CLUSTER EVALUATION

Projects Supporting Cross-Border Connectivity (Regional Integration)

European Bank
for Reconstruction and Development

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EBRD EVALUATION DEPARTMENT

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Report prepared by Tomasz Bartos, Associate Director, Senior Evaluation Manager, with the assistance of Alejandra Palma, Principal I, Evaluation Manager, Natalia Lakshina, Assistant Analyst and Stephanie Crossley, Analyst, all from EBRD Evaluation department. The team would like to thank the Bank's Infrastructure sector teams, as well as colleagues at EBRD's Resident Offices in Ankara, Baku, Istanbul, Kiev, Sarajevo, Warsaw and Zagreb for their help with provision of information and for their assistance with organising field visits.

One Exchange Square
London EC2A 2JN
United Kingdom
Website: www.ebrd.com

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Abbreviations

AADT	Annual average daily traffic
AfDB	African Development Bank
ADB	Asian Development Bank
AERA	Azerbaijani Energy Regulatory Agency
ATQ	Assessment of Transition Qualities
AZN	Azerbaijani manat
Bcm	Billion cubic metres
BiH	Bosnia and Herzegovina
BOT	Built, Operate, Transfer
BRI	Belt and Road Initiative
BTC	Baku-Tbilisi-Ceyhan oil pipeline
CAREC	Central Asia Regional Economic Cooperation
CBA	Cross-Border Agreement
CEB	Council of Europe Bank
CEE	Central Eastern Europe
CEER	Council of European Energy Regulators
CMEA	Council for Mutual Economic Assistance
COOs	Countries of Operation (of EBRD)
CRM	Concept Review Memorandum
CSs	Country Strategies (EBRD)
DSCR	Debt-service coverage ratio
EBITDA	Earnings Before Interest, Tax, Depreciation and Amortisation
EH&S	Environment, health and safety
EIB	European Investment Bank
EMRA	Energy Market Regulatory Authority
EPG	Economics, Policy and Governance Department (EBRD)
ESAP	Environmental and Social Action Plan
EU	European Union
EvD	Evaluation Department team (EBRD)
FBiH	Federation of Bosnia and Herzegovina
FDI	Foreign Direct Investment
FI	Financial Institutions team (EBRD)
GDP	Gross domestic product
GGG	Ganja-Gazakh-Georgian border highway
GOA	Government of Azerbaijan
GPA	Gdansk Port Authority
HRK	Croatian Kuna
ICA	Industry, Commerce and Telecoms (EBRD)
ICT	Information and Communication Technologies team (EBRD)
IDB	Inter-American Development Bank
IEG	Independent Evaluation Group (the World Bank)
IFC	International Finance Corporation
IFI	International Financial Institution
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IPPF	Infrastructure Project Preparation Facility
IsDB	Islamic Development Bank

KPIs	Key performance indicators
LEED	Leadership in Energy and Environmental Design
LTT	Legal Transition Team (EBRD)
LPI	World Bank's Logistics Performance Index
MEI	Municipal and Environmental Infrastructure team (EBRD)
MIS	Management Information Systems
MoU	Memorandum of Understanding
MSC	Mediterranean Shipping Company
OECD	The Organisation for Economic Co-operation and Development
OPA	Operational Performance Assessment
OPRC	Operation and Performance Contract
Opex	Operating expenses
PBMC	Performance-based maintenance contract
PERS	Port Environmental Review System
PSA	Port of Split Authority
PPPs	Public-Private Partnerships
PTI	Portfolio Transition Impact
RI	Regional Integration
RS	Republica Serpska
SAA	Stabilisation and Association Agreement
SASEC	South Asia Sub-regional Economic Cooperation
SCP	South Caucasus Pipeline
SEBR	South and East Baltic Region
SEETO	South East Europe Transport Observatory
SEIP	Social and Environmental Investment Programme
SEMED	South and Eastern Mediterranean
SGA	Selling, general and administrative expense
SGC	Southern Gas Corridor
SMEs	Small and medium-sized enterprises
TACIS	Technical Assistance to the Commonwealth of Independent States
TANAP	Trans-Anatolian Natural Gas Pipeline
TAP	Trans Adriatic Pipeline
TC	Technical Cooperation
TEN-T	Trans-European Transport Network
TEU	Twenty-foot equivalent unit
TI	Transition Impact
TIMS	Transition Impact Monitoring System
TIRs	Transition Impact Retrospective Report
TRACECA	Transport Corridor, Europe-Caucasus-Asia
ULCS	Ultra Large Container Ships
USD	United States Dollar
WBCN	Western Balkan Core Network
WBG	World Bank Group
WBIF	Western Balkans Investment Framework

Defined terms

the Bank /the EBRD	European Bank for Reconstruction and Development
The operation teams	staff of the Bank's teams responsible for the Bank's operations
Outputs	The products, capital goods and services which result from an operation (this and subsequent definitions adapted from OECD-DAC definition)
Outcomes	The short-term and medium-term effects directly attributable to operation outputs
Impacts	The positive or negative long-term effects to which an operation contributes, directly or indirectly, intended or unintended
Results	The output, outcome or impact (intended/unintended) of an operation

Executive summary

This report presents an evaluation of nine infrastructure projects promoting cross-border connectivity, eight in transport and one in energy. It assesses their overall performance, but gives particular emphasis to their intended and observable impact on cross-border connectivity and integration. While most (with one exception) were approved and largely implemented before "Integrated" was formally introduced as a transition quality, the evaluation nevertheless provides analysis, findings and insights directly relevant to current and future operations with regional integration elements and objectives.

The evaluation seeks to establish a broader context for its project-specific work - starting with a brief analysis of the evolution of the Bank's approach to regional integration, a review of the portfolio of early cross-border projects, as well as of more recent operations after "Integrated" became one of the six transition qualities. The linkages and incorporation of regional integration into selected country and sector strategies are examined, along with how other IFIs approach regional integration and how EBRD collaborates with them.

Bank work on cross-border regional integration has been almost exclusively through Transport sector operations. There are isolated projects in Energy sector, but they have been slow to implement and only one has been completed in recent years.

Regional integration was considered part of the "Market Expansion" transition quality up until 2017; but it was rarely formally targeted, despite being often cited as a potential project benefit. Since its introduction as a stand-alone transition quality, "Integration" has on the whole been the least frequently targeted transition quality (accounting for only 8% of explicitly targeted TQs in 2018). No incentives have been offered to bankers to pursue more complex multi-country, cross-border infrastructure projects and such projects have been rare. On the other hand, almost all country strategies (old and new) refer to regional integration; 12 current ones explicitly target physical connectivity. The most recent country strategies are supported by diagnostics, which identify meaningful gaps in regional integration and offer monitoring indicators, although these are relatively broadly defined.

Three key evaluation criteria have been used to evaluate the individual projects - relevance, effectiveness and efficiency. Overall ratings ranged from *Outstanding* (Gdansk DCT) to *Acceptable* (Port of Split and Azeri Roads). Although the latter achieved most of their physical objectives, their transition-related results have been marginal. Financial results varied; over-optimistic traffic projections were frequently observed. The Bank's investments in corridor Vc in BiH and, to some extent, in DCT in Poland, are likely contributed to the improved ranking of the infrastructure quality in these countries under the Logistics Performance Index (LPI). However, there was no discernible impact from infrastructure projects in other sample countries, the rankings for some of which deteriorated (Azerbaijan and Turkey). Their ranking slipped despite their overall LPI scores improvement. "Trading Across Borders" rankings under the "Doing Business" index improved in the last 10 years for all six sample countries, most so for Croatia and Azerbaijan and least for Turkey. The EU countries and BiH achieved relatively high rankings in this category. However, there is still ample room for improvement in the remaining countries where policies, procedures and inadequate border crossing organisation still hamper trade and cross-border movement.

Almost all IFIs had a Board-approved strategy in respect of their support for regional integration. The recent review of the approach to integration completed by the World Bank Group's IEG recommended that it develop a formal Integration Strategy covering all regions.

Main findings:

Policy and strategy context

- It proved challenging to conclusively assess the regional integration impact of most of the cross-border infrastructure projects as the **Bank does not have a framing strategy** for regional integration or cross-border investments against which to assess its operations, while work on many international corridors is still ongoing and relevant data is scarce;
- Historically, **three quarters** of the Bank's transport projects with cross-border components by volume were in the **road sector**. However, the evaluation of several of them demonstrates that in most cases actual traffic was disappointing. They had stronger local, rather than regional integrating impact;
- Historically, majority of the Bank's transport projects supported roads, while in the opinion of many interviewees **rail** played more prominent role in their countries' cross-border connectivity. However, the Bank has had relatively few rail projects with regional integration components;
- **Complex customs and immigration procedures**, as well as long waiting times at border crossings were often the principal hurdles to integration, slowing transportation and impacting choice of route by consignors. However only one among the Bank's four highway projects reviewed included components designed to address them through policy dialogue;
- As 70% of the world's trade is carried by sea, some **port container terminal** projects yielded evidence of a strong regional integrating impact;
- Also, as air passenger transportation is the fastest growing mode of cross-border movement of people, **airport projects** have shown solid regional integrating credentials;
- Tourism has gradually grown in the Bank's regions, however expectations of a large **tourist influx** ("catch up effect") to its countries of operation did not materialise;

Project design and performance issues

- Regional integrating impact potential was often cited, but without prior **diagnostics** completed. Performance **metrics** were insufficient and typically were limited to traffic/throughput, which projections were simply linked to a country's forecast GDP;
- There is no evidence of **experience from past** cross-border projects (or lessons from their evaluations) being utilised in the design of new projects;
- Most of the **physical infrastructure** components of cross-border projects were **completed**, albeit typically with substantial delays;
- Some projects had relatively modest **policy dialogue** objectives**,** however even these were often not achieved;
- Almost all **private sector** participation enhancement objectives set in the reviewed projects **failed;**

- The current traffic or throughput of **three quarters** of the evaluated projects has been well below the projected levels;
- The **transportation hubs** projects (sea ports and airports) have been generally able to demonstrate strong integrating impact much faster than those in roads (and easier to measure);
- Most evaluated projects were exposed to **political risks**, which often materialised, adversely impacting their connectivity potential;
- The **future prospects** for the evaluated projects achieving a stronger integrating impact after the transport corridors and pipeline interconnections are fully complete are generally good. Nevertheless, it will take a long time and huge investments will be required to fully realise their potential.

Country and sector strategies

- All 15 of the country strategies reviewed **referred to connectivity** as one of the transition challenges. Most of the recent strategies set improving cross-border connectivity as one of the Bank's operational **priorities**;
- Linkages to the "Integrated" transition quality in two thirds of the country strategies reviewed were assessed as **"strong"**;
- Subsequent Transport and Energy sector strategies have given **increasingly more prominence** to cross-border connectivity and offered more relevant performance monitoring frameworks related to it.

IFIs collaboration

- Two-third of projects reviewed (6) were **co-financed with other IFIs**. The Bank provided on average 52% of IFIs financing. It led financing in half of the projects, while it followed the lead of the World Bank or the IFC in another half;
- Clients were generally satisfied with IFI coordination but many sought **uniform procurement and reporting** requirements.

Recommendations:

- Prepare for Board approval a Bank-wide **strategy for Regional Integration,** including cross-border connectivity, to establish agreed objectives, priority sectors/sub-sectors, potential investment types, directions of policy dialogue and TC support areas;
- Target integration-related investments and particularly policy dialogue towards countries with the **largest ATQ gap score** for Integrated quality, i.e. in Central Asia, the Balkans and SEMED, actively pursuing opportunities in integration-boosting sub-sectors, such as rail, ports and airports;
- For projects targeting Integrated, ensure adequate system is in place **for gathering relevant data to measure it,** either by the client or by the Bank;
- Conduct a **focused assessment of why most of the private sector** enhancement and policy- related objectives of large infrastructure projects have **failed**.

1. Introduction

Integration was introduced as one of the Bank's new transition qualities in July 2017. EBRD defines the "Integrated" transition quality in relatively broad terms, focusing on its contribution to minimising transaction costs.

Box 1. Definitions of Integration

An integrated market economy has the policies, institutions and connectivity (energy, infrastructure and IT links) to minimise the transaction costs of trade, support competition in product and services markets, and tap a wide range of financial channels. Integration facilitates the upgrading of institutional arrangements to higher standards, and more generally, provides a coordination framework to governance, legal, regulatory and other institutions. The level of openness to trade and investment, as well the quality of cross-border and domestic infrastructure, are good indicators of the extent of integration in a country.

SGS17-114 – Transition Impact Methodology: Project Christopher- Guidance Paper on Operationalising the TI Qualities, 26 June 2017

The Bank's guidelines on measuring transition (see section 2.3) explain that this definition covers not only physical infrastructure but also projects which stimulate exports, FDIs or capital movements. Importantly, it also covers efforts to achieve higher standards, greater harmonisation with international norms, strengthening of institutions, development of regulatory frameworks, and greater adherence to the rule of law. Nevertheless, physical connectivity is clearly a critical enabler of a wider integration, i.e. enabling trade and the movement of people at greater speed and lower cost.

This review concentrates exclusively on projects which, implicitly or explicitly, aimed to support **physical connectivity among countries.** They are defined as infrastructure projects with a direct cross-border component or providing an essential link within national infrastructure for cross-border connectivity, with the ultimate objective of facilitating international trade or the movement of people across borders. This concept of regional integration in terms of physical cross-border connectivity, is arguably narrower than that of Integrated Transition Quality used by the Bank (see box 3).

Although integration as a source of transition has only recently been recognised, the Bank has, for many years, financed projects whose objectives included support for cross-border connectivity, through financing physical infrastructure and supporting systemic changes to bring institutional arrangements and practices in COOs in line with international standards.

This review assesses the extent to which the Bank has so far succeeded in strengthening physical connectivity and contributing to regional integration among its COOs or with other countries. It evaluates a cluster of nine projects[1] from six countries and two sectors - transport (eight projects)

[1] Originally 10 projects were proposed for this cluster, however, one (Trans Adriatic Pipeline - TAP), has not been completed yet and its integrating impact potential has been discussed as part of the TANAP project evaluation. EvD assessed (but did not fully evaluate) the integrating impact of an additional project - the Port of Sibenik, which included a client interview. Findings from this assessment are similar to those from the Port of Split evaluation and are presented in the related projects section of the Port of Split review in annex 2.

and energy (one project), which have been relatively recently completed and are representative of the Bank's efforts in this respect (see table 1 in annex 1).

The cluster projects were selected through discussions among the Banking, EPG and Evaluation departments. The criteria for selection included cross-border connectivity as a project objective (either explicitly articulated in the Board report or implicit), project completion, including availability of relevant traffic or throughput data, as well as relatively recent vintage (ensuring that the relationship between the client and the Bank still exists and Bank staff familiar with the project are still available). During selection, diversity of sub-sectors and countries was also sought (although inevitably highway projects account for almost half of the cluster, while for practical reasons the number of countries was limited to 6). The private sector is represented by three projects[2].

Moreover, it has been recognised from the start that regional integrating impact can rarely be assessed based on a single project. Therefore, although nine projects were earmarked as **core projects for evaluation**, the review also takes into account (to the extent possible) the impact, or potential impact, of related older Bank projects and newer ones which are not yet complete. These **associated projects** relate, for example, to sections of international routes financed by the Bank in earlier years, or still under implementation, connecting to the route financed by the "core" cluster project. They are listed in table 2 in annex 1.

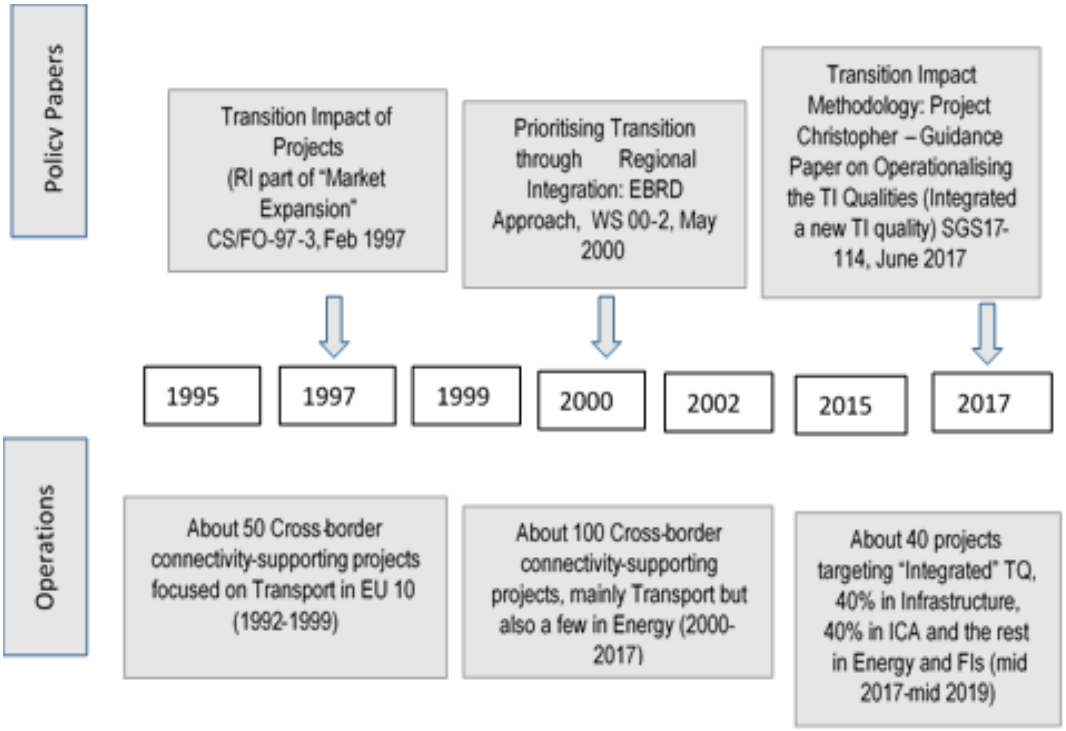
The evaluation starts with a short historical background, presenting the evolution of the Bank's approach to regional integration and briefly describes the Bank's landmark regional integration projects from the early days. It then examines whether and how the Bank's country and sector strategies treat regional integration. The main evaluation is summarised in section four, which first presents a brief assessment of the cluster projects' performance under three key evaluation criteria (relevance, effectiveness and efficiency), and then examines how each of the projects contributed to regional integration, measured in physical terms (e.g. change in traffic/flow of goods/passengers, comparing the forecast and actual levels), as well as in terms of "soft" integration, i.e. the extent to which the Bank's clients or COOs changed policies or adopted international standards and practices. The assessment is based on a review of relevant strategies, project documents and data, as well as interviews with government representatives, regulators, the Bank's clients, consultants and other stakeholders.

[2] The selection of projects for this cluster was challenging and can be seen as imperfect as projects clearly targeting regional integration have only been approved since mid-2017. As they involve public procurement and complex construction, many projects potentially well-suited for this evaluation are still at the early stages of implementation. On the other hand, the older projects, which implicitly targeted integration, have been repaid and in many cases the Bank has lost contact with their sponsors. However, section 2 reviews the Bank's cross-border project portfolio and describes the results of selected projects in an abbreviated format, often referring to past evaluations (see annex 6 and box 2).

2. Evolution of Bank's approach to regional integration

- From its inception the Bank financed a substantial number of projects with cross-border connectivity components, initially focusing on 10 EU accession countries. However, Integration was not defined as an objective until 1997. A formal policy statement related to regional integration came in 2000 but it did not set a strategic direction;
- Until 2017, Integration was treated as part of the Market Expansion transition quality. It was often mentioned as a benefit in international highway and railway projects but it was absent as part of the transition impact formally targeted by these projects;
- During the first 17 years of the new century the Bank financed almost 100 transport projects with cross-border components, amounting in aggregate to €5.8 billion. Half of them by number and 75% by value were in the road sub-sector. They were ultimately completed, usually with long delays, but their transition-related components often failed.
- Also the Energy Group signed seven cross-border projects, totalling almost €0.6 billion during that time. Three pipeline projects were completed (although the transition objectives of two were only partly achieved), however most electricity transmission projects were bogged down by very long delays and they are still under implementation or not yet started.
- Good lessons from previous regional integration projects were often highlighted in the new projects' Board reports, however there is no evidence that relevant mitigating measures were incorporated into the design of the new projects.
- "Integrated" is the least frequently targeted Transition Quality. It accounted for only 8% of all transition qualities targeted in 2018; it generally appears only as a secondary transition quality.

Figure 1. Timeline with the Bank's key policy documents and changes in operations related to cross-border connectivity.



It has been relatively challenging to discern how the Bank has been working and prioritising its work related to Regional Integration. Even harder is to capture the results of such work. Nevertheless, the Bank's approach to Regional Integration can be divided into three distinct periods. Figure 1 shows a timeline with key dates and events, while subsequent chapters briefly describe each of them.

2.1. Cross-border connectivity in the 1990s

In the first decade of transition, the integration of Central and East Europe into the world economy was often referred to in economic discussions, e.g. in the media, as one of the key challenges and priorities, next to building a market economy. However, until 1997 it was not explicitly specified as an objective in any of the Bank's policy documents. During the Bank's early days, its activities focused primarily on supporting privatisation and restructuring local enterprises, which at that time often lacked the managerial and financial prowess to substantially expand their operations internationally. Regional integration was generally seen as a welcome side-product of FDIs supported by the Bank. Nevertheless, many of the Bank's projects at that time promoted the adoption of international standards or governance practices by local companies. In terms of cross-border connectivity, many of the Bank's transport sector projects financed the construction of, or improvement to highways and railroads – parts of international corridors, as well as ports and airports, all of which *de facto* aimed at improving the integration of Bank COOs into the international economy.

The focus was clearly on the 10 EU accession countries, although some Balkan, Caucasus and Central Asian countries also benefited (see annex 3 for a list of these projects). Among the projects from non-EU accession countries, two Trans-Caucasian Rail link operations, undertaken separately in Azerbaijan and Georgia, were particularly interesting, see box 2.

Box 2. Trans-Caucasian Rail Link projects in Azerbaijan and Georgia

The Trans-Caucasian railway is a transport corridor between the landlocked countries of Central Asia and the West. The corridor, broadly based on the historic 'Silk Route', has become known as the TRACECA (Transport Corridor, Europe-Caucasus-Asia). The 924 km Trans-Caucasian rail link extends from Baku on the Caspian Sea (Azerbaijan) to the Black Sea ports of Poti and Batumi (Georgia).

In 1998 and in 1999 the Bank provided two sovereign-guaranteed loans under two separate operations – one each to the Georgian and Azerbaijan railway companies. Each loan was for US$ 20 million and was complimented by a substantial grant from EU TACIS. Both loans and grants were for track rehabilitation, signalling, telecommunication equipment and other related investments on the Trans-Caucasian railroad. The projects were completed with a three year delay. Since then, traffic has been good, exceeding original projections by about 25%. Both projects were evaluated in 2005 as **successful** albeit with many caveats and issues identified. One of them was: ***"Regional versus separate national project approach***". EvD argued that comparing the two railway projects and taking into consideration their rationales, history, similarity of project components and timeframe at the outset, there would be considerable merit for the Bank to approach both as a **regional** (i.e. cross-border) project, rather than as two distinct "national" projects. It identified a number of synergies between the two projects, including technical, procurement and corporate development. It proposed the following lesson/recommendation: *The Bank should seize opportunities for, if not actively promote, cross-border projects. Fostering regional cooperation and networking through regional development not only provides potential for synergy effects, but also tends to promote transition. This would include, by way of demonstration effects, increasing pressure to harmonise rules and regulations amongst the countries involved, and attracting increased private sector appetite for potential outsourcing opportunities.*

Following this evaluation the Bank continued to support an increasing number of projects with cross-border components, however there is no evidence that the suggestion to structure cross-border projects connecting two countries as "Regional", rather than national, has been followed. The Bank's "Regional" projects are almost all frameworks, investments into equity funds and multi-country corporate investment facilities in the ICA sector. In the 2000s there were a number of infrastructure and energy cross-border projects but they were all classified as one country projects (see section 2.2).

In addition to the projects listed in annex 3, in the 1990s the Bank financed other transport sector projects which indirectly contributed to the improved international connectivity of COOs, such as air navigation, rolling stock, intermodal logistics and railway stations. In total, by the end of the 20th century, the Bank had provided financing of approximately €2.3 billion to almost 50 projects with cross-border connectivity components, which *de facto* promoted integration.

During the 90s there were no electricity transmission, pipeline or ICT projects with clear cross-border components. However, it could be argued that many projects in these sectors strengthened the internal electricity transmission or telecommunication systems within individual countries, thus contributing to their better integration with international systems.

The Bank's first document which explicitly referred to regional integration as part of its transition architecture was ***"Transition Impact of Projects"*** (CS/FO-97-3) published by the Office of the Chief Economist in February 1997, which provided a conceptual framework for the analysis of the transition impact of projects and a checklist for the qualitative aspects of transition. As part of an illustration of the **Market Expansion** transition quality, the checklist referred to*: "Projects contribution to the integration of economic activity into the national or international economy".* The checklist was to be used for strategy and business planning, while designing the transition impact structure of a Bank project, and during the monitoring and evaluation[3] stages. In its description of the "Market Expansion" transition quality, the paper stated that there were two ways to expand markets, one being *"through project's contribution to the integration of economic activities into the national or international economy, particularly by lowering the cost of transactions."* However, there is limited evidence that this notion has been applied when designing the transition structure of subsequent Bank infrastructure projects. The benefit of improved integration is usually mentioned in the narrative story of selected projects which were to contribute to international transport corridors. However, even then, other transition qualities were chosen, rather than Market Expansion to justify the project's transition, e.g. "private sector development" (often through outsourcing of road maintenance, which rarely materialises) or "support for competition" (through competitive procurement). The reason for sidelining integration might be the difficulty in devising appropriate benchmarks for monitoring regional integration, which would be required if it was to be set as a transition quality supporting a project's rationale.

In 1999 the Board approved ***"The EBRD Operational Priorities for the Medium Term - Moving Transition Forward"*** (BDS99-24), which pointed to the policy trends supportive to regional integration (mostly related to the upcoming accession of 10 COOs to the EU) and argued that opportunities for projects with regional integration components would widen in the future. It directed the Bank to take an active role in *"addressing transition challenges in a cross-border framework"*.

[3] The paper also stated that the Evaluation Department (PED at that time) *"applies the checklist in reviewing the ex-ante checkable stories on transition impact, written by the bankers in their board reports".*

2.2. Cross-border connectivity projects during 2000-2017

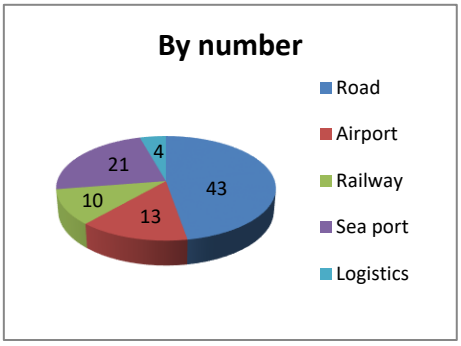
This encouragement prompted the Bank to publish ***"Promoting Transition through Regional Integration: the EBRD Approach",*** 5 May 2000 (WS00-2), which discusses the economic rationale for integration and EBRD activities in this area to date. However, despite its title, it did not offer any details of the proposed approach to regional integration, beyond suggesting the continuation of support for projects ranging from cross-border transport infrastructure to trade finance and tackling environmental hot spots, or supporting the expansion of local companies (see annex 5).

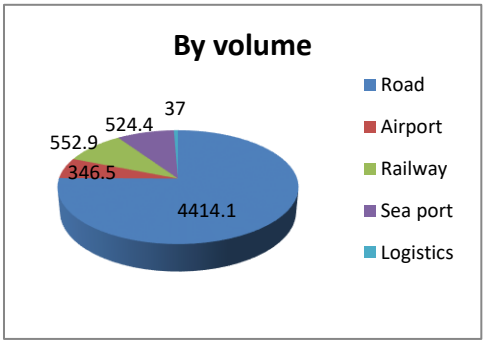
In EvD's view, although it contained some useful information on how the Bank understood the regional integration concept (i.e. very broadly), the 2000 paper was a lost opportunity to define the Bank's strategic approach to supporting regional integration. Instead, it focused on framing the Bank's activities to date under the regional integration concept, and proposing a continuation of the project-by-project approach, with no strategic vision or ambition to shape such future projects. Moreover, in EvD's view, deeming *"projects that have strong regional demonstration effect, e.g. regional post-privatisation funds, EU Phare-EBRD SME Programme*" to be supportive of regional integration, was questionable.

Nevertheless, in the new century the Bank markedly expanded the financing of projects supporting regional integration, with the Transport sector clearly leading the way in targeting improvements to cross-border connectivity. The transport projects falling into this category are listed in annex 4. They consist of highway and railway projects, which supported the construction or rehabilitation of international corridors, international airports and sea ports, as well as selected logistics projects. In total, between 2000 and mid-2017, the Bank financed 91 such projects with €5.8 Billion - 34% of total number and volume in the transport sector.

The sub-sector distribution of these projects is presented in figure 2. It illustrates dominance of road sector projects with €4.4 billion or 76% of the total volume and 43 or 47% of the total number of projects. Sea ports were also targeted relatively often (21 projects), although they accounted for only 8% of the volume. One could argue, that from purely cross-border integrating potential perspective, the Bank should have focused more on rail rather than road sub-sector (as in principal and according to several interviewees, rail is used more commonly for moving freight for distances longer than 300 km). But the Bank's cross-border rail sector projects were relatively less frequent than those in roads, accounting for about 11% of the total number and 9% of the total volume of the cross-border project portfolio.

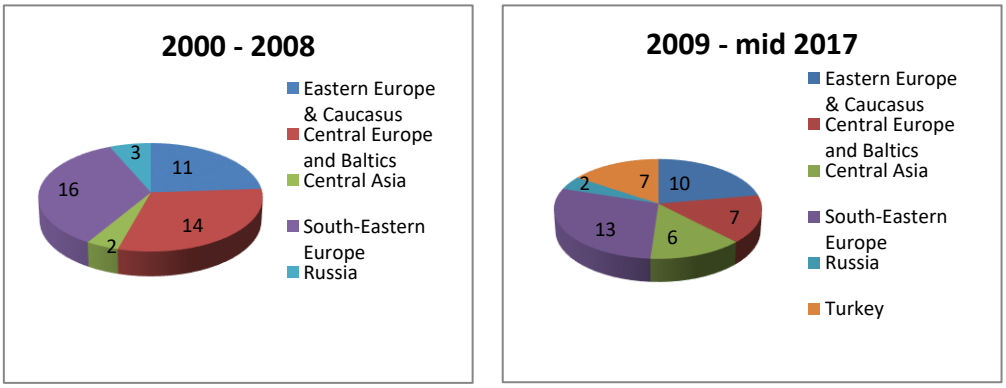
Figure 2. Transport projects supporting regional integration by sub-sectors





A division into two periods shows the gradual geographical diversification of cross-border connectivity projects. While cross-border projects were mainly in South-Eastern and Central Europe during the first eight years, they were more evenly spread over almost all regions during the subsequent eight and a half years. Figure 3 illustrates this change.

Figure 3. Regions targeted by cross-border transport projects in two periods



The results of the landmark road sub-sector projects financed during that time are summarised in annex 6. They point to some common characteristics of the Bank's road projects, which include long delays (in some cases twice the time planned), frequent cost overruns, problems with tenders and contractors but generally a completion of the road. At the same time, the projects usually failed to deliver on their transition impact expectations as road sector financing reforms, maintenance funding, outsourcing and especially that involving the private sector have rarely materialised. Provisions to streamline customs and immigration procedures have been incorporated into some projects but have not been implemented in practice. Traffic has been reported as increased but clients were rarely able to demonstrate this with the provision of exact numbers.

Also, the Bank's Energy Group signed seven cross-border projects during this period, three pipelines and four electricity transmission line projects, totalling €585 million. The former were the South Caucasus Pipeline (SCP) bringing gas from Azerbaijan to Georgia and to the Turkish border (the first part of the Southern Gas Corridor, see evaluation of operation 8 – TANAP, in annex 2), as well as the BTC and Thessaloniki-Skopje Crude Oil pipelines. Details of these two projects, as well as those of four electricity transmission projects are summarised in annex 6. Most of the transmission projects are still under implementation or did not start yet.

It is evident from these summaries that cross-border energy sector projects also experienced serious problems during implementation. The political commitment of the sponsors was critically important but also economic foundations were necessary to achieve the expected results. Where there was full determination of participating governments (e.g. SCP, BTC pipelines) they were completed without much delay. However, if there were government changes or, even worse, animosities between governments (Thessaloniki-Skopje pipeline), there were long delays or breaches of agreements. Similar to transport sector projects, energy operations had problems delivering on their transition objectives, such as sector reforms or related environmental and social programmes.

Board reports for some cross-border projects indicate that past experience has been gradually taken into account and the operation teams have been more aware of the risks related to such projects. However, not much evidence exists that these risks were better mitigated in subsequent projects. For instance, the "Past Experience" section of the Road Sector Development Project (Almaty-Bishkek) referred to the Bank's past projects in Belarus, Moldova and Azerbaijan, stating that the key lesson from them was that "*road sector institutions have been often much weaker than other transport entities, such as railways, ports or airports and more subject to political interference".* Another lesson pointed to risks related to complex procurement of large civil works and to contractors' performance. These were very good lessons, however not much was done to mitigate these risks and unfortunately all of them materialised in the Almaty-Bishkek road project (see annex 6). One of the key lessons from this project was that "*Cross-Border Agreements could be useful for trade facilitation, however they need to be implemented using definite action plan".* This was again a useful lesson and recommendation, however EvD hasn't found evidence of subsequent projects where such cross-border agreements have been used (with or without action plans), e.g. such an agreement was stipulated under the Corridor Vc project in Croatia, however it lacked a definite action plan and it remains unsigned.

2.3. "Integrated" transition quality and cross-border projects after 2017

In 2017 the Bank introduced a new approach to measuring transition to a market economy (project Christopher). It constituted a shift from the components of a market economy, to the desirable qualities of a market economy. Given the increasing populist backlash against globalisation, "Integrated" was included as a separate quality to stress the importance integration had for the Bank.

The new qualities were explained in the ***"Transition Impact Methodology: Project Christopher – Guidance Paper on Operationalising the TI Qualities",*** 26 June 2017 (SGS17-114). It included a chapter on Regional Integration, whose introduction as a new quality rested on the notion that to be efficient, market economies had to be integrated as *"internal and cross-border connectivity and integration of markets promotes competitiveness and resilience; thus integration could be considered as a tool to achieve other qualities"*. The paper also provided useful guidance as to type of projects and activities by sector, which could be classified as supporting the "Integrated" transition quality, see box 3.

Box 3. Guidance paper - Types of projects supporting the "Integrated" transition quality

ICA:

- Export boosting projects, particularly first time exporters
- FDIs (inward and by local companies elsewhere), particularly in sectors that have been hitherto relatively neglected

Financial Institutions:

- Investments in capital market infrastructure
- Trade facilitation across COOs

Energy:

- Expansion of electricity and gas networks, as well as petrol stations to new regions
- Development of cross-border interconnections capacity where energy is traded through the use of market coupling or in full compliance with the EU Congestion Management Procedure

Infrastructure:

- Expansion of physical transport infrastructure that addresses shortcomings/bottlenecks and materially improves the mobility of goods and people between or within regions, as well as between countries
- Associate reforms that facilitate cross-border institutional integration to simplify administrative processes with a view to improving the mobility of goods and people between regions
- International and regional connectivity (road bypasses, road corridors to airports/ports/logistics and new urban developments)
- Facilitate better regional integration between authorities, operations and other stakeholders

The guidelines paper provided a better explanation of the integration concept than the 2000 Approach paper did. Importantly, it classified projects as supporting integration if there were compelling arguments that they did indeed contribute to integration. For instance, unlike the 2000 approach, it excluded investments by private equity funds and, to a large extent, those in municipal infrastructure (although it is not clear what "new urban developments" meant, as "urban transport or roads projects connecting new areas" would have been a clearer definition).

The guidelines paper was very useful as it clarified the Bank's (particularly EPG's) approach to assessing a proposed project's transition qualities, methodology for rating a new project's transition impact and then measuring its achievement. Nevertheless, the guidelines did not constitute a document setting the Bank's long-term goals and strategic objectives in the framework of new transition qualities. These were articulated for some qualities (e.g. "Green" or "Inclusive") under the Bank's relevant initiatives, however, they were (and still are) missing for other qualities, such as "Integrated".

Alongside the new transition qualities, the Bank introduced a rule that only two qualities should be applied to any new project – one primary and one secondary.

During the two years after its introduction (July 2017- June 2019), "Integrated" was used as a transition quality in 41 projects. This accounted for 15% of the total projects, however as (on average) each project targeted two qualities, "Integrated" accounted for 8% of all transition qualities targeted during that two years. It was usually a secondary quality - applied as such in 65% of 2018 projects where it was used.

During the two years from mid-2017 to mid-2019 Integrated appeared in 41 projects, most frequently in Infrastructure projects (17 – all but one in Transport, accounting for 41% of all projects targeting Integrated) and also in ICA, accounting for 39% of all projects targeting Integrated (16 projects – with 11 in Agribusiness, four in M&S and one in ICT). The Integrated transition quality was much less applied in other sectors, i.e. in Energy and FI, both with four projects. Figures 4 and 5 illustrate the sectoral and geographical distribution respectively of projects where "Integrated" was used as a transition quality. Annex 7 illustrates the categories of projects targeting "Integrated" and the justification for including it as a transition quality.

Figure 4 – number of projects approved from mid-2017 – mid-2019 where the "Integrated" transition quality appeared, by sector

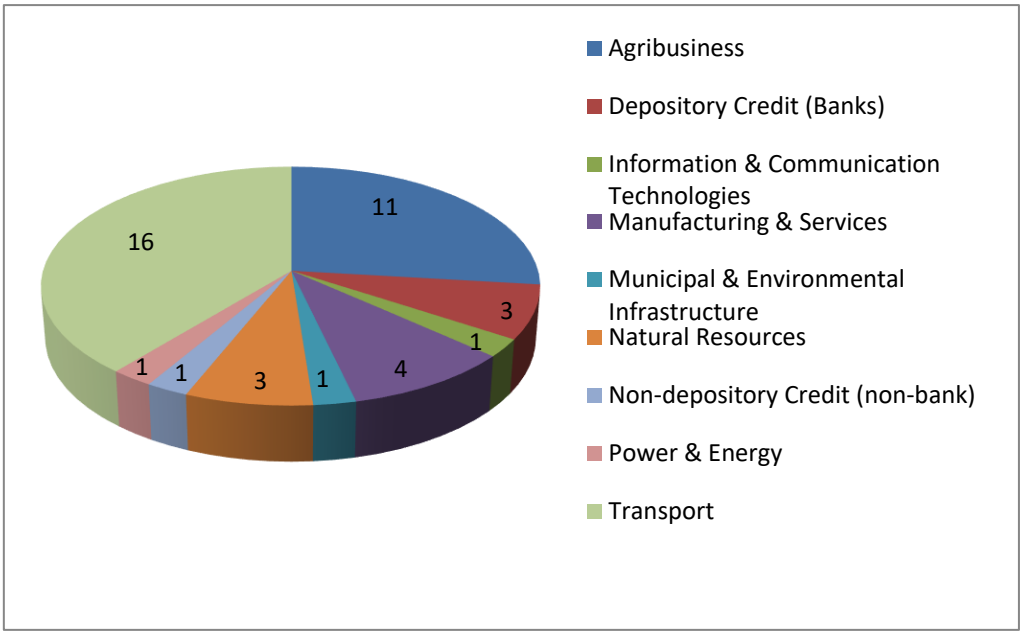


Figure 5 – number of projects approved from mid-2017 – mid-2019 where the "Integrated" transition quality appeared, by region

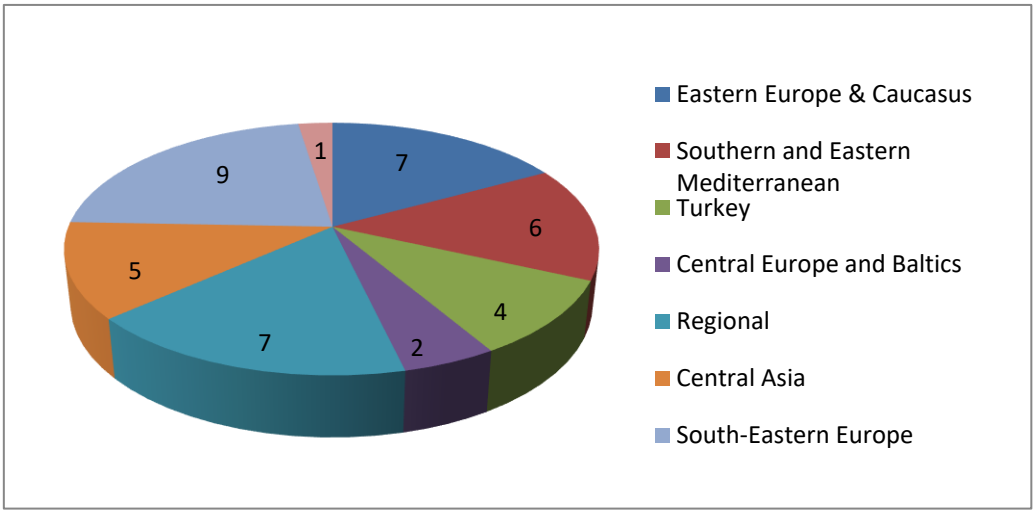


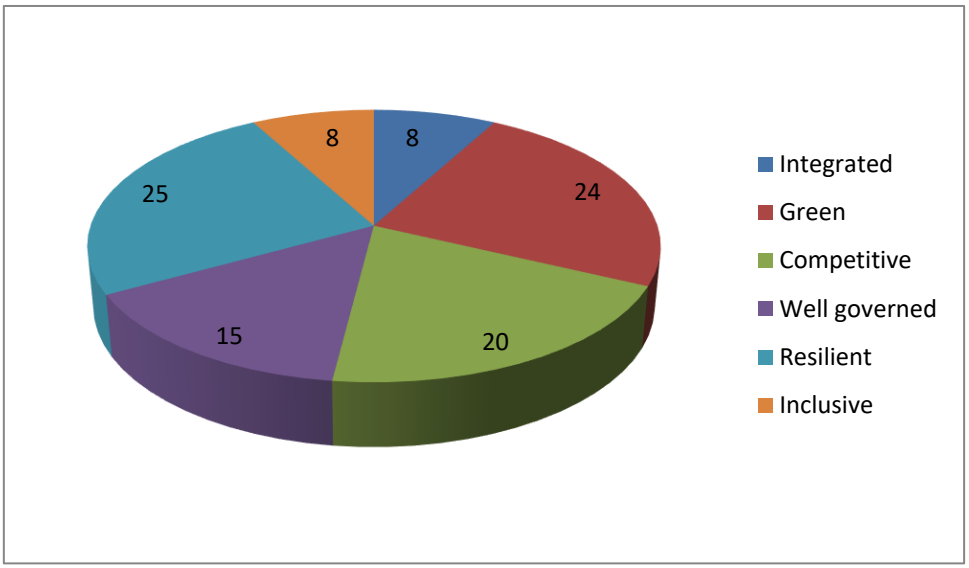
Figure 4 demonstrates that projects targeting the "Integrated" transition quality were concentrated in South-Eastern Europe (9) and Eastern Europe and the Caucasus (7). There were also seven "Regional" projects. These were mainly multi-country corporate facilities in the ICA sector, one Energy (TAP) and one Transport (project Nautilus – financing of a maritime company with operations in Kazakhstan and Turkmenistan). However, they were no multi-country infrastructure projects.

Further analysis conducted on a sample of 143 projects approved in 2018 indicates that "Integrated", has been a "poor cousin" in the family of Bank transition qualities. The "Resilient" transition quality was targeted most frequently (by 67 projects), followed closely by "Green", used in 64 projects, however the latter was a decisive leader in the "primary TI quality" category (49). Also "Competitive" and "Well-governed" were relatively frequently applied (in 54 and 41 projects

respectively). However, both "Inclusive" and "Integrated" were used in only 23 projects each and while "Inclusive" was more often used as primary quality (in 12 projects), "Integrated" was the primary quality in only eight projects and secondary in 15.

As these 143 projects targeted in aggregate 272 transition qualities (usually two qualities each, but in some cases only one), "Integrated" accounted for 8% of all qualities targeted. Figure 6 demonstrates the share of each transition quality in all targeted by 2018 projects.

Figure 6. Share of each transition quality in all qualities targeted by 2018 projects



The examples of projects targeting "Integrated" listed in annex 7 indicate that the EPG guidelines on the types of projects which could pursue "Integrated" have been largely followed, although it could be argued that the integrating potential is more clearly defined in some projects than others. For instance, some local infrastructure projects have more limited impact, while the projects supporting local suppliers' integration into a global network could be seen as more supportive of competition than integration.

Of 41 projects targeting "Integrated", most were in the Infrastructure sector (17 or 53% of all signed in this sector). Among them, EvD identified six supporting cross-border connectivity (three follow up projects to Corridor Vc, SMARTSA, Kriva Polanka and Project Frame – see annex 7), while one additional project can be regarded as having a cross-border component (UZ Electrification). The remaining projects supported mainly national or local connectivity (often important roads or rail lines but with no or minimum importance for cross-border movement). EvD identified five additional Transport projects signed during those two years, with a potentially strong cross-border connectivity impact, which did not target "Integrated" as one of their transition objectives, i.e. Queen Alia airport, Port of Tallinn, Port of Bar, Budapest Airport and Ekol Ro-Ro II project.

Therefore, in all, 11 Transport projects supported cross-border connectivity, accounting for 34% of all (32) Transport sector projects approved by the Board during the two years July 2017-June 2019. This may indicate that, although cross-border connectivity was pursued by the Bank in the Transport sector, it was targeted to a lesser extent (twice less) than national-level connectivity.

The reason might be stronger demand for Bank financing of national-level connectivity projects in COOs, likely combined with a larger proliferation of national-level projects overall. However, the

high degree of importance attached to cross-border connectivity in the transport strategies of the cluster project countries, as well as the low international connectivity scores attained by many COOs in the World Bank's Logistic Performance Index (see section 4.3) may indicate that opportunities to improve cross-border connectivity still exist and could have been represented more prominently in the Bank's portfolio.

As to other sectors, MEI has only applied the "Integrated" quality to one project so far – Cairo metro, which supports local connectivity. EvD notes however, that this quality was not applied to the Istanbul metro project.

After mid-2017, the Energy Group signed three cross-border gas pipeline projects (TANAP, TAP and BRUA), all related to the Southern Gas Corridor leading from Azerbaijan to Europe (see section 8 in annex 2), as well as one electricity transmission project - Moldova-Romania Power Interconnection (2017, €80 million), financing the interconnection of the Moldovan and Romanian electricity grids. This has not started disbursing yet.

In conclusion, EBRD's operations during its first decade of existence were almost exclusively country-oriented but this was justified by the status of its emerging network of COO. Market fragmentation, with some regions such as Central Asia and the Western Balkans presented challenges for the Bank's business efforts. However, the market evolved rapidly and the need to focus on sub-regions and the cooperation and integration among COOs toward transition grew fast. Over the years the Bank has progressively but very slowly crystallised its approach to regional integration. The first attempt in 2000 to address it (in the "Approach to Promoting Regional Integration" memo) lacked clarity on the Bank's strategic objectives in pursuing regional integration. It proposed the continuation of a project-by-project approach in response to market demand, rather than the more ambitious gaol of shaping such demand. The benefits of regional integration were referred to relatively often in transport sector Board reports during the early 2000s but it was rarely used as a transition objective targeted under the Market Expansion quality. A clearer statement on what encompasses Integration came only in 2017 when new transition qualities were introduced, among them "Integrated". Since then Integrated has been the least targeted of all qualities, although it was applied in 53% of Transport projects. About one third of these projects pursued cross-border connectivity, demonstrating stronger demand for national-level integration projects, rather than cross-border.

