I. Project Context

Country Context

The period of relative political stability that Ecuador has enjoyed in recent years is expected to continue, in contrast with the political instability of the 90’s when Ecuador witnessed seven Presidents in 11 years, and several Ministers of Finance that lasted an average of six months. During this period, high growth combined with falling inequality has led to important gains in reducing poverty and promoting shared prosperity. As a result of these efforts, Ecuador is one of the countries in the Latin America and the Caribbean Region with the strongest results in reducing poverty. During 2001-11, GDP per capita growth in Ecuador was above regional average levels (3.1% vs. 2.2%) . Growth has moderated (it was 5.1 percent in 2012), but remains strong at 3.5 percent year-on-year in the second quarter of 2013, and above the regional average of 3 percent. Progress in reducing inequality has exceeded regional trends. National poverty rate decreased from 37.6 to 23.7 percent between 2006 and June 2013. Extreme poverty rate fell from 16.9 to 8.5 percent. The income for the 40 percent of the poorest population grew by 8.8 percent on average annually between 2000 and 2011, compared to 5.8 percent at the national level, the highest growth rate in the two poorest quintiles of the region. Notwithstanding these significant strides in poverty
reduction and growth of middle class, more than half of the population in Ecuador remains poor or vulnerable to falling back into poverty.

The Government recently released its updated Development Plan. El Plan Nacional del Buen Vivir 2013-2017. This Plan relies upon 2 main lines of action: i) the development of a strategy for the eradication of poverty, which is currently being designed by SENPLADES (National Planning and Development Secretary); and ii) the transformation of the productive matrix (e.g. energy matrix, irrigation). The plan has 12 objectives focused on improving the quality of life of the population; fostering equality, cohesion, inclusion and social and territorial equity in diversity; among others. The water and sanitation (WSS) sector is a priority for the GoE and at the core of its poverty reduction strategy, as the GoE expects that through increased and improved access to both services, national poverty rates would be further reduced by over 9% by 2020.

The World Bank Group's Interim Strategy Note (ISN) for Ecuador discussed on April 9, 2013 identified access to WSS and other basic services at the sub-national levels as key priorities for the authorities to contribute to the country’s goal for inclusive and sustainable growth.

**Sectoral and institutional Context**

Although access to improved water supply and sanitation have experienced great progress over the last decade, service standards in Ecuador remain low in comparison with the regional average. In this sense, in 2010 the percentage of households connected to a public drinking water distribution networks was 72% in urban areas and 26% in rural areas, while the average in the Latin American and the Caribbean region was 94% and 62% respectively. Coverage of sewerage systems (54% in total, 71% in cities and 23% in rural communities) and wastewater treatment rate (24% in urban areas in 2007) are also low. Monitoring of drinking water quality is weak, with only 24% of water supply systems surveyed at the national level having a system in place for water quality monitoring.

The overall quality of WSS services varies significantly across cities and regions. With a few significant exceptions of the bigger cities (Quito, Guayaquil, Cuenca, Ibarra), the situation in many of Ecuador’s cities reflects decades of under-investment and poor management. For example: i) only about 40% of GADs have updated customer databases for water supply services and 16% for sanitation services; ii) technical and commercial losses are high – estimated at 65% in 2005; and iii) financial sustainability is at stake (in 2009 just in 92 municipalities, of a total of 221, drinking water services’ revenues represented 50% or more of the operation and maintenance costs, and 100% in just 33 municipalities, implying a heavy subsidization of service operation).

The WSS sector institutional framework is headed at the national level by the recently created National Water Secretariat (SENAGUA) as the single authority for water resources in the country. With regards to the WSS services, the Sub-secretariat for Potable Water and Sanitation within SENAGUA (Sub-secretaria de Agua Potable y Saneamiento, SAPyS) has inherited the competencies, which were formerly under the Ministry of Housing (MIDUVI). The SAPyS is currently institutionally nascent and insufficiently staffed to perform its functions. As part of the ongoing overall sector and institutional reorganization, it is envisaged that SENAGUA will have the following three functions: i) policy making, including the development of sector policies, strategic planning and norms; ii) regulation, including tariff structures and subsidy mechanisms, service standards and relations between GADs, service providers and users; and iii) the provision of
technical assistance to service providers and execution of regional multi-purpose water infrastructure projects. The new institutional framework is currently under design and Project Component 5 will assist in its finalization and operalization.

As per constitutional mandate, Ecuadorian municipalities are responsible for the provision of WSS services within their area of jurisdiction, either directly or through delegation to a public company or a community based organization. Of the existing 221 municipalities, 63 have established a dedicated WSS utility for the provision of services in urban areas; one has delegated its responsibility to a private operator (Guayaquil); and the rest provide the services directly through a municipal division. Most communities in rural areas have created a “Junta Administradora de Agua y Saneamiento” (JAAS, a community led organization) for the provision of the services. It is estimated that there are around 5,000 JAAS in Ecuador today.

