

Project Number: 50164-002  
Loan Number: 3463-PRC  
November 2019

Proposed Increase in B Loan  
China Water Environment Group Investment Limited  
and Xinkai Water Environment Investment Limited  
Integrated Wastewater Management 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 Access to Information Policy.

## CURRENCY EQUIVALENTS

(as of 24 October 2019)

Currency unit	–	yuan (CNY)
CNY1.00	=	\$0.1415
\$1.00	=	CNY7.0655

## ABBREVIATIONS

ADB	–	Asian Development Bank
CWE	–	China Water Environment Group Limited
ESMS	–	environmental and social management system
PPP	–	public–private partnership
PRC	–	People’s Republic of China
US	–	United States

## NOTE

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

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## PROJECT AT A GLANCE

<b>1. Basic Data</b>		<b>Project Number: 50164-002</b>	
<b>Project Name</b>	Integrated Wastewater Management Project	<b>Department /Division</b>	PSOD/PSIF2
<b>Country</b>	China, People's Republic of		
<b>Borrowers</b>	China Water Environment Group Investment Xinkai Water Environment Investment		
<b>2. Sector</b>		<b>Subsector(s)</b>	<b>ADB Financing (\$ million)</b>
✓ Water and other urban infrastructure and services	Urban sewerage		100.00
Agriculture, natural resources and rural development	Water-based natural resources management		50.00
<b>Total</b>			<b>150.00</b>
<b>3. Strategic Agenda</b>		<b>Subcomponents</b>	<b>Climate Change Information</b>
Inclusive economic growth (IEG)	Pillar 2: Access to economic opportunities, including jobs, made more inclusive		Climate Change impact on the Project Medium
<b>4. Drivers of Change</b>		<b>Components</b>	<b>Gender Equity and Mainstreaming</b>
Private sector development (PSD)	Promotion of private sector investment		No gender elements (NGE) ✓
<b>5. Poverty and SDG Targeting</b>		<b>Location Impact</b>	
Geographic Targeting	No	Rural	Medium
Household Targeting	No	Urban	High
General Intervention on Poverty	Yes		
SDG Targeting	Yes		
SDG Goals	SDG6		
<b>6. Nonsovereign Operation Risk Rating</b>			
<b>Obligor Name</b>		<b>Final Project Rating</b>	<b>Facility Risk Rating</b>
China Water Environment Group Investment			
Xinkai Water Environment Investment			
<b>7. Safeguard Categorization</b>		<b>Environment: B</b>	<b>Involuntary Resettlement: B</b>
		<b>Indigenous Peoples: C</b>	
<b>8. Financing</b>			
<b>Modality and Sources</b>		<b>Amount (\$ million)</b>	
<b>ADB</b>		<b>150.00</b>	
Nonsovereign Dual Currency Loan (Regular Loan): Ordinary capital resources		150.00	
<b>Cofinancing</b>		<b>350.00</b>	
Dual Currency Complementary Loan from Commercial Banks (Full ADB Administration)		350.00	
<b>Others<sup>a</sup></b>		<b>900.00</b>	
<b>Total</b>		<b>1,400.00</b>	
<b>Currency of ADB Financing: USD</b>			

<sup>a</sup> Derived by deducting ADB financing and Cofinancing from Total Project Cost.

## I. BACKGROUND

1. On 18 November 2016, the Asian Development Bank (ADB) approved loan facilities of up to \$250,000,000 in United States (US) dollars or its equivalent in yuan comprising (i) an A loan of up to \$150,000,000 equivalent in US dollars or yuan from ADB's ordinary capital resources; and (ii) a complementary loan of up to \$100,000,000 equivalent in US dollars or yuan to China Water Environment Group Investment Limited and Xinkai Water Environment Investment Limited, together China Water Environment Group Limited (CWE), for the financing of the Integrated Wastewater Management Project in the People's Republic of China (PRC).<sup>1</sup>

2. The project is designed to support the implementation of integrated wastewater management concessions, targeting environmental services for lakes and rivers. ADB's loan would support CWE in designing, constructing, and operating a series of facilities spanning several components, such as (i) wastewater treatment plants; (ii) sludge treatment plants; (iii) sewage conveyance and interception pipelines; (iv) dredging of rivers and lakes; (v) other civil works such as riverbank reinforcements, odor treatment plants, and landscaping; and (vi) the development of watersheds and wetlands.

