Program Information Documents (PID)

Appraisal Stage | Date Prepared/Updated: 26-May-2022 | Report No: PIDA266442

BASIC INFORMATION

A. Basic Program Data

Country	Project ID	Program Name	Parent Project ID (if any)
Tajikistan	P177563	Additional Financing to Power Utility Financial Recovery Project	P168211
Region	**Estimated Appraisal Date**	**Estimated Board Date**	**Practice Area (Lead)**
EUROPE AND CENTRAL ASIA	24-May-2022	27-Jun-2022	Energy & Extractives
Financing Instrument	**Borrower(s)**	**Implementing Agency**	
Program-for-Results Financing	Ministry of Finance	Barqi Tojik, Ministry of Energy and Water Resources	

Program Development Objective(s)

The program development objectives are to improve the financial viability, increase the reliability of electricity supply, and strengthen the governance of BT.

COST & FINANCING

SUMMARY (USD Millions)

Government program Cost	1,500.00
Total Operation Cost	489.00
Total Program Cost	489.00
Total Financing	489.00
Financing Gap	0.00

FINANCING (USD Millions)

Total World Bank Group Financing	80.00
World Bank Lending	80.00
Total Government Contribution	409.00

B. Introduction and Context

Country Context

1. Tajikistan is a land-locked country in southeast Central Asia with a population of about 9.5 million and 2021 per capita income (Gross National Income, Atlas method) of about US$1,100 - slightly above the lower-middle-income threshold. The poverty rate fell from 17.8 percent in 2015 to about 13.9 percent in 2021. Tajikistan's economy relies heavily on primary commodity production and exports, with limited economic diversification. Domestic investment and consumption depend on migrant remittances, which are about a third of Gross Domestic Product (GDP), thus leaving the economy highly vulnerable to external shocks.

2. **Real GDP growth rebounded to about 9.2 percent in 2021, after slowing to 4.5 percent in 2020 due to COVID-19**. A sharp increase in precious metal exports, recovery in remittance inflows, and a pickup in private investment and consumption supported this rebound. Tajikistan's external position improved considerably from higher export prices for metals and mineral products and remittance inflows. The current account was in surplus of about 1 percent of GDP in 2021, compared to a surplus of 4.1 percent in 2020. Precious metal exports reached US$897 million and were about 40 percent of total merchandise exports. Increased remittances and foreign direct investment (FDI) inflows stimulated consumer and capital goods imports. Strong foreign exchange inflows, including from the issuance of new Special Drawing Rights (SDR) by the International Monetary Fund (IMF), supported a stable exchange rate and allowed international reserves to grow to about 8 months of import cover by end-2021. After a fiscal expansion in 2020, the Government began to consolidate spending in 2021. The fiscal deficit narrowed to 1.5 percent of GDP from 3.1 percent in 2020.

3. **The National Bank of Tajikistan is undertaking efforts to reduce inflationary pressure**. In response to rising food and fuel price inflation, the National Bank of Tajikistan increased its policy rate four times from 10.75 at end-2020 to 13.25 percent by the end-2021. Nevertheless, average annual inflation rose from 8.6 percent in 2020 to 9 percent in 2021. Amidst lower remittances and a weakening ruble following Russia's invasion of Ukraine, the authorities allowed the somoni to depreciate by 13 percent against the US dollar in March 2022. Financial sector performance improved in 2021 - primarily due to liquidation being initiated for four insolvent banks (including two state-owned banks). The share of non-performing loans in the total lending portfolio declined by 10 percentage points to 13.7 percent in 2021. To support the most vulnerable groups, the government provided social assistance to 238,000 families and provided extra one-off emergency nutrition-sensitive transfers to over 164,000 families with children.

4. **Russia’s invasion of Ukraine is expected to lead to a contraction of Tajikistan's economy**. Sanctions on the Russian economy have exposed the vulnerability of Tajik economy to external shocks since Russia is the largest employer of Tajik migrant workers and is among the largest trading partners. The main driver of this contraction is a projected fall in remittances, which is expected to lead to lower private consumption and investment. Other factors, including high prices and disruptions to trade, are also expected to contribute to the contraction. This contraction of economic activity and a new tax code introduced at the beginning of the year are expected to lower tax revenues in 2022. Along with an anticipated anti-crisis spending increase, the fiscal deficit is expected to increase to about 3.4 percent in 2022.

