around the floodplains of the rivers crossed by the road which are often grazed by livestock.

The Critical Habitat (“CH”) and Priority Biodiversity Features (“PBF”) assessment showed presence of CH and PBFs in the study area. Among CH, the area considered contains sensitive biodiversity features including Issyk-Kul lake and adjoining rivers for their unique ecosystems; five rivers supporting endemic fish; habitats supporting the plant species *Astragalus projecturus*; and as a precautionary measure, habitats supporting the Asiatic frog; and Issyk-Kul Lake Ramsar site and Eastern Issyk-Kul Lake IBA for supporting globally significant migratory or congregatory species. Due to the temporary nature of the works and restricted extent of the construction footprint, impacts are considered to be low. Adequate mitigation measures have been included in the BMP and ESAP, including design measures to avoid impacts on sensitive features and pollution prevention and control measures to reduce impacts on watercourses and natural habitats. Additionally, the BMP stipulates implementation of pre-construction surveys, net gain measures (habitats restoration and replantation), post-construction monitoring and update of BMP accordingly.

The Project crosses several rivers and streams, which drain into the Issyk-Kul Lake. Works near rivers, land clearance and uncontrolled discharges of untreated water to surface water from construction camps and abstraction of water may also occur during construction. Impacts are expected to be mitigated through the implementation of detailed Water, Wastewater and Drainage Management Plan; Spill Prevention and Response Plan; and Emergency Preparedness and Response Plans. Noise and vibration effects as a result of the use of equipment, earthworks, and the movement of construction vehicles and workers will be addressed through mitigation measures defined in a Noise and Vibration Management Plan and Traffic Management Plan. The majority of the materials for reconstruction are expected to be provided in country, from

current resources, quarries or borrow pits. The Materials Use and Waste Management Plan and Soil Management Plan will require reuse and recycling of materials to minimise waste disposal.

Social risks include land acquisition and resettlement, labour influx and workforce management, preservation of the heritage sites, and prevention of the gender-based violence and harassment ("GBVH") concerns. The MoTC adopted and disclosed the LARF and will prepare and implement the Resettlement Plan ("RP") to address limited physical and economic displacement impacts including restricted and lost access issues. The delivery of the RP will be verified via the Completion Report that will be approved by the Bank prior to the start of works. To avoid impacts on heritage sites along the road alignment, the Contractor will develop a site specific cultural heritage management plan that will include an adoption of the chance find procedure and induction training of the project workforce.

The MoTC will ensure that the Contractor will adopt the PR2-aligned HR policy and procedures including a worker grievance mechanism including an anonymous grievance mechanism for GBVH. All temporary accommodation facilities for Contractor's and its sub-contractors' workers will be designed and provided in line with the requirements of the national sanitary norms and IFC/EBRD guidelines for worker accommodation.

The Project will aim to improve road safety as the current road has not been maintained with limited road markings, safety barriers or traffic signs. The recent works undertaken in Tyup village will be subject to a Road Safety Inspection. The MoTC will be required to appoint an independent road safety auditor to review the road design and will incorporate technically and economical feasible road safety recommendations made by the auditor into the design. The road will also undergo an IRap star rating assessment to confirm the design will achieve a 3 star or better rating. The road will require further periodical road safety reviews to ensure ongoing safety for all road users. Temporary traffic management arrangements will need to be implemented and periodically updated in consultation with affected communities to ensure minimal impact and maximum safety to project affected communities and local businesses. The Project will benefit from a Road Safety TC which will support the legal requirement for road safety audits, regulating driving hours for certain vehicle groups in line with the European Agreement AETR and a targeted road safety awareness campaign which will provide tools and materials that can be used on other projects.

The SEP includes a summary of information disclosure and community meetings conducted to date, as well as an outline of upcoming consultation activities and details of the grievance mechanism.

The MoTC will monitor the delivery of mitigation measures by the contractors via the Supervision Engineer. A Lenders' E&S Monitoring Consultant will be also retained to review and oversee the implementation of E&S management plans and report regularly to the Bank.

6.2 INTEGRITY

Integrity due diligence was undertaken on the GoK, the MoTC, and the PIU management, as well as other relevant parties. The review did not identify any material integrity issues.

All actions required by applicable EBRD procedures relevant to the prevention of money laundering, terrorist financing and other integrity issues have been taken with

respect to the project, and the project files contain the integrity checklists and other required documentation which have been properly and accurately completed to proceed with the project.

