

EBRD/GEF PROJECT CONCEPT

Project Name: Danube Pollution Reduction Programme - Financing of Pollution Reduction Projects by Local Financial Intermediaries.

Countries in which project is being implemented: Countries of the Danube River Basin, focusing primarily on Bosnia and Herzegovina, Bulgaria, Hungary, Romania, and Slovenia

GEF Focal Areas and/or Cross-Cutting Issues: International Waters

Operational Programme: OP8 (Waterbody-based)

Project Linkage to national and regional priorities, action plans and programmes;

The Danube River Basin is the heartland of south-central and south-eastern Europe. The river flows for a distance of 2,857km and drains an area of 817,000km². Tributaries flowing into the Danube include the Rivers Sava, Drava, Tisza, Vah, Iskar and Siret. About eighty million people live in the basin, which includes Hungary, Romania, the Slovak Republic, Slovenia, Bosnia and Herzegovina, Croatia, about a third of both Bulgaria and the Czech Republic, significant areas of Moldova, and small parts of Ukraine.

Significant problems have arisen because of discharges of municipal and industrial waste waters into the tributaries of the Danube and into the Danube itself. Few of the major cities in the Danube basin have adequate wastewater treatment plants and agriculture, rural housing, and solid waste and sludge disposal continue to pollute. Although the flow into the Danube is some three times the flow into the Rhine and the concentrations of pollutants in the main stream are generally similar to or less than those in the Rhine, the total loads of nutrients, phosphates, heavy metals and oil reaching the Black Sea exceeds that being discharged into the North Sea by all the European rivers together.

Where the Danube meets the Black Sea, the river has formed the Danube Delta, an extensive area including lakes, reedbeds, marshes, steppes, dunes, shingle bars, costs, lagoons, saltmarshes and climax forests. As a centre of wetland biodiversity, the Danube Delta ranks among the top sites in Europe. Its waters harbour over 60 species of fish, including several species of sturgeon, several globally threatened bird species including pygmy cormorants, red-breasted geese and two species of pelican, plus important populations of otter and mink. The delta is economically vital to this region providing a major source of natural resources, principally fish, and an important source of tourist income. with considerable potential for the development of eco-tourism projects.

Programme (DPP).

Through on-going discussion between the GEF and the European Bank for Reconstruction and Development (EBRD), the Bank has been asked to consider how it might participate in the implementation of projects supporting the aims of the Danube River Pollution Reduction Programme, focusing, in particular, on nutrients reduction.

Project Rationale and Objectives:

Within the framework of the Pollution Reduction Programme, between 420 and 450 high, medium and low priority projects related to 51 significant impact areas were defined. Of these, 73 project concepts have been collated to form the DPP, which is designed to facilitate the implementation of the Pollution Reduction Programme and attract financial and technical assistance from various financial institutions and donor organisations.

Projects included in the DPP are categorised into four groups: municipal wastewater treatment, wetland restoration, industrial pollution reduction, and agriculture. The projects are developed within both public bodies, such as municipalities, and private companies. Each project description includes information on the project justification, including its transboundary effects, the project activities and components, the environmental effects and required inputs. The required inputs include information on the financial viability, and the incremental costs of the project. Of the investment costs estimated for each project, a certain proportion would be provided by the GEP (the incremental costs), and the rest could be financed through a number of other channels such as the company's own resources, government grants, or local / international loans.

GEF and the DPP are seeking financial institutions, and in particular International Financial Institutions such as the IBRD and EBRD, to provide the loan portion of projects listed in the DPP. Given the size of these projects (between US\$ 300,000 and US\$ 5,000,000) and the fact that any loan would only represent a proportion of the total investment needs, the EBRD would not be able to directly finance the loan portion of any of these projects.¹ Therefore, in order to reach small and medium sized enterprises, the Bank provides finance to local banks (financial intermediaries or FIs) who then on-lend smaller amounts of money to local businesses. It is through these FIs that EBRD proposes to participate in the financing of DPP projects. It should be noted that this project proposal will only include projects in the industrial and agriculture groups, because they are most suitable for commercial cofinancing by FIs, while offering significant opportunities for the reduction of the nutrients load in the Danube.

Option (1)

The Bank creates a new central credit facility for project funding which can distribute funds on a regional basis. Project appraisal and structuring would be undertaken by a unit located either within the Bank or in the region. This unit would be staffed by non-EBRD experts, funded through GEF money, who would prepare the grant component for submission to GEF as well as ensuring that the projects meet the relevant criteria of the Bank and the particular FI through whom the project will be passed. In this case, the FI would simply act as conduit through which funding is channelled. For each country, EBRD would identify a partner FI with whom the Bank already has an existing relationship. In order to ensure that some ownership is taken by the FI, it becomes responsible for monitoring the progress of the project and collecting repayments of the loan. The FI would take a fee for providing this service.

Advantages: The Bank can retain more direct control of project structuring and approval to ensure that the projects meet sound banking criteria and also the environmental criteria of the GEF. The project approval structure would be simplified from an FI perspective as the amount of work they have to do is greatly reduced.

Disadvantages: The costs to the Bank in terms of administrative time to set up the facility, select consultants etc., is far greater. The Bank would be directly exposed to the risks of the project because it is lending its own funds.

