



Extended Annual Review Report

Project Number: 49084-001
Loan Number: 3357
October 2020

CT Environmental Group Limited Small and Medium–Sized Enterprise Industrial Wastewater and Sludge Treatment Project (People's Republic of China)

This is an abbreviated version of the document, which excludes information that is subject to exceptions to disclosure set forth in ADB's Access to Information Policy.

Asian Development Bank

CURRENCY EQUIVALENTS

- Currency units – yuan (CNY)
 – Hong Kong dollar/s (HK\$)

	At Appraisal (6 November 2015)	At Project Completion (25 May 2020)
CNY1.00 –	\$0.16	\$0.14
\$1.00 –	CNY6.35	CNY7.13
HK\$1.00 –	\$0.13	\$0.13
\$1.00 –	HK\$7.76	HK\$7.76

ABBREVIATIONS

AESPR	–	annual environment and social performance report
ADB	–	Asian Development Bank
CTEG	–	CT Environmental Group Limited
EHS	–	environment, health and safety
EIRR	–	economic internal rate of return
EPD	–	Environmental Protection Department
E&S	–	environmental and social
ESMS	–	environmental and social management system
FIRR	–	financial internal rate of return
IEE	–	initial environmental examination
IFC	–	International Finance Corporation
m ³	–	cubic meter
MOF	–	Ministry of Finance
MOHURD	–	Ministry of Housing and Urban–Rural Development
NDRC	–	National Development and Reform Commission
NSO	–	Non-sovereign Operation Risk Rating
PRC	–	People’s Republic of China
RRP	–	report and recommendation of the President
SMEs	–	small and medium–sized enterprises
SPS	–	Safeguards Policy Statement

NOTES

- (i) The fiscal year (FY) of CT Environmental Group Limited ends on 31 December. “FY” before a calendar year denotes the year in which the fiscal year ends, e.g., FY2019 ends on 31 December 2019.
- (ii) In this report, “\$” refers to United States dollars, unless otherwise stated.

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BASIC DATA
Small and Medium-Sized Enterprise Industrial Wastewater and Sludge Treatment Project
(LN3357–People's Republic of China)

Key Project Data	As per ADB Loan Documents (\$ million)	Actual (\$ million)
Total Project Cost	400.0	60.3
Equity size	150.0	24.9
ADB Investment:		
A Loan:		
Committed	100.0	50.0
Disbursed		35.4
Outstanding		0
B Loan:		
Committed	150.0	
Disbursed		
Outstanding		

Note: The actual figure is based on the exchange rate prevalent at appraisal in the report and recommendation of the President (\$1.00 = CNY6.5).

Key Dates	Expected	Actual
Concept Clearance Approval	April 2015	13 April 2015
Board Approval	September 2015	10 December 2015
Financial Agreements (date of signing of the Loan Agreement)	by Q2 2016	22 March 2016
First Disbursement	by Q2 2016	21 June 2017
Commercial Operations Date	by 2019	30 June 2017
Final Repayment	22 March 2026	8 January 2019

Financial and Economic Internal Rates of Return (%)	Appraisal	XARR
Financial Internal Rate of Return	8.3%	...
Economic Internal Rate of Return	27.6%	27.9%

Project Administration and Monitoring	Dates
Due Diligence/Fact-Finding/Appraisal	15 March, 8 June, 18 September, 30 November, 11 December 2015
Project Administration	23 February, 21 March, 14 April 2016
	27 July 2017
Extended Annual Review Report Mission	10 April, 19 September 2018
Others	18 October, 30 October, 27 November 2018

EXECUTIVE SUMMARY

On 10 December 2016, the Asian Development Bank (ADB) approved a 10-year dual currency loan facility of up to \$250 million (A loan of \$100 million or yuan equivalent, and a complementary loan of \$150 million or yuan equivalent) to CT Environmental Group Limited (CTEG) for the small and medium-sized enterprise (SME) Industrial Wastewater and Sludge Treatment Project in the People's Republic of China (PRC). The project aimed to develop industrial wastewater and sludge treatment capacities for SMEs.

