

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

Approved by the Board of Directors on 29 April 2026¹

AZERBAIJAN

SHAKI WATER AND WASTEWATER

[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 (2024), 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

AESR	Annual Environmental and Social Reports
ASWRA	Azerbaijan State Water Resource Agency
AZN	Azerbaijani manat
BCR	Benefit Cost Ratio
CHIA	Cultural Heritage Impact Assessment
CHMP	Cultural Heritage Management Programme
CJSC	Closed Joint-Stock Company
CP	Condition Precedent
CO2	Carbon Dioxide
DTSP	Digital Transformation Support Programme
E5P	Eastern Europe Energy Efficiency and Environment Partnership
EBRD	European Bank for Reconstruction and Development
EIA	Environmental Impact Assessment
EIP	Economic and Investment Plan
EIRR	Economic Internal Rate of Return
ENPV	Economic Net Present Value
E&S	Environmental and Social
ESAP	Environmental and Social Action Plan
ESDD	Environmental and Social Due Diligence
ESMS	Environmental and Social Management System
EU	European Union
EUR	Euro
FIDIC	International Federation of Consulting Engineer
FOPIP	Financial and Operational Performance Improvement Programme
GAP	Governance Action Plan
GBVH	Gender-based Violence and Harassment
GDP	Gross Domestic Product
GET	Green Economy Transition
GHG	Greenhouse Gas
GPMP	Green Project Monitoring Plan
HR	Human Resources
IFI	International Financial Institution
KfW	Kreditanstalt für Wiederaufbau
MDB	Multilateral Development Banks
MWp	Megawatt-peak
MoU	Memorandum of Understanding
OJSC	Open Joint-Stock Company
O&M	Operational and maintenance
PIA	Project Implementation Advisor
PIS	Project Implementation Support
PIU	Project Implementation Unit
PLE	Public Legal Entity of ASWRA
PPR	Procurement Policies and Rules
PR	Performance Requirements
PV	Solar Photovoltaic
SCADA	Supervisory Control and Data Acquisition
SDG	Sustainable Development Goals
[REDACTED]	
SSF	EBRD Shareholder Special Fund
TC	Technical Co-operation
TCRS	Technical Co-operation Request System
VAT	Value Added Tax
VET	Vocational Education and Training
WWTP	Wastewater Treatment Plant

PRESIDENT'S RECOMMENDATION

This recommendation and the attached Report concerning an operation in favour of the Republic of Azerbaijan (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 91 million (in two tranches). The loan will be provided for the benefit of the Azerbaijan State Water Resources Agency (the "ASWRA" or the "Client"), the national institution for management and protection of water resources. The Bank's loan will be co-financed by an investment grant of up to EUR 4 million from the Eastern Europe Energy Efficiency and Environment Partnership ("E5P").

The operation will enable ASWRA to finance the construction and rehabilitation of water supply and sewerage networks, stormwater management infrastructure, biological treatment process, and sludge treatment and management facilities for the wastewater treatment plant, as well as other water infrastructure improvements for the city of Shaki and the neighbouring villages (the "Project").

The Project's transition impact is expected to derive from the Green and Inclusive qualities, as the Project will help Shaki to address its priority needs by improving water supply service, ensuring adequate wastewater treatment, mitigating flood risks and supporting access to market-relevant technical skills and training programmes in the water sector. The Project will also contribute towards achieving the policy reform objectives [REDACTED] for the water sector in Azerbaijan. The Project is Gender Additional through ASWRA's commitment to attract more women to the sector. The Project is 100 per cent GET.

Technical Cooperation ("TC") support for the preparation of the Project was financed by the EU Economic and Investment Plan ("EIP") Facility for Azerbaijan, while TC support for digital transformation for ASWRA was financed by the TaiwanBusiness-EBRD TC Fund. Post-signing TC support for the skills development programme and cybersecurity capacity building is expected to be funded by international donors and/or the EBRD Shareholder Special Fund ("SSF").

I am satisfied that the operation is consistent with the Bank's Strategy for Azerbaijan, the Bank's Infrastructure Sector Strategy, Green Economy Transition 2030 Strategy, the Equality of Opportunity Strategy 2021-2025, the Strategy for the Promotion of Gender Equality, EBRD Digital Approach 2026-2030, and with the Agreement Establishing the Bank.

I recommend that the Board approve the proposed loan substantially on the terms of the attached Report.

Odile Renaud-Basso

BOARD DECISION SHEET

Azerbaijan – Shaki Water and Wastewater - DTM 56006	
Transaction / Board Decision	<p>Board approval² is sought for a sovereign loan of up to EUR 91 million, structured in two tranches, in favour of the Republic of Azerbaijan to finance the construction and rehabilitation of water, wastewater and stormwater management infrastructure in the city of Shaki and its nearby villages.</p> <p>Tranche 1 of EUR 57 million, which will be committed at signing, will be co-financed by a EUR 4 million investment grant from the Eastern Europe Energy Efficiency and Environment Partnership. Tranche 2 of EUR 34 million will be uncommitted. The approval of commitment of Tranche 2 shall be delegated to Management.</p>
Client	<p>Borrower: Republic of Azerbaijan, represented by the Ministry of Finance. Beneficiary and the Implementing Agency: Azerbaijan State Water Resources Agency.</p>
Main Elements of the Proposal	<p><u>Transition impact</u></p> <p><i>Green</i> – The Project will improve the reliability and efficiency of water and sewerage services, lower methane emissions through improved sludge management, optimize energy consumption with the integration of solar panels, and prevent the discharge of untreated wastewater into the local environment. The Project will also enhance Shaki’s resilience to frequent flood events.</p> <p><i>Inclusive</i> – The Project will foster human capital development within Azerbaijan’s water sector by supporting ASWRA to develop and deliver currently absent short-term programmes for water and sewerage network operations and smart water management systems.</p> <p><u>Additionality</u></p> <p><i>Financing structure:</i> The long-term financing necessary to structure the Project is not available in the country under commercial terms.</p> <p><i>Risk mitigation:</i> The Project will address major environmental risks by building resilience in water, wastewater and stormwater management infrastructure.</p> <p><i>Standard-setting:</i> The Bank’s experience, innovation, knowledge and capabilities are material to the timely realisation of the Project’s objectives.</p> <p><i>Gender SMART:</i> ASWRA will introduce new mechanisms for promoting women’s entry to the sector, as currently technical positions are held mainly by males.</p> <p><i>Digital Transformation:</i> The Project enhances the Client’s operational efficiency in defining technical requirements for implementation of digital technologies.</p> <p><i>Cybersecurity Capacity Building:</i> The Project will support the training for client’s IT team to enhance good governance and resilience of cybersecurity functions.</p> <p><u>Sound banking</u></p> <p>Sovereign loan. [REDACTED]</p>
Key Risks	<p><i>Borrower’s creditworthiness:</i> moderate. The country’s sovereign credit rating stands at BBB- with Stable outlook from Fitch, BB+ with Positive outlook from S&P, and Baa3 with Positive outlook from Moody’s.</p> <p><i>Implementation risk:</i> The Bank’s assessment of the implementation risk is medium; the Project includes comprehensive Project Implementation Support (“PIS”) consultancy to support the Project’s implementation. The Bank’s Procurement Policies & Rules (“PPR”) will apply to the procurement of goods, works and services for the Project.</p>
Strategic Fit Summary	<p>The Project is aligned with the Bank’s Strategy for Azerbaijan, the Bank’s Infrastructure Sector Strategy, Green Economy Transition 2030 Strategy, Equality of Opportunity Strategy 2021-2025, EBRD Digital Approach 2026-2030, and the Strategy for the Promotion of Gender Equality.</p>