3. CWE selects subprojects located in urban sections of key rivers and lakes in the central and western provinces of the PRC that are designated the government's priority areas for environmental protection. For each subproject, CWE develops and operates the component facilities as public-private partnerships (PPPs), governed under concession agreements signed with city or county governments. It is envisaged that, by 2024, river or lake rehabilitation subprojects will be developed with wastewater treatment capacity of 2.3 million tons per day, sludge treatment capacity of 2,900 tons per day, and 190 kilometers of sewage pipeline networks, among other infrastructure. The facilities will comply with ADB's safeguards and technical and financial eligibility criteria.<sup>2</sup>

4. Project implementation is satisfactory, and the project remains technically feasible, economically viable, and financially sound. [CONFIDENTIAL INFORMATION DELETED]

## II. ADDITIONAL FINANCING

### A. Rationale

5. The proposed increase in the B loan by up to \$250 million will address CWE's request to broaden its access to international commercial financing and expand the impact of ADB's cofinancing program by tapping into increased demand from commercial banks to participate in environmental PPPs in the PRC. [CONFIDENTIAL INFORMATION DELETED]

6. ADB's B loan product has been increasingly effective in catalyzing commercial cofinancing for infrastructure development in the PRC. During 2012–2018, ADB successfully syndicated 15 B-

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<sup>1</sup> The complementary loan is an Asian Development Bank (ADB) syndicated loan product that can be offered 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, while ADB approved loan facilities in US dollars or its equivalent in yuan, the A loan was fully disbursed in US dollars. Therefore, the complementary loan will be disbursed in US dollars and in this paper, be referred to as the B loan.

<sup>2</sup> Eligibility criteria shall include a concession agreement with service exclusivity; the satisfaction of an environmental and social management system (ESMS), which is compliant with ADB's safeguard requirements; location; compliance with PRC environmental standards; and exclusion of category A projects, among others.

loan and complementary loan transactions, mobilizing more than \$1.5 billion in financing from more than 60 different investors.

7. The proposed increase in the B loan to CWE is beneficial to both the company and the commercial banks, which will all be linked under the ADB B loan umbrella by aggregating multiple subprojects into a single loan facility. Thus, the B loan structure helps surmount the barrier of transaction costs, since each subproject by itself would be too small for international banks to consider financing. It will also allow banks participating in the project to gain from benefits accruing from participating in ADB's B loan structure. Finally, B loans benefit ADB by aligning the interests among lenders, avoiding potential conflicts that might arise between parallel facilities, and improving credit monitoring and administration.

8. The proposed increase in the B loan is consistent with the project's development objectives: to mitigate water pollution in rivers and lakes of the PRC and to encourage private investment in less-developed areas of the PRC. This is in line with the government's priority of encouraging new forms of PPP models to promote water pollution control and waterbody rehabilitation. The proposed increase in the B loan amount is also fully consistent with ADB's Strategy 2030, which targets a substantial increase in long-term cofinancing by 2030, with every \$1.00 in financing for ADB's private sector operations matched by \$2.50 of long-term cofinancing.<sup>3</sup> The increased B loan will catalyze wider commercial finance to support integrated wastewater management concessions targeting environmental services for lakes and rivers, where bank lending, especially from international commercial banks, is limited; and build confidence in future private sector participation in this emerging area.

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

9. The impact and outcome of the project remain unchanged while the outputs of the project have been increased to include two additional targets on gender. The project is aligned with the following impact: pollution of rivers and lakes in the PRC is mitigated. The project will have the following outcome: provision of wastewater management services under integrated concessions in selected central and western provinces of the PRC is expanded.<sup>4</sup> The key project output is the construction of wastewater treatment plants and associated civil works for the improvement of river and lake water quality, with river or lake rehabilitation subprojects being developed with wastewater treatment capacity of 2.3 million cubic meters per day, sludge treatment capacity of 2,070 cubic meters per day, and 190 kilometers of sewage pipeline networks, among other infrastructure.

10. While the project was approved under a "No Gender Elements" categorization, as part of the B-loan increase, CWE has committed to implementing the following gender initiatives: (i) implementation of internship programs for female students to support them to move into technical roles, and (ii) design and implementation of a non-discrimination policy to support equal treatment of women and disabled employees in the workplace. CWE will report on the implementation of the gender outputs that it has committed to, under the annual project monitoring and development effectiveness monitoring reporting mechanism.

