

DRAFT SECTOR REPORT ON

TRANSPORT

For Discussion: Transport Sector Session

Preparatory Senior Officials' Meeting on Central Asia Economic Cooperation
13-14 September 2004
Almaty, Kazakhstan

CENTRAL ASIA REGIONAL ECONOMIC COOPERATION PROGRAM
SENIOR OFFICIALS' MEETING
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TRANSPORT SECTOR REPORT

I. Performance in 2003 and Outlook

1. The economies of the Central Asia regional economic cooperation (CAREC) participating countries¹ generally showed strong growth in 2003 (Appendix 1). Despite the war in Iraq and the outbreak of the severe acute respiratory syndrome epidemic, GDP grew by more than 9% in Azerbaijan, Kazakhstan, Tajikistan, and the People's Republic of China (PRC).² GDP growth in the Kyrgyz Republic, Mongolia, and Uzbekistan was also higher than 2002. Resilient performance of external trade was one of the driving forces of growth. Exports increased significantly as a result of higher world prices of commodities³ and large inflows of foreign direct investment into the export-oriented sector. Imports showed double-digit growth primarily because of the rising demand for raw materials in the PRC, and for capital and consumer goods in other CAREC participating countries.

2. Strong GDP and trade growth triggered resilience in the transport sector of the CAREC participating countries. The volume of freight and passenger traffic increased in Kazakhstan, Kyrgyz Republic, Mongolia, Uzbekistan, and the Xinjiang Uygur Autonomous Region of the PRC in 2003 (Appendix 2). The rate of growth was more than 10% in Kazakhstan, Mongolia and Xinjiang of the PRC for freight traffic, and in Uzbekistan in terms of passenger traffic. Railway traffic increased since railways carried the majority of exports and imports. Road traffic soared due to the rapid increase in vehicle ownership and improvement of the national and regional road networks.

3. The medium-term outlook for the transport sector in the CAREC participating countries is promising. Given projected continued economic growth in the region and encouraging prospects for major developed countries over the next 2–3 years, the demand for freight traffic is projected to grow at about the same rate as GDP while the demand for passenger traffic is expected to rise somewhat faster over the medium term. Annual growth rate is projected at 2–3% for railway traffic and 4–7% for road traffic, respectively.

II. Progress of Cooperation Since the 2nd Ministerial Conference

4. The key activities and progress made on cooperation in transport since the 2nd Ministerial Conference in Tashkent in November 2003 are summarized below.

5. First, multilateral institutions⁴ provided continued lending assistance to the governments of the CAREC participating countries to support investments in improving the regional transport

¹ The CAREC participating countries comprise Azerbaijan, Kazakhstan, Kyrgyz Republic, Mongolia, People's Republic of China (PRC), Tajikistan, and Uzbekistan.

² GDP in Xinjiang Uygur Autonomous Region of the PRC grew by 10.8% in 2003.

³ These commodities include oil, gas, gold, aluminum, copper, cotton, and cashmere, which are the principal exports of the CAREC participating countries, except for the PRC.

⁴ Multilateral institutions refer to the Asian Development Bank, the European Bank for Reconstruction and Development, the International Monetary Fund, the Islamic Development Bank, the United Nations Development Programme, and the World Bank.

networks (Appendix 3). Since November 2003, the Asian Development Bank (ADB) have approved two loans totaling \$52.1 million for two transport projects, one for rehabilitating part of the road between Dushanbe and the Kyrgyz border (phase I) and the other for developing the remaining section of Mongolia's north-south road corridor to link the PRC and Russia through Mongolia. ADB is also processing a loan for the Kyrgyz southern transport corridor road (Osh-Sary Tash-Irkeshtam) rehabilitation project, which is scheduled for ADB Board consideration in the fourth quarter of 2004. In addition, ADB approved a technical assistance grant to Azerbaijan to study the feasibility of a project for rehabilitating the Yevlax-Ganja section of the road between Baku and Georgia for possible ADB financing. During this period, the European Bank of Reconstruction and Development (EBRD) approved €128.1 million in loans for two transport projects, one for upgrading the road between Aktau and Atyrau in Kazakhstan and the other for reconstructing the Hacıqabul-Kurdamir section of the Baku-Georgian road in Azerbaijan. The Islamic Development Bank (IsDB) approved a loan to Azerbaijan for reconstructing the Ujar-Yevlax section of the Baku-Georgian road.

