



An Interdisciplinary Research Project

FIRST RESEARCH WORKSHOP

The Economics of Private Sector Participation in Water and Sanitation

Paper:

“Public Private Community Partnerships for the Poor”

Richard Franceys
Institute of Water and Environment
Cranfield University

**School of Geography and the Environment
University of Oxford
January 16, 2002**

PRINWASS is supported by the European Commission under the Fifth Framework Programme 1998-2002 and contributes to the implementation of the Horizontal Programme “Confirming the International Role of Community Research”. The views and information in this document are the sole responsibility of the research consortium in charge of the project and do not represent the opinion of the European Commission. The Commission is not responsible for any use that might be made of data or other information appearing therein.

Contract: PL ICA4-2001-10041

Richard Franceys specializes in management and institutional development for the water supply and sanitation sector. Among other research and consultancy work he has carried out studies on public-private partnerships in Cyprus and Ghana, on contracting - out of water and sanitation services in India, Uganda and Mexico, on private sector participation in Sri Lanka and India, on institutional and management development for the National Water and Sewerage Corporation in Uganda, and offered a management development program for senior public health officials in India. He has collaborated, among other organizations, with UNICEF, WWF, UNEP, DFID, and has written several books on water supply, sanitation and urban services for the poor. He is currently a member of the Central Customer Services Committee of OFWAT, the UK water regulator, and Team Leader of an Asian Development Bank study on Public Private Community Partnerships to serve the Poor.

For enquiries on this paper, contact Richard Franceys:

r.w.a.franceys@cranfield.ac.uk

Water and sanitation is vital for public health. The statistics are that every eight seconds a child dies because of poor water and sanitation. Cholera outbreaks are still happening in the world at the moment. In Nigeria, 700 deaths from cholera have been reported in the last few months in the north of the country, so these things are still very important. Other presentations have also showed variations on the same statistics, which remind us that the poor people are not getting clean water and sanitation are suffering with poor health and they are the poor. If we are to do anything, we have to do something about that. The most recent statistics from the WHO/UNICEF reports that Africa needs 62% coverage to improve supplies, 36% of water supplies are contaminated, the population is growing very fast, and an average of 26% are living in informal settlements. The real challenge is not so much the public and the private debate, but how the needs of the informal housing settlements, the slums, the shanties, the poor living on less than a dollar a day can be met. I have been working for the Asian Development Bank (ADB) and some of these slides will focus upon Asia. This is urban Asia. They appear to be not doing too badly. The blue line for urban water supply is not too far apart, sanitation is a lot lower down, we know that sanitation is often more important to health than clean water, but 255 million in urban areas lack adequate sanitation at present and of course the population is still growing, so it is still a challenge. 80% of the global population is without access to improved sanitation, and two thirds without access to improved water

supply live in Asia, so most of the work will be in Asia etc. Officially 18% are living in informal housing areas, but this is up to 60% in some cities. What can we do about this? Even the ones that appear to be served may have a deficient service, as more than half the urban water supplies in Asia operate intermittently. Intermittent supplies mean that there is no pressure in the mains, reduced pressure can suck in dirty water, and so the systems get contaminated. The whole purpose of governments being involved in the social aspect of getting clean water to people, is to achieve good health. Intermittent supplies are destroying that. A supply for two hours every other day is very common in India, with a population of just over one billion people, of which 300,000,000 people live in urban areas. All the Indian water engineers who I talk to ensure that their wives boil the water before they use it. The sort of system that India has is one in which 20% is not disinfected and 21% of the samples are contaminated. The apparent good news is that India also has the lowest tariffs in the world at 22 cents per cubic metre, compared to the average world price of about one dollar per cubic metre, 14cents per cubic metre for sewerage which we all know is laughably small; at the end of the day it means that services are highly inadequate. With a median tariff per unit production cost ratio 0.7, it is simply not viable. The people are not getting the services, particularly the poor. Of course, it is the rich who are connected, not the poor. Asia needs reform. How can improvements be made in Asian cities with an average poor population of between 10% and 50%?. In addition, there are many these different characteristics of poverty: material lack, that is those on less than a dollar a day, but also insecurity, vulnerability, poor social relations, low self-confidence and powerlessness. We cannot just deliver services to the poor and expect them to meet the social and health needs, it must be about also being involved in participatory development and empowerment of the poor, other wise we will fail, no matter how much pipes are extended. Looking back over a number of years, say 20 years ago, the World Bank said that 70 % of the benefits by vale go to the non-poor. This is what governments have been putting all this money and resources and subsidies into, to subsidise the rich, not the poor, who do not get their connections. Efforts to bring safer water to the poor are hampered by deficient financial practices, which continues to this day. Ten years ago the ADB said that institutional reforms should be undertaken. NGOs must be involved, and individuals and communities should be actively involved in planning and management. This is nothing

