

**DOCUMENT OF THE EUROPEAN BANK  
FOR RECONSTRUCTION AND DEVELOPMENT**

Approved by the Board of Directors on a no-objection basis on 4 June 2024<sup>1</sup>

**KYRGYZ REPUBLIC**

**UPGRADE OF RECHNAYA SUBSTATION**

*[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]*

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<sup>1</sup> 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

CAPS	Central Asian Power System
DD	Due Diligence
E&S	Environmental and Social
EBITDA	Earnings Before Interest, Tax, Depreciation and Amortization
EBIT	Earnings Before Interest and Tax
EPC	Engineering, Procurement and Construction
ESAP	Environmental and Social Action Plan
ESDD	Environmental and Social Due Diligence
ESMS	E&S Risk Management Systems
EUR	Euro
FX	Foreign Exchange
GDP	Gross Domestic Product
HTM	Historical Twelve Months
HPP	Hydropower Plant
IFI	International financial institution
IFRS	International Financial Reporting Standards
KR	Kyrgyz Republic
MDB	Multilateral Development Bank
MoF	Ministry of Finance
MoU	Memorandum of Understanding
NEHC	National Energy Holding Company
PIA	Project Implementation Advisor
PIU	Project Implementation Unit
PP&R	Procurement Policies and Rules
PPA	Power Purchase Agreement
SFF	EBRD Shareholder Special Fund
SIF	Sustainable Infrastructure Fund
TC	Technical Cooperation
TDD	Technical Due Diligence
USD	US Dollar

### CURRENCY EQUIVALENTS

EUR / KGS (Soms)	94.67 as at 19.04.2024
USD / KGS (Soms)	89.01 as at 19.04.2024

### MEASURES

GW	Gigawatt
kV	Kilovolt
kWh	Kilowatt-hour
MW	Megawatt
TWh	Terawatt-hour

## **PRESIDENT’S RECOMMENDATION**

This recommendation and the attached Report concerning an operation in favour of the Kyrgyz Republic (the “Borrower”), are submitted for consideration by the Board of Directors.

The facility will consist of a sovereign loan to the Borrower in the amount of up to EUR 4.84 million. The loan will be on-lent to the National Electric Grid of the Kyrgyz Republic OJSC (the “Company”), majority state-owned electricity transmission and distribution company, which will be the project implementation entity. The loan is proposed to be co-financed by an investment grant of EUR 2.75 million from the EBRD Shareholder Special Fund (“SSF”).

The operation builds on the Bank’s broad efforts in supporting power sector reform in the Kyrgyz Republic, in parallel with investments, through well-designed projects combined with institutional support. It will enable the Company to finance modernization and voltage upgrade of the existing Rechnaya substation, located in Osh city, enhancing reliability of energy supply. The Project will strengthen the local grid to help integration of renewables, lead to reduction of technical losses and is expected to achieve an estimated carbon emission reduction of 5,354 tonnes of CO<sub>2</sub> a year. The expected transition impact of the project is through the Green quality and the Project’s GET share is 100% through mitigation and adaptation benefits.

Pre-signing project preparation TC was funded by the Government of Japan via Japan-EBRD Cooperation Fund (“JECF”). The post-signing TC package is proposed to be financed by an international donor or the Sustainable Infrastructure Fund (“SIF”).

I am satisfied that the operation is consistent with the Bank’s Energy Sector Strategy, the Green Economy Transition Approach as well as the Strategy for the Kyrgyz Republic and with the Agreement Establishing the Bank.

I recommend that the Board approve, on a no-objection basis, the proposed loan and SSF investment grant substantially on the terms of the attached Report.