3. Linkages of country strategies to regional integration

- Almost all of the 15 country strategies (CSs) reviewed referred to connectivity as one of the transition challenges, while some, particularly the most recent, set improving cross-border connectivity as one of the Bank's operational priorities. Linkages to the "Integrated" transition quality in two thirds of the country strategies reviewed were assessed as "strong";

- However, off all 37 current country strategies only one third (12) targeted physical connectivity;

- All of the strategies since the inception of the new transition qualities include a description of the challenges and diagnostic papers for the *Integrated* quality, albeit in very broad terms;

- Four strategies (2007 BiH, 2007 Ukraine, 2010 Azerbaijan, 2010 Croatia) underscored integration-related government strategic priorities, such as EU membership, EU integration, Euro-Atlantic integration and integration to the global economy;

- A third of the strategies indicated obstacles to connectivity in rail and road sectors. Other challenges included weak trade integration, missing or inadequate legal frameworks and logistics infrastructure, as well as inadequate borders crossings;

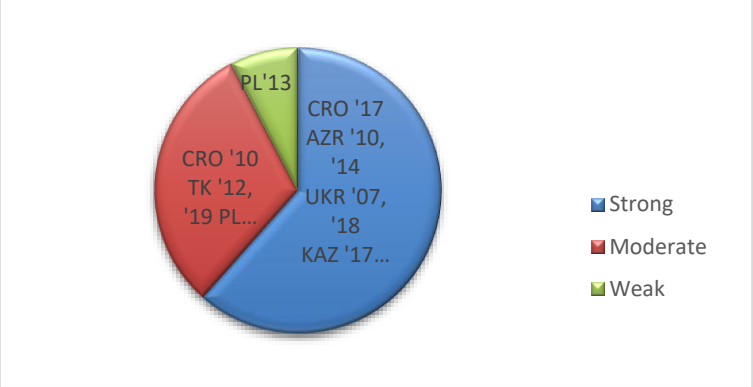
- Over half of the strategies reviewed, both older and newer, e.g. Croatia, BiH, Turkey, Ukraine, Mongolia and Georgia, set regional integration as an operational priority, mainly in the form of improvements to the transport and energy infrastructure;

- The six most recent strategies presented a monitoring approach with outputs/outcomes and tracking indicators, although the latter were quite general. In most cases baselines were missing, assumed to be zero or expected to be defined at project approval;

- Integration also featured in the Bank's recent Transport and Energy sector strategies. It was highlighted as one of transition challenges in both and set as the operational priority in Transport strategy. The ICT strategy focused on rural integration at a national level.

EvD reviewed six country strategies (CS) under which the evaluated cluster projects were approved (Azerbaijan, BiH, Croatia, Poland, Turkey, Ukraine), as well as the six current strategies and associated diagnostics for these countries. The latest CSs for an additional three countries (Georgia, Mongolia and Kazakhstan) were also reviewed, making a total of 15 CSs and four diagnostic papers (prepared to inform the most recent strategies 2017-2019. Annex 8 contains a full analysis of the linkages between the Integrated quality and the 15 country and seven sector strategies (Transport, Energy and ICT). This section presents a summary of key linkages in 12 country strategies related to cluster projects. As figure 7 demonstrates, linkages of most of the reviewed country strategies to "Integrated" were relatively strong and their strength has been gradually increasing. Strategies for Turkey and EU countries gave less prominence to "Integrated", although they also referred to it as briefly described below. Nevertheless, based on Strategy Implementation Plan 2020-22 (BDS19-169 (Rev1), EvD notes that out of 37 currently applicable (beginning of 2020) country strategies, only 12 (32%) targeted "Improved quality and connectivity of infrastructure" under Integrated quality. It was the only indicator (and very general one) for measuring physical connectivity (other indicators for Integrated were related to FDIs, enhanced trade, capital markets integration, etc.).

Figure 7. Assessment of linkages of country strategies to "Integrated" transition quality



Croatia CS 2010 intended to target priority infrastructure, including regional transport networks through the Western Balkans Investment Framework (WBIF). Transition goals for infrastructure included "support regional trade and investment through infrastructure development". Among its operational priorities was targeting infrastructure investments with EIB, through the WBIF. The Bank also intended to support the airport and port PPPs,

Croatia CS 2017 sets "Increased cross-border trade and investments flows" as one of its strategic objectives. It specifies indicative activities and tracking indicators to measure progress. Two of the proposed activities are "Support new investments linked to improving regional interconnectivity and co-operation in energy, transports and capital markets" and "Support logistic companies in Croatia in order to boost transport through ports, highways and railways".

Bosnia and Herzegovina CS 2007 set regional integration as one of its three priorities: "assist BiH's regional integration and its progress towards EU membership through physical investments in key infrastructure projects as well as institutional development and strengthening of state institutions". In the road sector, the EBRD expected to focus on the road network rehabilitation, to be co-financed with the World Bank and EIB. Commercialisation of the sector was to be supported through the introduction of performance-based maintenance contracts and MIS. The execution of projects on the north-south axis was to be prioritised under the Regional Road Development programme. One of the transition objectives underpinning the Bank's involvement in the BiH transport sector was support for regional integration. The Bank's activities were expected to be aligned with the Memorandum of Understanding on the Development of the South East Europe Core Regional Transport Network.

Bosnia and Herzegovina CS 2017 was informed by a "mini-diagnostic", which noted the low degree of integration between BiH and the EU, despite their Stabilisation and Association Agreement (SAA) signed in 2015. It identified a number of infrastructural and institutional deficiencies (see annex 8 for details). One CS priority was to "support development of key transport and energy cross-border links to promote Integration with the region, while enhancing resilience of the economy". It presented a Country Strategy Results Framework with indicative activities and two tracking indicators: net increase in the throughput of infrastructure and volume of electricity traded.

Azerbaijan CS 2010 identified two main challenges: "integration into the global economy" (particularly in relation to non-oil economy) and "advance public infrastructure reform". It set the Bank's strategic orientations, including "the regional development of all infrastructure sectors with a particular focus on interconnection with neighbouring countries". This encompassed support for reform in the road sector, preferably with other IFIs, and improving road sector administration and management efficiency.

Azerbaijan CS 2014 confirmed the Bank's commitment to the hydrocarbons sector, and highlighted the importance of the Southern Gas Corridor for "diversification of gas export routes and regional energy security in Europe." Within the strategic priority of improving governance and the business environment, the EBRD intended to "support projects of regional significance that enhance regional trade via diversification of hydrocarbon export routes and which favour regional integration of energy infrastructures".

Turkey CS 2012 stressed the "need to facilitate trading across borders, including support for further trade integration with the SEMED region." A second challenge was strengthening regional

and rural infrastructure, in which the expansion of regional infrastructure services was required due to rapid economic growth and accelerated regional integration. The EBRD would also continue to work with other IFIs and commercial lenders in financing large PPP projects with a regional dimension in the transport sector. Also, it was to provide "effective transport solutions in more remote regions" and to support private sector operators in the development of intermodal transport operations through the provision of long term funding.

Turkey CS 2019 was informed by diagnostics, which ranked internal integration higher than external. Challenges included low FDIs integration into global markets, partly due to the large domestic market. Domestic transport and logistics infrastructure, as well as cross-border integration were assessed as good, save for rail. ICT infrastructure was deemed below OECD levels. One of the strategic priorities was to accelerate Turkey's green economy transition and regional energy connectivity. One of the anticipated activities was to "support investments in gas transmission and distribution networks and infrastructure connectivity". Investments in ports and airports no longer appeared among the strategic priorities.

Poland CS 2013 did not make any direct references to cross-border connectivity, however, one of the strategic priorities was to "enhance the private sector's role in the economy, including supporting Polish companies in their regional expansion and cross-border investments."

Poland CS 2017 the diagnostic paper deemed infrastructure quality to be poor (low motorway density and quality of regional roads). Despite Poland's economy's generally advanced status it deemed "well-governed, competitive and integrated the transition qualities, which still substantially depart from the best international standards". One of the CS's strategic priorities was "development of integrated and intermodal transport infrastructure, including through PPP and concession structures".

Ukraine CS 2007 its transition challenges included low competitiveness, hampered by infrastructure and transport bottlenecks. The Bank was to support infrastructure, as being key to the country's integration into European transport networks and the world economy. It was to concentrate on the development of the TRACECA and other main corridors and their interconnections to the Trans-European Transport Networks. The objective was to "facilitate the transportation of goods and passengers, as recommended by the High-Level Group on the extension of the main trans-European transport axes to neighbouring countries, as well as by the Long-Term TRACECA Strategy".

Ukraine CS 2018 diagnostics identified poor and deteriorating infrastructure (mainly roads) and low quality of logistics (cost and time of border crossing and documentary compliance) among the challenges. This made the private sector less integrated. Customs procedures were found to be cumbersome, inefficient and excessively bureaucratic. More specifically, port dues and tariffs were higher than those in other countries. Also, ICT quality was poor. One of the strategy priorities was to "improve integration by facilitating trade and investment, expanding infrastructure links, and supporting convergence with EU standards". Also, the Bank was to support the integration of companies in cross-border value chains.

These examples demonstrate that the Bank's country strategies for almost all countries referred quite extensively to connectivity as one of the transition challenges. Moreover, many CSs, particularly the most recent ones, set improving cross-border connectivity as one of Bank's operational priorities. As a result, linkages to the "Integrated" transition quality in 10 out of 15

country strategies were assessed as "strong". Five country strategies for more advanced countries (Poland, Croatia and Turkey) had less pronounced linkages to Integrated (assessed as "moderate") as their EU membership or candidate country status elevated their degree of integration. Nevertheless, their infrastructure was deemed far from adequate and therefore set to be targeted by the Bank, supporting the "Integrated" transition quality.

EvD also reviewed seven **sector strategies** (Transport, Energy and ICT). It found that similarly to country strategies, prominence given to Integrated transition quality increased with time. Integration was indirectly referred to in the **2005 Transport Policy** (e.g. "need to work on TRACECA, REBIS and TEN-Ts, as well as ports, and address custom legislation, including with EIB"). Then it was treated more up front in **2013** (one of the roles of Transport was defined as supporting regional integration). In **2017 Transport Strategy**, regional connectivity was identified as one of the challenges and the "Connected Networks" has been designated as one of four strategic directions, aiming at improved quality and connectivity of network infrastructure. This strategy contains a performance monitoring framework with tracking indicators defined as outputs in the form of number/volume of investments and number of km of road/railway tracks. Outcome indicators include the increase in infrastructure usage and cargo/passenger capacity. This is certainly a step in the right direction. However, both strategic targets and monitoring indicators are very general, consequently evaluability of this framework is limited due to the lack of baselines and more specific targets.

The need for better integration of energy systems among the Bank's COOs was also mentioned in **2013 Energy Sector Strategy**. One of the transition gaps was identified as absence of sufficient physical and regulatory infrastructure preventing effective cross-border trading. One of the 7 pillars of this strategy directly referred to regional integration ("Building deep and liquid energy markets"). Under this pillar the Bank's objective was to "support energy interconnections in order to build greater regional integration". The **2016** update of this strategy emphasised energy security and cross-border infrastructure. Investments targeted were to include the Southern Gas Corridor, north-south transmission interconnections and the integration of electricity markets. **2018 Energy Strategy** pointed to the need to manage rising level of intermittent renewables through regional integration and interconnection. Cross-border cooperation and improved interconnectivity were identified as challenges. Absence of integrated regional markets was identified as an obstacle to energy security. The second strategic direction called for fostering the development of energy markets and integration in to regional markets. Outputs were to be measured in terms of number of investments, while outcomes were defined in very general terms, e.g. improved regional energy infrastructure. Similarly to Transport strategy, it was a step in right direction. Nevertheless, the strategy presented only very broad and general targets and monitoring indicators.

The **2019 ICT Strategy** focused on rural integration at a national level, although it also mentioned a need for improved international connectivity. See annex 8 for detailed analysis.

4. Performance assessment of cluster projects

The evaluations of nine cluster projects are presented in annex 2. Table 1 summarises the results of these evaluations. Principal issues identified for each category are described in the following sections, while integrating impact is addressed in chapter 4.2. Chapter 4.3 identifies the integrating impact of cluster projects at the country level.

Table 1. Summary of evaluation rating of cluster projects

Cluster Project, Country	Relevance and Additionality	Results	Efficiency	Overall Performance	Regional Integration Impact	
					Current	Future
1.Corridor Vc Bosnia & Hercegovina	Excellent	Fully satisfactory	Excellent	Good+	**Weak**	**Moderate**
2.Corridor Vc Croatia	Fully satisfactory	Fully satisfactory	Partly unsatisfactory	Good-	**Weak**	**Moderate**
3. Azeri Roads Rehabilitation, Azerbaijan	Fully satisfactory	Partly unsatisfactory	Fully satisfactory	Acceptable	**Strong**	**Strong**
4.Pan-European Highways Ukraine	Excellent	Fully satisfactory	Fully satisfactory	Good	**Weak**	**Moderate**
5.DCT Gdansk Poland	Excellent	Fully satisfactory	Excellent	Outstanding	**Strong**	**Strong**
6.Asya Port Turkey	Fully satisfactory	Fully satisfactory	Partly unsatisfactory	Good-	**Moderate**	**Moderate**
7.Dalaman Airport Turkey	Fully satisfactory	Fully satisfactory	Partly unsatisfactory	Good-	**Strong**	**Strong**
8.Southern Gas Corridor Azerbaijan	Excellent	Fully satisfactory	Not rated	Good	**Moderate**	**Strong**
9.Port of Split Croatia	Fully satisfactory	Partly unsatisfactory	Unsatisfactory	Acceptable	**Moderate**	**Moderate**

4.1. Overall performance

- The relevance of the cluster projects has been generally strong, testifying to their good fit with the Bank's strategic objectives, as well as the high importance of such projects for the host countries;

- The physical implementation of most of the cluster projects has been achieved, albeit often with very long delays and in some cases with cost overruns. However transition impact components were much more difficult to achieve and in two cases materialised only marginally, while most of the other projects achieved them only partially;

- Almost all private sector participation enhancement-related objectives set in the cluster projects failed.

- Half of the projects performed well financially, while the other half encountered financial problems, mainly due to political instability in the given region or country, which affected the clients' business performance.

4.1.1 Relevance

The relevance of four projects in the cluster was assessed as "Excellent" and five as "Fully satisfactory", indicating that in general, cross-border connectivity projects are among the top

priorities projects for both the Bank and the host governments, which are aware of their enabling role in supporting trade and ultimately economic growth and job creation.

The relevance of one project - the original 2011 Azeri Roads Rehabilitation project targeting regional, secondary roads, could be seen as only partly satisfactory as ultimately it was deemed a lower priority by the government and entirely reshaped in 2016 to target a different type of road – an international corridor. This shift improved the relevance of this project, particularly in respect of cross-border connectivity. As most of the Bank's loan was ultimately used for the new project its relevance has been rated fully satisfactory.

Among the projects with "excellent" relevance, the Southern Gas Corridor was of special importance as a long-awaited pipeline, connecting the Caspian gas fields with Europe for the first time. Its significance in terms of gas security (the first gas supply route to Europe, alternative to Russian pipelines) can be seen as even stronger than its potential for closer integration between the Azeri energy system and that of Europe.

Also, the road projects (Corridor Vc in Bosnia and Herzegovina, as well as Pan-European Highways in Ukraine) responded very closely to the needs of these countries, articulated in their governments' transport strategies, while addressing the priorities and transition gaps identified in the Bank's country and sector strategies.

Several projects (Corridor Vc in BiH and Croatia, port of Split, Pan-European corridors, Azeri Roads) were continuations of earlier Bank projects in the same sub-sector, or even rehabilitated new sections of the corridor, other parts of which were financed by the Bank's earlier projects (see the associated projects sections in annex 2). In some cases, they also reinforced or continued the sector reforms initiated under earlier projects.
The additionality of almost all projects was fully verified as the long economic life of infrastructure assets justified long-term financing, which was not generally available in the Bank's COOs. Moreover, almost all projects had a set of fairly ambitious transition and environmental objectives, which further supported the Bank's involvement in these projects.

4.1.2 Effectiveness

The effectiveness of seven projects (77%) was rated "fully satisfactory", while two were "partly unsatisfactory". In general, the physical implementation of all cluster projects has been achieved, albeit often with very long delays and in some cases with cost overruns (see table 2). However, the transition impact components were much more difficult to achieve and in two cases (Azeri Roads and Port of Split) materialised only marginally, while most of the others achieved them only partially.

In the case of Azeri Roads, the project's scope was changed and implementation suffered long delays. Part of the project is still under implementation. The project's market-promoting components, namely road network management, such as tolling, performance based contract and outsourcing of non-core maintenance have not been introduced. With 20,000 employees in 60 road maintenance departments the state road agency has not been interested in outsourcing. Tolling has also been seen as unfeasible, although the state agency maintains that it might try it in the future for Baku's northward highway. Similarly, almost all private sector-related benchmarks failed in other projects, including the introduction of PPP in Corridor Vc in BiH and in the port of Split in Croatia.

Even some other, less ambitious but market-oriented objectives proved difficult to achieve. For instance, local companies in BiH have not been able to work under maintenance performance contracts (as envisaged under the Corridor Vc project) and this corridor is currently maintained via standard contracts. Croatia and Bosnia and Herzegovina failed to sign the customs and immigration protocol, which was hoped for under the Corridor Vc Croatian section project. Environmental certifications have not yet been achieved by the port of Split and Dalaman airport. A new Energy Law (under Southern Gas Corridor) was prepared and it is likely to be approved soon but it won't be fully in line with the EU's Third Energy Package, as planned.

Notable transition achievements included the introduction of road sector financing mechanisms (for capex and maintenance), through dedicated fuel tax, levy or a fund in BiH, Ukraine and Azerbaijan, as well as the corporatisation of the highway agency in BiH. Table 2 summarises the cluster projects' results.

Table 2 – Summary of cluster projects' results

Cluster Project, Country	Physical objective	TI objectives not achieved	TI objectives achieved
1.Corridor Vc Bosnia & Hercegovina	Achieved (83% of planned), two year delay, 14% cost overrun	-PPP tender failed	-fuel levy introduced -Autoceste corporatised -corporate plan prepared and MIS introduced -PPP strategy prepared
2.Corridor Vc Croatia	Achieved, five year delay (one section still to be opened to traffic)	-customs and immigration protocol with BiH not signed -no separate entities for tolling and maintenance established	-corporate strategy for HAC prepared and adopted -procurement policy adopted
3. Azeri Roads Rehabilitation, Azerbaijan	Part 1 (under tranche A) achieved, four year delay, part 2 under implementation (to be completed in 2020), 4.5 year delay expected, savings expected	-tolling option not selected and tolling not introduced -performance based contract not implemented for maintenance -outsourcing of non-core maintenance not implemented	-Roads sector Master Plan adopted -funding allocated for road maintenance -performance based maintenance contract tender documents prepared
4.Pan-European Highways Ukraine	Part 1 (under tranche A) achieved, 1 year delay, part 2 under implementation, five year delay expected. Some savings expected	-axel weight tax not introduced yet	-fuel tax introduced and the State Road Fund established -performance-based maintenance contract awarded
5.DCT Gdansk Expansion Poland	Completed on schedule with 14% savings	-volume of transhipments (slightly short of the target due to sanctions on trade with Russia)	-volume and containerisation ratio increased -diversification of clients achieved -energy reduced

6.Asya Port Turkey	Completed with nine months delay and 28% savings	-diversification of client base (99% of business with one client) not achieved	-greater completion and increased transhipment volume achieved -large container vessels accommodated ISO certification obtained
7.Dalaman Airport Turkey	Completed on schedule and with 1% savings	-LEED and ISO certification (to be obtained in 2020)	-energy efficiency target exceeded -another airport concession without traffic guarantees granted
8.Southern Gas Corridor Azerbaijan	Completed on schedule with 24% savings	-new Energy Law prepared but not yet approve and is unlikely to be fully in line with EU's Third Energy Package	-Energy regulatory agency established and its staff training is ongoing -corporate governance improvements package implemented
9.Port of Split Croatia	Completed largely on schedule with 30% cost overrun	-PPP for new terminal not implemented -Ecoport status and PERS certification not obtained	-IFRS introduced

4.1.3 Efficiency

Six cluster projects (66%) were sovereign-guaranteed or sovereign loans. Nevertheless, repayment from an identified revenue stream, flowing to an implementing entity (e.g. a highway agency) was an objective under most of them.

One project (TANAP) was not rated for efficiency, as it was completed only recently and is not due to start generating positive cash flow until next year. Half of the eight projects which were rated performed well - two (DCT and Corridor Vc in BiH) were rated "excellent" as their performance substantially exceeded the projections, while the efficiency of two other projects was rated "fully satisfactory" as they largely achieved the forecast performance. The introduction of a fuel levy (and its subsequent increase) in BiH ensured the sound financial performance of the highway agency there, whose revenues, EBITDA and net profit exceeded the original projections by about 25-40%. DCT Gdansk benefited from increased container business due to Poland's economic growth, while Asya port suffered from a business slowdown in the Black Sea area due to conflict in this region. Such regional conflicts and political upheavals in Turkey also impacted Dalaman airport's business and its financial results. In summary, four projects experienced financial difficulties:

- Corridor Vc in Croatia - the highway agency revenues have been substantially below projections due to fuel tax growing much slower than expected. Consequently, the Bank had to waive its liquidity and DSCR covenants;
- Asya port – the container terminal suffered business slowdown in the Black Sea region due to conflict in Ukraine and the volume of containers handled was substantially below projections for 2016 and 2017. Its business has recovered since, however its 2018 revenues and EBTDA were 50% and 30% respectively below projections.

- Dalaman airport – due to political upheavals in Turkey and the region the airport's traffic was below projections for 2015-2016 but recovered in the following years. The client's 2018 revenues and EBITDA in TRY exceeded the forecast but due to TRY devaluation were below the Euro projections. The financial expenses (including FX loss) led to a net loss for the year of €23.4 million and negative equity of €1.6 million;
- Port of Split – the cruise ship traffic was about 30% below forecast, only partially compensated by better than projected domestic ferry traffic. Revenue projections were inflated by a "catch up effect" (which didn't materialise) to demonstrate the port's ability to service the Bank's debt on its own. The terminal's PPP failure deprived the borrower of the concession revenues forecast at approval. The loan is serviced mainly due to government transfers.

Overall, the performance of the cluster projects has been mixed. One project was assessed as *Outstanding* (Gdansk DCT) due to its strong relevance, as well as physical, transition and financial results, which exceeded the projections. Corridor Vc in BiH was rated *Good*+ as it attained most of its objectives and the client has been performing well (although its traffic has been disappointing as the highway is not yet finished). Two projects were rated *Good* and three other projects *Good*- as they achieved most of their objectives, however their financial performance suffered due to political instability in their respective regions. Finally, two operations (Azeri Roads and Port of Split) were rated *Acceptable*. Their investments were completed, albeit with difficulties, however their transition impact was marginal, while the financial performance of the latter was poor.

4.2. Regional integrating impact

- Only one cluster project included the 'Integrated' transition quality, however the Board reports for all other projects referred to regional integration as an expected benefit.
- Actual traffic on most of the road corridors was well below the projections. One was above the forecast, however the reliability of traffic data was poor.
- The integrating impact of the Bank-financed road projects was much stronger at the local level than the international/regional level. Their utilisation close to local hubs has usually been good, in line with or above the projections;
- Policy-related integration measures have rarely been included and those which were pursued were not always achieved.
- The future integrating potential of most projects was stronger than their current one due to their still fragmented status or lack of interconnections, which were expected in the future.

4.2.1 Hard integration - results

Except for one (Southern Gas Corridor), all the cluster projects were approved before the introduction of "Integrated" as a transition quality and therefore they had no explicit regional integration objectives. Nevertheless, almost all of them referred (in some cases extensively) to a potential regional integrating impact due to improved cross-border connectivity. Annex 9 summarises these references.

The three more recent projects, which financed new sections of corridor Vc in BiH and one in Croatia signed in 2018-2019 (see table 2 in annex 1) do target "Integrated" and specifically regional cross—border integration, as their primary transition objective. However, their Board reports do not provide any diagnostic justification in its support beyond the statements that said

impact will be achieved due to the concentration of population and business activity along this corridor, while the traffic projections are linked to forecast GDP increases in BiH or Croatia.

The "hard" integrating impact of the cluster projects has been assessed predominantly based on traffic or throughput levels, versus base data (pre-project) and projections made at approval[4]. Structure and the direction of traffic, as well as the type of goods traded were also analysed wherever data was available. Consequently, three cluster projects have been rated as having "strong", three as "moderate" and another three as having "weak" regional integrating impact (see table 1).

The actual traffic results of most cluster projects versus projections were disappointing. In many cases the reliability of data was poor, particularly for highways, as clients often counted traffic on road sections differently from what was assessed during the feasibility studies. However, using some approximations and averages, EvD calculated results as summarised in table 3 below:

Table 3. Summary of traffic/throughput assessment of cluster projects

Cluster Project, Country	Traffic/throughput	Comments
1.Corridor Vc Bosnia & Hercegovina	55-60% **below** projections (AADT)	Autoceste's (State Highway Agency) data. However independent report by SEETO reports that traffic on Corridor Vc was even lower and that it was the only international corridor in the Balkans where traffic has been decreasing. About 15% of traffic is reported from cargo trucks, with almost all of them from BiH.
2.Corridor Vc Croatia	50%-80% **below** projections (AADT)	HAC's (State Highway Agency) data. 50% below projections refers to the northern section (Hungary-BiH) and 80% below projections to the southern (BiH-Ploce).
3. Azeri Roads Rehabilitation, Azerbaijan	20-55% **above** projections (AADT)	AYS's (Azeri Highways Agency) data. 20% above projections refers to one regional road completed under tranche 1. 55% above projections was on Ganja to Georgian border road (still under construction). 47% of traffic was from cargo trucks. **However the reliability of this data has been questioned. AYS did not respond to EvD's additional queries.**
4.Pan-European Highways Ukraine	30% **below** to 15% **above** projections (AADT)	Ukravtodor's (Ukrainian Roads Administrator) data. 15% above projections was recorded on the first 10 km approach to Kiev from the western direction. Traffic on the remaining sections of the Kiev-Polish border and on Kiev-Odessa roads was 20-30% below projections.
5.DCT Gdansk Poland	8% **above** projections (m TEUs)	DCT (port operator) data. Direct shipments from Asia (twice weekly on ultra-large ships) have been growing at 20% p.a. since the terminal opened in 2017. Transhipments to Baltic ports grew (except to Russia where sanctions limit trade)
6.Asya Port Turkey	21% **below** projections (m TEUs)	Asya port operator's data. Direct shipments from Asia (once a week on ultra-large ships) increased but no exact data is available. All throughput was related to transhipments to the Black sea ports.

[4] Although transportation cost and time savings could be better indicators for assessing regional integrating impact, only two clients (see text) were able to provide some data on journey time or cost savings. All clients estimated that the new roads or facilities (including bridges, interconnections, etc.) resulted in substantial transportation time savings, which translate into cost savings for consignors.

7.Dalaman Airport Turkey	**In line** with projections (number of passages)	YDA's (airport operator) data. Traffic lower in earlier years due to political instability but recovered in 2018. 2019 traffic boosted by "Brexit effect" but later impacted by Thomas Cook's bankruptcy. Post-project connectivity grew by 26% (19 more direct connections)
8.Southern Gas Corridor Azerbaijan	**In line** with projections (bcm/y)	TANAP's (pipeline operator) data. The impact of the evaluated project was limited to the closer integration of Turkey's and Azeri energy systems. However, the project's "enabling effect" in respect of regional integration was strong as the next section of the pipeline (TAP) will join Azerbaijan with the EU's gas transmission network.
9.Port of Split Croatia	28% **below** forecast (number of cruise ships' passages)	PSA's (port authority) data. Traffic for domestic ferries was 8% above forecast but for international ferries 62% below projections. The number of cruise ships calling at Split modestly increased, although the number of their passengers was well below the projections.

The main reasons for the relatively low utilisation of road corridors were as follows:

- **Unfinished status** – bottlenecks and bad surfaces still existed on swathes of these corridors and, until they are fully completed, consignors seem to avoid them if possible;
- Obstacles related to **border crossings** – time loss due to long waiting times, particularly when countries are outside the EU. Alternative routes were favoured where possible;
- **Lack of inter-connections** or unattractive/unfinished final destination point - e.g. absence of connection to other main highways or sea ports with limited container terminal capacity;
- Existence of **better alternative route**s - completed, within one economic area and with good connections to other routes/ports/hubs.

Two clients provided some data on time or cost savings due to the Bank-financed investments, i.e. based on data provided by the Highway Agency of BiH, journey time from Tarcin to Zenica (87 km) was reduced from two hours to 42 minutes on average. The operator of the DCT terminal in Gdansk estimates that an Asian consignor saves half of the costs (although it takes twice as much time) sending a container to Europe by sea on a ULCS, rather than by rail[5].

There has been a clear difference between the impact of the Bank-financed roads on local level connectivity and international/regional connectivity. Evaluation found that their utilisation close to local hubs has usually been good, in line with or above the projections (Kiev approaches, Sarajevo bypass, Osijek). However, the further from a metropolis, the lower the traffic was and the larger the gaps between forecast and actual traffic. This may indicate that the Bank's (and its consultants') expectations of increased trade and mobility have been generally over-optimistic, as they were usually simply linked to projected GDP growth rates (which themselves have been often over-optimistic), rather than based on dedicated connectivity diagnostics.

[5] It was reported that the first long container train from China (Xian) to Slawkow Logistics Park, Poland arrived on 6 January 2020 after 12 days of journey. It takes a container ship about a month to travel from Shanghai to Gdansk.

Another important reason for the weaker integrating impact of selected cluster projects was their vulnerability to political risk, which often materialised, hampering the infrastructure's connecting impact. For example, the political and ethnic fragmentation of BiH resulted in a lack of shared vision and priorities, seriously impeding the implementation of the Corridor Vc project. Large parts of this corridor remain unbuilt as each of the ethnic groups (Bosniaks, Serbs, Croats) lobbies to align it to connect their own communities and in accordance with their own preferences. In the case of sea ports and airports, they fared better but also fell victim to political upheavals. Dalaman airport in particular, felt the impact of Turkey's political instability during 2015-2016, while. Role of Asya port as a trans-shipment hub in the Black sea diminished during the conflict in Ukraine (the latter also contributed to lower than expected traffic on the Odessa – Kiev highway). Finally, transhipments to Russia from the DCT container terminal in Gdansk were adversely affected when international sanctions on trade with Russia were introduced.

The future potential of regional integration impact of three highway projects and the TANAP pipeline was rated higher than the current impact because their completion and interconnections to larger networks are expected to increase their integrating impact, while there is evidence that their expansion or project continuation will very likely take place. However, large investments will be needed to achieve it, e.g. €3.8 billion and 10-15 years will be required to complete corridor Vc. The Bank is likely to continue providing part of the financing needed to complete this corridor as, during the last AGM, it signed a MoU with the government of FBiH, confirming its intention to support the project with indicative €700 million loans. However, for this corridor to play a truly international role, connecting Central Europe with the Adriatic, the Ionian-Adriatic highway needs to be built, as well as the port of Ploce's container terminal. Sources of financing for these investments are more questionable, although they remain a high priority for the Croatian government. In case of TANAP, the completion of TAP (on schedule for 2020) will substantially strengthen its integrating role, connecting Azerbaijan to the EU's gas network. However, to expand its integrating impact, particularly into Central Europe, an extension of TANAP's capacity will be needed. Its cost is estimated at about US$ 1 billion.

4.2.2 Soft integration – results

The cluster projects had relatively low level of ambition in relation to policy dialogue objectives supporting regional integration and most projects did not have them. However, selected projects did target policies designed to support integration. Their outcomes have been assessed taking into account the latest EU Commission reports on each country, which provide a snapshot of recent policy-related achievements and stil existing gaps in terms of a degree of a country's integration with the EU:

- **Bosnia and Herzegovina** – no specific soft integrating measures were envisaged under the Corridor Vc project. The EU Commission's 2018 Staff Working Document on BiH notes that: *"limited progress has been achieved by BiH in addressing non-tariff barriers to trade with the EU, such as required sanitary standards, overall compliance with these requirements remains a problem".*
- **Croatia** – the Corridor Vc Completion project included an objective to support the development and signing of the Customs and Immigration Protocol with BiH, designed to simplify border crossing procedures. The Protocol was prepared, however it has not been signed, mainly due to the accession of Croatia to the EU, which limited its ability to enter into bilateral agreements with third parties on border crossing. Croatia is expected to join the Schengen Area in 2020.

- **Ukraine** – The EU's 2019 Joint Staff Working Document on Ukraine reports that *"The Government adopted a new National Transport Strategy in May 2018 with the aim of improving the functioning of the transport sector and enhancing connectivity with the EU through the extended indicative Trans-European Transport Network (TEN-T); The State Road Fund started operations in 2018 and includes a road safety component. Key draft laws on market opening, including on road, railway and inland waterways, which shall be instrumental in harmonising Ukrainian transport legislation with that of the EU, have not yet been adopted".* Under the Pan-European Roads project, the Bank contributed to the approval of the fuel tax and the establishment of the Road Fund.
- **Azerbaijan** – the EU's 2019 Joint Staff Working Document for Azerbaijan stresses the importance of the Southern Gas Corridor project, stating that the EBRD provided financing for its sections. It also states that *"an independent energy regulator has been set up by the Azerbaijan authorities with the help of the EBRD".* However, in relation to road connectivity in noted that *"Azerbaijan does not have an integrated border management (IBM) strategy and action plan, but it takes part in the EaP-IBM capacity-building project led by the European Border and Coast Guard Agency".*
- **Turkey** – the EU Commission's 2018 Staff Working Document for Turkey states that *"significant progress has been made on gas networks, particularly on the Trans-Anatolian pipeline (TANAP). The project is expected to start delivering gas to EU market by 2020. There has been limited progress on the interconnection between Turkey and Bulgaria. However, no progress was made on setting up a transparent, cost-reflective and non-discriminatory gas transit system". "Turkey is well advanced in the area of Trans-European networks and free movement of goods. The country is moderately prepared in the area of transport policy, where further efforts are needed".*
- **Poland** – The EU Commission's 2019 Staff Working Document on Poland does not mention sea port infrastructure, however it touches upon the railway sector (important for the DCT project), i.e. *"Poland has been making progress in building its road infrastructure, however, planning and completing railway infrastructure projects have proved more difficult. The government presented plans to amend the railway network to facilitate the connectivity of the planned new airport west of Warsaw. However rail freight transport remains uncompetitive in relation to the road sector.*

The above summary presents a mixed picture. The Bank registered some successes with policy-related integrating measures, notably with the creation of the State Road Fund in Ukraine and the establishment of the energy regulator (AERA) in Azerbaijan. In both cases interviewees stressed concerted effort of a group of IFIs, which contributed to the success of these reforms (see section 5.1 for more info). The regulatory law in Azerbaijan is still not approved but the Presidential Decree issued recently ensures its approval by mid-2020. However, there were several disappointments, e.g. the failure of the Custom and Immigration Protocol between Croatia and BiH. However, in EvD's view the key deficiency in respect of soft integrating measures in cross-border projects has been their scarcity, i.e. such soft measures have been rarely included as part of said projects. This might be because "Integrated" was not one of the Bank's transition qualities at the time most of the cluster projects were approved. This should change now with "Integrated" as their transition quality.

To summarise, the regional integration impact of cross-border infrastructure projects (such as international corridors), might not be observable for many years, even decades, as they are only gradually put into operation and their impact can be conclusively measured only after their full completion. The current traffic or throughput of the three quarters of the projects evaluated are

below projected levels (in most cases substantially). Lack of data on cost and time savings limited the assessment. Although it is plausible that all of the infrastructure facilities financed by the Bank contributed to some extent to reducing transportation time and cost, this impact has been off-set by their relatively low utilisation so far. The integrating impact of transportation hubs (sea ports and airports) has been generally more profound, than that of the roads (and easier to measure). All projects have been exposed to political risks, which often materialised, adversely impacting their connectivity potential. Policy-related integrating measures have rarely been included in the Bank's cross-border projects and when they were, the record of their achievement has been mixed. The future prospects for the cluster projects achieving a stronger integrating impact after the transport corridors and pipeline interconnections are fully complete are generally good. However, it will take a long time and huge investments will be required to fully realise their potential.

4.3. Country level assessment

- Among the cluster projects, those in BiH and, to some extent Poland, could be regarded as those which contributed to the improved ranking of these countries in the Logistics Performance Index (LPI). However, there are no discernible links between changes in rankings of other countries to other relevant cluster projects;
- During the last 10 years overall connectivity scores have improved for most cluster projects' countries under the "Doing Business" index, most for Croatia and Azerbaijan and least for Turkey. The EU countries and BiH achieved relatively high rankings in this index's "Trading Across Borders" category.
- There is still room for improvement in the remaining countries where policies, procedures and inadequate border crossing organisation hamper trade and movement.

To identify the regional integration impact of the cluster projects on the six cluster countries, EvD reviewed changes in the relevant indicators in the World Bank's LPI and Doing Business – "Trading Across Borders" category, comparing their scores and rankings before and after the projects. In addition, changes in the EBRD's transition scores for "Integrated" (published in 2017 and 2019 Transition Reports) were examined. However, as the EBRD only started rating "Integrated" in 2017, it illustrates just the very recent and short-term changes. Table 4 summarises findings from these analyses.

Table 4. Rankings of six cluster project countries by international indexes

Country	LPI[1] 2007 score and ranking	LPI 2018 score and ranking	**Change in LPI score and ranking**	DB[2] 2008 Trading Across Borders ranking	DB 2020 Trading Across Borders ranking	**Change in DB "Trading Across Borders" ranking**	EBRD's Integrated score 2017	EBRD's Integrated score 2019	**Change in EBRD's Integrated score**
Azerbaijan	2.29/111	2.45/125[3]	**+0.16/-14**	173	83	**+90**	5.9	5.6	**-0.3**
BiH	2.46/88	2.81/72	**+0.35/+16**	53	27	**+26**	5.3	5.0	**-0.3**
Croatia	2.71/63	3.10/49	**+0.39/+14**	96	1	**+95**	6.9	6.5	**-0.4**
Poland	3.04/40	3.54/28	**+0.50/+12**	40	1	**+39**	6.8	6.8	**0**
Turkey	3.15/34	3.15/47	**0/-13**	56	44	**+12**	5.9	5.7	**-0.2**
Ukraine	2.55/73	2.83/66	**+0.28/+7**	120	74	**+46**	4.9	5.0	**+0.1**

[1]LPI – World Bank's Logistics Performance Index. Score to 5.0 max and rank among 150 countries
[2]DB – World Bank's "Doing Business" annual report. Rank among 190 countries
[3]Score and ranking from 2014 LPI. Azerbaijan did not provide data for any subsequent LPI publications

The changes under the LPI, compiled by the World Bank since 2007, are the most representative for determining changes in the quality of cross-border infrastructure, policies and procedures of specific countries. It includes "quality of infrastructure" as one of its six indicators. Box 4 summarises how this index is compiled.

Box 4. Logistics Performance Index

The logistics performance index (LPI) is the weighted average of the country scores on the six key dimensions:

1) Efficiency of the **clearance process,** i.e., speed, simplicity and predictability of formalities, by border control agencies, including customs;

2) Quality of trade and transport related **infrastructure,** e.g., ports, railroads, roads, information technology;

3) Ease of arranging **competitively priced shipments**;

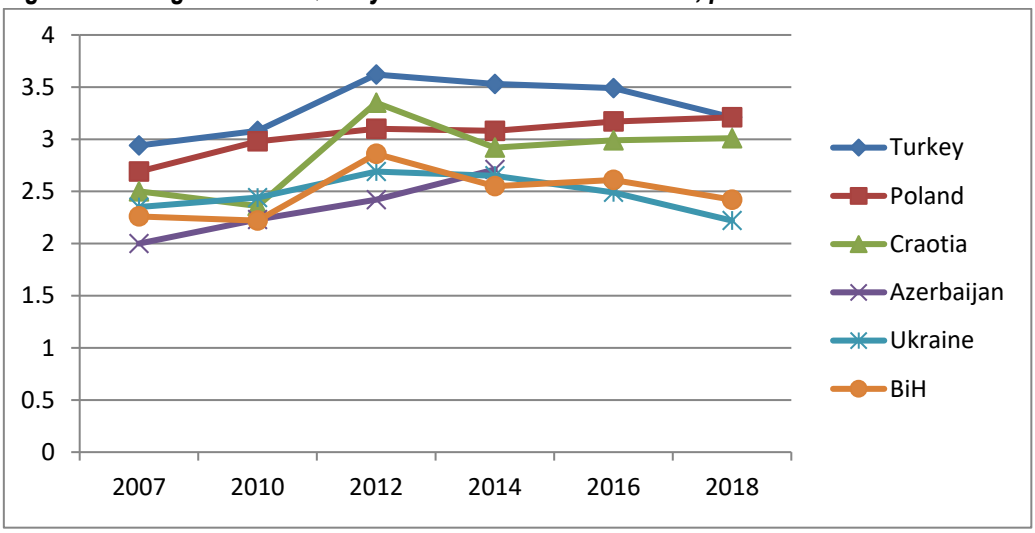
4) Competence and quality of **logistics services** (e.g., transport operators, customs brokers);

5) **Ability to track** and trace consignments;

6) **Timeliness of shipments** in reaching destination within the scheduled time.

Changes in the LPI scores and ranking for six countries (table 4) demonstrate that over the last ten years (when most of the cluster projects were implemented) five countries made advances in their logistics performance, while the score of one country (Turkey) remained unchanged.

Figure 8. Changes in the "Quality of Infrastructure" indicator, part of LPI



Nevertheless, as other countries increased their logistical efficiency, the ranking of two countries - Azerbaijan and Turkey - deteriorated by 14 and 13 places respectively. Poland made the largest advance by score (0.5), while BiH had the largest increase in ranking (16 places).

More granular analysis of this index shows that the "quality of infrastructure" indicator changed differently for each country over the years as illustrated in figure 8. It demonstrates that during the last 12 years, Turkey had the best quality cross-border infrastructure among the six sample countries, but it has been deteriorating since 2012. In contrast, Poland has been slowly improving its infrastructure and is now rated on a par with Turkey. The quality of infrastructure in Croatia made a large jump (42%) between 2010 and 2012 (when it was rated on a par with Ireland) but it quickly (and inexplicably) deteriorated (13%) and in 2014 it was rated on a par with Indonesia and below Poland. BiH's infrastructure underwent a similar but less dramatic increase and subsequent decline, but has, however, been declining in recent years. Ukraine's infrastructure also improved until 2012 but has been slowly declining since, although this can be explained by the conflict in the east of the country, which started in 2014. Ukraine was the only country out of the six in which

quality of infrastructure in 2018 was rated below the 2007 level. Finally, the quality of Azerbaijan's cross-border infrastructure has steadily improved, surpassing that of BiH and Ukraine in 2014, and approaching the score of Croatia. However, thereafter Azerbaijan has stopped providing data for LPIs.

It would be difficult to attribute any changes in the countries' LPI scores to any specific EBRD-financed infrastructure projects. However, EvD notes that the first section of corridor Vc under the 2008 loan was completed by 2012 and the remaining two were close to completion, which might have contributed to the large increase in BiH's score in 2012 (no other major infrastructure investments were implemented in BiH over that period). It is also plausible that the Bank-financed DCT project for the port of Gdansk contributed to Poland's improved infrastructure quality score in 2018 (the extended terminal was put into operation in 2017), although the implementation of the government-sponsored highway building programme probably had a decisive impact on the improved ranking. Due to delays and changes to the project, it is less plausible to attribute Azerbaijan's improved infrastructure quality score to the Bank's road improvement project there and unfortunately there is no data to analyse the changes to this indicator in later years. The Bank-financed sections of corridor Vc in Croatia were completed in 2014 (when its infrastructure quality score sharply deteriorated) and one section has not yet opened to traffic. Despite the Bank's investments in Asya port (2013) and Dalaman airport (2014), Turkey's cross-border infrastructure quality score has gradually declined since 2012. This might be due to small size of the cluster projects there, relative to the size of the Turkish economy and the state of other transport infrastructure assets there. Similarly, the completion of highway approaches to Kiev in recent years had no impact on the overall perception of the quality of infrastructure in Ukraine as its score has steadily declined since peaking in 2012, and now it stands below the 2007 level.

The 2018 LPI report states that "*Regression results show that a 1 point improvement in a country's LPI score increases trade by 16 percent, before accounting for relative price effects"* – which illustrates the importance of improvements to cross-border infrastructure. Moreover, respondents to LPI's questions consistently rated rail infrastructure the weakest of all types of infrastructure across all countries (ICT infrastructure and airports were consistently rated as being relatively of the highest quality in all countries). This confirms EvD's earlier findings, that railway infrastructure is both key for long-distance shipping, and also in need of major improvements in almost all COOs. Finally, it is noted that the COOs which achieved the lowest ratings for their cross-border infrastructure quality under the 2018 LPI were Moldova (2.02), Mongolia (2.10) and Tajikistan (2.17). Other Central Asia and SEMED countries also had relatively low ratings. The Bank should pay particular attention to addressing cross-border infrastructure deficiencies in these countries.

The World Bank's Doing Business analyses and rates countries in 10 categories, one being "Trading Across Borders", which mainly assesses policies, procedures and organisation related to trade across borders. Indicators for this category are as follows:

- Time to export and import - documentary compliance and border compliance (both measured in hours)
- Cost to export and import – documentary compliance and border compliance (both measured in USD)

2008 Doing Business noted that Eastern Europe and Central Asia region had the third longest time to export after Africa and South Asia. Four COOs appeared among the 10 countries where moving goods across borders was the most difficult (Azerbaijan, Tajikistan, Kyrgyz Republic and

Kazakhstan). However there were also some improvements that reporting year, including in BiH where customs sped up sharply thanks to the introduction of a new online clearing system.

2020 Doing Business presented a markedly better picture in respect of most of the Bank's COOs. Among the six cluster countries Croatia and Azerbaijan made the largest advances, leapfrogging 90-95 places in the ranking, Croatia to no 1 (one of 16 with this ranking, including Poland). BiH also improved its ranking to a respectable 27. However, analysis of specific issues (see table 5) shows sharp differences between the six countries and lots of room for improvement in non-EU countries.

Table 5. Doing Business 2020 – Indicators for "Trading Across Borders" category

Country	Time to export-border compliance (hours)	Cost to export - border compliance (USD)	Time to export-document compliance (hours)	Cost to export - document compliance (USD)	Time to import-border compliance (hours)	Cost to import - border compliance (USD)	Time to import-document compliance (hours)	Cost to import - document compliance (USD)
Azerbaijan	17	214	33	250	14	300	33	200
BIH	5	70	4	22	6	109	8	27
Croatia	0	0	1	0	0	0	1	0
Poland	0	0	1	0	0	0	1	0
Turkey	10	338	4	55	7	46	2	55
Ukraine	6	75	66	192	32	100	48	162

This table demonstrates that procedural and organisational obstacles to cross-border trade still exist among selected countries. The longest average time spent by importers is on the Ukrainian border (32 hours), while the most expensive border to cross is in Turkey (US$ 338). Ukraine also takes the longest time to clear all export documents (66 hours or almost three days), while it take one hour in the EU countries.