ANNEXES TO OPERATION REPORT

ANNEX 1 – PROJECT LOCATION AND REGIONAL RELEVANCE

The Issyk-Kul Lake transport ring runs through densely populated areas such as the city of Cholpon-Ata, the villages of Ananyevo, Tyup, etc. Outside the city of Karakol, the road runs along the southern part through the village of Kyzyl-Suu, Bokonbaevo to the town of Balykchy, thus closing the transport ring around the lake. The length of the northern half-ring is 218 km, the southern one – 220 km. The total length of the Issyk-Kul Lake transport corridor is 440 km. It is currently a priority project for the GoK supported by a number of IFIs.

The road is designated as an international route, providing linkage with Kazakhstan via the border at Karkyra. As well as being economically important as a tourist destination, the Issyk-Kul Lake basin is important for its agricultural production, food processing and mineral extraction.

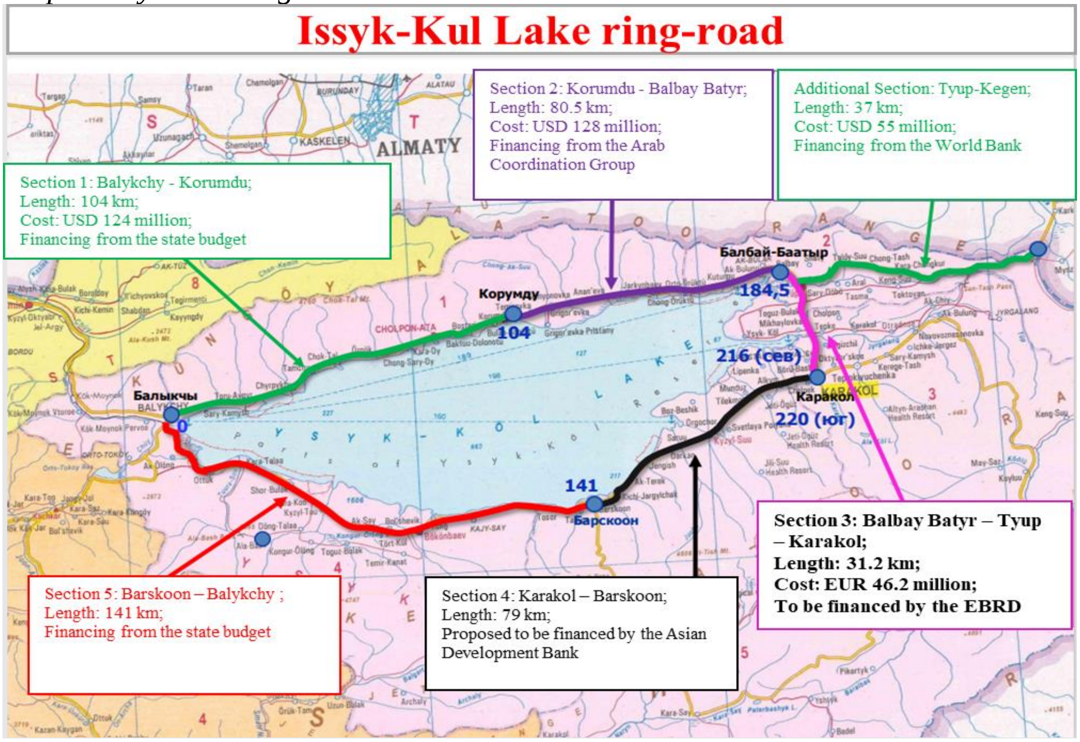
Dynamic development during the past decade has been accompanied by steady growth in passenger and cargo traffic. Improved interregional connectivity and rising tourist inflows have resulted in traffic growth of around 60 per cent since 2010. However, the road has not been properly repaired for the last 30-35 years due to the lack of financing, it is now inadequate for today's traffic making it dangerous. The rehabilitation/upgrade will not only improve road safety but also facilitate trade and tourist relationship of the KR, Kazakhstan and China, giving opportunities for the both national and regional development and further improvement of transport services.