**Odile Renaud-Basso**

## BOARD DECISION SHEET

<b>KYRGYZ REPUBLIC – UPGRADE OF RECHNAYA SUBSTATION – DTM 55487</b>	
<b>Transaction / Board Decision</b>	<p>Board approval<sup>2</sup> is sought for a sovereign loan of up to EUR 4.84 million in favour of the Kyrgyz Republic (the “KR” or the “Borrower”). Board approval is also sought for the use of EBRD Shareholder Special Fund (“SSF”) funds in the amount of up to EUR 2.75 million for co-investment grant.</p> <p>The proceeds of the loan and the grant will be used to finance the modernization and upgrade of the operating 35kV “Rechnaya” substation in Osh region of Kyrgyz Republic to 110kV voltage (the “Project”).</p>
<b>Client</b>	<p>The facility consists of a sovereign loan to the Kyrgyz Republic. The Project will be implemented by National Electric Grid of Kyrgyz Republic OJSC (the “Project Entity” or the “Company” or the “NEGK”), the national electricity transmission and distribution systems operator in the Kyrgyz Republic. The Company is 94% owned by the state and 6% by minority shareholders.</p>
<b>Main Elements of the Proposal</b>	<p><u>Transition impact</u></p> <ul style="list-style-type: none"> <li>Primary Quality – Green (Direct Track). The Project is expected to improve reliability, service quality of power supply, and facilitate transmission of energy from renewable sources and connection of new consumers to the electric grid. As the result of the project implementation, electricity losses are expected to reduce by c. 54.6 GWh annually, which corresponds to 5,354 tons of CO<sub>2</sub>/year emission savings. The Project is in line with EBRD's Green Economy Transition (GET) Approach and will deliver climate mitigation and adaptation benefits through modernization of the substation.</li> </ul> <p><u>Additionality</u></p> <ul style="list-style-type: none"> <li>Financing structure: The Bank provides long-term financing which is not available from local commercial banks.</li> <li>Standard-setting: The Bank will support the Project Entity in achieving higher standards above the current practice in the country through its conditionalities (e.g. PP&amp;R and ESAP). The Project Entity will benefit from EBRD's expertise on international procurement standards.</li> </ul> <p>Sound banking</p> <ul style="list-style-type: none"> <li>The financing is structured as a sovereign loan to the Kyrgyz Republic.</li> </ul>
<b>Key Risks</b>	<p><i>Sovereign risk.</i> Credit risk is mitigated by the manageable level of sovereign debt to GDP ratio, which stood at 46% as of December 2023. Substantial part of the sovereign debt is concessional, and the debt is expected to remain manageable in the medium and long term. The Bank's loan is a relatively small and targeted amount and is not expected to have major impacts on the sovereign debt capacity.</p> <p><i>Implementation and project completion risk:</i> Implementation and project completion risk is mitigated by the Company's experience with procurement under the Bank's PP&amp;R and by assistance of the Project Implementation Support consultant.</p>
<b>Strategic Fit Summary</b>	<p>The Project is in line with the Bank's Energy Sector Strategy, the Green Economy Transition Approach as well as the Strategy for the Kyrgyz Republic and with the Agreement Establishing the Bank.</p>

<sup>2</sup> Article 27 of the AEB provides the basis for this decision.

## ADDITIONAL SUMMARY TERMS FACTSHEET

<b>EBRD Transaction</b>	Up to EUR 4.84 million sovereign loan to the Kyrgyz Republic (the “Borrower”), to be co-financed by a capital grant from the EBRD Shareholder Special Fund (the “SSF”) Work Plan 2023 - 2024 in the amount of up to EUR 2.75 million (or its equivalent in USD) to finance modernization and voltage upgrade of the operating 35kV “Rechnaya” substation in Osh city. The Project will contribute to strengthening the power grid resilience and will result in CO2 emission reductions.
<b>Existing Exposure</b>	Sovereign exposure to the Kyrgyz Republic ( <i>Moody’s B3/Negative</i> ): EUR 176 million. Exposure to the Project Entity: EUR 16.0 MM through the following projects: <ul style="list-style-type: none"> <li>• Oshelectro Rehabilitation Project– EUR 3.4 MM;</li> <li>• Vostoelectro Rehabilitation Project– EUR 3.4 MM.</li> <li>• Electricity Supply Digitalization Project– EUR 9.2 MM.</li> </ul>
<b>Maturity / Exit / Repayment</b>	The proposed loan tenor is [18 years]. [REDACTED].
<b>Potential AMI eligible financing</b>	None.
<b>Use of Proceeds</b>	The proceeds of the Bank's financing will be used for (i) procurement and installation of equipment for 110 kV voltage upgrade, and (ii) procurement and installation of additional transformers at the operating 35 kV “Rechnaya” substation in Osh city. The use of proceeds will be monitored through application of the EBRD PP&R and via conditions precedent to disbursement, review of the progress reports on the agreed Project Implementation Plan (PIP) and monitoring visits, as well as other standard provisions in the legal documentation.
<b>Investment Plan</b>	[REDACTED]
<b>Financing Plan</b>	[REDACTED]
<b>Key Parties Involved</b>	Kyrgyz Republic represented by the Ministry of Finance (the “Borrower”). OJSC National Electric Grid of Kyrgyz Republic (the “Project Entity”, the “Company” or the “NEGK”).
<b>Conditions to subscription / disbursement</b>	[REDACTED]
<b>Key Covenants</b>	For the Project Entity: <ul style="list-style-type: none"> <li>• Environmental and social compliance;</li> <li>• Compliance with the Bank’s Procurement Policies and Rules.</li> </ul>
<b>Security / Guarantees</b>	Sovereign loan
<b>Other material agreements</b>	Project agreement with OJSC National Electric Grid of Kyrgyz Republic. Grant agreement with the Kyrgyz Republic, EBRD and the Project Entity.
<b>Associated Donor Funded TC and co-investment grants/concessional finance</b>	<b>A. Technical Cooperation (TC)</b>  <u>Pre-signing</u> <b>TC1: Environmental and Social Due Diligence:</b> The cost of the assignment amounted to EUR 12,500, funded by the Government of Japan via Japan-EBRD Cooperation Fund (“JECF”).