The table shows that the EU countries in the sample (Poland and Croatia) were able to fully liberalise and streamline their cross-border administrative procedures. Another success story is BiH – ranked 27, however all #1 rankings are taken by 16 EU countries, and most of the following positions are taken by the remaining EU states. Among the Bank's COOs, Serbia (23), Belarus (24) and Albania (25) demonstrate that it is also possible to improve cross-border management in the non-EU countries. BiH is ranked just behind Switzerland (26) and ahead of EU's Latvia (28), Hong Kong (29) and UK (33).

There is no evidence of EBRD projects contributing to the policy-related border crossing improvements in any of the six sample countries. However, there is certainly a role for the Bank to play supporting policy-related reforms facilitating trade across borders in selected COOs. Such measures should be routinely included in future infrastructure projects which target "Integrated" as their transition quality.

The EBRD's "Integrated" quality score (published in the Transition Reports since 2017) deteriorated between 2017 and 2019 for four sample countries, while it marginally improved for Ukraine and was constant for Poland. The completion of the Kiev approaches in 2018 and 2019 could have contributed to Ukraine achieving a relatively better result, although the EBRD's assessment contradicts the "quality of infrastructure" indicator for Ukraine under LPI, which deteriorated during that period.

In conclusion, it can be asserted that among the cluster projects, those in BiH and to some extent in Poland, contributed to improving the infrastructure quality rankings of these countries under the LPI. However, there was no discernible impact from infrastructure projects in other sample

countries, some of which saw their ranking deteriorate. However, over the last 10 years LPI scores improved for five sample countries and remained constant for Turkey. The "Trading Across Borders" rankings under the Doing Business index improved over the last 10 years for all six sample countries, most for Croatia and Azerbaijan and least for Turkey. The EU countries, as well as BiH, achieved relatively high rankings in this category. Nevertheless, there is still ample room for improvement in the remaining countries, where policies, procedures and inadequate border crossing organisation continue to hamper trade and cross-border movement. It is recommended that the Bank targets infrastructure and policy deficiencies in the COOs rated the lowest in the LPI and the "Trading Across Borders" indexes.

5. Regional integration and other IFIs

- Two-third of projects reviewed (6) were co-financed with other IFIs. The Bank provided on average 52% of IFIs financing. It led financing in half of the projects, while it followed the lead of the World Bank or the IFC in another half;
- Clients have been generally satisfied with IFI cooperation and coordination, however some pointed to different procurement and reporting requirements from different IFIs as the main deficiency of multi-IFI financing;
- Other IFIs particularly appreciated EBRD's coordinating role in environmental and social performance monitoring of the complex TANAP project;
- Unlike EBRD, most IFIs had Board-approved strategies or policy statements in respect of their approach to Regional Integration (EIB was an exception, and the World Bank only had a strategy for Africa.).

5.1. Cooperation with other IFIs on cluster projects

Sixty-six percent of the cluster projects were co-financed with IFIs - three with EIB and three with the World Bank/IFC/MIGA. In addition, ADB and AIIB also participated in financing selected projects (see annex 10 for full details). This rate was almost three times higher than the average 22% IFI co-financing rate for the Bank's transport projects[6], indicating that projects with cross-border components were typically challenging in technical, financial and often political terms, and therefore required the involvement of several IFIs. The Bank's share of IFIs' total financing varied from project to project, ranging from 22% for TANAP to 88% for GGG highway section under the Azeri Roads project. However, on average for the 6 IFI co-financed cluster projects, the Bank provided 52% of IFIs financing. It led financing in half of the projects, while it followed the lead of the World Bank or the IFC in another half.

One of the best examples of concerted IFI coordination and cooperation came in relation to a more recent project, related to the core cluster Corridor Vc project in BiH. The key covenant of the Bank's loan under this project called for an increase of the fuel levy to finance motorways from the equivalent of €0.05 to not less than €0.075. This required the passing of a law, which was politically contentious and it is doubtful whether a covenant in the EBRD loan alone would have ensured the approval of the increase. However, it was also a condition of the co-facilities from EIB and the European Commission, as well as the IMF's stabilisation loan. The law, although delayed, was eventually passed in December 2017, which not only unlocked €220 million of already committed EBRD funds for corridor Vc, but also €880 million from various partners. This co-ordination of

[6] EvD Transport Sector Strategy Review (SS17-106)

conditionalities and objectives enabled these partner institutions to bring to bear their combined influence (and financing of over €1 billion) to bring about tangible change in the sector and country.

The other clients had a generally positive view of IFI cooperation and coordination, particularly under the TANAP project. They praised the coordinating role of the World Bank, which made an important contribution to resolving practical or political issues. Moreover, there is evidence that the IFIs cooperated during the preparation of the regulatory legislation, supporting provisions related to the regulator's independence, which were politically sensitive.

There have been also practical benefits for IFIs from joint participation in this mega-project. The EBRD (being a late-comer to this project) effectively leveraged the work of the World Bank, e.g. in terms of due diligence, which enabled it to process the approval relatively quickly. On the other hand, AIIB commented that their team, as well as other IFIs highly appreciated EBRD consultant's coordination of environmental and social performance monitoring of this complex project. The client also stressed that IFIs coordinated their contacts with them, e.g. combining visits and meetings, thus minimising the clients' workload.

Benefiting from common IFI monitoring of environmental and social performance was possible because harmonisation of E&S policies among IFIs has been a long-standing priority since at least the 2005 Paris Declaration on Aid Effectiveness; this has largely been achieved and is now regularly monitored during the E&S policy update cycle of each IFI. For example, the EBRD has benchmarked IFIs' E&S policies, followed by the revision of its own in 2014 to be consistent with those of IFC and EIB. One potential area that was highlighted as requiring possible harmonisation in the future is mobility for the disabled to become enshrined into formal policies – provided that the emphasis on road safety in the multilateral agenda translates into specific points of interest related to that.

On the other hand, some interviewees expressed the view that the IFIs have not harmonised their procurement rules. Each IFI generally continues with its own particular set of rules and, even in co-financed transport projects, each IFI tends to apply its own rules to the particular part of the project it is financing – e.g. a section of a road project. Even where there has been tangible progress (such as standard tender documents for all IFIs) exceptions persist, for instance with the EIB - which is also the most frequent co-financier of the EBRD's transport projects. To mitigate this, in 2015 the EBRD's Procurement Policy and Advisory Department drafted a Memorandum of Understanding (MoU) of 'mutual reliance' with the EIB. The MoU broadly set out an approach where one of the two organisations is chosen as the leader of a co-financed project, to manage the whole procurement process. However, this arrangement was not yet in place when most of the cluster projects were implemented. One of the clients noted that it was a challenge to find contractors, while complying with EBRD's, EU's and national procurement regulations. They found some of the requirements excessive and difficult for an understaffed team to handle. Two other clients, generally satisfied with IFI coordination, pointed to differing reporting requirements, which needed additional effort from the implementation units. EvD also notes the EBRD participated in the Working Group on Sustainable Transport until at least 2015 but has not been able to confirm any other work in this regard since. On the Multilateral Development Bank Road Safety Initiative, the World Bank's Global Road Safety Facility has agreed to fund the EBRD to conduct an analysis and create a toolkit to be shared among the MDBs on occupational safety practices for vehicle fleets.

5.2. Approach to regional integration by other IFI

The World Bank's Independent Evaluation Group (IEG) analysed the IFIs approach to regional integration. It reported that EBRD is one of few IFIs in which regional integration plays relatively marginal role in terms of corporate-level targeting.

Table 6. Benchmarking of IFIs' alignment and execution on Regional Integration

RI Specifics	ADB	IDB	WB	AfDB	EBRD	AIIB	IsDB
RI as a Corporate Strategy and/or Key Pillar (Explicit references)	Yes	Yes	For Africa only	Yes	No	Yes	Yes
Sub-regional Programmatic Approach (e.g. CAREC, SASEC)	Yes	Yes	No	Yes	No	No	No
Leadership on RI Issues in Development Coordination Council (e.g. Active Donor Management)	Yes	Yes	Yes	Yes	Yes	No	No
Leadership in Developing RI Frameworks	Yes	Yes	No	Yes	No	No	No
Business Model Alignment for RI (Distinct Department/Country Director accountability)	Yes	No	No	Yes	No	No	No

Source: IEG analysis, presented with IEG's permission.

The only "Yes" related to EBRD in this table refers to the Investment Councils, which EBRD has been supporting in six ETC countries (including Kirgizstan and Tajikistan, which IEG visited as part of their review). However, EvD notes that these Investment Councils have predominantly country, rather than regional focus.

The IEG's review also found that the ADB and the AfDB did good work in this area given their regional mandates. Both have been more aggressive in business development for regional connectivity than the World Bank, but the outcomes of their activities have been less clear. Annex 11 summarises key findings and recommendations from the World Bank's review, while the section below briefly describes the approach to Regional Integration of selected IFIs.

African Development Bank (AfDB)

AfDB is guided by a **Regional Integration Policy and Strategy** prepared in 2014 and covering the period to 2023. It also has a specialised department in charge of regional integration set up in 2006 under AfDB's 2000 Economic Cooperation and Regional Integration Policy. This strategy is the outline for the AfDB's long-term support to Africa's economic integration. It builds on its experiences and those of other development partners in executing regional integration initiatives. This strategy intended to help operationalize AfDB's Ten Year Strategy and guide its support to regional member countries and regional bodies for economic integration. Its intention was also to provide guidance for formulating the regional integration strategy papers. The strategy's timeline followed that of the Ten Year Strategy to build synergies with other Bank sector strategies. The main points of the Regional Integration Policy and Strategy include:

- Key objective, to promote inclusive and green growth, through addressing constraints to intra-African trade and investment, increasing the continent's participation in regional and global value chains, supporting value addition and job creation, and using technology to develop cleaner infrastructure;

- Strategic pillars (operational priorities) are as follows: Pillar I - supporting regional infrastructure development (hard and soft regional infrastructure development; regional public goods). Pillar II - enhancing industrialisation and trade (industrialisation, export diversification and market development; trade policy and trade facilitation; trade finance capacity). Cross-cutting pillar - Strengthening regional and country mechanisms and institutional capacities (support to countries; human and institutional capacity building).
- Implementation will be through more detailed Regional Integration Strategy Papers and Country Strategy Papers. The AfDB's support for regional infrastructure development will be guided by continental and regional priorities, and will focus on design, implementation and maintenance activities.
- The AfDB will promote public-private partnerships in infrastructure development (planning, design, preparation and construction), operations, management and monitoring.

Asian Development Bank (ADB)

ADB launched a Regional Cooperation Policy already in 1994, which over the years culminated in a formal, Board-approved **Regional Cooperation and Integration Strategy** (RCIS) in 2006. A strong strategic priority on regional integration has remained at ADB since. Regional integration is also one of three complementary strategic agendas under ADB's overarching Strategy 2020. Moreover, regional cooperation and integration is one of the five core operational areas in Strategy 2020. ADB's Charter delineates the strategic importance of regional cooperation in its operations.

The main intention of the RCIS was to guide ADB support for the ongoing process of regional cooperation and integration in Asia and the Pacific in a coherent manner and to facilitate new forms of regional cooperation and integration initiatives. The strategy was to support poverty reduction through regional collective action, leading to greater physical connectivity; trade and investment expansion; financial market development and regional macroeconomic and financial stability; and improved environmental, health, and social conditions. It has the following key messages:

- Limitations to ADB's earlier support for regional cooperation and integration approach included fragmented efforts across departments and offices, uneven quality of lending and non-lending services due to the absence of a coherent strategy, and limited support for trade and investment integration.
- RCIS can support the improvement of cross-border connectivity, augment regional trade and investment, mobilise regional savings for regional investment, decrease macroeconomic vulnerability to shocks, encourage cooperation in regional public goods, and improve the overall governance standards across the region.
- RCIS is an additional platform supplementing individual programmes at the country level, to achieve the ADB's overarching objective of poverty reduction.
- RCIS defines strategic pillars to help reduce development member countries' poverty through regional collective action that would result in increased physical connectivity; expansion of trade and investment; development of financial systems and macroeconomic and financial stability; and improved environmental, health, and social conditions. Pillar I: regional and sub-regional economic cooperation programmes on cross-border infrastructure and related software. Pillar II: trade and investment cooperation and integration. Pillar III: monetary and financial cooperation and integration. Pillar IV: cooperation in regional public goods.

As part of the implementation of the RCIS, the ADB leads or actively participates such programmes as CAREC or TRACECA (see annex 12 for more details). The RCIS was evaluated in 2015. Please see a summary of this evaluation in annex 11.

World Bank Group (WBG)

The WBG has the Board-approved **Africa Regional Integration Assistance Strategy** (2008, 2018), which was endorsed by the Board of Executive Directors of the World Bank Group to partner with Sub-Saharan African countries and regional bodies to deepen regional integration. It delineates a direction for developing the next generation of the Group's engagement in regional integration. This strategy has provided direction to the operational teams working in the African region, but it has not been replicated elsewhere.[7] Key points of the Africa Regional Integration and Cooperation Assistance Strategy are presented in box 5 below.

Box 5. Key points of the World Bank's Africa Regional Integration Strategy

An important opportunity to define clear priorities for the future of the regional integration program arose from the scale-up of the regional window under IDA18. The new WBG Regional Integration and Cooperation Assistance Strategy (RICAS) for Africa covering FY18 – FY23 (IDA18 and IDA19 periods) was the response to this.

Objective

The strategy defines the priority areas for WBG engagement on regional integration, while the specific regional integration lending opportunities would be identified in the various country partnership frameworks. The strategy's purpose is threefold:

1. Identify lessons learned and assess the changes in the wider context.
2. Reposition the WBG's regional integration work and delineate strategic priorities
3. Identify improvements in the WBG's engagement model to strengthen the impact of the regional integration work.

Key Emerging Issues

1. Africa needs to restart its growth engine and strengthen the poverty elasticity of growth within a context of global uncertainties and modest prospects for a commodity price boom.
2. There exists opportunities ahead, including the demographic boom, rising urbanization, and the likely prospects of technological improvements.
3. Several fragility and environmental risks that have a cross-border dimension require effective collective action by multiple countries

WBG's Strategic Priorities for the Africa Region

1. Macroeconomic stability.
2. Boost competitiveness and economic diversification
3. Improve human capital and access to basic services
4. Resilience to shocks

Strategic priorities proposed for the WBG's RI program FY18–FY23

1. Generate economic dynamism along regional economic corridors.
2. Develop functioning regional markets in four priority sectors (Energy, ICT, Agriculture, Finance and Completion).
3. Scale up access to quality public services and entrepreneurship through complementary regional solutions.
4. Promote collective action to address risks of regional economic contagion, fragility, epidemic, and climate 'hot spots'.

Selected Expected Results

1. Economic diversification
2. Strengthened regional value chains
3. Built-up sub-regional energy and digital markets
4. More productive jobs for youth created

[7] World Bank. 2019. Two to Tango : *An Evaluation of World Bank Group Support to Fostering Regional Integration (English).* Corporate and process evaluation. Washington, D.C. : World Bank Group.

The WBG's evaluation department (IEG) conducted an evaluation in 2019, *Two to Tango: An Evaluation of World Bank Group Support to Fostering Regional Integration*. Its objectives were to assess the WBG's contributions in enhancing regional integration and to extract lessons to influence its future regional integration activities. See annex 11 for a summary of this evaluation.

European Investment Bank (EIB)

EIB does not have a policy statement or a strategy for regional integration. However, infrastructure is one of its four priorities as it connects citizens, internal markets and economies. The key priorities of EIB's *de facto* Transport Strategy (*Better Infrastructure, Better Economy)* are as follows:

- **Resilient infrastructure**: transport is key to growth and competitiveness. It is the largest sector in which EIB has been active since its foundation. Transport provides physical networks and services for the movement of people and goods.
- **Building a safe, interconnected Europe**: EIB's transport lending policy underscores climate action and safety, resource efficiency and strategic infrastructure that helps cohesion and the single market.
- **Transport projects fall within two main eligibility criteria**: (i) Strategic transport projects, including those on the Trans-European Transport Networks (TEN-T), within the EU and on the extended TEN-T network in neighbouring countries; (ii) Sustainable transport projects targeting urban transport, as well as urban railways, road safety, regional railways, conventional and high-speed railways outside the TEN-T network.
- **Energising the Economy**: A secure and sustainable supply of energy at affordable prices is crucial to the EU's economic growth and competitiveness. EIB supports making the energy supply sustainable for Europe's citizens and businesses through focusing on key energy links, energy efficiency and renewable sources of energy.

6. Findings and recommendations (to be updated in the Final version)

6.1. Findings

Policy and strategy context

- It proved challenging to conclusively assess the regional integration impact of most of the cross-border infrastructure projects as the **Bank does not have a framing strategy** for regional integration or cross-border investments against which to assess its operations, while work on many international corridors is still ongoing and relevant data is scarce;
- Historically, **three quarters** of the Bank's transport projects with cross-border components by volume were in the **road sector**. However, the evaluation of several of them demonstrates that in most cases actual traffic was disappointing. They had stronger local, rather than regional integrating impact;
- Historically, majority of the Bank's transport projects supported roads, while in the opinion of many interviewees **rail** played more prominent role in their countries' cross-border connections. However, the Bank has had relatively few rail projects with regional integration components;

- **Complex customs and immigration procedures**, as well as long waiting times at border crossings were often the principal hurdles to integration, slowing transportation and impacting choice of route by consignors. However only one among the Bank's four highway projects reviewed included components designed to address them through policy dialogue;
- As 70% of the world's trade is carried by sea, some **port container terminal** projects yielded evidence of a strong regional integrating impact;
- Also, as air passenger transportation is the fastest growing mode of cross-border movement of people, **airport projects** have shown solid regional integrating credentials;
- Tourism has gradually grown in the Bank's regions, however expectations of a large **tourist influx** ("catch up effect") to its countries of operation did not materialise;

Project design and performance issues

- Regional integrating impact potential was often cited, but without prior **diagnostics** completed. Performance **metrics** were insufficient and typically were limited to traffic/throughput, which projections were simply linked to a country's forecast GDP;
- There is no evidence of **experience from past** cross-border projects (or lessons from their evaluations) being utilised in the design of new projects;
- Most of the **physical infrastructure** components of cross-border projects were **completed**, albeit typically with substantial delays;
- Some projects had relatively modest **policy dialogue** objectives**,** however even these were often not achieved;
- Almost all **private sector** participation enhancement objectives set in the reviewed projects **failed;**
- The current traffic or throughput of **three quarters** of the evaluated projects has been well below the projected levels;
- The **transportation hubs** projects (sea ports and airports) have been generally able to demonstrate strong integrating impact much faster than those in roads (and easier to measure);
- All evaluated projects were exposed to **political risks**, which often materialised, adversely impacting their connectivity potential;
- The **future prospects** for the evaluated projects achieving a stronger integrating impact after the transport corridors and pipeline interconnections are fully complete are generally good. Nevertheless, it will take a long time and huge investments will be required to fully realise their potential;

Country and sector strategies

- All 15 of the country strategies reviewed **referred to connectivity** as one of the transition challenges. Most of the recent strategies set improving cross-border connectivity as one of the Bank's operational **priorities**;

- Linkages to the "Integrated" transition quality in two thirds of the country strategies reviewed were assessed as **"strong"**;
- Subsequent Transport and Energy sector strategies have given **increasingly more prominence** to cross-border connectivity and offered more relevant performance monitoring frameworks related to it;

IFIs collaboration

- Two-third of projects reviewed (6) were **co-financed with other IFIs**. The Bank provided on average 52% of IFIs financing. It led financing in half of the projects, while it followed the lead of the World Bank or the IFC in another half;
- Clients were generally satisfied with IFI coordination but many sought **uniform procurement and reporting** requirements.

6.2. Recommendations

- Prepare for Board approval a Bank-wide **strategy for Regional Integration;** including cross-border connectivity, to establish agreed objectives, priority sectors/sub-sectors, potential investment types, directions of policy dialogue and TC support areas;
- Target integration-related investments and particularly policy dialogue towards countries with the **largest ATQ gap score** for Integrated quality, i.e. in Central Asia, the Balkans and SEMED, actively pursuing opportunities in integration-boosting sub-sectors, such as rail, ports and airports;
- For projects targeting Integrated, ensure adequate system is in place **for gathering relevant data to measure it,** either by the client or by the Bank;
- Conduct a **focused assessment of why most of the private sector** enhancement and policy- related objectives of large infrastructure projects have **failed**.

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Turkey: Dalaman Airport, BDS14-335

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ANNEX 1: Core Cluster Projects and Related Projects

Table 1. Core cluster projects

OpId	Project Name	Country	Bank's loan €m	Signed, portfolio	Short description
International highways					
38716	**Corridor Vc,**	Bosnia and Herzeg.	205	10.2008, public	The Bank's flagship, multi-phase project, aiming to support integration of BiH with Europe. Construction or upgrading of several sections of the Mediterranean TEN-T corridor linking Budapest through BiH to the port of Ploce in Croatia The Bank provided five follow-up loans to BiH, bringing total EBRD financing so far to €0.8 billion, as well as to Croatian sections (see below). Co-financed with EIB and EU.
41325	**Corridor Vc Completion Project**	Croatia	58.9	Nov.2010, public	Financing of two motorway sections required to (almost) complete the Croatian part of the Corridor Vc (see above), adjacent to the northern and southern borders with Bosnia and Herzegovina. Southern link vital for the corridor's connection to the port of Ploce.
43094	**Azeri Roads Reconstruction and Rehabilitation**	Azerbaijan	750	12.2011, public	Co-financing with eight IFIs and ECAs of Azerbaijan's main highway. Part of the TRACECA corridor and of the Silk Road connecting Baku with the EU. Part of the Government's priority programme to support connectivity and Azerbaijan's integration into the global economy.
40185	**Pan-European Corridors (tranche A only)**	Ukraine	450 (tranche A 250)	Nov 2010 public	Rehabilitation of approaches to Kiev on several Pan-European corridors connecting Ukraine's capital to the EU and the port of Odessa.
Sea ports					
45805	**DCT Gdansk expansion**	Poland	24.6	11.2014, private	Construction of a second deep-water container terminal at the port of Gdansk – the largest port in the southern Baltic and the main transhipment hub, connecting to the Baltic-Adriatic TEN-T corridor. The fastest growing container terminal in Europe, recently sold by Macquarie to the port of Singapore.
4417	**Asya Port**	Turkey	62.6	12.2013, private	Financing of a container terminal – the largest on the Sea of Marmara and primary transhipment port of the Black Sea region. Co-financed with IFC.
42542	**Port of Split Infrastructure Rehabilitation**	Croatia	24.4	12.2012, public	Development of the passenger wharves at the port of Split to allow large cruisers and ferries, linking Croatia to Italy and the main European cruise ports. One of the priorities of Croatia's Pre-accession Strategy and part of Bank's three Croatian ports programme.
Airport					
46467	**Dalaman Airport**	Turkey	81	Dec 2014, private	Construction of a new international terminal and financing of initial concession payment for a hub airport in southern Turkey, linking it with the European, Russian and Middle Eastern destinations.
Gas pipeline					
48376	**Southern Gas Corridor (TANAP)**	Azerbaijan (Turkey)	$500	Oct 2017, public	Part of $40 billion mega-project of strategic importance to the EU's energy security, crossing five countries and bringing for the first time Azeri gas to Europe.

Table 2. Projects related to core cluster projects

Id	Associated Project	Country	EBRD finance €	Date signed	Relation to the evaluation project
CORE: Corridor Vc, - Bosnia and Herzegovina and Croatia sections					
35264	M6 motorway	Hungary	25.3	7.2005	Coridor Vc is a TEN-T linking Budapest through Bosnia to the port of Ploce in Croatia. The Bank first co-financed the Hungarian part of this corridor from Budapest to the Croatia border (with M60 branch to Pecs) as a private concession. It recently provided financing for M6 PPP (2015 projects) In 2008 the core project co-financed the first 66 km of corridor Vc in BiH. Subsequent loans financed selected other sections, including part of the ring road off Sarajevo and a part of corridor Vc crossing Republica Serpska. The core Croatian project financed two sections connecting Hungarian and Bosnian borders and Bosnia and the Port of Ploce at the end of corridor Vc, linking it to the Adriatic. The Bank has also signed financing for the modernisation and extension of the liquid and the bulk cargo terminals at this port (although one was cancelled and another prepaid).
35256	M6 Refinancing		32	3.2006	
38376	M6-M60 Motorway		74.6	5.2008	
47490	M6 Duna		6	6.2015	
47530	M6 Tolna		19	6.2015	
47372	Corridor Vc 2	Bosnia and Herzeg.	80	12.2015	
48999	Corridor Vc Extension		76	12.2016	
49053	Corridor Vc R. Serpska		70	12.2017	
49058	Corridor Vc FBH 3		120	9.2018	
36127	Ploce Port Bulk Terminal	Croatia	11.2	11.2007	
46695	Luka-Ploce Liquid Cargo Terminal		9.6	5.2015	
CORE: Azeri Roads Reconstruction and Rehabilitation, Azerbaijan					
1863	Silk Road	Azerbaijan	35.7	7.2004	M2 highway (financed under the core project) is strategically important route, part of TRACECA road network and the Silk Road, connecting Baku to Georgian border and further to Turkey and EU. The Bank's 2004 loan financed the section from Sumgait to Zarat and the second loan, a northern branch from Baku to Samur (towards the Russian border). The core project (2011) co-financed the main sections – Mingachevir – Bahramtap, as well as Ganja –Gazakh – Georgian Boarder
34723	Baku to Samur		87	12.2005	
CORE: Pan-European corridors, Ukraine					
2213	Rehabilitation of M06	Ukraine	75	12.2000	2000 loan financed M06 highway from the western border through Carpathian mountains to Lviv approach. 2005 loan financed the middle-western section of M06 and 2006 loan financed middle-eastern part through Rivne to Zhitomir section. Tranche A of the core project (2010) finances Kiev-Zhitomir (eastern part) of the approach to Kiev by M06. Tranche B finances five different sections of other highways, all approaches to Kiev from different directions. These projects are under implementation and will not be part of this evaluation.
31928	Kiev-Chop Road Rehab.		100	2.2005	
36547	3rd Project-Kiev-Chop		200	12.2006	

CORE: Port of Split, Croatia					
13451 39749	Port of Dubrovnik Port of Sibernik	Croatia	26.5 10	1.2005 4.2010	The Bank financed modernisation and extension of three main ports in Croatia – Dubrovnik, Sbernik and Split (the latter is the core project). All projects encompassed berth extensions to increase space for cruise ships – key for connecting Croatia to the lucrative cruising market, and in some cases, cargo handling.
CORE: DCT Gdansk, Poland					
50798	Project Felicjan	Poland	46.2	5.2019	The project signed in 2019 co-financed the acquisition of the DCT terminal by a consortium led by the Singapore Port Authority and further extension of the terminal.
CORE: TANAP, Azerbaijan and Turkey					
45599	Lukoil Overseas: Shah Deniz Gas Condensate Field Develop. II	Azerbaijan	178	2.2014	Both loans financed development of Shah Deniz II off-shore gas field located under the seabed of the Caspian Sea near Baku. Both were completed and are repaying.
46766	Lukoil Shah Deniz Stage II	Azerbaijan	222	8.2015	
45690	TAP	Greece	500	11.2018	Construction of the last section of the Southern Gas Corridor section in Greece, Albania and under the Adriatic, linking it with the Italian (EU) gas system in Brindisi.
49149	BRUA Pipeline	Romania	58	2.2018	Construction of the gas transmission corridor between Romania, Hungary and Austria

ANNEX 2: Cluster Projects Evaluations

1. Corridor Vc – a highway project in Bosnia and Herzegovina, OpId 38716

Background

Corridor Vc is a Pan-European corridor, designated as an indicative extension of the Mediterranean TEN-T corridor, connecting central Europe (Budapest) with the southern Adriatic (port of Ploče in Croatia), thus constituting the most direct transport route for central European exporters to global markets. Of its total 550 km, 335 km run through Bosnia and Herzegovina (see section below on Regional Integration Impact for more details on Corridor Vc).

In 2008 the Bank provided a €180 million sovereign loan to the government of the Federation of Bosnia and Herzegovina (FBiH), which was increased by €25 million in 2013, to construct four sections of Corridor Vc. The project was to add 66.5 km of highway standard road to the existing 45 km highway, substantially upgrading the standard of the central section of Corridor Vc. Parallel co-financing of €300 million was provided by EIB. A TC package (€1.08 million in aggregate) was granted for the preparation of a resettlement action plan, project implementation and institutional support for the Ministry of Transport, as well as for the preparation of a PPP tender. Transition impact was to be derived from institutional changes, i.e. the transformation of the Ministry's Highway Directorate into a public company, which would be financed by a new fuel levy (to be introduced as a key TI component) and would subsequently take over the debt service. The project's TI also included the preparation of a corporate plan and the development of the newly established company, as well as the preparation and implementation of a PPP strategy for future Corridor Vc sections, including the launch of the first PPP tender.

Relevance

In accordance with the Dayton Agreement, the State of Bosnia and Herzegovina (BiH) consists of the Federation of BiH (FBiH), autonomous Republica Serbska (RS) and the District of Brcko. Corridor Vc crosses FBiH and RS. The Bank and both BiH governments have worked well together on three previous road sector projects: Post-war Road Reconstruction, Regional Roads Rehabilitation (including the Sarajevo bypass by Vc) and Banja Luka – Gradiska road, connecting Republica Serbska with Corridor X in Croatia. Under these projects, consultants prepared a state-wide Transport Sector Policy and Strategy, which was adopted by the FBiH government. The consultants also prepared the Road User Charges Study, recommending the introduction of a fuel levy and a vehicle registration tax.

Thus the 2008 Corridor Vc project was a natural continuation of the Bank's engagement in BiH road sector development. Corridor Vc was designated as a top priority in the BiH government's Transport Strategy, as 50% of the country's population lives, and 60% of GDP is produced, within 30 km of this corridor. EvD's meetings with FBiH government representatives confirmed that Corridor Vc has been, and remains, the government's top priority infrastructure project. However, due to an increasing debt burden, the government confirmed that its approach to building the corridor will continue to be gradual, i.e. completing relatively short sections every few years.

In EvD's view, the project was closely aligned with the Bank's Country Strategy for Bosnia and Herzegovina (BDS/BH/07-1(F)) applicable at that time, where specific reference was made to the Bank supporting the development of Corridor Vc: *"The most important transport artery in BiH is Trans-European Corridor Vc. The Bank will intensify discussions with all relevant authorities and potential financiers in order to assist in developing the most appropriate financial structure for this crucial project".*

Following several subsequent loans (see section below), Corridor Vc has evolved over the years into the Bank's flagship project in BiH. The Bank's 2017 BiH Country Strategy indicated the "*improved regional integration through EBRD funding of Corridor Vc motorway*" as a key achievement of the previous country strategy. "Regional Integration" with four projects (all related to Vc) accounted for 50% of the Bank's ABI in BiH between 2014 and 2016. The Bank's 2017 BiH strategy presents the promotion of regional integration (through the development of key transport and energy cross-border links) as one of three strategic priorities.

The project was also consistent with the Transport Operations Policy (BDS04-072 (Add 1) (F)), which stressed the importance of the strategic corridors to the development of South East Europe as a whole, and the role that institution building can play in the advancement of the road sector.

In terms of additionality, in 2008 local Bosnian banks were unable to provide loans with the 15-year tenors required to finance highway assets. The EIB has been active in the BiH road sector but it is subject to a 50% maximum financing rule and co-financed the initial sections of Corridor Vc with the FBiH government. Therefore, another IFI was sought to co-finance further Corridor Vc upgrades. The World Bank has been involved in the railway sector in BiH, while the project appealed to the EBRD as it had worked on the BiH road sector previously, and the TI potential of this project was seen as strong. The Bank continued to support Corridor Vc during subsequent years, committing €626,000 under five new projects (see "associated projects" section below).

As this project was very well aligned with both the Bank's and the host government's top priorities, its additionality was not in question and its design included support for important systemic reforms, its relevance is rated ***excellent***[8].

Results

The loan didn't become effective for about a year after signing, due to the delay in introducing a fuel levy (a key covenant, and an integral source of loan repayments). When this finally took place, the loan was fully disbursed in three tranches and three sections of the highway were built, although two years later than originally planned. The main reasons for the late delivery were delayed loan effectiveness, a long procurement process, adverse weather (flooding), difficult terrain, ethnic issues (difficulty in agreeing on the highway's alignment as each community wanted it to pass close by) and the financial crisis (the first two main contractors went out of business and had to be replaced). According to the project team, the main difficulty was the lack of a "political champion" for the project in FBiH, as well as the conflicting priorities of FBiH on one side (strongly supporting Corridor Vc, i.e. north-south connection) and Republica Serbska's government on the other (prioritising a west-east connection between its capital Baja Luka and Belgrade in Serbia).

The project also experienced cost overruns of €25 million (or 14% of the total) on two sections. The reason for this was that parts of the highway had to be built on higher terrain than envisaged in the initial design, as the mayors of many towns refused to agree to the originally-planned lower alignment, which would require terrain they had allocated for residential or other building (the FBiH Parliament has only recently adopted the Corridor Vc alignment law, which will prevent such opposition in the future). Higher terrain meant that special barriers preventing mud slides had to be built and other technical solutions introduced, which substantially increased the cost. Moreover, funds from one section (Odzak-northern border) were reallocated to another section, due to questions related to the construction of a bridge to Croatia (the originally targeted section and the bridge were built in subsequent years). Ultimately, 55.6 km of highway (rather than the 66 km planned) were built under this project.
In terms of transition impact, the Motorways Directorate was duly transformed into a limited company - Autoceste FBiH – its corporate plan prepared and MIS introduced. A €0.05/l fuel levy was also introduced in July 2009 and, importantly, it is directly passed to Autoceste. This became the main revenue source of the new company, which took over the sovereign loan, and is the source of funds for servicing the loan. The Bank's consultants prepared a resettlement plan and played an important role in ensuring the payment of fair compensation for land expropriation. Also, a PPP strategy was prepared and the tender for constructing the Corridor Vc section under PPP was organised. However, there was only one bidder, whose final financial requirements were inflated and unacceptable to the government, therefore the tender was cancelled. Nevertheless, there is evidence that the PPP strategy played some role, as in recent years the BiH government has engaged IFC to prepare another PPP tender for a different (and shorter) Corridor Vc section (Poprikuse-Medakovo). As more traffic data is available now than ten years ago, it is hoped that the current tender will attract more competitive bids.

The project's other benefits range from the substantial reduction of transportation time (e.g. travelling to Zenica from Tarcin takes 42 minutes, compared to two hours before the project) to increased safety (there were two deaths due to accidents on Corridor Vc in 2017, compared to 15 in 2013).

[8] Ratings for each category are based on the following scale of: **Excellent – Fully Satisfactory – Partly Unsatisfactory – Unsatisfactory**. The overall performance rating scale is: **Outstanding – Good – Acceptable –Poor – Very Poor**. In addition, regional integration impact rating scale is: **Strong, Moderate, Weak**.

In summary, 83% of the highway planned under the project was completed, with a 14% cost overrun and taking twice as long as planned. However, a significant milestone in the construction of Corridor Vc was achieved. Importantly, it spearheaded systemic reforms (the creation of Autoceste and the introduction of the fuel levy), which enabled development of the sector and the subsequent projects, bringing the Corridor Vc completion closer. The project's PPP component initially failed, however its introduction might have been attempted prematurely. Recent developments indicate that it may yet yield some results. On this basis, the effectiveness of this project is rated ***fully satisfactory***.

Efficiency

Autoceste FBiH (the Company) reported €103.0 million of revenues in 2018 compared to the €80.1 million initially forecast. The difference is mainly due to the fuel levy increase which was approved in December 2017 and made effective in February 2018. The increase in total revenues was slightly offset for the following two reasons (i) traffic data was lower than initially forecast by consultants and (ii) the opening of new Corridor Vc sections has been delayed during the last 2-3 years as new loans were not secured as quickly as anticipated in 2013.

The EBITDA stood at €88.6 million in 2018 compared to the €68.0 million forecast. This is due to the increase in the fuel levy as described above, but was somewhat offset by higher operating expenditures (actual €14.3 million compared to €10.2 million forecast). Nevertheless, the Company made a €60.1 million net profit in 2018 compared to the €16.5 million forecast. This was mainly due to the above-mentioned reasons, and also because the depreciation charge was lower than initially projected (as new sections were introduced/opened later than anticipated). The Company is performing well and covenants as set out in the loan agreements (the most important being the DSCR) have been met. Opex is covered by tolls, while the fuel levy charges are entirely dedicated to loan servicing. As the original forecast was exceeded by 25-40%, this category is rated **excellent**.

Overall rating

The project's relevance was particularly strong given the priorities of FBiH government and the Bank, as well as the need for co-financing with a long-term loan. The project encountered many difficulties, with long delays and budget over-runs. However it is recognised that the country's political composition (with two competing ethnic governments) posed unique challenges for this project, which were eventually overcome and the project largely completed. Of particular importance for the sector (and also for the Bank's subsequent road projects in BiH) were the reforms introduced under this project – the corporatisation of Autoceste and the introduction of fuel levy, subsequently increased. This ensured that Autoceste was put on sound financial footing. On this basis the project is rated ***good+*** overall.

Status of follow-up associated projects

In terms of the regional integration impact, it is difficult to consider the 2008 project on its own, as it financed only three sections of the corridor, adding 55.6 km of highway-grade road.
Subsequent to the 2008 loan, the Bank signed five more projects to upgrade other Corridor Vc sections in BiH as follows:

- Corridor Vc, part 2 (47372), 2015, €90 million
- Corridor Vc Extension (48999), 2016, €76 million
- Corridor Vc Rep. Serpska (49053), 2018, €70 million
- Corridor Vc in FBH- Part 3 (49058), 2018, €180 million
- Corridor Vc-Doboj Baypass (50603) 2019, €210 million

In total, (including €205 million of the 2008 and 2013 loans), the EBRD has so far committed €831 million to upgrading Corridor Vc in BiH (this is in addition to the €210 million provided for a road connection between Corridor Vc and Banja Luka - 41370, 2012). The five projects listed above are to add 80.4 km of highway grade road to Corridor Vc. They are financing (or will finance) sections comprising exits, level crossings and several tunnels, thus they are even more challenging (and more expensive per km) than the sections completed under 2008 and 2013 loans. Currently, projects 47372 and 48999 (Corridor Vc part 2 and its extension) are disbursing, tendering has been completed and contracts signed and under implementation. They suffered delays in the start-up phase due to the condition to increase the fuel levy to €0.10, which took place only in December 2017. The remaining three projects are not yet effective.

When these projects are implemented, the new sections will increase the attractiveness of Corridor Vc and its traffic, amplifying the corridor's regional integration impact, however it will still only be about half completed.

The new projects do include "Regional Integration" as a primary transition source. However, EvD notes that the claims of regional integration impact to be achieved through these projects were not supported by any diagnostic research, beyond the statement that said impact will be achieved due to the concentration of BiH's population and business activity along this corridor.

Regional Integration impact

Background:

The 550 km long Corridor Vc connects central Europe (Budapest) with the southern Adriatic (Croatian port of Ploče), crossing Hungary, Croatia, Bosnia and Herzegovina, and a further narrow strip of the Croatian coast. The corridor is the top infrastructure priority for BiH and potentially of high importance also for central European connectivity, particularly for land-locked countries such as Hungary, Slovakia and Czech Republic as it is the most direct route from central Europe to the port of Ploče, which could potentially constitute a convenient point of shipment from/to Mediterranean markets, as well as global markets, including Asia (via the Suez canal). It is estimated that shipment through Adriatic ports can cut shipping time by up to seven days, compared to using Baltic or North Sea ports for shipments to the Middle or Far East. Corridor Vc also joins with the Zagreb-Split-Ploče highway (part of the planned Adriatic-Ionian Highway) in the south and with Banja Luka highway (capital of Republica Serbska) in the middle, as well as with the western branch of Corridor X in the north.

The Corridor Vc project forms part of the EU's Connectivity Agenda, which promotes transport connectivity in the Western Balkans as a means of integrating the regions with the EU. Moreover, Corridor Vc is one of the most important and advanced projects under the EU's Western Balkans Transport Community (which evolved from the South-East Europe Transport Observatory – SEETO initiative).

Current status:

Hungary built 180 km of the highway grade Corridor Vc from Budapest to Boly (close to its border with Croatia), partially financed by the EBRD (about €160 million was provided between 2005 and 2015 for the M6 motorway under five projects). There is still a 19 km section north of the Croatian border which, according to Croatian Autoceste, the Hungarians have promised to build at a cost of €157 million by 2023.

In Croatia, the southern part of Corridor Vc (BiH border – port of Ploče) was fully completed (partially financed by the Bank), while the northern part has been partly built, with 66 km completed. Bank financing will be proposed for the last two sections (22.5 km combined) in late 2019 (OpID 50712) - see the review of the Croatian Vc project below for more details.

The longest section of Vc traverses Bosnia and Herzegovina (61% of its total length). Out of 335 km there, 100.5 km have been completed (29%), mainly north and south of Sarajevo and close to both Croatian borders. This compares with 45 km, which were completed (or were under construction) at the time of the 2008 project approval. Under the evaluated project the Bank financed three sections with a combined length of 55.5 km, which more than doubled the length of the highway grade Corridor Vc in BiH (extensions to previously built sections leading north and south of Sarajevo, as well as close to the southern BiH border with Croatia).

Traffic results:

The Board Report stated that on most Corridor Vc sections, traffic was relatively high (ranging between 5,000 to 15,000 AADT). The 2006 Feasibility Study identified three sections, all around Mostar, with the most intense traffic (13,000 – 16,000 AATD), however these sections were not financed by the Bank (, indeed, they have not yet been financed at all). The feasibility study assumed average annual traffic growth of 5.6% between 2008 and 2018. However, according to Autoceste, traffic has only grown 1.8% annually on average between 2008-2015, and has only picked up recently (2016-2018), achieving 9.4% growth.

Nevertheless, this data might not be entirely reliable, as the 2018 SEETO report states that between 2010 and 2016, average traffic on the whole Corridor Vc actually decreased from 8,000 AADT to 7,800. According to this report, Vc was the only one of the six corridors in the Western Balkans on which traffic decreased. It states that in 2016, the average AADT on the region's six corridors and 13 main routes was 8,800. Corridor Vc's traffic results compare particularly badly

with those of Corridor X (Budapest-Thessaloniki), which, in 2016, achieved AADT of about 14,000, as well as with Corridor VIII, with 10,000 AADT.

The table below shows traffic levels on four Corridor Vc sections, comparing projections from the 2006 feasibility study with actual 2018 figures (data provided by Autoceste):

Section of Corridor Vc	Length (km)	2018 projected traffic (AADT)	2018 actual traffic (AADT)	Actual as percentage of projected
Josanica-Podlugovi	9.7	36,993	16,607	45%
Podlugovi-Visoko	7.5	33,341	14,264	43%
Visoko-Kakanj	16.4	29,340	12,312	42%
Kakanj-Lucani	10.2	29,450	11,898	40%

Kakanj-Lucani was one of the sections co-financed by the Bank. A broader review of traffic on other sections and its comparison with projected levels is not possible as there are relatively few sections monitored by Autoceste, and these are not always included among the projections made in the project's feasibility study. However the general picture is fairly clear – the actual (current) traffic levels are less than half of those forecast at the time of project approval.

In 2014 the Bank's consultant revised these traffic projections downwards. They were more realistic, but still proved to be well above the actual traffic levels.

About 15% of the current traffic on Corridor Vc is from cargo trucks (TIRs). Of these, 94% were from BiH, 3% from Croatia and only 3% from other countries. According to Autoceste and FBiH government representatives, the current low utilisation of Corridor Vc by international freight services providers is due to the following:

- The unfinished status of Corridor Vc, i.e. less than one third of its length has been upgraded, while the rest suffers from low quality surface conditions and bottlenecks (often related to the ongoing construction on several sections). As a result, central European exporters/consignors often prefer Corridor Vb, which has been completed and leads to the ports of Rijeka (Croatia) and Koper (Slovenia);
- BiH's status as a non-EU (and non-Schengen Treaty) country, which requires longer and more complex custom procedures (Corridor Vb leads through Croatia, which is in the EU and is expected to become a Schengen country soon);
- The underdevelopment of the port of Ploče, which specialises in bulk and liquid cargo (more suitable for transportation by train than by trucks) and has only a small container terminal, while Rijeka and Koper (in Slovenia in the northern Adriatic) have huge terminals and the fully completed Corridor Vb to connect them with key markets.
- Incomplete connections to other main corridors. Although corridor VC has relatively good connections in the north (to corridors Vb and X) it does not have any in the south. In Autoceste's view, BiH is not yet seen by its neighbours as a transit country and its prospects of becoming one will only improve substantially when the Adriatic-Ionian highway (Trieste-Peloponnese, alongside the Adriatic) is completed. The completion of this highway is strongly pushed by Croatia, which has completed most of its sections, however Montenegro is currently concentrating on the Bar-Belgrade highway and the construction of its 100 km section might not start for several years. There is no indicative date for the completion of the Adriatic-Ionian highway.

EvD agrees with this view. Corridor Vc currently remains a key transportation channel for FBiH companies, both within the country and towards international markets, because it is the only route partly upgraded to highway standards, which leads to the north and further west or east (thanks to Vc's connections with corridors Vb and X) or to the wider world (to the south through the port of Ploče). Eighty percent of trade within FBis data)
As to "soft" measures supporting integration, the project followed EU technical standards (the EU provided a grant to prepare technical specifications for the project). However, not much progress was achieved in harmonising BiH's laws with those of the EU. The EU Commission Staff Working Document, Bosnia and Herzegovina Report of 2018 stated that: *"limited progress has been achieved in addressing non-tariff barriers to trade with the EU, such as required sanitary standards, overall compliance with these requirements remains a problem".*

In summary, the project constituted an important step, spearheading the upgrade of Corridor Vc, with a view to creating a backbone for FBiH's transport system. It more than doubled the length of the highway grade road, however this upgraded section still represents less than one-third of the whole length of the corridor in BiH. The implementation of new Bank co-financed projects to upgrade further Corridor Vc sections has been delayed, and when completed will bring the highway grade road to almost half of its total length. However, it is estimated that upgrading the whole length of this corridor will not be complete until 2026/27 under the most optimistic scenario and, more realistically, by around 2030. Based on the experience to date, this may indicate that Corridor Vc won't become wholly highway grade for at least 10 years. Moreover, there are other important conditions (see section below), which need to be fulfilled for this corridor to play a truly international role connecting Central Europe with the Adriatic.

Due to the relatively low utilisation of Corridor Vc as compared to the original traffic projections and by international freight companies, its current impact on regional integration is rated as ***weak***.

Future prospects:

The piecemeal approach (gradual completion of relatively short sections over years) results from IFI recommendations, which stemmed from the limited debt capacity of the BiH government and its limited capacity to manage large projects, as well as the government's half-hearted approach to the PPPs. But it is, indeed, the only realistic approach, although it will prevent Corridor Vc from realising its full regional integration potential until it is completed.
It is now estimated that an additional €3.8 billion is required to finish Corridor Vc in BiH. Due to a healthy cash flow following the increased fuel levy (see section on efficiency above), Autoceste's debt service capacity increased and it envisages increased borrowing – about €900 million – over the next five years. EIB is expected to provide about €1.5 billion. On 26 February 2018, the EBRD signed an MoU with the FBiH government for the provision of €700 million over the next three years for the construction of new Corridor Vc sections, including a possible PPP. Recently, a consortium of local banks proposed a €240 million, 14 year loan to Autoceste, but only if co-financed by about €60 million of EBRD funds. Other agencies, such as the Kuwait Fund for Arab Economic Development and OFID (OPEC Fund for International Development), as well as the EU and the FBiH government, are expected to finance the balance.

