### PROJECT INFORMATION DOCUMENT (PID)
**CONCEPT STAGE**

Report No.: PIDC238

<table>
<thead>
<tr>
<th><strong>Project Name</strong></th>
<th>Private Sector Competitiveness (P130091)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Region</strong></td>
<td>EUROPE AND CENTRAL ASIA</td>
</tr>
<tr>
<td><strong>Country</strong></td>
<td>Tajikistan</td>
</tr>
<tr>
<td><strong>Sector(s)</strong></td>
<td>Other industry (40%), General industry and trade sector (30%), Payments, settlements, and remittance systems (30%)</td>
</tr>
<tr>
<td><strong>Lending Instrument</strong></td>
<td>Specific Investment Loan</td>
</tr>
<tr>
<td><strong>Project ID</strong></td>
<td>P130091</td>
</tr>
<tr>
<td><strong>Borrower(s)</strong></td>
<td>Ministry of Finance</td>
</tr>
<tr>
<td><strong>Implementing Agency</strong></td>
<td>State Committee for Investment and State Property Management</td>
</tr>
<tr>
<td><strong>Environmental Category</strong></td>
<td>B-Partial Assessment</td>
</tr>
<tr>
<td><strong>Date PID Prepared</strong></td>
<td>13-Mar-2012</td>
</tr>
<tr>
<td><strong>Estimated Date of Appraisal Completion</strong></td>
<td>00000000</td>
</tr>
<tr>
<td><strong>Estimated Date of Board Approval</strong></td>
<td>10-May-2012</td>
</tr>
<tr>
<td><strong>Concept Review Decision</strong></td>
<td>Track II - The review did authorize the preparation to continue</td>
</tr>
</tbody>
</table>

### I. Introduction and Context

#### Country Context

The proposed Private Sector Competitiveness Project aims to foster development of the private sector in Tajikistan to support economic growth, enhanced competitiveness, and job creation. The project aims to do so by creating a more conducive business environment, diversifying sources of growth through the development of selected sectors where Tajikistan has a competitive advantage, and improving access to financial services in Tajikistan.

Prior to the 2008-09 global financial crisis, Tajikistan had been enjoying a period of sustained economic growth. The economy grew at an average of 8 percent per year during 2000-2008. This growth was driven mainly by a favorable external environment. World prices for cotton and aluminum—Tajikistan's main export commodities—soared. Rapid growth in Russia and other trading partners boosted demand for Tajik labor. The resulting growth in remittances fueled a consumption boom in Tajikistan, which helped to support buoyant growth in real GDP during the 2000s.

However, this period of buoyancy masked the build up of severe macroeconomic imbalances which were unveiled at the end of 2007. The fiscal position was weakened by an increase in external borrowing from bilateral creditors to finance large infrastructure projects (the fiscal balance shifted from a surplus to a large deficit of 6.2 percent of GDP in 2007), while supply side shocks (a steep rise in global fuel and food prices in the second half of 2007 and first half of 2008) and the growth of aggregate demand (fueled by expansionary monetary policies) led to a spike in inflation and the widening of the trade and current account deficits. At the end of 2007, the NBT’s international reserves fell below two weeks of imports; the money supply nearly tripled, and inflation accelerated to nearly 20 percent.

Despite an IMF economic stabilization program and a temporary improvement in macroeconomic performance in 2008, Tajikistan's economy remained weak and suffered significantly from the 2008-09 global financial crisis. Under an IMF and a PRGF program, and the backdrop of increasing commodity prices, the economy grew by 8 percent in 2008, inflation receded to 12 percent by end 2008, and the current account deficit declined to 8.8 percent. However, these successes were short-lived as the global financial crisis led to economic stagnation in 2009 and a steep exchange rate depreciation, as a result of a sharp drop (of 30-50 percent compared to 2008 levels) in remittance flows (resulting from Russia's recession and the consequent depreciation of the ruble), a deterioration in the terms of trade leading to an increase in the current account deficit to 12.8 percent of GDP in 2009, and a reduction in foreign direct investment and trade-related finance.

While Tajikistan's economic prospects have improved after the global financial crisis, severe structural weaknesses continue to depress the country's longer term growth and poverty reduction prospects. Economic performance began to gradually improve in 2010, as demand and trade recovered and the government successfully implemented its anti-crisis action plan. However, Tajikistan continues to face important structural challenges. Among these is the fact that Tajikistan is one of the least accessible countries in the world. Its remote, landlocked location, together with a deteriorating infrastructure, high input costs, and weak regulation, poses barriers to international trade, connectivity, and investment. Tajikistan is also faced with a young and rapidly growing population making job creation a key policy priority. The average annual growth rate of the population was 1.9 percent during 2003-07, and 40 percent of the population is under the age of 17. Limited employment opportunities in Tajikistan have encouraged a large number of workers (up to 40 percent of the working population) to seek better job prospects overseas—largely in Russia. It has also led to a
high incidence of poverty (Tajikistan is the poorest country in ECA, with an annual per capita income at US730 in 2010 and 47 percent of the population in poverty by national standards) and food security concerns.

