

## **GEF PROJECT CONCEPT FOR PIPELINE ENTRY**

<b>Country:</b>	Regional – East Asia and the Pacific
<b>Project Title:</b>	Strategic Partnership for a Land-Based Pollution Reduction Investment Fund for the LMEs of East Asia – Phase 1
<b>Focal Area:</b>	International Waters
<b>Operational Program:</b>	OP10 – Contaminant-based
<b>Strategic Priority:</b>	IW-1: Catalyze financial resource mobilization for implementation of reforms and stress reduction measures agreed through TDA-SAP or equivalent processes for particular trans-boundary water systems.
<b>Estimated Program Cost:</b>	\$1.0-1.5 billion (GEF inputs, plus leveraged investments)
<b>GEF Project Financing:</b>	\$70-80 million
<b>Estimated WP Entry:</b>	November 2005
<b>Estimated Start Date:</b>	Mid-late 2006 (first co-financed project effective)

### **Problem statement and strategic context**

1. As documented by the GEF/UNDP/IMO PEMSEA<sup>1</sup>-facilitated “Sustainable Development Strategy for the Seas of East Asia”, which was endorsed by Ministerial representatives of the 12 PEMSEA-participating countries<sup>2</sup> in December, 2003, land-based pollution of east Asia’s seas, coasts and estuaries is severe and worsening. It is making thousands of poor people sick every year, degrading the natural aquatic resources on which millions of the region’s inhabitants depend, and destroying the region’s globally-significant freshwater and marine biodiversity. East Asia’s many large, rapidly-growing coastal cities and their surrounding industrial and agro-industrial agglomerations are particularly severe land-based pollution “hot-spots”.

2. East Asian countries recognize the severity of the problem and plan to invest several US\$ billion in water pollution reduction measures over the next 5 years, some of which will be funded by the World Bank, the Asian Development Bank and other lenders. However: (a) these planned investments will be insufficient to reverse worsening local and trans-boundary water pollution; and (b) most of the investment will be concentrated in a few large cities and in publicly-owned and managed waste-water treatment facilities. This leaves three major gaps in the region’s land-based water pollution control efforts: (i) pollution from secondary cities and their industrial complexes, (ii) agricultural pollution, and (iii) private investment and public/private partnerships for pollution reduction.

3. In addition to PEMSEA, the GEF is currently co-financing large marine ecosystem strategic action planning and management projects for the Yellow Sea<sup>3</sup> and for the South China Sea and the Gulf of Thailand<sup>4</sup> that are producing country-driven

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<sup>1</sup> Partnerships in Environmental Management for the Seas of East Asia

<sup>2</sup> Brunei Darussalam, Cambodia, China, DPR Korea, Indonesia, Japan, Malaysia, Philippines, RO Korea, Singapore, Thailand and Vietnam.

<sup>3</sup> GEF/UNDP Strategic Action Programme for the Yellow Sea Large Marine Ecosystem

<sup>4</sup> GEF/UNEP Reversing Environmental Degradation Trends in the South China Sea and Gulf of Thailand

pollution reduction programs and new commitments for reform and investment in the participating countries. However, the country consultations facilitated by these projects have revealed that, without new pollution-reduction awareness-raising initiatives and new financial incentives and mechanisms, insufficient additional investment resources and reform actions will be catalyzed to even begin to close the above-mentioned gaps in water pollution reduction policy initiatives and investments.

#### Project objectives and goals

4. The objective of this proposed World Bank/GEF East Asia Land-Based Pollution Reduction Investment Fund Project (the Partnership Fund) is to reduce local, national and trans-boundary degradation of East Asia's marine ecosystems due to land-based pollution. It would focus on the countries involved in and help implement the action plans that are emerging from the GEF-supported planning efforts for the South China Sea and the Yellow Sea Large Marine Ecosystems, and the national and local commitments facilitated by the GEF/UNDP/IMO PEMSEA Project (Partnerships for Environmental Management of the Seas of East Asia). Its strategic objective would be to help address the above-referenced three major gaps in regional land-based pollution control efforts.