	<p><u>Post-signing</u></p> <p><b>TC2: Project Implementation Support:</b> This technical cooperation will aim to provide the following services to the Company:</p> <p>(i) assistance with procurement of the goods, works and services under the Project including development of tender documentation, tender evaluation and contracting, (ii) assistance with the establishment of the PIU; (iii) assistance with the supervision of contracts' implementation and supervision of the works (in the role of the contracts' Engineer); and (iv) environmental and social implementation support and assistance with compliance and reporting obligations under the financing documents. Total estimated cost of the assignment is up to EUR 500,000 and it is proposed to be financed by an international donor or the SIF.</p> <p><b>Reimbursement:</b> The assignments above will not be reimbursable.</p> <p><b>Cost-sharing:</b> No financial contribution is expected from the Company due to the affordability constraints. In line with the Bank's cost-sharing policy dated 1 January 2021, financial contributions will not be provided taking into account Company's public utility status and no pass-through of such contribution in the regulated tariff. The Company will be providing in-kind contribution (office space, local transportation etc.).</p> <p><b>B. Co-investment grants / Concessional Finance (Non-TC)</b> The Project is expected to be co-financed by a EUR 2.75 million investment grant from the SSF Work Plan 2023 - 2024.</p>
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[REDACTED]

## **INVESTMENT PROPOSAL SUMMARY**

### **1. STRATEGIC FIT AND KEY ISSUES**

#### **1.1 STRATEGIC CONTEXT**

The Project supports the Kyrgyz Government's objective to promote climate mitigation activities as reflected in its updated Nationally Determined Contributions (NDC), where the Government has set a mitigation goal of reducing greenhouse gas emissions by 43.62% by 2030. At COP28, Kyrgyz Republic also endorsed the Global Renewables and Energy Efficiency Pledge, targeting tripling the world's installed renewable energy generation capacity to at least 11,000 GW by 2030. The Project forms part of grid enhancements that will be critical to achieving this target.

Addressing bottlenecks in the transmission grid is essential to accelerate renewable energy integration in Kyrgyz Republic, reduce GHG emissions and ensure reliable electricity supply to the population, including through the increased power sector resilience to climate change. Kyrgyzstan's hydro-rich energy sector is characterised by the ageing infrastructure and significant losses, which are exacerbated by a combination of climate shocks (draughts, severe winter conditions etc.) and growing demand. The sector has been suffering from years of underinvestment and lack of cost-reflective tariffs. Particularly, c.90% of the existing power substations are more than 25 years old, demonstrating high deterioration of transmission system network. The system's technical and commercial losses stand at 11.6% (as of YE2023) which is higher than international standards. These challenges pose a significant threat to the country's energy security and make it particularly vulnerable to the impacts of climate change. Thus, the modernization of the Rechnaya substation will strengthen the local grid, which in turn will pave the way for transmission of electricity from renewable sources to consumers in Osh city.

The Bank and other IFIs have been encouraging the Kyrgyz Government to address the long-lasting challenges in the energy sector. To support the Government with priority reforms in the energy sector, in January 2022 the Bank signed a memorandum of understanding ("MoU") with the Kyrgyz Ministry of Energy with an objective of fostering the development of renewable energy including through modernization of energy infrastructure. Further to this, in February 2024, the Bank signed an MoU with the Ministry of Energy to cooperate in developing renewable energy projects and develop the first wind auction in the country on a pre-selected location through the EBRD funded technical cooperation program.

The proposed Project, the Bank's first financing of the transmission grid upgrade in the Kyrgyz Republic in the last 20 years, builds on this policy dialogue and on the Bank's previous engagement with NEGK which focused on the low-voltage distribution networks. Most recently, in November 2023, the Bank signed the Electricity Supply Digitalization Project providing financing for procurement of household smart meters and rehabilitation of low-voltage distribution infrastructure. The Project is expected to reduce technical losses in the transmission grid, as well as to improve the reliability of the grid through expanding capacities of the existing substation, thus reducing loads in the local grid infrastructure. The Project will also help avoid wide-spread shutdowns caused by overvoltage thanks to introduction of modern circuit breakers.



Furthermore, improvement of grid resilience under the Project is expected to have a positive regional impact. Specifically, the Kyrgyz Republic aims to connect renewable energy to the grid and interconnect with the grids of the neighbouring Kazakhstan and Uzbekistan to provide balancing capacity and supply green energy under the regional initiatives. Grid improvements are expected to enable the Kyrgyz Republic become a net exporter of clean energy and provide balancing services to Kazakhstan and Uzbekistan.