**Sectoral and Institutional Context**

Tajikistan experiences a low level of private sector activity: the private sector constitutes a relatively low share of national output and employment, even by regional standards. In 2008, Tajikistan’s private sector contributed 48 percent of total GDP, relative to 75 percent in Kyrgyzstan and 77 percent in Kazakhstan. The private sector’s contribution to total employment the same year was even lower (at 31.4 percent) despite consistent growth since 2000. The limited economic contribution of the private sector reflects the inherited weakness of a landlocked economy, but also the wide range of remaining obstacles in the investment climate that continue to prevent enterprise investment and growth.

Private sector expansion is constrained by insufficient access to financial services to finance operations and investments. In the Doing Business 2012 report, Tajikistan was downgraded from position 170 to 177 for the getting credit indicator. There were 260 bank branches as of July 2011, representing one branch for every 30,437 people, which is very low by international standards. Non-bank financial institutions only play a minor role in Tajikistan. Overall, outstanding loans to SMEs amount to less than 1 percent of GDP, the lowest level in the ECA region. Interest rates, which are among the highest in the region, are cited by SMEs as the primary reason for them not applying for loans. Nominal lending rates in local currency at end-November 2011 averaged about 21 percent (up from about 19 percent in 2010) and the spread between the average lending rate and average deposit interest rate stood at about 20.4 percent. In foreign currency, average lending rates stood at 20 percent at end-November 2011 (down from 22.1 percent in 2010), with a spread of about 18.5 percent.

Private Sector growth is also constrained by a poor business environment. According to the Business Environment and Enterprise Performance Survey (BEPS), firms in Tajikistan face a number of significant constraints including: (i) tax policy and administration; (ii) electricity supply; (iii) corruption in interactions with public officials; and (iv) access to finance. The Doing Business indicators confirm that the investment climate in Tajikistan is among the least supportive of private sector growth in Central Asia. According to the Tajikistan 2010 Country Economic Memorandum (CEM), “the combination of an ongoing legacy of heavy-handed regulation and weak enforcement creates ample opportunities for rent-seeking by public officials and contributes to regulatory uncertainty”.

Improving the business environment and enhancing access to finance by the private sector would significantly contribute to reducing the cost of doing business and providing an incentive for enterprise creation and private sector investments. Regulatory simplification through the streamlining of procedures and the better implementation of these on the ground will make it less onerous to create businesses and to operate in Tajikistan. It will also reduce opportunities for rent-seeking. Increased access to financial services will facilitate the financing of working capital needs and investments. Overall, improving the business environment will provide an incentive for private sector initiatives and investment, thereby generating new private sector activity, jobs, and sources of economic growth.

Constraints in the business environment also prevent the emergence of a thriving private sector, even in sectors where Tajikistan has a competitive advantage, such as mining. Tajikistan has a rich geological potential, but, the mining sector has not yet taken off in Tajikistan and its mineral sector potential remains largely untapped. The sector is dominated by small operators and artisanal miners that are not well poised to take advantage of the global mining investment boom. Tajik laws and regulations which control business activities are a great hindrance to entrepreneurs in the mineral sector in that much of their drafting has been dominated by outdated Soviet philosophy which provide for significant government control and make Tajikistan uncompetitive relative to other exploration expenditure destinations (the competition is not with other CIS countries who suffer from a similar throwback philosophy, but rather from emerging countries in South America, Southeast Asia and Africa). Moreover, there is no law specific to minerals and the legal and regulatory responsibilities pertaining to the sector are spread over a large number of agencies, resulting in long time lags between requests by the private sector to advance on mineral projects and the time all the necessary approvals come through. In addition, geological data are very difficult to access, greatly dissuading new entrants to the sector.

With global commodity prices steadily rising, and investor interest peaking around the globe, Central Asia stands to be the next frontier for mining exploration and exploitation, and Tajikistan may position itself to benefit from a surge in mining investment. In September 2010, the President of Tajikistan mandated the organization of a mining technical working group that aims to make the mining sector more attractive and open to investors. The President reaffirmed the commitment to mining sector reforms in early 2011 in his annual address. A number of reforms are envisioned, including a mining strategy, changes to the mining law to bring it to international level and improvements to the country’s mineral licensing regime. The Government has already started working with the World Bank on mining sector reform, and requested assistance in the minerals sector and the implementation of the Extractive Industries Transparency Initiative (EITI) in a letter from May 10, 2011, signed by H.E. Akilov, the Prime Minister. The very large Konimansur silver deposit is currently under tender, with assistance from the IFC. However, without deeper and more structured policy and institutional reform of the mining sector, this development may be the exception rather than the rule. The current system is very unattractive to the junior exploration companies, who are crucial for changing mineral resources into economically feasible deposits as well as identifying new resources and deposits.

