

**PROJECT INFORMATION DOCUMENT (PID)
APPRAISAL STAGE**

Report No.: 32127

Project Name	IQ-EMERGENCY PRIVATE SECTOR DEVELOPMENT
Region	MIDDLE EAST AND NORTH AFRICA
Sector	Private sector development; communications infrastructure; financial sector
Project ID	P091344
Borrower(s)	REPUBLIC OF IRAQ
Implementing Agency	Ministry of Planning and Development Cooperation Iraqi Telecommunications and Postal Company (ITPC)
Environment Category	<input type="checkbox"/> A <input type="checkbox"/> B <input checked="" type="checkbox"/> C <input type="checkbox"/> FI <input type="checkbox"/> TBD (to be determined)
Safeguard Classification	<input type="checkbox"/> S ₁ <input checked="" type="checkbox"/> S ₂ <input type="checkbox"/> S ₃ <input type="checkbox"/> S _F <input type="checkbox"/> TBD (to be determined)
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1. Key development issues and rationale for Bank involvement

i) Key development issues

a) Iraq needs rapid economic growth if it is to meet the aspirations of its 25 million people. Income levels are low – GDP per head is estimated at \$840 in the year 2003 – and there are high levels of unemployment and under-unemployment. Some estimates place this number at 50% or more, with an official estimation of unemployment at 28%. Increased oil production is one part of this equation and will help on the income side, but it will do little for jobs. The other part and the key to jobs is a growing private sector. Growing the private sector requires action on a number of critical dimensions. This project addresses four dimensions:

- Creating the necessary institutional underpinnings for the private sector – to facilitate and promote investment and markets, as well as to provide pressure points for reform.
- Resolving some critical market failures facing the private sector – the sanctions regime and the conflict within Iraq has destroyed connections with the outside world. There is no insurance industry to help bring lost capacity back on line.
- Facilitating the development of some key building blocks of the financial sector – a payments system and a system of effective property rights.
- Providing essential infrastructure – a modern private sector cannot survive without reliable telecommunications.

b) Relative to the size of the Iraqi economy the formal private sector is quite small. The oil-led state-owned enterprise (SOE) sector, a large agriculture sector, and the public sector account for the majority of employment in the country. The private sector is characterized by very few large companies, a number of small-medium enterprises (SMEs) and a very large number of micro-enterprises. It is estimated in excess of 90% of the over 100,000 enterprises fall within the last category. Most large enterprises are in the state sector. Because of the sanctions regime, there is very little by way of exports and the services sector is very weak. Constraints to private sector activity include virtually every aspect of the investment climate (infrastructure, finance, security, business regulation, etc.). Moreover businesses have suffered from the conflict – capacity has been destroyed. Yet at the same time, there are opportunities: There will be huge reconstruction flows; there are export-ready SMEs based on a proud and vibrant arts and crafts heritage; and there are potential comparative advantages in the oil and agricultural sectors, the SOE sector that is ripe for reform, the religious tourism industry, and the information communications technology.

c) The private sector cannot develop and be able to compete if it does not have rapid access to financial services, such as an efficient network of branch banks. Modern financial systems depend on computerized information processing and settlement mechanisms to move money through local and global telecommunications networks. This network is a precondition for establishing a national payments and settlements (P&S) system that is in line with the requirements of a market economy. The Iraqi Central Bank, supported by the Government, wants to establish a proper P&S system by connecting some 80 nodes/locations across the country. Likewise property rights are critical to the financial sector – if contracts cannot be enforced, if property rights cannot be secured it is unrealistic to expect significant financial sector development.

d) In the trade regime, most aspects of a modern supply chain are heavily dependent on telecommunications. This is an area which offers substantial productivity gains to Iraq (this could be as much as 20% of GDP). Trade facilitation systems, including customs management, general logistics management, and inventory controls require efficient and reliable data communications systems. Telecommunications lies at the heart of modern marketing and selling – connecting to customers, reviewing market information and even internet sales. If trade is to be expanded in Iraq, national and international connectivity will have to be increased. As Iraq eliminates its networking bottlenecks, it should be able to acquire its imports more cheaply, organize its primary and secondary production more efficiently, operate its markets more efficiently (goods, assets, labor, capital), and exploit its intellectual and human capital more effectively. It should also be better able to attract and exploit FDI. Telecommunications is, therefore, a fundamental necessity for Iraq's trade facilitation.