6. Second, multilateral institutions continued advisory assistance to the CAREC participating countries on transport related issues. ADB approved an advisory technical assistance grant for Tajikistan to strengthen road maintenance in December 2003. In response to a request from Kazakhstan on behalf of the Central Asia Cooperation Organization (CACO)⁵ in September 2003, multilateral institutions provided support for the establishment of a transport consortium of CACO. In close coordination with other multilateral institutions, ADB has been playing a lead role in such support, providing comments on the draft concept of the transport consortium and preparing a proposal for implementation. The World Bank has completed a study on trade and transport facilitation in Central Asia and plans to present its findings and recommendations at the Senior Officials Meeting (SOM) in Almaty in September 2004. In addition, ADB continued its efforts to strengthen transport links and cooperation between Central and South Asia, and convened a working group meeting on transport and trade in Central and South Asia in Dubai, United Arab Emirates on 4–5 March 2004.⁶

7. Third, based on the request from various CAREC participating countries and the decision of the 2nd Ministerial Conference in Tashkent, the Transport Sector Coordinating Committee (TSCC) was established. The participating countries nominated their focal points for this committee and the inaugural meeting of the TSCC was held in Almaty from 30 June to 1 July 2004, co-chaired by Kazakhstan and ADB. At the meeting the delegations reaffirmed transport as one of the priority areas for cooperation in Central Asia as a means to promote sustained economic growth and reduce poverty. The delegations endorsed the following strategic priorities for the improved transport systems in Central Asia: (i) development of regional transport corridors, (ii) harmonization of the regulatory framework, (iii) simplification of cross-border procedures, (iv) restructuring and modernization, (v) marketing and tariff identification based on competition, and (vi) improvement in financing and management. The implementation status of the meeting agenda is as follows.

- **Sector Road Map.** The Secretariat circulated the draft regional transport sector road map to all the participating countries for review on 12 August 2004. The draft regional

⁵ The Central Asia Cooperation Organization comprises Kazakhstan, Kyrgyz Republic, Tajikistan, and Uzbekistan.

⁶ The objectives of the meeting were to (i) review pending matters related to the establishment of the Central and South Asia Transport and Trade Forum, (ii) review the background studies prepared by ADB on customs harmonization, border infrastructure, and law enforcement on drug and human trafficking and money laundering, and (iii) determine the date and venue of and prepare the agenda for the Second Ministerial Conference on Trade and Trade in South and Central Asia. Senior officials from Afghanistan, Iran, Pakistan, Tajikistan, Turkmenistan, and Uzbekistan and representatives from the World Bank participated in the meeting.

transport sector road map will be further discussed at the SOM in Almaty in September 2004.

- **Gap Analysis.** ADB is considering an increase in grant resources for technical assistance to the CAREC participating countries in the transport sector.
- **Identify Requirements for External Financing.** Kazakhstan provided the Secretariat with a list of investment projects for 2004–2008 on 22 July 2004 (Appendix 4).
- **IFI Work Program.** The Secretariat has prepared a consolidated assistance program of multilateral institutions in 2004–2006 to be presented at the SOM for discussion in September 2004.

With the guidance and support from the participating countries, the TSCC is developing effective mechanisms for coordination and implementation of cooperation activities in the transport sector.

8. Fourth, multilateral institutions made further efforts to strengthen their cooperation in support for regional cooperation in transport. Major activities in this regard included:

- Active participation in the SOM on 15–16 April 2004 and the Inaugural Meeting of the TSCC from 30 June to 1 July 2004.
- Joint preparation of the Transport Sector Report for the SOM to be held in Almaty in September 2004 and the 3rd Ministerial Conference to be held in Astana from 31 October to 1 November 2004.
- Joint preparation of the work program indicating the lending and non-lending activities in 2004–2006 for discussion at the SOM in Almaty in September 2004.
- Joint participation in the three meetings with heads of working groups of CACO providing support for the establishment of the transport consortium.