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

ADDITIONAL SUMMARY TERMS FACTSHEET

EBRD Transaction	<p>A sovereign loan in the amount of up to EUR 91 million to the Borrower for the benefit of ASWRA, a government entity in charge of management and protection of water resources in Azerbaijan. The loan will be divided into two tranches:</p> <ul style="list-style-type: none"> • Tranche 1 of up to EUR 57 million for the construction of water supply and wastewater networks, stormwater management system, water reservoirs, as well as upgrades to the Wastewater Treatment Plant (“WWTP”) in Shaki city (to be committed at signing); and • Tranche 2 of up to EUR 34 million for the construction of water supply and wastewater networks in Kish, Okhud and Gokhmud villages (the “Villages”), neighbouring Shaki city (uncommitted). <p>[REDACTED] Tranche 1 will be co-financed by an investment grant of up to EUR 4 million from the E5P.</p>
Mutual Reliance	No
Existing Exposure	<p>Sovereign exposure: The total amount of sovereign portfolio stands at EUR 520 million [REDACTED](OpID: 43094, 52399, 52419, 55197 and 48376).</p> <p>Azerbaijan State Water Resources Agency: ASWRA is an implementation agency under the sovereign loan for the Ganja Water and Wastewater project, the “Ganja Water”).</p>
Maturity / Exit / Repayment	Eighteen-year maturity [REDACTED]
Potential AMI eligible financing	None
Use of Proceeds - Description	<p>The proposed EBRD loan (provided in two tranches) and the E5P grant (for Tranche 1) will finance construction of up to 245 km of drinking water supply and up to 300 km of wastewater collection network, construction of up to 9 drinking water storage reservoirs, construction of biological wastewater treatment, sludge drying and storage facility, installation of solar panels for the WWTP, construction of up to 48 km stormwater management system, procurement of operational and maintenance (“O&M”) equipment, installation of the SCADA system for the water supply. The EBRD loan will also finance the PIS consultancy services, including design preparation, technical and Environmental and Social (“E&S”) supervision.</p>
Investment Plan	[REDACTED]
Financing Plan	[REDACTED]
Key Parties Involved	<p>Borrower: Republic of Azerbaijan, represented by the Ministry of Finance.</p> <p>Project Entity: Azerbaijan State Water Resources Agency.</p>
Conditions to subscription / disbursement	[REDACTED]

Key Covenants	[REDACTED]
Security / Guarantees	Sovereign loan
Other material agreements	<ul style="list-style-type: none"> • Loan Agreement between the Bank and the Borrower. • Project Agreement between the Bank and ASWRA. • Grant Agreement between the Bank and ASWRA.
Associated Donor Funded TC and Blended Concessional Finance	<p>A. Technical Cooperation (TC) <i>Pre-signing:</i></p> <ul style="list-style-type: none"> • TC 1: Feasibility Study. The cost of the assignment is EUR 337,650 financed by the EU Economic and Investment Plan (EIP) Facility. • TC 2: Digital Transformation Support Programme (DTSP). The assignment supports the development of digital transition plan for ASWRA to identify priority investments and build capacity for smart and efficient water infrastructure management. The cost of the assignment is EUR 75,000 financed by the TaiwanBusiness-EBRD TC Fund. • TC 3: Advance Procurement Support to assist ASWRA with the procurement of PIS consultants. The estimated cost of the assignment is up to EUR 60,000, proposed to be financed by an international donor and/or the EBRD Shareholder Special Fund (the “SSF”). • TC 4: Cultural Heritage Impact Assessment. This TC supports the preparation of the CHMP to avoid or mitigate adverse impact on cultural heritage sites and take a precautionary approach in construction works, in line with local and international guidelines, including the EBRD Performance Requirement 8 (Cultural Heritage). The cost of the assignment is up to EUR 120,000, to be financed by the EBRD SSF and/or an international donor. <p><i>Post-signing:</i></p> <ul style="list-style-type: none"> • TC 5: Skills Development Programme. This TC will support broadening access to market-relevant technical skills and employment opportunities in the water sector. The estimated cost of the assignment [REDACTED], proposed to be financed by an international donor and/or the SSF. • TC 6: Cybersecurity Resilience Programme: This TC will support a Cybersecurity Capacity Building training for the client’s IT team to enhance resilience and good governance of cybersecurity procedures. The assignment value [REDACTED], proposed to be financed by an international donor and/or the SSF. <p><i>Client contributions:</i> ASWRA plans to provide financial contribution to the Project [REDACTED].</p> <p>B. Blended Concessional Finance The Project will be co-financed by a EUR 4 million investment grant from the E5P. The grant was approved by the E5P Assembly of Contributors in November 2025 through written procedure.</p>
[REDACTED]	[REDACTED]

INVESTMENT PROPOSAL SUMMARY

1. STRATEGIC FIT AND KEY ISSUES

1.1 STRATEGIC CONTEXT

Water stress is a significant concern in Azerbaijan. Approximately 70 per cent of its surface water resources are connected to transboundary waters, which face increasing pressures in upstream regions. In addition, Azerbaijan experiences significant interannual and seasonal water variability due to its climate and hydrological characteristics. The problems are further exacerbated by the impact of climate change, which intensifies the strain on vital water resources.