The strategy is to upgrade the Issyk-Kul Lake ring-road or the Balykchy-Karakol-Balykchy Road in 5 phases as follows:

- Section 1 from Balykchy to Korumdu (104 km) was financed in with USD 124 million from the Republican budget;
- Section 2 from Korumdu to Balby Batyr (80.5 km) was financed in with USD 128 million from the Arab Coordination Group ("ACG"), consisting of the Saudi Development Fund, the Kuwait Fund for Arab Economic Development, the Abu-Dhabi Fund for Development, the OPEC Fund for International Development, and the Islamic Development Bank;
- The section from Balbai Batyr to Karakol (estimated 30 km) is proposed to be financed by a sovereign loan of up to EUR 44.2 million from the EBRD;
- The section from Karakol to Barskoon (79 km) is proposed to be financed by the Asian Development Bank. Feasibility study is ongoing;
- The final section Barskoon to Balykchy (141 km) is being financed by the state budget.

In addition, the road between Tyup village and the border with Kazakhstan at Karkyra is being rehabilitated/upgraded with support from the World Bank to boost international trade and improve access to tourist sites along that route.

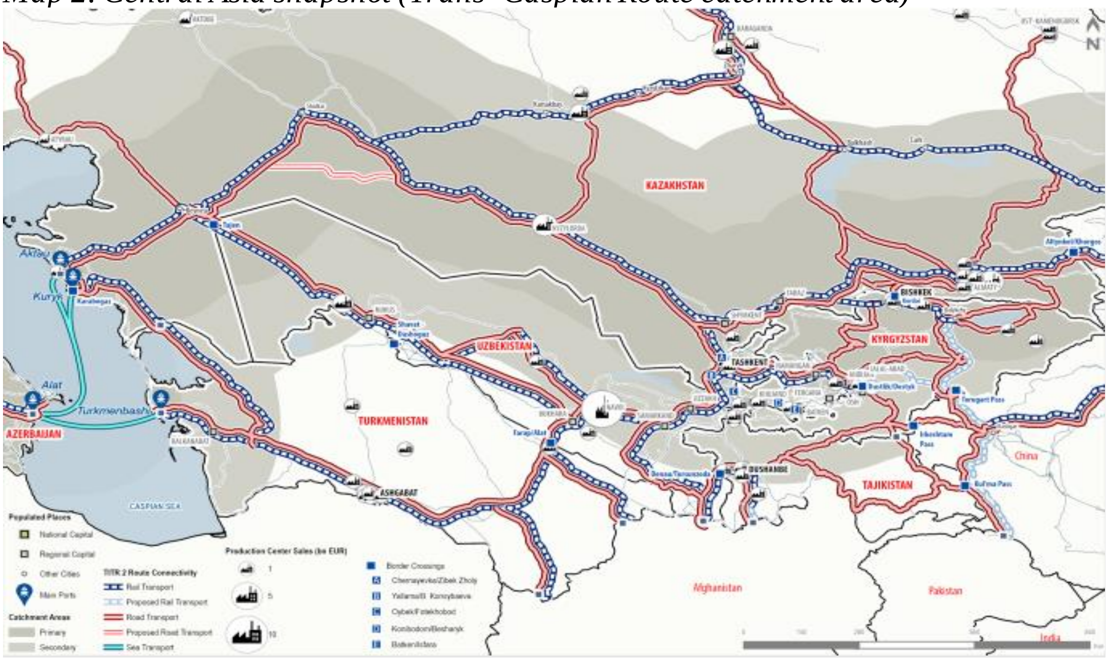
Map 1. Issyk-Kul Ring Road



**Costing estimate for the EBRD financed section includes PIS & Construction Supervision.*

Additionally, the Project is aligned with the findings of the EBRD-led and EU-funded, study on the sustainable transport connections between Europe and Central Asia. Based on the high-level financial, economic, political, social and environmental sustainability assessment of different route alternatives within the wider TCR (routes bypassing Northern Corridor through Russia, and traversing from the Chinese border to the Caspian Sea), the area covering South Kazakhstan and northern parts of other Central Asian countries is found to provide the highest benefits for regional economic development.

Map 2. Central Asia snapshot (Trans- Caspian Route catchment area)



This requires not only a shift in economic patterns, but also a well-developed transport network that is conducive to moving goods and people fast and in an efficient manner. Currently, high trade costs due to time delays and uncertainty are among the key reasons for the lack of regional integration.

The Project is located within the identified catchment area, potentially offering opportunities to support the KR's integration into regional and international value chains through improved transport operations, which is a major factor hampering the development of such economic opportunities.