III. Challenges in Transport and Proposed Actions

A. Development of Regional Transport Corridors

9. Development of regional transport corridors is crucial for promoting economic growth and poverty reduction in Central Asia and integration of the region with the rest of the world. Despite recent improvements, the existing transport networks in Central Asia cannot fully meet the needs of the reviving regional economies. There is a lack of direct road connections to state capitals, production centers, markets, and ports. The dislocations caused by the breakup of the railways into national units have resulted in numerous cross-border operational obstacles. Many regional roads and railways are in poor conditions due to inadequate maintenance, which limits the expansion of trade and transport services. There is a need of further investments to improve transport infrastructure and develop well-connected regional transport corridors.

10. In recognition of this, the CAREC participating countries plans to make greater investments in improving transport infrastructure. Kazakhstan proposes to invest nearly \$5 billion for developing transport corridors over the medium term (Appendix 4).

11. Multilateral institutions will continue to support development of regional transport corridors by providing public sector lending and helping mobilize cofinancing resources. A

consolidated assistance program of multilateral institutions for lending and non-lending products in 2004–2006 is provided in Tables 1 and 2, respectively, of Appendix 5. The program shows a total of 23 loan projects amounting to \$546.9 million for developing east-west and north-south transport corridors in the CAREC participating countries in 2004–2006 (Appendix 4, Table 1). The major projects likely to be supported in the road sector are the Kyrgyz southern transport corridor, east-west and north-south corridors in Azerbaijan, the Aktau-Atyrau and Borovoe-Petropavlovsk corridors in Kazakhstan, and the Dushanbe-Kyrgyz corridor in Tajikistan. In the railway sector, a regional railways rehabilitation project to strengthen the Uzbekistan-Afghanistan link and a north Tajik railway improvement project are included in the program. In addition, a regional traffic enhancement project is proposed. ADB plans to provide \$334.9 million loans while IsDB loans will amount to \$212 million. ADB and IsDB will explore cofinancing from OPEC and the Saudi Fund for the projects in Azerbaijan, Kyrgyz Republic, and Tajikistan. In addition, EBRD proposes a \$7.4 million loan for an air fleet upgrade project in Tajikistan.

B. Harmonization of the Regulatory Framework

12. A harmonized regulatory framework is vital to creating a level playing field for transport companies to achieve efficient transport and transit systems in the region. Lack of harmonized transport regulations results in an incomplete and nontransparent regulatory framework; lack of common standards (e.g., on technical aspects, tariff, traffic safety, and vehicle weight control) among regional countries; nonconformity with best international practices; road permit quotas for foreign vehicles that restrict competition, a skewed rules for transport services, road user charges not related to costs of road use, discretionary tariff setting, and discriminatory transit fees. It is important that the CAREC participating countries make efforts to harmonize the regulatory framework to enable efficient and effective use of the corridors for transit and transport.

13. The CACO has recently developed a concept of the establishment of a transport consortium, which will aim to, among others, harmonize transport sector regulations and policies among the CACO members (i.e., Kazakhstan, Kyrgyz Republic, Tajikistan, and Uzbekistan). Multilateral institutions support this initiative and stand ready to provide assistance for implementation. Based on the experience gained, they will help harmonize the transport regulatory framework covering all the CAREC participating countries.

C. Simplification of Cross-Border Procedures

14. Simplified cross-border procedures are essential to achieving efficient regional transport operations. The transport sector studies on Central Asia highlighted the issue on inefficient and excessive bureaucratic cross-border requirements, which are not based on international best practices or international conventions. These procedures, mainly related to customs, visas, quarantines, and other cross-border formalities, are time-consuming, complicated, and expensive. It has resulted in considerable transport delays at borders and increased transport costs. Concerted efforts from the CAREC participating countries are needed to establish simplified cross-border procedures to expedite cross-border traffic.