5. The project's development goal would be to promote sustainable development of the coastal areas of the East Asia region by reducing land-based pollution of its rivers and seas. Its global environment goal would be to promote the environmental sustainability of several of East Asia's large marine ecosystems by reducing land-based pollution of them.

#### How would the project achieve these objectives and goals?

6. The project would establish a World Bank-implemented, GEF-financed Investment Fund to Address Land-Based Pollution of the Large Marine Ecosystems of East Asia, the first five-year phase of which would be capitalized with \$70-80 million of GEF resources. The Fund would co-finance: (a) a series of large-scale publicly-managed, World Bank co-financed pollution-reduction investment projects or programs in regional land-based pollution "hot-spots"; and (b) a revolving fund or funds to stimulate and co-finance site-specific private and/or public-private land-based pollution investments, particularly in the manufacturing and agro-industrial sectors, also in regional land-based pollution hot spots. It would be loosely modeled on the World Bank/GEF Nutrient Reduction Investment Fund for the Danube/Black Sea Basin, which was established in 2002 and has catalyzed over \$400 million worth of anti-pollution measures.

#### Consistency with national priorities

7. The consistency of all Fund-supported initiatives with national priorities for both World Bank and GEF assistance on land-based pollution reduction would be ensured by requiring that all Fund-supported projects be both: (a) action priorities of at least one of the three on-going GEF-supported East Asia regional marine ecosystem management projects; and (b) part of the World Bank's agreed country assistance program for the relevant client country. As mentioned above, the recently-endorsed "Sustainable

Development Strategy for the Seas of East Asia”, facilitated by the UNDP/GEF/IMO PEMSEA Project, identifies land-based pollution as one of the major threats to these seas, and calls for new initiatives to address it, including policy reform, innovative financing mechanisms to stimulate investment, and public-private partnerships. It thus provides the strategic under-pinning for the Partnership Fund concept. In parallel, through the UNDP/GEF Strategic Action Program for the Yellow Sea Large Marine Ecosystem and the UNEP/GEF Program to Reverse Environmental Degradation Trends in the South China Sea and Gulf of Thailand, the participating countries are identifying their priorities for reducing land-based pollution of these two international water bodies and are trying to mobilize new and additional investment resources to finance them. These emerging strategies will also under-pin and guide the Fund’s activities.

#### Consistency with the Bank’s regional environment and country assistance strategies

8. The reduction of water pollution is an agreed priority for World Bank assistance to most of its East Asia client countries, including Cambodia, China, Indonesia, Philippines and Vietnam. The Bank’s East Asia and Pacific Region has also agreed to help its non-borrowing clients, such as Malaysia and Thailand, address this problem through knowledge-sharing and technical assistance. This proposed Partnership Fund would accord priority to coastal pollution reduction measures and actions that are identified through World Bank policy and country assistance strategy dialogues with these clients, as under the WB/GEF Danube/Black Sea Basin Strategic Partnership.

9. The proposed project is consistent with World Bank’s East Asia and the Pacific Region’s plan to expand its client assistance on regional environment issues and challenges. Marine pollution and the related problems of degraded fisheries and coastal zone areas are specifically identified as potential key issues in the Region’s draft regional environment assistance strategy, which will guide this initiative.

#### The World Bank’s comparative advantage

10. The World Bank is currently lending almost \$1 billion per year to its East Asia client countries for land-based pollution reduction measures. In developing and managing this large program, it has developed a uniquely strong combination of relevant technical skills and knowledge of country and local environmental and investment conditions, institutions and policy frameworks. The World Bank will establish an inter-sectoral core group (of its East Asia urban infrastructure, agricultural and environment specialists) to manage the Partnership Fund.