Moreover, the development of the port of Ploče (in Croatia) will be of key importance for Corridor Vc's role in regional integration. It currently specialises in bulk and liquid cargo, more suitable for transportation by train than by trucks. Nevertheless, until now fuel has been transported on trucks by BiH operators (through Corridor Vc), although the government wants them to switch to rail for safety reasons. Ploče has a relatively small container terminal (20,430 TEUs as of 2010). On the other hand, Rijeka has the largest container terminal in Croatia (137,000 TEUs as of 2010), with Ro-Ro facilities, can accommodate Panamx ships, and is undergoing a capacity expansion to 600,000 TEU. The port of Koper (on the western side of the Istrian peninsula) has the largest container terminal on the Adriatic (600,000 TEU as of 2013). Both of these ports have a long track record of serving exporters from Croatia, Hungary, Slovakia, Czech Republic, Austria, western Ukraine, southern Poland and southern Germany.
Importantly, the port of Rijeka has prepared a development master plan (devised by the Rotterdam Maritime Group) to construct a large container terminal in Omišalj on Krk Island by 2030. The container terminal would increase the annual capacity of the port by 2.5 million TEUs, although it is not clear whether this plan will be realised. The Croatian Ministry of Transport confirmed that space for development is limited at the port of Rijeka, and the port of Ploče provides the only option for expanding container terminal capacity on the northern coast of the Adriatic.

In all, given the importance of Corridor Vc for BiH's economy and progress so far, it is plausible to assume that it will be completed in the medium term (in about 10-15 years). By that time, if other conditions are also fulfilled, such as the simplification and streamlining of FBiH's custom procedures, an advance in the status of the Ionian-Adriatic highway, and importantly, the development of a container terminal at the port of Ploče, Corridor Vc will make a stronger contribution to European integration, beyond BiH. Nevertheless, as the port of Rijeka is expected to remain the preferred option of central European exporters for the foreseeable future, its wider impact on European integration will probably be limited, and important mainly for FBiH's exporters (as well as the local population and international tourists heading to the Adriatic). Its future potential in terms of regional integration is therefore rated ***moderate***.

Key findings

- The regional integration impact of physical infrastructure projects connecting countries (such as highways), might not be observable for many years, even decades, as they are only gradually realised and their impact can be measured only after their full completion
- The political and ethnic fragmentation of BiH results in a lack of shared vision and priorities, seriously impeding the implementation of large infrastructure projects aiming at regional integration. A large part of Vc remains unbuilt as each of the ethnic groups (Bosniaks, Serbs, Croats) lobbies to align it to connect their own communities and in accordance with their own preferences;
- The setback in the first PPP project on Corridor Vc has discouraged subsequent attempts to work with the private sector in the road sector;
- Local companies in BiH have not been able to work under maintenance performance contracts (as envisaged at project approval). Corridor Vc maintenance is currently contracted based on standard contracts.

Operational considerations <u>for strengthening the regional integration impact</u> of similar future projects:

- As the Bank intends to finance additional sections of corridor Vc, as well as other corridors in southern Europe, undertake a small TC project, conducting a diagnostic survey among a group of Bank clients (and selected non-clients) from COOs, to better understand their connectivity needs, routing preferences, obstacles to more intensive trade, etc. The results could then feed into a data base, which would provide more reliable assessment of regional integration potential of different corridors to be financed by the Bank.
- In future Corridor Vc projects, consider including (as a TI component) assistance to FBiH authorities to streamline customs procedures and simplify tariff and non-tariff regimes;
- Consider working with the port of Ploče on developing its container terminal. As the container terminal in Rijeka is at the limit of its capacity and has few options to expand, the importance of the port of Ploče is expected to grow. Such a container terminal should attracting central European exporters and help Corridor Vc realise its potential of becoming critical for European connectivity;
- Consider supporting the development of the Ionian-Adriatic highway, particularly the Montenegrin section. Completion of this highway will substantially enhance the regional integration role played by Corridor Vc;
- Consider joining forces with the World Bank on restructuring and upgrading BiH's railways, particularly alongside Corridor Vc. As the port of Ploče remains a mainly bulk cargo port, adding a railway component to Corridor Vc could result in much stronger integration than currently provided by the highway.

2. Corridor Vc Completion Project – a highway project in Croatia, OpId 41325

Background:

The Corridor Vc Completion Project aimed at constructing several sections of Corridor Vc in Croatia, connecting its northern and southern ends at the borders with BiH (please see section 1 above for details related to this corridor). In 2010, the EBRD approved a sovereign-guaranteed loan of up to €60.6 million to a state highway company of Croatia Hrvatske Autoceste d.o.o. (HAC). The loan was to be co-financed by the European Investment Bank (EIB) on a 50/50 basis. Transition impact (TI) was to result from (i) border crossing enhancement, with the project supporting government policies aimed at improving the efficiency of border crossing customs and immigration procedures, resulting in higher trade flows along Corridor Vc; (ii) institutional strengthening for HAC, mainly the improvement of procurement policy and practices; and (iii) commercialisation of, and potential private sector participation in, tolling and maintenance operations.

Relevance:

At the time of approval, the Bank had provided four sovereign-guaranteed loans to the Croatian road sector. The project constituted a logical next step in developing the Trans-European Corridors and was a good fit with the prevailing EBRD regional transport strategy in the Western Balkans. It complemented the Bank's involvement in the Port of Ploče, the maritime gateway of Corridor Vc (DTM 36127), as well as the EBRD funding of the Corridor Vc sections in Bosnia and Herzegovina (DTM 38716) and in Hungary (DTM 35264, 38376, 39293), as well as provided regional transport continuity along the Corridor. The EBRD's experience in Croatia also included the two HAC projects signed in 2002 and 2003, which supported regional integration through the completion of Trans-European corridor X, a key transit route for Western and Eastern Europe, linking Italy, Germany, Slovenia, Croatia, Serbia and Macedonia with Greece and Turkey. Due to the Bank's earlier engagement in Croatia and other countries (see above section 1) this project was a continuation of the EBRD's involvement.

The expected regional impact of the operation was, from the outset, aligned to the EBRD's 2010 Strategy for Croatia: 2010 – 2013 (BDS/CR/10-1 (Final)). One of the priorities put forth was to "enhance regional trade and development by investing in regional transport infrastructure and continuing support for regional trade initiatives". At approval, the project appeared closely aligned with, and helpful to the delivery of, the Bank's strategic agenda, but this is no longer the case, as the construction of roads/motorways is not a priority in the current strategy (BDS/CR/17-1 (Final)). At approval, the project was also consistent with the Bank's 2005 Transport Operations Policy 2005 – 2008 (BDS04-72 (Final)) which identified the following key opportunities in the public sector*: "[continuing] to develop projects with a regional focus", "in the Western Balkans (…) co-financing of roads in the Trans-European network corridors with the EIB"* or *"financing projects which are complementary to these projects, such as the rehabilitation of feeder roads leading to the Trans-European Network routes".* Again, it has not retained this alignment with the current transport sector strategy (2019) as roads are not a priority under the strategic directions "Connected Networks" in CEB. Finally, the project was in line with the Croatian government's Transport Development Strategy, which underscored as strategic investments the key sections of the road network along the two TEN-T corridors within Croatia - Corridor X and Corridor Vc.

The Bank's additionality was to stem from the provision of a long term loan, matching the life of the financed assets, and its established history of co-funding in the road sector, combined with its sector knowledge and expertise from a long standing involvement in road sector funding and commercialisation in Croatia. The EBRD was additional because, at the time of approval, IFIs were the only lenders to the motorway sector. The Bank's expertise in the sector during project preparation was additional and it provided institutional support by mobilising an independent consultant under the Infrastructure Project Preparation Facility (IPPF) to assess the operational practices within HAC. This consultant prepared a comprehensive Operational Restructuring Action Plan and a Labour Restructuring Action Plan. In addition, procurement was done under EBRD rules, improved the transparency of the process.

This project was in line with both EBRD and Croatian government's priorities in the transport sector and the Bank's additionality was established. Relevance is rated ***fully satisfactory***.

Results:

The project was signed at the end of 2010. Execution was delayed because of procurement difficulties in relation to the Svilaj bridge, and also financial difficulties experienced by one of the contractors for the Drava bridge-Osijek Interchange and Halasica Bridge-Drava bridge. Project completion suffered from a total 5-year delay. These delays, combined with the failure to sign the customs and immigration protocol between Croatia and Bosnia and Herzegovina according to schedule, led to EPG's final rating of Moderate Good/Negligible (PTI 60) when TI monitoring for this project was closed in mid-2019.

Physical completion of the road sections was achieved at the end of 2018:

Group I: Section from Sredanci to the border with Bosnia and Herzegovina - Route.	3.5km (end section of the A5 Motorway & extension of the section Đakovo-Sredanci)	The works for this section were completed at the end of 2014 and it opened for traffic in 2015 except for the Sava bridge, planned for mid-2019).
Group II: Section from Sredanci to Bosnia and Herzegovina - bridge over river Sava – (Croatian side).	0.66km	An agreement between EBRD, EIB and HAC was reached, whereby EIB was to finance the construction of the bridge on its own. Completion expected in 2019.
Group III: Section from Ploče interchange to Bosnia and Herzegovina - Border crossing Metkovic	21.6km	Section completed on time and opened for traffi
Group IV: Section from Ploče interchange to Bosnia & Herzegovina – Route.	9km (part of A10 Motorway Mali Prolog-Ploče)	Section completed on time and opened for traffi
Group V: Section from Osijek interchange to bridge over river Drava (construction & equipping).	3.8km	Construction completed. In mid-2014, the Bank approved on a non-objection basis the use of loan savings (€22.5M) to finance the construction of a 3.8 km section between Osijek and the Drava Bridge. In 2015, the Bank gave a no objection approval for savings (€2.5M) to be reallocated for road equipment and utilities for the section Drava bridge - Osijek interchange.
Group VI: Section from bridge over river Drava to Halasica bridge	0.8km	Construction completed. Osijek interchange – Halasica Bridge section has not been opened to traffic yet.

The project is completed and all of the Bank's funds have been disbursed (€1.7 million has been cancelled).
With regard to the transition impact objectives, the customs and immigration protocol between Croatia and Bosnia & Herzegovina to simplify the border crossing control procedures has not been achieved. It is important to note that the situation has changed since 2010, when it was anticipated that this protocol would be in place by 2013. In the meantime, Croatia has joined the European Union and is now part of its external border. Currently, the prerequisite for the signing of the protocol is building of the border crossing with BiH - the Sava bridge (which is outside the scope of this project). It is expected that the structure will be concluded in 2019. In terms of setting standards for corporate governance and business conduct, the adoption of a procurement policy has been approved. A procurement policy audit report was prepared by KPMG, and the corresponding covenant cleared. Finally, regarding the demonstration effects of successful restructuring, a corporate strategy was produced and approved. However, neither of the two separate operating centres for tolling and maintenance have been set up as planned, and both functions are performed by one entity. Tenders were launched in accordance with Croatian public procurement rules and the corporate strategy. Overall, the transition impact benchmarks have been partially achieved.

In summary, the project was completed, although not all the segments financed under this project have been opened to traffic as of mid-2019. Unlike in BiH the project involved building of a new highway from scratch, rather than an upgrade of an existing one. This involved challenges such as land acquisition, agreement on alignment and the need to comply with more stringent environmental requirements. The operation achieved substantial savings, which allowed for the construction of additional sections of the corridor. The transition objectives of the project were only partially achieved, although there is still good chance that the border protocol with BiH will be signed soon when the Sava bridge is completed. Overall, the results of the project are considered ***fully satisfactory***.

Efficiency:

Although this was sovereign-guaranteed project, it was presented and approved based on the assumption that HAC would eb able to service the loan. In 2018, income from tolls amounted to 70% of the Company's total revenue and that from fuel excise taxes represented 19%. The Company generated its own revenues of HRK 2,418 million (excluding excise tax related income), representing growth of 26% y-o-y, which included a 13% growth in tolling revenues for the same period. This was supported by an 6% increase in tourist traffic, however it was 33% below the revenue level forecast at approval.

According to the final credit analysis, the year before, toll revenues reached HRK 1,825 million, an increase of 15% y-o-y but only half of HRK 3,573 million forecast at approval. The shortfall was mainly due to fuel tax income, which was three times lower than projected. Due to political considerations, fuel tax has not been growing as projected.

On the profitability side, EBITDA was HRK 1,199 million (€162.1 million) in 2017 (+19% y-o-y), which was slightly below projected HRK 1,286 m. This was achieved largely on the back of strong top-line performance that outpaced selling and general admin (SGA) costs growth (+80% y-o-y). This yielded an EBITDA margin of 64% (compared to 61% the year before). The rise in SGA costs was due to the merger of HAC-ONC into HAC which resulted in an increase in the number of employees (from 203 in 2016 to 3.035 in 2017). In the first nine months of 2018, EBITDA was €156.7 million (9M 2017: €140.9 million), whereas the EBITDA margin declined to 66% (compared to 69% for the same 2017 period) as a consequence of higher SGA costs. Overall, in 2017 HAC realised a net profit of HRK 137.6 million (€18.6 million), which was six times less than the projected level of HRK 864 million. In the first nine months of 2018 realised net profit was better at €58.3 million, however it was still far from the overoptimistic €160 million forecast for the whole 2018.

The current ratio was at 0.22x as of end-2017 and 0.19x at end-2018 versus the minimum covenanted level of 1.0x (waiver approved by the Bank). At end-2017, the total debt/EBITDA ratio amounted to 18% and decreased to 14% in 2018. The latest CRM document (for a new project covering the remaining sections of Corridor Vc) notes that the Company's financial debt is secured by sovereign guarantees provided by the Republic of Croatia. The first phase of financial debt restructuring was conducted in November 2017 via the issuance of a Eurobond by the Ministry of Finance, in a total amount of €1.3 billion, with a yield of almost 3% and a coupon rate of 2.75%. With the bond maturing in 2030 and HAC's share of €673 million, the Company expected interest cost savings. To this effect, interest expenses in 2018 were 9% lower than in 2017. In April 2018, the Company completed the second phase of the financial debt restructuring, with refinancing loans in the amount of €1.1 billion. The result of the refinancing is that the Company has increased the overall tenor of the debt stock and made its debt stable and sustainable in the long term.

It is expected that until the comprehensive restructuring of the client's short-term and long-term financial debt is completed, the Company will not be able to produce positive liquidity changes. In February 2019, the Bank waived compliance with certain ratios for 2018, as stipulated in Section 4.03 of the Loan Agreements. These included the current ratio. The Forward Debt Service Cover Ratio is not covenanted. At this point the DSCR was expected to be at the level of 0.18x for 2018, with the actual ratio reaching 0.23x. The projection for the current ratio was 0.19x, which materialised.

Based on this evidence, the performance is assessed as ***partly unsatisfactory***.

Overall rating:

The project was relevant, providing vital missing sections of the international corridor, while its additionality has been largely verified. The operational objectives were achieved with budgetary savings, although with substantially delays.

The transition objectives were partly achieved, although there are reasonable chances that they will be achieved in the future. Overall, the operation is rated ***good***.

Results and status of associated projects

The regional integration impact of this project is tied to completing the remaining missing links and to the continuation of the motorways beyond the Croatian jurisdiction. Projects related to Corridor Vc sections in Croatia include:

- Corridor Vc Motorway Completion (50712), CRM-approved stage in mid-2019 , €77 m
- Port of Ploče (46695)

Motorway Completion (50712)

The concept-cleared completion project (50712) is intended to address some of the missing links. It furthers the construction of two Corridor Vc motorway sections in Croatia, the first of 17.5 km between Beli Manastir and Halasica Bridge on the A5 motorway, and the other a 5 km motorway section from Beli Manastir in Croatia to the Hungarian border. This second stage foresees building a border section in cooperation with Hungary and also plans the construction of eight crossings (grade separated intersections with the existing roads), Beli Manastir interchange, Sudaraš Frontal Toll Gate (FTG), Beli Manastir Road Service Facility (RSF), eight bridges, drainage, road furniture and utilities. It is expected that the construction permit will be issued in March 2020.

The construction of these sections is likely to increase the utilisation of Corridor Vc and thus promote the regional integration impact. Nevertheless, the border crossing with BiH from the original project remains to be completed.

The new project states "Regional Integration" as its primary transition source. The proposed operation claims to support regional integration by improving the connectivity of main cities with neighbouring countries. It also states that its implementation will materially improve mobility and traffic safety. However, no current data on traffic, mobility and safety were presented, nor were the expected results.

Port of Ploče Liquid Terminal (46695)

A €9.6 million loan was signed in mid-2015 and was intended to finance the modernisation and extension of a liquid cargo terminal at the port of Ploče. In parallel, the Croatian Bank for Reconstruction and Development was to provide a €28.9 million loan to finance the modernisation and extension of the bulk cargo terminal at the port. However the EBRD's loan was only partially disbursed and pre-paid as the client considers its terms to be uncompetitive.

Port of Ploče Bulk Terminal (36127)

The Bank's loan was to finance a small part of the cost of constructing a new bulk terminal at Ploče, most of which was to be financed by the World Bank. The sovereign-guaranteed loan agreement was signed in 2007 for €11.2 million. However following the tender the bid price was lower than estimated and the World Bank's loan was sufficient to finance the whole contract. The EBRD loan was then cancelled. Nevertheless, the Bank's consultant provided assistance to the port of Ploče by drafting two concession agreements - for the bulk terminal and the container terminal. Both concessions were signed.

Regional Integration impact

Background & Current Status - see previous section on BiH Corridor Vc (Opid 38716).

Traffic results:

The project's Board Report presented traffic forecast based on a 2009 feasibility study, as follows:

Forecast Traffic on the Corridor Vc Motorway Sections (AADT)				
Section	**Length (km)**	**2015**	**2020**	**2025**
Northern Section: Sredanci Interchange to BiH Border	3.5	6,500	7,795	9,348
Southern Section: Ploče I/C to BiH Border	7.5	10.052	11,450	13,044

Source: December 2009 Feasibility Study

Northern section

As mentioned before, not all the segments financed under this project have been opened to traffic yet (namely the section between the Osijek interchange and the Halasica Bridge), and thus a direct comparison of the projected and actual traffic levels might be seen as premature. Nevertheless, the projections were made and even with some allowance for the project implementation delays (comparing 2015 projections with 2018 actuals) it is evident from the data provided by HAC that traffic on both sections has been well below the projections (see table below).

In particular, it is not entirely clear why the Board Report provided a traffic forecast for the northern part in relation to only a very short (3.5 km) section (Sredanci-BiH border), and not an average forecast for the whole Osjek-BiH border highway. If the projections were indeed for the Sredanci-BiH border section, the 2018 AADT was 271 as compared to the projected 6500 for 2015 (it was actually 149 in 2015, i.e. 46 times lower than projected). However, if Sredanci-BiH border was used as illustrative for the whole northern section, traffic on it was 2738 in 2015 (2.3x lower than projected) and 3266 in 2018, i.e. about half of that projected for 2015. In short, traffic on the northern section has been about half of that projected and very slowly growing. Due to the unfinished border crossing to BiH, traffic on the Sredanci-BiH border was negligible. See table below:

Traffic (AADT) on the Northern section

Section	Length (Km)	2017	2018	Increase (%) 2017/2018
Osijek – Čepin	8.8	2,372	2,594	9.34
Čepin - Đakovo	23.8	3,031	3,304	9.02
Đakovo - Sredanci	21.0	3,603	3,876	7.56
Sredanci - Svilaj	2.6	238	271	13.86
Total AC A5	56.2	3,012	3,266	8.43

Southern section

For the southern section, recent traffic figures for the segment between the BiH Border and the Port of Ploče, showed a substantial increase (24-42%) in average annual daily traffic in 2014 and 2016, which in recent years has continued to rise at more modest rates (6-7%). However, these results are substantially below the projections, i.e. 6.5 times for 2015 (1538 actual vs 10052 projected AADT). A gradual increase of traffic levels has narrowed the gap, but it still remains very large (2018: 2150 actual vs 11450 projected for 2020)

Traffic (AADT) on Southern section

	average annual daily traffic	Increase in traffic (%)
2014	1,084	-
2015	1,538	41.88
2016	1,906	23.98
2017	2,011	5.49
2018	2,150	6.93

Traffic in the north appears to be affected by the lack of continuation of certain sections. However, in the southern section, which has been fully completed, there seems to be limited demand for more extensive utilisation of Corridor Vc. This is probably related to the fact that the port of Ploče is primarily a bulk and liquid cargo port, rather than a container port. As such, delivery of its cargo is mainly by rail, rather than truck, although petrol has reportedly been transported to BiH by trucks. This is to cease due to safety concerns as soon as the railway link is upgraded. Moreover, the incomplete Ionian-Adriatic highway also impacts the low utilisation of this section.

The northern Croatian section has been slightly better utilised, however it appears that for the time being traffic is mainly local as links to Hungary and BiH are missing. This section will benefit from the completion of the remaining missing links, for instance between the Hungarian border and the Drava bridge (the Drava bridge itself has been completed). Likewise, although the Sava bridge became operational in July 2019, the border crossings with BiH have not yet been built.

As per softer measures supporting integration, the customs and immigration protocol between Croatia and Bosnia & Herzegovina to simplify the border crossing control procedures has not been achieved.

In sum, traffic on both the northern and southern Croatian Corridor Vc sections has been disappointing so far, remaining well below expectations. Missing links and border crossings are still under construction. The impact on regional integration is rated ***weak***.

Future prospects:

As stated in the previous section, the EBRD is contemplating addressing the missing links of this project under a new operation: Corridor Vc Motorway Completion (50712). It will finance the construction of two sections of Corridor Vc between Beli Manastir and Halasica Bridge, and from Beli Manastir in Croatia to the Hungarian border. The second phase will be to build a border section in cooperation with Hungary. Finally, it will support the construction of eight crossings.

Regarding furthering integration through Corridor Vc, the main opportunity arises from its connection to the port of Ploče. Northern Adriatic ports are at the limits of their capacity, while they do not have available space to expand (Rijeka, Koper and Venice). The port of Ploče, on the other hand, is the only one in the area with substantial available land to expand. It is the second most important port in Croatia after Rijeka. Located at the southern end of Corridor Vc, it has connections to existing road and railways (the former partially financed by the Bank). The port of Ploče is critically important for neighbouring BiH as a transportation route for seaborne imports and exports. Improving and expanding this port can increase its regional significance, and could serve as a gateway for/to markets in Serbia and Hungary. The EBRD attempted to support the extension of the port's liquid cargo terminal under project 46695 (see above), however this loan was only partially disbursed and pre-paid. To fully realise Corridor Vc's integrating potential, it will be necessary to expand a container terminal at the port of Ploče. This will require a decision by the Croatian government and a private investor to support such a project. However, as these are still distant prospects, the future integrating potential of Corridor Vc's Croatian sections is rated ***moderate***.

Finally, it is noted that Croatia became a member of the EU in 2013, but it is not yet a Schengen Area member. The country forms an external EU border and its customs and immigration services are still adapting to this. EU accession spearheaded the closer integration of Croatia with the rest of the EU, however its integration with its non-EU neighbours (with which it shares the 1,000 km borders) could now prove more complex.

Key findings

- Although the Corridor Vc sections under this project were completed, the missing links and current specialisation of cargo type at the port of Ploče prevent the Croatian sections from being more extensively utilised, especially the southern part.
- Completion of Corridor Vc depends on the actions of other countries/governments or the government of Croatia, beyond the authority of HAC. Construction on the other side of the borders is incomplete, and in some cases has not started. Agreement among different governments and different levels within the same government is required for the location and construction of border crossings, which can be a very lengthy process.
- The Croatian government's perception of motorway infrastructure has slightly shifted from interconnections, towards supporting tourism and creating other benefits/alternative uses such as reindustrialisation.
- Romanian and Bulgarian transport companies generally prefer to ship goods via Hungary (using Corridor Vb) as opposed to Serbia, BiH and Croatia, because they do not need to leave EU territory (including the Schengen Area). This has a substantial negative effect on Corridor VC's traffic levels.
- Most traffic on the northern Croatian section of Corridor Vc appears to be local.

Operational considerations for strengthening the regional integration impact of similar future projects:

- Consider incorporating support for border crossings on both sides when designing future cross-border highway projects. These components should be "front-loaded", i.e. the first to be implemented (or even a prerequisite for starting the construction of the proper highway).
- For any future Corridor Vc projects, consider supporting an agreement between Croatia and BiH on customs.
- Consider a diagnostic of the potential use of motorways by international and regional transport companies when contemplating new projects with "regional integration" as a transition quality.

- For highway projects, consider incorporating the introduction of KPI's for highway companies (or cooperating with other IFIs in the same - as was done by the Company in cooperation with the World Bank) to improve the planning, monitoring and supervising of investments as well as to enhance efficiency and standards.

3. Azeri Roads Reconstruction and Rehabilitation Project – a highway project in Azerbaijan, OpId 43094

Background

In 2011, the Board approved a sovereign loan to the Republic of Azerbaijan for up to US$750 million, to reconstruct selected sections of the regional road network, which were deemed the priority investments under a programme prepared by Azeravtoyol, the state-owned road agency. The loan originally had three equal tranches of US$250 million each.
The full amount of tranche A was committed upon loan signing and was designated for the construction of a 156 km Mingachevir – Bahramtapa road section, which runs from north to south through Azerbaijan's rural heartland.

In December 2013, the Board committed part of Tranche B (US$120 million) to match the expected construction cost of a 62 km Bahramtapa to Bilasuvar road section and two other regional roads. However, this sub-project was not implemented as, after completing the design and early procurement process, the Government changed its priorities and put the construction of these roads on hold.

By December 2016 the project has been entirely restructured and the Board was requested to approve the reallocation of the remaining loan to finance a section of another road. Under the new plan, US$500 million of the Bank's loan tranches B and C would finance the dualisation and rehabilitation of 130 km of the Ganja - Gazakh - Georgian Border Highway (GGG Highway), part of the 500 km M2/E60 road corridor, included in the TRACECA road network and the part of one of alternative routes of the Silk Road. Other amendments to the original project scope included funding consultants to assist Azeravtoyol with project implementation, preparation of the performance based maintenance contracts (PBMC), institutional strengthening aspects and the use of any savings to finance the previously approved Bahramtapa to Bilasuvar road. In summary, the reallocation of US$500 million of the Bank's loan comprised:

1. the change in use of proceeds under previously committed part of Tranche B (US$120 million) to the GGG highway;
2. commitment of the remaining US$130 million under Tranche B to be used for GGG highway;
3. commitment of the whole US$250 million of Tranche C to be used for GGG highway.

The amendment was signed after a year delay, in February 2018, however the time was used to prepare technical designs and procurement documents. It included yet another "amendment to the amendment", reducing the amount of the Bank's commitment by US$ 50 million, i.e. to US$ 450 million.

The situation as of September 2019 was:

1. Tranche A: US$250 million had been committed for the construction of a 156 km Mingachevir Bahramtapa road section
2. Tranche B and C: US$450 million was committed for the dualisation and rehabilitation of a 130km Ganja-Gazakh-Georgian border road section and the rehabilitation of a 60 km section from Bahramtapa to Bilasuvar. The reduced amount was considered in line with the updated budget for construction, due to abnormally low-priced tenders.

Relevance

At approval, the project was in line with the EBRD's 2010 Country Strategy for Azerbaijan (BDS/AZ/10-1) for the 2010-2013 period. The strategy underscored the need for continuous support for the development of Azerbaijan's infrastructure and noted that the majority of investments would be financed on a sovereign basis.

The project was also consistent with the Bank's 2004 Transport Operations Policy (BDS04-72) for the 2004-2008 period. This policy indicated that the EBRD would support reform progress in the road sector with particular value placed on multi-IFI cooperation. The operation was also aligned with the Bank's intention to encourage improvement in the efficiency of road sector administration and management by supporting the introduction of PBMC.

In terms of national strategy, the Ministry of Transport's Road Network Development Programme assigned a high priority to upgrading the road network, making the Road State Agency responsible for implementation. Upgrading the three major international routes to a dual, two lane standard was an important component of this Programme. The Government underscored the importance of transport corridors in the promotion of sustainable international trade, regional cooperation and economic growth in the regions of Azerbaijan, outside of Baku. Funding from the EBRD was to be used to accelerate the regional road reconstruction programme for roads feeding into the core corridor system and affecting the regional connectivity and development.

In December 2013, the Board approved the commitment of Tranche B (US$120 million, €103 million equivalent) to match the expected construction cost of a 62 km Bahramtapa to Bilasuvar road section. The relevance of this reconstruction of the R42 highway rested on the expectation that it would facilitate regional integration and interconnectivity and promote economic diversification.

The initial intention of the project was to ensure adequate road connectivity for regions outside the core corridors and to support economic diversification and non-oil sectors (since much of the non-oil trade comprised small size shipments transported by road to neighbouring countries). The narrow, low quality roads were to be replaced. The key business purpose of the project was to contribute to reconstructing the key regional ("magistral") roads which either fed into the key corridors or led directly to key border crossings with Georgia and Iran. The operation amendment shifted the focus of the project from financing regional roads to financing the main highway in Azerbaijan, connecting its capital and the Caspian Sea coast with the Georgian border – the gateway to Turkey and Europe.

The amended project (rehabilitating part of the GGG Highway) was highly relevant as it was part of the TRACECA corridor, and part of one of the alternative routes of the Silk Road route, which connects Baku with Georgia, Turkey and the EU. This highway was considered critical part of the above-mentioned Government's priority programme to upgrade the national road network to support the economic growth of the regions outside Baku and to facilitate international trade, connectivity and integration into the global economy. However, it is unclear why the completion of the road so critical for Azerbaijan's international connectivity was not prioritised from the start of the project.

The expected additionality of the project was to be derived from the EBRD's terms, as the sector's financing needs could not be met entirely by one single financier. The investment programme was coordinated with the World Bank and ADB to ensure efficient and complementary engagement in the sector. Other additional attributes were that the EBRD was willing to undertake the sector and political risk. It also had a well-established relationship with the Government, the MoTC and ARS on road sector issues, which would enable it to promote a reform agenda. Finally, the EBRD was one of the few IFIs operating in the road sector that was willing to engage in policy dialogue with the Government.

The addendum at the end of 2017 noted that Additionality also stemmed from the financing and sector reform aspects of the Bank's project, which were coordinated with other IFIs active in the sector to ensure efficient and complementary engagement.

In December 2013, upon approval of the Tranche B commitment, it was expected that the some other identified priority regional roads, would be co-financed either by another IFI or by the Republic of Azerbaijan. Specifically, it was hoped that EIB would co-finance the project and their participation was actively encouraged by the EBRD.

The Board minutes (2 December 2016) indicate that one Director recalled his abstentions on the two previous occasions when the Board had considered the project, due to the lack of a co-financing partner and the limited transition impact. Management explained that they hoped to pursue co-financing opportunities with IFIs in the future, and that the client wished to revisit the business case for tolling which would have a positive impact on the transition potential; based on the team's responses, the Director supported the project. Nevertheless, by end 2017 (Addendum 2), it was reported

that neither option materialised, as the EIB had pursued other priorities in Azerbaijan, thus ruling out this co-financing, and the tolling component was dropped.

The project's relevance has been strengthened due to the amendment, while the Bank's additionality has been reaffirmed due to EIB's absence. However, as in fact the Bank approved two very different projects, their relevance is rated separately. Relevance of the original project has been reduced due to the change of the government's priorities and it is rated ***partly unsatisfactory***, while relevance of the amended project is rated ***fully satisfactory***.

Results

With regard to the physical completion of the project, progress as of September 2019 was as follows:

Tranche A: (Mingachevir - Bahramtapa road section) - three lots:
- Lot 1 works contract started in January 2016 and was completed in July 2017.
- Lot 2 works contract started in April 2016 and was completed in October 2018.
- Lot 3 works contract started on November 2016 and was completed in December 2017.

Trance B and C: four lots
- The R42 road construction contract was awarded in November 2018.

For the GGG highway road construction contract:
- Lot 1 contract was awarded in November 2018.
- Lot 2 contract was awarded in April 2019.
- Lot 3 contract was awarded in November 2018.

The expected completion date for both projects (R42 and GGG) is June 2021.
In terms of timing, it was initially expected that first tranche would be completed three years post signing, i.e. by December 2014. Due to delays in collecting legal opinions, procurement and mobilisation and keeping in mind the latest completion date of October 2018 (Lot 2), completion has been delayed by 4 years.
It was anticipated that Tranche B and C would be deployed/committed in consecutive years after Tranche A and completed in three years, approximately by December 2016. With the new Tranche C completion date of June 2021, this amounts to 4.5 year delay versus the original plan.

As per transition benchmarks, monitoring indicators:

1. Framework for markets: institutions, laws, policies that promote market functioning and efficiency

    a. Adoption of the Road Sector Master Plan and the Maintenance Strategy by end of 2013
    Achieved
    The road sector master plan was completed by Louis Berger consultants (under the World Bank's TC) in 2012. EPG however found that there were some gaps in the analysis. The transport team hired an external consultant to update the Master Plan. A revised Master Plan was completed in July 2016 and approved by AYS in October 2016.

    b. Allocation of agreed level of funding for the adequate maintenance and management of the relevant classes of the regional road network by end of 2013
    Achieved
    In 2016 the Road Fund resources amounted to 290 AZN million. Estimates from two independent consultant confirmed that sufficient funds were being allocated to maintain the road network overall and that levels of maintenance funding were adequate for all categories of regional and local roads. However, they found that many regional and local roads were beyond repair and would need to be rehabilitated to put them into a maintainable condition.

    c. Select the road tolling strategy for the sector (partial tolling; tolling of core corridors; section tolling - to be selected upon review of tolling options) by end of 2013
    Not Achieved

    d. Introduce tolling on selected sections of the network by end of 2016
    Not Achieved
    The Tolling Study Report 2013, funded by ADB offered a cautious outlook and limited options on the prospects for privately financed toll road projects in Azerbaijan. It cited that tolling opportunities in Azerbaijan were quite weak, mainly due to low traffic on potential roads and legal requirements to have

a free alternative road run alongside any toll road. Tolling was not recommended at the time. As of June 2018 there had been no further interest from the GOA.
During EvD interviews, the Road State Agency indicated that tolling will be revisited once the new road is finalised. They anticipate that the road from Baku to the Russian border will be tolled at the end of 2019 (120 km), and operational in 2021. It was decided that tolling will be tested once the basic infrastructure is in place.

e. Finalisation of performance-based routine maintenance contract tender documentation and submission for approval to relevant authorities by end of 2013
Achieved
The PBMC model contract was developed by an independent consultant. All documents relevant to the PBMC strategy and tender were completed in mid-2016 and subsequently approved by AYS. The tender was expected to be launched towards end 2017/2018.

f. Successful rolling out of performance based contracts for selected road sections by end of 2018
Not Achieved
This is considered delayed due to the pressures the PIU is undergoing with the GGG highway procurement process, which has become very complex (3x lots being tendered separately) due to the bidders opting to mix and match the different lots. Moreover, AYS has 60 maintenance units employing 20,000 people. They are not interested in outsourcing, although they claim that this will be revisited in the future.

2. Demonstration of ways of successfully restructuring companies and institutions

2.1 Implement outsourcing of non-core maintenance tasks by end of 2016
Not Achieved
Based on the recommendations of the Institutional Strengthening assignment in relation to PBMC introduction, it was proposed that non-core maintenance tasks were best kept within the AYS's remit until after the PBMC contracts have been tendered and proven to be a successful, more efficient and more economical way to maintain roads in Azerbaijan.

At project's amendment new transition benchmarks were added in order to ensure reform progress continued under AYS management as follows:

For R (regional) roads

- Percentage in poor condition (from 14% in 2015) to less than 10% by 2021
- Percentage in very poor condition (from 16% in 2015) to less than 12% by 2021

For Y (local) roads:

- Percentage in poor condition (from 13% in 2015) less than 10% by 2021
- Percentage in very poor condition (from 43% in 2015) less than 36% by 2021

These have not been reported on in the latest TIMS, but the target dates are still two years ahead. However, during interviews with EvD, AYS representatives stated that the percentage of roads in poor condition has substantially decreased in recent years, as about 20-25 AYS maintenance units have been deployed to repair regional roads. Moreover, a 40 km section of a regional road was rehabilitated under an ADB project last year. However, no exact numbers were given for roads that are still in poor condition.
Seven years after signing, progress on the project has been slow and complicated due to several delays, a change in PIU management, poor coordination between the IFIs (according to TIMS – between ADB and WB but no details given), poor quality of the original consultant's master plan assignment (2012), and change in AYS management. The loan agreement was declared effective after a delay of one year, and the consultancy assignment tenders were also delayed. The road sector master plan completed by the World Bank's consultants in 2012 had to be revised by EPG due to some gaps. In addition, a road tolling strategy was drafted by an ADB consultant, which did not recommend tolling the country's motorways. In 2018, it was considered hardly feasible to roll out performance based contracts for selected road sections and outsource non-core maintenance tasks. On this basis, EPG increased the TI Risk to High.

Based on the results achieved so far, the results of the project are rated ***partly unsatisfactory***.

Efficiency

This is a sovereign operation and the Client is the Republic of Azerbaijan, for the benefit of AYS, the State Road Agency and implementing agency. As such, its creditworthiness is that of the state.

In September 2019, the IMF concluded its Article IV consultation with the Republic of Azerbaijan. It indicated that the economy continues to recover from a banking crisis and recession. Real GDP growth was 1.4% in 2018 and 2.4% in the first half of 2019, supported by a rise in natural gas production and activity in the services sector. Increased oil prices have helped improve internal and external balances. Looking forward, economic growth is anticipated to reach 2.7% in 2019 on strong hydrocarbon production and robust domestic demand, benefitting from new spending measures. With oil prices expected to be around US$60 per barrel, the current account surplus is forecast to remain sizeable. Public debt is set to decline relative to the size of the economy.

Azerbaijan is rated at Ba2 with a stable outlook by Moody's (2019), Fitch's rating is BB+ (2019) and S&P's 2018 outlook was also stable. Moody's links the preservation of rating to the government's growing net creditor position, supported by current budgetary reforms and gradual risk reduction in the banking sector. It adds that current reforms in the fiscal and financial sectors can strengthen the resilience of a sovereign credit profile to shocks, including lower oil prices, and contribute to increasing the credibility and effectiveness of policies to a greater extent than Moody's currently expects. Finally, it expects that Azerbaijan's state debt will be reduced to 29% of GDP (from 33% in 2018) by 2020.

It is not possible to assess the effectiveness of the implementing agency, but the creditworthiness of the Government is rated ***fully satisfactory***.

Overall rating

The relevance of the original project was not very strong as the "priority" regional roads, originally selected for the Bank's financing, turned out to be of lower priority in the two years following loan signing and the project went through substantial changes. These changes shifted the project's focus and improved its rationale, particularly in relation to cross-border connectivity. Implementation was challenging and resulted in a four year delay, with an anticipated 4.5 year delay in delivering the main component (still under implementation). The project's achievements to date in terms of transition benchmarks have been very modest and there are limited prospects for their full achievement in the future. Overall, the project is rated ***acceptable***.

Results and status of associated projects

1863 - Azerbaijan: Silk Road (2004)

The operation was to rehabilitate approximately 500 km of the eastern section of M2 road - part of the TRACECA corridor and historic Silk Road (the western section of the road, which was rehabilitated under the core project - Azeri Roads Reconstruction, described above). The total cost was US$173 million co-financed by a number of IFIs and bilaterals (loans in favour of the Azeri Road Service OJSC). The EBRD's US$41 million sovereign loan financed the reconstruction of an 85 km road section from Hajigabul (formerly known as Gazi Mammed) to Kyurdamir.

The project was sub-divided into eight segments, one of which was financed by the EBRD, while other IFIs and bilateral agencies financed the other seven. Other funding sources included the Islamic Development Bank, the Asian Development Bank, the Saudi Fund for Development, the Kuwait Fund for Arab Economic Development, the European Union and the Government of Azerbaijan. The project also aimed to enable improvements in managing and financing the Azeri road sector.

A 2010 EvD evaluation of the project rated it overall *successful* for the EBRD-financed section. The achievement of the physical objective was *good*. The road rehabilitation was achieved and the quality of the restored road asset was considered to have improved significantly. The overall transition impact was rated *satisfactory*. In terms of the overall project implementation, at end-2009, the majority of the eastern section of the Silk Road was in full operation and maintenance was also being fully implemented.

34723 - Baku to Samur (2005)

A US$100 million sovereign loan to reconstruct and upgrade a 61 km section of road, located on the north–south route between Baku and the Russian border (Samur). In 2008, the Government asked to change the scope of work and the priorities of certain sections. As a result, the originally planned 61 km was reduced to 17 km. The final project cost was nevertheless that of the original loan. The cost increase resulted from (i) the increase in the scope of the civil works, (ii) the high level of inflation in local road construction costs between 2005 and 2008, and (iii) a 22% drop in the value of the dollar against the Manat. Project completion was originally expected in September 2008, but after significant delays, it was reached two years later, in November 2010. The road section from km 45 to km 89 was financed by the Government of Azerbaijan.

The 2013 EvD evaluation of the project rated it *partly successful*. Transition impact was considered *marginal* due to the slower than expected transport sector reform process and the operation change in focus.These two projects were the starting point of the Bank's investment cooperation and policy dialogue engagement in the road sector. The Azeri Roads project was considered a continuation of the efforts to reinforce the EBRD's long-term work with the government and to support reform. It was also expected to complement the continuing IFI lending program.

Regional Integration impact

The original project was to support regional connectivity within Azerbaijan, rather than cross-border (although it was to have a spill-over effect on international integration. Part of the project's business purpose was *"supporting the government's priority of rehabilitating and reconstructing principal road corridors and key regional roads to enable trade and regional cooperation with neighbouring countries, and facilitating economic development across the country as a whole"*. It underscored the strategic need for the reconstruction to guarantee adequate road connectivity for regions outside the core corridors and the authorities' decision to enhance economic diversification and non-oil sectors. At the time, most of the non-oil trade comprised small shipments transported by road to other countries and access to international markets was considered to require the provision of suitable regional road infrastructure. The objective was to meet the demand derived from strong traffic increases and to replace the narrow, low quality roads. The Board report also stated that *"the main business purpose of the operation is to contribute to the reconstruction of the key regional roads by feeding into the key corridors or directly leading to key border crossings with Georgia and Iran"*.

The Board report for the 2016 amendment referred extensively to the regional integration benefits, arguing that connecting TRACECA countries to the trans-European networks would help to develop trade relations and integrate the economies in the world market. The Ganja-Gazakh-Georgian border road was the only remaining M2 highway section in need of upgrading to dual carriageway standards.

The original project focused on refurbishing different sections of the various regional roads that connect Azerbaijan's cities. The amended project was to finance additional traffic lanes on the last 130 km of the main highway (M2 or GGG highway) leading to the Azeri-Georgian border, connecting capital Baku (and port of Alat) with Georgia (Tbilisi) and further with the EU. The amendment elevated the importance of the project to one that is critical for the country's entire economy, as well as for international connectivity, given that it is part of TRACECA and the Silk Road, connecting Central Asia/China with Europe.

According to AYS, Georgia has also been renovating its part of M2, which will be completed by 2020. The investments include improvements to the M2 border crossing. The current waiting time at the border depends on the season and time of day, but reportedly it is no longer than half an hour for trucks.

Traffic results:

The Board reports for both the original and the amended project contained base line data and traffic forecasts, the first one on the Bahramtapa to Mingachevir section, and the second on the GGG highway.

However, as the GGG highway project has not been completed, it is too early to conclusively verify the traffic. It is anticipated that the fully reconstructed GGG highway will be re-opened in 2021, following a three year construction period. Nevertheless, traffic has been flowing on the GGG highway's parallel lanes, completed under the ADB's 2010 East-West Highway Improvement Project. The 2018 traffic data provided by AYS for the GGG highway section financed by the Bank (under amended $450 million project) and for the completed Bahramtapa-Mingachevir R18 road section (financed under the originally approved tranche A of $250 million) are presented below.

Traffic on Bank-financed sections of Azeri highways (AADT)

Road Section	2007 Base Traffic - average from 7* sections	2015 Base Traffic - average from seven sections	Forecast for 2020 (average from seven sections)	Forecast for 2021 (average from 15 and five sections)	Actual 2018
Bahramtapa-Mingachevir R18	1975		3800		4596
Ganja to Georgian border M2		6519		5303	8233
Gazakh -Georgina border M2		2209		3020	6508

* AYS provided actual traffic data for entire length of each of the three sections, however baseline data and forecasts were broken down into seven, fifteen and five sub-sections respectively for each of the above three. To make them comparable with actuals, EvD calculated average baseline and forecast traffic levels for these three sections.

The table demonstrates that for the Mingachevir to Bahramtapa Road (completed under tranche A), traffic in 2018 was 20% above the 2020 forecast and 131% above the 2007 baseline traffic.

Data for the GGG international highway indicates that in 2018 traffic was 55% ahead of the 2021 projection on the entire length financed by tranches B and C of the Bank's loan. However, it was an impressive 115% ahead for the final section before the Georgian border (Gazakh-border). If AYS' data are reliable, it would point to the project having a strong cross-border connectivity relevance as traffic has substantially grew even before its completion (expected in 2021). However, it is noted that for the entire Bank-financed section of the M2, the 2021 forecast was 18% below actual baseline traffic recorded in 2015. It is unclear why the consultant forecast that traffic would actually decrease after the highway renovation. However, one reason for such an outcome could have been that the calculation of averages distorted the projections. Detailed analysis of the projections by section show that they were very conservative, however assumed a slight increase in traffic on certain sections, e.g. traffic on the Ganja to Shamkir section was to grow in 2021 by 7% from the 2015 base. Another reason for such an outcome might be that the data gathering methodology used by the consultant for baseline differed from that used by AYS for actual.

Moreover, data provided by AYS indicate that 47% of traffic on the entire Ganja-Georgian border section was from cargo trucks, which accounted for 82% of traffic on the final section before the Georgian border. This demonstrates that the highway is used intensively by cargo trucks, which could indicate that in the future when it is completed, the project will have a strong impact on international trade and thus on cross-border connectivity.

EvD has some questions about the reliability of the traffic data, and the GGG highway has not been completed yet. Nevertheless, based on available traffic data on R18 section and indicative data for GGG highway regional integration impact is rated ***strong*** with high probability that it will remain strong in the future.

Key findings:

- Road projects are exposed to frequent changes in governmental priorities;
- Public highway agencies typically have large numbers of employees and are often reluctant to consider outsourcing of their core services to the private sector (although there have been exceptions, e.g. successful outsourcing in Albania);
- Actual traffic data and traffic projections are often difficult to compare due to differing data gathering methodologies, as well the traffic being counted on different sections of the road.
- Different IFIs financing different sections of large highways may have slightly diverse priorities (e.g. related to their individual mandates) and may not always closely coordinate their actions.

Operational considerations for strengthening the regional integration impact of similar future projects:

- To be able to assess the regional integration impact of road sector projects, provision should be made in the loan agreement to ensure that the client will provide traffic data for sections, comparable to those in the feasibility studies, and gathered using the same methodology.
- The capacity of the highway agencies in many COOs to manage large scale capital investment projects is relatively weak. Considerable capacity building and implementation support components should always be included as part of such projects;
- IFIs financing different sections of large road projects should set up a working group with regular meeting schedule to ensure exchange of information and close coordination of their work.