**Relationship to CAS**

The proposed Project contributes to the higher level objective of fostering the development of the private sector in Tajikistan. The long-term goal is to attain the high and sustainable level of private sector-led economic growth needed to reduce poverty and create opportunities for job creation. This will be facilitated by creating a more conducive business environment to facilitate new business
entry, stimulate higher private sector productivity, and encourage increased private investments, in particular in the mining industry. This objective is aligned with the Bank's Country Partnership Strategy (CPS) and the Government's goals.

II. Proposed Development Objective(s)

Proposed Development Objective(s)

The development objective of the project is to enhance the private sector development through further improving the business environment, encouraging the development of high-potential industries, and enhancing access to financial services while strengthening the financial sector.

Key Results

Suggested Project Development Objective indicators:

1. Increased private sector contribution to GDP and employment as measured by private sector output to GDP and private sector employment to total employment
2. Improved business environment as measured by improved Doing Business ranking and reduction in the number of significant business and regulatory constraints faced by firms in Tajikistan
3. Improvement in the development and regulation of high-potential industries (e.g., mining) as measured, for instance, by the number of tenders announced, volume of investments, and number of laws and regulations revised according to international best practices
4. Enhanced access to financial services and increase in the consumer confidence and efficiency of the financial system as measured by the increase in credit to private sector as a share of GDP and deposits as a share of GDP and decrease in interest rate spreads
5. Strengthened bank regulation and supervision as measured, for instance, by the key bank regulations revised and passed, IT systems for bank supervision updated, and number of NBT’s personnel trained to use them.

III. Preliminary Description

Concept Description

The tasks contemplated under the project would leverage the work conducted over the last 3-4 years by the World Bank Group as well as other donors in the PSD and FSD areas in Tajikistan.

The Project consists of the following two components:

Component 1: Improving the business environment;
Component 2: Encouraging the development of high-potential mining industry; and
Component 3: Enhancing access to financial services while strengthening the financial sector.

Component 1: Improving the business environment.

This component of the project aims to:

- Continue support in selected areas of the investment climate, where the technical assistance provided by the Bank over the last few years needs to be extended in depth and breadth.
- Support the implementation of reforms by complementing the technical assistance with a dedicated investment and capacity building component.

The assistance envisioned under this component aims to cover four specific problem areas:

1. Starting a Business: Despite the reforms, the process of starting a business in Tajikistan could be further improved; entrepreneurs still need to visit the three agencies (the Tax Committee, the Statistics Committee and the Pension Agency) to obtain three separate registration numbers. Also, there are a number of procedures that could be simplified and costs that could be reduced.

2. Registering Property: Despite the legislative amendment that calls for the unification of land and building registries, this reform has not yet been implemented. As a result of an unreliable system of property registration, it is very difficult to carry out adequate urban planning, transportation and infrastructure design and planning, and agricultural or tourism development. In addition, the uncertainty associated with real estate titling makes the use of real estate as collateral a challenge for creditors, thereby, affecting the ability of farmers and business to gain access to credit at favorable terms. The burdensome process of registration has also developed a prevalent system of informal transfer of property (especially in the rural areas) in Tajikistan. The implementation of unified registry would simplify the process, reduce costs and likely decrease the number of informal property transfers.

3. Construction Permits: While the legislative reforms carried out are a positive step forward, they need to be broadened and implemented for them to have an impact. For example, while the legislative amendments call for the implementation of a one-stop-shop for utilities no such mechanism currently exists. In addition, the regulatory framework lacks key components, such as a
modern licensing framework for building practitioners, best practice codes and risk-based approaches for construction permitting. Due to the lack of implementation and an under-developed regulatory framework, in Tajikistan, it is still very expensive and burdensome to comply with building rules.

4. **Getting Credit (Secured Transactions):** Although the current collateral registry in the Ministry of Justice has a modern computerized core, the system is outdated, with a poor and old IT base that makes the registry unreliable.

To address the above issues, this component will have three sub-components:

i. Technical Assistance. The aim of this sub-component is to scale up the technical assistance provided to date by the Bank through an additional funding that will be allocated for this purpose during the life cycle of the trust fund;
ii. Investment and Capacity Building: the component would revolve around capacity-building and IT implementation (development/purchase of software and purchase of hardware); and
iii. Project Management: Monitoring and Evaluation: This component will support implementation and monitoring of the project by the Project Management Unit in the SCISPM.