The KR has the largest share of regional value-added in gross exports compared with other countries. This demonstrates its greater integration into regional and global value chains as a result of the country's relatively more liberal trade regime, despite its small scale. Its share of external value added in total exports is as high as 55 per cent for wholesale trade, indicating significant integration into value chains. Also, export services such as construction, finance and hospitality service include 20-30 per cent of external value, providing some bright spots for further integration.

The top three regions by industrial production in the KR are Chui, Issyk-Kul, and Jalal-Abad regions. The Chui Region is home to the capital Bishkek, connected to other countries by its rail network. It is the top producer in the country, including a variety of manufactured products such as glass, copper, and food. The Issyk-Kul region is the second by industrial production values on the east of the country bordering China and Kazakhstan. Its top export commodities include a variety of manufactured products, including food, land transport parts and accessories, medical instruments, and other finished textile products.

Given the Project is to support the transport connectivity of the Issyk-Kul Lake region, both domestically and internationally, it provides an opportunity to the KR to facilitate diversification and economic development. This would support further integration of local producers into value chains, starting with bright points including wholesale trade, and tourism, and then on a wider scale benefiting from possible spillovers to the rest of the economy.

ANNEX 2 – GREEN ASSESSMENTS

Introduction

The Project involves reconstruction of an estimated 30 km sub-section as part of the Issyk-Kul Lake ring-road of 440 km. The Project was subject to the PA alignment and GET eligibility assessments. As a sovereign transaction, climate-related financial risk assessments were not applicable. The Project is assessed as aligned for both mitigation and adaptation goals of the PA. The Project is expected to deliver climate resilience outcomes of reduced weather-related damage to the road assets and reduced weather-related disruption on the road network. This results in a GET attribution of 16 per cent, in line with the GET Handbook and the j-MDB methodology for attribution of climate adaptation finance.

Paris Agreement alignment

Alignment with the mitigation goals of Paris Agreement

The Project was subject to a specific assessment for alignment with the mitigation goals of the Paris Agreement. The key findings from this assessment are as follows:

The Project is consistent with the Kyrgyz Republic Nationally Determined Contribution ("NDC"). The KR submitted[5] an updated NDC for the period up to 2025 and up to 2030 in October 2021. A long-term strategy ("LTS") is not yet submitted[6]. The NDC does not quantitatively disaggregate further the contribution of individual sectors emissions reductions to the unconditional target. As such, it is not possible to draw any further definitive conclusions from the NDC. In any case, as the Project is reducing emissions, the Project will contribute positively to NDC objectives by reducing overall emissions compared with a BAU scenario.

The Project is consistent with a low-carbon pathway ("LCP"). In the absence of a national or regional low-carbon pathway for passenger and freight connectivity, the Bank assessed the Project against benchmarks from the IEA Net Zero 2050 scenario[7]. This scenario signals that vehicle fleet electrification is a key benchmark for transport decarbonisation. As such, consistency of the Project with the LCP primarily entails being compatible with EVs and other alternative fuel vehicles, and being able to accommodate infrastructure required for charging of future low-carbon vehicle fleets. The project section is 30km long and is located between two municipalities. The proposed EU Alternative Fuels Infrastructure Regulation ("AFIR") as part of the Fit for 55 regulatory package indicates that a charging station should be made available at least every 60km on main highways. Application of this framework in this context as a proxy suggests that no specific provision for charging infrastructure along the route is required to demonstrate consistency with the global LCP.

The Project demonstrates a low-risk of carbon lock-in. Road infrastructure delivers passenger and freight connectivity, and the infrastructure needs to be considered in the context of a wider transportation system alongside other modes. A high-level qualitative review of whether the Project prevents investments in low carbon emission modes of transport was also undertaken. It is not anticipated that the road connection will undermine rail usage, as there is no railway infrastructure in that part of the country. Moreover, developing railway infrastructure in that area would require a

[5] https://unfccc.int/NDCREG
[6] https://unfccc.int/process/the-paris-agreement/long-term-strategies
[7] https://www.iea.org/reports/net-zero-by-2050

disproportionate investment considering the population covered and the likely economic benefit.