The Banco del Estado de Ecuador (BdE) is a government-owned public financial institution established in 1976 to provide financing for investment in public services and infrastructure through the granting of loans to local governments and state-owned entities. Since 2007, BdE has been actively involved in the financing of municipal water and sanitation infrastructure and technical assistance services, having already invested nearly USD 800 million in more than 450 projects across the country with the financial support of the German Reconstruction Bank (KfW), the Corporacion Andina de Fomento (CAF) and the Inter-American Development Bank (IDB) and the World Bank, amongst others. Some of the investments financed with CAF and IDB support through the PROMADEC I and II projects and the PYRSA project respectively are still under implementation.

The PROSANEAMIENTO Program (the “Program”) was developed in 2012 to operationalize the GoE’s public investment strategy in the WSS sector and later on to reach the ambitious goals set by the 2013-2017 National Development Plan for WSS services coverage: by 2017, 95% of the households should get their water from a public drinking water distribution network and their toilets should discharge to a sewer or a septic tank. To achieve these goals, the Program, will finance water and sanitation infrastructure and technical assistance services for improving service provision quality and sustainability. The program builds and scales up achievements of the above mentioned programs previously funded by BdE. The estimated total cost of the PROSANEAMIENTO Program is US$ 5 billion, including direct subsidies from the national government (US$ 3 billion) and contributions from municipalities through loans from BdE (US$ 2 billion). The amount of the subsidy responds to a pre-established formula, based on poverty rates, WSS coverage and nutrition levels, which will favor both the poorest and least served municipalities, subsidies range from 14% to 95% of the cost of the investment.

II. Proposed Development Objectives
The Project Development Objectives (PDO) for the proposed Project are to increase sustainable access to water supply and sanitation services in participating GADs (Gobierno Autónomo Descentralizados) and to strengthen institutional capacity for improved management and delivery of these services at the national and local level.

III. Project Description
Component Name
Component 1: Pre-investment (US$20 million, 100% financed by the IBRD)
Comments (optional)
This Component will finance the preparation of studies for investment subprojects, which includes, inter alia, pre-feasibility and feasibility studies, basic designs and other technical studies, and environmental and social assessments. The Component will also finance the specialized independent supervision of such studies (‘fiscalización de estudios’). BdE, SENAGUA and MAE are currently developing standard Terms of Reference for technical studies and environmental and social impact evaluations and assessments. The feasibility studies will incorporate an assessment of the subproject’s economic and financial viability.

Component Name
Component 2: Municipal Water Supply and Sewerage Infrastructure (US$ 311.2 million of which the Bank will finance US$206.2 million)

Comments (optional)
This Component will finance subprojects for the construction and rehabilitation of water supply and sanitation systems, including, inter alia, transmission, distribution and collection networks, water treatment plants, storage tanks, pumping stations and main collectors, wastewater treatment plants and discharge infrastructure, septic tanks and other sanitation solutions. The Component will also finance the specialized independent supervision of construction activities (‘fiscalización de obra’).

Component Name
Component 3: Technical Assistance, Institutional Strengthening and Capacity Building for Municipal Autonomous Decentralized Governments (GADs) and Service Providers (US$ 10 million, 100% by IBRD)

Comments (optional)
This Component will finance consultancy services, equipment and capacity building activities to BdE and the GADs and/or their municipal utilities to strengthen the existing administrative, technical, financial, commercial, and operational capabilities at the GAD level to improve overall management, operational efficiency and financial viability of the services. Technical assistance for the strengthening of GADs and/or their municipal water utilities will be provided through BdE's existing Technical Assistance Program, the PATGES (Programa de Gestión de Servicios), and initiated by a task-force of independent experts and consultants to be hired by BdE under the Component.

Component Name
Component 4: Project Management and Administration within Banco del Estado (BdE)(US$7 of which US$6 million will be financed by the IBRD)

Comments (optional)
This Component will finance activities associated with overall Project management by BdE, including project-related audits, monitoring and evaluation activities, systems and equipment, and ad-hoc consultants to support BdE and the GADs in the management of environmental and social issues as well as safeguards and fiduciary aspects (including capacity building and training activities on these aspects for BdE and the GADs).

Component Name
Component 5: Technical Assistance, Institutional Strengthening and Capacity Building for SENAGUA (US$1.8 million, 100% financed by the IBRD)

Comments (optional)
This Component will finance the strengthening of SENAGUA to perform its functions with regards to the WSS sector in order to ensure medium and longer term sustainability of investments. The Component will focus on three lines of action: (i) design and implementation of a regulation
strategy (including the design and development of regulation tools, systems, equipment and training for SENAGUA); (ii) development of specific policies and technical norms and technical assistance studies for the improvement of specific aspects of service provision in the GADs and for the implementation of PROSANEAMIENTO, including training and capacity building activities for SENAGUA and the GADs; and iii) Project management (audits, reporting, and ad-hoc costs of administering the component within SENAGUA).

**IV. Financing (in USD Million)**

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**V. Implementation**

**VI. Safeguard Policies (including public consultation)**

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Comments (optional)

**VII. Contact point**

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