The Project is expected to be co-financed by an SSF investment grant of up to EUR 2.75 million. The grant component will help strengthen the country's energy sector by improving reliability of electricity supply and modernizing the country's ageing infrastructure. As the country has limited debt capacity, following the guidelines of the IMF, mobilising concessional finance is essential to ensure affordability while the necessary investments take place. In accordance with the current IMF programme, the Kyrgyz Republic needs to refrain from contracting or guaranteeing non-concessional debt. Public Debt Management Strategy of the Kyrgyz Republic, adopted by the Ministry of Finance, further specifies the minimum required grant intensity level of 35% in all new projects. The proposed Project is in line with the Bank's Strategy for Kyrgyz Republic, Energy Sector Strategy 2024-2028 and supports the Bank's Green Economy Transition Approach. The Project contributes to several UN Sustainable Development Goals ("SDGs"), namely: SDG 7. Clean and Affordable Energy, SDG 9: Industry, Innovation and Infrastructure, and SDG 13. Climate Action.

## 1.2 TRANSITION IMPACT

The table below sets out the TI Objectives and details of the project.

### Primary Quality: Green (GET Direct Track)

Obj. No.	Objective	Details
1.1	<i>The percentage of EBRD use of proceeds that supports a green economy transition and therefore qualifies as GET finance exceeds 50%.</i>	The share of GET-compliant EBRD proceeds is 100%. The Project will contribute to reduction in the electricity losses estimated in the amount of 54.6 GWh/year, translating into reduction of GHG emissions in the amount of 5,354 tons/year.

Delivery Risks: One of the main risks is associated with the Project implementation, which will be mitigated by a Project Implementation Support consultant to assist with the Project procurement and construction supervision.

## 1.3 ADDITIONALITY

Identified triggers	Description
A subsequent/consecutive transaction (issuance) with the same client/group either with the same use of proceeds or	The Project will be the Bank's first financing of transmission grid upgrade in Kyrgyz Republic in the last 20 years. The Bank previously provided sovereign loans to Kyrgyz Republic that were on-

in the same destination country ( <b>repeat transaction</b> ).	lent to JSC Oshelectro (Oshelectro Rehabilitation Project) and JSC Vostokelectro (Vostokelectro Rehabilitation Project), two low voltage distribution companies existing as separate entities until September 2022, and now part of NEGK after the distribution sector reorganization, aimed at increasing corporate efficiencies. In November 2023, the Bank provided a loan to NEGK to provide smart meters to households and rehabilitate low-voltage distribution lines (Electricity Supply Digitalization Project Building on these efforts to strengthen electricity distribution system in the Kyrgyz Republic, the Bank is working with the Kyrgyz government and NEGK, on the upgrade of the transmission infrastructure to ensure stability and reliability of the electricity grid. The Project will enable the Bank to strengthen its involvement in the country's energy transition efforts, through modernizing the substation to ensure uninterrupted electricity supply to consumers. Given large investment needs in modernizing the ageing grid infrastructure coupled with the tariff affordability concerns, the long-term financing is viewed as key for sustainable development of the energy system in the country.
<b>Additionality sources</b>	<b>Evidence of additionality sources</b>
<b>Financing Structure -</b> EBRD offers a <b>tenor</b> , which is above the market average and is necessary to structure the project.	The Bank will provide a loan with [18 years] tenor [REDACTED] which is not currently available from commercial banks in the local market.
<b>Standard-setting: helping projects and clients achieve higher standards</b> Client seeks/makes use of EBRD expertise on <b>best international procurement standards</b> .	EBRD is providing the Project Implementation Support that ensures the use of international procurement standards and is also designed to strengthen the Company's procurement capacity. The Bank's conditionalities such as applying EBRD PP&R and implementation of ESAP will help develop the Company's capacity and allow for the Project's efficient implementation.

#### 1.4 SOUND BANKING – KEY RISKS

Risks	Probability / Effect	Comments
Sovereign risk	Low / High	Kyrgyzstan has increasingly borrowed from bilateral creditors to address the most critical bottlenecks in the infrastructure sector. Kyrgyz Republic remains vulnerable

		<p>to inflationary pressures, international commodity price volatility and fiscal policy. According to the IMF, the general government deficit is estimated to widen to 5.2% of GDP from 0.8% in 2021 and remain slightly under 5% of GDP in the medium term.</p> <p><i>Mitigating factors:</i> sovereign debt reduced from 68.1% of GDP in 2020 [REDACTED] to 46% by the end of 2023. In accordance with the IMF recommendations, the major part of sovereign debt for Kyrgyzstan was raised on a concessional basis. Most of KR's debt remains external. At the same time, KR's gross international reserves have expanded from USD 2,978 million in December 2021 to USD 3,492 million in April 2024. Overall, IMF estimates Kyrgyzstan's public debt to GDP ratio to decline, reaching 42% by 2028. The risk of debt distress is expected to remain moderate.</p>
Implementation and procurement risk	Medium Medium	<p>Project implementation may incur cost overruns and/or completion delays.</p> <p><i>Mitigating factors:</i> the Company has experience implementing EBRD financed projects. A standalone PIU will be established to coordinate, manage, monitor and evaluate all aspects of the Project. An international consultant will assist with the Project's implementation. Application of the EBRD's PP&amp;R should ensure that an experienced and creditworthy contractor is selected to perform the work and that a balanced construction contract is signed between the parties. Engineering supervision will further mitigate implementation risks. Please refer to further details on the Project implementation in <b>Annex 1</b>.</p>
The Company's creditworthiness as first source of repayment	Medium Medium	<p>Creditworthiness of the Company depends on the tariff increases.</p> <p><i>Mitigating factors:</i> The World Bank and the Bank are supporting the Government with tariff reforms and sector development to help enhance the financial viability and improve transparency and accountability in the power sector. The most recent positive development was end-users tariff indexation effective from May 1<sup>st</sup>, 2024, which entails 10.8% CPI-indexation for all consumer groups. The change will strengthen the Project's feasibility as NEGK's profitability is expected to grow helping it to fund its capital expenditures program. Ministry of Finance is to inject additional equity into the Company to support its debt service obligations, according to the Government Decree of August 2023. [REDACTED] Ultimately the loan repayment is protected by the sovereign nature of the loan.</p>