new and yet these problems are still with us. Such that at the end of this global assessment WHO/UNICEF said something will have to change dramatically. I could argue that what is changing dramatically is this argument about public-private partnerships (PPPs). Information from my database of about 800 different contracts around the world shows what has been happening over this last decade. Reform has been taking place at one level, but is it also reform which benefits the poor, because otherwise there would be no point. Let the rich carry on with their already fairly effective coping strategies. We saw the PPP models earlier this morning, this table was prepared by my colleagues in Delft. One of the things I would point out is the different types of user management, but also the small scale independent providers who do so much of the work at the moment. The private sector has been serving the poor for a very long time because the public sector has failed, and the poor are using private sector vendors who all serve independent providers. They are all there already. It is not a case of one or the other, but it is going to continue with public and private in various forms. My Dutch colleagues like the public water plc - government owned but running like a private water company. In Great Britain, the Scottish system is much closer to that. The French approach that is being copied around the world is in the middle of the PPP spectrum. If we go into more detail, breaking all these down into different levels of service contracts but also community contracting and NGO contracting, there is a vast spectrum of private sector involvement.

Just to mention these two ideas of participation, when I became interested in this subject we were talking only about private sector participation and now it is private public partnerships. I think we use these terms interchangeably. Participation on the Arnstein ladder of participation; information, consultation etc. partnerships does suggest the act of deciding together and acting together. Back to imparting power to the poor, we need genuine partnerships where there is deciding together and acting together, and not just token participation. We want genuine public private partnerships to empower the poor. There is therefore a large number of stakeholders, and not just a Vivendi and a government to think about. The poor, who we find are generally willing to pay reasonable tariffs for water supply, but not for sewerage and not for these exalted connection fees which we like to use as barriers to entry. Community based

organisations are excellent, they initiate new projects before coming together, but find it difficult to sustain them. NGOs act as facilitators and enablers, as do the whole range of private agencies I've mentioned already, and not just the Ondeos and Thames's. We do need to recognise that we need the public sector in the partnership, as legislative assemblies have to be there with pro-poor legislation which will form the basis of a primary duty of the regulator, to serve the poor. We must also recognise civil society and the knowledge community which all have their part to play. I recommend that we cannot just think about institutional factors, we have the others as well; social, health, technical, economic, financial and environmental, for which I use the acronym SHTEFIE). So, if we are just talking today about institutional forms these other things are part of the equation to get service to the poor.

We have had public private partnerships for a long time as very few public sector organisations build water works themselves, certain states in India do, but they are the exception. So we have long had public private partnerships. To my way of thinking, this has got us so far in terms of service coverage and service quality and that tends to be meeting the needs of high income and middle income people before hitting this performance ceiling. Sadly, around the world, public sector direct providers seem to keep on hitting this performance ceiling. There are exceptions, but I think they tend to be the exceptions. Because of that void, we get the small-scale independent providers - the NGOs and the CBOs meeting the needs of the poor in a rather erratic way. My red line at the top represents them. The good news from a particular study that I am just finishing for ADB is the discrete disaggregated services - the CBOs, SSIPs - are meeting the needs of the poor. Unfortunately they tend to be rather too expensive in terms of resources and finance. The problems are how to scale those up and ensure long-term sustainability. Community management works wonderfully to get things built, but people find it hard to keep it going. The poor especially have better things to do with their lives than running their own water system.

The question is how to get through this ceiling, how to reform the public private partnerships. From my worldwide experience, I think that the PPPs take us to the next level through this reform and get us this blue line in terms of better service – but are not yet there, the typical 'S' curve of provision. It also means that the poorest are still being

left out, whose needs are being met by the NGOs and CBOs, but with the related problems of sustainability. I have interesting examples for all of these from different countries. The case studies from Asia will be on the ADB's website in about a month's time if anybody wants to see them. We added into it the example of Kampala, where, interestingly, a new PPP has failed. PPPs do not always work, and we accept all the criticisms and the points that have been brought up in previous presentations. PPPs have weaknesses and are not a panacea that solves everything. The financial indicators show from the start of this Kampala Revenue Improvement Project has actually gone down in terms of return of fixed assets and their days receivable ratio has got worse as a result, and the poor are still being served by NGOs and vendors. It does not work everywhere. But we do want to have a universal service obligation, and one of the tricks of the PPPs is demanding private operators to try to achieve and 98 or 100% service coverage for universal service obligation, which by default then includes the poor. We want it to achieve a consistent quality of network service which is not achieved through NGOs, with least cost provision, by using economies of scale and the possibilities of cross subsidies, which are very important in this system. The good news is that in the large scale metropolitan citywide services, experienced international private operators with clear goals do seem to be working in some parts of the world. How can we take that further? My graph then finishes off in a way which has absorbed the NGOs into the overall system and we are clearly getting those benefits and it is exciting to see the multinational global operators delivering through participatory development in different regions of the world. Not all of them, because not all of them have learnt the tricks yet. But a good number have. That is good news. So we have a new acronym PPCPP - Public, Private, Community Partnerships for the Poor. In our study for the ADB, we looked at England and Wales, Buenos Aires and Manila, in a way the standard ones, and the real challenge is how we extend these beyond these particular individual cases. In the world of PPPs, a complete mixture of all sorts of things are happening. It would appear that concessions are the most popular type of contracts, constituting 19% of reported new contracts since 1990.

