I. Introduction and Context

Country Context

Nigeria is a federal system comprising the federal government at the center, a federal capital territory administration, 36 state governments and 774 local government councils (LGCs). Nigeria is the most populous country in Africa with 162.5 million people (8th highest in the world) and is growing rapidly at about 2% annually (with 40% of this population estimated to be below 14 years of age). It is also the third-largest economy in Africa, with a GDP of about USD 340 billion annually (about USD 2,400 per capita) in PPP terms, split almost equally between agriculture, industry, and services. It is one of the fastest growing economies in the world, with average GDP growth rate between 2003 and 2010 of 7.6 per cent. The economy is dominated by oil (it is the 8th largest oil exporter globally); and gas, which constitute 25% of GDP and provides 85% of government revenue. Over 75 percent of agricultural households in the north live below the poverty line. Nigeria’s Human Development Index ranking is 158th in the world.

Nigeria faces significant short-term challenges. The global economic crisis is affecting the economy through decreased international financial flows—direct foreign investment, private foreign lines of credit, and remittances—as well as a lower price of oil, which has a large impact on Nigeria’s trade and fiscal balances.

Medium term development challenges are equally large, however. Poverty is significant in Nigeria,
and reducing it will require strong non-oil growth and a focus on human development. Constraints have been identified to enhancing growth, including the investment climate; infrastructure, incentives and policies affecting agricultural productivity; and quality and relevance of tertiary education. In spite of successful initiatives in human development, Nigeria is off-track for meeting most of the Millennium Development Goals (MDGs), with a particular focus required on Northern Nigeria.

According to the WHO/UNICEF Joint Monitoring Program (JMP), access to reliable water sources in Nigerian urban areas has declined from 79 percent in 1990 to 74 percent in 2010 (JMP 2012), while developing countries’ urban water coverage is on average 94 percent. While the JMP concludes that the world is on track to meet the urban water supply Millennium Development Goals (MDGs), this does not seem to be the case for Nigeria. Considering that Nigeria accounts for nearly 47 percent of the West African population, this sub-region’s success in meeting the MDGs in urban water may be compromised.

Sectoral and Institutional Context

The state of water services in Nigeria is one of the poorest in sub-Saharan Africa. Historically, Nigeria’s water supply and sanitation sector has been characterized by the absence of policies that could enable efficient and sustainable services to be provided. Specifically, water tariffs do not reflect the cost of services; there are no autonomous state water boards; perpetual operating deficits deprive the state water boards of funds for maintenance and new investments, while power shortages cause intermittent water services and damage to electromechanical equipment. The public sector has in most cases not been successful in meeting more than a small portion of the demand for water and sanitation. Many households, often the poorest, end up purchasing water from private vendors much more expensively than from the public supply. Water supply services, where they exist, are still unreliable and of low quality and are not sustainable. Many water supply systems have extensive deterioration and poor utilization of existing capacities due to under-maintenance, poor operation and inadequate power supply.

In the Nigerian urban water sub-sector, flat rate water tariffs are the norm, and the revenues collected from them only represent a small portion of the cost of production and distribution. While difficult to measure in the absence of metering, non-revenue water is considered to be very high, estimated at 50 percent or more. Lack of financial autonomy is at the heart of the poor performance of all water utilities, coupled with frequent changes in management. Overstaffing in water utilities is also a problem. Worse still, countrywide, house connections to urban water supplies have declined from an average of 32 percent in 1990 to only 8 percent in 2010 (JMP 2012).

The Government's strategy for urban water supply is embedded in each State Economic Empowerment and Development Strategy (SEEDS) and stresses that increasing access to potable water is key to achieving health outcomes and sustained poverty reduction. This is also affirmed in the Government of Nigeria’s water supply policy. The water policy states that the overall objective of the urban water supply is to “improve the public health and economic well-being of urban populace through provision of adequate, safe and sustainable water for domestic, commercial and industrial purposes in a planned and coordinated manner, at reasonable cost to enable water operators to breakeven. At the Federal level, good foundations upon which future reform activities can be easily built have been recently developed, including inter alia: (i) National Low Income Household Service Strategy (LIHSS) for Water Supply & Sanitation; (ii) Model Water Supply Service Regulatory Law (WSSRL); (iii) Model National Water Supply Regulatory Handbook; (iv)