Currency Risk	Medium High	/	<p>The loan currency is denominated in EUR, whereas the Company revenues are in Kyrgyz som. Devaluation in local currency may have an adverse impact on the Company's debt service ability.</p> <p><i>Mitigating factors:</i> The cost-reflective tariff methodology, effective from 2023, would allow the Company to increase the tariffs in line with inflation partially offsetting the currency devaluation risk.</p>
Political and governance risk	Medium High	/	<p>[REDACTED]The energy sector is particularly prone to the risk due to the ongoing restructuring and consolidation, which as reported by the World Bank, if poorly implemented, can increase the risk and threaten sustainability of the energy reforms.</p> <p><i>Mitigating factors:</i> The Government has taken measures to mitigate these risks including by preparation of information outreach and communication campaigns, supported by the IFIs through continuous engagement with the authorities to provide policy dialogue and advisory support.</p>

## 2. MEASURING / MONITORING SUCCESS

Overall objectives of project	Monitoring benchmarks	Implementation timing
Timely implementation of the Project	Completion according to the timeline and within the budget	[REDACTED]
Maintaining appropriate environmental standards	Successful and timely implementation of the ESAP	[REDACTED]

### Primary Quality: Green

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date
1.1	Energy savings (GJ/year)	Energy savings stemming from electricity losses reduced as the result of the Project	0	196,693	[REDACTED]
1.2	CO2e emissions reduced (tonnes/year)	Confirmation on GHG emission reduced as a result of electricity losses reduction	0	5,354	[REDACTED]

## 3. KEY PARTIES

### 3.1 BORROWER

The EBRD will extend a sovereign loan to the Kyrgyz Republic (B3/Negative by Moody's). The macroeconomic profile of Kyrgyz Republic is underpinned by the economy's solid growth potential and financial and technical assistance of development partners, which keep debt servicing costs low and external vulnerability contained. The country's economy has rebounded with 3.6% GDP growth in 2021 and 7% growth in 2022 and grew by further 6.2% in 2023. Annual inflation halved to 7.3% in 2023. The Kyrgyz som has been relatively stable against the US dollar since early 2023.

In 2023, budget revenues increased by 35.2% 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. On 4 March 2024, IMF updated Kyrgyz Republic's medium term GDP growth forecast to 4% and inflation forecast to 8.0%.

Sovereign debt that had been declining since 2015, increased to 68% of the GDP during 2020, due to additional external financing and depreciation of the Kyrgyz som, but reduced to 46% by 2023 year-end and is expected by the IMF to further decline, reaching 42% by 2028, implying a medium risk of debt distress. As of 2023, KR's public debt stood at US\$ 6.3 billion, around 70% of which (US\$ 4.48 billion) is external. Multilateral concessional loans account for 52.4% of external debt and bilateral concessional debt accounts for 46.3%. The external public debt has declined from 49.2% of GDP in 2021 to 41% of GDP in 2023. While most of the government debt is FX-denominated, the high share of concessional debt (98 % of external debt) helps mitigate foreign currency risks. Shrinking in January-April 2023, Kyrgyz Republic's international reserves have been trending upward in recent months and amounted to US\$ 3.492 billion in April 2024 (up 26% y/y). As per the IMF, KR's risk of debt distress is expected to remain "moderate" as its sovereign debt is largely made up of long-term concessional loans and is backed by adequate FX reserves.

### 3.2 PROJECT ENTITY

The Project will be implemented by the National Electric Grid of Kyrgyzstan OJSC (the "Project Entity" or the "Company" or the "NEGK"), transmission and distribution systems operator, that owns and operates more than 10,000 km of power transmission lines of 110 kV and higher, as well as 190 substations with primary voltages of 500, 220 or 110 kV.