To address the escalating water challenges, the Government of Azerbaijan has advanced a series of reforms since the early 2020s. As a first step, in March 2023, ASWRA was established to replace the fragmented incumbents. Subsequently, in February 2024, the Government strengthened the institutional structure, clearly separating policy-setting, technical supervision, and operating functions. Operating functions were further streamlined among five subordinate entities.

In October 2024, the Government adopted the National Strategy on the Efficient Use of Water Resources (the “National Strategy”), which outlined a comprehensive set of measures to improve infrastructure and protect water resources over the next two decades. The reforms are ongoing, as the Government seeks to finalise institutional transformation and operationalise the implementation of the National Strategy.

To support the reforms, following the signing of the Ganja Water project, the Bank and ASWRA have jointly advanced a structured institutional transition agenda. This agenda is designed to improve governance, financial and operational management policies through the Governance Action Plan (GAP) and Financial and Operational Performance Improvement Programme (FOPIP). [REDACTED] The implementation of these programmes is further reinforced by a Reform Support Team embedded within the Agency, enabling hands-on delivery, close coordination and continuous monitoring of the reforms.

Since the launch of these initiatives, the Bank and ASWRA have made tangible progress. Detailed assessments have been completed and key diagnostic outputs have been developed and endorsed by ASWRA management. Furthermore, in line with agreed work plans, core compliance, anti-corruption and anti-bribery (ABC) policies have been prepared and are now progressing through ASWRA’s internal review and approval process. Institutional restructuring is also advancing in line with reform objectives. In February 2026, the Government of Azerbaijan transformed two key operating entities into CJSCs and introduced supervisory boards to strengthen governance, alongside other structural improvements.

Furthermore, as part of this Project [REDACTED], the Bank and ASWRA have agreed clear conditions for effectiveness [REDACTED]. These concrete, timebound milestones anchor delivery and create strong platform for advancing reforms under upcoming investment projects.

[REDACTED] This approach enables the Bank to support critical infrastructure delivery, while maintaining strong reform leverage towards a more modern and well-governed water sector in Azerbaijan.

This approach is particularly urgent in the context of proposed investments in Shaki and Ganja cities. Shaki, a city with a population of 68 thousand situated in north-western Azerbaijan, is facing acute challenges in the provision of modern municipal water and wastewater services. Despite earlier modernisation efforts, only around 75-80 per cent of the initially planned investments were completed, leaving some parts of the city and neighbouring villages (which were not part of the initial plan) underserved and exposed to environmental and public health risks.

Currently, approximately 20 per cent of Shaki's population is not connected to the piped water supply network, while around 70 per cent lack access to the sewerage system and rely on septic tanks and open drains. Populations in nearby villages (approximately 18 thousand) are connected to neither the water supply nor the sewerage systems.

The existing WWTP remains incomplete: its physical treatment units have been constructed but are not operational, and there is no biological treatment process or associated sludge management facility. As a result, the discharge of untreated wastewater into local rivers has led to substantial environmental degradation, threatening the quality of downstream water resources and posing significant health risks to local communities. In addition, the stormwater infrastructure remains inadequate, resulting in frequent localised flood events.

The Project represents a strategic, integrated intervention to address these challenges. It will improve public health, hygiene, and living conditions for more than 65 thousand people. Upon completion of the upgrade, the WWTP will have the capacity to treat 5.84 million m³/year, safeguarding the water quality for the downstream catchment and enabling re-use for agricultural purpose. On-site solar photovoltaic ("PV") panels will offset the plant's energy demand. Together with the greenhouse gas ("GHG") emission savings associated with the introduction of wastewater treatment, the Project will yield overall emission savings [REDACTED].

Furthermore, the introduction of up to 48 km of stormwater infrastructure will reduce flood-related economic damages and enhance resilience against flood events. All of this will be further complemented by the deployment of modern SCADA and advanced monitoring systems to track flows, detect leakages, and optimize pumping schedules, thereby improving efficiency and climate resilience of water infrastructure services.

In addition to the GAP and FOPIP, the Bank and ASWRA are cooperating across further on priority areas under the National Strategy. The feasibility study identified a shortage of professionals in specialised areas of water management, such as water quality analysis and the management of WWTPs. This challenge is further exacerbated by the lack of vocational education and training (VET) programmes that adequately contribute to skills development in the water sector. To address the above-mentioned skills gaps, the Project will support ASWRA in promoting upskilling and reskilling solutions for the water sector by developing short-term programmes to be delivered by the training centre under the Agency.

Furthermore, the Bank's Digital Hub is supporting ASWRA in undertaking digital maturity assessments and identifying priority investment needs for digitally enhanced and secure water infrastructure management services. The Project also supports ASWRA through a capacity building programme aimed at training key personnel in cybersecurity principles. In doing so, the Project will contribute to the operational resilience and long-term good governance of the client and the water sector.

The Project aligns with the Bank’s Infrastructure Sector Strategy and the Country Strategy for Azerbaijan by investing in sustainable and inclusive municipal and environmental infrastructure. Furthermore, the Project is aligned with the Equality of Opportunity Strategy 2021-2025, EBRD Digital Approach 2026-2030, and the Strategy for the Promotion of Gender Equality by considering gender and inclusion aspects in the tailored training programmes.

The Project is assessed as aligned with the Paris Agreement (“PA”) mitigation goals according to the joint Multilateral Development Banks (“MDB”) aligned list and the water sectoral guidance in the EBRD alignment methodology. This makes the Project consistent with the Bank’s Green Economy Transition 2030 Strategy. It also contributes to several UN Sustainable Development Goals (“SDGs”), including SDG 5: Gender Equality, SDG 6: Clean Water and Sanitation, SDG 11: Sustainable Cities and Communities, and SDG 13: Climate Action.