#### GEF program and policy conformity

11. The Fund will demonstrate ways to overcome the barriers to the adoption of best practices to limit contamination of the international waters environment. It will focus on priority “hot spots” identified by at least one of the three GEF-supported east Asian large marine ecosystem management projects (East Asian Seas, Yellow Sea, and South China Sea/Gulf of Thailand). It is thus consistent with the objectives and scope of the GEF’s

Contaminant-based Operational Program (OP10). It will catalyze financial resource mobilization for implementation of reforms and stress reduction measures agreed through TDA-SAP or equivalent processes for particular trans-boundary water systems, and is thus consistent with the GEF's 2004-06 strategic priority IW-1.

#### Preliminary project description

12. The East Asia Land-based Pollution Investment Fund Partnership Project would comprise an initial \$70-80 million envelope of GEF resources which would be approved by the GEF Council *en bloc* and released by the GEF CEO in several tranches to finance eligible sub-projects. The Partnership Fund Project would have two sub-components: (a) a \$40-45 million World Bank-managed pool of GEF grant and concessional loan funds (the Investment Sub-Fund) that would co-finance a series of new, large-scale World Bank land-based pollution reduction projects or programs; and (b) a \$30-35 million pool of World Bank-administered GEF resources that would finance either a regional "revolving fund" and/or several sub-regional "revolving funds" (the Revolving Sub-Fund) which would provide re-imbursable co-financing and small "project facilitation" grants for site-specific private or public-private pollution reduction investments. The design of this revolving fund or funds would be based on country-driven requests and on feasibility assessments conducted during GEF co-financed preparation of the Partnership Fund Project. The World Bank's considerable experience with revolving funds has shown that they are relatively complicated to design and operate and have mixed results. This sub-component will pilot test where and how this modality can be successful and identify what determines that outcome. Its experimental nature, uncertain impact and higher risks justifies the input of fewer scarce GEF resources than into the investment fund sub-component, the demand for and impact of which are certain to be substantial.

13. Local and provincial governments and private investors in the countries of east Asia would be able access either of these two financing modalities, as appropriate, to co-finance agreed new and additional investments and policy measures to reduce land-based pollution of their estuaries, coasts and seas. Strategically, the Partnership Fund would seek to catalyze: (a) greater involvement of the private sector in both investment and facilities management to reduce land-based pollution; (b) pollution control investments in secondary cities; and (c) pollution control investments by industrial and agricultural enterprises in regional pollution "hot spots".

14. More specifically, the Investment Sub-Fund component would finance GEF incentive grants and/or concessional loans to catalyze several large-scale (US\$250 million-plus) World Bank co-financed water pollution investment and policy reform programs or projects, similar in scale to the World Bank/GEF Guangdong/Pearl River Delta Urban Environment Project (GPRDUEP) that was recently admitted to the GEF pipeline. To ensure that this sub-fund catalyzes only new initiatives, it would not co-finance any large-scale pollution reduction projects, other than the GPRDUEP, that are currently in the World Bank East Asia and Pacific Region's agreed country assistance programs. To maximize the sub-fund's leverage, the World Bank would aim to achieve

an overall leveraging target of at least 10 units of non-GEF resources to 1 unit of GEF resources for each new sub-project that this component would support.

15. The Revolving Sub-Fund component would probably establish several sub-national, national, (and perhaps even a regional - depending on feasibility) revolving pollution investment incentive funds that would focus on land-based pollution “hot spots” within the region’s pollution reduction framework and operate to internationally-accepted financial standards. In order to be both commercially sustainable and responsive to local investment conditions, these funds would probably be managed by one or more existing, technically capable, financial intermediary-type institutions in the region. The fund(s) would provide either (a) low interest, relatively short-term loans, or (b) loan guarantees to catalyze investments in pollution control by private enterprises, public/private partnerships and by collaborating municipal governments in their target area that are major polluters. A special relationship would be developed between PEMSEA and the World Bank on the design of this component during the project preparation phase.