e) Low telecommunications penetration, old technology and small backbone data transmission capacity mean Iraq's telecommunications does not meet the needs of a modern private sector. Iraq currently has an average of 4 fixed telephones per 100 people provided by the state-owned national operator – Iraq Telecommunications and Post Company (ITPC), 2 mobile phones by 100 people – provided by 5 private regional operators, and 2 Internet connections per 1000 people. Jordan, for example, has penetration levels of 20, 20 and 10 per 100 people, respectively. Iraq's telecommunications indicators are obviously low by

regional and international standards and cannot support a vibrant private sector. All these indicators will be significantly improved with the establishment of a national long-distance backbone network. The absence of such a network has been the biggest bottleneck in developing the sector further. In particular it will encourage private sector participation by allowing private mobile, internet, and voice telephone operators to interconnect.

ii) The Rationale for the Bank's Involvement

The proposed Project is fully consistent with the [World Bank's Interim Strategy Note for Iraq](#) (January 2004), which emphasizes the need for short-term employment generation, institutional capacity building, and rapid rehabilitation of critical infrastructure as prerequisites for long-term sustainable recovery. Indeed, the Project addresses all three aspects. Furthermore, the proposed operation supports the Government of Iraq's (GOI) objective to create a dynamic private sector by improving the investment climate where private participation can flourish. Indeed, the project is closely integrated with the Government of Iraq's National Development Strategy.

There are important reasons for the World Bank to be involved at this stage in supporting the investment climate, the payments and settlements system, and telecommunications infrastructure development:

- The Iraqi authorities have expressed a strong desire for the World Bank to take the lead on these areas;
- The Project covers crucial areas of development that insure sustainable job growth. They constitute the building blocks necessary for the private sector to grow;
- The Bank is in a position to share international experiences and best practices based on the Bank's considerable international experience with private and financial sector development, SOEs reform, and telecommunications infrastructure in conflict-affected areas (including Bosnia-Herzegovina, Ethiopia, West Bank and Gaza, and Afghanistan);
- The telecommunications infrastructure will enable the effective functioning of several institutions in the financial and commercial sector. This should also provide the badly needed connectivity for private telecommunications service providers (mobile, data, and internet), and facilitate the extension of services to all regions in the country;
- Bank financing, unlike the financing of many other donors, will be implemented by Iraq through the country's own institutions (ministries and agencies), which ensures Iraqi ownership and helps build Iraq's institutional capacity, both crucial for the country's sustainable development;
- The Bank will integrate financing of specific initiatives with policy advice, assisting the GOI with urgent policy decisions, while laying the ground for sector restructuring essential for long-term sustainability of the private sector; and

2. Proposed objectives

The principal objective of this Project is to provide priority building blocks to facilitate private and financial sector development and ensure its growth leading to sustainable employment generation

3. Preliminary description

The Project consists of five components, including a project management component:

- (i) Development of enabling public institutions that support the private sector;
- (ii) Improving the competitiveness of Iraqi private firms by improving their ability to access finance and foreign markets;
- (iii) Building reliable telecommunications infrastructure to interconnect key parts of the Central Bank's payments and settlements system; and
- (iv) Building a high capacity national communications network capable of supporting corporate needs.
- (v) Project Management.

Component (i): Development of enabling public institutions that support the private sector (Estimated cost of US \$7 million)

This component would help establish and/or strengthen institutions that support or encourage the private sector and financial sector in Iraq and enable them to play their appropriate role. The Project will support institutional strengthening with business planning, design of procedures, design of any necessary rules and regulations, provision of start-up facilities, training, support of twinning arrangements, support for the initial activities of the agency, and provision of any other necessary technical assistance for selected institutions. The institutions that would be targeted for this assistance are:

- Investment Promotion Agency: International experience in post conflict countries shows that an early focus on building investment facilitation and promotion capacity is a key to private sector development. In Iraq, the role of the state and private sector in investment remains a fundamental question. Assistance in this area will focus on: (a) developing a public awareness campaign on the need and benefits of private investment, and (b) managing an inter-ministerial reform dialogue. Other donors will assist with the detailed work in creating this investment promotion agency;
- Export Promotion Agency: For the private sector to grow, export markets are essential. Because Iraq has been cut off from the international community, this will require extensive support. An agency that can focus on the issues and constraints facing private sector exporters will be helpful in developing an export culture in Iraq. This work will include the institutional support activities mentioned above;

