Expanding Water Supply and Sanitation Coverage through Output-Based Aid

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• Output-based aid is a scheme that uses performance-based grants to support delivery of basic services to traditionally marginalized poor households.

• Such schemes have generally targeted rural villages but, on occasion, large cities. For its first use of OBA, ADB will test the scheme in small towns in Nepal.

The Asian Development Bank is set to undertake its first output-based aid (OBA) initiative. Will it prove to be the right modality for Nepal’s small towns and their water supply and sanitation concerns?

Background

Roughly 69% of Nepal’s total population still has no access to improved sanitation, with more than half practicing open defecation. A much lesser 12% have no access to safe drinking water but this figure is misleading—a closer look reveals that water availability is intermittent in many areas, half of the gravity flow systems in the hills need major repairs, and more than half of the tube wells are contaminated.

This general condition is echoed in Nepal’s 265 small towns. In 2000, the government formulated a 15-year development plan to address the water supply and sanitation needs of small towns. In the 8 years that followed, though, only 32 towns experienced major improvements in services. Twenty-nine out of the 32 towns were covered by the ADB-assisted Small Towns Water Supply and Sanitation Sector Project, completed in November 2008. This project had a productive run—it introduced water users to the principle of cost sharing, reduced the occurrence of waterborne diseases, fostered community involvement, and more. However, it also had shortcomings. For example, high connection fees prevented the poor from connecting to the water supply system, and tying subsidies to inputs, not outputs, meant that some of the latrines and water connections set up were not always sound from a technical point of view.

In 2009, ADB approved the Second Small Towns Water Supply and Sanitation Sector Project to provide improved water supply and sanitation services to roughly 240,000 people in 20 small towns. To address some weaknesses of the first project, ADB aims to introduce the OBA approach to a small segment of the target group.

The OBA approach is not new. But the targeting of small urban towns, coupled with the fact that it is ADB’s and Nepal’s first foray into OBA, makes this initiative a potentially rich source of lessons for future projects.

Approach

OBA in a Nutshell. OBA uses performance-based grants to support delivery of basic services to poor households that have traditionally been left out or provided with poor quality service. The aid bridges the gap between the total cost of providing a service to a user and the user’s ability to pay the cost. Unlike traditional subsidies, however, aid is given only after successful completion and inspection of the service (output). In the meantime, a service provider pre-finances the cost of installing the service, with counterpart from the poor households targeted.

Key Players. The OBA scheme being piloted by the Second Small Towns Water Supply and Sanitation Sector Project will have two major outputs—house or yard connections to piped water supply and private latrines.

The project management office in Nepal’s Department of Water Supply and Sewerage will manage the scheme in partnership with the towns’ water users and sanitation committees. The committees will pre-finance the construction of facilities and will only receive OBA upon successful validation of outputs. Local nongovernment organizations (NGOs) will serve as independent verification agents.

Applying the Scheme. The first challenge is to ensure that the poor receive aid. The project is currently surveying households with monthly incomes ranging from 3,000–4,500 Nepalese

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2 Ibid.
3 Small towns are defined as having a population of 5,000–40,000 inhabitants, located on a road linked to the strategic road network, and having at least one secondary school, a health post, grid electricity, basic telecommunications, and banking.
rupees (NRs) to find out who does not have proper water and sanitation facilities. Once the target households have been identified, the water users and sanitation committee will engage with them until an agreement on financing, benefits, and obligations is reached. An initial commitment fee of NRs500 will be required from households.

The construction phase will begin with a local NGO acting as independent verification agent, photo-documenting the conditions of the proposed sites prior to any construction. For installing water connections, the water users and sanitation committee will tap the services of a civil works contractor. For latrines, the committee will provide a voucher to households, who will procure construction materials.

Once the facilities are completed and their functionality has been validated by the NGO, the Department of Water Supply and Sewerage will release 80% of the aid to the committee. The NGO will revisit the sites 6 months later to ensure that the facilities remain in working order. If so, the department will release the remaining 20% to the committee. If work is unsatisfactory, the committee will not be reimbursed. This would provide strong incentives to the committees to closely supervise the work and ensure that facilities work as planned.

**Getting the Numbers Right.** OBA schemes must ensure that the poor receiving aid can pay for services on a long-term basis and that their payments, combined with the payments of the nonpoor, can support the financial and technical sustainability of the services.

For this project, a thorough review of alternative financing schemes point to the following as the most feasible subsidies:

- The poor will receive up to 75% of water connection costs as OBA. The monthly water service charge to poor households will be about NRs220.
- The OBA for latrines will increase to NRs10,000 for the substructure and superstructure, covering about 75% of substructure cost. The balance will be shouldered by households.

**Pilot Towns.** The approach, to be initially piloted in 12 small towns, is based on an OBA study undertaken for two towns, Phidim and Duhabi.

Phidim comprises 1,556 households. While 87% of its population is already connected to the water supply system, water is not available at all times and water quality does not meet World Health Organization standards.

Duhabi is a growing industrial town encompassing 5,415 households. Only 16% of them have piped water in their house; the rest rely on community taps or tube wells. Half of the population practices open defecation.

**Challenges Ahead**

It is too early to say if the OBA approach will work for this project.

The government’s transition to a federal structure and the political uncertainty that comes with the change, coupled with complex peace processes, can potentially derail the project’s progress at the macro level.

At the town level, the project must contend with the households’ readiness to abandon traditional practices, i.e., open defecation, willingness to pay for piped water and sanitation services, the proposed financing scheme’s ability to sustain the water and sanitation services, and more.

The OBA component is a small portion of the Second Small Towns Water Supply and Sanitation Sector Project, accounting for only $1.3 million of the project’s $71.7 million total cost. Still, its success will potentially strengthen the design of ADB’s future water supply and sanitation projects.