# Template for a PAD/PCN Project Component for Blended Financing with Domestic Commercial Banks

*The following is a sample template for including a component to a WSS World Bank Project designed to access commercial finance for investment financing. The template can be used for inclusion into Project Appraisal Document (PAD) or shortened for a Project Concept Note (PCN).*

1. Component Objectives
2. The component will have several objectives. The first will seek to expand water and sanitation infrastructure investments by leveraging public finance to facilitate access to commercial financing in a blended finance arrangements. Secondly, the project will seek to reduce information gaps that have deterred commercial lenders from lending to the WSS sector. Thirdly, World Bank financing will seek blended financing arrangements whereby to: (i) improve the financial sustainability of the WSP(s) through performance improvements; and (ii) better allocate financial resources by leveraging additional commercial domestic finance.
3. Component Beneficiaries
4. The primary beneficiary will ultimately be the WSS existing and future customers that receive expanded and improved services from their utility. The WSP itself will improve its capacity to finance future investments when they are in fact required. The government will benefit from being able to crowd-in commercial sources of finance, commensurately expanding the total pool of financing for infrastructure services and allowing it to allocate more limited budgetary resources to non-revenue generating sectors and programs.
5. Component Description
6. The project supports the use of public sector funds in a blended financing structure to facilitate the access by the WSP to commercial financing. The project will provide technical assistance for implementation support activities as well as a mix of public grant and/or concessional loans for facilitating access to commercial financing.
7. Pre-project preparation activities have carried out an assessment of the financial sector and determined a capacity for commercial lender participation under several criteria including: (i) well developed and performance improvement programs; (ii) adequate loans security measures; (iii) blending arrangement with World Bank and donor participation, and (iv) other provisions for participations. In addition, some preliminary screening has been carried out of eligible WSP to ascertain several bankable financing options.
8. *Sub-Component 1 - Implementation Support Activities - Project Management, Coordination with Commercial Lenders, Final WSP Selection, Sub-Project/Financing Preparation, and Supervision ($1.M to $2M)[[1]](#footnote-1).*This sub-component will provide technical assistance for the management of the overall program as follows:

* Additional screening of WSPs to target with more thorough diagnosis of best candidates.
* Carrying out tariff adequacy analysis to determine whether tariffs are cost reflective aside from needing to cover performance inefficiencies.

* Working with the WSP to best articulate their action plans for performance improvement and for developing preliminary cost estimates to be submitted for financing.
* Putting together a financial projection model and populating it with preliminary cost and revenue date encompassing the entire WSP operation inclusive of the current capital investment requirements to assess financial viability.

* Developing a blended financing plan and determining the appropriate staging of commercial loans within that plan. Reviewing the financing plan with commercial lenders and determining requirements for loan security and/or subordinate loan agreements. Assess financial viability of the plan with the inclusion of commercial financing component.
* Discussing the need for additional guarantees if necessary.
* Finalize sub-plans for financing and implementation.
* Monitor post finance implementation to ensure appropriate progress against plans by WSP. Troubleshooting and determine the need for follow-up financing in case corrective actions are needed.
* The activity will also work with commercial lenders to transfer knowledge on diagnosing and financing water sector entities.

1. *Sub-Component 2 - Public Financing Support to Leverage Commercial Loans to Sub-Project Financing ($5M to $10M).*This sub-component provided the public finance component of the financing plans forsubprojects. The financing support can be a mix of concessional loans or grants that are provided by the implementing agencies under subsidiary loan and grant agreement for each subproject. The public portion of the financing will be blended with pledges of commercial loans based on the financial engineering that derives a financial solution for the intended financial structure. The financial solution will be one that yields a projected positive cash flow for each year of the projected period and that will accommodate criteria for lending of the commercial lender. Besides amounts related to the mix of funds, the financial engineering will also determine the appropriate timing for each.
2. The program will support many different WSP investments, but the following are considered the most viable options for creating bankable subprojects for commercial lenders.

* WSPs that may be just recovering costs but also possess a series of performance issues that, if corrected, can improve the entity’s long term financial viability. These are WSPs that may also have tariff levels that are close to cost recovery but consumers have been overcharged in paying for performance problems. The tariff adequacy analysis carried out under the TA support will be able to determine this.
* The program can also support creditworthy WSPs but, for various reasons, have not have access to commercial financing. Blending can increase tenor and reduce costs for economically justifiable projects.
* Leakage programs are indeed worthwhile investments, but these should be combined with a connection program such that can immediately create revenue from additional paying customers. Similarly, commercial loss initiatives much also be combined with increasing new paying connections. Cutting off non-paying customers or reducing water thefts does little to add to the bottom line unless the water saved is transferred to a paying customer.
* Connection programs where the system is still underutilized.
* Under this program, WSPs should not consider investments that require major works such as, investing in an additional water source. Again, while these investments may be desirable they typically do not yield quick financial returns and as such may create additional risks and may not be bankable for commercial lenders.

The program should be demand-based, and criteria would be established for prioritizing eligibility for blending arrangements with public grants and concessional loans. A competitive process would be desirable whereby interested WSPs would come forward with their preferred commercial lender and with a cohesive investment for financing.

1. For support between 5 to 7 separate blended financing transactions. [↑](#footnote-ref-1)