



## Additional Financing

---

Project Number: 47923-002  
Loan Number: 3071-PRC  
November 2015

### Proposed Increase in B-Loan China Water Affairs Group Limited Urban–Rural Integration Water Distribution Project (People’s Republic of China)

This is an abbreviated version of the document approved by ADB's Board of Directors that excludes information that is subject to exceptions to disclosure set forth in ADB's Public Communications Policy 2011.

Asian Development Bank

## CURRENCY EQUIVALENTS

(as of 5 November 2015)

Currency unit	–	yuan (CNY)
CNY1.00	=	\$0.1578
\$1.00	=	CNY6.3355

## ABBREVIATIONS

ADB	–	Asian Development Bank
CWA	–	China Water Affairs Group Limited
ESMS	–	environment and social management system
PRC	–	People's Republic of China
SSD	–	Shanghai Silver Dragon Investment Limited

## NOTE

In this report, "\$" refers to US dollars unless otherwise stated.

<b>Vice-President</b>	D. Gupta, Private Sector and Cofinancing Operations
<b>Director General</b>	T. Freeland, Private Sector Operations Department (PSOD)
<b>Directors</b>	C. Thieme, Infrastructure Finance Division 2, PSOD S. Chakraborty, Private Sector Transaction Support Division, PSOD
<b>Team leader</b>	H. Kimura, Principal Investment Specialist, PSOD
<b>Team members</b>	C. Chan, Guarantees and Syndications Specialist, PSOD C. Dizon, Associate Investment Officer, PSOD M. Greenhow, Principal Counsel, Office of the General Counsel M. A. Manabat, Senior Investment Officer, PSOD A. Porras, Safeguards Officer, PSOD M. Principe, Senior Social Development Officer, PSOD V. Ramasubramanian, Safeguards Specialist, PSOD S. Roberts, Investment Specialist, PSOD

In preparing any country program or strategy, financing any project, or by making any designation of or reference to a particular territory or geographic area in this document, the Asian Development Bank does not intend to make any judgments as to the legal or other status of any territory or area.

## CONTENTS

## Page

### PROJECT AT A GLANCE

I.	BACKGROUND	1
II.	ADDITIONAL FINANCING	1
	A. Rationale	1
	B. Impact, Outcome, and Outputs	2
	C. Revised Financing Plan	2
	D. Due Diligence	2
	E. Implementation Arrangements	2
III.	THE PRESIDENT'S RECOMMENDATION	3
	APPENDIX	
	Revised Design and Monitoring Framework	4

## PROJECT AT A GLANCE

<b>1. Basic Data</b>		<b>Project Number: 47923-002</b>	
<b>Project Name</b>	Urban-Rural Integration Water Distribution Project	<b>Department /Division</b>	PSOD/PSIF2
<b>Country</b>	China, People's Republic of		
<b>2. Sector</b>		<b>ADB Financing (\$ million)</b>	
✓ Water and other urban infrastructure and services	Subsector(s) Urban water supply		0.00
		<b>Total</b>	<b>0.00</b>
<b>3. Strategic Agenda</b>		<b>Climate Change Information</b>	
Inclusive economic growth (IEG)	Subcomponents Pillar 2: Access to economic opportunities, including jobs, made more inclusive	Climate Change impact on the Project	Low
<b>4. Drivers of Change</b>		<b>Gender Equity and Mainstreaming</b>	
Private sector development (PSD)	Components Promotion of private sector investment	Some gender elements (SGE)	✓
<b>5. Poverty Targeting</b>		<b>Location Impact</b>	
Project directly targets poverty	No	Rural Urban	Medium Medium
<b>6. Nonsovereign Operation Risk Rating</b>			
<b>Obligor Name</b>	<b>Obligor Risk Rating Local Currency</b>	<b>Obligor Risk Rating Foreign Currency</b>	<b>Facility Risk Rating</b>
CHINA WATER AFFAIRS GROUP LTD.	NSO6	NSO6	NSO7
<b>7. Safeguard Categorization</b>		<b>Environment:</b>	<b>Involuntary Resettlement:</b>
			<b>Indigenous Peoples:</b>
<b>8. Financing</b>			
<b>Modality and Sources</b>		<b>Amount (\$ million)</b>	
<b>ADB</b>		<b>0.00</b>	
<b>B-Loans</b>		<b>100.00</b>	
Dual Currency Complementary Loan from Commercial Banks		100.00	
<b>Official Cofinancing<sup>a</sup></b>		<b>0.00</b>	
None		0.00	
<b>Others<sup>b</sup></b>		<b>0.00</b>	
<b>Total</b>		<b>100.00</b>	
<b>9. Effective Development Cooperation</b>			
Use of country procurement systems		Yes	
Use of country public financial management systems		Yes	

<sup>a</sup> Concessional financing from external sources.

<sup>b</sup> Derived by deducting ADB financing, B Loans and Official Cofinancing from Project Total Cost.