- Economic Development Fund: The financial sector in Iraq is at a very early stage of development and private banks are not yet ready to support the private sector's SMEs. The support will build capacity so the Fund can eventually provide such services; and
- Industrial Zones: These zones will provide a mechanism to deal with security issues, infrastructure deficiencies and local economic development. The zones are not intended to provide tax havens. Development plans for potential industrial zones will be prepared: one in Basra and the other in Arbil. These plans will examine market demand, specification of infrastructure requirements, examination of regulatory concerns and the design of an implementation process.

Component (ii): Improving the competitiveness of Iraqi private firms by improving their ability to access finance and foreign markets.

(Estimated cost of US \$5 million)

This component will be a pilot to address two elements of market failure that the export and private sectors are currently facing in Iraq. The first is related to the inadequate knowledge the Iraqi export sector has when it comes to accessing export markets. As a result of the sanctions, potential export industries in Iraq have deteriorated and exporters need to update their products and services to meet international standards and expectations. Entry to new export markets requires extensive researching and planning that cover target markets, consumer preferences, product design, etc. The private sector enterprises (especially SMEs) are unable to mobilize resources to develop an export plan at this time. In addition, many exporters and/or potential exporters lack the technical knowledge to develop a viable export plan that would ease access to new markets.

The second market failure refers to the inability of the Iraqi private enterprises, especially SMEs, in obtaining credit for new projects or businesses. Feasibility studies are required by financial institutions before extending credit for a proposed project. To a large extent, SMEs do not have the knowledge to prepare such studies in-house and the management consulting industry in Iraq is incapable of preparing acceptable studies.

This project will provide assistance to eligible Iraqi private firms to build the necessary capacity to qualify as a potential player in the new market economy. This assistance will be channeled through two agencies: (i) The Export Promotion Fund (EPF) at the Ministry of Trade (MOT), will channel technical assistance to eligible firms to develop export plans to access new export markets; and (ii) The Economic Development Fund (EDF) at the Ministry of Planning and Development Cooperation will channel technical assistance to Iraqi private enterprises to develop feasibility studies for new projects that require funding from financial institutions.

Component (iii): Building reliable telecommunications infrastructure to interconnect key parts of the Central Bank's payments and settlements system.

(Estimated cost of US \$3 million)

This component will fund the critical physical communications infrastructure for providing enhanced capacity for interconnecting the Central Bank of Iraq (CBI) Headquarters

with CBI's Mosul and Basra branches (currently connected via VSAT) and for networking CBI with the two Government owned banks, Rafidain and Rasheed and the headquarters of 20 private banks in Baghdad. Based on the successful implementation of this phase, CBI will establish a communications network to interconnect with banks throughout Iraq. In this regard, the expanded CBI network will make effective use of good and reliable bandwidth capacity that would become available with ITPC beginning April 2006 under this project and augment it with appropriate state of the art technologies to establish transmission links to banks in other provinces/districts of Iraq.

Component (iv): Building a high capacity national backbone communications network capable of supporting corporate needs and develop the human capacity to operate it efficiently.

(Estimated cost of US \$39.5 million)

This component supports ITPC's rehabilitation program for 2004 – 2007 approved by the Iraqi Strategic Review Board (ISRB) to build a modern and integrated national digital backbone microwave network to improve delivery of communications services to the government and to the people of Iraq. In particular, this component would focus on rehabilitating and upgrading three of the five national backbone microwave routes and associated spur routes that have been severely damaged. The three routes are: (i) Baghdad - Trabil, (ii) Baghdad - Mosul, and (iii) Baghdad – Ammara - Basra. The remaining two routes would be developed under the Japanese Government Bilateral Assistance program to Iraq. The support.

