

Privatization of Water in the Developing World

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Why I am Interested in this Issue?

- Thorny, complicated
- Major issue for our world
- Classic NW issues: sustainability, provision of service, pricing, conservation, good government
- Experience with ppp's in Seattle
- UW has integrated programs: environment, water, public administration, international development

Water Facts

- Water borne diseases kill: one child every 8 seconds; 12 million people a year
- Two-fifths of the world's people have serious shortages (more than 1 billion people)
- People in rich countries use 10 times more water than poor
- World water supply can't be increased – just managed better (while population increases)

UN Goals (by 2015)

- Reduce by half the people without access to safe water
- Extend water to 83% of population (currently 66%)
- Economic benefit of reaching that goal est. \$300-400 million annually
- Estimated cost of investment - \$110-180 billion

It's all About Money!

- Turnover in the global water market \$100 bn annually.
- Massive investment needed to modernize and adapt infrastructure in the USA (c. \$240 bn. over 20 years) and the EU (EUR 100-150 bn over 5-10 years).
- Big investment requirements in the safer markets of the USA and EU would compete strongly with the needs of developing countries.

My Premises

- This is a critical issue that needs to be addressed
- “Privatization” has become a term that creates conflict
- PPP’s are a form of privatization that can add value in the developing world with cash infusions, knowledge, skills, training, management
- Key: creating a balanced partnership with government so that government retains ownership and control; Government needs to step up to become a quality partner

Making money from water?

- The cash flow from typical water project describes a J-curve,
 - starting with heavy negative flows with initial investment, then
 - stabilizing at positive levels, which continue for the life of the project, usually long.
- Long term funding is in short supply.
- Increasing private sector financing depends on mitigating risks and increasing the returns.

'Privatization' Matrix

	O&M ¹	Leasing	BOT ²	Concession	Asset Sale ³
Ownership	public	public	public	public	private
Investments	public	public	private	private	private
Operations	private	private	private	private	private
Billing	public/private	private	public	private	private
Remuneration	Fee	Tariff	Fee	Tariff	Tariff
Contract length	5 y	10-15 y	10-30 y	20-30 y	∞
Example	Atlanta Suez	Senegal Bouygues	Sydney Vivendi	Berlin Vivendi/RWE	London RWE

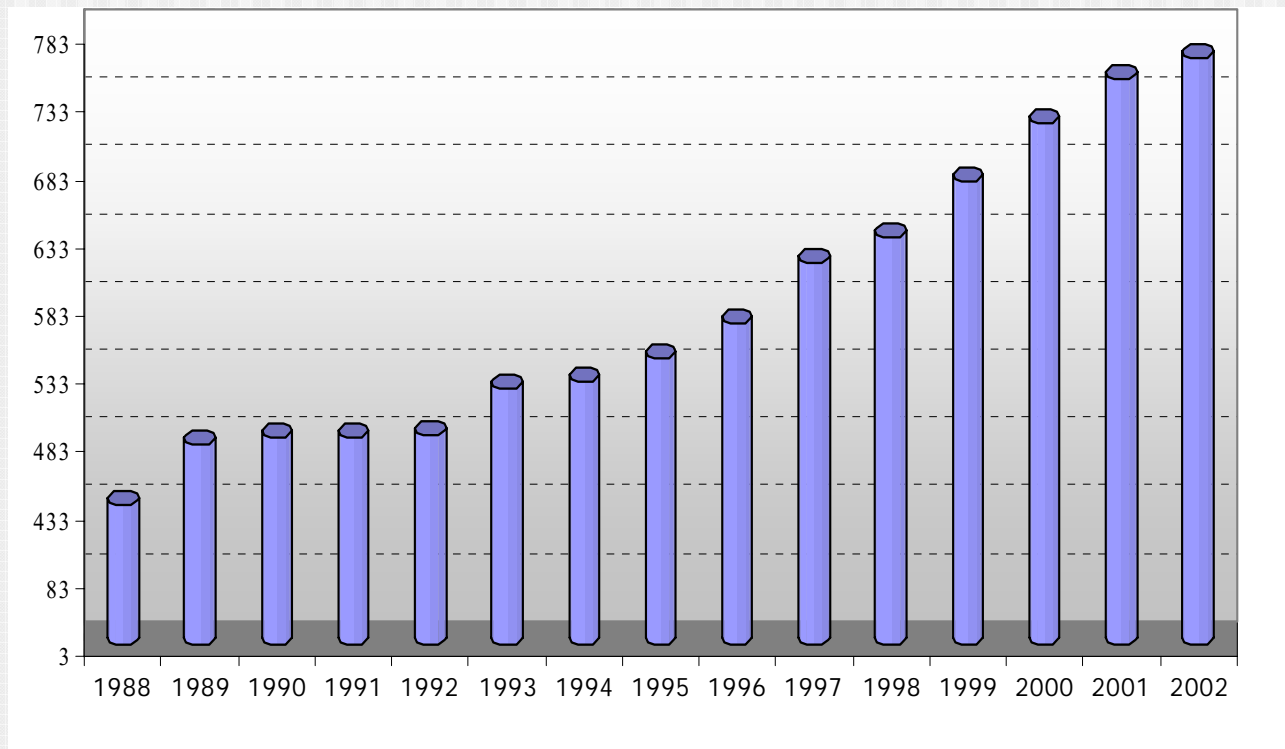
- 1 O&M Operations & Maintenance
- 2 BOT Build-operate-transfer
- 3 Asset sale = regulated business