Sectoral and Institutional Context

5. **The electricity sector in Tajikistan is comprised of two state-owned electricity generation companies, two independent power producers (IPPs), electricity transmission and distribution companies, and a concession in Gorno-Badakhshan Autonomous Oblast (GBAO) combining electricity generation and distribution**. Barqi Tojik Open Joint Stock Holding Company (BT) is the state-owned generation company

which owns and operates all utility-scale generation plants in the country, except for GBAO, and is the electricity market operator. Rogun Joint Stock Company (JSC) is responsible for construction and operation of the 3,780 MW Rogun HPP project. Two Independent Power Producers (IPPs) – Sangtuda-1 and Sangtuda-2 HPPs – were commissioned in 2006 and 2011 respectively to help the country address the issue electricity supply shortages. Both IPPs have 20-year Power Purchase Agreements (PPAs) with BT. In June of 2019, the Government established the new state-owned electricity transmission and distribution companies - Shabakahoi Intiqoli Barq (SIB) Open Joint-Stock Company (OJSC) and Shabakahoi Taqsimoti Barq (STB) OJSC respectively. Pamir Energy Company (PEC) generates and supplies electricity to around 245,000 people as well as public and commercial sector consumers in GBAO under a 25-year concession agreement, which expires in 2027.

6. **Financial viability of the electricity sector remains a top priority for the Government because the sector will continue playing a major role as an important pillar of an export-oriented economy**. It is not only a service essential for social development and economic activity in the country but also an important building block of the Government's objectives to develop an export-oriented economy consistent with the National Development Strategy 2030. The Government has mobilized major resources to address the main challenges facing the sector, and the Bank and other development partners have been helping the Government to address these challenges through several ongoing projects.

- **Challenge #1: Financial distress of BT**. BT has been in financial distress due to: (a) below cost-recovery tariffs; (b) increasing debt levels, which reached US$1.2 billion equivalent by end of 2020; (c) low collection rates for billed electricity; (d) operational inefficiencies; (e) lack of opportunities for realization of full export potential; and (f) 61 percent depreciation of TJS vs US$ in 2015-2021. This has led to significant deterioration of financial standing of BT.
- **Challenge #2: Reduction of electricity supply reliability due to dilapidation of electricity generation, transmission and distribution (T&D) assets**. The financial distress of the electricity sector impacted the reliability of electricity supply, which deteriorated due to obsolescence and under-maintenance of main power generating plants and T&D networks. Specifically, only 77 percent of the generation capacity of Nurek HPP is operational because generating units require refurbishment given the age and technical condition.
- **Challenge #3: Lack of electricity access for about 43,000 people (0.5 percent of population) in GBAO and Khatlon regions**. In parts of Khatlon, bordering Afghanistan, there are 74 settlements with total population of 31,500 without access to electricity. Those settlements could not be connected to the grid due to severe financial difficulties of BT. There are 61 settlements with 11,600 people in GBAO region without access to electricity. This was due to prohibitively high cost of connection to PEC network because the settlements are small and scattered over large geographical territory.
- **Challenge #4: Financing completion of the Rogun HPP project**. The Government has increasingly been struggling to finance the project, which has significant financing needs relative to the size of the economy. While the Government has been spending around US$300-US$600 million per since 2016, the macro-fiscal implications of COVID-19 and the ongoing conflict between Russia and Ukraine conflict would most likely require the Government to limit the annual capital expenditures on the project at US$375 million in 2022-2028. This was confirmed by the joint International Monetary Fund (IMF) – World Bank debt sustainability analysis (DSA) from end-2021. There have been no other sources of financing for the project thus far.

7. **The ongoing US$134 million Power Utility Financial Recovery Program-for-Results (PforR) is supporting implementation of the Government's Program for Financial Recovery of Barqi Tojik Open Joint Stock Holding Company (BT) for 2019-2025**. The Government program includes policy, financial, and operational measures aimed at improving the financial viability of BT and increasing reliability of electricity supply. To ensure reliable electricity supply and improvement of the financial viability of BT, the Government intends to undertake several critical steps, which are reflected in the Government program, which was approved on April 15, 2019. The total size of the Government program for 2019-2025 is US$1.5 billion, which is financed from BT's additional cash flows and cost savings due to implementation of operational and financial efficiency improvements; Asian Development Bank's support for introduction of metering and billing in seven large cities accounting for about 55 percent of total annual electricity consumption; and the financing under the ongoing PforR operation

PforR Program Scope

8. The updated Program includes the following.

Results Area 1: Achievement of Financial Viability of Electricity Sector

- Achievement of cost-recovery end user tariffs.
- Revision of subsidiary agreements between MOF and BT.
- Improved prioritization, predictability, and transparency of collection and distribution of revenues in the electricity sector.