## I. BACKGROUND

1. On 3 December 2013, the Asian Development Bank (ADB) approved loan facilities of up to \$200 million equivalent without government guarantee to China Water Affairs Group Limited (CWA) and Shanghai Silver Dragon Investment Limited (SSD),<sup>1</sup> comprising (i) an A loan of up to \$100 million equivalent in dollars and yuan, and (ii) a dual-currency complementary loan<sup>2</sup> of up to \$100 million equivalent in dollars and yuan for the Urban–Rural Integration Water Distribution Project.

2. The project is designed to address the increasing challenge of providing reliable, affordable, and safe water supply to rural and semi-urban communities in the People’s Republic of China (PRC). To that end, ADB funds will support CWA in (i) expanding existing water utility networks into adjacent semi-urban and rural communities; and (ii) establishing water treatment and distribution hubs in second- and third-tier cities that have the potential for urban–rural integration. At least 10 water supply subprojects with combined capacity of 2 million cubic meters per day will be developed in rural areas and second- and third-tier cities during 2014–2017, connecting an estimated 740,000 households to improved piped potable water.

[CONFIDENTIAL INFORMATION DELETED]

## II. ADDITIONAL FINANCING

### A. Rationale

3. The proposed increase of the B loan by up to \$100 million will allow a larger and more diverse group of international commercial banks to participate in the project, gain from benefits accruing from participating in ADB’s B loan structure, and expand the impact of ADB’s cofinancing programs. The amount of the ADB A loan and its terms and conditions will not be affected by the proposed increase in the B loan. The proposed increase of the B loan does not fundamentally alter the structure, outcome, or risk profile of the ongoing project.

[CONFIDENTIAL INFORMATION DELETED]

4. The proposed B loan increase is consistent with the project’s development objective—to encourage private investment in improving water access in less-developed areas of the PRC. This is in line with the government’s priority of rectifying development imbalances between city and countryside through provision of basic infrastructure services, particularly in water supply. The proposed increase in the B loan amount is also consistent with the Midterm Review of Strategy 2020, which emphasizes that deepening cofinancing partnerships is an important area to strengthen ADB’s capacity and effectiveness.<sup>3</sup> The increased B loan will catalyze wider commercial finance to support rural water supply, where bank lending is limited, and build confidence in future private sector participation in this emerging area.

---

<sup>1</sup> SSD is a holding company, wholly owned by CWA as an onshore investment vehicle, to hold investments in water treatment and distribution project companies. Since the A loan was disbursed wholly in US dollars, SSD will cease to be a borrower under the loan agreement.

<sup>2</sup> The complementary loan is an Asian Development Bank (ADB) syndicated loan in various currencies (including local currencies) funded by commercial banks, where ADB is the lender of record. B loans are complementary loans which are cross-border and in US dollars. For this project, as stated in para. 4, CWA requested syndication of loans only in US dollars from international banks; thus, in this paper, this loan is referred to as the “B loan.”

<sup>3</sup> ADB. 2014. *Midterm Review of Strategy 2020: Meeting the Challenges of a Transforming Asia and Pacific*. Manila.

## **B. Impact, Outcome, and Outputs**

5. The impact, outcome, and outputs of the project remain unchanged. The anticipated project impacts are (i) expanded access to safe and reliable water supply for rural and urban households and other customers in the PRC; (ii) improved water efficiency; and (iii) increased private participation in rural and urban network investment and operation. The expected project outcome is improved water services in rural, semi-urban, and small-town areas of the PRC. The key project output is the installation and operation of wastewater treatment plants and distribution facilities with a total capacity of up to 2 million cubic meters per day.

## **C. Revised Financing Plan**

6. ADB funded the A loan from its ordinary capital resources, whereas the B loan will be funded by commercial banks. The proposed change will increase the amount of the B loan by up to \$100 million, taking the total amount of the B loan up to \$200 million, to accommodate the robust capacity of participating banks to finance the project.

[CONFIDENTIAL INFORMATION DELETED]

7. The project investment plan and project scope remain unchanged. The project's financial sustainability will not be affected, nor will the additional financing have an impact on the project's overall risk profile.

## **D. Due Diligence**

8. The safeguard categorization for the proposed increase in the B loan remains unchanged from the original classification—category B for environment and involuntary resettlement and category C for indigenous peoples. CWA established an environment and social management system (ESMS) consistent with ADB's safeguards requirements prior to signing of CWA's first loan with ADB in 2011.<sup>4</sup> The ESMS was updated in 2014 based on the due diligence findings and corrective actions identified in an environmental and social compliance audit. In line with CWA's ESMS requirements, the safeguard documents for subprojects under the ADB A loan were reviewed and approved by ADB prior to disbursement. This will be continued for subprojects to be considered under the B loan. With the experiences gained in implementing ADB's safeguard requirements in its operations since 2011, the institutional capacity and commitment of CWA to manage the project's social and environmental impacts are deemed adequate. CWA, as required in its ESMS, will continue to comply with national labor laws and, pursuant to ADB's Social Protection Strategy (2001), will take measures to comply with the internationally recognized core labor standards.<sup>5</sup> Information disclosure and consultation with affected people will continue to be conducted in accordance with ADB requirements.