In 1989 the UK water sector was privatised through an asset sale. The regulatory framework proved to be inadequate and the results of that privatisation were unsatisfactory (underinvestment).

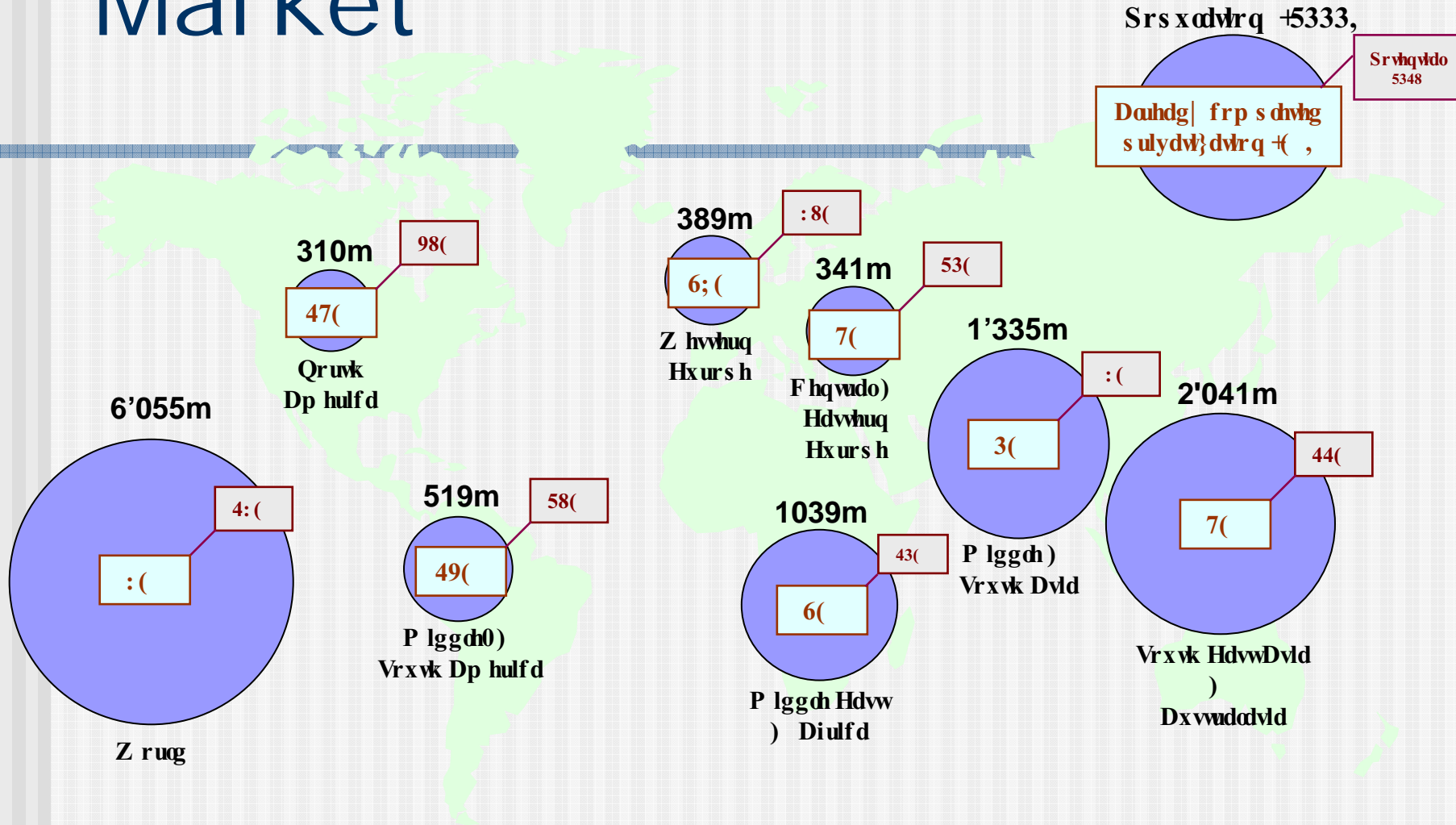
The O&M, BOT model developed in France is highly successful all over the world. This model focuses on the service business (no asset sale) and is promoted by companies like Vivendi Environnement and Suez.