4. Pan-European Corridors – a highway project in Ukraine. OpId 40185

Background

The operation sought to upgrade and rehabilitate the key road approaches to Kyiv. It comprised the road sections on M-01, M-05, M-06, M-07, N-01 and R-02 highways, which are arterial routes of the Ukrainian road network and CIS[9]. These are also part of international transport corridors that connect Kiev to the European Union (to the west), to Odessa (to the south) and CIS (to the east and north). Moreover, the facility intended to finance the introduction of performance based maintenance contracts in the country's road sector on a pilot basis. Finally, it was to finance works supervision and technical advice for a reform component.

In 2010, the EBRD approved a sovereign loan, to be provided in two tranches to Ukravtodor, the Ukrainian state roads administrator. The first tranche was up to €250 million and the second up to €200 million (to be committed at the Bank's sole discretion). It was anticipated that EIB would also provide financing of up to €450 million to co-finance the project.

The project was to promote transition through the introduction of a fuel tax, entirely dedicated to roads maintenance, the axel load tax, as well as the launch of a performance based contract tender for road maintenance. Finally, a new strategy for the roads sector development was to be prepared and adopted. The operation was expected to generate substantial energy efficiency benefits by reducing congestion and improving the fuel efficiency of vehicles using the network.

Relevance

The Bank has been involved in restructuring and modernising Ukravtodor's operations and the road sector reform in Ukraine through three earlier projects (see Associated Projects section). This project was intended to build on the significant reform progress attained under these projects and to enable the Bank to strengthen its long-term co-operation with the Government as well as encourage additional reforms.

At origination, the operation aligned with the Bank's 2007 Country Strategy for Ukraine (BDS/UK/07-1), in which a key area of medium term operational focus was "completing modernisation of the M06 road linking Kiev to the border with the EU as well as financing the implementation of other major international axes". Moreover, the strategy highlighted that "the preparations for the finals of the European Football Championship in 2012" were expected to become an important catalyst for public and private investment to upgrade the transport infrastructure sustainably to meet the requirements of the Championship. In the current (2018) country strategy (BDS/UK/18-1 (Final)), one of the strategic priorities for 2018-2023 is to "improve integration by facilitating trade and investment, expanding infrastructure links, and supporting convergence with EU standards", and one of the expectations is to achieve improved connectivity through enhanced infrastructure.

The project was also consistent with the 2005-2008 Bank's Transport Operations Policy (BDS04-72), in force at the time of approval. The policy stated that the EBRD would concentrate on the reconstruction and upgrading of the international transport corridors in Ukraine, and would emphasise co-operation with EIB. Additionally, the operation was consistent with the Bank's intention to promote improvement in the efficiency of the road sector administration and management. One of the strategic directions of the new draft Transport Sector Strategy (2020-2024) is to improve the quality and connectivity of network infrastructure, within the transition quality of Integrated. More specifically for roads, it proposes to complement co-financing partners with investment in the construction, upgrade and modernisation of motorways, national, regional, local and rural cross border road infrastructure "to improve access to markets and services, and create linkages to key transport networks and corridors, including TEN-T, WBCN, CAREC, TRACECA and BRI in COOs. In addition, it seeks to encourage sustainable funding of road maintenance and support performance-based maintenance, and where feasible to out-source to the private sector.

In terms of regional integration, the focus on the rehabilitation and renovation of the key road approaches to Kyiv was substantiated as it was considered the main destination and transit point for domestic and international road users. The operation was expected to contribute to the integration of the country's transport network into the core international and regional transport networks, including that of the European Union, and the promotion of Ukraine's transit potential, which were key strategies of the Government. The economic and financial crisis added importance to this project and to public

[9] Commonwealth of Independent States (Armenia, Azerbaijan, Belarus, Kazakhstan, Kyrgyz Republic, Moldova, Mongolia, Russian Federation, Tajikistan, Turkmenistan, Ukraine, Uzbekistan).

investments in infrastructure, given their potential to stimulate economic growth, create jobs and generate a multiplier effect throughout the economy by creating demand without causing economic distortions.

The project was also aligned with the "Ukraine's 2030 National Transport Strategy". Its priority area is the innovative development of the transport sector and global investment projects. One of the expected results is the reconstruction of Ukraine's motorway network and its full compliance with TEN-T standards and interconnections to regional centres, and particularly to Kyiv in order to increase regional mobility.

The Bank's additionality was to stem from the provision of financing, as the needs could not be met entirely by one single financier. EIB had agreed to work alongside the EBRD to co-finance projects providing financing on reasonable terms which was otherwise not available. The EBRD brought additional finance at a time when no other long term funding was available. In terms of attributes, the Bank was willing to undertake sector and political risks. It also had a well-established relationship with the authorities, the Ministry of Transport and Communication (MoTC) and Ukravtodor on road sector issues, which allowed it to promote reform agendas. Finally, the EBRD was one of the few IFIs working in the road sector and was willing to engage in policy dialogue with the Government.

As presented in this section, the operation was well aligned with both the EBRD's and Ukraine's priorities in the transport sector. It has also remained aligned with evolving Bank strategy over time. Additionality claims were plausible. Relevance is thus rated ***excellent***.

Results

The loan was signed in November 2010 and declared effective in September 2011. Tranche B was committed in April 2014 following a separate Board approval as part of the Bank's crisis response programme for Ukraine. Under Tranche B €80 million out of €200 million had been disbursed as of Q3 2019.

Tranche A:
€239 million has been disbursed out of €250 million approved under this tranche. The rehabilitation works and related supervisions services on the M06 and M07 roads sections are considered substantially completed. The remaining Tranche A funds have been earmarked for the Operation and Performance Contract (OPRC) component currently being implemented by Onur (a local contractor with a contract awarded mid-2014).

Tranche B:
€101 million has been disbursed out of €200 million. Some progress has been achieved on the works under Tranche B, but the key section of the project (M05) has been experiencing almost five year delays. It was to be completed by January 2015, but after two extensions only 60% of the works were completed in 2018. The client's request for an extension to the end of 2019 is currently under consideration by the Bank.

Section N01 is substantially completed. For M01, (contract signed in October 2018) the contractor is proceeding with mobilisation. The contractor for M06 - Zhytomyr bypass – (contract signed in June 2018) is moving forward with implementation. It is intended to cancel R02 due to its low priority at the present time.

As savings have been achieved during the project, the client has requested the lenders to re-allocate the funds towards financing additional project components. These include (i) construction of additional interchanges on the M06 and M05 roads as part of the road safety enhancement measures; and (ii) rehabilitation of an additional M05 road section (km 87-128). Both requests are being considered by the EBRD and EIB.

The transition impact objectives of the project were considered largely achieved. Most importantly, the fuel tax, entirely dedicated to road maintenance was introduced and is fully allocated to the Road Fund established in January 2018. The mechanism for load tax has been prepared, however there is no specific date for its introduction. The tender for the performance based contract for road maintenance was successfully completed (Onur – a local company has been contracted and has been already working under this contract). Also the new strategy for the road sector development was prepared and approved by the Bank. It is the basis for the sector reforms currently under preparation, which envisages privatisation of Automobiles Roads of Ukraine.

The objectives set under tranche A were achieved and those under tranche B have been under very slow implementation, however the likelihood of them being achieved is relatively high. Importantly, the project achieved key transition objectives, which should have a lasting impact on Ukraine's road sector. With a proviso that the works under tranche B will be achieved, the overall project results are rated ***fully satisfactory***.

Efficiency

Ukravtodor is budgetary institution that does not produce financial statements. Its creditworthiness is that of the state. The project is a sovereign loan with debt service payments made directly by the Ministry of Finance. Ukravtodor manages the funds from road user charges collected by the State and allocated to the road network maintenance and development.

The sector revenues accumulate in a special Road Fund within the state budget. This Fund was created in 2018 on the basis of new legislation approved as part of the Bank's conditions precedent to the loan's disbursement. A gradual roll-out is expected: 50% of road user charges were sent to the Fund in 2018, 75% in 2019 and 100% are to be directed there in 2020 and onwards. Sixty per cent of the proceeds are allocated to national roads which are managed by Ukravtodor, 35% to regional roads and 5% to a special road safety fund. The main revenue sources of the Road Fund are: (i) the excise taxes on fuel and vehicles; (ii) import duties on fuel, vehicles and petrochemicals; and (iii) payments for heavy vehicles.

The road sector's most important source of revenue is the excise tax on fuel. The Bank's original requirements were €182/ton for petrol and €66/ton for diesel. Ultimately, these levels were exceeded, rising to €213/ton for petrol and €139/ton for diesel in 2019. €1.6 billion total revenues from fuel excise tax is projected for 2019.

In September 2019 Fitch increased Ukraine's sovereign credit rating to 'B' from 'B-' and assigned a positive outlook. The reasons supporting the upgrade included demonstrated timely access to fiscal and external financing improving macroeconomic stability and declining public indebtedness, in addition to a shortened electoral period that has reduced domestic political uncertainty. Standard & Poor's credit rating stands at B- with stable outlook. Moody's rating was set at Caa1 with stable outlook at the end of 2018. As Ukravtodor does not produce financial statements, the financial performance of the client cannot be assessed. Its creditworthiness is that of the state, rated ***fully satisfactory***.

Overall rating

This operation was relevant at the time of approval and has remained aligned to both the EBRD's and Ukraine's strategies. Additionality claims were plausible. Operational objectives have been achieved albeit implementation is still suffering from long delays. In terms of budget, savings were realised, with the proceeds expected to rehabilitate additional road sections. Important sector's financing reform objectives were achieved under this project, which overall is rated ***good***.

Results and status of associated projects

EBRD projects in the road sector in Ukraine include:

- Rehabilitation of M06 H'way (2213), 2000, €75 million
- Ukraine Second Project Kiev-Chop Road Rehabilitation (31928), 2005, €100 million
- Ukraine Third Project Kiev-Chop Road Rehabilitation (36547), 2006, €200 million
- Ukraine Road Corridors (50831), CRM 2019, €450 million

If the last-listed project is approved and signed, the Bank's commitments to the Ukrainian road sector will near €1.3 billion.

The 50831 project would provide an additional €450 million to Ukravtodor in order to finance:

- the rehabilitation of the M-05 Kyiv-Odesa road section in Cherkasy region
- the construction of the northern section (24 km) of the bypass around the city of Lviv
- the rehabilitation of the M-05 Kyiv-Odesa road section in Kirovohrad, Mykolaiv and Odesa regions

The project is expected to be co-financed by a parallel loan from EIB of up to €450 million. The proposed investments are part of the country's Road Development Programme for 2018-2022. The road sections belong to the TEN-T network

and are considered vital in terms of connectivity within the country and the EU. The M-05 Kyiv-Odesa road is the main north-south highway and is also one of the busiest roads connecting Kiev to the largest southern city and the ports located in the Black Sea. Building the Lviv Northern bypass is expected to reduce the traffic flow through central Lviv, which is located at the intersection of four international highways and is the biggest city in the West. It is envisaged that redirecting traffic to the northern section of the bypass will reduce congestion and travel time, especially for traffic going to/from Poland and the EU.

The primary TI quality of the project is Integrated. It claims to support the provision of new infrastructure between or within regions that are currently inadequately integrated. The rehabilitation of the roads is expected to contribute considerably to the economic integration of the country by improving the quality of export-oriented cargo transportation between the industrial and agricultural regions to the sea ports. However, the CRM document did not present a baseline of current volumes of cargo, levels of traffic, travel times nor safety levels.

Regional Integration impact

Background & Current Status

Regional integration was not part of the project's transition objectives as it was not yet part of the Bank's TI qualities. However, the Board report stated that *"the international corridors (including approaches to Kiev), linking Ukraine with the EU and other CIS countries are considered by the Government of Ukraine as a high priority and part of the country's preparations for hosting EURO 2012."* It was deemed that Ukraine's export-oriented trade sector needed improved transport infrastructure in order to successfully participate in the global economy and obtain World Trade Organisation membership. Rehabilitating and upgrading international corridors was thus an important component of the socio-economic development of Ukraine. The economic and financial crisis compounded the importance of the operation to public investments in infrastructure, which were considered to stimulate economic growth, create jobs and generate a multiplier effect throughout the economy by creating demand without causing economic distortions.

The Board report stated that the principal benefits from improving these road sections were savings in vehicle operating costs, due to improved road surface conditions, time savings for road users, as well as in road maintenance costs. Benefits from a lower occurrence of traffic accidents were also predicted. However, no baselines or projections were presented for these indicators. Moreover, the project was also expected to have other economic benefits, but it stated that these were difficult to quantify: regional economic growth and *"integration effects, including with the EU"*. However no baseline or projections were presented for them, beyond a traffic forecast (see below).

Traffic results:

The Board report presented a traffic forecast for all sections to be financed and the data presented for existing traffic was said to have been obtained from automatic traffic counters installed by Ukravtodor. Nevertheless, during an interview with EvD, Ukravtodor stated that no counters were installed, so equivalent follow-up data was not available.
In EvD's view, a wider regional integration cannot be measured based on the traffic on small sections of the interchanges. Instead, longer distances could give a more accurate outlook. Estimates for the years 2011 and 2017 for the M-05 and M-06 were the only information available, and were provided to EvD by the agency.

Annual average daily traffic (AADT)								
Projections						**Actual**		
Road	**Section in the projections**	**Length (km)**	**2009 Base Year Traffic**	**2015**	**2020**	**Section verified in 2017**	**2017**	**2017 actual/ 2015 projected**
M-06	km 14.08 to km 17.94	3.86	33,040	46,748	64,460	km 14.08 to km 15.71		
Kyiv – Chop	Km 17.94 to km 20.05	2.11	29,120	41,191	56,783	Km 15.71 to km 24.72	*48,005*	***1.15***
	km 20.05 to km 24.72	4.67	26,170	36,989	50,946			

	km 24.72 to km 39.09	14.37	20,990	26,619	40,721		-	
	km 39.09 to km 51.76	12.67	19,150	27,013	37,152	km 36.00 to km 51.85	*21,227*	***0.79***
	km 51.76 to km 103.05	51.29	17,100	24,103	33,095	km 51.850 to km 68.43		
						km 68.43 to km 86.36	*19,498*	***0.81***
						km 86.36 to km 103.50		
	km 103.05 to km 120.16	17.11	15,930	22,440	30,791	km 103.50 to km 109.47	*15,973*	***0.71***
						km 109.47 to km 120.16		
	km 120.16 to km 128.00	7.84	20,320	28,649	39,348	km 120.16 to km 128.60	21,853	**0.76**
(Zhytomyr Bypass)	km 128.00 to km 152.40	24.40	6,920	9,687	13,199	km 128.60 to km 138.83	*6,656*	***0.69***
						km 138.83 to km 152.48		
M-05	km 17.74 to km 26.20	8.46	38,200	54,157	74,842	km 11.66 to km 26.60	41,047	**0.76**
Kyiv to Odessa	km 26.20 to km 36.00	9.8	28,460	40,272	55,537	km 26.20 to km 36.00	30,590	**0.76**
	km 42.00 to km 65.80	23.5	24,800	35,083	48,367	km 42.00 to km 65.80	23,118	**0.66**
	km 65.80 to km 79.60	13.8	20,300	28,711	39,571	km 65.80 to km 79.60	20,795	**0.72**
	km 79.60 to km 87.00	7.4	14,250	20,108	27,645	km 79.60 to km 87.00	14,424	**0.72**

By 2017 the actual traffic remained 20-30% below the projections for 2015, with the exception of an M-06 section near Kiev that had slightly exceeded the 2015 forecast (and it can be asserted it met 2017 forecast). However this highway section was located on the first 10km from Kiev in the western direction to Zhitomir, implying that traffic on this section is primarily local, i.e. from commuters travelling between Kiev and its suburbs. The 2017 level of traffic on the sections more distant from Kiev it was similar to that of 2009 (before the project). Likewise, in 2017, traffic on the M-05 in the direction of Odessa remained about 25-35% lower than projected and at a level largely similar to that of 2009. The upgrade of the approaches to Kiev appear to have streamlined the local traffic, but there is no evidence yet that they impacted an increase of traffic at a regional level, therefore the current regional integration impact of this project is rated ***weak***.

Future prospects:

The Government of Ukraine has launched a highly ambitious National Transport Strategy, "Drive Ukraine 2030". Its premise is to *"create a new reality instead of repairing the old one"*. Its goals are the creation of a free trade area between Ukraine and the EU; integration of its transport infrastructure in the Trans-European Transport Network; and integration

of EU key rules in Ukrainian transport legislation and practice. It anticipates the construction of 10 highways, including Kyiv – Bila Tserkvia, and motorways from Sumy, Kharkiv, Dnipro, Luhansk, Donetsk, Odessa and Mykolaiv towards other EU countries.

The EBRD has continued its involvement in the sector, and a new proposed project includes priority investments, which respond to the Government-approved Road Development Programme 2018-2022. The road sections to be rehabilitated under the new project are part of the TEN-T network and are a crucial element affecting connectivity, both within Ukraine and to the EU. These sections are: M-05 Kyiv-Odesa in Cherkasy region, the northern section of the bypass around the city of Lviv (24 km); and M-05 Kyiv-Odesa in Kirovohrad, Mykolaiv and Odesa regions. The construction of the northern section of the bypass will allow the completion of the circle on the south-eastern and western ends of the city, reduce congestion and decrease travel time. This will serve in particular for transit traffic going to/from Poland and the EU.

These sections are part of the Gdansk-Odesa Highway (GO Highway), which is to connect the Baltic sea ports of Gdansk and Gdynia in Poland to those of Odesa and Mykolaiv on the Black Sea. It is part of the TEN-T network. The highway's strategic importance lies in the improvement of the country's connectivity to the EU, reduction of transportation costs and delivery times between Ukraine and Poland by up to 30% and the inauguration of a new transport corridor servicing the flow of goods between Asia and the eastern part of the EU through Ukraine.

Moreover, the prospects of the road transport sector in Ukraine seem assured, at least in the short-term, also due to deficiencies in rail transport. There are serious security concerns related to rail transport (difficulty of insuring cargo). In addition, the width of the gauge is different to that of neighbouring countries. Consequently, about 90% of bulk cargo is transported by road.

However, future competition to road transport might come from river transport as the Dnipro river is navigable and flows in the direction of the Black sea ports. This type of transport has been largely underutilised so far. However, in 2018 a leading grain trader Nibulon launched a project, financed by EBRD, to develop riverside infrastructure and increase exports of ari-products through Dnipro. One of the operation components is the construction of three new river terminals for grain; a 42,000-tonne storage facility, a barge quay and a new railway at the firm's Mykolaiv terminal.

Overall, there are clear prospects for the further development of Ukraine's connectivity, which should result in increased long-distance traffic on sections financed by this particular operation. However, the assessed project is expected to have the strongest impact primarily on local traffic. The future integrating potential of this operation is rated ***moderate***.

Key findings

- Upgrade to approaches to large urban conurbation may streamline local traffic but its impact on long-distance traffic is unclear. There is no evidence in the case of the Kiev project that an upgrade of its approaches increased long-distance traffic and thus impacted integration on a regional scale.
- The availability and quality of traffic data related to the Bank's highway projects has been poor. There has been no systematic data gathering by qualified institutions. The quality of available data is questionable. It is difficult to determine exact traffic levels on the sections financed by the Bank.
- The Ukrainian Government's new strategy for transport is extremely ambitious, anticipating the construction of ten highways and the creation of an international hub in a time span of 11 years.
- Ukravtodor remains a part of the government, rather than a separate state-owned entity with a separate budget and KPIs (as is the case of the highway agencies in other COOs). It manages the funds from road fuel tax collected by the State and allocated to road network maintenance and development. It does not appear to have been consulted in the preparation of the country's new transport strategy.

Operational considerations for strengthening the regional integration impact of similar future projects:

- For transport projects, particularly highways, covenant the requirement for the client to monitor traffic levels. Measuring points should be aligned with those from the feasibility study to allow for easy verification, adjustment of expectations, as well as evaluation.

- Improve diagnostics and due diligence, focusing more on needs assessment. For instance, one of the interlinks in this operation will probably be cancelled due to its low priority. It is difficult to discern why it was included in the project in the first place.
- When designing future road projects in Ukraine, consider how the road infrastructure interlinks with other transport modes, such as river transport, which has particularly high potential in this country.

5. DCT Gdansk Expansion – a sea port project in Poland, Opid 45805

Background:

In November 2014 the Bank provided a €31.1 million loan to the Deepwater Container Terminal SA (DCT) to finance the construction of a second deep-water container terminal at the port of Gdansk, Poland, as well as to refinance the loan incurred for the construction of Terminal 1. The main objective of the project was to expand DCT's capacity from 1.35 million TEU to 2.55 million TEU to meet growing demand from large container ships coming directly from Asia.

Since 2007 DCT has operated the largest and fastest growing maritime container port and the only deep-water terminal in the Baltic Sea Region, having direct connection with the Far East. DCT has been both a gateway port for Poland and a major transhipment hub for the majority of the South and East Baltic Region (SEBR). The Company was at the time of the loan majority owned by Macquarie's Global Infrastructure Fund II.

Port of Gdansk (of which DCT is a part) is the most-easterly Baltic port with a deep draft, capable of receiving Ultra Large Container Ships (ULCS) with up to 18,000 TEUs container capacity - the most cost efficient and commonly used vessels for the inter-continental trade between Asia and Europe. The containers with goods delivered to DCT are transhipped either by feeder vessels or other transport modes, such as rail or road to Central and Eastern Europe and Baltic countries. Being the largest private sector terminal operator in Poland, DCT has a pivotal role in the development of the regional intermodal and logistics sector. Its operations are focused on transferring containers from import vessels or onto export vessels, as well as onward transhipment by feeder vessels and transit transport by road (trucks) or rail (DCT has its own rail terminal). The EBRD loan was co-financed by commercial lenders who jointly provided the balance of €258.9 million for the investment (with an entire loan amount of €290 million). The loan had a 15 year tenor, including a 2-year grace period, and is currently being repaid.

Relevance:

The project's relevance with regard to the sector strategy was relatively strong. One of the objectives of the Bank's Transport Sector Strategy (BDS13-205 (Final)), was to "invest in key safe, clean and efficient port infrastructure developments" and address capacity bottlenecks, which "act as a constraint on transition and broader economic development". At approval, the DCT terminal was already operating at approximately 92% of its capacity and bottlenecks were building up in the system. To meet growing demand, new capacity was needed to alleviate these constraints. This provided a strong rationale to support the construction of a second terminal, which would increase its handling capacity.

With regard to the country strategy, the case for the project seemed slightly weaker as the strategy for Poland did not refer directly to supporting the country's connectivity, being strongly based on promoting a low carbon economy. However, as the project aimed to increase economies of scale in transporting containers by sea, thus reducing the number of trucks on the road, it responded to this strategic priority fairly well. Moreover, the project contained a number of energy efficiency components, which further strengthened its strategic fit.

The Bank's additionality was based on the long tenor (15 years) needed to repay a large loan at a time when Polish commercial banks were only able to extend loans for up to 10 years. IFI participation provided comfort, enabling them to extend the tenor. The Bank's loan was relatively small, enabling local banks to provide the bulk of the financing. Furthermore, the Gdansk Port Authority (GPA) granted DCT leasing rights for terminal 2 without a public tender. This was deemed justified because part of the land already leased to DCT for terminal 1 was needed for terminal 2 to fulfil the length requirements to accommodate large ships (no other operator would have been able to construct a long terminal, preventing key project's objectives being achieved). However, this has raised concerns among some institutions (EU and EIB). After analysing the rationale for granting the lease without a tender, the EBRD agreed that it was justified and an exception from the Bank's policy was granted. However, as there was some controversy (and a

complaint logged at the EU by a competing Gdynia container port operator) commercial banks felt much more secure with another IFI participating in this financing.

The Polish Government's Transport Development Strategy to 2020 and the Sea Ports Development Strategy to 2020, singled out DCT as a key element in Poland's transport system and its connectivity to the world. The project explicitly aimed to expand this connectivity by enabling more direct links between Poland and Asia and reaffirming DCT's position as the Baltic Sea's container hub. For this reason the project's relevance, particularly from a regional integration perspective, is rated ***excellent***.

Results:

After the tender for constructing the new terminal, the total project costs decreased from an estimated €361 million to €311 million (14%), due to a fall in capex cost (as per the final offers submitted for the construction contract and the STS cranes supply contract), the transfer of the contingency amount into a separate tranche of €7.8 million, and further reductions amounting to €18.6 million related to working capital. As a result of this reduction and following the completion of the construction, the structure of the facility changed. This change included cancellation of the undisbursed portion of the Bank's loan (€7.6 million) and renegotiation of the terms of the loan (due to the removal of the construction risk).

The new terminal was put into operation in January 2017, a few months ahead of plan. The current maximum capacity is 2.9 million TEU. Moreover, eight large cranes have been procured and are operational at the new terminal (three more than planned). The ramp-up period took more time due to a decrease in transhipments to Russia following a change in the political situation and the RUB devaluation in 2014, which resulted in a sharp reduction of Russian imports. As a result, 2015 handling dropped to 1.07 million TEU, recovering to 1.3 million in 2016. It has since grown steadily to 1.9 million TEU in 2018, with 2.1 million expected in 2019.

The original DCT Gdansk loan has been now refinanced by a new facility (where EBRD participated).

In terms of **transition benchmarks**, the current status is as follows:

- *Increase in container volumes from Polish ports from 1.9m TEU to 3.0m TEU in 2019.*
Considered achieved. DCT is on track to achieve 2.1 million TEU in 2019 and 0.9 million should be easily achieved by other Polish ports (Gdynia alone had throughput of 0.8 million TEU in 2018 and this figure has continued to grow).

- *Increase in containerisation ratio in Poland from 43 TEU per 1,000 inhabitants in 2012 to 80 TEU in 2018*
Likely to be achieved or almost achieved. The latest data currently available are for 2017 YE, and show the containerisation ratio growing from 43 in 2012 to 64 (based on containers passing through the ports). The following monitoring year is expected to bring an additional improvement of the containerisation ratio, although it might fall a bit short of the target. Importantly, DCT's share of container handling at Polish ports was 60% as of 2018.

- *Increase in transhipment cargo from 632,000 TEU in 2013 to 1,000,000 by end of 2018*
Not achieved. Following a downturn in trade with Russia after 2014, when transhipments decreased to 0.4 million TEU, transhipment rebounded to 0.7 million in 2018. The volume and value of transhipments continued to grow in 2019 but it is unlikely that 1 million TEU will be achieved this year (more realistically in 2020-21).

- *At least one more shipping group calling at DCT Gdansk*
Achieved. Upon completion of Terminal 2, DCT attracted other major shipping lines. Maersk remains DCT's largest client (in line with its position as the world's largest container ship operator), but the share of other lines has been steadily increasing. The largest other lines are now: MSC, the Alliance, Ocean Line, Hyundai and 2M Alliance.

- *Minimum 20% of Terminal 2 capacity to at least one other major liner company other than Maersk.*
Achieved. In 2018, 53% of DCT's handled volume was from Maersk containers and 47% from other lines.

In addition to operational/integration-related benchmarks, the project set energy efficiency benchmarks. They included:

- Energy reduction to 23 kwh/TEU - reduced to 12 kwh/TEU (2018)

- Accreditation of ISO 14001 and 50001 – both obtained
- Development of carbon footprint accounting and publication – completed
- Introduction of cold ironing technology – the new terminal prepared for cold ironing, however there is no demand from berthing ships
- Adoption of recommendations on climate change adoption - adopted

Results of this project are rated ***fully satisfactory***.

Efficiency:

In 2017 DCT's revenues went up 31% to €100 million (vs €75 million projected), the EBITDA margin was sustained at 60% (vs 47% forecast) and net profit more than doubled to €44 million on the back of positive FX gains (vs €2.3 million projected). Improved profitability translated into +31% increase in cash flow with €55.5 million sufficient to cover €10.6 million capex, €22.8 million debt service (repayment started in July 2017) and €11.4 million dividends (one-off approval by lenders). Leverage has been decreasing on account of increased profitability (total debt of €204 million constituting 3.4x EBITDA and 1.2x equity, including €37 million shareholder loans vs 4.5x and 1.5x respectively in 2016.

In Q1 2018, DCT registered its strongest volume yet; handling 471,575 TEUs (+45% y-o-y) as a result of developing business with OCEAN Alliance and +18% increase in the number of import/export containers. It is anticipated that in 2018 figures will show a 37% increase in revenues, a stable 60% EBITDA margin and €82 million cash flow, implying comfortable coverage of due debt service (€16 million) and anticipated capex €34 million.

In mid-2018 DCT was taken over by a consortium of Singapore Port Authority, IFM Global Development Fund and the Polish Development Fund. The consortium plans to further develop DCT by building a third terminal (to increase capacity to 4.5 million TEU by 2025), investing about €0.4 billion. The project's efficiency is rated ***excellent***.

Overall rating:

The project is rated ***outstanding***, as it had a strong rationale, achieved its stated operational objectives on schedule and with savings. Its key transition objectives were also largely achieved (with one outstanding likely to be achieved the next year). It had important positive impact on wider Polish economy and its connectivity. It performs very well financially, substantially exceeding its original projections.

Results and status of associated projects

In mid-2019 the Bank signed a follow up project – Project Felicjan (50798) providing a senior loan of €46.25 million to:

(i) DCT Gdansk SA (€19.5 million) to refinance the outstanding debt from the first loan
(ii) A consortium of Port Singapore Authority, Polish Development Fund and an Australian pension fund (€18 million) to co-finance acquisition of 100% shares in DCT from a consortium led by Macquarie fund
(iii) DCT Gdansk Group (€8.75 million) to co-finance capex at DCT

This operation will primarily co-finance the acquisition of DCT by a new investor (total costs €144 million) and refinance the existing debt. The capex tranche will co-finance €70 million programme to increase waterside handling capacity of terminals 1 and 2.

The project did not include "regional integration" among its TI objectives (TI was based on resilience - developing PPP secondary market transaction, and governance – implementing company's standards). However, in EvD's view this project will enhance regional integration as the capex component is to add to the terminals' capacity, increasing it from the current 2.9 million TEU to 3.3 million TEU by 2023. Moreover, the new investor has very ambitious development plans for DCT, including building the third terminal by 2024, which will increase DCT's capacity to 4.5 million TEU, as well as two more terminals by 2040 bringing it to 7.5 million TEU.

Regional Integration impact

At the time of project approval (2014), Regional Integration was not part of the Bank's transition qualities. However the Board report made several references to benefits stemming from improving Poland's connectivity by increasing DCT's capacity, such as:

- *The Project not only improves connectivity by bringing the intermodal link-up closer to final destinations, it also reduces the costs of the logistics chain by up to 20 per cent.*

- *With increased container throughput, the Project will strengthen the integration of the regional transport market by:*
  (i) expanding the most energy efficient and competitive export gateway for Polish and SEBR products, thus helping the SEBR economies to compete in the global markets
  (ii) facilitating the development of new a cross-border intermodal rail transport connecting Poland with Slovakia and Hungary
- *DCT has a dedicated 2 km long railway track, which is directly connected with Gdańsk North Port railway station and in turn links the DCT Port with the Polish and European network of railway lines. It is therefore a key link in the Trans-European Network – Transport ("TEN-T") Corridor No. 6 (the Baltic-Adriatic Corridor) connecting the Nordic countries with the SEBR and CEE countries.*

In 2018 DCT's container throughput was 1.9 million TEU, 14% increase on 2017 and 8% above projections. The construction of the second terminal at DCT substantially increased its ability to attract shipments directly from Asia, which has grown at the rate of around 20% per year since the new terminal opened and now accounts for 70% of the total volume handled. Regular service includes two calls per week from large container ships from Asia (105 in total in 2018). The total volume in 2019 is set to reach 2.1 million TEU (vs 1.9 million TEU projected). The number of major shipping companies increased, while the volume of transhipments is recovering after a decrease following sanctions on Russia.

However, the expectation that the project would "*facilitate the development of new a cross-border intermodal rail transport connecting Poland with Slovakia and Hungary"* was not realised. Nevertheless, DCT operates a rail terminal in Paskow, Czech Republic and by the end of 2019 it plans to increase regular service there from one to two trains per week. The capacity constraint of the Polish railway system remains the main obstacle to realising the full potential of DCT to connect to hinterland but DCT itself has very little ability to change this situation. The Polish government (Ministry of Infrastructure) is fully aware of this weakness and plans to improve Poland's railway network with €16 billion in investments to be realised in the coming years, with priority being given to north-south lines from Polish ports to its southern borders. In recent years the Polish government's focus has been on improving road infrastructure, and only key railway lines - mainly leading west-east - were rehabilitated.

DCT's priority is to enable long train services, even if their speed will remain relatively low (80 km/h). Long trains would enable the economies of scale applied to large shipments from Asia to be retained also in the containers' onward journey. The ability to send long trains to Poland (on previously rehabilitated west-east lines) is one of the main advantages of German ports which still handle a large number of containers destined to/from Poland and SERB. Improved rail connections are of particular importance for DCT as Maersk (its main client) has recently started to ship containers from China to St Petersburg by rail. Some of them are then transhipped to DCT, from where they would be expected to smoothly continue their journey to the Polish hinterland. Therefore rail is both a threat and an opportunity for DCT. Rail is faster than sea transport (half of the time, i.e. 18 days, rather than 36 from Shanghai) but can be subject to bottlenecks and is more expensive (double the cost).

Following a meeting with the Ministry of Infrastructure, EvD understands that a number of investments improving DCT's connectivity through Poland are planned, including a new ring-road for the Tri-city of Gdansk-Sopot-Gdynia (to be realised as a PPP) and the completion of the A1 highway to Slovakia (by 2023). Moreover, two large investments – the Central Port of Gdansk and the Central Transport Hub (near Lodz) are the top strategic priorities for the Polish government in terms of infrastructure. This is in addition to the development of container terminals (there are 31 in Poland, which will double in the coming years). Financing for most of these investments is to be provided by the Polish development Fund, BGK, EU and IFIs.

Another obstacle to improving DCT's connectivity is posed by the border procedures, particularly on the Belorussian and Russian (Kaliningrad) borders. The Ministry confirmed that a common working group on custom procedures was recently reactivated with Russia (after a six year hiatus) and the prospects for streamlining procedures look good.

In conclusion, the extension of DCT Gdansk has substantially improved its direct connectivity with the Far East and other regional ports. Its impact on regional integration has been somewhat hampered by the suboptimal development

of railway and highway connections, however these are being addressed by current and planned projects. The regional integration impact of this project is rated ***strong***.

Key findings:

- Investments into port infrastructure usually enhance connectivity. However such investments may be insufficient for a port to fully realise its integrating potential if the infrastructure connecting it to hinterland is underdeveloped.
- Political upheavals constitute a key risk for international hubs to fully realise their potential (in the case of DCT its transhipments to Russia were affected by EU sanctions).
- Investments into deep water container terminals may be particularly beneficial for strengthening connectivity as such terminals attract large vessels providing a direct service to/from distant locations.

Operational considerations for strengthening the regional integration impact of similar future projects:

- Due diligence of transport hub-type projects (ports/airports) should include analysis of their connectivity to the hinterland.
- Whenever possible, the Bank should seek synergies and inter-modal complementarity among the projects it finances in the transport sector, for example, supporting complementary projects connecting the transport hubs it finances to hinterland or combining projects in different transport sub-sectors to complement each other promoting inter-modality.

6. Asya Port – a port project in Turkey, OpId 4417

Background:

In 2013 the EBRD provided a US$92 million loan (€67.7 million) for the design, construction, operation and maintenance of the Asya Port container terminal – a greenfield investment, located on the Marmara Sea in Turkey. The International Finance Corporation (IFC) and Isbank contributed parallel loans of US$69 million and US$105 million, respectively. The intention was for the new terminal to become a transhipment hub for cargo bound for the Black Sea and provide additional container handling capacity to locally-bound traffic, allowing for more efficient and safer operations through the Bosporus Strait. The new terminal was to serve almost exclusively the Mediterranean Shipping Company (MSC) – the second largest shipping company in the world. MSC's transhipment business was to be moved from Marport (port of Istanbul) to Asya port. The project's transition impact potential was to stem from: i) greater competition in the Black Sea container shipping, and ii) setting standards for corporate governance and business conduct.

Relevance:

The project was aligned with the Bank's 2013 Transport Sector Strategy (BDS13-205 (Final)), as it sought to promote productive, competitive private sector activity in the port sector in order to address infrastructure bottlenecks and, more specifically, to support liberalisation and privatisation, including processes to reduce monopolistic situations within seaports by allowing the free entry of new private operators. The project was designed in a manner intended to contribute to the Strategy's commercial orientation objective. While the support to the private sector has been realised, the capacity to be utilised by third party liners has not developed as expected.

The operation was also in alignment with the 2012 Country Strategy for Turkey (BDS/TK/12-1(Final)), which underscored the EBRD's continuous support for private sector operators in the development of intermodal transport operations through the provision of long term funding. It is also in line with the Strategy's objective to support regional infrastructure projects by assisting regional authorities to attract more private sector investment into the infrastructure sector.

Regarding additionality, the Bank's loan provided 10-year financing for this greenfield infrastructure investment – the tenor needed due to the economic life of infrastructure assets. At the time of approval, it was considered that the commercial banks did not have appetite for longer tenors and were not inclined to bear the construction risk. However, based on EvD's interviews, it appears that in the absence of Bank financing, alternatives could have been found. EvD notes that the owners of Asya port are from the prominent Soyuer family of Soyuer Group, who are connected by family ties to the owners of MSC, the leader in global container shipping and the world's second-largest shipping line in terms of container vessel capacity. Nevertheless, the financing needed for a greenfield port terminal was sizable and could pose a certain challenge even for billionaires to fund without external financing.

An important part of the Bank's additionality was its attributes. The EBRD joined the financing of the port in 2013, three years into its construction. At that time, Asya Port did not operate under any documented management systems, policies, plans or procedures for environment, health and safety (EH&S) or social aspects. No planned stakeholder engagement activities were in place. The EBRD designed and covenanted the Environmental and Social Action Plan (ESAP). Via the ESAP implementation, the project was constructed and operated in compliance with the Bank's environmental standards. The EBRD assisted the Port in developing resource efficient solutions, which since than have been implemented on site. These included: solar panels, liquid natural gas powered trucks, electric engine STS and RTG's, systems for purification and re-use of collected rainwater for landscaping and firefighting. The client appreciates the close relationship with the EBRD team, and underscores the importance of the Bank's local presence, with its deep knowledge of the country context and sector, and the ability to make contact whenever necessary, as well as the Banking team's willingness to assist and solve issues. This, in client's view, is particular to the EBRD compared to other IFIs and partners.

In terms of commercial mobilisation, Isbank, a local commercial bank, provided 40% of the total debt financing. Additionally, in 2016/2017, the EBRD mobilised a further US$ 44 million in commercial funding via B-loan sell-downs to two international investment funds. The Bank's additionality in this project might not have been the strongest, nevertheless it fitted well with the Bank's strategic objectives of supporting Turkey's private regional infrastructure, built and maintained in line with European EH&S standards.

The project's relevance is assessed ***fully satisfactory*** as most additionality-related claims made at approval were realised as planned.

Results:

Seventy-five per cent of the loan was disbursed by the end of 2015, with the remainder cancelled at the borrower's request. Subsequently, the EBRD sold down US$ 44 million of its loan to the B-lenders, who proceeded with the purchase despite the coup d'état in Turkey of July 2016.

The terminal's construction was completed in July 2015, with a nine month delay. However, loan repayments were not affected as the Client serviced the debt with its own cash flows. The construction cost was ~28% below budget, with savings achieved on civil works and equipment. As part of the original investment plan Asya Port expected to procure 11 STS cranes to undertake its quay operations. Ultimately, the Borrower decided to acquire only nine cranes, which resulted in a decrease in actual project costs to US$283 million (along with savings in civil works) and led to lower than anticipated drawdowns (i.e. US$92 million committed vs. US$70.3 million disbursed by the EBRD). As market conditions have improved and capacity utilisation has continued its upward trend, the client has decided to complete the original investment plan by acquiring the two additional STS cranes and other complementary equipment (e-RTG cranes, tractors), through an extension of the project with the Bank (see status of future and associated projects section below).

The terminal operates as a transhipment hub for MSC, which ships containers to Asya Port, from where they are loaded onto smaller feeder vessels and transported to final destinations in the Black Sea region. The port has a maximum handling capacity of 2.5 million TEU, higher than the initially planned 1.9 million TEU. The status of the transition benchmarks is as follows:

1. Greater competition in the Black Sea container shipping:
   a. Capacity utilisation at Asya Port – 75% (1.4m TEUs) – 2016
      Delayed. The port started operations in July 2015, six months later than planned. The capacity utilisation in 2016 was 0.70m TEUs (37%). By 2018, capacity utilisation reached 60%. The original target capacity is expected to be achieved in 2021. Factors affecting the timeline include the slowdown in the container market on the back of slowing economies in the Black Sea region, partly affected by the conflict in Ukraine.
   b. Increase in the volume of transhipments to the Black Sea region (from 650 thousand TEUs estimated in 2012 at the two main transhipment ports of Piraeus and Marport) to at least 1 million TEUs – 2016
      Achieved. In 2018, the total transhipment in the region was 1.1 million TEUs.
   c. At least a quarter (25%) of Asya Port's capacity (450 thousand TEUs) to be taken up by third party liners – 2017

Not Achieved. At Q3 2019, only 1% of capacity was taken up by third party liners. MSC constituted around 99% of Asya Port's traffic and revenues. The Client states that it is engaged in discussions with third party shippers to attract more volume. However, it does not appear to be a priority as it is considered to contradict the investment rationale of shareholders (a port built for MSC). Thus MSC has priority in the utilisation of the Port and it seems this will continue for the foreseeable future.

d. Large container vessels (12,000 TEU +) handling at Asya Port; – 2015
Achieved. Since July 2015 the Port has been capable of handling mega vessels. It can accommodate the largest ship in the world with a capacity of over 19,000 TEU. Ultra-large container ships call at Asya port once a week.

2. Setting standards for corporate governance and business conduct
   a. ISO 14000 certification – 2016
   Achieved. ISO 14001 certification was obtained in June 2016.
   b. ISO 50001 certification – 2016
   Achieved with delay. A waiver was given for this covenant, postponing the due date to June 30 2017. ISO 50001 certification was obtained in May 2017.

The project was executed with a nine month delay but with over a quarter of budget savings. It has been operating well since then, despite capacity utilisation being lower than expected so far. It is expected that target capacity utilisation will be achieved in 2021. Other TI benchmarks were met, except for third party service. With some caveats, the results of the project are rated ***fully satisfactory***.

Efficiency

The client's financial performance has lagged behind the original expectations. The key factor for this has been the lower volume of container handling in 2015 and 2016, resulting from the economic slowdown in Black Sea countries. The Client prepared a revised business plan in 2017 and updated the market expectations and the financial model. Against the revised model, performance in 2017 and 2018 was marginally above the projections, however it was substantially below the original forecast contained in the project's Board report. The analysis below is based on annual IFRS audited financials versus the original projections at Board approval and the Client's updated business plan:

Base Case projections at Board Approval (Dec 2013)

	2016			**2017**			**2018**		
Financials	**Audited**	***Forecast***	**Difference**	**Audited**	***Forecast***	**Difference**	**Audited**	***Forecast***	**Difference**
DSCR (covenanted at 1.2x)	1.33x	*3.08x*	↓	1.43x	*1.52x*	↓	1.56x	*1.53x*	↑
USDm									
Revenue	40.1	*118.2*	**(78.0)**	62.0	*132.4*	**(70.3)**	71.1	*138.6*	**(67.4)**
EBITDA	25.1	*68.5*	**(43.3)**	47.6	*78.9*	**(31.3)**	57.3	*82.9*	**(25.7)**
Net Income	(2.3)	*23.0*	**(25.4)**	22.6	*31.3*	**(8.7)**	32.2	*36.1*	**(3.9)**
EBITDA margin	62.6%	*58.0%*	**4.6%**	76.8%	*60.0%*	**16.8%**	80.5%	*60.0%*	**20.5%**

Client's updated Business Plan (2017)

				2017			**2018**		
Financials				**Audited**	***Forecast***	**Difference**	**Audited**	**Forecast**	**Difference**
DSCR (covenanted at 1.2x)				1.43x	*1.96x*	↓	1.56x	*2.2x*	↓
USDm									
Revenue				62.0	*58.6*	**3.4**	71.1	*66.4*	**4.8**
EBITDA				47.6	*42.2*	**5.4**	57.3	*47.6*	**9.6**
Net Income				22.6	*17.3*	**5.3**	32.2	*22.7*	**9.5**
EBITDA margin				76.8%	*72.1%*	**4.7%**	80.5%	*71.8%*	**8.7%**

In 2018 Asya Port generated total revenues of US$71.1 million, an increase of 15% compared to the previous year but about 40% below original projections. The increased turnover was fully in line with the growth in traffic, as the throughput showed a 15% increase against 2017 traffic (969k TEU). The revenue was composed largely of quay income (US$54.8 million) from container handling and the balance from complementary services (yard and ancillary income). Despite the depreciation of the Lira throughout the year, the EBITDA margin was 80% in 2018 compared to 77% in 2017, generating an EBITDA of US$57.3 million (vs. US$47.6 million in 2017) but 30% below projections. This was due to rigorous operating cost control. Overall, compared to the projections presented to the Board in 2013, the efficiency of the operation is rated ***partly unsatisfactory***.

Overall rating:

The project is overall rated ***good***, as its relevance has been solid and the results are largely satisfactory (despite missing some of the transition benchmarks). The financial performance has been lower than expected, but still sound, resulting in a relatively high operating margin.

Results and status of associated projects

Operation change/Additional commitment Asya Port (44717)

In 3Q 2019, eh board approved an additional commitment of up to US$12 million (€10.9 million) in favour of Asya Port Liman A.S. The purpose is to finance the acquisition of six additional cranes, terminal tractors and other equipment. The total project cost will amount to US$24 million, of which IFC will provide the remaining US$12 million.

The extension will introduce incremental improvements to the existing transition qualities, *Competitive* and *Well-Governed*, by promoting higher operational standards, setting meaningful energy efficiency targets and introducing public disclosure standards. It does not target *Integrated* transition quality but one of the incremental TI objectives of this loan extension is the expansion and modernisation of the Client's physical capacity. The additional commitment has the potential to contribute to regional integration as it is expected to increase the quay capacity of the terminal from 1.9 million TEU to over 2 million TEU and help the Client to complete the investment plan associated with the original project (2013).

Tekirdag Port Project (50172)

This project was approved in mid-2019. The loan is for up to US$17.5 million (€15.4 million equivalent) and will finance the acquisition of the operating rights ("Concession") of Tekirdag Port (an existing port terminal in the Thrace region in Turkey) and its modernisation and capacity. Transition impact is to be derived from *Competitive* and *Integrated* qualities by supporting the concession of the port and improving the efficiency of its operations. *Integrated* is the project's secondary quality, and it is anticipated that the operation will support material quality improvements in the regional maritime infrastructure through the modernisation/expansion of the port. The project is expected to improve the port's operational efficiency by expanding and optimising its capacity, which in turn will have a positive impact on load factors of the goods transported, enhance modal shift and direct a larger share of the cargo from roads to the railway and shipping lines. The *integrated* TI benchmark for this quality expects that after project implementation, traffic at the Port will increase from 1.6 million tonnes in 2017 to 1.9 million tonnes in 2022 for general and dry bulk cargo, mainly due to improvement in the Port's infrastructure; and from 150k to 260k tonnes for liquid cargo for the same period mainly due to improvements in storage.