1.2 TRANSITION IMPACT

Primary Quality: Green

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>	100 per cent of the EBRD’s use of proceeds under the Project qualifies as GET finance, reflecting strong alignment with the Bank’s GET objectives. The Project integrates significant climate mitigation and adaptation measures, including the installation of up to 0.8 MWp PV systems at the WWTP to offset part of its energy demand and reduce GHG emissions[REDACTED]. It also introduces a 48 km stormwater network for Shaki city and improves water and energy efficiency through the SCADA system and network rehabilitation. The Project will prevent pollution of freshwater resources by treating an estimated 5.84 million m ³ of wastewater annually, helping to preserve water resources for users in the downstream catchment. These components collectively contribute to reduced emissions, improved resource efficiency, and enhanced climate resilience.
1.2	<i>The project results in water savings equivalent to at least 0.05% of annual national freshwater withdrawal, so significantly contributes to reducing the national water footprint.</i>	By commissioning the WWTP, the Project will prevent the discharge of approximately 5.84 million m ³ of untreated wastewater annually into the receiving river, thereby protecting the river ecosystem and safeguarding significant volumes of freshwater resources downstream from pollution. A dilution calculation shows that the protected freshwater resources are greater (0.051 percent) than 0.05 per cent of annual national freshwater withdrawal. In addition, network rehabilitation and SCADA activation will help minimise non-revenue water.
1.3	<i>The project has a good climate resilience benefit-to-cost ratio which exceeds one.</i>	The Project demonstrates strong climate resilience, with an indicative resilience benefit-to-cost ratio of about 1.3, based on conservative assumptions that

		consider avoided flood damage and the introduction of wastewater treatment in a wider context of water stress.
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Secondary Quality: Inclusive

Obj. No.	Objective	Details
2.1	<i>EMPLOYABILITY: The Project broadens access to market-relevant skills and training opportunities, boosting the supply of human capital with demonstrably high need and robust effectiveness.</i>	<p>The Project feasibility study highlighted a significant skills mismatch in Azerbaijan, particularly in regions such as Shaki. Over 60 per cent of general education graduates enter the labour market without specialization, and 66.8 per cent of the economically active population lacks formal qualifications. Low participation in VET programme, especially among women (only 25 per cent of VET students are female) exacerbates structural unemployment. This gap is present in the water sector, where outdated infrastructure and specialised needs require skilled professionals. Existing VET programmes do not fully address these sector-specific skills, thereby limiting workforce competence and operational efficiency.</p> <p>To address critical skills shortages, the Project will introduce a tailored training programmes developed in partnership with Training and Innovations Centre under ASWRA. These programmes will train at least 60 students per year across three areas: water and sewerage network operations, smart water management systems, and wastewater management and treatment. This initiative will help build a skilled local workforce capable of supporting the long-term operation and maintenance of Shaki's water infrastructure, while also contributing to broader economic inclusion and resilience in the water sector.</p>
2.2	<i>EMPLOYABILITY: The Project delivers inclusive business policies, practices or standards at the client level with verifiable commitment within 1-2 distinct behavioural change area</i>	<p>The Project delivers inclusive business practices at the client level through a verifiable commitment to one behavioural change area:</p> <p><i>Formal Partnership between private sector and Local Education/Training providers.</i></p> <p>The Training and Innovations Centre plans to carry out above mentioned short-term programmes in collaboration with sector associations and institutes, ensuring that the perspectives of major players in the water sectors (i.e. contractors, consultants) are reflected in the curriculum and content of the programmes. These programmes will be available to all prospective workers in the sector. Through career guidance and support, the Training and Innovation Centre will ensure that its graduates are better positioned to find adequate employment or improve their career options.</p>

Delivery risks: The primary risks associated with the delivery of the TI objectives are linked to ASWRA's capacity to effectively deliver the planned infrastructure works and training

programme. Outcomes may also be delayed by regulatory approval processes beyond ASWRA’s control. To mitigate these risks, the Bank has collaborated with ASWRA to align proposed measures with regulatory requirements and comparable successful benchmarks. Furthermore, the PIS consultant, composed of the team of experienced and appropriately trained experts, will be mobilised to support ASWRA from the initial planning until the final delivery of the Project. The loan documentation will incorporate appropriate covenants on implementation of the Project, including cooperation with the PIS consultant.

Digital Approach: The Project is aligned with the Adaptation area of intervention outlined in the EBRD Digital Approach 2026-2030, as it will strengthen the client’s digital maturity and cybersecurity governance through a Digital Action Plan and cybersecurity trainings relevant to water management. The digital and cybersecurity components of the Project are aligned with the Bank’s Non-Financial Additionality under “Knowledge and Capacity Building” and in section 1.4 – Sound Banking – Key Risks, respectively.

1.3 ADDITIONALITY

	Description
No triggers identified.	n/a

Additionality sources	Description of additionality sources
Financial additionality:	
Financing Structure EBRD offers financing that is not available in the market from commercial sources on reasonable terms and conditions , e.g. a longer grace period. Such financing is necessary to structure the project.	There is a limited market for long-term borrowing in Azerbaijan under commercial terms. Due to existing market inefficiencies, local banks cannot offer loans matching the requirements of such infrastructure projects.
Non-financial additionality:	
Risk mitigation EBRD helps the client to mitigate environmental, social and governance (ESG) risks through identification of risks related to the depletion of natural capital assets, raw materials and water availability, etc., and to manage these risks.	The feasibility study has helped ASWRA to assess local needs and prepare the investment plan in line with the EBRD and EU standards. The proposed measures will help to address major environmental, health, and climate-related risks and contribute to ESG objectives.
Standard-setting: helping projects and clients achieve higher standards <i>Gender SMART: Client seeks/makes use of EBRD expertise on higher Equality of Opportunity /inclusive standards</i> Client seeks/makes use of EBRD expertise on best international procurement standards.	The Shaki Water Reclamation Systems Operation Department currently employs 364 persons and only 8 per cent are women, which is in line with other regional offices, with only 1.5 per cent of all technical specialists being women. ASWRA will establish key recruitment tools and career fairs to attract women to the Training and Innovation Centre. The Project will support a community outreach and engagement programme, supported by a comprehensive communication strategy to attract women, particularly recent graduates, to the newly developed training programmes, which target at least 30 per cent of female participation. EBRD’s impact, environmental and social related conditionalities go far beyond what commercial

	<p>funding sources would require, including on procurement procedures, E&S standards and transition to the green economy. Application of the EBRD PPR will ensure application of good international practices and facilitate efficient implementation of the Project.</p>
<p>Knowledge, innovation, and capacity building EBRD provides expertise, innovation, knowledge and/or capabilities that are material to the timely realisation of the project's objectives, including support to strengthen the capacity of the client.</p>	<p>The Project will strengthen the client's operational efficiency by providing TC support for the digital transformation programme, including a digital maturity analysis and the development of a strategic digital roadmap. This assignment will result in a Digital Action Plan with phased investment priorities and contribute to strengthening of the client's institutional capacity and ensuring that future digital investments are effectively designed and implemented with EBRD financing.</p> <p>The Project will also provide TC support for Cybersecurity Resilience Programme, which will enhance the client's operational resilience and cyber preparedness.</p>