15. The CAREC participating countries have taken steps in this regard. With assistance from the United Nations Conference on Trade and Development, a draft Transit Traffic Framework Agreement (TTFA) is being negotiated among Mongolia, the PRC, and the Russian Federation. The CACO also plans to simplify cross-border procedures among its members under the proposed transport consortium. ADB will assist Mongolia and the PRC in developing simplified

cross-border procedures under the Regional Road Development Project approved in July 2004. ADB has participated in ongoing negotiations on the draft TTFA, and is considering assistance to Mongolia and the PRC for implementation of the TTFA. In addition, ADB has programmed technical assistance for 2006 to support the harmonization of cross-border initiatives for the transport sector in Central Asia. The TA will analyze the current status of cross-border procedures in Central Asia, and help prepare an action plan to develop common minimum standards and procedures on border crossing. The World Bank also plans to provide TA for conducting a transport and trade facilitation workshop in Central Asia in 2005.

D. Restructuring and Modernization

16. Restructuring and modernization of the transport sector is an important component of the strategic priorities for improving the transport systems in Central Asia. However, the monolithic and monopolistic nature of the organizations in the railway sector has led to a lack of competition in railway service supply, lack of open regional procurement practice, unclear basis for commercial management and investment, lack of management information tools, obsolete rolling stock, and outdated internal telecommunications technology. In addition, tariff setting is not based on competition and does not separate movement and terminal costs. Given the majority of foreign trade being carried by rail in Central Asia,⁷ restructuring and modernization of the railway sector is vital to the development of efficient regional transport services.

17. Multilateral institutions will continue to support the efforts from the CAREC participating countries in restructuring and modernization of the railway sector. ADB and IsDB plan to provide three loans with a total amount of \$70 million to the railway sector in Tajikistan, Turkmenistan, and Uzbekistan in 2004–2006. In addition, technical assistance from ADB is also proposed for Kazakhstan and Uzbekistan in 2005 to support policy, institutional, and corporate reforms, and to assist in preparation of an investment plan in the railway sector. Further assistance will be considered to promote development of a competitive railway sector in the region.

E. Improvement in Financing and Management.

18. Improving financing and management in the transport sector is the greatest challenge faced in Central Asia. The road sector in many CAREC participating countries has failed to receive adequate funding for maintenance. This led to the consequence that while investments are being made in the road sector, the existing road network is deteriorating and deferred road maintenance has been accumulated in these countries. This poses a threat to road sector development and effective regional cooperation in transport. Moreover, the institutional capacity of government agencies in the transport sector in many CAREC participating countries remains limited. This results in a lack of sound planning of transport infrastructure investment; road design standards that do not conform to economic fundamentals and lack safety features, roadside services, and telecommunication facilities; weak financial management; inadequate capacity of managing project implementation; and a lack of effective monitoring mechanism and indicators. Increased financing in the transport sector, particularly for road maintenance and improved transport sector management can significantly contribute to development of an efficient regional transport system in Central Asia.

⁷ The railway sector carries about 94% of exports and 80% of imports in Central Asia. ADB. *Draft Sector Note on Transport*, prepared for discussion at the Transport Sector Session of the Regional Preparatory Meeting in Tashkent on 27–28 September 2003.

19. Multilateral institutions will continue to help improve financing and management in the transport sector in the CAREC participating countries. Public sector loans will be provided to various CAREC participating countries in 2004–2006 to finance transport investment projects and continue policy dialogue on increased road maintenance funding, and enhance the capacity for improved governance in the transport sector. Such assistance will address fiscal constraints of the governments concerned and attract private sector investments. Moreover, eight TA grants from ADB, IsDB, and the World Bank are proposed to (i) update trade and transport audits; and (ii) build up the capacity for regional road planning, funding for road maintenance, and effective management of project implementation in these countries.

Table: GDP and Trade Performance Indicators for CAREC Participating Countries, 2003
(% changes over 2002)

Countries	GDP	Exports	Imports
Azerbaijan	11.2	13.9	49.3
Kazakhstan	9.2	26.0	14.1
Kyrgyz Republic	6.7	18.5	21.9
Mongolia	5.5	11.1	7.1
Tajikistan ^a	10.2	14.2	23.2
Uzbekistan	4.4	29.1	10.0
People's Republic of China	9.1	34.6	41.0
of which, Xinjiang Uygur Autonomous Region	10.8	94.3	61.2

^a Preliminary figure.

Sources: Governments of the CAREC participating countries.