16. The Partnership Fund Project’s project eligibility criteria are likely to include: (a) consistency with documented national priorities; (b) achievement of minimum effluent quality standards; (c) financial sustainability; (d) collaboration on regional water quality data production and sharing, and (e) consistency with “hotspots” identified by the regional LME trans-boundary diagnostic analyses or commitments made in the Strategic Action Program and/or in approved PEMSEA integrated coastal management strategies.

17. Its establishment (which would be widely publicized), its eligibility criteria (particularly the requirement that recipients achieve minimum effluent quality standards), and regular show-casing of its activities and results would increase pressure on public officials to be accountable for reducing land-based pollution and would thereby have significant motivational and catalytic impact on them. Assuming it is successful, the prospect of the Fund’s replenishment would also encourage and facilitate the scaling-up of municipal land-based pollution reduction programs over time.

#### GEF project preparation and implementation procedures

18. The Partnership Fund Project’s objectives, design, sub-project eligibility criteria, operational modalities and GEF resources would be approved by the GEF Council. When approving the project and its \$70-80 million of GEF resources, the GEF Council would delegate authority to the GEF CEO to release Fund resources to the World Bank in tranches to: (a) co-finance a group of World Bank co-financed projects that were fully consistent with the Bank-managed investment sub-fund’s eligibility criteria; and (b) establish revolving fund(s) that satisfy the agreed eligibility criteria for such funds. All commitments would reported to the GEF Council in an annual progress report. The World Bank would strive to achieve maximum leverage of its own-managed sub-fund’s resources by, *inter alia*, identifying large projects or programs that mobilize many times their GEF co-financing, and by using non-grant financing modalities, such as contingent grants and no-interest contingent loans, whenever possible. A firm co-financing goal of

10:1 would be set for the overall Strategic Partnership and individual sub-projects that exceed this target would be given preference.

19. The relevant GEF partners - the World Bank, UNDP, UNEP and the ADB - would all promote investor access to the two sub-funds through their assistance and policy dialogues with their client national and local governments, major industrial and agricultural polluters, and with potential private investors and/or operators. Projects identified through these dialogues for support would be reflected in the appropriate World Bank Country Assistance Strategy (CAS) documents. The World Bank would also use its convening power to encourage other lenders, donors, potential investors and their country clients learn about and access the Fund.

20. The Fund would have the following strategic attributes: (1) Up-front commitment of a funding envelope by the GEF Council, which would signal the availability of a predictable supply of GEF grant and concessionary financing for pollution reduction measures that could be released quickly by the GEF CEO in tranches, based on eligibility criteria being met and on satisfactory overall Fund performance. (2) Its creation would focus more attention on the east Asia region's serious and growing environmental problem of land-based pollution and stimulate more action on it. (3) The investments that the Fund supported would have regional as well as local benefits. (4) The Fund would provide an effective framework to transfer land-based pollution investment and policy experience, to build cooperation on this issue with other partners, and to encourage replication of successful initiatives throughout the east Asia region.

#### Types of projects that would be supported

21. The following types of project would be eligible for support from the Fund:

- Municipal wastewater treatment facilities and sustainability reforms.
- Industrial and agri-processing wastewater collection and treatment.
- Agricultural and land management reforms and actions that reduce point and non-point sources of peri-urban and rural water pollution.

#### Sustainability

22. The sustainability of the projects supported by the investment fund component would be achieved by focusing on investments that have strong local commitment, are set within a supportive policy and institutional framework, face moderate to low risks, are economically justified, and offer good prospects of full cost recovery. These criteria would be enforced by requiring each sub-project to fully satisfy the World Bank's demanding project evaluation criteria, risk assessment and social and environment safeguard procedures in order to qualify for GEF co-financing. The sustainability of the revolving fund component would be promoted by: (a) using well-established, financially-sound local financial institutions to administer the individual funds whose staff know their local financial market conditions and borrowers and are experienced at providing financial intermediation services within those markets; (b) establishing eligibility criteria

for applicant sub-projects that include rigorous financial feasibility standards; and (c) monitoring the operational performance of the managing institutions closely.