1.4 SOUND BANKING - KEY RISKS

Risks	Probability / Effect	Comments
Borrower's creditworthiness	Low/ Medium	Heavy reliance on volatile hydrocarbon markets and exposure to global oil price fluctuations might negatively impact Azerbaijan's debt service capacity. However, the country benefits from solid FX reserves (17.7 per cent above GDP) and low external indebtedness (6.3 per cent of GDP). Recent rating notices have reflected improved fundamentals: Moody's affirmed Azerbaijan to Baa3 with a positive outlook in January 2026, Fitch affirmed BBB- with a stable outlook in June 2025, and S&P reaffirmed BB+ with a positive outlook in December 2025.
Cost over-run risk	High/ Medium	The feasibility study consultant and ASWRA worked together to define the project scope and validate unit costs through a detailed engineering design review and benchmarking against recent water sector investments in Azerbaijan, as well as comparable international projects. To mitigate further price escalation risk, the investment plan includes appropriate physical work and price contingencies as well as inflationary expectations. In addition, the Government will commit to cover any cost overruns, ensuring that the Project's implementation remains funded at all times.
Implementation risk	High/ Medium	ASWRA will be supported by experienced PIS consultants with experience in carrying out procurement and contract administration in line with IFI requirements. The internationally recognised forms of contract for construction works (FIDIC) will be used, and the works will be supervised by an experienced international supervision consultant. Please refer to Annex 3 for further details on the Project implementation and procurement arrangements.
Exchange rate risk	Low/ High	Although currency risk remains inherent for a hydrocarbon-reliant economy, several factors mitigate currency-volatility risk. The local currency operates in a managed-float regime supported by sizeable foreign-exchange reserves. [REDACTED] Additionally, the authorities

		maintain conservative fiscal and external policies, which helps limit exchange-rate pressures.
Cybersecurity risk	Medium/Medium	[REDACTED] a cybersecurity due diligence was carried out, which identified a number of gaps that EBRD will help to address by deploying a post-signing TC for training key personnel in cybersecurity principles. [REDACTED]
Geopolitical risk	Low/High	[REDACTED] No disruption on implementation is expected, as the Project does not rely on critical materials or suppliers from Iran or other Middle East countries.

2. MEASURING / MONITORING SUCCESS

Transition Impact Monitoring Indicators

Primary Quality: Green

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date	[REDACTED]
1.1	New or updated GET technology or product leading to energy efficiency introduced	The deployment of modern SCADA and an efficient hydrophore pump station is expected to reduce energy use by optimising pressure and operations, contributing to lower pumping costs and supporting energy savings of up to 15-20 per cent.	No	Yes	[REDACTED]	
1.2	CO2e emissions reduced (tonnes/year)	The Project is expected to reduce emissions [REDACTED] through introduction of improved wastewater management, renewable energy generation at the WWTP and additional savings from optimized pumping and SCADA-driven operations.	0	[REDACTED]	[REDACTED]	
1.3	New or updated GET technology or product leading to pollution prevention control introduced	The Project will commission a biological wastewater treatment plant with a design capacity of 16,000 m3/day and add sludge drying facilities, preventing untreated discharge and ensuring compliance with EU standards.	No	Yes	[REDACTED]	
1.4	New or updated GET technology or product leading to water savings introduced	The Project will implement leak detection and pressure control to minimise water losses.	No	Yes	[REDACTED]	
1.5	New or updated technology introduced	The Project will implement a stormwater management system to improve resilience and reduce flooding.	No	Yes	[REDACTED]	
1.6	Wastewater treated (m3/year)	The Project is expected to treat 5,840,000 m3/year of wastewater, improving sanitation.	0	5,840,000	[REDACTED]	
1.7	Renewable energy - electricity produced (MWh/year)	The Project is expected to produce approximately 575 MWh/year of clean energy from a 0.8 MWp solar PV system installed at the WWTP.	0	575	[REDACTED]	
1.8	Number of individuals (local population) with improved access to wastewater services	The Project is expected to improve wastewater collection and treatment services for over 70,000 people, in line with international best practice.	0	70,000	[REDACTED]	
1.9	Drinking Water - no of people connected	The Project is expected to connect over 31,000 additional people to the water supply network.	58,912	90,379	[REDACTED]	

Secondary Quality: Inclusive

Obj. No.	Monitoring indicator	Details	Baseline	Target	Due date	
2.1	Training programme developed and implemented	The Client will develop and implement three internally certified training programmes on water and sewerage network operations, smart water management systems and wastewater management and treatment.	No	Yes	[REDACTED]	
2.2	Partnership with education providers established or strengthened	ASWRA will partner with the sector association and other stakeholders to create and carry out above-mentioned programmes. At least one MoU will be signed.	No	Yes	[REDACTED]	
2.3	Number of individuals enhancing their skills as a result of training	At least 60 individuals annually will enhance their skills through the newly developed training programmes, with a target of 200 participants over the course of the Project.	0	200	[REDACTED]	

Additional Indicators

Indicator type	Monitoring indicator	Details	Baseline	Target	Due date	
Advisory & Policy Indicators	Practices of the relevant stakeholder improved (equal opportunity policies and practices)	A comprehensive communication strategy to attract women, particularly recent graduates, to the newly developed training programme that will be developed.	No	Yes	[REDACTED]	
Advisory & Policy Indicators	Number of women enhancing their skills as a result of training	The training programme will target at least 30 per cent female participation, translating into at least 60 women being trained over the first three years.	0	60	[REDACTED]	

3. KEY PARTIES

3.1 BORROWER

The Borrower is the Republic of Azerbaijan, represented by the Ministry of Finance. [REDACTED]

3.2 AZERBAIJAN STATE WATER RESOURCES AGENCY

ASWRA is the national water and wastewater services provider of Azerbaijan. It was established in March 2023, on the basis of three public institutions that operated countrywide and independently covered different functions in the water sector. Under the new structure, ASWRA acts as a single authority with broader policy and governance responsibilities, which now also include the development of stormwater management infrastructure and the protection of water resources.

Following a presidential decree of February 2026, two public legal entities - Large Cities Water Supply PLE and Regional Water Melioration PLE - operating under ASWRA, were transformed into closed joint-stock companies (“CJSCs”).