## **E. Implementation Arrangements**

9. All other implementation arrangements of the project remain unchanged.

---

<sup>4</sup> ADB. 2011. *Report and Recommendation of the President to the Board of Directors: Proposed Loan for Municipal Water Distribution Infrastructure Development Project in the People's Republic of China*. Manila.

<sup>5</sup> ADB. 2003. *Social Protection*. Manila (adopted in 2001).

### III. THE PRESIDENT'S RECOMMENDATION

10. The President recommends that the Board approve an increase in the B loan to China Water Affairs Group Limited by up to \$100,000,000 for the additional financing of the Urban–Rural Integration Water Distribution Project in the People’s Republic of China, to be funded by commercial banks.

## REVISED DESIGN AND MONITORING FRAMEWORK

<p><b>Impacts the Project is Aligned with</b></p> <p><b>Current project</b></p> <p>Expanded access to safe and reliable water supply for rural and urban households and other customers in the PRC</p> <p>Improved water efficiency in the PRC</p> <p>Increased private sector participation in rural and urban water networks</p> <p><b>Overall project</b></p> <p>Unchanged</p>
-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------

Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting	Risks
<p><b>Outcome</b></p> <p><b>Current Project</b></p> <p>Improved water services in second- and third-tier cities, and surrounding semi-urban and rural areas</p> <p><b>Overall project</b></p> <p>Unchanged</p>	<p><b>Current Project</b></p> <p>At least 740,000 households are connected to improved piped potable water from 2014 to 2018<sup>a</sup></p> <p>An average of CNY600 million of local goods and services procured per annum from 2018 onwards</p> <p>An average CNY140 million per annum paid in taxes to municipal governments from 2018</p> <p>At least a 5% decline in nonrevenue water in acquired networks from pre-acquisition condition between 2014 and 2018</p> <p>All water treatment plants funded by ADB meet the national standards for drinking-water quality by 2018<sup>b</sup></p> <p><b>Overall project</b></p> <p>Unchanged</p>	<p>Project monitoring and development effectiveness monitoring reports</p> <p>Audited financial statements and annual reports</p> <p>Audited financial statements and annual reports</p> <p>Project monitoring reports</p> <p>National Standards for Drinking-Water Quality (GB5749-2006)</p>	<p>Project schedule slips due to approval delays.</p> <p>Only a few municipal governments have adequate facilities to test all 106 indicators of the national standards for drinking-water quality.</p>



<b>Results Chain</b>	<b>Performance Indicators with Targets and Baselines</b>	<b>Data Sources and Reporting</b>	<b>Risks</b>
<b>Outputs</b>  <b>Current project</b>  Rehabilitation and operation of water treatment plants and distribution	<b>Current project</b>  At least 10 subprojects of a combined capacity of 2 million cubic meters per day rehabilitated, expanded, or newly constructed in rural areas and second- and third-tier cities from 2014 to 2017 <sup>c</sup>  Additional 500 local workers employed during construction from 2014 to 2017  Goods and services purchased locally amount to CNY3 million per annum from 2014 to 2017  Revision and update of current environmental and social management system, including staff recruitment and capacity building plans, implemented before the first disbursement	Project monitoring and development effectiveness monitoring reports  Project monitoring and development effectiveness monitoring reports  Audited financial statements and annual reports  Annual environmental and social monitoring reports	Delay by municipalities in granting concession rights to private sector due to unforeseen regulation changes  Raw water supply is constrained or contaminated
<b>Overall project</b>  Unchanged	<b>Overall project</b>  Unchanged		

#### **Key Activities with Milestones**

1. Signing of loan agreements by Q4 2013 (completed)
2. Financial closure by Q1 2014 (completed)
3. Clearance of all loan drawdown conditions by Q2 2014 (completed)
4. Fully disbursed loans by Q4 2017 (unchanged)

#### **Inputs**

ADB: An A loan of up to \$100 million equivalent in US dollar–yuan loan (unchanged)

#### **Complementary loan**

up to \$100 million equivalent in US dollar–yuan loan (current)  
up to \$100 million equivalent in US dollar–yuan loan (additional)  
up to \$200 million equivalent in US dollar–yuan loan (overall)

**Assumptions for Partner Financing**

**Current project**

Not Applicable

**Overall project**

Unchanged

ADB = Asian Development Bank, MOHURD = Ministry of Housing and Urban–Rural Development, NDRC = National Development and Reform Commission, PRC = People’s Republic of China, Q = quarter.

<sup>a</sup> Based on production capacity of 2 million cubic meters per day, nonrevenue water of 23%–25% per subproject, and household consumption of 166 cubic meters per year.

<sup>b</sup> The PRC’s national standards for drinking-water quality were announced in 2006 (GB5749-2006), with increases in stringency to 2015. The water-testing facilities of China Water Affairs Group Limited (CWA) will be tested against the 2015 standards level, and used to generate reports on national water quality standards met or exceeded.

<sup>c</sup> CWA will record the capacity of rehabilitated, expanded, and newly constructed network pipes.

Source: Asian Development Bank.