Option (2)

The Partner FIs take full responsibility for project appraisal and implementation, using a standardised loan format to ensure that the relevant criteria are met. Funds for the project are provided by the FIs, who are then fully responsible for project monitoring and collection of repayments. As the Bank would be working with existing FIs, there would be no need to establish a new separate EBRD credit facility.

Advantages: The costs and responsibilities of project preparation are borne by the FIs. The FIs take more ownership of the projects and are therefore more motivated to see that the projects are successful.

Disadvantages: The costs to the borrower might be greater since the project preparation costs have been borne by the FI and may well be passed on to the borrower. Since the FI is putting its own funds at risk, there is a greater likelihood that projects will be rejected as too risky. It is unlikely that FIs will have the capacity to prepare the grant components for GEF submission.

In order for EBRD's FIs to participate in these projects, a much clearer idea of the borrowing requirements for the DPP projects is required. As it stands, the total estimated borrowing requirements of the industry and agriculture groups within the DPP are US\$ 11,119,93 from

<i>Country and Sector</i>	<i>Total Investments</i>	<i>Intl. Borrowing Needs</i>	<i>Domestic Contribution*</i>
	US\$	US\$	US\$
Bosnia and Herzegovina			
Industry	0	0	0
Agriculture	8,000,000	1,600,000	0
Bulgaria			
Industry	25,646,616,	5,669,933	4,802,222
Agriculture	3,800,000	2,100,000	0
Croatia			
Industry	0	0	0
Agriculture	2,300,000	0	0
Czech Republic			
Industry	0	0	0
Agriculture	3,200,000	0	1,280,000
Hungary			
Industry	0	0	0
Agriculture	11,673,900	0	2,886,300
Romania			
Industry	11,530,000	0	6,000,000
Agriculture	12,877,000	0	0
Slovakia			
Industry	8,260,000	1,400,000	1,300,000
Agriculture	0	0	0
Slovenia			
Industry	0	0	0
Agriculture	5,273,080	350,000	1,895,000
Ukraine			
Industry	0	0	0
Agriculture	500,000	0	0
Total	93,060,596	11,119,933	18,163,522

* Figures have been included either where a specific number of domestic loans is shown or where a generic figure, covering all three categories under Baseline Domestic Contribution, is included.

Added to this, the projects need more due diligence work to ensure that, from a credit perspective, they are acceptable. There is no information on the long-term viability of the project companies, nor information necessary to make funding decisions. This would include an analysis of the companies financial statements, capacity to support the proposed investments, and preparation of a business plan. Finally, it is our understanding that further work is required on the calculation of the project component (if any) which would be eligible for GEF funding (incremental cost) and the preparation of appropriate funding applications.

In the light of the above, the following is proposed:

A GEF project preparation grant in the order of Euro 318,890 to identify and prepare 50 bankable projects (10 per country) which will contribute to the reduction of the pollution load in the Danube river Basin, with a particular emphasis on nutrients reduction, and which require commercial borrowing for at least a part of the total project cost. Additional project selection criteria are

- endorsement by the host country
- commitment of client company to implement the project
- demonstration effect / replicability
- sustainability, particularly for those project with a large grant component

Primary target countries are Bosnia and Herzegovina, Bulgaria, Hungary, Romania, and Slovenia. In identifying suitable projects, consultants will use to the maximum existing information and preparatory work, in particular the Project Concepts included in the DPP, and the Project Files prepared as part of the National Reviews under the Danube Pollution Reduction Programme. Given the limited demand for credit currently identified in these project concepts/files, a better understanding of the actual needs of the companies concerned is required. In addition, consultants may need to screen additional projects not included in the above materials.

For each project a financial analysis of the Company is required to understand whether or not the Company is able to accept the additional lending burden required to implement these projects. This information would be required by the partner FIs anyway, and be preparing this at this stage, it is more likely that the FIs would accept the projects. Project preparation will also involve determining the incremental cost element of the project and other GEF eligibility criteria.

For each project, consultants will prepare a detailed business plan suitable for submission to FIs as well as to GEF and other co-financing institutions where relevant.

Key skills require of consultants will include credit analysis/project financing environmental

options, some GEF funding would be needed for implementation support. In addition, GEF would be requested to provide the incremental investment costs identified for each project during the project preparation phase.

Breakdown of Costs (in Euro)			
Direct Expenses			
<i>1. Fees</i>	<i>Day Rate</i>	<i>Number of Days</i>	<i>Total</i>
Senior Environmental Consultant	750	135	101,250
Credit Specialist	1000	135	135,000
Administrator	350	20	7,000
<i>2. Per Diem Allowance²</i>	<i>Per Diem Rate</i>	<i>Number of Days</i>	<i>Total</i>
Bosnia & Herzegovina	210	50	10,500
Bulgaria	140	50	7,000
Hungary	126	50	6,300
Romania	165	50	8,250
Slovenia	132	50	6,600
Reimbursable Expenses			
<i>3. Air Travel</i>	<i>Cost</i>	<i>Number of Trips</i>	<i>Total</i>
	500	10	5,000
<i>4. Local Travel</i>	<i>Cost</i>	<i>Number of Trips</i>	<i>Total</i>
	40	50	2,000
<i>5. Miscellaneous</i>			<i>Total</i>
Report production			1,000