The Company is 94% owned by the state (61% by Ministry of Energy of Kyrgyz Republic and 33% by the Ministry of Finance of Kyrgyz Republic). The remaining 6% shares are owned by minority shareholders. NEGK has been the Bank's client since 2015 through Oshelectro Rehabilitation Project, Vostokelectro Rehabilitation Project and Electricity Supply Digitalization Project. NEGK transports around 12 TWh of energy on an annual basis, and brings wholesale electricity to Kyrgyz energy distribution companies, large industrial consumers as well as to the neighbouring countries - Kazakhstan, Uzbekistan and Tajikistan. In 2023, NEGK sold 11.9 TWh of electricity to the following groups of customers: residential (62%), industry (12%), state organizations (8%), agricultural (2%) and others (16%). The electricity losses in the transmission and distribution grid constituted 11.6% as of 2023 and are expected to be reduced as part of the broader transmission and distribution grid rehabilitation efforts.

## 4. MARKET CONTEXT

The Kyrgyz power sector was restructured in 2002, when the national utility was unbundled into generation, transmission and distribution. State-owned JSC Electric Power Plants is the largest electricity generator, and NEGK is the state-owned transmission system operator (TSO) that also operates the national dispatch service. As the result of further reforms in the energy sector, all four local distribution companies were merged with NEGK in 2022 in order to save costs and improve corporate efficiency through consolidation.

More than 80% of electricity generation in the country relies on the hydropower. As of 2023, JSC “Electric Power Plants” operated 7 HPPs and 2 CHPs with the total installed electricity capacity of c. 3.9GW, generating 98% of total electricity in the country. NEGK is responsible for electricity transmission through high voltage grid (110kV-500kV) and for distribution to ultimate customers.

The Kyrgyz energy system faces 3-5% growth in demand annually. Electricity generation fluctuates between 12 TWh and 14 TWh depending on the inflow of water and the amount of water accumulated in the Toktogul reservoir. The Kyrgyz Republic has traditionally been a net exporter of electricity, but export has diminished in the last decade due to increased domestic demand with the country becoming a net importer.

The energy system of the Kyrgyz Republic is divided into northern (60% of electricity consumption, 20% hydropower capacity) and southern (40% of electricity consumption, 80% of hydropower capacity) parts, which are connected by a 500 kV Toktogul-HPP Frunzenskaya line and a 500 kV Datka-Kemin line, as well as through the Central Asia Power System (“CAPS”). Total depreciation of the NEGK equipment is 36% for high voltage lines of 110-220-500 kV and 69% for substations of 110-220-500 kV, demonstrating chronic underinvestment in the past decades.

Electricity tariffs to end-users are set by the regulator based on the Mid-Term Tariff Policy (MTTP) approved by the Government. The recent amendment to the 2021-25 MTTP that is effective from May 1<sup>st</sup>, 2024 introduced tariff increases for population by c.11% to 1.11 KGS/kWh or USDc 1.24/kWh and by different levels for businesses. In terms of the purchase tariffs, NEGK pays 0.511 KGS/kWh or USDc 0.6/kWh to JSC “Electric Power Plants”.

The Government’s primary focus is on modernizing the electricity grid, diversifying energy sources including via integration of utility scale renewable energy (sun, wind) and increasing domestic production, mainly from hydropower, given that the potential of Kyrgyzstan's rivers is approximately ten times what is currently utilised.

## 5. FINANCIAL ANALYSIS



## **5.1 FINANCIAL ANALYSIS OF THE PROJECT ENTITY**

[REDACTED]

## **5.2 PROJECTED PROFITABILITY FOR THE BANK**

[REDACTED]

# **6. OTHER KEY CONSIDERATIONS**

## **6.1 ENVIRONMENT**

Categorised B (2019 ESP) as the environmental and social risks associated with the acquisition and replacement of transformers as part of modernisation of site-specific substation, are readily identified and can be mitigated through good management practice. The Bank has ongoing relationship with National Electric Grid of Kyrgyz Republic OJSC (“NEGK”) and a corporate Environmental and Social Action Plan (“ESAP”) was agreed as part of Electricity Supply Digitalization Project at the end of 2023.

The Bank’s Environmental and Social Due Diligence (“ESDD”) has been carried out by an independent consultant and included E&S documentation reviews, a site visit and a review of the Client’s current operations, E&S management practices as well as an assessment of the E&S risks associated with the proposed Project.

The results of the ESDD have re- confirmed that NEGK has limited organisational capacity and does not have an environmental and social management system (ESMS) in place. Organisational capacity will need to be enhanced and an ESMS developed and implemented in accordance with PR1. Contractors will be obliged to adhere to E&S requirements through clauses included in legal agreements and be subject to contractor management plans developed by the Company.

Key issues from the ESDD relate to environmental and social management systems, pollution prevention, health and safety and, labour and working conditions.

The current ESDD identified that improvements are required for storage and management of hazardous waste, transformers oils, acid batteries, PCB and SF6. The issues related to transformers oil management will be addressed in the ESAP.