ASWRA oversees the following companies operating under its authority:

- Large Cities Water Supply CJSC – responsible for water supply, wastewater and stormwater management infrastructure in selected large cities.
- Regional Water Melioration CJSC – provides irrigation and melioration services across the country, as well as water supply, wastewater and stormwater management infrastructure services in areas outside the mandate of the United Water Service for Large Cities PLE.
- Directorate for the Facilities under Construction PLE – manages the development and delivery of large infrastructure projects funded by the national budget and IFIs.
- Institute for Design and Scientific Research in Water and Melioration PLE – conducts scientific and experimental research in the water sector and is responsible for the design of water supply and wastewater infrastructure assets.

The State Control Service for Water Use and Protection is a functionally remote entity under ASWRA, responsible for technical control, assurance, monitoring, and protection of water resources, as well as ensuring compliance with national standards.

ASWRA is managed by the Chairman and four Deputies appointed by the President of Azerbaijan. Other senior officials of ASWRA and the underlying entities are appointed by the Chairman. The CJSCs under ASWRA are operated by the Supervisory Board consisting of five members with executive management responsible for the day-to-day management.

[REDACTED]

Under the new structure, the implementation of all infrastructure investments, including the Project, is undertaken by the Directorate for the Facilities under Construction PLE. Upon completion of the works, the Large Cities Water Supply CJSC or the Regional Water Melioration CJSC take over and operate assets, depending on the location of the infrastructure assets.

4. MARKET CONTEXT

The water sector in Azerbaijan faces challenges that impact the efficiency and quality of services provided to the population. Largely outdated and inefficient infrastructure leads to infrastructure failures, loss of valuable water resources, and damage to the local environment.

Until 2023, the sector operated under a fragmented institutional setup, with multiple ministries and agencies exercising overlapping mandates. The establishment of ASWRA in 2023 and subsequent reforms aim at building an institutional framework and integrated approach for achieving long-term water security. [REDACTED] Combined with a structural dependency on transboundary water resources, these institutional gaps hamper the country's water security in the face of climate-driven changes.

In Shaki the current water supply network serves approximately 16 thousand households, 750 commercial entities and 31 public organisations, which account for 80 per cent of total subscriber base. More than 90 per cent of connected households and commercial entities have meters installed, facilitating the invoicing and collection process. In the unconnected parts of the city, the population relies on private wells or purchases water delivered by trucks.

For the wastewater network, the connection rate is approximately 30 per cent, due to the lack of a comprehensive wastewater collection network. The population relies on septic tanks and open channels for wastewater discharge. In densely urbanised sections of the city, where wastewater network has already been constructed, intense rainfall events frequently result in local drainage problems due to the absence of functioning stormwater management infrastructure.

The tariffs for water services are set by the Tariff Council, an inter-ministerial institution chaired by the Minister of Economy. [REDACTED] The most recent tariff change took place in 2021, resulting in a doubling of water supply and sanitation tariffs. According to the National Strategy, the Government is expected to gradually move towards a differentiated and cost-based tariff structure by the end of 2027. [REDACTED]

5. ECONOMIC ANALYSIS

5.1 SOVEREIGN ASSESSMENT

As of the end December 2025, Azerbaijan's total foreign debt stood at around 6.3 per cent of its GDP. The total external public debt has decreased from EUR 5.0 billion in December 2024 to EUR 4.1 billion in December 2025 due to ongoing repayments and limited new borrowings. In July 2025, Moody's upgraded Azerbaijan's long-term foreign currency rating by one notch to Baa3, thereby upgrading Azerbaijan to an investment-grade rating. Standard & Poor's affirmed Azerbaijan's BB+/B rating in December 2025 while revising its outlook from stable to positive, and Fitch maintained its BBB- rating with a stable outlook.

Azerbaijan's strong fiscal and external assets position acts as a buffer against economic and financial shocks. The country's large foreign assets, generally prudent fiscal policies, and domestic political stability are considered credit strengths by the rating agencies. On the other hand, weak institutional effectiveness and governance indicators, narrow and concentrated economic base with a moderate growth trend, weak domestic banking system and exposure to developments in hydrocarbon markets are considered as rating weaknesses.

[REDACTED]

5.2 ECONOMIC ANALYSIS

[REDACTED]

5.3 PROJECTED PROFITABILITY FOR THE BANK

[REDACTED]

6. OTHER KEY CONSIDERATIONS

6.1 ENVIRONMENT

Categorised B under the Environmental and Social Policy (2019). The Project will improve water and wastewater services in Shaki city and the neighbouring villages, reduce pollution of the local environment from untreated discharges, improve sludge management and resilience to climate risks. The Project includes construction of water and wastewater networks, reservoirs, pumping stations, a WWTP with the estimated capacity of 75,000 P.E. including biological treatment, a sludge drying facility and a small 0.8 MW distributed solar PV. Environmental and social due diligence ("ESDD") has been carried out by independent consultants as part of the Feasibility Study and included a review of the earlier studies prepared by KfW such as Environmental Impact Assessments ("EIAs") from 2013 and 2017, an independent E&S audit/review and an analysis of potential E&S impacts associated with the PIP.

The ESDD has identified that the Client's organisational capacity to manage E&S risks in line with EBRD Performance Requirements ("PRs") appears limited and will require further improvement, and that the PIU will be established with the responsibility to manage the Project. There is currently no established Environmental and Social Management System ("ESMS") in place, but there are various elements, including an environmental policy statement and an Environmental Management Plan generally aligned with good international practice, covering how ASWRA deals with the environmental matters. ASWRA and its PIU will need to dedicate environmental and social management staff for Shaki and further develop its ESMS in line with ISO 14001 and ISO 45001 for environmental management and occupational health and safety, respectively. Environmental permits for the respective Project components will need to be obtained in line with the national legislation prior to the start of any construction. It is understood that a local EIA will be required for all Project components to undergo the state ecological expertise and obtain the necessary permitting.

ASWRA will also need to further develop a Human Resources ("HR") policy and procedures in line with PR2. A collective bargaining agreement is in place, and no collective retrenchment is expected due to the Project. An internal grievance procedure will need to be developed, adopted, and communicated to all employees. ASWRA will also be required to prepare and implement a policy on gender-based violence and harassment ("GBVH") and communicate it to staff and other stakeholders such as contractors. The above requirements are included in the Environmental and Social Action Plan ("ESAP").