Regional Integration impact

The Bank's new transition qualities had not yet been introduced in 2013, so *Integrated* was not specifically stated as an objective at project approval. Nevertheless, the operation aimed to provide additional container handling capacity to regionally-bound traffic, allowing for more efficient and safer operations through the heavily congested Bosporus Strait and increase the capacity to handle larger vessels (up to 18,000 TEUs). These larger ships, (known as motherships) were expected to carry containers to Asya Port, where they would subsequently be transferred onto smaller 'feeder' vessels and then transported to their final destinations, and vice versa. Therefore, the project was clearly expected to contribute to regional connectivity.

The port deals with regional transhipment only, but it receives the vessels from Greece, Italy and other countries. Almost 80% of the traffic volume is estimated to come from transhipment activities while the remaining portion (~20%) is from gateway (local) containers. The products handled include wheat, chickpeas and iron. As an example of an activity

differing from pure transhipment, wheat arrives at the Port, and is then transported to the local bakery which produces bread. In turn, this bread is brought back to the port and sent away to other locations.

The volumes and port utilisation are compared against the original Base Case forecast:

		Projected	**Actual**	**Difference**
2016	TEUs capacity (m)	*1.76*		
	Capacity Utilisation (%)	*75*	37	-38
	TEUs m utilised	*1.32*	0.69	-0.63
2017	TEUs capacity (m)	*1.9*		
	Capacity Utilisation (%)	*75*	51	- 24
	TEUs m utilised	*1.4*	0.96	- 0.4
2018	TEUs capacity (m)	*1.9*		
	Capacity Utilisation (%)	*75*	60	-15
	TEUs m utilised	*1.4*	1.1	-0.3

In 2018 throughput was 21% below projections. It is expected that 1.3 million TEUs will be handled by the end of 2019, and with the inclusion of the project extension, that 75% capacity utilisation (1.5 million TEU) will be achieved in two years (2021).

The original project and the extension are expected to further increase the volume of transhipments to the Black Sea region (Marport and Port of Pireaus) from 1.05 million TEU in 2018 to at least 1.20 million TEU in 2023.

There is a custom's point at the port, under the jurisprudence of the State Authority, but the Company helps with investigations when requested. One factor that inhibits greater capacity utilisation is the level of bureaucracy that exists. The client believes that if the government agencies could streamline their work and requirements, utilisation could be improved by up to 10%.

Asya Port's broader regional integration impact is challenging to assess as, prior to its construction, MSC utilised Marport (the main port of Istanbul) for both gateway and transhipment business. After Asya port was built, transhipment was transferred there, while most of MSC's gateway business (reception of cargo for or from Turkey, particularly Istanbul) stayed at Marport. However, Asya Port also runs services connecting it to other Turkish ports including, Gemport, Marmara, Yia, Izmir, and Mersin. Both ports – Asya and Marport, belong to the same owners. Asya port effectively serves only one client - MSC. This might be the reason why Asya port does not have any data on the routes serviced by the ships calling at its berths, as these are kept by MSC. MSC was not interviewed by EvD, however its website and the departures schedule of Asya Port indicate that vessels under the following flags call there regularly: Turkish, Panamanian, Portuguese, Liberian, and Maltese. The service routes include Marmara Sea Feeder (local transportation), NWC to/from Turkey, Turkey to East Mediterranean, Antalya Shuttle, Gioia Tauro to Turkey & Black Sea Shuttle, Turkey to Adriatic, Georgia String, Tekirdat to/from Bulgaria feeder, Turkey to Israel Shuttle, IMED (East Mediterranean and India), Tiger (King Abdullah – Yarimca – Istanbul – Asya Port – Piraeus – Port Said), Adriakia (Adriatic Ports & Turkey), and Turkey-Canada.

The Antalya Shuttle service (under the Hong Kong flag) is performed by an ultra-large container ship (300m length and DWT of 111,862. It calls at Asya Port once a week. It is not clear which of these services were added after the port's construction (contributing to Turkey's connectivity) and which were transferred by MSC from Marport. However, it is plausible to assume that most were transferred at the start of Asya port's operation. However, as TEUs of containers handled at Asya port have almost doubled since the port's inauguration, it is likely that some new routes have been added and the port has had a positive impact on expanding Turkey's connectivity.

Although the project has lagged behind the volume and utilisation projections, they have risen consistently, and Asya Port has become the first and largest transhipment port in the region. In 2018 Asya Port was classified as the fourth largest container terminal in Turkey (behind Mersin, Marport and Kumport). Its full capacity utilisation has so far been affected by subdued trade due to the adverse geopolitical situation in the Black Sea region. However, as this situation stabilises, its future prospects are positive. The assessment of this project's full regional integration impact has been hampered by the lack of data on ship routing. Its regional integration impact is rated ***moderate***.

Key findings:

- Ports (particularly these servicing one client) might not keep data on the origin or destination of ships calling at their berths, making it difficult to assess their regional integration impact;
- An important TI benchmark, supporting the diversity of Asya port's connections (capacity utilisation by third party liners), was unrealistic from the start as it runs contrary to the project sponsor's objectives. It should not have been included and it is surprising it remains a benchmark under the project extension.
- Port operations can be highly profitable, relatively resilient to changing market conditions and achieve impressive operating margins.

Operational considerations for strengthening the regional integration impact of similar future projects:

- If a port project's regional integration impact is part of the Bank financing rationale, the operation team should ensure that the client will ensure availability of relevant data on routing, origin and destination of ships serviced by such a port.
- Due diligence of port projects should include a review of the effectiveness of customs processes and how they would affect cargo movements.
- The Bank should seek synergies and complementarity among projects such as Asya Port and the Tekirdag Port.

7. Dalaman Airport – a regional airport project in Turkey, OpId 46467

Background

In 2014 the Bank provided €162 million loan (half syndicated) to finance a new airport terminal in Dalaman - southern Turkey's tourism hub. The loan was provided to YDA Havalimani – an SPV established by YDA Insaat San – one of Turkey's premier construction and infrastructure operation companies, which won a tender for the construction and operation of the terminal. Initially, the new terminal was to serve domestic passengers, however later on (loan restructuring of September 2016) its designation was changed to international terminal. The company agreed with the aviation regulator that the existing international terminal (which YDA had already operated since 2006) would be converted into a domestic one, while the new terminal would serve international traffic and both international and domestic during the off peak season. The concessioner was the first in Turkey to accept full traffic risk (previous airport concessions were based on a minimum traffic guarantee by the state). This was because Dalaman Airport has been already serving as a gateway since 1981 to well-known and high profile tourist destinations in Turkey, such as Marmaris, Fethiye, Dalyan, Kalkan, Oludeniz, Goecek and Kas.
The transition impact of the project was to be derived from private ownership of transport infrastructure, which was expected to have a demonstration effect (with a target of one more regional airport concession in Turkey based on full traffic risk), as well as by setting standards for governance and business conduct (energy performance benchmark - 30% below average, i.e. less than 160klWh/sqm, as well as obtaining LEED and ISO 50001 certificates).

Relevance

The Bank's Turkey Country Strategy (BDS/TK/12-1 (Final)), emphasises the "strengthening of regional and rural infrastructure". It also encourages the Bank to support "the Turkish Governments privatisation programme in the enterprise, financial and infrastructure sectors including through active participation in financing PPP projects". Dalaman Airport was clearly in line with these priorities. It was to be the first regional airport PPP in Turkey financed by the Bank. Energy efficiency improvement was also included in both the project and in the country strategy as one of strategic objectives.

Similarly, the Bank's Transport Sector Strategy (BDS13-205 (Final)) targeted support for "the airport management through a range of different schemes and models, such as PPPs", as well as "the development of a low carbon economy". Additionally, the Transport Sector Strategy targeted the alleviation of bottlenecks, which "hamper development of tourism" among other sectors and promote "economic diversification and regional integration". Through the construction of a new domestic terminal, the project was expected to alleviate travel bottlenecks in the region, especially during the peak summer season, as well as increasing the connectivity between Turkey's southern region and its main cities (original project - domestic terminal) and the wider world (amended project – international terminal).

Developing its airports has been a high priority for Turkish government, although it has been centred on the completion of the new Istanbul airport hub. In the last 10 years €12.6 billion has been invested in Turkish airports, although €10.2

billion of that was for the new Istanbul airport. Nevertheless, many of Turkey's 52 regional airports were also upgraded and expanded, most under PPPs. DHMI – Turkey's Aviation Regulator, presides over these airports, grants and monitors the concessions.

The Bank's additionality is considered verified based on the long-term (15 year) loan needed to finance infrastructure assets such as an airport, which was not available in Turkey. The participation of EBRD was needed due to the long tenor required, as well as the size of financing. The argument of the Bank's attributes (involvement in Turkish PPPs) was less plausible as the concession for YDA had already been granted. The project's relevance is rated ***fully satisfactory***.

Results

As per the background section above, two years after its approval the project scope was subject to a major amendment as it was decided that the existing international terminal (already operated by YDA) would become domestic, while the new terminal would be designated as international. This was due to much higher traffic expected from intentional passengers. Despite the amendment and the 13% increase in the airport's space, the price of the original construction contract remained unchanged. The amendment package also updated the traffic and financial projections of the project. The period of 2015 - 2016 has been particularly challenging for the Turkish tourism industry due to the extraordinary political events (migrant crisis, coup d'état attempt, downing of the Russian aircraft, terrorist attacks, etc.), therefore the new traffic projections for the next three years have been about 25% below the original level, however they envisage slow growth afterwards, catching up with the original projections in 2033. In EvD's view, the project, particularly the airport traffic, should be assessed based on the projections amended in 2016 as the project scope and its geopolitical environment substantially changed from what was originally approved in 2014.

The project was implemented as per the amended schedule, with a total of €375 million spent (€4 million below the original budget). The terminal has been operating since July 2018, with a capacity of 10+10 million passengers (arrivals and departures) per year, which is about four times the current traffic, i.e. it has been clearly designed with traffic growth in mind. The airport has a modern, attractive design, large commercial and food areas and it seems well maintained and managed. Its design incorporated all agreed energy efficiency features and during January-September 2019 its average energy consumption was 127 kWh/sqm, i.e. 20% better than the benchmark. The company plans to apply for LEED and ISO certificates in 2020. The project's demonstration effect is difficult to attribute but in April 2018 Cesme Alacati airport was tendered as a BOT concession, similar to that of Dalaman. The commercial success benchmark is yet to be verified based on longer term operation, however in 2018 the traffic was largely in line with the revised projections presented at amendment. Project results are rated ***fully satisfactory***.

Efficiency

2018 traffic substantially recovered from the 2015-2016 low. It was 23% above 2017 and only marginally (1.8%) below the projection. Although the traffic and financial results of Dalaman airport have been largely in line with the revised projections, the Turkish Lira devaluation caused an underperformance in EUR terms. In 2018 revenues grew 24% in TRY but declined 10% in EUR terms. Operational revenue in 2018 was slightly below the projection (€61 million projected vs. €57 million actual) mainly due to lower penetration rate in F&B and duty free facilities as a result of the TRY depreciation. The EBITDA margin improved to reach 14.4% (€15.8 million vs €-6.6 million in 2017). The financial expenses (including FX loss) of €53.1 million led to a net loss for the year of € 23.4 million and a negative equity of €1.6 million in 2018. As of 2018 year-end, the balance of the funds provided by the YDA, to support the project, was €12.3 million. The Borrower's current ratio is below 1.0x at 0.78x in 2018-YE (vs 0.94x in 2017-YE), which implies short-term liquidity issues; however this is mitigated by the Sponsor's support. Importantly, in June 2018, the airport's operator paid to DHMI a €25 million lease fee deferred from 2016-2017. Efficiency is rated ***partly unsatisfactory***.

Overall rating

The project was challenging due to the adverse exogenous environment, which hit Turkey, particularly its tourism industry, hard in 2015-2016. Nevertheless, the new terminal was completed on time, on budget and to a high standard. The terminal has been operating since mid-2018, while passenger traffic at Dalaman recovered to a level largely in line with the projections. Also, although the borrower's financial performance is generally sound, it remains slightly below

projections due to the TRY devaluation. Strong support from the sponsor mitigates any risks. The project is rated ***good*** overall.

Regional Integration impact

Regional integration was not part of this project's TI (as it was not one of the Bank's TI qualities at the time of approval). Nevertheless, improved connectivity was cited in the Board report as one of its objectives and benefits. However, no analysis of expected changes to connectivity was presented beyond general traffic projections.

In 2018 Turkish airports served 210.5 million passengers (intentional and domestic), while receiving 2 million arriving or departing flights. This represented 40% growth from 2013, however about 50% of these figures related to three Istanbul airports. Dalaman was the fifth busiest regional airport in Turkey (after Ankara, Antalya, Izmir and Adana) with 4.56 million passages served. This was almost in line with the projections (4.64 million), as was its international traffic (2.97 million vs 2.99 million projected). The Dalaman region is a prime tourist destination in Turkey, however unlike some other regional centres (Izmir, Trabzon, Gaziantep), it is not a business or industrial base. Therefore traffic at Dalaman airport is almost 100% dependent on tourism – individual or package holidays (charter flights accounting for about 50% of traffic in high season). Since the loan was signed, the project's rationale (and its potential regional integration impact) has been threatened by the collapse of Turkish tourism following the shooting down of Russian Sukhoi Su-24 in November 2015, and the coup d'état in July 2016. The country's instability has been further exacerbated by war in neighbouring Syria, the migrant crisis and terrorist attacks. Due to these developments, traffic in Dalaman airport plunged to 3.1 million in 2016 and it only began to recover during the following year to 3.7 million and 4.5 in 2018. This represented a 34% increase on the 4.1 million recorded in 2013 before the project.

These trends persisted as, in the first quarter of 2019, international air passenger volumes rose 7% across Turkey, buoyed by a weakening lira, which has made Turkey relatively cheap for holidaymakers, while the geopolitical situation has stabilised. International traffic at Dalaman airport outperformed the national average, posting 24% growth during January-April 2019. Dalaman recorded 2.48 million passengers in the first half of 2019, slightly exceeding the forecast of 2.43 million. It is likely that Dalaman airport will meet or even exceed its 2019 traffic forecast of 4.65 million. Resorts in the Dalaman region, which attract a large share of UK tourists, are enjoying a positive "Brexit effect" as, due to GBP devaluation against the Euro, more UK tourists are choosing non-Euro destinations (in 2019 Turkey overtook Greece as UK's second favourite package holiday destination). However, Dalaman's last quarter 2019 results will be affected by the Thomas Cook bankruptcy as it was the largest airline servicing this airport, with a 26% share of its international traffic. Some of Thomas Cook's routes (accounting for 13,000 passengers) have already been taken over by Jet2, and its other landing slots filled by the increase in connections with Russian destinations. However, Thomas Cook's demise is expected to have some negative bearing on Dalaman airport's 2019 results.

In terms of connectivity, following the project, Dalaman airport was able to expand its connection network to 85 world cities served in 2018 (an increase of 19 compared with 2014) and better diversify its passenger base. For example, before the project, Dalaman's passenger base was dominated by UK tourists (about 70%), which has now decreased to about 50%, while the number of UK cities connected grew from 16 to 19 (following Thomas Cook's recent demise, the share of the UK market might further decrease, although the number of UK airports connected to Dalaman will remain the same as they are also serviced by other airlines). At the same time, the share of Russian passengers doubled from 11 to 22%. Dalaman is now connected to 20 Russian cities. The share of German and Dutch traffic decreased, with only a marginal loss of connections but Dalaman obtained new routes, mainly to Ukraine (which now has seven cities directly connected to Dalaman and accounts for 6% of traffic), as well as Slovakia, Moldova, Hungary, Bulgaria, Norway, Lebanon and Iraq. It should be noted that connections, particularly by charters, are seasonal and often change. For example, since 2014 16 connections have been dropped, including three airports each in UK, Russia and Poland. Out of non-European destinations, in 2018 Dalaman serviced (mainly charter) flights to and from Jeddah, Medina, Amman, Tel-Aviv, Beirut, Baghdad, Baku and Siberian cities, such as Novosibirsk and Chelyabinsk.

Dalaman airport's traffic and its connections are primarily driven by travel agencies signing up hotels and then combining them with airline connections as a package. Thus Dalaman airport's traffic is constrained by the number of available hotel beds in the region. These amounted to 125,000 in 2014, growing by 12% to 140,000 in 2019. Moreover, DHMI stated that the Turkish government is in the process of opening many previously protected southern coastal areas to hotel development.

In terms of airlines servicing Dalaman airport, largely due to the bankruptcy of two large UK charter airlines, their structure is now much more diverse than before the project. In 2014 Thomas Cook and Monarch (both now bankrupt), together with Thompson, accounted for 56% of international traffic. Currently the largest airlines servicing international routes are Jet2 with 15% of the traffic, TUI with 13% and EasyJet with 10%. The rest of the traffic is serviced by Turkish Airlines, Pegasus and smaller Russian and Ukrainian airlines – in total 61 different airlines serviced Dalaman in 2019. Domestic traffic is dominated by Pegasus (a Turkish low-cost airline).

A large part of Dalaman's international connections is seasonal, as the tourism-oriented character of the airport justifies only this type of operation. However, during low season the number of domestic flights increases, often carrying international passengers, connecting them primarily from the Istanbul hub. The Dalaman region has been successfully marketing its unique position as an international paragliding centre (in the Oludeniz resort), attracting an increasing number of year-round enthusiasts, particularly from China and Russia. The region's marketing campaign seems to be working as Dalaman posted 24% growth in the 2019 first quarter low-season, as compared to the same period in 2018.

Overall, the project resulted in a substantial increase and diversification of direct connections between south-western Turkey and Europe and even some non-European destinations. The airport weathered the challenges of geopolitical upheavals and charter airline bankruptcies relatively well. Its traffic increased from the pre-project level by 34% and was largely in line with projections. The project's regional integration impact is rated ***strong***.

Key findings

- A stable geopolitical environment is a pre-condition to increasing tourism and therefore to realising regional integration objectives in airport projects dependent on tourism; adverse geopolitical events can have a profound impact on tourist traffic, however it can recover over a number of years if the environment improves.
- Currency devaluation can have a detrimental effect on domestic air traffic but can boost international tourist traffic;
- Overreliance on one market for tourism, particularly if dominated by one airline, is highly risky for airport operations. Reliance on the UK market, combined with the collapse of Thomas Cook (26% share of international flights at Dalaman), had a negative impact on its performance (although this has been partly mitigated by the positive impact of Brexit on overall UK tourist traffic to Turkey);
- Airports in regions reliant on tourism are particularly strongly exposed to seasonality, as well as the bankruptcy risk of smaller or charter airlines (Monarch, Thomas Cook and several German carriers);
- Integrated approach to the promotion of tourism, involving hotels, tour operators and airlines, is key for the success of regional airports and the achievement of a project's regional integration objectives.

Operational considerations for strengthening the regional integration impact of similar future projects:

- The Bank's airport projects, particularly those targeting regional integration impact, should include an analysis of the connectivity improvements expected from the project;
- Airport projects should be considered by the Bank more often as they generally present strong regional integration impact potential, because air transportation is the fastest growing mode of people transportation across borders (in addition to promoting private sector participation in infrastructure);
- The growth of regional airports (fuelled by the rise of budget airlines in recent years) presents the Bank with particular opportunities, which should be better explored.

8. Southern Gas Corridor (TANAP) – a gas pipeline project in Azerbaijan and Turkey, OpId 48376

Background

In 2017 the Bank joined the financing of the Trans-Anatolian Pipeline (TANAP), which was to become an important part of the Southern Gas Corridor (SGC) – a cross-regional mega-project for the total value of US$40 billion, designed to bring Azeri gas to Europe for the first time. The Bank provided a US$0.5 billion sovereign-guaranteed loan to SGC joint stock company, owned by the Republic of Azerbaijan and SOCAR (Azeri state oil company). The proceeds were to be used for a US$5.4 billion co-financing with the World Bank, AIIB, MIGA, SOFAZ (Azeri state fund) and UFK (Republic of Germany's guarantee agency) a US$5.4 billion for SGC joint stock company's commitments to the TANAP project,

which the main part was the pipeline stretching for a 1,850 km pipeline from the Georgian-Turkish border to the Turkish-Greek border.

TANAP is a vital part of the SGC group of projects, which includes the development of the Shah Deniz 2 gas field, the South Caucasus Pipeline (SCP and its expansion - a pipeline leading through Azerbaijan and Georgia) and the Trans-Adriatic Pipeline (TAP – crossing Greece, Albania and the Adriatic sea to Brindisi in Italy), with a total pipeline length of 3,500 km. The SGC project has been designated by the EU as a key priority for its energy security - a "Project of Common Interest". The pipeline was to enable transportation of 16 bcm/y of natural gas per year from the Shah Deniz 2 field, of which 6 bcm/y would go to Turkey and 10 bcm/y to Europe. An important technical feature of TANAP was to be its ability to expand, i.e. to enable the doubling of its capacity in the future by adding compressor stations (subject to relatively small additional investments).

The transition impact of the project was to be realised though resilient and regional integrating qualities. The former was to materialise through the introduction of a regulatory law in Azerbaijan, in line with the EU's Third Energy Package to support the establishment of an independent energy regulator, as well as through the implementation of the Compliance Action plan at the SGC company (Risk Management, Compliance Officer, ethical conduct). Finally, the government was to implement the recommendations of the Council of European Energy Regulators (CEER) developed under the TC.

In terms of integration, natural gas was to become available to Europe and Turkish regions (10 bcm/y and 5.7 bcm/y respectively by 2021), and third party access was to be introduced in line with best regulatory practices on expansion of capacity, to account for 20% of such an expanded capacity. Interestingly, although the entire investment under this project was in Turkey, the project was not classified as Turkish or Regional but Azeri (based on the borrower's domiciliation, sovereign guarantee and transition impacting mainly Azerbaijan).

Relevance

The project's regional integration focus was in line with the Bank's Country Strategy for Azerbaijan (BDS/AZ/13-1(F)), which called for *"enhanced regional trade via the diversification of hydrocarbons export routes and which favour regional integration of energy infrastructure".* The Bank was to support projects, which *"promote energy security and integration*", specifically *"investments alongside SGC".* The project was also in line with the Bank's Green Economy Transition (BDS15-196) approach as it promotes the transition to low-carbon energy, as well as with Energy Sector Strategy (BDS13-291 and its update CS/FO16-07). The latter document put the emphasis on improving energy security by diversifying routes and promoting integration.

Azerbaijan's new "Strategic Road Map" for the energy sector is still under development. However, other strategic documents, e.g. "Azerbaijan – Sustainable Development of Energy – Gaps in Energy Efficiency and Ways to Eliminate Them" (2019), make explicit reference to regional integration and the project in particular. The latter document states that "*The basis for development will be integration into global and regional value chains".* It then specifically points to TANAP as a vital part of this integration approach, which is expect to be fully realised in 2020 when TAP is completed.

The European Commission's 2014 Energy Security Strategy referred to this project as critically important to the diversification of Europe's gas supply and thus its energy security. Seventeen percent of EU's energy mix comes from gas but this is to grow to about a quarter. Europe's own natural gas resources cover about 50% of its needs but will reduce to 35% by 2025. Many countries rely on gas imports from only one supplier. Thus the SGC is of vital importance for the diversification of EU supply sources (although TAP's route was only the "second best" for the EU – see section on regional integration impact below).

In terms of additionality, the Bank was one of several IFIs financing the project. The total amount of funding required the participation of major IFIs active in the region. An 18-year maturity (critical to enable project finance-style repayment) was not available in Azerbaijan, while other IFIs were already at the limit of exposure to to TANAP.

Finally, the project was a natural continuation of four earlier projects already financed by the Bank (SCP, Shah Deniz I, II and the latter's extension), which supported the development of the gas fields feeding into the SGC and its Azeri-Georgian section, therefore it complemented the Bank's prior engagement in the sector well.

Due to its high degree of compatibility with the Bank's strategic objectives, as well as those of EU and Azerbaijan, the relevance of this project is rated ***excellent***.

Results

The loan was entirely disbursed and about 80% of its proceeds were applied retroactively to five previously signed construction contracts, as planned. The project was completed on time with substantial savings of almost a quarter of the budget (US$6.5 billion spent vs. US$8.6 billion budgeted). For this reason, financing initially considered from the UFK and EIB was not taken. In June 2018 gas started to flow to Turkey (the Eskishehir station), while a year later (June 2019) the construction of the entire TANAP to the Greek border was completed. During the first year gas was delivered to Turkey as planned and in July 2019 the throughput was doubled (information on the exact amount of gas delivered is confidential). The target throughput of 5.7 bcm/y is to be achieved in July 2020. According to TANAP and SGC companies, all required infrastructure is in place to receive this amount of gas, as well as to accommodate additional gradual throughput of 10 bcm/y when TAP is ready in 2020.

In 2016, as part of the preparations for financing TANAP, the Bank signed an MOU with the Azeri government on the establishment of an energy regulator. The AERA (the Azerbaijani Energy Regulatory Agency) was established by the President of Azerbaijan in 2017 and is now operational with 200 staff. Since then the Bank has led IFI efforts to support the development of a regulatory legal framework and build capacity at AERA. So far, several workshops have been organised with CEER (Council of European Energy Regulators) on specific topics of regulation, and a TC assignment was launched devoted to: i) drafting a regulatory law, largely in line with the EU acquis and ii) training AERA's staff. The latter is under implementation and so far there have been two engagements, with Azeri regulators trained by Dutch and Latvian colleagues.

The draft regulatory law was prepared under the Bank's TC co-managed by LTT and EPG and currently (October 2019) it is at an advanced stage of approval (government consultations completed). The consultants are working on a consolidated version integrating the latest comments received by state agencies and market players. The law is to be officially submitted to the Cabinet of Ministers and Presidential Administration in late 2019/early 2020. Although the law was prepared largely in line with the EU's Third Energy Package, the Ministry of Energy commented that Azerbaijan is not yet ready for such package, which might be adopted only in the long term. One of the key achievements of the Bank's policy dialogue was a decree issued by the President of Azerbaijan in May 2019, which sets a clear target for the adoption of the regulatory law, alongside other sector legislation, by early June 2020. Considering the lengthy consultation and approval process, this decree can be considered as a clear declaration of political support for the new law (although its provisions related to Third Energy Package are likely to be diluted).

The approval of the new law is highly important, as currently the regulator reports to the Ministry and is not independent. The new law changes this, ensuring its independence, i.e. the appointment of its Head by the Republic's President and its financing by fees paid by energy market participants. The Council of European Energy Regulators (CEER) has been working on the preparation of operational recommendations for AERA. It is not yet clear whether they will be implemented but cooperation is reportedly going well.

Another ongoing TC related to this project supports the Azeri authorities on the design and implementation of an auction for renewable energy projects. Auctions are the primary mechanism envisaged under the RES Law for supporting RES investments (the Bank did not participate in drafting this law but was consulted on the draft and provided substantial comments, most of which were adopted). This TC only started in September 2019, so its results are not yet known. The outcome of the TC is seen as relevant for the TANAP project because if RES are to play a more prominent role in the Azeri energy generation mix, more gas will be available for export.

SGC company confirmed the implementation of corporate governance improvements (risk management, compliance officer and ethical conduct code), which were conditions precedent to loan effectiveness the Bank's loan. Moreover, the SGC company signed an information sharing agreement with the newly established Azerbaijan Commission on Transparency in Extractive Industries to provide reports as required by this commission. As to third party access (final 2 TI benchmarks), it will be possible to verify their achievement only if and when TANAP and TAP are expanded (for now all their capacity has been booked for 25 years and access of a third party would not be technically possible).

According to all stakeholders the expansion is highly likely to take place (see the regional integration section below). Although, as stated in the Board report "TANAP's expansion is dependent on the availability of additional gas beyond the currently committed 16 bcm/y of gas produced by Shah Deniz 2, which might come from Azerbaijan and/or from other suppliers around the Caspian sea", SGC confirmed that proven reserves of gas in Shah Deniz 2 field are above 1.3 trillion cm, while a demand test conducted by TAP (see below) confirmed high additional demand for Azeri gas. Therefore the probability of the TANAP extension materialising is seen as high. If this happens, third party access will be granted in accordance with EU regulations but applicable only to the expanded part (TAP obtained an exception from EU third party access regulations for its initial 10 bcm/y capacity). However, EvD notes that in response to DAQs, Banking stated that a *"set of third party access rules should be developed and adopted before the expansion decision for TANAP is made. Adopting these rules, would have wider applicability than the specifics of this project"*. Although so far, there is no evidence of the Bank working towards "wider application" of third party rules in Turkey or Azerbaijan, the TI benchmark for it is only 2026. Therefore one could argue that it would have been premature working on it now.

Beyond TI benchmarks, the construction of TANAP made a positive contribution to the Anatolian economy. 13,000 people were employed during construction and the company implemented a comprehensive Social and Environmental Investment Programme (SEIP) along the pipeline's route, with a budget of US$84 million, encompassing over a thousand diverse projects. Key achievements of this programme included the provision of clean drinking water to 91 villages, irrigation systems for 23 villages, equipping of ambulances for 33 hospitals, training of almost two thousand teachers and provision of a programme for children with autism. Some other villages were provided with waste disposal equipment or solar energy generators. Disadvantaged groups and women were prioritised. In terms of land acquisition, out of 21 thousand parcels, 55% were purchased through amicable settlements, while the remainder of the owners asked for higher compensation and acquisitions were settled through court suits. The pipes have been buried underground (or under water) throughout the whole length of TANAP and are not seen as a major risk for the environment. Part of the EBRD's added value to the project (highly valued by other IFIs) has been the commissioning of an integrated environmental and social monitoring team.

The physical implementation of this project was successful, even exemplary. However, there are still uncertainties related to most TI benchmarks, partly because these related to Integrated quality are due only in 2021 – one and 2026-two (the regulator is not yet independent, the law is not yet approved and is unlikely to be fully in line with the EU's Third Energy Package, while the achievement of some other benchmarks will be possible only if TANAP expands). All of these are likely to happen in the future. With some caveats (and taking into account the early stage and likelihood of future developments), the results of this project are rated ***fully satisfactory***.

Efficiency

It has been projected that TANAP will produce its first positive cash flow in 2020 and SGC is on track to achieve this milestone. This category ***is not rated***.

Overall rating

The project was very well executed, on schedule and with substantial savings (although to a large extent they were the result of currency devaluation). Importantly, the SEIP implemented alongside pipeline investments introduced many benefits for affected communities. The Bank engaged with the government on the establishment of the energy regulator and the preparation of regulatory law. The law has not yet been approved and might not be fully in line with EU standards, however the chances for its approval are high due to the Presidential decree. The achievement of other TI benchmarks is dependent on the pipeline extension (which is likely but not yet decided) and will be verifiable only after 2026. Overall the project is rated **good**.

Status of associated projects

In total, the Bank's financing of Azeri gas field developments and different parts of the SGC amounts to US$2.38 billion. During 2005-2015, the Bank provided five loans to develop the Shah Deniz 1 and 2 gas fields (US$810 million in aggregate) through financing of Lukoil, one of the field's shareholders. All projects were implemented and contributed to the availability of gas for TANAP and TAP. In 2005 the Bank also provided US$70 million loan to Lukoil for South Caucasus Gas Pipeline (through Azerbaijan and Georgia), which enabled TANAP and TAP. Most of Lukoil loans have now been repaid.

In 2018 the Bank provided EUR$1 billion (half syndicated) for the Trans-Adriatic Pipeline (TAP). The loan will co-finance funding from a number of IFIs to construct a 878 km pipeline linking TANAP's westernmost end at the Turkish-Greek border, through Greece, Albania and under the Adriatic Sea to Brindisi in Italy, where it will connect with the Italian (and European) gas network. As of October 2019, 90% of the pipeline had been completed (all land route), with the marine pipe being laid. TAP will carry 10 bcm/y. Out of the Bank's COOs, Greece booked 1 bcm/y and Bulgaria 0.94 bcm/y. The rest of TAP's capacity was booked by energy majors from France, UK, Germany, Italy, and Switzerland. However TAP will have a physical "reverse flow feature", so theoretically companies from these seven countries could sell part of its gas to other countries, benefiting some other COOs. However, the stronger integrating impact of TAP will only be realised if and when it is expanded. Both TANAP and TAP are designed to expand relatively easily but will require major investments, although at a lower level than the current projects (very early estimates of investments required to expand TANAP are about US$ 1 billion and the time to complete them four years). Demand tests conducted by TAP confirmed eight additional parties interested in purchasing gas (although confidentiality prevents it from disclosing from which countries). However, it is likely that countries such as Albania (TAP features two exit points in this country) and North Macedonia indicated their interest in receiving Azeri gas. Moreover TAP is setting the foundation for a northward Ionian-Adriatic Pipeline (IAP) through Montenegro, Bosnia and Croatia (total 5 bcm/y planned), which is planned as the gateway for Azeri/Caspian gas to the Western Balkans. TAP is seen as a backbone of the West Balkan Ring, a multi-project initiative aimed at creating a regional gas market (see "Future integration potential" section below for more info).

The TAP project's TI is centred on closer integration of the Albanian gas system with that of EU. The Bank contributed to the Gas Master Plan (prepared under the EU-financed WBIF project), which developed a strategy for a sustainable and interconnected gas system in Albania. The EBRD's TC supports the development of and capacity building of the legal and regulatory functions of Albgaz, the newly established transmission and distribution company. Albgaz is to play a critical role in the maintenance of TAP but also in the future gasification of Albania. Consultants started work in mid-2018 and, according to Banking, their work is on track. TAP also provided €6.7 million investment support for a project to develop of gas connectivity.

Regional Integration impact

Regional integration was an important part of the project's relevance. The President's Recommendations stated that *"the project will facilitate integration of regional gas markets through cross-border energy transportation…."*. The Board report emphasised that the project was to *"interconnect regional markets, unlocking gas to European consumers"*. The project was expected to *"foster international cooperation across countries along the SGC, which would fuel regional development", "assist in the creation of an integrated well-functioning European gas market and contribute to cross-regional trade and connectivity".* Also, the "soft" integrating potential of the project was emphasised, i.e. *"establishment of an independent regulator in line with the European best practices and support for the development of RE potential".*

The project was a part of cross-regional value chain, enabling the export of natural gas from Azerbaijan to Europe via Georgia, Turkey, Greece and Albania (under TAP), i.e. affecting five of the Bank's COOs and facilitating broader regional integration of European energy systems. However, the integrating impact of TANAP itself can be discerned in relation to Azerbaijan and Turkey only.

Azerbaijan

There is evidence that, through this project, the Azeri energy system has moved closer to European standards, although as of now (October 2019) this process is not yet complete. The Bank supported the creation of an energy regulator, absent prior to the project, building its capacity and drafting an energy law, largely in line with EU acquis, although the Ministry stated that Azerbaijan was not yet ready to fully adopt the EU's Third Energy Package but it is likely to do it in the long term. The law is in the final stage of approval and its chances of being accepted are relatively high as the President's decree requires its approval by mid-2020 at the latest (see "Results" section above for more details). Importantly, TANAP ensured that infrastructure exists, enabling Azeri gas to reach Europe's geographical boundaries for the first time, therefore TANAP physically connects Azerbaijan to Europe.

Turkey

40% of Turkey's energy is generated from gas, which is entirely imported (c.50 bcm/y). The anticipated 6 bcm/y to be transported here by TANAP will account for about 12% of its current natural gas demand. This demand is to grow to 72 bcm/y by 2023. Fifty-five per cent of Turkey's imported gas comes from Russia and the balance from LNG supplies. In

addition to the existing Blue Stream and West Gas Pipeline, Russia is completing the construction of TurkStream under the Black Sea, which will provide 32 bcm/y to Turkey (although according to the Ministry of Energy of Turkey, this gas will replace existing Russian gas supplies). Gas from TANAP is seen in Turkey as important for diversifying supply, however the Ministry stated that no change is expected in the Turkish gas market as a result of its arrival. Nevertheless, several supply contracts from Russia expire in 2021 and having TANAP (and its expansion option) may help in negotiating advantageous prices for their extension. Gasification has been a priority for Turkish government in recent years. In 2002 only about 10 major cities had gas, while now 60% of the Turkish population has access to gas. Gas from TANAP will be pumped into the network and may benefit all Turkish regions.
No "soft" integrating measures were planned or undertaken in Turkey as part of the project. The Turkish Energy Market Regulatory Authority (EMRA) was established 15 years ago and reportedly operates in line with EU standards, ensuring full transparency of tariff-setting. It is understood that in Turkey the barriers to third party access are more technical (availability of gas and pipeline capacity), rather than legal (according to the Ministry, anyone can get a license if gas is available). However, all gas to be transported through TANAP has already been contracted for 25 years, i.e. there is currently no room for a third party.

Other countries
In 2014 natural gas accounted for 17% of the European energy mix (with a total consumption of 490 bcm/y) but this share is projected to grow to 22% by 2030. About 50% of Europe's gas is imported (20% LNG, mainly from Algeria and 30%, by pipelines from Russia – the latter 171 bcm/y on average). It is projected that by 2030 Europe will require imports of 390-400 bcm/y. TANAP has paved the way for TAP, which potentially could have a stronger integrating impact among other COOs. TAP has not been completed as of the writing of this report and therefore has not been reviewed under this cluster evaluation (its completion is expected in 2H2020, see Associated Projects section above for more info). TAP is expected to affect the Greek energy system, as Greece is TAP's main host country and is to receive 1 bcm/y of gas. It can be stipulated that TAP will integrate the Greek gas system closer with that of the EU as it will connect it to the EU system though Italy. Moreover, the construction of a Greece-Bulgaria gas interconnection has been confirmed (to be financed by EIB). Bulgaria will receive 0.94 bcm/y of gas per annum through TAP. There are no clauses preventing interconnectivity in TAP's purchase agreements (i.e. on the destination of gas from TAP), therefore it is theoretically possible that other COOs might receive Azeri gas from Greece or Bulgaria. Unlike TANAP, TAP is subject to EU regulations, however it obtained an exception from key aspects of these regulations - third party access and ownership unbundling rules.

EvD notes that in its current form TAP is only the "second best" for the EU and by going to Italy and supplying primarily West European markets, it somewhat delayed EU's hopes for integrating the central European gas systems more closely with that the core EU system. During 2002 - 2013 the EU Commission strongly supported the plan to build the Nabucco pipeline, which was designed to take Azeri gas from the Turkish-Greek border to Bulgaria, Romania, Hungary, to a hub in Austria (where it could be further interconnected with the gas systems of Slovakia, Czech Republic or Poland). Nabucco would have benefited more COOs than TAP. However, reportedly the much higher costs of Nabucco, compared to TAP (and allegedly political considerations), led to TAP being selected as the preferred route to deliver its gas to Europe. However, eventually, the future expansion of TAP and potential interconnections (see below) might yet bring Azeri gas to some central European countries.

Future integrating potential
TANAP has been designed to be expandable to 31 bcm/y and TAP to 20 bcm/y. Subject to the availability of gas, its transit through TANAP to Europe could double to 20 bcm/y and off-take by Turkey could increase to 11 bcm/y. TANAP's throughput could be increased with the addition of five compressor stations, at a cost of about US$ 0.8-1 billion. Additional work would take four years to complete. The SCP (Azeri and Georgian part of the pipeline) would be able to accommodate increased throughput. Should TAP be extended by another 10 bcm/y (which is likely, given that demand from eight companies has been confirmed following several recent tests), Albania would be the most likely COO to receive gas through the extended TAP/TANAP (and could potentially sell it further to Kosovo). At this time there are a number of ongoing studies (financed by the EU's WBIF) to assess the feasibility of interconnections between an extended TAP and other Western Balkan countries through the Ionian-Adriatic Pipeline (IAP), such as Bosnia and Herzegovina, Montenegro and Serbia, as well as Croatia. However the feasibility of the planned 516 km, reverse-flow, 5 bcm/y IAP is still some way off as it might not be economically viable without a large EU grant. Moreover, Bosnia and Herzegovina lacks the required legislation to accommodate a new pipeline. It is also unclear which companies/countries

expressed interest in contracting additional gas from the extended TAP as commercial confidentiality applies at this stage. Other interconnections possible in the case of TAP's expansion include Bulgaria-Serbia and Bulgaria-Macedonia and a further pipeline into Hungary. SGC is seen as an important part of the Energy Community West Balkans Gas Ring – a gas ring connecting different countries in the region. This EU initiative is designed to create a regional 12 bcm/y gas market by 2040.

It should be noted that the planned follow-on projects to bring Russian gas from TurkStream into Europe include the Tesla Pipeline, to run from Greece to Northern Macedonia, Serbia and Hungary, ending at the Baumgarten gas hub in Austria; and Eastring, intended to carry gas north via Bulgaria, Romania, Hungary and Slovakia. EvD notes that these are similar routes to those designated for the abandoned Nabucco pipeline, which was originally meant to carry Azeri, rather than Russian gas to Baumgarten through these European countries.

Finally, in the longer term, TANAP (as part of the larger SGC) might play some role in unlocking vast Turkmen gas resources to supply Europe. A declaration on the use of the Caspian seabed (a prerequisite for the Trans-Caspian pipeline) was signed this year between Azerbaijan and Turkmenistan.

Overall, TANAP/TAP's integrating impact could be viewed as moderate, particularly as compared to Russia's TurkStream (32 bcm/y designed to supply gas to Turkey, Bulgaria and Serbia). In total, at its peak capacity, SGC will provide less than 10% of the gas supplied to Europe by Russia. The regional integrating impact of TANAP itself can be seen as mainly that of enabling further interconnections (the extent of which depends largely on the TAP's currently undecided future expansion). Nevertheless, TANAP did physically connect Azeri gas fields with Europe for the first time. The outcome of the project's "soft" integrating measures is also still unclear. The Azeri regulatory law, prepared under this project, is unlikely to be fully in line with the EU Third Energy Package and it has not yet been approved. It is also noted that while the EU gas regulatory system (under the Third Energy Package and Gas Directive EC2009/73) promotes liberalisation through ownership unbundling and third party access, TAP (important for enhancing TANAPs regional integration impact) obtained an exemption from unbundling and third party access rules (for initial TAP's capacity). This might be beneficial for SGC but limits this project's regional integrating impact. Therefore, such current impact of TANAP project is rated *moderate*, with future potential to become *strong* in the event of its expansion and Azerbaijan's the full adoption of an EU-compliant energy regulatory regime.

Key findings

- The regional integration transition objectives of pipeline projects (particularly their upstream sections) can often only be fully realised through incremental investments into their downstream sections;
- Gas transmission companies may seek exceptions from the liberal EU gas transmission regulations. This may enhance their credit but limits the regional integration impact potential of the projects;
- Third party access – a keystone of EU gas transmission regulation, may be legally permitted but technically impossible to execute.

Operational considerations for strengthening the regional integration impact of similar future projects:

- If the Bank finances incremental pipeline investments, care should be taken not to "double-count" regional integration benefits stemming from one or the other project. The dependence of TI on a subsequent project materialising should be clearly explained;
- Regional integration and energy supply security are different concepts. Although they could be complementary, they should not be mixed and each needs to be separately and clearly articulated in the project's TI structure.

9. Port of Split – a port project in Croatia, OpId 42542

Background

In 2012 the Bank provided an €18.8 million sovereign-guaranteed loan (increased by €5.6 million in 2014) to the Port of Split Authority (PSA) to extend and reconfigure the passenger wharves at the port of Split to improve cruise and ferry operations and to enable their growth. The port of Split is the largest port in Croatia in terms of passengers served and

the third busiest in the Mediterranean. The loan was to finance the extension of wharves and dredging of the seabed to enable access by larger cruisers. Redeployment of the ferry port to the northern port was also part of the project.

The key objective was to enable longer cruise ships with a greater draft to berth at the port, as previously they have had to anchor in Split bay, with passengers ferried to the city by smaller ships. This limited Split's attractiveness to cruising companies and left the PSA unable to charge more than half of the berthing fees. The mid-size cruisers berthed at Ro-Ro wharves, limiting their access for ferries (including international ones, connecting Split with Ancona in Italy).The alleviation of congestion in the southern part of the port was another objective. It was to service mainly cruise passengers, while the ferry port was to be relocated to the northern port of Split. As part of the project, a TC (financed by PSA) was to support a PPP tender for the construction and operation of a passenger cruise terminal at the port. Another TC was to support the implementation of environmental and corporate governance improvements at the PSA.

The transition impact of this project was based on increasing private participation in the provision of port services (organisation of the PPP tender for the terminal), as well as the demonstration effect of the acquisition of Ecoport status by the port of Split, as well as improved corporate standards (introduction of IFRS and MIS, development and implementation of a five year business plan).

Relevance

Regional integration was not an objective of this project, however the enhancement of international cruise and ferry links was implied, as extending the wharves was to substantially increase the number of large-size cruise ships calling at Split. The rearrangement of the port and relief of the Ro-Ro terminal (occupied now by mid-size cruise ships) was to enable better and more frequent ferry services, including from Ancona. This was ultimately to improve the international connectivity of the middle-Adriatic Croatian coast. Moreover, the relocation of the ferry port to the north was to improve ferry operations and increase frequency of their services, enhancing connectivity between the mainland and many Croatian islands.

The tourism sector's contribution to Croatia's GDP has been growing, increasing from 11% in 2011 to 20% in 2017, with foreign tourists accounting for about 85% and their number growing at about 8% annually in recent years. The Croatian coast is the major draw and development of Croatia's ports is one of the government's key strategic objectives. The Ministry of Maritime Affairs, Transport and Infrastructure included Split on the list of six ports of "national importance" and the improvement of its infrastructure was included in the Pre-Accession Maritime Transport Strategy of the Republic of Croatia (2005). This strategy envisaged the building of the cruise terminal in Split under private concession, as planned under the project. Moreover, in accordance with the "Croatian Tourism Development by 2010", Split has been focus of the Croatian government's effort to promote cities outside the most popular tourist hubs of Dubrovnik and Istria.

The project was also broadly consistent (although less closely) with the Bank's strategic objectives. The Country Strategy for Croatia BDS/CR/10-1 (Final), called for the Bank to seek opportunities to finance the modernisation of national and local transport infrastructure. The Ports section of the Transport Operations Policy 2005-2008 (BDS04-072 (Final)) concentrated on institutional and financial strengthening measures when lending to state owned port authorities with a view to paving the way for engaging the private sector in their future terminal operations. Although EvD notes that support for the cruise sector was not specifically mentioned in any of the Bank's strategies, tourism was to be targeted in Croatia as one of the priorities, i.e. "*In the tourism sector, the Bank will support capacity building, privatisation and foreign direct investment*". This project was the Bank's third investment in cruise port infrastructure in Croatia (with loans to the ports of Dubrovnik and Sibenik signed in 2005 and 2010 respectively). Therefore it is considered that it was a relatively good fit with the Bank's broader objective to improve cruise port infrastructure in Croatia and support its tourism sector.

In terms of additionality, a 15-year maturity with a four year grace period (required due to the asset life of wharves) was not available from local banks. The World Bank and EIB financed mainly large scale transport corridor projects in rail and road sectors, which left a niche for the EBRD to finance smaller size investments to upgrade regional transport infrastructure.

Relevance of this project is rated ***fully satisfactory***.

Results

The preparation of the tender for marine infrastructure works took longer than expected and in the meantime Croatia joined the EU. This had an important bearing on the cost of the project as the technical specifications of the new wharves had to comply with EUROCODE. This resulted in the winning bid exceeding the cost of earlier estimates and the client had to request an €5.6 million loan increase, which was approved by the Board in April 2014. The works started in October that year and were completed in March 2017, which was only one month later than the original plan. The port has been operating since, receiving large cruise ships, which now can berth at two wharves. This improvement has resulted in a slight increase in the number of ships and cruise passengers visiting Split, although the number is about 30% below the forecast at approval (see integrating impact section below).