### Replicability

23. The Partnership Fund Project will promote replication of its activities in two directions - sequentially and in parallel. Sequentially, as it is intended to be the first phase of a long-term (at least 10 year) GEF East Asia pollution reduction investment promotion program, the project will lay the groundwork for its own replication through a second, and hopefully larger second-phase. This will be achieved largely through an intensive monitoring, learning, outreach and evaluation process. In parallel, the project will promote replication of its successes, and particularly its more innovative initiatives, during its own lifetime. A key element of its replication strategy that will serve both these objectives will be an aggressive awareness and results dissemination program. This will employ multiple mechanisms (regional and global conferences, project and sub-project websites, printed materials, etc.) and involve multiple partners (UNDP, UNEP, ADB, PEMSEA, ASEAN, etc). Through these multiple mechanisms and partnerships, information on successful investment and policy reform promotion strategies, innovative financing modalities and new partnerships will be widely disseminated. This will promote replication of both individual sub-project initiatives and of the Phase 1 project itself. Given the high level of concern throughout the region with land-based pollution of its marine ecosystems, the Partnership Fund has excellent prospects of attracting new partners, such as neighboring developed nations. This too will be encouraged.

### Stakeholder Involvement

24. A wide variety of regional stakeholder awareness and involvement mechanisms will be actively utilized during both project preparation and implementation. The three on-going GEF-supported regional LME management projects would be one of the primary mechanisms for stakeholder outreach and involvement. Their Secretariats have been consulted on this initiative and some have offered suggestions which are reflected in this proposal. Following its admission to the GEF pipeline, the project proposal will be explained to the national participants in each of these projects and their advice on its design and their support will be requested. The Project Concept will be circulated to all the concerned GEF Focal Points and their advice and support will be requested. In parallel, the World Bank will explain the concept to the national counterparts with whom it develops and monitors its Country Assistance Strategies and Programs, and to its technical counterparts who are directly concerned with land-based pollution reduction in their respective national, regional and local institutions. All these partner groups will be regularly briefed on and encouraged to advise on the emerging project design during its preparation and will be briefed and consulted annually on implementation progress.

### Monitoring and evaluation

25. Each sub-project co-financed by the Partnership Fund would have specific pollution reduction objectives and a rigorous activity, output and impact monitoring and

evaluation system, which would feed into a Fund-wide monitoring and evaluation program. The Partnership Fund's activities and their emerging impacts would be reported annually to the regional UNDP/GEF and UNEP/GEF LME project secretariats and to the GEF Secretariat and Council. The three GEF regional projects would each nominate one member of a coordination committee, to be established and chaired by the World Bank, that would advise the project management team on the project's design and on the implementation process.

#### Partnership preparation funding and strategy

26. Following pipeline entry, the GEF will be requested to provide a PDF Block B grant of up to \$700,000 to co-finance detailed preparation of the Partnership Fund. Those resources would finance both its technical design and dialogue with the countries participating in the three regional GEF international waters projects with regard to the types of revolving fund(s) to be tested in Part B of the Partnership. (National, sub-national and perhaps regional revolving funds may be tested). It is recognized here are potential benefits and risks to each type of revolving fund. A regional revolving fund may have more potential to leverage capital than a national or sub-national fund, attracting not only the private sector but also interest from IFIs, donors, Socially Responsible Investment (SRI) funds and commercial financial guaranty insurers (on a reinsurance basis). In addition, a regional fund may be able to spread risk, with a greater number and variety of projects underway at any one time. In contrast, national and sub-national revolving funds operated by existing financial institutions may be more acceptable local clients, involve less risk and complexity, and may be better tailored to local investment contexts and to existing financial intermediation capacity. The feasibility of each type of revolving fund would be examined during Partnership Fund preparation.