The ESDD confirmed that, as a result of the Project, the drinking water supply and WWTP in Shaki will be in compliance with national and broadly with EU requirements with some improvements under ESAP structuring the Project to bring it into compliance with EU requirements for sewage sludge. Any potential adverse impacts from replacement of the existing water networks will be associated with the construction works and will be limited, localised, and short-term, and will be mitigated or prevented by adhering to good construction practices. ASWRA will also need to improve local laboratory services to ensure timely and efficient water quality monitoring. ASWRA will need to develop a long-term sludge management strategy and a final long-term solution for the sludge after temporary storage of the stabilised sludge on-site. Options considered include potential agricultural re-use, subject to testing, AD/biogas for energy recovery, or sending to the landfill. ASWRA will also take steps to manage odour issues effectively. All these requirements are included in the ESAP.

The reservoirs, networks and facilities are all located in a highly urbanised area of Shaki. Precautions will need to be taken during the construction works including a chance finds procedure. Some limited private land acquisition may be required for the location of the water reservoirs, and a Resettlement Framework has been developed to manage these potential impacts in line with PR5. The Project does not require any physical resettlement of households or businesses, and any economic displacement will be limited mainly to the construction stage and managing temporary access restrictions. The households nearest to the WWTP are 850 m away to the west and will not be heavily impacted by noise and dust arising from the construction works. This distance is also larger than 400 m and satisfies the Sanitary Protection Zone requirements for this plant. A Resettlement Plan may need to be developed depending on detailed design review, and if required, it would be disclosed, approved and implemented by ASWRA to manage all related impacts in line with EBRD PR5.

The Project's footprint is urban, and ESDD confirmed that no critical habitat or priority biodiversity features are expected to be impacted by the Project. Nature protected areas adjacent to the Project footprint include Shaki Important Bird Area and Shahdagh National Park, and the ESAP includes precautionary and mitigation measures before and during construction to minimise disturbance, including pre-construction biodiversity surveys, implementation of adaptive biodiversity management approach and biodiversity monitoring to meet EBRD PR6.

Sheki Town, the historical part of Shaki city, is designated in its entirety as UNESCO Site and World Heritage Site, which means all buildings, monuments, and their surrounding ensemble of cultural/historic settings are protected as the cultural heritage of international significance. Since some of the Project components are going to be implemented within the buffer zone or inside of UNESCO Site and World Heritage Site, in line with PR8 requirement ASWRA will commission the CHIA and prepare a CHMP, which will be discussed and agreed, prior to the start of the works, with the Bank, the regulator and UNESCO Secretariat. CHMP requirements will be incorporated into procurement documentation for the construction works that will affect the Cultural Heritage Sites and their buffer areas. A Cultural Heritage Monitor will also be assigned by ASWRA to carry out an external supervision over the CHMP implementation, submit quarterly monitoring reports to the Bank during construction and prepare a CHMP completion report at the end of the works. The Project is structured to meet PR8 through ESAP and future implementation of the CHMP.

Given the scale of the construction works, specific precautions will need to be taken by the contractors, including development of the Construction E&S Management Plan. Relevant E&S requirements will need to be included in the tenders and contracts for the contractors. ASWRA will need to develop and implement E&S management plans, including an emergency response plan, a traffic management plan, pollution prevention and control plan, construction waste management and hazardous waste management plans; occupational and community health & safety management plans including provision of the necessary PPE, training and incident reporting to ensure everyone's safety during construction works. Risks of small distributed solar PV will be managed through procurement. ASWRA also needs to implement a Stakeholder Engagement Plan (SEP), including a grievance mechanism, to ensure adequate information disclosure prior to the commencement of works. ASWRA will assign a community liaison officer to manage implementation of the SEP and handle grievances.

An ESAP with the corrective E&S measures has been prepared for and agreed with ASWRA to address all identified gaps and structure the Project in line with EBRD's PRs. ESAP will be included as part of the legal documentation. SEP and a Non-Technical Summary (NTS) have also

been disclosed locally by ASWRA. The PIU to be established at ASWRA will be supported by the Project Implementation Support consultants to implement the respective elements of the ESAP. The Project will also promote higher gender equality and equal opportunities standards with the support of the GAP consultants. The Bank will monitor the Project through annual E&S reports. The Bank may also undertake monitoring site visits, if deemed necessary.

6.2 INTEGRITY

In conjunction with OCCO, internal and external integrity due diligence was carried out on ASWRA, its underlying entities, their senior management and other relevant stakeholders. [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 OTHER ISSUES