**Component 2: Encouraging the development of high-potential mining industries.**

This component would aim at supporting the development of the mining industry which has a high competitiveness potential in Tajikistan, leveraging the new Competitiveness Partnerships Initiative (CPI) developed under the FPD network. The mining component would be developed in collaboration with SEGOM and leverage preliminary work implemented by SEGOM in recent years.

The component would aim at (i) increasing the attractiveness of Tajikistan as a destination country for large mining developments and (ii) building the capacity to manage and regulate the sector, building upon a number of previous Bank ad-hoc interventions in the mining sector (a mining strategy review, a review of mining legislation, and preliminary work on the Extractive Industry Transparency Initiative (EITI)). The project would be complemented by efforts being undertaken by the working group led by the Ministry of Finance preparing Tajikistan for candidate country status for EITI, at which time it would be eligible for funding from the Multi-Donor Trust Fund to enable it to strive towards compliant country status. (The goal of the working group is to become an EITI candidate country by spring 2012.)

The component would build upon the preliminary steps taken by the Government of Tajikistan on mining sector reform—including the organization of a Mining Technical Working Group—with a combination of technical assistance, capacity building, and investment that would make the mining sector more attractive for investment in exploration and exploitation as well as enhance the benefits received by the country from the development of mining operations.

Sub-component 2a: Mining Sector Laws and Regulations Technical Assistance.
Sub-component 2b: Development of a Modern Mining Cadastre and Associated Capacity Building.
Sub-component 2c: Modernization of the Geological Survey Functions Investment, Technical Assistance and Capacity Building
Sub-component 2d: Stakeholder Outreach Technical Assistance.

**Component 3: Enhancing access to financial services while strengthening the financial sector.**

The objective of this component is to improve access to financial services by enterprises and individuals while enhancing financial sector stability.

Access to finance in Tajikistan is low compared to other countries in the region and around one in three firms identified this as a major constraint for growth. Credit to the private sector as a share of GDP amounted to 15 percent in 2010, and deposits as a share of GDP amounted to 13 percent. Moreover, cash outside of banks is 72% of the total money supply, compared to 6% in OECD countries and 22% in countries that borrow from the World Bank. The high ratio of cash outside of banks in Tajikistan is an indication of the shallowness of the financial sector resulting from the low confidence that the public has in banks and the lack of non-cash payment instruments (e.g., debit and credit cards).

At the same time, the National Bank of Tajikistan (NBT) faces limitations to its institutional capacity and systems to regulate and supervise banks’ activities to ensure the stability of the financial sector and sustainability of credit. Several factors have contributed to a dramatic deterioration in bank asset quality since 2009. These factors include prior rapid credit growth until 2008, weaknesses in banks’ risk management systems, poor performance of directed lending to the agriculture sector (especially cotton), and deficiencies in the regulatory and supervisory framework. Non-performing loans (NPLs) peaked at 28% in early 2010, declining to 16% in June 2011 following some write-offs and reclassifications. In addition, some loans are misclassified and NPLs are understated due to certain bank practices and gaps in regulations.

The component would support the following tasks:
Sub-component 3a: Support to enhance access to financial services
Sub-component 3b: Development of the payment systems infrastructure
Sub-component 3c: Strengthening of bank regulation and supervision
IV. Safeguard Policies that might apply

<table>
<thead>
<tr>
<th>Safeguard Policies Triggered by the Project</th>
<th>Yes</th>
<th>No</th>
<th>TBD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Environmental Assessment OP/BP 4.01</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Natural Habitats OP/BP 4.04</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Forests OP/BP 4.36</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Pest Management OP 4.09</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Physical Cultural Resources OP/BP 4.11</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Indigenous Peoples OP/BP 4.10</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Involuntary Resettlement OP/BP 4.12</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Safety of Dams OP/BP 4.37</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Projects on International Waterways OP/BP 7.50</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Projects in Disputed Areas OP/BP 7.60</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
</tbody>
</table>

V. Tentative financing

<table>
<thead>
<tr>
<th>Financing Source</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>BORROWER/RECIPIENT</td>
<td>0.00</td>
</tr>
<tr>
<td>IDA Grant</td>
<td>10.00</td>
</tr>
<tr>
<td>Total</td>
<td>10.00</td>
</tr>
</tbody>
</table>

VI. Contact point

World Bank

Contact: Karen Grigorian
Title: Private Sector Development Spec.
Tel: 458-7451
Email: kgrigorian@worldbank.org

Borrower/Client/Recipient

Name: Ministry of Finance
Contact:
Title:
Tel: (992-372) 21-14-17
Email:

Implementing Agencies

Name: State Committee for Investment and State Property Management
Contact:
Title:
Tel:
Email: amcu@gki.tj

VII. For more information contact:

The InfoShop
The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 458-4500
Fax: (202) 522-1500
Web: http://www.worldbank.org/infoshop