In the PRC, SMEs are key drivers of income and employment growth; however, most SMEs lack sufficient capacities to treat wastewater and tend to dump untreated wastewater into waterways or sewers. ADB assistance was intended to support CTEG to build, own, and operate a series of specialized SME industrial wastewater and sludge treatment plants. On 21 June 2017, \$35.4 million was disbursed under the \$50 million A loan (initial) facility signed on 22 March 2016. The rest of the approved loan facilities were never disbursed after ADB's memo seeking cancellation of undrawn commitment and uncommitted loan facilities in October 2018.

While the loan facility was originally rated NSO7 at the time of approval, there were multiple breaches of financial and information covenants since the end of 2017. As a result, the risk ratings were downgraded, and in September 2018, because of increasing concerns about corporate liquidity and integrity, the Office of Risk Management deemed the ADB loan impaired and booked 50% provision on the balance outstanding. ADB then pursued CTEG for a full prepayment, which was achieved on 8 January 2019.

Overall rating of the project is *unsuccessful*, based on the evaluation of the following dimensions.

The development results are rated *unsatisfactory* overall. The contribution to private sector development and ADB strategic development objectives is *less than satisfactory*. The projects combined several features that were innovative in PRC infrastructure finance and were structured as a multi-project loan facility, in effect bundling SME subprojects to avoid the high transaction costs associated with stand-alone project financing and to diversify risk. As of ADB project approval and loan disbursement, CTEG had established corporate governance mechanism and a strong management team, but CTEG's corporate governance deteriorated and malfunctioned with undue influence by the chairperson, which led to multiple operational, financial, and integrity issues. CTEG failed to effectively implement ADB's environment, social, health and safety requirements and was accused of violating local environment regulations by alleged illegal dumping. The subsequent full exit by ADB underlined the risks of private sector development in the sector and the project did not achieve the expected catalytic effects to encourage local and foreign financing.

The recalculated economic internal rate of return (EIRR) is 27.9%, almost matching the estimated EIRR of 27.6% at the report and recommendation of the President (RRP) stage. However, the project functioned at a reduced scale after ADB's draw stop compared with what was originally planned at the RRP stage. Because the recalculated EIRR exceeds the reference social discount rate of 12.0% followed during the RRP stage, the economic performance of the project is *satisfactory*.

The environment, social, health, and safety performance of the project is rated *unsatisfactory*, because CTEG failed to meet safeguards and social provisions in the facility agreement to comply with applicable laws for all its subprojects.

The project's business success is rated *unsatisfactory* considering the credit, business, and integrity concerns. The financial internal rate of return (FIRR), estimated as 8.3% in the RRP, is not computed for assessment of business success in the extended annual review report because of the absence of sufficient information sources to make a proper projection as well as the lack and unreliability of historical financial data.

The ADB additionality to this project is rated *unsatisfactory* because the funding structure was not successful in catalyzing other lending. The arrangement of the complementary loans was canceled.

Investment profitability is *less than satisfactory* considering the prepayment and the low utilization rate of the approved facility after ADB's draw stop, although there is no actual loss incurred despite borrower's financial difficulty.

ADB's work quality is rated *satisfactory*, based on a satisfactory evaluation for screening, appraisal, structuring, monitoring, and supervision of the project.

Key lessons and recommendations are:

- (i) **Corporate governance and key person risk.** Thorough assessment of such risks should be vital throughout the loan life cycle.
- (ii) **Identifying early warning signals and taking immediate actions.** Collecting market intelligence from various channels and taking immediate actions are important to identify early warning signals and resolve underlying issues.
- (iii) **Security structure critical at exit.** While equity pledges are often regarded as not adding much security value, the ADB security structure facilitated ADB's full loan recovery.
- (iv) **Cross departmental collaboration.** The full loan recovery was achieved through establishment of a cross departmental team and its collaborative efforts.

Because ADB no longer has any exposure with CTEG, no further follow-up actions are required.