Several donors have been supporting the water and sanitation sector in Nigeria during the last decade. The Bank gave a US$ 5 million credit for the small towns’ water supply and sanitation program pilot project that was implemented from 2000 to 2003. In 2004, the Bank approved the first National Urban Water Sector Reform Project (NUWSRP1) in Kaduna, Ogun, and Enugu States of US$ 120 million (followed by an additional financing of US$ 80 million in 2010). In 2005, it approved the Second National Urban Water Sector Reform Project (NUWSRP2) in Lagos and Cross River States of US$ 200 million (and an additional financing of US$ 120 million has been approved on May 2012). The African Development Bank is processing their support to two States (Oyo and Taraba States) while the European Commission is assisting six States of Cross River, Anambra, Osun, Kano, Jigawa and Yobe States in their water sector reform with limited investment on water supply infrastructure rehabilitation and expansion. The French Development Agency is in the process of assisting Cross River State through the Bank NUWSRP2, and USAID is providing institutional and reform support to Bauchi State.

The main objectives of the NUWSRP1 and NUWSRP2 are to increase access to piped water networks in some urban areas and make urban utilities more reliable and financially viable. The projects cover rehabilitation of treatment facilities, extension and rehabilitation of distribution networks, increasing the number of household connections and stand posts, updating the customer database and full metering to reduce water loss and to ensure that billing efficiency is increased. Support is also provided for the structuring of Public Private Partnerships (PPP) and capacity building/strengthening for investment planning, linking investments to cost recovery and ensuring the financial sustainability of the urban water sector.

While the two projects are on track and efforts are being made to ensure achievements of the set objectives, a number of lessons have been learnt in the course of implementing the projects as follows:

- The reform component (policy, legal framework, institutional strengthening, tariff reform and capacity building) was not given adequate attention at project design; reforms were programmed to be implemented concurrently with the physical rehabilitation and systems upgrading. Consequently, the State Government (SG) and the Water Agencies (WA) have not be giving sufficient incentives/penalties to focus on them, which puts the projects’ sustainability into question.
- Reform requires a top-bottom approach. The reform of the WA ought to have been led by the Ministry superintending them. Since this has not been the case in the on-going projects, this has undermined the reform process;
- The scheduled rehabilitation works were not based on adequate feasibility studies. This has led to serious cost overruns in virtually all the states, with the attendant additional financings that were provided by the Bank albeit delays that were registered.
- Selection of the five States that are currently participating in the project was not adequately backed up with commitment to carry out the necessary reform by the political leaders in the States. This partly explains the modest achievements so far made on the water sector reform efforts in the States.
Following the January 2012 workshop on water utilities reforms designed by the World Bank Institute and attended by the SWAs of all States of Nigeria, the latter were asked to prepare Performance Improvement Plans (PIPs) to plan their reform agenda. To accompany this process, a provision was included in the NUWSRP2 Additional Financing for the FMWR to train the SWA operational staff on financial modeling and preparation of PIPs. The SWAs will be requested to develop their PIPs based on the financial model and submit it to the FMWR to serve as an input for selecting the participating States. Additional to the PIPs, a benchmarking training and implementation exercise carried out by the Water and Sanitation Program (WSP) at the end of September 2012 would allow identifying additional states that could be eligible for emergency and rehabilitation works based on their commitment to reform.

Relationship to CAS

The Project is consistent with two out of the three priority themes presented in the Bank’s Country Partnership Strategy for Nigeria (2010-2013). The CPS focuses on three themes to transform and diversify Nigeria’s economy: (i) improving governance; (ii) maintaining non-oil growth; and (iii) promoting human development. Improving governance in the water sector is part of the first theme, and access to improved water supply will contribute to the third theme, promoting human development. One of the aims stated in the CPS is to develop measurable service standards for State Water Boards. This is to be achieved by developing frameworks for assessing accountability and responsiveness. The areas to be covered by the water governance reforms include expenditure management, development of sector strategies, strengthening of sector institutions and improving the policy and regulatory environment. These activities combined with targeted investments in infrastructure to improve services will be part of the proposed new operation.