In addition, sufficient capacity will be available to meet the needs of both the public sector agencies and the private telecom service providers thus facilitating and enabling further competition and private participation in the provision of backbone microwave systems will provide much needed transmission capacity between Baghdad and the Districts in the North, South and Western parts of Iraq. These microwave links will provide immediate voice and data connectivity for the key cities in the districts of Baghdad, Baquba, Kirkuk, Arbil, Mousa, Sulaimaniya, Dohuk, Ramadi, Hadetha, Alquaim, Kut, Ammara, Basra and Um Qaser, and improve national and international connectivity.

This component consists of two parts: (i) supply, installation and commissioning of the above three backbone microwave routes and the associated spur microwave routes on a single responsibility basis utilizing tried and tested technologies that can be rapidly rolled out in the current Iraq environment; and (ii) provision of training and operational telecommunication services. ITPC will be expected to interconnect with all interested telecommunications and data service providers and provide transmission capacity at cost-based prices in line with the principles of transparent regulation and fair competition.

Component (v): Project Management.

(Estimated cost of US \$0.5 million)

The component will finance expenditures directly related to the management of the project such as: procurement consultants; audit consultants; maintenance of office equipment; transportation and travel, including per diem allowances for Project staff in travel status; rental of office space; utilities and office administration, including translation, printing and advertising;

fuel costs; communication costs; costs for production of bidding documents and drawings; and commercial bank charges. No salaries of the Recipient's civil servants will be financed under the project. The grant recipient will finance the salaries of the PMT staff.

4. Implementation Arrangements

This is a multi-sectoral operation with several beneficiaries. To facilitate implementation, the Project components will be split into two groups and will be executed by two Implementation agencies (IAs). Components (i) and (ii) will be implemented by the Ministry of Planning and Development Cooperation (MOPDC), which will also be the Grant Recipient. Components (iii) and (iv) will be implemented by the Iraqi Telecommunications and Postal Company; a Subsidiary Grant Agreement between the MOPDC and the ITPC will transfer the implementation responsibilities, liabilities and accountability to the ITPC for these components. The ITPC would be required to carry out the Project in accordance with similar implementation arrangements agreed between the MOPDC and the World Bank. Furthermore, a Project Agreement between the ITPC and the World Bank is envisaged to complement the Subsidiary Grant Agreement.

A Project Management Team (PMT) in each Implementing Agency, namely the MOPDC and the ITPC, will be responsible for the procurement, financial management, the management of day-to-day activities, consolidated reporting, and coordination and monitoring of project components. To facilitate coordination and processing, the PMT would work closely with representatives from Ministries/Agencies involved, such as the Export Promotion Fund and the Economic Development Fund, and the Central Bank of Iraq, to ensure that their needs and requirements are met.

The IAs will recruit international and local consultants to assist the PMT to finalize components' design, prepare tender documents, evaluate bids, and sign contracts. The security situation could prevent Bank staff and international consultants from traveling to Iraq during project preparation and implementation. Project supervision would primarily rely on local Iraqi and international consultants with presence in Iraq, supported by Bank staff working from outside Iraq. Regional consultants with a branch office in Baghdad have been recruited to assist with project preparation.

5. Procurement

Procurement for this project will be carried out in accordance with the World Bank's "Guidelines: Procurement Under IBRD Loans and IDA Credits" dated May 2004; and "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" dated May 2004, and the provisions stipulated in the Trust Fund Grant Agreement. For each contract to be financed by the grant, the procurement methods or consultant selection methods, the need for pre-qualification, estimated costs, prior review requirements, and time frame have been agreed upon between the Recipient and the Bank project team in the Procurement Plan (PP). The PP will be updated as required to reflect the actual project implementation needs and improvements in institutional capacity.

Goods procured under this project will include supply and installation of a microwave backbone component for the ITPC and a Telecommunication Infrastructure component for the Central Bank of Iraq to support its National Payments System. The supply and installation of a Telecommunications Backbone component for the ITPC and a Telecommunication Infrastructure for the Central Bank of Iraq Payments and Settlements System will be procured separately using International Competitive Bidding (ICB) procedures and the Standard Bidding Documents (SBD) for procurement of Supply and Installation of Plant and Equipment. Other goods procured under this project would include small value office equipment and supplies, furniture and computers. These would be purchased by using either National Competitive Bidding (NCB) or Shopping methods depending upon the estimated value for each contract.