Carbon lock-in assessment also looks at whether there is a high likelihood of transition to low-carbon vehicle fleets within the lifespan of the asset. Scenarios for fleet electrification were prepared for the Bank as part of technical due diligence to inform the economic assessment. Conservative scenarios see a significant displacement of internal combustion engine vehicles in the overall fleet (approximately 40 per cent) over the lifespan of the asset. As (1) the Project is in an isolated part of the country with no rail alternatives with low population density, (2) is an inter-urban road (as opposed to urban roads that present a higher risk of carbon lock-in), (3) does not prevent alternative modes from being developed, and (4) there is a high likelihood of eventual transition to low carbon vehicle fleets, the risk of carbon lock-in is assessed as low.

The Project is economically viable, incorporating a shadow price of carbon. The majority of emissions from the Project are related to scope 3 emissions associated with vehicle fleets. The Project has average annual absolute emissions of 33ktCO2e per year (with project scenario) and peak absolute emissions of 41ktCO2e/year in 2047. There is a net decrease in average annual Scope 3 emissions of approximately 13ktCO2eq/year over the assessment period (2025-2050). The traffic and economic assessment incorporating a shadow price of carbon results in a positive economic case, compared with a no-project scenario.

Based on the assessments undertaken above, the Project is considered as aligned with the mitigation goals of the PA.

Alignment with the adaptation goals of Paris Agreement

A comprehensive climate risk assessment identified floods and extreme heat events as the major hazards for the road, as well as rockfalls. Suitable resilience measures, both in design and maintenance will be included in the. Such specific measures include changing pavement materials, replacing a bridge (or at least, significantly increasing its resilience) and adapting the drainage design. The Project does not undermine the resilience of wider systems as it does not have a material negative impact on any associated water and land systems. In addition, it is not inconsistent with the national policy for context adaptation.

Based on the application of the three-step approach, the Project is considered aligned with the adaptation goals of the PA.

GET attribution

A GET share of 16 per cent is attributed to this Project based on the Climate Resilience Outcomes that the Project is expected to deliver. The three-step approach in line with j-MDB methodology for attribution of climate adaptation finance was followed. The GET adaptation finance assessment is based on reductions in both weather-related damage to the road infrastructure and weather-related disruption to traffic on the road network, that result from financing and implementing a climate-resilient road design. Specifically, the cumulative impact of structural resilience measures as well as improved monitoring are estimated to reduce vulnerability to damage and disruption from floods, extreme and chronic heat events and rockfalls.

ANNEX 3 – PROJECT IMPLEMENTATION

Procurement classification – *Public sovereign*

[REDACTED]

For the purposes of this annex, the reference to the Client is the reference to the MoTC. The Client's capacity was assessed as a part of the Project due diligence by the PIA using the EBRD capacity assessment toolkit (simplified). All categories, i.e. legal framework, organisation of procurement function, support & control systems, staffing, record keeping, procurement planning, procurement cycle, general assessment of the Client, as well as the project risks have been assessed.

It was found that the Project Implementation Unit (PIU) already exists within the MoTC and has experience in implementation of IFI funded projects, including the EBRD financed Osh-Isfana Road Upgrading project. However, the size as well as the complexity of the proposed Project exceeds the Client's overall capacity for supervision and project implementation. In addition, existing PIU is working mostly on ADB funded projects almost at full capacity.

Contracts risk assessment – Moderately Low
The Project capital expenditure component consists of one tender, where the works contract will be based on FIDIC Multilateral Development Bank (MDB) Harmonised version (Pink Book). The PIU is familiar with the mentioned form of the contract and no complications in terms of the contract administration are foreseen.

Moreover, the PIU will be supported by an international consultant during the procurement process, tendering, contract implementation as well as construction supervision, acting as a FIDIC Engineer.

Project implementation arrangements:
The PIU has already been established within the MoTC by the decree of the Government of KR to manage projects in road sector. The PIU is a government entity working in coordination with various departments of the MoTC and other relevant agencies and organizations. However, due to the existing PIU being fully devoted to other projects, it is envisaged to finance involvement of several individual experts that will strengthen the PIU and be devoted only to the Issyk-Kul Ring Road Improvement Project. To build up the PIU implementation capacity further it is intended to select the TC funded reputable consultant who will also prepare the tender documents and assist with project management and reporting as well as construction supervision services. The Lender's Monitor will be engaged by the Bank to: (a) monitor and audit the performance of the PIU and the MoTC, as the implementing agency; (b) assist the Bank to monitor the implementation of the Construction contract; and (c) identify any material issues which may threaten a successful implementation of the Project so that a corrective action can be taken.