The ESDD also recommended for safety risks to be managed in accordance with national legislation however, measures will be required to improve health standards and the hygiene of working conditions. Additional measures are required to secure each project site from unauthorised access by third parties and public health and safety measures to protect nearby communities. The ESDD recommended further improvements in relation to the use of PPE, contractor's management in relation to workers H&S risks during construction and public safety, as well as formalisation of the H&R procedures and grievance mechanism.

The Project will not need to acquire any additional land or result in land use changes or economic displacement as modernisation process will take place at two operational substations. Any land required temporarily during construction will be subject to leases and reinstatement. In addition, these locations are not expected to have material impacts on

biodiversity as Project works do not pose risks to sensitive areas such as Important Bird Areas, Ramsar Sites and World Heritage Sites.

Based on the ESDD an updated ESAP has been agreed, incorporating actions to ensure the Project is structured to comply with the Performance Requirements (PRs) and good industry practice. The ESAP will address the Company's operational risks such as: hazardous waste management, the provision of appropriate personal protective equipment, health and safety measures, regular H&S trainings, hygienic workplace facilities for both men and women and, community hazard awareness raising and training. The Human Resources Policy will require improvements regarding working relationships and an employee grievance mechanism will be established.

Project-specific disclosure documentation includes a Non-technical Summary (NTS) and a Stakeholder Engagement Plan (SEP) and will be disclosed by the client. A public grievance mechanism will be established, and the Company will make effort to engage with local communities to inform them about E&S social risk mitigation planning.

The Company will receive additional technical cooperation assistance and capacity building to implement the ESAP including development of a robust E&S management system that will allow future management of E&S risks and E&S related grievances.

EBRD will monitor the Project through review of annual environmental and social reports (AESR's) and site visits, if necessary.

## **6.2 INTEGRITY**

In conjunction with OCCO, integrity due diligence was carried out on NEGK, its shareholders, their senior personnel, and other relevant parties. NEGK is a debt client of the Bank, most recently through Electricity Supply Digitalization Project. [REDACTED]

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.

## **6.3 CONCESSIONAL FINANCE**

The Project is expected to be co-financed by investment grant from the SSF of up to EUR 2.25 million. The grant component will help strengthen the country's energy sector by modernizing ageing transmission infrastructure, which will improve reliability of energy supply to consumers. As the country has limited debt capacity, mobilising concessional finance following the guidelines of the IMF is essential to ensure necessary investments take place. In accordance with the current IMF programme, the Kyrgyz Republic needs to refrain from contracting or guaranteeing non-concessional debt. Due to this reason, the Kyrgyz Government has approved a Public Debt Management Strategy specifying the mandatory grant intensity level of 35% on all sovereign projects. There is no commercial debt available in KR to finance long-term infrastructure projects requiring similarly long-term tenor financing.

The grant partially alleviates pressure on the household tariff, as investment grant related components are not envisioned to be included in the tariff calculation. Avoiding passing of the



grant-funded costs through to population through a higher tariff would have a direct impact supporting affordability for the citizens and industries in Osh region.

## ANNEXES TO OPERATION REPORT

ANNEX 1	PROJECT IMPLEMENTATION
ANNEX 2	GREEN ASSESSMENTS
ANNEX 3	EBRD SSF PROPOSAL FOR CO-INVESTMENT GRANT ALLOCATION
ANNEX 4	SHAREHOLDING STRUCTURE OF THE PROJECT ENTITY
ANNEX 5	HISTORICAL FINANCIAL STATEMENTS

## ANNEX 1 - PROJECT IMPLEMENTATION

### Procurement classification – *Public [sovereign]*

[REDACTED]. This is the second EBRD financed project with NEGK, although it should be noted that the Bank has previously worked with OJSC Vostokelectro and OJSC Oshelectro, that prior to 2022 existed as separate distribution companies, however at the end of 2022 have been merged with NEGK. After the merger, OJSC Vostokelectro and OJSC Oshelectro ceased to exist as separate entities and OJSC NEGK became the Bank's existing client. In November 2023, the Bank signed "Electricity Supply Digitalization" project with NEGK for procurement of smart meters and low-voltage cables.

For the purposes of this annex, the reference to the Client is a reference to the National Electric Grid of Kyrgyz Republic OJSC. 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 were assessed.

Areas of opportunities and improvements have been identified and discussed with the Client. [REDACTED]. Therefore, a qualified PIU Consultant will be hired (funded by the TC Funds) to support the Client in the tender preparation phase as well as during the whole procurement and project implementation phase. Furthermore, the Bank will explore options to further enhance the PIU before the start of an active phase of the project implementation.

### *Contracts risk assessment – Moderate High*

The contracts under the Project fall in the risk category "*Moderate High*". Apart from the Consultancy Contract (PIU Consultant), there will be one major Bank-financed contract under the Project, namely: Rehabilitation of Rechnaya substation. The mentioned contract will be procured through an open tender using the EBRD's Standard Procurement Documents for Works and the resulting contract will follow FIDIC Conditions of Contract for Plant and Design-Build (Yellow Book).