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<sup>3</sup> ADB. 2018. *Strategy 2030: Achieving a Prosperous, Inclusive, Resilient, and Sustainable Asia and the Pacific*. Manila.

<sup>4</sup> The revised design and monitoring framework is in the Appendix.

### C. Revised Financing Plan

11. 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 \$250 million, taking the total amount of the B loan up to \$350 million, to support the company's robust investment pipeline and accommodate the increased capacity of participating banks.

[CONFIDENTIAL INFORMATION DELETED]

### D. Due Diligence

12. 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. CWE established an ESMS consistent with ADB's Safeguard Policy Statement requirements before the first disbursement of ADB's A loan. The ESMS was designed based on the due diligence findings and corrective actions identified in an environmental and social compliance audit conducted during the project processing stage. In line with CWE's ESMS requirements, ADB reviewed and approved the safeguard documents for the two ADB-funded subprojects under the A loan before disbursement and disclosed them on the ADB website. The two subprojects were visited by the ADB team safeguard specialists during the annual review mission in 2019. While the on-site team did not identify any significant risks and impacts, and confirmed the original categorization, it found information gaps between one of the subproject's environmental and social audit reports and its implementation (e.g., wetland design and its operational management, and renting of land as opposed to purchase at some subproject components). Hence, the audit report did not fully assess the environmental and social impacts and risks related to the subproject as required under the ESMS. CWE's annual monitoring report of ADB-funded subprojects will address these gaps identified during the review mission. ADB will continue its review and approval role in the environmental and social due diligence process for additional subprojects under the B loan to ensure that CWE and its consultant thoroughly identify and manage all the environmental and social issues. This support by ADB will continue to strengthen CWE's capacity and resources to identify and manage subproject-related environmental and social risks and impacts. As required in its ESMS, CWE 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 by CWE in accordance with ADB requirements.

13. CWE has been and will be subject to an annual integrity due diligence review in accordance with ADB's Integrity Due Diligence Guidelines for Nonsovereign Operations.<sup>6</sup> No significant or potentially significant integrity risks were identified, as there are no unresolved or substantiated adverse media or other related information. Having reviewed the investment, ADB does not believe that it is being used for money laundering, or terrorism financing.

### E. Implementation Arrangements

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

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

<sup>6</sup> ADB. 2003. *Enhancing the Asian Development Bank's Role in Combating Money Laundering and the Financing of Terrorism*. Manila.

### **III. THE PRESIDENT'S RECOMMENDATION**

15. The President recommends that the Board approve an increase in the B loan by up to \$250,000,000 to a total of up to \$350,000,000 to China Water Environment Group Investment Limited and Xinkai Water Environment Investment Limited, together China Water Environment Group Limited, for the additional financing of the Integrated Wastewater Management Project in the People's Republic of China, to be funded by commercial banks.



## REVISED DESIGN AND MONITORING FRAMEWORK

<b>Impacts the Project is Aligned with</b> <b>Current project</b> Pollution of rivers and lakes in the PRC is mitigated. <sup>a</sup> <b>Overall project</b> Unchanged			
Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting Mechanisms	Risks
<b>Outcome</b>  <b>Current project</b>  Provision of wastewater management services under integrated concessions in selected central and western provinces of the PRC is expanded	<b>Current project</b>  a. Amount of wastewater treated increased to 755 million m <sup>3</sup> per year by 2028. <sup>b,c</sup>  b. Number of jobs provided during operation are at least 400 local workers by 2028.  c. Total domestic purchases during operation are at least CNY6,189 million over 2017–2028.  d. Total payments to government provided during construction and early operation are at least CNY2,356 million during 2017–2028.	<b>Current project</b>  a.–d. Annual project monitoring and development effectiveness monitoring reports by CWE	<b>Current project</b>  Associated infrastructure, such as tap water distribution network and sewage pipelines, is delayed.  Local government does not adequately implement a wider watershed management plan to arrest pollution.
<b>Overall project</b>  Unchanged	<b>Overall project</b>  Unchanged	<b>Overall project</b>  Unchanged	<b>Overall project</b>  Unchanged