Private Sector Delivery: 1 in 14

- Number of individuals using water of PPP (in millions)



Global Water Service Market



A 260bn market growing at 6% per annum

#1: Water Provision Is a Basic Responsibility of Government

- Governments have a fundamental duty to see that basic services, such as water, sewerage, and energy, are provided to their people.
- International lending agencies and development organizations:
 - once helped governments to provide these services.
 - Now they push privatization as a new solution.

Response

- Governments must own and control water on behalf of their citizens
- Governments can exercise control through the contracting process; they may be helped with developing good contracting procedures
- International organizations pushed privatization because of the lack of capital in the developing world

#2: Privatization May Bypass Under-represented and Under-served Communities

- Poor peri-urban populations are under-served.
 - Lack political clout.
 - May be illegal.
 - Unable to pay as much for water as residents in wealthier areas.
- Privatization can potentially worsen this neglect.

Response

- Currently poor people pay up to 10 times more than rich because they have to buy their water or bring it from distant sources
- PPP's tend to be used in urban areas; local private companies can be used in the more rural areas
- Contracts can require that services be extended to more rural areas (especially with stand-pipes and common wells)
- The poor tend to pay their water bills reliably

#3: Privatization will Worsen Economic Inequities and Affordability

- Privatization will lead to *higher* costs for water and water services.
- *Lack* of water subsidies can have disastrous results, especially when combined with pressures to recover costs.

Response

Contracts can create regulatory mechanisms to:

- Protect the public interest from excessive charges
- Ensure that water service providers recover the full cost of providing the service (limit profit)
- Ensure service levels promised are delivered
- Provide subsidies and cross subsidies as needed (use ascending block rates)

Costs will go up; water is not free; poor will pay less; middle and upper incomes groups will pay more

#4: Protection of Public Ownership of Water and Water Rights

- Loss of local ownership of water systems can lead to neglect of the public interest.
- There has been neglect of these issues by some who promote privatization.

Response

- PPP's can be structured so that the local government continues to own the assets.
- Government should retain a strong oversight or regulatory role
- Contracts should include performance standards that are audited and maintained

#5: Agreements Often Fail to Include Public Participation and Contract Monitoring Oversight

- Monitoring of public-private agreements are key public responsibilities.
- Weaknesses in monitoring progress can lead to ineffective service provision, discriminatory behavior, or violations of water-quality protections.

