



<b>1. Project Data:</b>		<b>Date Posted :</b> 03/18/2004	
<b>PROJ ID:</b> P002957		<b>Appraisal</b>	<b>Actual</b>
<b>Project Name:</b> Small Towns Water	<b>Project Costs (US\$M)</b>	48.0	47.42
<b>Country:</b> Uganda	<b>Loan/Credit (US\$M)</b>	42.3	40.8
<b>Sector(s):</b> Board: WS - Sanitation (32%), Water supply (32%), Sewerage (32%), Sub-national government administration (2%), Central government administration (2%)	<b>Cofinancing (US\$M)</b>		
<b>L/C Number:</b> C2583; CP660			
	<b>Board Approval (FY)</b>		94
<b>Partners involved :</b>	<b>Closing Date</b>	12/31/2001	06/30/2003

<b>Prepared by :</b>	<b>Reviewed by :</b>	<b>Group Manager :</b>	<b>Group:</b>
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**2. Project Objectives and Components**

**a. Objectives**

The main objective of the project was to support the Government 's economic recovery program by upgrading or rehabilitating water supply and sanitation systems in towns that were already served and establishing new facilities in towns that were not yet covered . Specific objectives included :

- (i) Improve health conditions through better water supply, excreta disposal, wastewater management, and public hygiene;
- (ii) Alleviate poverty and improving the lot of women; and
- (iii) Reduce environmental degradation through better waste management .

Bank involvement was expected to (a) assist GOU in developing a policy framework for the sustainable provision of water and sanitation services to small and medium sized towns; (b) initiate appropriate institutional and policy reforms for the WSS sector and provide technical assistance to DWD; (c) provide guidance for the development of institutions responsible for sustainable service delivery; and (d) demonstrate the integration of top-down and bottom up approaches involving user communities in planning, implementation and management of WSS facilities .These expectations appear in the ICR, but are not stated as such in the SAR . Thus, the project had a significant ratcheting-up of institutional and policy objectives /expectations (see section 4).

**b. Components**

Two groups of towns were included in the original project : (a) eleven mall towns (Busia, Kalisizo, Kyotera, Lugazi, Luwero, Lyantonde, Malaba, Ntungamo, Rakai, Rukungiri, and Wobulenzi ), where most of the town populations drew water from

boreholes with hand pumps, springs, rivers and lakes, to be implemented by the Directorate of Water Development (DWD); and (b) the rehabilitation of the water supply and sewerage services in the Jinja -Njeru service area to be implemented by the National Water and Sewerage Corporation (NWSC).

Specific components included : (i) Construction and rehabilitation/expansion of the water and sanitation facilities .

- (ii) Hygiene education related to water supply and sanitation .
- (iii) Mobilization of communities to participate in planning, implementation, operation, maintenance and management of water supply and sanitation facilities .
- (ii) Institutional strengthening, technical assistance and training of water sector organizations .

**c. Comments on Project Cost, Financing and Dates**

The objectives were not revised, but as a result of the MTR, the project was restructured by scaling down the rehabilitation works for the two larger towns of Jinja and Njeru . The closing date was extended by 18 months to June 30, 2003.

**3. Achievement of Relevant Objectives:**

- i. *Water services -- satisfactory* The Independent Participatory Impact Study concluded that the project provided

Improved water services to more people than originally planned -- to about 161,000 people in excess of the SAR target of 126,000. In addition, the project has improved service conditions for the estimated 30,000 people who had access to improved supply at appraisal. Currently, the total population with access to improved water supply service is estimated at 191,000, in excess of the SAR target of 156,000. Technical inspections have shown that the quality of construction and maintenance has been of good quality.

i. *Improve the lot of women--satisfactory* Most of the town populations used to draw water from boreholes with hand pumps, springs, rivers and lakes. The Study found that the main drawers of water in the towns were women and children and they benefited most in terms of reduction in the burden associated with collecting water. Receiving piped water allowed households to free up their time to engage in other economic and social activities.

iii *Environmental degradation -- satisfactory* Under a limited project budget, the project financed construction of 45 public toilets and 14 km of storm drains, supply of 45 refuse bunkers, and tractors/trailers for solid waste management; these improvements were selected by the town authorities from a menu of options. The garbage bunkers are being utilized, but maintenance could be strengthened.

#### **4. Significant Outcomes/Impacts:**

1. Twenty-four hour water supply is now available due to: (a) development of good quality water supply infrastructure; (b) customer friendly commercial and financial policy that has subsidized installation of connections, from USh 50,000 to USh135,000 (US\$25-70) per connection; (c) a flexible approach that allows for provision of a range of options to serve the various types of users and responding to demand for connections.

2. Town residents now have a better quality and a higher quantity of water supply and noted a significant shift from point sources towards piped water usage; currently, about 70% of the households, compared to 5% at the start of the project depend on piped water as their primary source.

3. The project's institutional development impact is rated as high. The water entities in the small towns are evolving into financially viable operations 2 years after the commissioning of water operations in the project towns. Except for Rakai and Malaba, the other towns have either surpassed or recently reached break-even point and show signs of sustainable operations (i.e. they would be able to finance all operating expenses and maintenance). Measures implemented under the project have resulted in improved performance of the Water Corporation. Kampala, which constitutes 70% of NWSC's operations, is already managed by a private operator under a management contract, while the other operational areas of NWSC are under Area Performance Contracts and service contracts with existing NWSC staff. Plans are underway to convert the areas into autonomous entities that would operate under management contracts with NWSC.

