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**INFORMAL DAC - PRIVATE SECTOR MEETING: STRENGTHENING PUBLIC-PRIVATE
PARTNERSHIPS IN THE WATER AND SANITATION SECTORS IN DEVELOPING COUNTRIES**

26 February 2003

DISCUSSION SUMMARY

The attached note provides a summary of the informal DAC - Private Sector discussion. It is provided as BACKGROUND for the POVNET programme of work discussion in respect of the infrastructure theme [see DCD/DAC/POVNET(2003)1, section IIIc].

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INFORMAL DAC – PRIVATE SECTOR MEETING: STRENGTHENING PUBLIC-PRIVATE PARTNERSHIPS IN THE WATER AND SANITATION SECTORS IN DEVELOPING COUNTRIES

I. Background.

1. DAC Members held an informal meeting on 26 February 2003 with representatives of the private sector on the issue of strengthening public-private partnerships (PPPs) in the water and sanitation sector in developing countries. The objective of the meeting was to scope the obstacles to more and better PPPs in this area and identify some directions for tackling them, in preparation for the Third World Water Forum in Kyoto, March 2003.

2. Presently, over one billion people lack access to safe drinking water and 2.5 billion people have inadequate sanitation facilities. It has been estimated that meeting the Millennium Development Goal (MDG) of halving, by 2015, the proportion of people that do not have access to safe drinking water and sanitation will require a major increase in current annual financing flows devoted to water and sanitation from all sources – public and private, domestic and external. Put another way, meeting this MDG means that 290 000 people would have to gain access to clean water and 500 000 to sanitation every day of every week until end 2014. It will also require a turn around in recent financing trends. Foreign direct investment and bank lending to the sector is down; more, and more effective ODA is needed, and domestic public investment in both large and small scale systems needs to be increased.

3. Delivering sustainable water and sanitation to meet poor peoples' needs is a major issue on the international development agenda. Water and sanitation occupied a prominent position at the Johannesburg Summit. It gave particular emphasis to the need to facilitate PPPs – developing countries, donors, the private sector and civil society need to work better together to significantly improve provision and management of water and sanitation infrastructures. These issues were pursued at the Kyoto Third World Water Forum in March 2003, with the aims of stimulating global awareness of water problems and generating concrete actions to address them.

4. Some of the key, and sobering, messages coming from the discussion are summarised below, with more information provided in section III of this summary:

- *Connecting up:* Meeting the water and sanitation MDGs represents a major challenge in connecting up people, particularly the poor, to water and sanitation. But there is also a major challenge in respect of better connecting up the various stakeholders involved in PPPs in this sector – developing country governments (national and municipal levels), bilateral and multilateral donors, the private sector (foreign and local suppliers) and civil society.
- *Financing:* Major increases are needed from all sources (public and private, domestic and foreign) and better financial instruments and tools are required, and this at a time when financing from all sources has been declining.
- *Governance and regulatory difficulties:* These are viewed by many as a critical dimension of the problem and particularly inhibiting to improved private sector involvement. These difficulties

underpin the fact that private sector involvement in water and sanitation is severely limited by the lack of viable projects.

- *Modest expectations/long term perspectives:* Presently, only about 5% of global water provision is via the private sector and only 0.3% of commercial bank financing goes to the water sector. So, there are quite generic issues to address in promoting PPPs in water and sanitation, in addition to those particular to developing countries. In the latter, “ideology” and “mantras” need to be addressed, non-issues identified and set aside, trust needs to be built and governments and donors need to work out how much they are able/prepared to take on difficult issues in areas such as water pricing, corruption and governance frameworks.

II. Opening remarks by Michel Camdessus (World Panel on Financing Water Infrastructure)

5. A large section of humanity, and particularly the poor in developing countries, suffers from severe water stress. If we are to meet the MDGs, and if PPPs are to realise their potential contribution, we need to address important and difficult financing and governance challenges. The following key messages were given:

- The water and sanitation MDGs can be met, but this will require significant changes in our approaches to financing, providing and managing water and sanitation, and the pace of actions must be significantly geared up.
- The main problem is a “system” one. All stakeholders need to be engaged in funding the additional requirements. We need multidimensional action involving all actors, not just developing country central governments and donors.
- We need to double the financing effort – from its present level of \$80 billion per annum. This is less frightening than at first glance, but it does need additional efforts from all financing sources, more and better adapted financial instruments and a key role for water pricing schemes.
- PPPs in the water and sanitation sector are presently not doing well. The recent trend is one of withdrawal, from all sources. Major preconditions if this trend is to be bucked include improvement in the governance of the water sector, dealing with perceptions (sometimes misperceptions) about the role of the private sector, and reminding ourselves that while water is a public and free good, pipes and sanitation and maintenance are not, and it is the poorest who presently pay the highest price for water.

III. Main discussion themes

a) *Financing*

6. While more ODA is required, even more efforts are needed to mobilise international and, in particular, domestic financing. Particular attention should be devoted to sustainable cost recovery through tariffs as the provision of water and sanitation services is an economic good and should therefore be priced. In addition, more attention needs to be devoted to the use of guarantees and risk mitigation instruments (e.g. in respect of exchange and tariff risk), debt swaps and better mixes of public and private finance.

7. In fact, a number of shifts in the balance of financing are required -- from public to private, from taxes to charges and from central to municipal finance. In particular, private sector providers see sustainable cost recovery through charges as central to the long term financing and sustainability of water and sanitation provision.

8. The private sector also mentioned a number of other issues that require attention – difficulties in blending ODA loans with private finance, local currency issues, and export credit rules where local content ceilings limit greater recourse to local involvement. In addition, long term ODA financing commitments are needed in light of the long term nature of many projects but, as one donor mentioned, “aid runs in five year flavours”.

b) Governance

9. The private sector is very sensitive to poor governance. For some participants, governance issues were clearly more critical than financing ones for improving the access to water and sanitation. Good governance is therefore central to enhancing private sector involvement. Issues were raised concerning the areas of procurement, corruption and contract enforcement.

10. A major set of issues lie with the legal and regulatory framework. Private sector providers feel they often have to bear the cost of weak or non-functioning frameworks, and approaches need to be developed that better allocate risk in relation to who is best placed to manage it (e.g. commercial risk/private sector; currency and political risk/public sector and donors). Otherwise, the private sector perspective of limited profitability but unlimited loss potential will persist and hinder further involvement.

c) PPP issues

11. The major challenges in increasing and improving PPPs are related to governance and business issues rather than technical ones. Private sector participants expressed the need to better “legitimise” PPPs, by getting rid of dogmas and taboos through a better dialogue among stakeholders to build mutual trust and to better assign roles and responsibilities.

12. The focus should be on the real issue of how to improve water and sanitation *provision*, and not on an ideological and emotional debate about *ownership*. It is therefore important to distinguish between ownership of the *resource* and provision of the *service*. There are many different forms of PPPs and private sector involvement (privatisation, management contracts, concessions, leasing, BOTs, BOOs, etc.) and the effort should be on identifying the approach best suited to the specific need at hand.

d) Institutional capacity building

13. Increasing the number and quality of PPPs requires major capacity building efforts. These include attention to financial and project preparation (especially at municipal levels) and to contract negotiation skills, so that developing countries are equal partners in negotiations, and to supply side capacity building for local partners and providers. Too often, projects are launched before the required capacities are in place.

14. Many of the problems in improving access to water and sanitation can be traced to the fact that developing governments themselves often don't attached a higher priority to water. Water and sanitation are not always seen as key elements of national development and poverty reduction strategies and there is often no corresponding national water strategy linked to the broader development strategy.