Response

- PPP contracts do need to be monitored
- Countries may need training in how to regulate and monitor; this is a role that International Organizations could undertake to train personnel and finance the training and oversight.

#6. Impacts on Ecosystems or Downstream Water Users

- Many privatization contracts include provisions to encourage the development of new water supplies,
- If privatization contracts do not also guarantee ecosystem water requirements, development of new supply options will undermine ecosystem health and well-being (for both public and private developments).

Response

- Effective water law and regulatory mechanisms are necessary to provide an investment friendly environment
- Investing PPP's must respect and honor those laws
- Governments should define and enforce water quality laws

#7: Neglect Potential for Water Use Efficiency & Conservation Improvements

- Efficiency programs can be ignored or even cancelled after authority for managing public systems is turned over to private entities.
 - Improvements in efficiency reduce water sales, and may lower revenues reducing the financial incentive to encourage conservation.
- Conservation is often less capital intensive and therefore creates fewer opportunities for investors.

Response

- Conservation and efficiency programs are planning functions that can and should be retained by the local government.
- Contracts can be written with incentives to increase efficiency or to require increased levels of conservation

#8: Privatization will Lessen Protection of Water Quality

- Private suppliers of water have few economic incentives to address long-term health problems associated with low levels of some pollutants.
- Private water suppliers have an incentive to understate or misrepresent to customers the size and potential impacts of problems that do occur.

Response

- Water Quality protection is a national regulatory responsibility. Countries need good water law.
- Use of PPP's requires a strong regulatory climate.

#9: Privatization & Dispute-resolution Procedures

- Public water companies are usually subject to political dispute-resolution processes involving local stakeholders.
- Privatized water systems are subject to legal processes that involve non-local stakeholders.
- Increased potential for political conflicts over privatization agreements.

Response

- Contracts should include dispute resolution clauses
- All stakeholders should have access to dispute resolution procedures
- Accurate assessments should be made of the quality of the facilities and of the desired level of improvement in the performance as part of the contract negotiations. Contractors should not be encouraged to “low ball bid”

#10: Privatization May Be Irreversible

- Transfer of control over water system to private companies may result in the loss of internal skills and expertise.
 - May be irreversible, or nearly so.
 - Many contracts are long term - for as much as 10 to 20 years.
- Management expertise, engineering knowledge, and other assets in the public domain may be lost for good.

Response

- Contracts should be written so that every 8-10 years they are reviewed and possibly rebid.
- Requirements can be made to hire local employees
- Local companies can be developed in rural areas to learn all the skills, requirements of running a system
- International partnerships can be made to train and develop local talent.

Other Issues

- Privatizers:
 - Nationalization
 - Devaluation of currency
 - Local economic problems
 - Change in political objectives
- Local Communities
 - Impact on graft and corruption
 - Maintaining a “minimum safety net standard”
 - How much profit should a PPP make?

Peter Gleick's* Principles

- Meet basic human needs
- Meet ecosystem needs
- Provide subsidies to overcome poverty
- Set water rates at reasonable levels
- Link rate increases to agreed upon increases in services
- Use subsidies only when sound
- Require that a new project is less expensive than a project that would increase efficiency

*President, Pacific Institute

Gleick (cont) – Contracting Principles

Standards for Government regulation and control should include the following:

- Public ownership and control of the water sources
- Public monitoring of water quality
- High quality contracts
- Clear dispute resolution mechanisms
- Independent third party technical review of contract proposals
- Transparency and openness during negotiation

My Tentative Conclusions

- PPP's are a tool that can bring needed capital and know-how into developing areas
- PPP's must be aligned with strong government agencies that can regulate and oversee the contracts and the projects
- More international energy needs to be put into developing the governmental skills to make this a "balanced challenge"
- Calling PPP's "privatization" and bad mouthing them is not useful

Conclusions (cont.)

- Water is going to cost money; we all need to face up to the cost of providing a basic human service
- Subsidies can be designed to give the poor a minimum service level; the wealthy will be paying more
- PPP's need to limit expectations of ROI to around 6%
- PPP's need to work with International NGO's to bring partnerships to the table to bring training, skill development into the countries they work with