4. Following the MTR, the project assisted GOU to adopt: (i) a flexible approach that provides a range of options to serve the various types of users, responding to increased demand for connections; and (ii) implementation of a model that ensures sustainable management of the water supply systems - operations have been contracted out to local private operators since July 2001 and the systems are being managed and operated well. These approaches are now being applied nationwide.

5. Stakeholder outreach programs were notable. The project has a good video showing the benefits of piped water and the importance of paying water bills on time. The video has been shown to communities in all project towns.

#### **5. Significant Shortcomings (including non-compliance with safeguard policies):**

1. Annex 3 of the ICR shows negative FNPVs/FIRRs for all towns. The combined FIRR for the project is -7.7%. The major factor contributing to this very high negative IFRR is relatively low sales and demand in the towns compared to the very large investment costs incurred. The analyses show that under the current sales/demand scenario a positive overall FIRR could only be achieved if investment costs were a quarter of the actual size. Four of the towns (Malaba, Lyantonde, Rakai and Rukungiri) do not have calculable FIRR as they do not yet generate positive incremental cashflows. Except Rakai, the towns are expected to generate positive incremental cash flows, as the number of connections and hence consumption increases over time, but there is no clear indication as to when and by how much. Current consumption in the small towns is too small, nor is it likely that future consumption increases will be large enough to generate a positive FIRR. Thus, the project was over-designed and/or the objectives were misconceived. Clearly, water services to small towns cannot be put on a cost-recovery basis from the point of view of capital costs.

2. While the water systems are not returning positive financial returns on the capital costs, the ICR concludes that they are operationally sustainable i.e. they meet the costs of operations and maintenance. A review of BTO reports issued by the supervision missions shows that this was not the case in all years. Except for Rakai and Malaba, the other town water systems are now either showing positive operating margins or are close to break-even. The project's emphasis on setting tariffs at levels sufficient to recover operations and maintenance costs is being met. However, the negative rates of return on total investment imply that at the appraisal stage, the project should have been identified more clearly as partly "a social good", and the benchmarks on financing and cost recovery should have reflected that approach.

6. Ratings :	ICR	OED Review	Reason for Disagreement /Comments
<b>Outcome :</b>	Satisfactory	Satisfactory	Project objectives achieved, but with negative IFRR explained).
<b>Institutional Dev .:</b>	High	High	Significant strengthening of the DWD and NWSC achieved. Adoption of private operator model. Good stakeholder outreach programs.
<b>Sustainability :</b>	Likely	Likely	Provision of small town water services that can be financed over the long term depends on continuation of the private operator model, helped in part by government grant financing of capital costs for social purposes.
<b>Bank Performance :</b>	Satisfactory	Satisfactory	Project design was over-dimensioned, but careful implementation with MTR restructuring led to a satisfactory rating overall.
<b>Borrower Perf .:</b>	Satisfactory	Satisfactory	
<b>Quality of ICR :</b>		Satisfactory	

NOTE: ICR rating values flagged with '\*' don't comply with OP/BP 13.55, but are listed for completeness.

### 7. Lessons of Broad Applicability:

1. With the experience from the project and subsequent GOU programs in the small towns, a reduced investment would

have seemed possible, but it was unlikely that the investments could have been reduced by 75%. It was determined that piped water supply was the appropriate method to provide safe water in Uganda's small towns, and it became increasingly clear that the project had a strong social objective. Therefore, a positive financial rate of return on *total capital* investment may not have been the appropriate project benchmark for the original project design. A more appropriate benchmark would have been to ensure the financial sustainability of operations and maintenance expenditures and to rely on GOU policy of allocating grants for capital investments in socially deserving cases.

### 8. Assessment Recommended? Yes No

**Why?** The issue of cost recovery of capital costs vs . only recovering maintenance and operating costs in small towns needs to be examined in depth . This has implications for the Bank's projects portfolio in the water and sanitation services sector in Africa and other low-income countries. Such an analysis should look at the use of targeted subsidies and the various ways capital investment could be structured (grants; part grants and part loans; on-lending to the utility using various concessional terms and conditions; etc.) to encourage full O&M cost recovery, and partial capital cost recovery. The objective should be that the utility is able to generate sufficient funds for further investments, especially to finance system growth.

### 9. Comments on Quality of ICR:

1. The report is clearly written, and brings to the surface the basic issue of cost recovery on capital assets . There was a lack of realism in project design in setting the capital cost recovery targets without a full analysis . The ICR 's position that the appropriate benchmark is to recover operating and maintenance costs, but not full capital costs, needs to be studied further . If a more detailed assessment is undertaken, the costs and financing of providing water and sanitation services in small towns should be compared to the costs of such services in the larger cities (Kampala and Entebbe), and also be compared with the costs of service provision in small towns of other countries that have a similar economic and social structure.

2. The ICR was prepared using the services of the economist in the Bank's Nairobi office, who was part of the supervision team. This makes good use of decentralized project teams. The ICR was carefully reviewed by sector management, especially regarding the analysis and conclusions on the sustainable financing issues.