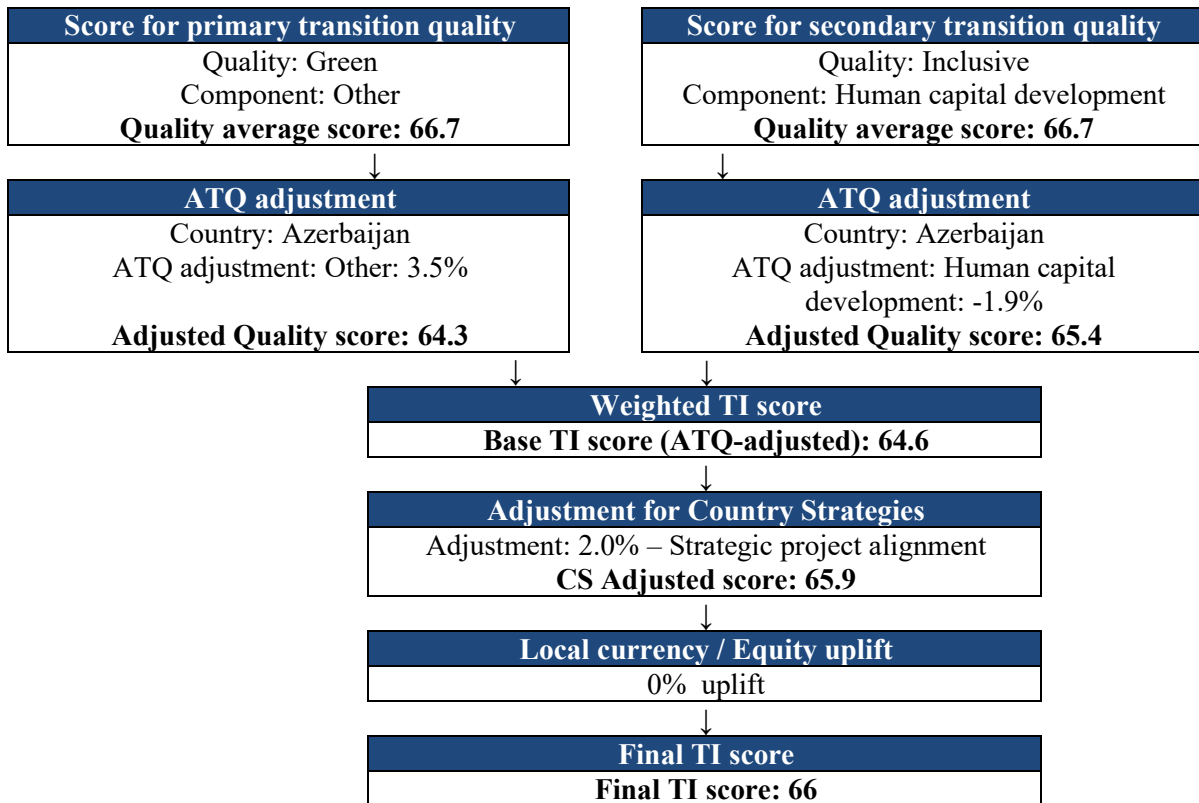
Concessional Finance

The Project will be co-financed by a EUR 4 million investment grant from the E5P. The Project will support sustainable development and improve the quality of life for the population by minimising inefficiencies and addressing environmental risks. The use of concessional finance will enable the implementation of higher standards, which, in turn, is expected to catalyse further investments in the water sector in Azerbaijan.

ANNEXES TO OPERATION REPORT

ANNEX 1	Transition Impact Scoring Chart
ANNEX 2	Ownership and Governance Structure
ANNEX 3	Green Assessments
ANNEX 4	Project Implementation
ANNEX 5	Project Economic Internal Rate of Return (EIRR)

Annex 1 - Transition Impact Scoring Chart



Annex 2 – Ownership and Governance Structure

[REDACTED]

Annex 3 – Green Assessments

SUMMARY

- The Project is a comprehensive water sector programme including water supply and sewerage network, WWTP and the introduction of stormwater systems for the city of Shaki and neighbouring villages, Azerbaijan. It is designed to meet both water supply and wastewater management standards according to EU regulations.
- The Project is determined **aligned with both mitigation and adaptation goals of the Paris Agreement**.
- The Project is attributed **100 per cent Green finance**.
- Climate-related financial risks have been assessed [REDACTED]

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 activity is included in the 'MDBs' aligned list' under the category “Water supply and wastewater”.
- There are no activities included in the 'non-aligned list'.

Alignment with the adaptation goals of Paris Agreement

The Project is determined as aligned with the adaptation goals of the Paris Agreement as it satisfies all three steps of the assessment. All material physical climate risks have been addressed.

GREEN FINANCE ATTRIBUTION

The Project is attributed 100 per cent green finance. This share has been calculated in line with the approach for directly financed investments.

Nature: The investment will ensure that the wastewater collection system is rehabilitated and extended, including the establishment of a separate stormwater system, and will ensure that the collected wastewater is treated to EU standards.

Other environmental activities: The Project will secure and extend the supply of safe drinking water and increase system efficiency (leak reduction).

Climate mitigation: The Project will achieve a net reduction of GHG emissions by introducing wastewater treatment. Currently, wastewater enters the environment untreated, leading to uncontrolled methane emissions. Further, the installation of a dedicated solar PV plant at the WWTP will further reduce carbon emissions.

Climate adaptation: The introduction of improved stormwater management will reduce the cost of flood-related damage. While Shaki itself is not at risk from water stress, communities in the downstream catchment are vulnerable to this risk due to reduced river baseflows and groundwater recharge. The Project will safeguard these resources for downstream communities through introduction of wastewater treatment.

The expected transition impacts of the Shaki Water and Wastewater Network Project will be monitored through key indicators, including [REDACTED] the treatment of up to 16,000 m³ of wastewater per day at the WWTP, and reliable drinking water supply to additional approximately

31,000 people across Shaki and surrounding villages. The Project also incorporates SCADA activation, network rehabilitation and a 0.8 MWp photovoltaic system at the WWTP, all of which promote sustainable water management and climate resilience in line with EBRD's Green Economy Transition objectives.

[REDACTED]

Annex 4 - Project Implementation

Procurement classification – *Public, sovereign*

[REDACTED]

ASWRA (the Client) will implement the Project via a dedicated Project Implementation Unit (PIU). The capacity of the Client to carry out procurement works and implement the Project in accordance with Bank's requirements was reassessed by the Project-dedicated Project Implementation Advisor (PIA), based on the findings of the original assessment for Ganja Water project (OPID 55197). The Client, building up on the experience of its predecessors, has adequate to strong institutional capacity for procurement under IFI financing (ADB, IsDB, World Bank, KfW and others).

ASWRA will be responsible for the Project implementation via a dedicated PIU. Taking into account that the Project will be implemented in parallel with the larger Ganja project, the Client will require additional capacity to manage an additional large-scale project. The structure of the PIU and relevant reporting and cooperation with other departments of ASWRA appear to be robust, building up from previous experience of implementing international projects, and the Bank has provided guidance on optimal composition of the PIU. An experienced PIS Consultant will be selected to bridge the gaps in the PIU's capacity and to provide hands-on support during the Project implementation period. The PIS consultant will provide the required knowledge, project management and technical expertise to build the PIU's and ASWRA's capacity, as well as to assist with compliance to loan agreement covenants and achievement of agreed project monitoring indicators in stipulated time frame.

[REDACTED]

Contracts risk assessment: - **Moderate High**

The water, sewerage and stormwater networks contracts are not technically complex, but carrying out the works in built-in urban conditions often causes delays associated with unforeseen ground conditions (e.g. old communication lines), the need to coordinate with third party providers etc. Design documentation is partially available (approx. 70 per cent in Shaki city and none in the villages), and the PIS Consultant will prepare the designs for the remaining works scope.

[REDACTED]

Project implementation arrangements:

ASWRA has a dedicated Project Management Unit that has experience of implementing internationally funded projects. [REDACTED]

The PIS consultant will be engaged [REDACTED] to facilitate the timely and efficient implementation of the Project by rendering assistance to the PIU and ASWRA. [REDACTED]

Procurement arrangements:

All goods, works and services, financed from the EBRD loan, will be procured following open competitive procedures in accordance with the requirements of the EBRD PPR for public sector

operations. The Project will use the Bank's latest templates of standard procurement documents and will conduct all procurement processes via EBRD Client E-Procurement Platform (ECEPP), to ensure highest degree of transparency and efficiency.

[REDACTED] All contracts will be subject to prior review by the Bank.

[REDACTED]

[REDACTED]

Annex 5 – Project Economic Rate of Return

[REDACTED]