II. Proposed Development Objective(s)

Proposed Development Objective(s) (From PCN)

Improve the coverage, quality and efficiency of water supply

Key Results (From PCN)

13. Proposed Key Performance Indicators (KPIs) to measure project success in achieving the PDO may include the following:
   a) Percentage of O&M costs recovered from revenue
   b) Number of additional households receiving water services
   c) Number of Private Partnership providing services for Small Towns
   d) Increase in number of hours of water supply in selected utilities
   e) FMWR has established a framework for supporting States and Water Utilities based on competitive criteria.

III. Preliminary Description

Concept Description

The strategic thrust of the project is to facilitate the transformation of the way services are provided, by supporting the introduction of sector reforms accompanied with significant improvements in water service delivery in both quality and coverage. While the financial needs for the rehabilitation and expansion of the selected States are considerable, of even more crucial importance will be in the “software” – the changes in how utilities and other water providers makes investment decisions and charge and collect for services.

The project would focus on two or three States selected accordingly to technical and economic
criteria including demonstrated willingness and commitment to continue further reforms, readiness to implement sound large investments, and potential for replication in other States.

Project Description

The project will have three main components:

Component 1: Rehabilitation and Expansion of Water Production and Distribution Facilities ($250M) and Small Towns Water Supply Improvement through PPP in the selected States under an OBA (Output-based Aid) basis (minimum subsidy) ($30M). Total of $280M

Subcomponent 1.1 - Rehabilitation and Expansion of Water Production and Distribution Facilities ($250M)
This will be carried out in six (6) emerging States to be selected through an evaluation during project preparation, including any State that may qualify based on previous reform efforts but with an aim of having broad geographical representation. The Bank project loan would support 2-3 emerging States, while other donor partners will support additional States where the impacts from reforms and investments can demonstrate the performance improvements of the proposed approach. Investments under this component may include large PPP transactions so that sizable parts of the urban system or network could be outsourced, including water production, water metering-billing-collection (including reduction on NRW), sewerage treatment or management of secondary and tertiary networks.

Subcomponent 1.2 - Small Towns Water Supply Improvement through PPP in the selected States under an OBA (Output-based Aid) basis (minimum subsidy) ($30M).

The support to the selected States will comprise the implementation of pilot experiences in the provision of small towns’ water services.
The Small Towns water component will be built on the experience of successful projects in Uganda, Colombia and Paraguay, where “reverse concessions” allow the private sector in partnership with local governments and water users associations to Design, Build and Operate the system under negotiated tariff against system output payments from the government.

Component 2: Institutional Reform, Capacity Building and Emergency Works at the State level ($55M) – This component will finance studies, training, goods, emergency and rehabilitation works and services in up to 12 selected States and Federal Capital Territory to lay a solid foundation for reform;
It is proposed that all the selected 12 States be carried on to this Stage. Under the stage, funding should be allowed for each State to carry out, among other the following activities: establishment of water policy and law, customers enumeration (cadaster), Improving revenue billing and collection, Tariff reform, Regulatory reform, improving financial management, reduction of non-revenue water including metering, implementation of limited emergency works to maintain minimum service standards, and strategic training of the State Water Agency (SWA) staff as well as development of urban water supply master-plans.

Component 3: Institutional Reform, Capacity Building and Project Management at the Federal Level ($15M) – This component will be implemented by the Federal Ministry of Water Resources, and will cover Capacity Building and Institutional Reform ($8M) and Project Management,
Monitoring & Evaluation ($7M).

Subcomponent 3.1 - Capacity Building and Institutional Reform ($8M). This subcomponent will support the establishment of a framework that allows a more transparent and efficient support from the Federal level to the State level. It will comprise the clarification of roles and responsibilities, innovative mechanisms for co-financing between level of governments (Federal, State and Local), as well as the elaboration and enactment of associated regulations and financial tools. Additionally this subcomponent will explore on the feasibility of establishing continuous federal programs – rather than single projects – that can redress the current geographical and sub-sector dispersion of donor’s funds that limit project’s impact.

Subcomponent 3.2. Project Management, Monitoring & Evaluation ($7M). Additional fiduciary and safeguards staff would be financed under this component, as well as other operational and logistical incremental costs associated with the project. The subcomponent will also finance the Monitoring and Evaluation Framework for the project.

IV. Safeguard Policies that might apply

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V. Tentative financing

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VI. Contact point

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