The relocation of the ferry terminal to northern Split has not yet taken place, as it was concluded that it would lengthen the journey. However, as cruise ships can now berth at the new, dedicated wharves, access to Ro-Ro wharves has been entirely allocated to ferries, which has slightly relived congestion at the ferry port.

The PPP for the cruise terminal has not been initiated yet as legal challenges regarding property rights to the land where it is to be built took a long time to resolve. Nevertheless, the PSA reported that it has now been resolved and the construction of a cruise terminal is again being considered. It is urgently needed to house border control, customs and offices. The University of Split is currently preparing a study on different options for creating the terminal, including PPP, although the PSA believes that with a terminal fee (payable to a private operator) the port of Split would be less competitive. Therefore it is still uncertain whether this PPP will happen.

The achievement of other TI benchmarks has been partial. IFRS accounting was introduced. Also the five year business plan was approved and implemented. Standard MIS has not been implemented but another system (CIMIS), tailored for all Croatian ports is under implementation. However, the achievement of Ecoport status and the approval of PERS certification have been delayed due to the need to collect data over a longer time period. EMS certification was obtained for “soft measures” only (education and publicity).The PSA does not expect to achieve environmental results above the required EU emission standards due to the need to sustain and even increase the frequency of ferry services to the islands (and ferry ships are often old, with diesel engines). Moreover, larger cruise ships, which now call more frequently at Split increase pollution. The PSA plans to incentivise cruise operators to reduce pollution by charging higher fees to those ships, which exceed pollution norms. This may also apply to domestic ferries in a few years.

In conclusion, the results of the project implementation have been generally positive as the key component – the new wharves for large cruise ships, has been completed on time, although exceeding the original budget by a third. However the achievement of TI benchmarks has been relatively poor. The most important one – PPP for a cruise terminal, has not been realised and its future prospects are uncertain. Corporate governance benchmarks have been achieved, however those related to environmental performance (demonstration effect) have failed. It was particularly disappointing as part of €0.25 million of the Bank’s grant was spent on TC to assist the PSA in improving environmental management of the port. The current results of the project are rated ***partly unsatisfactory***.

Efficiency

PSA’s most recent available accounts for 2017 indicate substantial underperformance in comparison with the projections. The total revenues were 33% lower than projected (€5.7 million, vs €8.6 million forecast), while operating expenses were 28% higher than projected (€4.9 million vs €3.8 million projected). This resulted in a squeeze on operating cash flow, which was 15x lower than expected (€0.3 million, rather than €4.6 million). Capital investments were over four times the level expected (€1.8 vs €0.4 million planned). This left PSA finances dependent on subsidies from the Ministry of Maritime Affairs (MMA). Such subsidies are now recorded off-balance and their level was not clear. However, the PSA confirmed that the MMA has been contributing to its investments and repaying 70% of the EBRD’s loan (PSA was repaying 30%, however cash for that share must have been coming from MMA’s subsidies).

The Bank’s PSA revenue projections included “concession revenues”, in principal from the cruise terminal (15% of the total revenues), however the terminal’s concession did not take place. Moreover, PSA stated that cruise ship traffic projections were somewhat inflated by the consultant to demonstrate PSA’s ability to repay the loan on its own, however it was clear from the start that they were unrealistic.

In conclusion, the financial performance of the borrower has bene well below the forecast. The Bank's loan is being serviced, however not by the PSA as presented in the Board report, but by the government. This category is rated ***unsatisfactory***.

Overall rating

The Bank's investment in the port of Split was relevant and it took place largely as planned. However its impact on the increase of cruise ship and passenger traffic has so far been well below expectations (although they were artificially inflated). This contributed to the borrower's financial performance being well below what was forecast. Also, the project's transition impact results were very modest. Private participation and environmental certification did not happen. Overall, this project is rated ***acceptable***.

Results and status of associated projects

The Bank financed similar projects (extension of cruise ship berths) at two other Croatian ports:

Port of Sibenik Infrastructure Rehabilitation Project (39749)
In 2008 the Bank signed €12 million loan with the Port of Šibenik Authority (PSA) to extend its cruise ship berths and reconfigure the passenger wharves, in order to increase the port's capacity and allow for more efficient processing of the island ferry traffic and the entry of medium sized cruise ships into the port area. The transition impact was to be derived from private sector participation (tender for the construction and operation of a new passenger terminal), as well as the strengthening of PSA's management through the implementation of an MIS to cover financial reporting, traffic analysis and projections, investment planning, etc. The MIS system package prepared for PSA was to be replicated by other small and medium sized local ports in Croatia.

The extension and reconfiguration of the passenger wharves was completed in 3Q 2014 as planned. The PSA has also launched a tender for a concession of a passenger terminal (to be built), however it was not successful due to lack of interest from private companies. A Croatian version of an MIS (CIMIS, similar to Split) was introduced. The number of ferry passengers has increased from 2015 onwards, compared to the total number of passengers (5,000) handled by the port in 2007. Nevertheless, these remain significantly below base case projections – less than half of the projected numbers for ferry passengers and 30% less than forecast for cruise passengers. Regarding cruise passengers, traffic figures show significant oscillations, with an increase in 2017 as the Company activated one additional berth for vessels longer than 240 meters, which can carry a larger number of passengers. The lower than expected number of passengers may be due to the absence of a passenger terminal. The PSA expects cruise traffic will increase once this terminal - of a smaller size under the revised PPP - is constructed.

Table 1. Passenger traffic figures for the 2016-2018 period ('000)

	Ferry		Cruise		
	Base Projections	Actual	Base Projections	Low Case Projections	Actual
2016	616	276	38	29	12
2017	647	285	44	36	28
2018	680	290	51	40	36

Port of Dubrovnik Infrastructure Modernisation (13451)
A €32.7 million sovereign loan provided to Dubrovnik Port Authority (DPA) in 2005 to extend its cruise berth to accommodate larger cruise ships. Civil works were completed in October 2011. An institutional strengthening TC reportedly achieved its main objectives of introducing International Financial Reporting Standards which, together with the marketing and business planning TC modules, established a management information system at the DPA.

Regional Integration impact

It was assumed at approval that the project would have a "catch up effect", i.e. larger vessels that were previously prevented from accessing the port due to congestion and draft restrictions could be accommodated, so cruise companies which had not previously docked at Split would rush to catch-up with the others. Therefore the total number of cruise passengers was forecast to grow 2.5 times over seven years, from 180,000 in 2011 to 450,000 in 2018,

reaching 0.5 million in 2019 and then growing more slowly to 0.75 million by 2025. Similarly, domestic ferry passenger traffic was to grow from 3.6 million in 2011 to 4.5 million in 2018, while international ferry passengers were to increase from 0.3 mil. to 0.47 mil. in 2018.
It proved to be relatively easier for domestic ferry operators to increase the frequency of their services and therefore their passenger traffic, which in 2018 slightly exceeded the projections (particularly as no catch-up effect was forecast for them). However, the project's main objective (and PSA's main revenue driver), i.e. substantial cruise ship traffic increase, did not materialise, see table below.

Traffic levels at the port of Split before the project, projections and actual

	2011 – base year	2018 – forecast	2018- actual	Forecast/actual
Domestic ferry passengers ('000)	3,595	4,500	4,900	+8%
International ferry passengers ('000)	308	475	180	-62%
Cruise passengers ('000)	181	450	320	-28%
Cruise ships received	252		264	No forecast, 5% increase

Based on berthing already contracted for 2019, the PSA now forecasts 285 cruise ships and 350,000 cruise passages for 2019, which will be 30% below the 0.5 million forecast at approval.

The PSA explained that the cruise passenger growth forecast prepared by the Bank's consultants was considered unrealistic even at the time of its preparation. However, it was prepared as such to demonstrate PSA's ability to service the Bank's loan on its own (without the government's help).

It is surprising the Bank did not verify these projections better, since the Lessons Learned section of the Board report stated that *"the key lesson for the sector learned from previous evaluations of port projects is the need for carful assessment of future traffic levels".* However, the traffic risk and over-optimistic forecast was picked up in the Credit notes to the Final Review (29.5.2012), which stated: *"Traffic risk is elevated and growth projections predicted on catch-up effect".* It pointed out the 2014-2015 projected traffic increase of 20-22% as a result of unrealised demand, despite a significant exposure to the strained Mediterranean market being the primary risk facing the project.

Despite a substantial shortfall in actual cruise ships' passenger visits, PSA maintains that the project was hugely beneficial for Split's connectivity. The large cruise ships can finally berth at the port and their passengers can safely and securely disembark. This encourages them to explore Split on daily visits, which contributes greatly to the local economy. Importantly, the PSA can now charge the full berthing tariff. Of 46 main cruise ship companies operating in the world, 36 of them have ships, which call regularly at Split (all of those operating in the Adriatic).
The number of ships calling at Split increased only marginally (4%) between 2011 and 2018, however those calling now are much bigger, which is reflected in a 20% increase in passenger numbers. Also the quality and frequency of domestic ferry services benefited from more available space. In 2018 they ferried 811,000 vehicles, including 183,000 heavy trucks, while their passenger numbers increased 36% from 2011, slightly above the forecast. However, international ferry traffic has been highly disappointing, dropping by 41% from the pre-project level (and missing projections by 62%). There is clear explanation of this result, beyond the speculation that the increase in prices in Croatia, in its run up to the EU accession, rendered it less attractive to day-trippers from Ancona.

There are no statistics regarding the country of origin of cruise ships tourists, although this may change as the University of Split has been contracted by the city to research the impact of the cruising industry on the city of Split, including its environment.
Due to the lower than projected (although slowly increasing) number of cruise passengers and substantially lower number of international ferries, partially balanced by the increased traffic from domestic ferries, the regional integration impact of this project is rated *moderat*e. The current state is not expected to change dramatically in the foreseeable future.

Key findings:

- Regional Integration, for example, accession to the EU, can result in higher project costs due to the need to comply with more stringent technical and environmental requirements (as the port of Split learned);

- Tourism traffic projections for some of the Bank's cruise port renovation projects have been substantially overestimated. The international tourism market (particularly sea cruising) is highly volatile. Many attractive destinations in the Bank's COO are relative new-comers and have to compete with established locations.
- The "catch-up effect" factored into the traffic projections for some port projects has not materialised.
- Implementing more ambitious TI objectives for port projects has been difficult. PPP suffered due to property rights issues, while environmental objectives turned out to be unrealistic.

Operational considerations for strengthening the regional integration impact of similar future projects:

- Port investment projects, which aspire to increase regional integration, should include diagnostics of cruising and/or ferry companies to verify their future plans regarding specific port of call.
- Avoid including "catch up effect" in traffic forecasts for tourism-related projects.
- Apply a very cautious approach to consultants' projections of tourism-related traffic. The tourism market is highly volatile, while many attractive places in the Bank's COOs are not yet established as prime tourism destinations.

Table 1. Summary of evaluation rating of cluster projects

Cluster Project, Country	Relevance and Additionality	Results	Efficiency	Overall Performance	Reg. Int. Impact Current	Future
1. Corridor Vc Bosnia & Hercegovina	Excellent	Fully satisfactory	Excellent	Good+	**Weak**	**Moderate**
2. Corridor Vc Croatia	Fully satisfactory	Fully satisfactory	Partly unsatisfactory	Good-	**Weak**	**Moderate**
3. Azeri Roads Rehabilitation Azerbaijan	Fully satisfactory	Partly unsatisfactory	Fully satisfactory	Acceptable	**Strong**	**Strong**
4. Pan-European Highways Ukraine	Excellent	Fully satisfactory	Fully satisfactory	Good	**Weak**	**Moderate**
5. DCT Gdansk Poland	Excellent	Fully satisfactory	Excellent	Outstanding	**Strong**	**Strong**
6. Asya Port Turkey	Fully satisfactory	Fully satisfactory	Partly unsatisfactory	Good-	**Moderate**	**Moderate**
7. Dalaman Airport Turkey	Fully satisfactory	Fully satisfactory	Partly unsatisfactory	Good-	**Strong**	**Strong**
8. Southern Gas Corridor Azerbaijan	Excellent	Fully satisfactory	Not rated	Good	**Moderate**	**Strong**
9. Port of Split Croatia	Fully satisfactory	Partly unsatisfactory	Unsatisfactory	Acceptable	**Moderate**	**Moderate**

ANNEX 3: Transport projects with cross-border components signed by the bank in the 1990s

Project	Country	Year signed	€ million
Highways			
European Roads Rehabilitation (corridor 4)	Romania	1993	84
Transit Roads (corridor 10)	Bulgaria	1993	45
International Road Corridor (corridor 4)	Slovakia	1993	15
Motorway Development (corridor 3, Krakow-Katowice)	Poland	1993	45
M1-M15 Motorway (corridor 7, Budapest-Bratislava)	Hungary	1993+1999	66+64
Transport Project (corridor 10)	Lithuania	1994	20
Belavtostrada (corridor 2, Polish border-Russian boarder)	Belarus	1994	50
DARS –Company for Motorways (corridor 10)	Slovenia	1994	33
Highway Reconstruction (corridor 10)	Croatia	1995	36
M5 concession BOT (corridor 10, Budapest-Szeged)	Hungary	1995	95
Via Baltica (corridor 1)	Lithuania	1996	24
Road System Restructuring and Rehabilitation (corridor 4)	Romania	1996	90
Motorway Upgrade and Tolling (corridor 4, Bucharest-Pitesti)	Romania	1996	55
Railroads			
Slovenske Zeleznice (corridor 10)	Slovenia	1994	45
Ceske Drahy - Czech Railway Corridor (corridor 4)	Czech Republic	1994	50
Railway Modernisation (corridor 2)	Poland	1996	21
Ventpilis Port Rail Terminal	Latvia	1998	41
Trans - Caucasian Rail Link (Traceca)	Georgia	1998	20
Trans – Caucasian Rail Link (Traceca)	Azerbaijan	1999	20
Sea Ports			
Aktau Port Reconstruction	Kazakhstan	1996	53
Turkmenbashi Port Development	Turkmenistan	1997	31
Ventpilis Port Multipurpose Terminal	Latvia	1999	10
Baku Port Development	Azerbaijan	1999	16
Airports			
Riga International Airport	Latvia	1993	11
Yerevan Air Cargo Terminal	Armenia	1994	23
Tallinn Airport Rehabilitation	Estonia	1994	12
Skopje Airport Rehabilitation	Northern Macedonia	1995	9
Tbilisi Airport Refurbishment	Georgia	1995	11
Tashkent Airport Rehabilitation	Uzbekistan	1997	37
Tallinn Airport Passenger Terminal	Estonia	1999	8
Khoujand Airport	Tajikistan	1999	3

ANNEX 4: Transport sector projects with cross-border components 2000 - mid 2017

OPID	Operation Name	Corridor	Country	Date of BA	Loan € m	Sub-sector
2213	Rehabilitation of M06 Highway and Reform of Road Sector Financing	V	Ukraine	2000	74.2	Road
4783	St.Petersburg Air Cargo Terminal Pulkovo		Russia	2000	4	Airport
7654	Corridor IX and LG Restructuring Project	IX	Lithuania	2001	44.1	Railway
10224	Railways Recovery Project	Vc	BiH	2001	20.9	Railway
11846	Channel Energy (Poti) Oil Terminal		Georgia	2001	10.1	Sea Port
18492	Atyrau Airport Project		Kazakhstan	2001	21.7	Airport
18659	Yugoslav Railways – ZTP Belgrade Reconstruction	X	Serbia	2001	57	Railway
20178	Autocesta Rijeka-Zagreb	V	Croatia	2001	60	Road
22705	Road Recovery Project	X	Serbia	2002	76	Road
27171	Motorway Rehabilitation Project	X	Croatia	2002	45.3	Road
27969	Tallinn Airport Loan		Estonia	2002	7.3	Airport
28092	Road Rehabilitation Project II	VIII	Albania	2002	17	Road
24998	M5 Toll Motorway Project – Refinancing		Hungary	2003	67.5	Road
31848	Corridor 10 Motorway Completion Project	X	Croatia	2003	45	Road
34132	Airports Modernisation Project		Serbia	2003	10.2	Airport
1863	Silk Road	TRACECA	Azerbaijan	2004	35.7	Road
13451	Port of Dubrovnik Infrastructure Modernisation		Croatia	2004	32.7	Sea Port
14849	Ukraine Railways - Fast Passenger Trains	V	Ukraine	2004	104.5	Railway
31788	Regional Road Development Programme	Vc, X	BiH	2004	70	Road
31928	Second Project Kiev-Chop Road Rehabilitation	III, V	Ukraine	2004	99.2	Road
34012	Constanta Port Development and Commercialisation	IV, VII	Romania	2004	16	Sea Port
35047	M5 Phase II		Hungary	2004	100	Road
32190	Novi Sad Motorway	X	Serbia	2005	72	Road
33391	Constanta By-Pass	IV, IX	Romania	2005	131.9	Road
34052	Tirana Airport Privatisation Project		Albania	2005	29.7	Airport
35264	M6 Motorway	V	Hungary	2005	25.3	Road
36566	M6 Motorway Refinancing	V	Hungary	2005	32	Road
31849	Croatia Road Programme	Vb	Croatia	2006	33.3	Road
35414	Serbian Railways Rollingstock	X	Serbia	2006	59.8	Railway
35790	Croatia Road Programme	Vb	Croatia	2006	50	Road
36013	Armenia International Airport - New Passenger Terminal		Armenia	2006	16.8	Airport
36127	Port of Ploce Bulk Terminal	Vc	Croatia	2006	0.3	Sea Port
36385	Tbilisi International Airport		Georgia	2006	22.5	Airport
36547	Third Project Kiev-Chop M06 Road Rehabilitation	III, V	Ukraine	2006	200	Road
31245	Illichivsk Sea Commercial Port Infrastructure	IX	Ukraine	2007	0.5	Sea Port
35862	Port of Durres	VIII	Albania	2007	14	Sea Port
36651	Belgrade Highway and Bypass Project	X	Serbia	2007	79	Road

37057	Levan-Vlore Road Project	VIII	Albania	2007	29.5	Road
37140	Rosmorport		Russia	2007	58.7	Sea Port
37534	Joint Stock Company TransContainer		Russia	2007	133	Railway
37671	Moldova Road Rehabilitation Project	IX	Moldova	2007	17.5	Road
37879	Chisinau Airport Modernisation Project II		Moldova	2008	6.5	Airport
38376	M6-M60 Motorway	Vc	Hungary	2008	74.6	Road
38716	Corridor Vc	Vc	BiH	2008	205	Road
39358	South-West Corridor Road Project	Western Europe – Western China International Transit Corridor	Kazakhstan	2008	109.1	Road
47372	Corridor Vc 2	Vc	BiH	2008	90	Road
38773	Osh-Isfana Road Upgrading Project	South-west Kyrgyz to China and neighbouring Central Asian	Kyrgyz Rep	2009	30.5	Road
39334	Armenia International Airport Phase II		Armenia	2009	40.6	Airport
39432	R1 Motorway - Slovakia	V	Slovak Rep	2009	399	Road
39750	K10	X	Serbia	2009	150	Road
39838	Euroterminal Odessa Project		Ukraine	2009	14	Logistics
40109	Odessa Terminal Holdco		Ukraine	2009	0	Sea Port
40327	Mahovljani Interchange	X	BiH	2009	19.9	Road
40344	Montenegro Rail Infrastructure Emer Rehab II		Montenegro	2009	15	Railway
39029	Pulkovo Airport Concession Finance		Russia	2010	97	Airport
39749	Port of Sibenik Infrastructure Rehabilitation		Croatia	2010	8.1	Sea Port
39858	Poti Port: Phase 1		Georgia	2010	8	Sea Port
40153	Local And Regional Roads		Albania	2010	50	Road
40185	Pan-European Corridors	III, V, IX	Ukraine	2010	450	Road
41125	Serbian Railways Corridor X	X	Serbia	2010	100	Railway
41325	Corridor Vc Completion Project	Vc	Croatia	2010	58.9	Road
41327	Macedonian Railways - Corridor X	X	N Macedonia	2010	17.6	Railway
41442	Moldova Road Rehabilitation III	IV, IX	Moldova	2010	75	Road
41981	Corridor X	X	N Macedonia	2011	91.1	Road
42262	JSC Serbia Railways	X	Serbia	2011	1	Railway
42319	Fier and Vlore bypass roads	VIII	Albania	2011	53	Road
42899	Global Ports (f.Kornilov)		Russia	2011	48.7	Sea Port
43094	Roads Reconstruction and Upgrading Project	TRACECA	Azerbaijan	2011	609.4	Road
45515	Corridor X Tolling	X	N Macedonia	2011	15.9	Road
42163	Turkey Eurasia Tunnel		Turkey	2012	130.6	Road
42232	Dushanbe-Uzbekistan Border Road Improvement	CAREC, E60, 65	Tajikistan	2012	54.4	Road
42542	Port of Split Infrastructure Rehabilitation Project		Croatia	2012	23.3	Sea Port
42921	North Macedonia: Railway Corridor VIII - Phase I	VIII	N Macedonia	2012	46.4	Road
43271	Shymkent-Tashkent Road Reconstruction Project	Western Europe – Western China International Corridor	Kazakhstan	2012	106.2	Road
43343	Khujand International Airport Emergency Loan		Tajikistan	2012	3.4	Airport
44212	Baltic Transhipment		Lithuania	2012	27.5	Sea Port

44277	DLF - Georgia Logistics Terminal		Georgia	2013	2.8	Logistics
45475	LEF: Akel Logistics		Turkey	2013	1.7	Logistics
44717	Asya Port		Turkey	2013	61.2	Sea Port
45193	Mersin International Port Bond		Turkey	2013	69.2	Sea Port
45805	DCT Gdansk expansion		Poland	2014	24.6	Sea Port
46467	Dalaman Airport		Turkey	2014	81	Airport
44175	Rail Corridor VIII - Second Phase	VIII	N Macedonia	2014	145	Road
49067	Ekol Ro-Ro II		Turkey	2014	18.5	Logistics
47218	Astana Airport Rehabilitation		Kazakhstan	2015	5.8	Airport
47229	Kurty Buribaytal road project	CAREC Cor 1	Kazakhstan	2015	89.7	Road
47320	Global Ports Holding Plc (f. Global Liman (f. Prime))		Turkey	2015	53.4	Sea Port
45035	Olimpex Dry Port		Ukraine	2015	16.3	Sea Port
47383	Yuzhny Grain Terminal		Ukraine	2016	32.2	Sea Port
46695	DFF: Luka Ploce-Liquid cargo terminal		Croatia	2015	9.6	Sea Port
47546	Port of Brcko		BiH	2016	10	River Port
Total	**91**				**5874.9**	

ANNEX 5: Key messages of "promoting transition through regional integration" memo

The memo presented data showing the extent of disintegration of Central Europe's internal trade links after 1989, which dropped on average to 23% of their export share as compared to 70% in the CMEA era. It referred to a range of policy, administrative, infrastructure, financial and informational obstacles to intra-regional trade (although with no specifics). It noted activity of Russian natural resource companies, Baltic countries' banks and some larger Hungarian companies, which invested cross-border, often with the Bank's support. The paper also spelled out the rationale for regional integration, specifying political, economic and financial arguments. It gave useful examples of EBRD's contribution to the Stability Pact for South-Eastern Europe. The "Bank's project-level contribution to regional initiatives" section argued that *"the Bank contributes its investor perspective to regional integration initiatives and ensures that integration concepts become effective on the ground"*. This wasn't very clear. However, the paper gave examples of Bank's projects with a regional dimension classified into 4 categories:

(i) Projects that develop regional concepts for infrastructure and environmental action – e.g. Bank's involvement in the environmental action plan for the Baltic Sea (St. Petersburg Vodokanal), support for transport corridors, ports and airports. It estimated, the Bank provided €3.1 billion[10] for such projects.

(ii) Projects that support cross-border investments of local companies, e.g. Estonian banks' investments in other Baltic states, investments of Hungarian and Croatian oil companies, some pipelines (€0.5 billion);

(iii) Projects fostering regional trade, e.g. the Bank's Regional Trade Facilitation Programme

(iv) Projects that have strong regional demonstration effect, e.g. regional post-privatisation funds, EU Phare-EBRD SME Programme, estimated to date for €1.4 billion.

The only clue of the proposed Bank's future approach was the statement that "*the policy framework for integration was not the direct objective of the Bank interventions, rather the promotion of concrete steps towards the removal of obstacles through policy dialogue from an enterprise-level perspective, focusing on issues such as administrative and legal impediments to investment."* The conclusions section reiterated that *"a bottom-up, project-driven approach can complement policy, as at the end effective integration will be a decentralised process. EBRD can build critical mass in cross-border exchanges and to coordinate capital investments"*. The paper closed with the statement: *"Responding to the needs of its clients in business and government and as an active participant in regional initiatives, the Bank will further develop its activities in this area in the coming years"*.

[10] This figure differs from €2.3 billion mentioned earlier as it includes MEI projects supporting local integration.

ANNEX 6: Results of selected cross-border projects implemented before 2017

Transport Sector:

38773- Osh-Isfana Road Upgrading (Ferghana Valley), Kirgiz Republic

In 2009 EBRD provided 18-year sovereign loan of US$ 35 million for the rehabilitation, upgrading and rerouting 60 km of single carriageway road, the part of Osh–Batken–Isfana road in the South-West of Kyrgyz Republic – an important link within Central Asia and part of its connection with Europe. The entire road was 358 km long and its other sections have been rehabilitated with funding from the EU (US$ 17.8 million grant, 14 km) and the World Bank (US$ 20 million loan, 30 km), while the Government of the Kyrgyz Republic has upgraded 93 km.

One of the objectives was to reroute the road to run entirely through The Kyrgyz Republic, rather than crossing Uzbek boarder six times, which caused delays and extra cost for travellers. After rerouting and upgrade, the road has an important role as international transit route linking Kirgiz Republic and neighbouring countries of Tajikistan and Uzbekistan with China.

The project was completed in 2016, with two year delay and 9% savings. The road maintenance component was cancelled and institutional reforms were not implemented. According to OPA, the road increased connectivity of relatively remote Batken oblast and boosted international transit. Traffic almost tripled from pre-project levels from 600 to 1600 AADT, exceeding original forecast.

41981 Corridor X, Northern Macedonia

In 2011 the Bank provided €107 million sovereign loan to finance the construction of 28 km section of Pan-European corridor X. The project of the total cost of €334 million was co-financed by EIB (€130 million loan) and EU grant of €45 m. The corridor X is the backbone of connectivity in south-eastern Europe. It runs from Salzburg to Thessaloniki, through Belgrade, Nis and Skopje, with a separate branch reaching Budapest. The road was of critical importance for Northern Macedonia, linking its capital Skopje with the rest of Europe in the north and Greece (and further with Turkey/Asia) in the south.

The project was physically completed with three months delay in February 2018. However, almost none of its transition benchmarks (sector reform, tolling, private sector participation, etc.) were achieved and were transferred to subsequent Bank's road projects in Northern Macedonia. Many of these benchmarks were covenanted in the loan agreement and thus required waivers. According to SEETO 's report of 2018, traffic on corridor X in 2016 was the highest of all corridors in the Western Balkans and amounted to 14,000 AADT, exceeding the project's forecast.

8072 – Road Sector Development (Almaty –Bishkek Road), Kazakhstan

In 2000 the Bank provided US$ 28.5 million for the rehabilitation of one Kazakh section of the Almaty-Bishkek road. The project was co-financed by US$ 65 million loan from ADB (financing two Kazakh and one Kirgiz sections), US$ 2 million grant from EU-Tacis programme and US$ 27 million funding form the Kazakh government. The road formed a part of TRACECA corridor, leading from China to Europe. Traffic analysis indicated large differences in traffic level, which picked close to Almaty at 17300 AADT but then decreased to 4400 AADT further away with

projected increase of 15 and 5% respectively. The project was expected to "*contribute substantially to cross-border regional integration between Kazakhstan and Kirgizstan"* because as part of the project both countries were to sign a Cross-Border Agreement (CBA) designed to remove non-physical barriers to movement. The project's implementation was very slow.

In 2006 the Board approved operation change, agreeing to the termination of the initial contract due to many defects and slow progress and extending the existing ADB-financed contract (granted in accordance with ADB tender procedures) to finalise the EBRD-financed section.

The Joint Evaluation Report of ADB and EBRD of 2009 noted that 19 km, rather than the planned 41 km were rehabilitated due to cost overruns, mainly in The Kyrgyz Republic. The project was completed in 6, rather than three years and overall had 8% cost overruns. Ratification of the Cross-Border Agreement was a covenant to the loans' disbursement and due to delays with its ratification disbursements were delayed by one year. The joint evaluation rated the project **partly successful** as its main output was achieved but its transition objectives were not. Both countries have no system to generate revenues dedicated for road maintenance, while the Cross-Border Agreement was ratified but has not been implemented. Stakeholders interviewed by evaluators were of the opinion that crossing the border had become more difficult due to bureaucratic procedures on the Kazakh side. Traffic on the road reportedly increased with higher vehicle speed but no exact counting has been done. However, available data indicates that trade between both countries at the Almaty-Bishkek road crossing has been increasing on average by 23% per annum between 2000 and 2007, although this could be attributed to economic growth.

Energy Sector – oil pipelines

18806 - Baku-Tbilisi-Ceyhan oil pipeline

In 2003 the EBRD approved a US$0.25 billion 12-year loan to co-finance the Baku-Tbilisi-Ceyhan oil pipeline (BTC). This 1,768 kilometers pipeline was to bring for the first time Azeri oil from the Caspian Sea, through Georgia and Turkey to the port of Ceyhan on the Mediterranean Sea, so it could be easily available for worldwide transportation by tankers. Half of the Bank's loan was syndicated. The IFC, export finance agencies, such as US-Exim, JBIC, Nexi, Hermes, SACE, Coface, ECGD, OPIC; and a number of commercial banks such as Société Générale, ABN Amro, Citibank and Mizuho, co-financed this mega-project of the total value of US$3.8 billion.

BTC was developed by 11 oil companies, including BP, Statoil, ConocoPhillips, ENI, INPEX, ITOCHU, SOCAR, TOTAL, TPAO and UNOCAL. It is operated by BP.

For Georgia, the project was to become the first major alternative source of energy to its traditional supplies from Russia. For Azerbaijan and its Caspian oil, it was the first route to the West, effectively a huge step in the country's integration with world's economic system.

The political and strategic significance of the project attracted media attention, while its technical, financial and legal complexity illustrates challenges often faced by large cross-border projects. It involved two lead project sponsors (BP and Statoil), representing all other sponsors (which

representatives nevertheless often participated in the negotiations), two IFIs (EBRD and IFC), six export credit agencies, four commercial bank-mandated lead arrangers, four main law firms, two financial advisers, two technical advisers (upstream and midstream), one insurance adviser, one environmental and social adviser and a few other additional parties. Each of those had at least two to three staff attending negotiations, bringing negotiating group to about 70. Moreover, the project was very challenging environmentally, drawing attention from civil societies.
The EBRD and IFC engaged in six public meetings and conflict resolution, which provided lessons for the TANAP and TAP gas pipeline projects (see annex 2).

The project was successfully concluded in 2005 with a 'first oil' ceremony taking place at the Turkish Ceyhan terminal on the Mediterranean sea in the presence of the Turkish, Azeri and Georgian heads of state and government, as well as minister level representatives from G-7 countries.

EvD's 2008 evaluation rated the project overall **partly successful** due to delay in the implementation of the Regional Development Initiative, which was designed to contribute to sustainable development activities in various sectors of the economy after the completion of the BTC construction. Through this program the Sponsors wished to visibly contribute to the region and thus enhance their long-term business. However at the time of the evaluation the program was delayed and EvD's report suggested the project's results re-evaluation around 2010 (which did not take place).

7858 - Thessaloniki-Skopje Crude Oil pipeline

In December 2000 the Bank provided $50 million to the Pipeline Operating Company. The loan was intended for the construction of a pipeline capable of transporting crude oil or petroleum products between Hellenic Petroleum's facilities at Thessaloniki and the OKTA refinery in Skopje. The project was completed on time and on budget and initially it transported oil as intended, reducing transportation costs by 40%. The investment was the largest FDI in Northern Macedonia.

Unfortunately, provisions of the Concession Agreement have been openly breached by the government as Makpetrol (a 70% government owned retail competitor to the Sponsor), was unofficially granted privileges similar to those denied to the Sponsor.

The 2003 Operation Evaluation of this project rated it overall **partly successful** as the operation has failed to generate the anticipated Transition Impact, rated Marginal, due to the Bank's frustrating policy dialogue in the face of crippling political corruption in the country and an unfriendly political climate between Greece and Northern Macedonia

Energy Sector – electricity transmission

39579 Black Sea Transmission Line project and **45181 Jvari-Khorga Interconnection**

The first project of 2009 provided €56 million loan and the second of 2013 €25.2 million. Both loans were to help Georgian hydroelectricity producers sell renewable energy to Turkey. The first

project was co-financed with EIB, KfW and EU, for the construction of a 315km 500 kV high voltage transmission line between West and East Georgia, enhancing grid reliability and enabling exports of the excess electricity to Turkey. The first project was successfully completed but the second (the extension of the first), has been dogged by technical problems and the bankruptcy of the main contractor. The main contract is currently being retendered. The line (completed under the first project) improved the stability of the energy system and increased exports to Turkey. Georgia's membership in the EU Energy Community, prompted it to harmonise its policies and standards to those of the EU. However, exporting electricity to Turkey has recently become less attractive for Georgian producers because domestic electricity demand has increased, while electricity prices in Turkey have fallen sharply[11].

46274 MEPSO: Northern Macedonia – Albania Transmission Line

2015 loan of €37 million financed the construction of a 400 kV transmission line from Bitola substation in Northern Macedonia to the Albanian border, and the construction of a new 400/ 110 kV substation at Ohrid. The Project is the first phase of a regional interconnection project between North Macedonia and Albania. The project suffered long delays due to government changes and difficulties with the fulfilment of conditions precedent. It started disbursing only in 2018 (€1.8 million disbursed to date).

47221 Cross Regional Power Trade project

This 2015 loan of €97 million aimed to enable power exchanges between Tajikistan and the Kyrgyz Republic, providing financing for the construction of the AC/DC converter station and connection from the existing AC Tajik substation, as part of the high-voltage transmission infrastructure for the Central Asia - South Asia Electricity Transmission and Trade Project (CASA-1000). The second procurement process (since the first failed) took place from October 2016 until the contract was awarded in September 2018. The loan is expected to start disbursing by the end of 2019.

[11] See full evaluation of these two projects in Hydropower projects, Georgia (SS18-137), October 2019

ANNEX 7: Categories of projects targeting "Integrated"

Infrastructure
• **Cross-border infrastructure projects, e.g.:**
-Southern Gas Corridor and TAP (see annex X) -BRUA Pipeline – gas transmission corridor between Romania, Bulgaria, Hungary and Austria -Moldova-Romania Power Interconnection (see section X) -SMARTSA Upgrade, Serbia – part of Single European Sky programme, aiming to integrate European air traffic systems through improvement of safety, efficiency and interoperability of neighbouring systems -Energy Exchange, Greece – market coupling of Greece with Italy and Bulgaria -Kriva Polanka, Northern Macedonia – improvement of connectivity to Bulgarian border -Project Frame – upgrade of international airport of Belgrade
• **Local infrastructure projects, with cross-border component, e.g.:**
-Main Roads reconstruction, Montenegro – reconstruction of mainly internal roads but also those connecting to Serbia -UZ Electrification, Ukraine – electrification of selected internal rail lines but including those leading to Mykolaiv port -Kijeve-Zahqq Highway, Kosovo – improving connectivity among Kosovo's main cities but also with Montenegro; -Railport, Turkey – inland intermodal logistics terminal in Kocaeli, enhancing international connectivity of the Turkish market -Kazirnavigaiton, Kazakhstan – introduction of performance based navigation, enhancing Kazakhstan's airspace safety
• **Local infrastructure projects, e.g.:**
-Magticom, Georgia – regional expansion of a telecom company and integration through acquisition of a local competitor -SNCFT Network, Tunisia – improving connectivity of Tunisia's remote areas -Belarus Road Sector Reform – enhancement of internal roads network -Cairo Metro Line, Egypt – improvement of local connectivity -Atyrau-Astrakhan Road, Kazakhstan – connecting two regional cities -Kurty-Kapshagai Road, Kazakhstan – connecting two regional cities
ICA
• **Support for exporters, e.g:**
-Jurabek Amopoule, Uzbekistan – support for export expansion of a pharmaceutical company to Kazakhstan and Tajikistan -Nibulon Grain Infrastructure, Ukraine – improved logistics and infrastructure enabling export volume increase by over 50% -Project Chimera, Poland – support for biological medicine exports to the EU and USA -Project de Jure, Turkey – investment in IPO which proceeds will be used for expansion in Moldova, Ukraine and Romania -MCS Spring, Mongolia – production and export of the new mineral water category and expanded outreach to underserved areas outside of Ulaanbaatar
• **Support for FDIs/cross-border acquisitions, e.g:**
-Project Nautilius – cross-border provision of services and FDI (tug vessels) -Project Baguette – FDI financing of a Chinese yeast producer in Egypt -Project Carolinium, reginal – FDI support by a Czech beverage producer in Hungary, Slovakia and Bulgaria -Medlabas Consultancy, West Bank – FDI by a Jordanian company -Project Union, Lithuania – acquisition of Polish supermarket chain by Lithuanian chain -Project Selim, Turkey – acquisition of a Turkish company by a Belarusian animal feed company

• **Integration of local suppliers into global supply chain, e.g.:**
-Soufflet Grain Financing, Regional – integration of suppliers from Ukraine, Romania and Bulgaria into the company's global supply network
Financial Institutions
• **Trade Facilitation Programme, e.g:**
-Fransabank, Lebanon – trade finance guarantee

ANNEX 8: Linkages of country and sector strategies to regional integration

EvD reviewed six Country Strategies (CS) under which the evaluated cluster projects were approved, as well as the current six strategies and associated diagnostics. The latest CSs for additional three countries (Georgia, Mongolia and Kazakhstan) were also reviewed for a total of 15 CSs and four diagnostic papers (prepared to inform the most recent strategies 2017-2019). The review aimed to verify whether:

- a country diagnostic was prepared, particularly in respect of Regional Integration;
- the transition gaps and challenges associated with Regional Integration were described;
- any of the strategies set Regional Integration as its operational priority;
- if so, whether specific activities (projects, TCs, policy dialogue) were identified and of what type they were;
- results monitoring indicators (including baselines and targets) related to Regional Integration were presented.

Country Strategies:

Croatia

Both Croatian projects, evaluated under this review, were approved under the **2010** CS. No diagnostics paper was prepared to inform this strategy, however the CS referred to the EBRD's 2009 Assessment of Transition Challenges. There was no specific mention of regional integration, but the CS stressed that Euro-Atlantic integration had remained the key priority of the Croatian authorities. The CS identified the electricity utilities and railways as the remaining significant transition challenges in the infrastructure sector. Other challenges identified were those related to economic reform and the preparation for integration into the European internal market. These included among others, investments in environmental infrastructure, regional networks and sustainable energy.

In response to these challenges, the Bank proposed as one of its operational priorities "financing priority infrastructure including regional transport networks through the Western Balkans Investment Framework (WBIF)". Transition goals for infrastructure included "support regional trade and investment through infrastructure development". The priorities included infrastructure investments with EIB, through the WBIF. The Bank also intended to support the airport and port PPPs, where EBRD was already fostering concessions. No specific activities or monitoring indicators were mentioned.

In the latest CS **2017**, one of the strategic objectives is "Increased cross-border trade and investments flows". The 2017 CS does include activities and tracking indicators to measure progress. Two of the proposed activities are "Support new investments linked to improving regional interconnectivity and co-operation in energy, transports and capital markets" and "Support logistic companies in Croatia in order to boost transport in ports, highways and railways". The corresponding indicator was net increase in the throughput of infrastructure (annual tonnage, Baseline – 0). While the old Croatia strategy had some, i.e. **moderate** linkages to regional integration, the current one can be seen as having **strong** linkages due to Integrated featuring as one of strategic priorities.

Bosnia and Herzegovina

The first Corridor Vc investment in BiH was approved under the **2007** Strategy. No diagnostic document was prepared to feed into this Strategy. The document directly referred to regional integration as one of its three priorities: "assist BiH's regional integration and its progress towards EU membership through physical investments in key infrastructure projects as well as institutional development and strengthening of state institutions".
The CS described the transition gaps and challenges. In infrastructure, it sought to address those in transport, focusing on the road, rail, and aviation sectors. Pointedly, in the road sector, EBRD's expectation was to focus on the road network rehabilitation, which was to be co-financed with the World Bank and EIB. The Bank aimed to support the commercialisation of the sector through the introduction of performance-based maintenance contracts and enhancement of management information systems. Under the Regional Road Development program, the execution of projects on the north-south axis was to be prioritised. One of the transition objectives underpinning the Bank's involvement in BiH's transport sector was support for regional integration. The activities of the Bank were expected to be aligned with the Memorandum of Understanding on the Development of the South East Europe Core Regional Transport Network. At the time, it was expected that adopting the BiH Transport Sector Policy and Strategy would provide an appropriate framework for implementing priority investments in the sector.

The latest BiH CS **2017** covers the 2017-2022 period and was informed by a "mini-diagnostic paper" (2017). These diagnostics concluded that BiH was lagging behind peers in all six transition qualities, including Integrated. The paper stated that the support of cross-border integration was at the heart of long-term economic development. Even though BiH had a Stabilisation and Association Agreement (SAA) with the EU (2015), trade openness levels were low. Also, the transport infrastructure's quality was deemed inadequate (with poor scores in all categories: rail, road, water and air) and the region's difficult terrain, which made transport projects complex and costly. A lack of fiscal space was also noted, along low private sector involvement in projects and no successful PPPs. Finally, progress in cross-border energy integration was noted with the 2014 establishment of the Coordinated Auction Office in Montenegro for SEE. Whereas BiH was the second largest producer of electricity in the Balkans, large investments were deemed required to enhance intra and inter regional energy linkages.
One of the 2017 CS priorities was to **"**support development of key transport and energy cross-border links to promote Integration with the region while enhancing Resilience of the economy". It presented a Country Strategy Results Framework with indicative activities and two tracking indicators: net increase in the throughput of infrastructure and volume of electricity traded. No targets were presented and baselines were to be established at project approval. Both old and new BiH CSs had **strong** linkages to Integrated transition quality.

Azerbaijan

The Azeri Road Rehabilitation project was approved under the **2010** CS. There was no diagnostics prepared to inform this strategy. The CS described the two main country's transition gaps and challenges, the first being "integration into the global economy". It indicated that the long-term development of the non-oil economy would depend on the capacity to integrate into the global economy as closer integration would improve productivity and competitiveness. The second challenge was "advance public infrastructure reform". The CS highlighted the government's accelerated investments in power, transport and water supply to improve services. The CS set the Bank's strategic orientations for the 2010-2013 period, which included the regional development

of all infrastructure sectors with a particular focus on interconnection with neighbouring countries. EBRD would continue to provide financing mainly on a sovereign basis, although it anticipated gradual facilitation of private sector investment in all infrastructure sectors. The strategic directions were based on some of the transition objectives of the 2004 Transport Operations Policy, in the form of supporting reform in the road sector, desirably with multi IFI cooperation and improving efficiency of road sector administration and management. In terms of results, the CS did not specify activities for the implementation of priorities. Monitoring indicators were not identified.

The more recent gas corridor project was approved under the **2014** CS. The document indicated the continued commitment of the Bank in the hydrocarbons sector, stating that "involvement in strategically important projects such as the Southern Gas Corridor will contribute to export route diversification and regional energy security in Europe."

EBRD would continue to pursue investments under the Sustainable Energy Initiative (SEI), via investments in energy projects that improve energy security, generate capacity, stimulate competition, diversify energy sources, increase efficiency, and create wider and larger markets through regional integration. Within the strategic priority of improving governance and the business environment, EBRD's intent was to "support projects of regional significance that enhance regional trade via diversification of hydrocarbon export routes and which favour regional integration of energy infrastructures". Both, old and new CSs for Azerbaijan are considered having relatively **strong** linkages to Integrated quality.

Turkey

Among challenges identified in the **2012** Strategy for Turkey was that "need to facilitate trading across borders, including support for further trade integration with the SEMED region." A second challenge was strengthening regional and rural infrastructure, in which expansion of regional infrastructure services was required due to rapid economic growth and accelerated regional integration. Implementation of transparent PPP projects was expected to attract more private sector investment into the infrastructure sector. The Bank's operational response was to enable private sector financing of significant transport investment requirements. EBRD would also continue to work with other IFIs and commercial lenders in financing large PPP projects with a regional dimension in the transport sector. Also, it was to provide "effective transport solutions in more remote regions" and to support private sector operators in the development of intermodal transport operations through the provision of long term funding. There was no results framework presented in the strategy, and thus specific activities with baselines, indicators and indicative targets were not included in the document.

The **2019** Strategy for Turkey (2019-2024) was informed by country diagnostics prepared in the same year. It ranked the country's Integrated quality 20th out of 38 EBRD CoOs, with internal integration higher than external integration. The CS presented the country's key transition challenges related to Integrated: FDIs integration into global markets was low compared to middle-high income peers, partly due to its large domestic market, tariff uncertainty and the impact of political and financial instability. Domestic transport and logistics infrastructure and cross-border integration were assessed good, save for rail. ICT infrastructure was deemed below EBRD and OECD levels, and the quality of electricity supply was low.

One of the strategic priorities was to accelerate Turkey's green economy transition and regional energy connectivity. The only activity foreseen related to regional integration was to "support

investments in gas transmission and distribution networks and infrastructure connectivity". One indicator tracked the progress of this output: "Target infrastructure network extended / replaced as measured by increase in network capacity and/or efficiency". Ports and airports no longer appeared in the strategic priorities. Linkages of both CS for Turkey's to Integrated transition quality were **moderate**. This was largely the reflection of the perception and later diagnostics, which deemed the level of Turkey's integration, including most of transport infrastructure relatively adequate.

Poland

The **2013** Country Strategy for Poland did not make any direct references to regional integration. However, one of the strategic priorities was to enhance the private sector's role in the economy. This would require "more innovation, providing risk capital and corporate restructuring, and supporting Polish companies in their regional expansion and cross-border investments." No results framework was presented with activities, outputs, outcomes or indicators to measure progress towards objectives.

In 2017, a diagnostic paper was prepared to support the design of the latest **2017** CS. It assessed the country along the six transition qualities. In respect to Integrated, it deemed infrastructure quality as poor. Motorway density was found to remain relatively low and the perception of transport infrastructure quality was one of the lowest in OECD countries in spite of substantial infrastructure investment since the EU accession (2004). The 2017 CS succinctly listed the transition challenges associated with the Integrated quality. It noted that "infrastructure quality remained poor, particularly in the transport sector" and that Poland ranked 65th of 137 economies in roads quality in the Global Competitiveness Index".

The CS presented a results framework. The first strategic priority was enhancing competitiveness through innovation, commercialisation and stronger global linkages. Under the objective of increasing private sector participation in state-dominated sectors, the proposed actions were the "development of integrated and intermodal transport infrastructure, including through PPP and concession structures". The tracking indicators were number of projects outsourcing activities to private sector, and implementation of PPP/concessions. The 2013 CS for Poland had **weak** linkages to Integrated transition quality, while the new strategy strengthened these links to **moderate**.