Table: Growth of the Volume of Traffic in the CAREC Participating Countries, 2003
(% changes over 2002)

	Freight Traffic	Passenger Traffic
Azerbaijan	n.a.	n.a.
Kazakhstan	11.6	2.3
Kyrgyz Republic	5.7	0.5
Mongolia	13.6	6.5
Tajikistan	n.a.	n.a.
Uzbekistan	4.4	12.1
People's Republic of China of which, Xinjiang Uygur Autonomous Region	10.2	3.4

Source: Governments of the CAREC participating countries.

Table: Loans Approved by Multilateral Institutions Since October 2003

Project Title	Country	Loan Amount (million)	Approval Date	Brief Project Description
Asian Development Bank				
Dushanbe–Kyrgyz Border Road Rehabilitation (Phase I) (Loan 2062)	Regional TAJ	US\$15.0	18 Dec 2003	To rehabilitate the 140 km Dushanbe-Nurobod section of the road linking Tajikistan to the Kyrgyz Republic and onward to the PRC.
Regional Road Development (Loan 2087)	Regional MON	US\$37.1	22 July 2004	To develop the remaining section of the road to link the PRC and Russia via Mongolia.
European Bank for Reconstruction and Development				
Road Sector Restructuring	Regional KAZ	€94.6	2003	To upgrade the 900 km section of the road between Aktau and Atyrau.
Silk Road	Regional AZE	€33.5 (US\$41.0)	June 2004	To reconstruct the 85 km Hacıqabul-Kurdamir section of the road between Baku and Georgia.
Islamic Development Bank				
Reconstruction of the Ujar-Yevlax Road	Regional AZE	\$22.0	22 Oct. 2003	To reconstruct the 53 km Ujar-Yevlax section of the road between Baku and Georgia.

AZE = Azerbaijan, KAZ = Kazakhstan, MON= Mongolia, TAJ = Tajikistan.

Sources: Websites of the Asian Development Bank, the European Bank for Reconstruction and Development, and the Islamic Development Bank.

Multilateral Institutions' Assistance Pipeline for the Transport Sector, 2004–2006

Table 1: Assistance Pipeline for Lending Products

Project Title	Country Involved	Lending Agency	Amount (US\$ million)	Proposed Year for Approval
<u>2004 Loans</u>				
1. Regional Road Development	MON/PRC	ADB	37.1	2004 (Approved on 22 July)
2. Aktau-Atyrau Road Rehabilitation	KAZ	ADB	55.0	2004
3. Kyrgyz Southern Transport Corridor Road (Osh-Sary Tash-Irkeshtam) Rehabilitation (phase I)	KGZ	ADB	32.8	2004
4. Reconstruction of the Borovoe-Petropavlovsk Road	KAZ	IsDB	30.0	2004
5. Anjrobi-Poyong Road	TAJ/PRC	IsDB	9.5	2004
6. Turkmenbashi-Begdesh Road	TKM	IsDB	67.0	2004
7. Rehabilitation of Railway Networks	UZB	IsDB	6.0	2004
Subtotal for 2004			237.4	
2005 Loans				
1. Yavlex-Ganja Road Rehabilitation	AZE	ADB	22.0	2005
2. Borovoe-Petropavlovsk Road Rehabilitation	KAZ	ADB	40.0	2005
3. Dushanbe-Kyrgyz Border Road Rehabilitation (phase II)	TAJ	ADB	23.0	2005
4. Regional Railways Rehabilitation	UZB	ADB	20.0	2005
5. TSA Air Fleet Upgrade	TAJ	EBRD	7.4	2005
6. Improvement of Aktobe and Shymkent Airports	KAZ	IsDB	40.0	2005
7. Osh-Irkeshtam Road Rehabilitation (phase I)	KGZ	IsDB	10.0	2005
8. Shagon-Zigar Road (phase II)	TAJ	IsDB	9.5	2005
9. Telecommunication of Railways for Asbagat-Farab and Turkmenbashi-Asbagat	TKM	IsDB	30.0	2005
10. Shymkent-Samara Road	KAZ	WB		2005
11. Osh-Isfana Road	KGZ	WB		2005
Subtotal for 2005			194.5	
2006 Loans				
1. Regional Traffic Enhancement	Regional	ADB	50.0	2006
2. Central Road Corridor Improvement (Qazax-Georgian Border)	AZE	ADB	15.0	2006
3. Kyrgyz Southern Transport Corridor Road (Osh-Sary Tash-Irkeshtam) Rehabilitation (phase II)	KGZ	ADB	20.0	2006
4. Tajik North Railway Modernization and Improvement	TAJ/UZB	ADB	20.0	2006
5. Reconstruction of the Taraz-Talas-Suusamyr Road (phase II)	KGZ	IsDB	10.0	2006
Subtotal for 2006			115.0	
TOTAL (2004–2006)			546.9	