Procurement arrangements:
Works contract to be financed from the Loan proceeds will be procured via electronic portal ECEPP using the 'Open' two stage tendering procedures in accordance with the Bank's Procurement Policies and Rules Section III Article 3 and using the Bank's

Standard Tender Documents for Works. Despite the fact that a detailed design will be available for the road construction, the Client requested to avoid following the single stage open tendering process in order not to be under the “influence of a price” and agreed to undergo a two-stage process. As further clarified by the Client, it is a common practice for high value contracts. The procurement exercise will be subject to a Selective Review.

All consultancy contracts will be procured via ECEPP in accordance with the EBRD PP&R Section III Article 3.

All contracts will be subject to the Bank's prior review. The Project procurement plan is provided below. No derogation from the Bank’s Procurement Policies and Rules is proposed. [REDACTED].

ANNEX 4 – PUBLIC DEBT SUSTAINABILITY IN THE KYRGYZ REPUBLIC

The Kyrgyz economy expanded by 3.3 per cent year on year in January-August 2023, below the 2022 growth rate of 7.0 per cent. However, this slowdown was almost entirely due to a contraction (-12.4 per cent) in a single sector – gold and base metals – which accounts for more than 50 per cent of the country's manufacturing output. Other manufacturing activities expanded at increased rates, led by the fast-growing, labour-intensive textile sector (+ 44 per cent year on year). The revival of tourism provided a boost to hospitality (+ 16 per cent) and other services, such as wholesale and retail trade (+ 15.5 per cent), despite a plunge in net remittances (-28.4 per cent) due to high base effects. In January-July 2023, imports and exports grew 29.4 and 45.6 per cent year on year, respectively, on the back of a resumption in gold exports and a boom in intermediated trade activities.

Inflation peaked at 16 per cent in February 2023, but slowed to 9.6 per cent in September 2023. Having raised the interest rate from 5 per cent in January 2021 to 14 per cent in March 2022, the National Bank of the Kyrgyz Republic reduced it by 1 per cent to 13 per cent in November 2022 (no changes as of late October 2023). The Kyrgyz som has been relatively stable against the US dollar since early 2023.

In January-July 2023, budget revenues increased 32.7 per cent year on year. Sales tax receipts grew nearly threefold, driven mainly by improvements in tax administration, while significant gains were recorded in receipts from all tax and non-tax revenue sources. Expenditures grew as well (+ 30.6 per cent), but the budget recorded a small surplus of about 1.2 per cent of GDP. The International Monetary Fund (IMF) continues to project an increase in the fiscal deficit as a result of recent hikes in public wages and pensions and ambitious public investment plans.

The share of public debt to GDP dropped from 56.2 per cent in 2021 to 49.2 per cent in 2022, mostly thanks to strong economic growth. IMF assesses the overall risk of debt distress as moderate and projects public debt to GDP ratio to decline, reaching 47.9 per cent by 2028. While most of the public debt is FX-denominated, high share of concessional debt (98 per cent of external debt) helps mitigate foreign currency risks. [REDACTED].

ANNEX 5 – TRANSITION IMPACT SCORING CHART

Score for primary transition quality

Quality: Integrated

Component: Overall

Quality average score: 65.0**

ATQ adjustment

Country: Kyrgyz Republic

ATQ adjustment: Overall: 5.3%

Adjusted Quality score: 68.4

Score for secondary transition quality

Quality: Resilient

Component: Overall

Quality average score: 67.5

ATQ adjustment

Country: Kyrgyz Republic

ATQ adjustment: Overall: 4.5%

Adjusted Quality score: 70.5

Weighted TI score*

Base TI score (ATQ-adjusted): 68.9

Adjustment for Country Strategies

Adjustment: 2.0% – Strategic project alignment

CS **Adjusted score:** 70.3

Final TI score

Final TI score: 70

***The Primary Quality score is weighted 75% for the calculation of the Base TI Score. The Secondary Quality is weighted 25%.

** Based on PSD's recommendation from Dec 2022, the Integrated TI score was manually adjusted from 60 to 65 reaching project TI score of 70.

ANNEX 6 – SSF TC FICHE

[REDACTED]