### **Project implementation arrangements:**

NEGK will be required to enhance the established Project Implementation Unit. The Client's PIU will be assisted by a qualified PIU Consultant for the preparation of tender documents (including concept design, employer's requirements and etc) for Works, procurement process, acting as a FIDIC Engineer and overall project implementation matters. This arrangement should strengthen the project implementation ability within NEGK and mitigate the risks of procurement as well as overall project delivery related delays. The current project (*Upgrade of Rechnaya Substation*) will be implemented by the Client in combination with Modernisation of Dolinka Substation project.

### **Procurement arrangements:**

The Works contract mentioned above in Contracts Risk Assessment section will be procured via ECEPP using the 'Open' multi-stage method, as long as the Employers Requirements are yet to be finalised. The tendering procedures will be conducted in accordance with the Bank's PP&R Section III Article 3 and using the Bank's Standard Procurement Documents for Works.

The PIS consultancy contract 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 PP&Rs is proposed. [REDACTED].

## ANNEX 2 – GREEN ASSESSMENTS

### Summary

The Project entails financing of modernization and voltage upgrade of operating 35 kV “Rechnaya” substation in Osh region.

The Project’s GET share is 100%, based on attributions under both the GET mitigation and GET adaptation methodology. The Project has been assessed as aligned with the mitigation and adaptation goals of Paris Agreement. Climate-related financial risk (CT and PC score) has been assessed as low.

### Paris alignment assessment

#### *Alignment with the mitigation goals of Paris Agreement – General screening*

The project is determined as aligned with the mitigation goals of the Paris Agreement based on the application of the Bank’s Paris alignment approach for direct finance.

- The project/economic activity **is included** in the joint MDB 'aligned list'.
- Regarding project/economic activity(ies), **there are no activities** included in the 'non-aligned list'.

#### *Alignment with the adaptation goals of Paris Agreement*

The project is considered aligned with the objectives of the Paris Agreement as climate resilience measures integrated into project design have addressed the physical climate risks assessed as material for the project: flood and heavy rainfall events, increasing heat stress and extreme wind events.

### **GET attribution**

The project is attributed 100% GET based on both climate mitigation and climate adaptation benefits it delivers. The expected impacts are:

**Climate mitigation:** the Project is expected to lead to a reduction in GHG emissions estimated at 5,354 tonnes of CO<sub>2</sub> annually, through brownfield efficiency improvement of transmission infrastructure (section 2.11 of the GET Handbook).

### **Climate Adaptation**

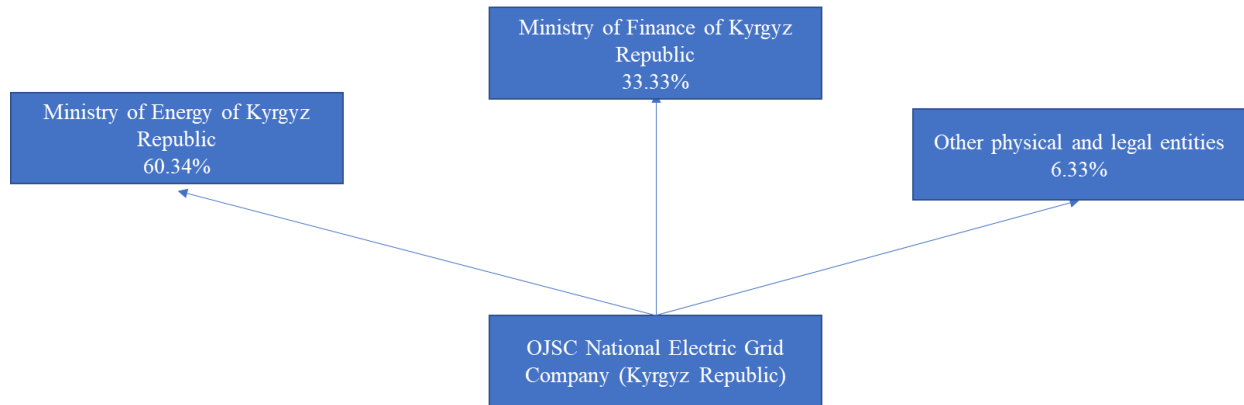
The design of the substation will integrate measures to adapt them to a range of climate hazards expected under future climate change. This will include adoption of technical standards (such as IEC6006) for the design of transformers to ensure resilience to rising temperatures, integration of design elements to raise critical equipment above ground and beyond the reach of flooding events, and the upgrading of busbars and structures to accommodate extreme wind events.

## **ANNEX 3 – EBRD SSF PROPOSAL FOR CO-INVESTMENT GRANT ALLOCATION**

[REDACTED]

## ANNEX 4 –SHAREHOLDING STRUCTURE OF THE PROJECT ENTITY

The shareholding structure of the Project Entity (NEGK) is the following:



## **ANNEX 5 – HISTORICAL FINANCIAL STATEMENTS**

[REDACTED]