

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

Report No.: PIDA1092

Project Name	Kenya Urban Water and Sanitation OBA Fund for Low Income Areas (P132979)
Region	AFRICA
Country	Kenya
Sector(s)	Water supply (70%), Wastewater Collection and Transportation (30%)
Theme(s)	Other urban development (60%), Municipal finance (40%)
Lending Instrument	Investment Project Financing
Project ID	P132979
Borrower(s)	The National Treasury, National Treasury
Implementing Agency	Water Services Trust Fund
Environmental Category	B-Partial Assessment
Date PID Prepared/Updated	04-Jun-2014
Date PID Approved/Disclosed	04-Jun-2014
Estimated Date of Appraisal Completion	30-Apr-2014
Estimated Date of First Grant Approval	30-Jun-2014
Decision	Project authorized to proceed to negotiations.

I. Project Context

Country Context

Poverty and vulnerability remain key development challenges in Kenya, which has a population of about 41 million. Although better macro-economic conditions in the last decade have improved the welfare of Kenyans, levels of poverty remain high – in urban areas, about 39% of the population live below the income poverty line. In addition, Kenya’s population is estimated to increase by one million a year. Today, 28% of the population live in urban areas, in 2050, the World Bank estimates that about half will live in cities. Access to basic services is therefore key to improving welfare.

Sectoral and institutional Context

Kenya’s national development plan, the Kenya Vision 2030, aims to ensure that improved water and sanitation is available and accessible to all by the year 2030. Although access to water and sanitation services remains modest, based on 2010 reports to the regulator by 62 water service providers (WSPs), only 40% of the 20.5 million people within their service areas are being covered, the rate of progress over the last five years have been quite commendable - growing by 5% in the last 5 years. This progress is a result of sector reforms started in 2002 with the separation of

responsibility for policy-making, regulation, asset ownership and development, and operations of water systems. Under the 2002 Water Act, the Ministry of Water and Irrigation (now the Ministry of Environment, Water and Natural Resources) is responsible for setting strategic goals for the sector, while the Water Services Regulatory Board and Water Appeals Board provide oversight. Eight Water Services Boards, each responsible for services in different regions, own the water supply assets and are responsible for their development and rehabilitation and contract with water services providers, who are responsible for delivering services on a commercial basis. Kenya's 2010 Constitution provides for the creation of an entirely new tier of 47 county governments. Many essential services, including water and sanitation, are devolved to county level while urban services are also re-centralized to county level. This simultaneous devolution and recentralization of services to county level poses a number of challenges for delivery of county and urban services.

II. Proposed Development Objectives

The project development objective is to increase the number of people in low income areas with access to improved water supply and sanitation services in Kenyan towns and cities. This objective will be realized by incentivizing urban Water Services Providers to invest in water supply and sanitation improvement subprojects to benefit households in low income areas by applying one-off Output-Based Aid subsidies to make water and sanitation access affordable.

III. Project Description

Component Name

Implementation Support for project management, subproject preparation and supervision, and to contract an independent verification agent

Comments (optional)

Project manager: US\$300k; Capacity building: US\$1.35 million; Independent Verification Agent: US\$400k; Publicity & workshops: US\$50k; administrative & audit: US\$235k

Component Name

Output-Based Aid subsidies for water and sanitation subprojects

Comments (optional)

IV. Financing (in USD Million)

Total Project Cost:	18.14	Total Bank Financing:	0.00
Financing Gap:	0.00		
For Loans/Credits/Others			Amount
Borrower			6.30
Global Partnership on Output-based Aid			11.84
Total			18.14

V. Implementation

The project grant of US\$ 11.835 million will be administered by the Water Services Trust Fund (WSTF), a state-owned corporation with the mandate to fund pro-poor water and sanitation related investments. The terms and conditions for implementing the project will be governed by the Grant Agreement. In addition to the Grant Agreement, a detailed Operations Manual will describe the modus operandi of the project. The WSTF will supervise the overall fiduciary and safeguards

compliance for the project, and will be responsible for reporting to the World Bank as per the project monitoring and reporting framework. The task team and especially the project manager will provide guidance to WSTF in consultancy planning, procurement, financial management and reporting, and will supervise fiduciary compliance as part of regular supervision. Component 1 has dedicated funds to hire an experienced senior program manager, with experience in procurement and financial management, to run the facility.

Service providers. WSPs licensed by WASREB will be responsible for implementing the utility subprojects, including preparation of subsidy and loan applications, procurement of contractors for construction and supervision of subproject implementation. WSPs will provide water and sanitation services to consumers targeted under the project over the long term and will generate revenue in the form of connection fees and tariffs. WSPs will be obligated to repay the loans to the commercial lenders net of subsidy. Component 1 has dedicated funds to hire external consultants to assist with creating technical and financial plans for submitting to both commercial lenders for loans and the WSTF for subsidy.

Lenders. Kenyan based commercial lenders will appraise loan applications, enter into loan agreements with the WSPs and pre-finance the construction of subprojects. The loan agreements may stipulate a cash sweep of the subsidy into the borrower's loan account, with the remainder of the loan amount being repaid over a longer period. In preparing the project, the task team has received indicative interest from several commercial banks. Three banks have recently signed a partial credit guarantee with USAID summing to US\$9 million exclusively for lending to the water sector in Kenya. The Water and Sanitation Program is working with WASREB on a second credit assessment of the 43 WSPs and has a technical assistance program to help banks build capacity in lending to the water sector. In the event that the WSPs are unable to access commercial loans, the use of other mechanisms to support access to credit shall be explored.

Independent Verification Agent. The independent verification agent (IVA) will be contracted by WSTF to carry out baseline surveys of the proposed subprojects and assist in establishing clear and tangible output targets. The IVA will verify subproject costs before and after implementation, and will ascertain the amount of subsidy payable at each of the three stages of disbursement: on signing of loan agreement (10 percent), on achievement of outputs (65 percent), and on demonstrated measure of sustainability (25 percent). The IVA will also be responsible for ensuring that the beneficiaries are in the low-income areas targeted by the project, based on the WSTF criteria and the majidata.com website, and will analyze socio-economic indicators to further ascertain the impact of the project.

VI. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01	x	
Natural Habitats OP/BP 4.04		x
Forests OP/BP 4.36		x
Pest Management OP 4.09		x
Physical Cultural Resources OP/BP 4.11		x
Indigenous Peoples OP/BP 4.10		x
Involuntary Resettlement OP/BP 4.12	x	

Safety of Dams OP/BP 4.37		x
Projects on International Waterways OP/BP 7.50		x
Projects in Disputed Areas OP/BP 7.60		x

Comments (optional)

VII. Contact point

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Implementing Agencies

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