Ukraine

The Pan-European Roads project was approved under the **2007** CS. It presented key transition challenges, including the country's competitiveness which was deemed hampered by infrastructure and transport bottlenecks. The Bank's intended response was to support Ukraine's transport and communications infrastructure, as key to the country's integration into European transport networks and the world economy. It was to concentrate in the development of the TRACECA corridor and the other main corridors and their interconnections to the Trans-European Transport Networks. The objective was to "facilitate the transportation of goods and passengers, as recommended by the High-Level Group on the extension of the main trans-European transport axes to neighbouring countries, as well as by the Long-Term TRACECA Strategy". No results framework defining activities and indicators was included in this CS, but medium term operational focuses were presented. These comprised modernisation of the M06 road linking Kiev to the

border with the EU and financing other major international corridors and the modernisation of the Ukrainian aviation sector.

In 2018, a country diagnostics was drafted to identify the main obstacles to private sector development and to feed into the strategic priorities and project selection. One of the important challenges was the poor and deteriorating state of physical infrastructure (mainly roads) and low quality of logistics (cost and time of border and documentary compliance). This made the private sector less integrated both internally and externally. Customs procedures were found to be cumbersome, inefficient and excessively bureaucratic. More specifically, port dues and tariffs were higher than ports in other countries. Also, ICT quality infrastructure lagged behind peers.

The 2018 CS presented the transition challenges based on the findings of the diagnostics. One of the strategy priorities was to "improve integration by facilitating trade and investment, expanding infrastructure links, and supporting convergence with EU standards". The anticipated results were "improved connectivity through enhanced infrastructure and increased trade and investment flows". The CS included activities and results framework, describing how these outcomes would be achieved. This comprised investments into domestic core transport network (rail, air, maritime, road, waterways); investments in logistics; and support for "soft" connectivity. One indicator was proposed to encompass all activities: improved/increased infrastructure capacity. Also, the Bank was to support companies' integration in cross-border value chains. This would be measured by the total number/volume of Bank's TFP transactions. The indicators seem to be very broad, and would have to be more specific at the project level to be meaningful in measuring success. Both CSs for Ukraine had relatively **strong** linkages to Integrated transition quality

Other Countries

No diagnostics paper was prepared to inform the latest **Mongolia CS 2017**. The CS did refer to regional integration directly under the strategic objective of "improving the quality and sustainability of infrastructure services". It stated that EBRD would "help to enhance connectivity and regional integration through rail and road projects, and support PPPs in the energy sector with a view to introducing state-of-the-art technologies and renewable (wind and solar) energies."

For **Kazakhstan's CS of 2017**, a diagnostic paper was prepared in 2016 to assess the country's progress and challenges. For integration, one of the main concerns was the low levels of investment and maintenance in regional and local roads and the sub-standard connectivity between major urban and rural areas. In the rail sector, challenges related to the structure of tariffs and cross-subsidies. Overall, underdeveloped cross-border connectivity was considered a critical constraint to growth. Enhancing the quality of domestic and cross-border infrastructure, including soft infrastructure and logistics were considered a key priority. The 2017 CS covering the 2017-2021 period referred to the "need to boost regional connectivity", underscoring the challenges presented in the diagnostic paper. In response to these needs, one of the strategic orientations was to enhance inter-regional connectivity and international integration. The Bank's response would be to commercialise and upgrade inter-regional and cross-border transport infrastructure and to encourage companies to integrate with the wider region, "capitalising on Kazakhstan's geographic position on the new Silk Road connecting the two economic poles of European Union and South-East Asia." A results framework was presented to measure the progress towards the strategic objectives. Tracking indicators included evidence of increasing private sector participation, operational efficiency, and improvements to legal and institutional frameworks. These are very general indicators, and no baselines or targets were presented.

The latest **Georgia CS 2016** presented key transition challenges, which included inter-regional connectivity. Capacity and legislative framework were considered outdated, limited and inconsistent with international practices. Logistics needed modernisation and there was a lack of appropriate infrastructure and regulatory framework, which were deemed necessary to increase cross-border energy trade. However, no diagnostics were produced to inform this CS. The Bank's proposed operational focus was to support the development of transport infrastructure to strengthen regional economic links. Specifically, it would "contribute to further develop the East/West and North/South transport corridors connectivity, in cooperation with other MDBs and encourage PPP structures". EBRD would also support ports and airports to enhance the country's potential as a regional logistics platform and tourism. It would invest in gas storage facilities and gas pipeline connections to support "energy security and integration into regional gas markets, as well as support power infrastructure enhancing Georgia's internal capabilities and interconnections with the region". Finally, it would assist in developing "logistics and warehousing centres that can support Georgia's potential for becoming a regional transit hub." **All three** CSs described above are assessed as having **strong** linkages to Integrated transition quality.

These examples demonstrate that the Bank's country strategies for almost all countries referred quite extensively to connectivity issue as one of the transition challenges. Moreover, many CSs, particularly those most recent ones, set improving cross-border connectivity as one of Bank's strategic operational priorities. As a result, linkages to the "Integrated" transition quality in 10 out of 15 country strategies were assessed as "strong". Five country strategies for more advanced countries (Poland, Croatia and Turkey) had less pronounced linkages to Integrated as their EU membership or candidate country status elevated their degree of integration. Nevertheless, their infrastructure was deemed far from adequate and therefore set to be targeted by the Bank, supporting the "Integrated" transition quality. Diagnostics were prepared only for the most recent strategies. Also results and monitoring frameworks were developed for the most recent CSs although some of the proposed indicators were very broadly defined.

Sector Strategies

Transport Policy (2005)

The Transport Operations Policy 2005 – 2008 considered developing projects with a regional focus by working with the EU on regional initiatives (e.g. TRACECA and REBIS) as a key opportunity. A second key opportunity was co-financing "of roads in the Trans-European network corridors with the EIB and EU". Another of the key sub-sectors were sea ports. Port development was considered significant, as they were facilitators of trade and maritime transport. They were deemed to have important environmental benefits against alternative modes of transport. The Policy noted that ports in the COOs faced crucial changes in cargo and passenger flows after the fall of the Soviet regime. These resulted in declining traffic volume and reduced capacity to handle new cargo in an efficient manner. Also, the Bank's intention was to promote the development of passenger terminals to support the local tourist industry in the countries on the Adriatic and Baltic seas. This Policy noted that the development of ports was not separate from the development of other modes of transport such as hinterland connections, multi-modal transport terminals and inland depots, as well as policy measures, such as customs legislation. The policy did not identify specific activities through which the Bank would implement the priorities. Monitoring indicators, baseline or target figures associated with the desired outcomes were not presented.

Transport Sector Strategy (2013)

This SS defined the role of transport as "providing the physical networks and services […] for the movement of people and goods, transport increases the access of businesses and consumers to markets and services, promotes economic diversification and regional integration, supporting growth of the wider economy". An overview of the remaining transition challenges by country was presented, specifically for the road and rail sectors. The SS noted that infrastructure bottlenecks and raising private capital as well as non-sovereign funding represented additional challenges. The transport bottlenecks remained, particularly in the port sector.

The priorities elaborated in the 2013 Transport Sector Strategy included promoting private ownership, financing and operation of transport infrastructure; supporting the creation and expansion of competitive markets for transport services; and improving the efficiency of management of public sector transport assets. Four Strategic Performance Indicators (SPIs) were presented in order to assess the transition and sustainability progress under the Strategy. These indicators were quite general, although none of them was related to regional integration. The SS acknowledges that these region-wide SPIs had limitations, given the different priorities in different countries. It adds that they are skewed towards objectives, which are measurable and have region-wide relevance. It was expected that more specific transport sector objectives would be identified in country strategies, which would better reflect the particular transition challenges and context in each of the countries.

Transport Sector Strategy (2019)

The transition challenges included in this strategy are presented by transition quality. For Integrated, these were identified as network reliability, intra-regional connectivity, and regional and international connectivity (however without further elaboration).

This strategy presents "Connected Networks" as one of its strategic directions, aiming at improved quality and connectivity of network infrastructure, including support for the roads, railways, logistic and intermodal, maritime and aviation sectors.

A performance monitoring framework is presented. Nine tracking indicators are defined for outputs in the form of number/volume of investment and number of km of roads/railway tracks. For outcomes four indicators include increase in infrastructure usage and cargo/passenger capacity. Nevertheless, no baselines or indicative targets are presented.

Energy Sector Strategy (2013)

The 2013 Energy Sector identified a key challenge in the delivery of energy in a manner that is secure, affordable and sustainable. The SS took a broad view of the energy security challenge, "recognising that diversification of sources, in particular through better integration into regional markets, can deliver it more effectively and efficiently". The main transition gap was found to be the "failure to promote diversity through open markets, the absence of sufficient physical and regulatory infrastructure to allow for effective cross-border trading and the failure to price the value of security and diversity."

The Bank's operational response to this included seven pillars. One of these pillars directly referred to regional integration: Building deep and liquid energy markets. The Bank's intention was to pursue the expansion of markets (domestic and cross border), the liberalisation of prices and more extensive private sector participation. EBRD would "support energy interconnections in order to build greater regional integration."

Energy Sector Strategy Update (2016)

The 2016 Energy Sector Strategy Update emphasised energy security and cross border infrastructure. The Bank would support operations that improved regional energy security, efficiency and promoted integration and market competition (consistent with the EU's Energy Union goals and 3rd Energy Package). Among these were investments along the Southern Gas Corridor and into gas storage facilities (UGS), North-South transmission interconnection, and integration of electricity markets. This updated document presented five performance indicators, stating that benchmark data had been collected, which would measure the countries' progress towards outcomes: energy efficiency; carbon intensity; private participation; interconnections/energy trade; and cost reflective pricing. Data was expected to be collected at the end of the strategy period in 2019.

Energy Sector Strategy (2018)

The 2018 Energy Sector Strategy (ESS) discussed maturing renewable energy markets, and identified the need to manage rising levels of intermittent renewables through regional integration. In terms of achieving transition away from coal, the strategy notes the necessity of a "sector-wide strategy to develop alternative energy supplies based on renewable deployment, regional integration, smart networks and balancing, and backup capacity from gas and other sources." The ESS identified transition challenges, including cross-border cooperation and improved interconnectivity, under the Integrated quality. It considered the absence of integrated regional markets as an obstacle to energy security and efficient energy flows within and across borders. An integrated market would encourage competition and a decrease in prices. It would also enable the integration of intermittent renewable energy sources. Small market sizes would require regional cooperation to develop liquidity. Integration could be facilitated by the establishment of cross-border energy trading mechanisms or the construction of new infrastructure.

The strategic directions for the 2019-2023 period included general groups of activities (investments, policy engagement, capacity building, TCs) for their achievement. These were presented in a monitoring framework of objectives - activities and tracking indicators for outputs and outcomes. The second strategic direction, fostering the development of energy markets and integration into regional markets, sought to support the Integrated, Competitive and Resilient transition qualities. One of the objectives was to improve gas infrastructure. Outputs were measured in terms of number of investments. Outcomes were not adequately defined as they were very general, e.g. "improved regional/cross-border energy infrastructure capacity through Bank-assisted projects" and "improved gas-infrastructure capacity through Bank-assisted projects". No specific baselines or targets were presented.

Information and Communication Technologies (2019)

A draft of the ICT SS 2020 – 2024 was submitted for Board consideration in late 2019. The key transition challenges for the Integrated quality were the need for affordable broadband access, deemed essential for regional economic integration. A performance monitoring framework was presented to measure results. Under the one strategic priority associated with the Integrated quality, "enhancement of ICT infrastructure", improvement of rural, regional and international connectivity through technology infrastructure was one of the objectives. The tracking indicators were number/volume of investments in ICT infrastructure and number/volume of access to ICT services. These were linked to CSs indicators (in relevant countries) such as net increase in ICT

infrastructure capacity (regional and/or cross-border) and number investments that improve integration into regional/global value chains.

All sector strategies for transport and energy made extensive reference to regional integration and connectivity as one of key challenges and sectoral priority. ICT strategy focused on regional/rural integration within the country, rather than cross-border.

ANNEX 9: References to regional integration in cluster projects' board reports

Cluster Project, Country	References to regional integrating in Board Report
1.Corridor Vc Bosnia & Hercegovina	None in project 38716 of 2008 but a follow-up project 47372 of 2015 stated that *the project will rehabilitate BiH's major international road corridor and therefore it is vital to the country's further integration into international markets.* Three subsequent follow-up projects (49053, 49058, 50603) had "Integrated" as their primary TI quality, stating: *The project will support BiH's regional integration through development of its main international road corridor.*
2.Corridor Vc Croatia	*By ensuring continuity with the Corridor Vc sections in Bosnia, while at the same time connecting the existing motorway networks of Croatia, the Project will allow Corridor Vc to function as a regional corridor. Upon completion, Trans-European Corridor Vc will connect Budapest to the Adriatic Sea at the Port of Ploce in southern Croatia and will be the fastest connection between north eastern and southern Croatia and the most direct route from Eastern Europe to the Adriatic. The additional section will attract traffic and trade from the whole region and will greatly improve the connectivity of Croatia with neighbouring countries: directly via Corridor Vc from Hungary and BiH, via A5 from Northern Croatia, via A1 from Southern Croatia, via A3 from Slovenia and Serbia.*
3. Azeri Roads Rehabilitation, Azerbaijan	*The project is supporting the government's priority of rehabilitating and reconstructing principal road corridors and key regional roads to enable trade and regional cooperation with neighbouring countries, and facilitating economic development across the country as a whole. The main business purpose of the operation is to contribute to the reconstruction of the key regional roads by feeding into the key corridors or directly leading to key border crossings with Georgia and Iran.* No connectivity impact was mentioned in the project's Board Report for the revised scope of 2016.
4.Pan-European Highways Ukraine	*The international corridors (including approaches to Kiev), linking Ukraine with the EU and other CIS countries are considered by the Government of Ukraine as a high priority and part of the country's preparations for hosting EURO 2012. Ukraine's export-oriented trade sector needed improved transport infrastructure in order to successfully participate in the global economy and obtain World Trade Organisation membership. Benefits will include regional economic growth and integration effects, including with the EU.*
5.DCT Gdansk Poland	*The Project not only improves connectivity by bringing the intermodal link-up closer to final destinations, it also reduces the costs of the logistics chain by up to 20 per cent. With increased container throughput, the Project will strengthen the integration of the regional transport market by: (i) expanding the most energy efficient and competitive export gateway for Polish and SEBR products, thus helping the SEBR economies to compete in the global markets, (ii) facilitating the development of new a cross-border intermodal rail transport connecting Poland with Slovakia and Hungary.* *DCT has a dedicated railway track, which links the DCT with the Polish and European network of railway lines. It is therefore a key link in the Trans-European Network – Transport ("TEN-T") Corridor No. 6 (the Baltic-Adriatic Corridor) connecting the Nordic countries with the SEBR and CEE countries.*
6.Asya Port Turkey	Regional integration was not an objective, however it was implied as the purpose of the project was construct a new port, which would be key transhipment port for the Black Sea area, effectively connecting its eight main ports in five countries.
7.Dalaman Airport Turkey	Regional integration was not mentioned, although it was implied as the original project was to finance a domestic terminal, increasing southern Turkey's connectivity with the rest of the country. The 2016 amendment focused on the loan restructuring and the change of the project's scope to international terminal, however no improved connectivity benefit was mentioned.

8.Southern Gas Corridor Azerbaijan	"Integrated" was this project's secondary TI quality (after "Resilient"). *The project will facilitate integration of regional gas markets through cross-border energy transportation. The project will interconnect regional markets, unlocking gas to European consumers. The project is expected to foster international cooperation across countries along the SGC, which would fuel regional development, assist in the creation of an integrated well-functioning European gas market and contribute to cross-regional trade and connectivity. The project will establishment of an independent regulator in line with the European best practices and support for the development of RE potential.*
9.Port of Split Croatia	Regional integration was not an objective, however the enhancement of international cruise and ferry links was implied, as extending the wharves was to substantially increase the number of large-size cruise ships calling at Split. The rearrangement of the port and relief of the Ro-Ro terminal (occupied by mid-size cruise ships) was to enable better and more frequent ferry services, including from Ancona. This was ultimately to improve the international connectivity of the middle-Adriatic Croatian coast.

ANNEX 10: Cluster projects' co-financing with other IFIs

Project	Year	Co-financing (EUR million)
BiH: Corridor Vc	2008	EBRD: 205 EIB: 300 Federation of Bosnia and Herzegovina's Ministry of Transport's Motorway's Directorate (FBHMD): 125 (equity) EBRD leading the financing, providing 40% of IFI finance
Ukraine: Pan-European Corridors	2010	EBRD: 450 EIB: 450 Ukravtodor State Road Service of Ukraine: 250 (equity) EBRD leading the financing, providing 50% of IFI finance
Croatia: Corridor Vc Completion Project	2010	EBRD: 60.63 EIB: 42.3 Hrvatske Autoceste Doo: 44.3 (equity) EBRD leading the financing, providing 60% of IFI finance
Croatia: Port Of Split Infrastructure Rehabilitation	2012	*No IFI co-financing* EBRD: 24.4 Port of Split Authority: 4.6 (equity)
Azerbaijan: Roads Reconstruction and Upgrading Project	2011	EBRD: 636.5 Other sections of the GGG highway have been financed by: World Bank: US$ 40 ADB: US$ 40.4 (US$ 54.5 for the Ganja bypass, cancelled) State Road Agency: 104.5 (equity) IFI financing on highway 2 coordinated by the World Bank but largely separate for each IFI. EBRD provided 88% of IFI finance for GGG section
Turkey : Asya Port	2013	EBRD: 83.6 IFC: 62.7 Isbank: 96.9 Asyaport Liman As: 115.49 (equity) IFC-coordinated, EBRD provided 57% of IFI finance
Poland: DCT Gdansk Expansion	2014	*No IFI co-financing* EBRD: 31.03 Group of local commercial lenders provided PLN equivalent of € 125 loan DCT Gdansk SA: 71.2 (equity)
Turkey : Dalaman Airport	2014	*No IFI co-financing* EBRD: 87.2 Unicredit Bank Austria AG: 81
Azerbaijan: Southern Gas Corridor (TANAP)	2017	EBRD: 454.6 World Bank: 363.7 AIIB: 545.6 MIGA: 682 State Oil Company of Azerbaijan: 1,084.8 (equity) No clear leader, EBRD provided 22% of IFI finance

ANNEX 11: Summary of IFIs' recent evaluations of their support for regional integration

1. IEG's report "Two to Tango - An Evaluation of the World Bank Group Support to Fostering Regional Integration"[12]

The WBG's role in promoting regional integration is three-fold:

- support clients through advisory and analytical work,
- finance projects through policy and investment loans, and
- assemble state and non-state actors for coordination and collective actions.

The WBG's evaluation department (IEG) conducted this evaluation in 2019. The objectives of this evaluation were to assess the effectiveness and comparative advantage of the WBG in fostering regional integration during 2003-2017 and presented lessons to inform future regional integration operations.

Method

The evaluation applied three sets of methods to gather the evidence related to WBG's effectiveness:

1. Portfolio review and analysis of a stratified sample of regional integration interventions;
2. Regional case studies in East Africa, Central Asia, and South Asia based on the intensity (high or low) of Bank Group regional integration activities; and
3. Econometric analysis on the macroeconomic effects of Bank Group support, construction of a regional integration index, and a data-envelopment analysis to identify frontier regions and sub-regions with the most potential for regional integration.

Main Findings

1. Overall, the Bank Group's efforts to foster regional integration have led to mostly positive development outcomes in the Sub-Saharan Africa Region and in infrastructure sectors. Bank Group regional integration efforts in other regions and sectors have been sporadic and not prioritized according to regional needs or client demand.

2. Although the IDA Regional Window program has also contributed to regional integration (mainly in the Africa Region), the development outcomes of its interventions are not significantly different from similar projects co-financed outside the program.

Comparative Advantages

The assessment revealed WBG's comparative advantage in:

[12] World Bank. 2019. *Two to Tango: An Evaluation of World Bank Group Support to Fostering Regional Integration (English)*. Corporate and process evaluation. Washington, D.C.: World Bank Group. http://documents.worldbank.org/curated/en/180771555372859192/Two-to-Tango-An-Evaluation-of-World-Bank-Group-Support-to-Fostering-Regional-Integration

1. **Global knowledge**: coverage that facilitates knowledge exchange and transfer of good practices and lessons from one region to another.
2. **Breadth of financial instruments**: E.g. Development Policy Loans centering on policy and institutional actions are potentially useful tools to prompt regional policy coordination and harmonization, considered the most difficult part of regional integration.
3. **Synergies** derived from the strength of three Bank Group institutions (IBRD/IDA, IFC and MIGA): They provide the WBG the capacity to catalyse finance and draw on synergies among its institutions for regional initiatives which cannot be entirely supported through its own balance sheet.
4. **Convening power**: Yielding from its apolitical approach and neutral position during difficult conversations with clients on regional integration issues, which makes it possible to mobilize global expertise to strengthen regional public goods.

Challenges

The previous advantages have not been fully utilized due to internal and external challenges:

1. Prevalence of the World Bank Group's single-country business model;
2. Lack of strategic prioritization of, accountability and incentive for pursuing regional integration interventions (regional projects more complex, longer and costlier);
3. Sub-optimal collaboration and partnership efforts with key stakeholders, such as the Regional Economic Communities, the private sector, regional development banks, and other development partners.

For the WBG to fully utilize its comparative advantages, it needs to address these challenges.

Conclusions

The WBG has contributed to fostering regional integration in client countries through its roles as an enabler, financier, and convener. It has nevertheless missed opportunities and not used its full potential. It has comparative advantage and untapped potential for fostering regional integration initiatives, mainly in encouraging global knowledge flows to the regions, supporting regional public goods, and strengthening sectors such as agriculture, health, and education. The IDA Regional Window has proven useful in encouraging regional integration initiatives, but its allocation criteria need recalibration.

Recommendations

1. Initiate high-level, strategic commitments to regional integration in all operational regions in addition to Sub-Saharan Africa, with tailored approaches.
2. Realign the Bank Group's business model to achieve managerial accountability both at country management unit and Global Practice levels, and create incentives for project teams.
3. Rebalance the Bank Group regional integration projects to emphasize regions with high integration potential, and regional public goods.
4. Create and promote universally accepted frameworks at the region and sector levels, and crowd-in new partners, most notably the private sector, international industry associations, and regional institutions.

5. Strengthen the design of projects supported by the IDA Regional Window, to improve the assessment of spill over effects and to generate evidence based on robust indicators.
6. Recalibrate the IDA Regional Window's resource allocation to expand support for sub-regions with high untapped potential for integration.

Fragment of the IEG's report in respect of the WBG's operations in the Central Asia region

In Central Asia, the World Bank's convening power and leadership potential remain underused, and **coordination among donors was insufficient**: all development agencies ultimately bound by their own mandates across the three countries IEG visited: Kazakhstan, the Kyrgyz Republic, and Tajikistan. The Europe and Central Asia region is **crowded with development institutions** and a wide array of efforts by regional development banks (ADB, Islamic Development Bank (IsDB), EuDB, European Bank for Reconstruction and Development (EBRD)), sovereign efforts (BRI), and donors (DFID, USAID, EU). In addition, Russia's Official Development Assistance steadily increased from about $100 million in 2004 to $1,1 billion in 2016 and is largely focused on the five Central Asian Countries. The latter amount combines both bilateral and multilateral ODA, including contributions through the World Bank-managed TFs. Although the Bank Group has maintained cordial engagements with most players especially for CAS and CPF feedback, development partner workshops, conducted by IEG mission teams in three Central Asian countries, indicated that the Bank Group's existing coordination mechanisms and discussions didn't provide sufficient clarity to partners on division of labour, or to the clients on Bank Group approaches, and didn't sufficiently strengthen the regional integration project pipeline. These issues are exacerbated by the lack of proximity with the clients and partners. Finally, within Europe and Central Asia, the Bank Group's approaches lacked deeper engagements with regional platforms and initiatives supported by other multilateral banks, most notably CAREC and SASEC, led by the ADB.

2. Thematic Evaluation Study: ADB Support to Regional Cooperation and Integration (October 2015)

The evaluation presented the findings of a review of ADB's support for regional cooperation and integration (RCI). It assessed the RCI experience and drew on lessons and evidence from the broader global experience, the evaluation offered guidance to strengthen the effectiveness of ADB's work. The findings intended to feed into the 2016 RCI operational plan.

Evaluation Assessment

Relevance:

1. The RCI agenda was rated **relevant** in terms of its alignment with RCI stakeholders' needs and demands.

2. The RCI agenda also conformed closely to international good practice

3. RCIS's design relevance was mixed. Positive aspects included demarcation of departmental responsibilities across pillars and adoption of a flexible approach to operations implementation. Less positively, the focus across the RCI pillars was somewhat unbalanced, giving pillars 2 and 3 (trade and investment; and money and financial cooperation) less relevance and weight than the other two pillars (regional and subregional programs on cross-border infrastructure and related software; and regional public goods).

4. Other ADB policies and strategies were broadly in line with the RCI agenda.

Responsiveness:

1. ADB was rated **less than responsive** in putting in place the necessary enabling environment needed to support the implementation of the RCI agenda.

2. Resourcing of the RCI agenda was found to be adequate, but institutional structures had not fully performed as intended.

3. Given limited resources, the community of practice did relatively well on knowledge (mainly sharing and dissemination).

4. Neither the Office of Regional Economic Integration nor the RCI Thematic Group regularly monitored or reported on the RCIS's results framework. Both fell short in performing their coordination role.

Results:

1. Overall, ADB's efforts were rated **significant** (second highest rating out of four), mainly due to high project success rates and positive results from regional and sector project evaluations.

2. Performance of completed and evaluated RCI projects was positive. On average 81% of projects were successful, compared with ADB's average success rate of 61%, and a non-RCI success rate of 59%.

3. RCI project designs were better than those of many non-RCI projects.

4. The value addition of the RCI work was assessed positive across the four RCIS roles.

5. The impacts of ADB's RCI work were not easy to assess, but there was some evidence that they were positive.

Findings:

1. RCI projects had been generally successful

2. Main subregional cooperation programs had been effective

3. There were important weaknesses in the RCI policies and strategies, some of which had been corrected during implementation.

4. Wide scope for future RCI work

Key Issues:

1. The classification of trade facilitation-related activities needed to be clarified

2. The project approvals database contained projects with incorrect RCI pillar classifications.

3. Clarity was needed on what constituted a regional project.

4. There was a need to ensure that subregional and cross-subregional strategic planning had Board and ADB Management direction and oversight in the future.

5. ADB needed to consider how best to address the RCI needs of graduated and middle-income countries.

6. Ongoing and future regional initiatives were considered to have major implications for ADB's future RCI partnerships.

Recommendations:

1. Broaden the RCI agenda by doing more work in pillars 2 (trade and investment), 3 (monetary and financial cooperation) and 4 (regional public goods).

2. Deepen the RCI agenda by paying greater attention to fragile, island, and linchpin countries.

3. Continue the RCI agenda in pillar 1 (cross-border infrastructure).

4. Improve intrasubregional, intersubregional and operational/non-operational RCI work coordination.

5. Strengthen country ownership in the ADB secretariat-led subregional cooperation programs.

6. Develop new RCI project models.

ANNEX 12: Selected Regional Integration Initiatives in the Bank's COOs

In addition to the European Union (of which 12 Bank's COO are members, 5 have Accession Status and 12 others are covered by the European Neighbourhood Policy), the main regional integration blocks and initiatives related to the Bank's COOs are the following:

The Eurasian Economic Union (EAEU) – is an economic union of states located in central and northern Asia and Eastern Europe. The Treaty on the Eurasian Economic Union was signed on 29 May 2014 by the leaders of Belarus, Kazakhstan and Russia, and came into force on 1 January 2015. Subsequently, Armenia and Kyrgyzstan also joined EAEU. Moreover, two of EAEU's prospective members are also COOs: Mongolia and Tajikistan, while Moldova has an observer status.

The Eurasian Economic Union has an integrated single market of 180 million people and a gross domestic product of over USD 5 trillion. The Eurasian Economic Union has sought to base its model on the European Union. The EAEU encourages the free movement of goods, services and provides for common policies in the macroeconomic sphere, transport, industry and agriculture, energy, foreign trade and investment, customs, technical regulation, competition and antitrust regulation. Provisions for a single currency and greater integration are envisioned in future. The union operates through supranational and intergovernmental institutions. The Supreme Eurasian Economic Council is the supreme body of the Union, while the day-to-day work of the EAEU is done through the Eurasian Economic Commission, the executive body of the Union.

The Eurasian Economic Union is designed to reach a number of macroeconomic objectives such as reducing commodity prices by reducing the cost of transportation of raw materials, increasing return on new technologies and products due to the increased market volume, and promoting "healthy" competition in the common market. It is also designed to lower food prices, increase employment in industries and increase production capacity. EAEU members like Belarus and Kazakhstan seek to leverage the EAEU as a bridge between the European Union and the New Silk Road economic belt.

The significant potential for developing cross-border infrastructure has led the member states and its partners to create links by constructing roads, railways, electric power grids and fibre-optic cables. For instance, historically railways have been the primary way of linking countries in the Eurasian Economic Union and the union ranks 2nd in the world in terms of railway trackage (about 7.8% of the world's share). However, it is still looking to improve cross-border trade within the union. The Trans-Asian Railway and the Asian Highway Network are cooperative projects among countries in Asia and Europe, promoted by EAEU, which have helped to improve highway and railway systems across the region. Six of the eight major Asian highways go through the Eurasian Economic Union (the AH3, AH4, AH5, AH6, AH7 and the AH8). The highways connect the EAEU to many countries including Finland, Turkey, Iran, Pakistan, India, Laos, Thailand, Burma and China. AH6 goes through Russia's Trans-Siberian Highway, which is over 11,000 kilometers long. The Trans-Siberian Highway is one of the longest national highways in the world. Another project - the Eurasian Land Bridge allows goods to be transported by rail from China and the EAEU to Europe. An expansion of the original railway line named the New Eurasian Land Bridge provides an uninterrupted rail link between China and the EAEU. Talks with China, India and Burma are ongoing to expand the railway network. Moreover, Russia, North Korea and South Korea intend to cooperate to expand the Eurasian Land Bridge to connect the peninsula. Advantages of exporting products by rail through the EAEU are reduced shipping times and reduced costs. The

railways also have the potential for expansion, with the future creation of high-speed railway lines being considered.

Union for the Mediterranean (UfM) – established in 2008 between the EU and the countries around the Mediterranean Sea, this programme includes the Bank's EU and SEMED countries, and Turkey**.** It is not yet an economic union, rather a looser block supporting integration through specific projects, aimed at increasing the countries' socio-economic development and ensuring stability in the region.

Transport Corridor Europe-Caucasus-Asia (TRACECA) – a programme established in 1993, involving the EU and 14 member States of the Eastern European, Caucasian and Central Asian region. Its members include the Bank's Caucasus and Central Asian COOs, as well as Turkey and Ukraine. The programme aims to strengthen economic relations, trade and transport in the regions of the Black Sea basin, South Caucasus and Central Asia

The Central Asia Regional Economic Cooperation (CAREC) Program is a program established in 1997 by the Asian Development Bank (ADB) to encourage economic cooperation among countries in the Central Asian region. 11 countries participating in CAREC include the Bank's 8 Central Asian and the Caucasus COOs, as well as Afghanistan, Pakistan and China (two northern Autonomous Regions). EBRD is one of several "Partner Institutions" of CAREC.

The program is a proactive facilitator of practical, results-based regional projects, and policy initiatives critical to sustainable economic growth and shared prosperity in the region. Since its inception in 2001 and as of September 2019, CAREC has contributed to the mobilization of more than $34.5 billion investments that have helped establish multimodal transportation networks, increased energy trade and security, facilitated free movement of people and freight, and laid the groundwork for economic corridor development.

"CAREC 2030" provides the new long-term strategic framework for the program leading to 2030. It is anchored on a broader mission to connect people, policies and projects for shared and sustainable development, serving as the premier economic and social cooperation platform for the region. CAREC's development partners facilitate financing for regional projects that benefit the entire CAREC region, and also ensure the quality of investments made by providing strategic and technical advice.

Helping to increase cross-border connectivity of countries participating in the CAREC programme has been one of its main tasks. It has been coordinating (usually at conceptual stage) financing of several railway and highway projects. It also contributed to the development of the Railway Strategy and Highway Safety Strategy for the region. For instance, the Azeri Roads project (see annex 2) was part of CAREC's programme in which EBRD participated.

Three Seas Initiative - also known as the Baltic, Adriatic, Black Sea (BABS) Initiative, is a forum of twelve states in the European Union, located in Central and Eastern Europe. The combined area connects the Adriatic Sea, Baltic Sea, and Black Sea. The initiative aims to create a regional dialogue on a variety of questions affecting the member states. The Three Seas Initiative has twelve member states along a north–south axis from the Baltic Sea to the Adriatic Sea and the Black Sea: Austria, Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia. It aims to increase co-operation among participating countries, in the field of energy, transport and communications infrastructure, particularly strengthening north-south corridors. During the third summit the participants approved a list of priority interconnection projects in the three key areas – transport, energy and digital.

The initiative is closely related to two major infrastructure projects in the region: (i) a north–south highway "Via Carpathia", connecting Klaipėda in Lithuania with Thessaloniki in Greece and (ii) Liquefied natural gas infrastructure, with sea terminals in Poland and Croatia and a connecting pipeline. Other projects are the Baltic-Adriatic Corridor, Via Baltica road, Rail Baltica and Amber Rail Freight Corridor rail connections.

In 2019, Bank Gospodarstwa Krajowego of Poland and Export–Import Bank of Romania signed the founding act of the Three Seas Initiative Investment Fund. It is to focus on projects creating transport, energy and digital infrastructure in the Three Seas region. Private investors from pension funds, private investment funds, and other entities will also be invited to the fund. The aim is to raise up to EUR 3-5 billion. The Fund will engage, on a commercial basis, in infrastructure projects with a total value of up to EUR 100 billion, while the needs of the Three Seas region have been estimated at over EUR 570 billion. The fund is to activate other sources of financing, such as the resources of individual countries of the region, IFIs' or EU funds.

The Belt and Road Initiative (BRI) - is a global development strategy adopted by the Chinese government in 2013 involving infrastructure development and investments in 152 countries. "Belt" refers to the overland routes for road and rail transportation, called "the Silk Road Economic Belt"; whereas "road" refers to the sea routes, or the 21st Century Maritime Silk Road. The Chinese government calls the initiative "a bid to enhance regional connectivity and embrace a brighter future". Some observers see it also as a push for stronger Chinese influence in global affairs with a China-centered trading network. The project has a targeted completion date of 2049, which coincides with the 100th anniversary of the People's Republic of China. Nevertheless, BRI is to primarily benefit the participating countries, addressing their "infrastructure gap" and thus accelerating economic growth across the Asia, Africa and Central and Eastern Europe[13].

The Belt and Road Initiative is about improving the physical infrastructure along land corridors that roughly equate to the old silk road. Infrastructure corridors encompassing around 60 countries, primarily in Asia and Europe but also including Oceania and East Africa, will cost an estimated US$4–8 trillion. The projects receive financial support from the Silk Road Fund and Asian Infrastructure Investment Bank while they are technically coordinated by the B&R Summit Forum. The key land corridors include:

- The New Eurasian Land Bridge, which runs from Western China to Western Russia through Kazakhstan, and includes the Silk Road Railway through China's Xinjiang Autonomous Region, Kazakhstan, Russia, Belarus, Poland and Germany.
- The China–Mongolia–Russia Corridor, which will run from Northern China to the Russian Far East. The Russian government-established Russian Direct Investment Fund and China's China Investment Corporation, a Chinese government investment agency, partnered in 2012 to create the Sino-Russian Investment Fund, which concentrates on opportunities in bilateral integration.
- The China–Central Asia–West Asia Corridor, which will run from Western China to Turkey.
- The China–Indochina Peninsula Corridor, which will run from Southern China to Singapore.

[13] It is estimated that Asia, excluding China, requires up to US$900 billion of infrastructure investments per year over the next decade, mostly in debt instruments, 50% above current infrastructure spending rates. This gaping need for long term capital explains why many Asian and Eastern European countries joined BRI.

- The China–Pakistan Economic Corridor (CPEC), which is also classified as "closely related to the Belt and Road Initiative", a US$62 billion collection of infrastructure projects throughout Pakistan, which aims to rapidly modernize Pakistan's transportation networks, energy infrastructure, and economy.

Some of these investments have already been realised. On 13 November 2016, CPEC became partly operational when Chinese cargo was transported overland to Gwadar Port for onward maritime shipment to Africa and West Asia. The first long container train from Xian, China arrived in Slawkow Logistics Park, Poland on 6 January 2020 after 12 days of journey via the New Eurasian Land Bridge.

Annex 13: Management Comments

Executive Summary

- Management welcomes the draft EvD Study on Projects Supporting Cross-Border Connectivity (Regional Integration), as a timely and interesting. The wide coverage of the types of projects contributing to regional integration is also welcome.

- The study recommendations focus on the Bank's approach to support regional integration, recommending a separate strategy, the way the Bank targets its engagements in this area, as well as learning from the experience through an assessment of factors that affected our ability to achieve private sector enhancement and policy- related objectives in large infrastructure projects.

- Management welcomes and shares the view that regional integration is an important area for the Bank's continued efforts to improve the effectiveness of our support, including through improved narrative and learning from the experience through an assessment of large infrastructure projects. Nevertheless, Management believes support to regional integration does not require a separate strategy. Thematic strategies are typically temporary in nature and are designed to help focus efforts and incentives to scale up EBRD engagement in a particular area, particularly when other tools have yet to be developed. In the case of regional integration, "Integrated" is one of the six Transition Qualities under the updated transition concept and the methodology for transition impact assessment and already provides incentives to target projects that support integration. Management notes that - as recognised in the study - regional integration is an important priority area identified in both the Transport Sector and Energy Sector Strategies as well as a number of Country Strategies. Management believes that the link to country strategies is the most important. EBRD leverages these strategies to prioritise and operationalize integration as a key transition quality based on a transition gap analysis and country diagnostics. This will be a priority area for the Bank in particular in countries where economic potential is hampered by lack of regional integration such as in the Western Balkans, Central Asia and the SEMED region. A separate strategy on regional integration would not have a clear ownership in the organisation (as it covers the work of many teams) and, importantly, may create confusion and undermine the central role of country strategies as the Bank's key planning tool for achieving impact.

- Management recognises the role of the Bank in facilitating Regional Integration and agrees to leverage the available instruments to target appropriate engagements in both investments and policy in countries with the largest gaps. The Assessment of Transition Qualities (ATQ) is updated annually for the Integrated quality, based on a number of indicators and is the basis for a deeper dive on key challenges in country diagnostics. Country diagnostics are used to prepare country strategies that include key priorities and objectives and in turn guide our investments and policy engagement in a country. The ATQ assessment is also used as part of the transition impact assessment of projects (ex-ante TOMS) to incentivise investment and policy in countries with the largest integrated gaps to help the selection and design of our investments.

- Finally, Management recognises the importance of adequate information collection systems to enable the measurement of impact.We currently use the Compendium of indicators for this purpose and are developing other methods to collect data and reduce clients' costs. Management will continue to refine the indicators in the compendium

through internal and external calibration exercises (such as MDB indicator harmonisation efforts), and use innovative ways to improve measures of impact on regional integration. Additional Bank's instruments include, for instance, the development of transit data and measurement of connectivity using Google Maps big data.

Management comments focus on the EvD's study recommendations followed by a few comments on the analysis and findings. Detailed comments that we provided at the draft stage are already incorporated by EvD in this final version of the study.

1. Study Recommendations

Recommendation 1:
Prepare for Board approval a Bank-wide strategy for Regional Integration, including cross-border connectivity, to establish agreed objectives, priority sectors/sub-sectors, potential investment types, directions of policy dialogue and TC support areas

Management disagrees with this recommendation. Management welcomes and shares the view that regional integration is an important area for the Bank and we should continue efforts to improve the effectiveness of our engagements. Nevertheless, Management believes that the Bank's support to regional integration does not require a separate strategy. As a demand driven organisation the Bank will continue to focus efforts in targeting Integrated as a quality in projects, acknowledging that setting targets (e.g. number or volume of operations or policy interventions) is neither feasible nor desirable for an organisation primarily focused on private sector operations. To aid future evaluability of EBRD interventions and operations, Management will further develop details of the Theory of Change underpinning the Transition Qualities (as part of the Joint Action Plan following-up on Kirk's Report recommendations with a update on results architecture in a Board Information Session organised in due course in Q2 2020).

Management would like to note that - as recognised in the study - regional integration is an important priority area identified in both the Transport Sector and Energy Sector Strategies as well as a number of Country Strategies. These strategies outline the key objectives, approach and types of instruments (including investments and policy engagement) the Bank would use to achieve impact across specific priorities such as regional integration. Moreover, EBRD leverages these strategies to prioritise and operationalise integration as a key transition quality based on a transition gap analysis and country diagnostics. The Sector Strategies identify key directions based on sector trends, developments and relevant transition challenges in the region; whereas the Country Strategies define the Bank's operational priorities and expected transition results at the country level over the strategy period.

Management notes that thematic strategies are typically used in the Bank to help focus efforts and incentives to scale up new EBRD strategic initiatives, for instance, for early transition countries, small business, etc., which have now been mainstreamed as part of the introduction of the new transition concept and six transition qualities. Since "Integration" is at the core of the updated transition concept and assessment methodology, Management believes there are strong incentives to focus on regional integration and connectivity. Management nevertheless recognises the merit and will continue its efforts to develop a better narrative around regional integration as a way to better understand and further support this important agenda. Management suggests that this improved narrative on regional integration, including on how to coordinate with key partners and other MDBs can be addressed through a Board Workshop or a Board information session.

Recommendation 2: *Target integration-related investments and particularly policy dialogue towards countries with the largest ATQ gap score for Integrated quality, i.e. in Central Asia, the Balkans and SEMED, actively pursuing opportunities in integration-boosting sub-sectors, such as rail, ports and airports*

Management supports the recommendation to target integration - related investments and policy dialogue- towards countries with the largest gaps. Currently, EBRD measures the transition gap along the "Integrated" transition quality through the yearly Assessment of Transition Qualities (ATQ) that includes an analysis of the challenges in cross-border transportation and other institutional and policy related challenges. This analysis is further developed and contributes to the country diagnostics and strategies. Such diagnostic analysis is a significant part of any country and sector strategy (e.g. Transport or Energy).

The ATQ assessment informs our activities also because it is used as part of the transition impact assessment (ex-ante TOMS) to incentivise investment and policy in countries with the largest integrated gaps and thus help the selection and design of our investments. In addition, the BEEPS survey conducted every 2-4 years also specifically focuses on key business environment issues related to infrastructure development. Finally, Management also prepares special studies on Integration (e.g. on Logistics in Kazakhstan; Central Asian connectivity). These analytical tools help to inform the Bank's policy engagements with the government and to align them with national infrastructure priorities. The analysis also contributes to EBRD's cooperation with other players such as the EU, which is a key institution that supports regional integration and defines strategic international corridors.

Recommendation 3: *For projects targeting Integrated, ensure adequate system is in place for gathering relevant data to measure it, either by the client or by the Bank*

Management agrees with this recommendation. Management notes that the Compendium of Indicators at includes a number of indicators that measure results relevant to integration and connectivity Monitoring indicators for projects that target integration take into account their feasibility and the client and country capacity to gather the relevant data. Management would also like to note that the Bank is in the process of developing more refined measures of connectivity (e.g. using Google Maps Application Programming Interface), to automate the process for collecting travel times and speed data across a large number of road links.

Management will continue to refine the indicators through internal and external calibration exercises (such as MDB indicator harmonisation efforts), Management is working also on other methods to reduce client cost and collect data, using innovative ways to improve measures of impact on regional integration (as per the measure described above). For some indicators (e.g. road use) data gathering will require additional resources to support client and internal capacity building.

The Transition Report 2017-18 found that integrated infrastructure can significantly reduce transhipment times and costs even if the impact on the overall traffic may be lower-than-projected (as highlighted in the report). Similarly, the 1997 concept of transition highlighted the importance of bringing down infrastructure-related transaction costs, as acknowledged in the EvD report (page 5).
Furthermore, Management would like to note that indicators such as travel times could now be collected without burdening clients with the cost. By using Google Maps AGI, it may not be necessary or desirable to collect such data from clients (page 23 states that "two clients provided some data on time/cost savings"), not least because clients often count traffic on road sections differently, as page 22 of the report acknowledges. Reduced travel times could in turn be linked to outcomes such as increased trade through additional analysis, as was done in the Transition Report 2017-18.

Recommendation 4: *Conduct a focused assessment of why most of private sector enhancement and policy- related objectives of large infrastructure projects failed.*

Management notes the value of understanding lessons learned from past projects. Management agrees to undertake a high-level assessment and analyse the reasons why we did not succeeded to achieve the objectives related to private sector enhancement and policy- related objectives for

some large infrastructure projects that form part of the study. Management will share the findings internally with relevant teams to feed back as lessons learnt for future engagements. Management notes however that a number of such objectives were not directly related to integration (but for instance commercialisation and outsourcing of activities).

2. Comments on the analysis and related findings

Management welcomes the discussion on customs and immigration procedures and always encourages and supports bilateral initiatives. Nevertheless, it recognises that the limitations of the Bank influence on its own as addressing these issues systematically would require overarching engagements with governments often done by the EU or World Bank. In Western Balkans, for example, the EU targets a range of "Soft Measures", which includes cross border protocols, defining freight corridors, opening of rail and electricity markets etc. The most effective role for the Bank would be to support measures promoted by the EU, for example, through loan covenants, as is currently the practice.

Management disagrees with the conclusion that road projects have less integration impact than railroad projects since roads are less suitable for cross-border, long-distance transportation, in particular for distances over 300km. This is conclusion is not supported by wider evidence from advanced economies or indeed by the methodology or evaluation of projects in this study, where road and rail were never compared directly. Management believes there are a number of factors that influence mode of transport. In certain specific cases, such as very long distance transport for bulk commodities, it is clear that rail transportation is more competitive. However, roads are a key part of integration in all advanced economies and industries. In some countries (e.g. Ukraine) goods of higher value, or goods less suited to rail transportations are transported by roads despite distances exceeding 300km. In some countries rail network coverage does not provide enough flexibility for efficient transportation. Technical and cost considerations are also the reason why rail might not be more economic than roads for transporting goods over distances of 300km. Often road projects can be built in difficult terrain where rail projects would be far more expensive. The study also looked at passenger transport, where both road transport and aviation have a very strong impact on integration, arguably much stronger than rail for cross-border connectivity.

Based on the experience, Management would like to reiterate its view that financing projects in more than one country as a combined project and not on a "national" basis, it is unlikely to work as most projects in the road and rail sector are financed on a sovereign basis. Many cross-border multiple county/government privately financed connectivity projects have been beset with problems or failed entirely. Laws and legislations are different between two or more countries and the private sector requests sovereign guarantees from one government. Such connectivity strategies have been better achieved as programmes of single in country projects linked together with common technical and capacity standards. This is incentivised through one or more MDBs coming together to create funding and financing packages around the programme but mandating that to benefit from these the individual countries must adopt the standard specifications and overarching connectivity ambitions.

Management notes that projects supporting integration accounting for 8% as cited in the study does not take into account that transport projects that support the Integrated quality are few but large in volume (so they account for a small share of projects, but a larger share of business volume). Management would like to highlight that traffic generally is highly correlated to GDP, hence both Bank's and its external consultants forecasting is linked to GDP. Management also notes that while receiving data on impact is important, the Bank has to be selective and consider private sector client protection due to sensitive for some types of data (e.g. for ports).