Table 2: Assistance Pipeline for Non-Lending Products

	Project Title	Country Involved	Donor Agency	Amount (US\$'000)	Proposed Year for Approval
<u>2004 Technical Assistance</u>					
1.	Yevlax-Ganja Road Rehabilitation (PPTA)	AZE	ADB	150.0	2004 (Approved on 12 Aug)
2.	Establishment of the Transport Corridor Management Authority (ADTA attached to the Kyrgyz South Transport Corridor Road Rehabilitation Project, phase I)	KGZ	ADB	600.0	2004
3.	Dushanbe-Kyrgyz Border Road Rehabilitation (phase II) (PPTA)	TAJ	ADB	500.0	2004
4.	Jirgtal-Karamik Road	TAJ	IsDB	200.0	2004
5.	Feasibility Study on Dushanbe Airport Terminal	TAJ	IsDB	250.0	2004
6.	Feasibility Study on Turkmenbashi-Karabogaz Road Rehabilitation	TKM	IsDB	275.0	2004
7.	Transport Sector Strategy	KAZ	WB	390.0	2004
8.	Update of Trade and Transport Audits	KGZ/TAJ	WB	390.0	2004
	Subtotal for 2004			2,755.0	
<u>2005 Technical Assistance</u>					
1.	Regional Road Development (phase I) (RETA)	Regional	ADB	600.0	2005
2.	Regional Traffic Enhancement Project (RETA)	Regional	ADB	600.0	2005
3.	Central Road Corridor Improvement (PPTA)	AZE	ADB	500.0	2005
4.	Strengthening the Financial Management and Delivery of Road Maintenance (ADTA attached to the Yevlax-Ganja Road Rehabilitation Project)	AZE	ADB	400.0	2005
5.	Capacity Building in the Transport Sector (ADTA attached to the Borovoe-Petropavlovsk Road Rehabilitation Project)	KAZ	ADB	300.0	2005
6.	Capacity Expansion of Railway Station on Border with the PRC (ADTA)	KAZ	ADB	150.0	2005
7.	Kyrgyz Southern Transport Corridor Road (Osh-Sary Tash-Irkeshtam) Rehabilitation (phase II) (PPTA)	KGZ	ADB	300.0	2005
8.	Altai Transport Corridor (ADTA)	MON/PRC	ADB	150.0	2005
9.	Furthering Policy Reforms in the Railway Sector (ADTA attached to the Regional Railways Rehabilitation Project)	UZB	ADB	500.0	2005
10.	Transport and Trade Facilitation Workshop	Regional	WB	110.0	2005
	Subtotal for 2005			3,610.0	
<u>2006 Technical Assistance</u>					
1.	Regional Railway Development (phase I) (RETA)	Regional	ADB	850.0	2006
2.	Harmonization of Cross-Border Initiatives for Transport (RETA)	Regional	ADB	850.0	2006
3.	North-South Road Corridor Improvement (PPTA)	AZE	ADB	600.0	2006
4.	Dushanbe-Kyrgyz Border Road Rehabilitation (phase III) (PPTA)	TAJ	ADB	400.0	2006
	Subtotal for 2006			2,700.0	
	TOTAL (2004–2006)			9,065.0	

ADB = Asian Development Bank, ADTA = advisory technical assistance, AZE = Azerbaijan, EBRD = European Bank for Reconstruction and Development, IsDB = Islamic Development Bank, KAZ = Kazakhstan, KGZ = Kyrgyz Republic, MON = Mongolia, PPTA = project preparatory technical assistance, PRC = People's Republic of China, RETA = regional technical assistance, TAJ = Tajikistan, TKM = Turkmenistan, UZE = Uzbekistan, WB = World Bank.

Sources: Multilateral institutions.