<b>Output</b>			
<p><b>Current project</b></p> <p>1. Wastewater treatment plants and associated civil works for the improvement of river and lake water quality constructed<sup>d</sup></p>	<p><b>Current project</b></p> <p>1a. Integrated river or lake rehabilitation subprojects with a total value of CNY9.0 billion are constructed by 2024.</p> <p>1b. Total installed wastewater treatment capacity of subprojects increased to 2.3 million m<sup>3</sup> per day constructed by 2024.<sup>b</sup></p> <p>1c. Sludge treatment subprojects with a total capacity of about 2,070 m<sup>3</sup> (2,900 tons) per day constructed by 2024.<sup>e</sup></p> <p>1d. 190 kilometers of sewage pipeline networks constructed by 2024.</p> <p>1e. Total domestic purchases during construction amount to CNY7,388 million by 2024.</p> <p>1f. Number of jobs provided during construction phase are at least 1,200 by 2024.</p>	<p><b>Current project</b></p> <p>1a–1f. Annual project monitoring and development effectiveness monitoring reports by CWE</p>	<p><b>Current project</b></p> <p>Delays by host governments in granting concession rights to private sector because of unforeseen regulation changes.</p>
<p><b>Overall project</b></p> <p>1. Unchanged</p> <p>2. Gender-inclusive approach of CWE is strengthened</p>	<p><b>Overall project</b></p> <p>1a–1f. Unchanged</p> <p>2a. At least 5 female students supported by an internship programs each year for 5 years to move into technical roles starting from 2020 (2019 baseline: 0)</p> <p>2b. Non-discrimination policy to support equal treatment of women and disabled employees in the workplace designed and implemented by 2021</p>	<p><b>Overall project</b></p> <p>1a–1f. Unchanged</p> <p>2a–2b. Annual project monitoring and development effectiveness monitoring reports by CWE</p>	<p><b>Overall project</b></p> <p>1. Delays by host governments in granting concession rights to private sector because of unforeseen regulation changes.</p> <p>2. Lack of management commitment to implementing gender initiatives across all operating subsidiaries</p>

Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting Mechanisms	Risks
	(2019 baseline: not applicable)		
<p><b>Additional Key Activities with Milestones</b></p> <p><b>1. Wastewater treatment plants and associated civil works for the improvement of river and lake water quality constructed</b></p> <p>1.1 Sign B loan agreements by Q4 2019</p> <p>1.2 Financial closure of B loan agreements by Q1 2020</p> <p>1.3 Complete conditions precedent for B loan drawdown by Q3 2020</p> <p>1.4 Fully disburse B loan by Q4 2020</p>			
<p><b>Inputs</b></p> <p><b>ADB A Loan</b> Up to \$150 million equivalent in US dollar–yuan loan (unchanged)</p> <p><b>ADB Complementary loan</b> Up to \$100 million equivalent in US dollar–yuan loan (current) Up to \$250 million equivalent in US dollar–yuan loan (additional) Up to \$350 million equivalent in US dollar–yuan loan (overall)</p> <p><b>Commercial bank financing</b> Up to \$730 million equivalent in yuan (current) Up to \$480 million equivalent in yuan (revised)</p> <p><b>Sponsor equity:</b> \$420 million equivalent in yuan (unchanged)</p>			
<p><b>Assumptions for Partner Financing</b></p> <p><b>Current project</b> Not applicable</p> <p><b>Overall project</b> Unchanged</p>			

CWE = China Water Environment Group Limited, m<sup>3</sup> = cubic meter, PRC = People's Republic of China, Q = quarter, US = United States.

<sup>a</sup> State Council. 2015. Water Pollution Prevention and Control Action Plan. Beijing.

<sup>b</sup> One ton of wastewater is assumed to have a volume of one cubic meter

<sup>c</sup> The treatment plants will meet the Ministry of Environmental Protection's Grade 1A standard of the Discharge Standard of Pollutants for Municipal Wastewater Treatment Plant (GB18918-2002).

<sup>d</sup> As specific projects that will receive ADB funding are yet to be identified, an estimate was made on the extent of operations that can be supported by ADB assistance in terms of number of wastewater and sludge treatment plants. Outputs from these subprojects were then extrapolated using information from existing CWE operations.

<sup>e</sup> One cubic meter of sludge is assumed to weigh 1.4 tons.

Source: Asian Development Bank.