The selection of consulting firms will be carried out by Quality and Cost Based Selection (QCBS) or in the event of the estimated cost being US\$300,000 or below, using the Consultants' Qualifications (CQ) procedure.

6. Disbursement

Disbursement will be made based on two methods. (a) Disbursements of amounts equal or higher to \$10,000 will be made by direct payments by the Bank to the contractors, consultants and vendors' accounts at commercial banks capable of receiving funds transferred through the international banking system and (b) Disbursements of amounts less than \$10,000 will require implementing agencies to spend from their own funds and request reimbursements from the Bank. Reimbursements will be done on a periodical basis upon presentation of supporting documents (invoice), proof of payment and signed Withdrawal Application. All expenditures must be approved by the respective PMT and Withdrawal Applications will be also reviewed by the Monitoring Agent. The PMTs and the implementation teams' staff will be subject to intensive training in Bank disbursement procedures.

7. Financial Management

Each implementing agency will be responsible for the proper financial management of its own components including i) maintaining adequate FM arrangements throughout the project implementation, ii) maintaining separate accounting records and follow-up spreadsheets for the project, iii) approving all payments related for the project, iv) submitting copies of all payment supporting documents along with Withdrawal Applications to the Bank both for direct payments and reimbursement. Each PMT will maintain an appropriate and adequate financial management system, including records and accounts, and will prepare financial statements adequate to separately reflect the operations, resources, and expenditures of the project. The financial statements will be audited annually by qualified by a qualified auditor acceptable to the Bank with scope and standards accepted internationally. The audit report will be submitted to the Bank within two months of year-end.

The financial management risk associated with this operation is considered as high. A number of measures are being taken to mitigate these risks during project preparation and supervision. The project financial resources will be managed within the framework of the Iraqi government financial management system in addition to World Bank financial management procedures. The grant funds will be made available to the implementing agencies who will enter

into contractual agreements with contractors, consultants, and vendors for the developing and building the activities financed under the project.

Risks arising from the lack of adequate control over project supervision will be mitigated by putting in place additional controls and procedures including: (a) each PMT will verify and authorize payments under the grant for its respective implementing agency; (b) the PMTs will include competent financial staff from the implementing agencies and if needed will be supported by financial management consultants, (c) the ITPC, MOPDC will assign qualified staff from their finance departments, including internal auditors, to track the project activities, follow-up on project transactions and provide support to the PMTs, (d) disbursements by the Bank will be made by direct payments and on reimbursement basis supported by documentation, and (e) the Monitoring Agent will review Project expenditures.

8. Safeguard policies

This is a category ‘C’ project. The project is an emergency project and will be processed under Operational Procedure (OP) 8.50 (Emergency Recovery Project). Based on section 13 of OP 4.01, exemption has been sought from the Bank’s executive management (March 2004) in order that any Environmental Assessment requirements will not be conducted prior to project appraisal. Hence, the environmental assessment mitigating measures (if any) will be carried out during project implementation under provisions incorporated in the construction contracts. However the project will have to comply with the Environmental and Social Screening and Assessment Framework (ESSAF). The ESSAF entails that: (a) sub-projects be screened by the Recipient through the checklist attached to the Framework; (b) a code of practice be included as part of the design, preparation and civil work contracts as well as of purchase and installation of equipment contracts, and (c) the Safeguard Procedures, as per Attachment 6 of the ESSAF, would be included in the Technical Specifications of the contracts of all Contractors.

9. Risks

The proposed Project is subject to substantial risks, including: (i) security issues; (ii) political risks; (iii) Government commitment and (iv) unfamiliarity with Bank safeguards and procedures (accountability, financial management, and procurement). To mitigate these risks, the Project design will be kept simple. Training on project management and procurement has been provided and the Project provides for additional training and capacity building for PMT staff. Security issues will be managed through project and contract design, and the extensive use of national consultants and contractors. Critical Government commitments to project success will be identified and secured at project negotiation stage.

10. Tentative financing

Source:	(\$m.)
RECIPIENT	0.5
SPECIAL FINANCING	55
Total	55.5

11. Tentative processing schedule

Pre-Appraisal Decision Meeting	October 17, 2004
Appraisal	November 15, 2004
Negotiations/Approval	Late November or early December, 2004

12. Contact point

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