Results Area 2: Ensuring Electricity Supply Reliability

- Adequate electricity supply from Sangtuda-1.
- Timely rehabilitation and upgrade of SIB's and STB's electricity transmission and distribution assets.
- Reduction of electricity sector costs.

Result Area 3: Strengthening of BT, SIB, and STB Governance and Improvement of Transparency

- Implementation of good-practice corporate governance at BT, SIB, and STB.
- Use of technically, economically, and financially sound principles for investment decision-making in generation, transmission, and distribution.
- Improvement of operational and financial transparency of BT, SIB, and STB.

C. Program Development Objectives

Program Development Objective(s)

9. The revised Program development objectives are to improve the financial viability, increase the reliability of electricity supply, and strengthen the governance of Barqi Tojik OJSHC, Shabakahoi Intiqoli Barq OJSC, and Shabakahoi Taqsimoti Barq OJSC.

D. Environmental and Social Effects

10. **Environmental**. The environmental performance of the Program remains consistently satisfactory. The Government has made progress implementing the four Environmental Actions in the PAP. Specifically, the following three are completed: (i) BT, SIB, and STB developed corporate environmental policy and key guidelines, regulations and norms to facilitate adequate environmental performance in implementing rehabilitation, replacement, and upgrade of key assets; those will be adopted formally by the companies by end of July 2022; (ii) BT hired an additional environmental consultant to work with its operations; SIB and STB

are in the process of hiring their relevant environmental staff; and (iii) developed the relevant educational modules related to requirements of the Committee of Environmental Protection and carried out the trainings with participation of all three companies. The fourth, the annual evaluation and monitoring of Program activities with the requirements of local legislation has been delayed due to COVID-19 impacts and first such assessment will be completed by December 2022.

11. The proposed new measures under the Program related to fuel cost savings (elimination of HFO purchases), reduction of costs of materials and some other expenditures, and improvement of predictability and transparency of revenue distribution in the sector are not expected to have any negative environmental impacts. In fact, reduction of purchases of HFO would help to reduce the CO2 emissions from use of HFO in supply of electricity and heat and thus would have a positive environmental impact.

12. **Social**. The new activities under the Program do not have any social impacts. The overall impacts of the updated Program remain largely positive because it will improve the financial standing of electricity sector and therefore contribute to improving reliability of electricity supply. However, two aspects of the Program merit attention. First, STB needs to enhance efforts at reaching out to the consumers and improvements on complaint handling. Second, tariff revisions are expected. The expected tariff increase trajectory, which anticipates lower tariff increases until 2026[1] compared to the trajectory in the original project and relatively higher tariff increases after 2026, is not likely to lead to material impacts on the poor and that was confirmed during preparation of the parent operation. Specifically, it was estimated that poverty will increase by less than 0.6 percent in 2024 under the anticipated tariff increase trajectory. The impacts of potential tariff increases would be mitigated through introduction of block tariffs, which is under development, and, once the fiscal situation of the country allows, with increased allocation to Targeted Social Assistance (TSA) program to mitigate those impacts.

E. Financing

13. **Program Financing**. The Program would be financed with combination of own resources of BT and IDA. As presented earlier, BT's financing of the Program fell short of the level projected during appraisal of the parent project due to external shocks.

Financing Sources of the Program

Source	Original PforR (US$)	AF (US$)	Updated with AF US$)
BT own funds (tariff-regulated revenue)	305,100,043	-	265,100,043
IDA (PforR funding)	134,000,000	80,000,000	214,000,000
Financing gap	40,000,000	-	-
Total	**479,100,043**	**-**	**479,100,043**

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[1] It is expected that tariff increase in 2023-2026 will not exceed 6 percent per year compared to 8 percent under the 2019 Program. The tariff increase is expected to be lower until the macroeconomic situation improves.

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