I have another role sitting on an OFWAT customer services committee soon to be renamed "Water Voice", I believe. Quoting Oakes 'vigour, enthusiasm and a drive

for efficiency have replaced a lacklustre performance that was all too common when water was in the public sector'. We see that around the world, it is not just Thames or England, it was everywhere. There have been massive capital investments - speaking as a customer representative - \$58 billion over ten years, which would not have been possible when it was in public hands. Excellent water quality improvements, porpoises in the river Thames and salmon in the River Mersey, what more could we wish for?

We are being serviced by excellent water, and service quality is happening for all due to cross-subsidising rural areas. The rest of the world would like to have that benefit. The ban on disconnections, which only came 9 years after privatisation. Free meters, easy payment facilities, charitable trusts to help those who cannot pay, vulnerable charging schemes - it would be quite interesting to do a study to see how many of these come about as a function of BBC Panorama programmes from 8 or 9 years ago. We also have this customer committee oversight for what that is worth. It is worth remembering that significant efficiencies have resulted from this. We saw some of the numbers this morning. The operating expenditure efficiencies are dramatic and all credit to the water companies for achieving them. It gets the price of water down. This is what we want.

Seven Trent is now boasting a 7% capital efficiency, a result of tighter targets. These constitute real improvements. However, from the customer's point of view, water has been quite different from telecom, gas and electricity. Some argue that that is a function of competition. Although the other utilities have had similar levels of capital expenditure. At the most recent price review, the companies asked who had redlined; increase in prices and got given the lower blue line. So regulation is working in conjunction with privatisation.

My customer services committee meets every two months. We audit complaints, compensation costs by CSCs? are greater than the running costs, and my colleagues suggest that: 'privatisation has been a move forward, a two-edged sword, that costs have risen disproportionately'. Quite a balancing act is going on. In particular, something that I have been looking at is that, if domestic tariffs are actually plotted in real terms, they are significantly higher than the K factor, which is the headline factor

that we all hear about. Particularly unmeasured tariffs when set against the average household income for the East and West Midlands,. There has been a price to pay for all these benefits. There is no price cap in the UK, there is a revenue cap and the tariff basket has had some strange effects which have not always been looked at. So you have to keep watching all these factors all the time.; there is no simple solution. I always understood that we were getting the profit sawtooth in price cap regulation, whereby the benefits were shared. Sawtooth is where you get increased efficiency over the period and then you share it with the customers before price efficiency gains come again. OFWAT gave us the glide path and one could argue that this gave the water companies an extra 4.5 billion pounds in profits. The point is that regulation is a complex sophisticated task can go wrong even with the best will in the world , even to the extent of 4.5 billion pounds. In this case I believe the companies deserved their out performance over the glide path, but the glide path over the cost of capital was a gift to the companies. They spent some of this on global investments.

I want to look at the significance of these. The one billion people without clean water and the 2.5 billion without adequate sanitation. Is it PPP and regulation or is it simply wealth and a stable population? The ‘modern equivalent asset value’ of our fixed assets in this country is now about 5,500 dollars, with continuing investment at the rate of 100 dollars per capita per year. This is an affordable investment level for UK but if you take the standard 5% figure in operating costs in low and lower-middle income countries of the world, 455 dollars per capita per generation for lower-middle income countries, and 155 for low income countries, and these represent the majority of the world’s poor. How can we meet those needs? In places like Dhaka which has a population doubling time of 9.5 years at the moment, wealth and population are the real challenges.

So what direction are the PPPs taking at the moment? The majority of course are investing in Latin America and the Caribbean, because it is the richest of the MLIC regions, and the next richest, East Asia and the Pacific. Sadly, therefore, the money is going to where the wealth is. I previously touched on here I think the capital expenditure is, a total of operational 115 billion dollars over the decade.. Service contracts are a wonderful way perhaps of promoting reform and efficiency. The

contractor of the new plant in Hyderabad wanted to invest to improve, and put in new rubber bearings under the aerators to prolong their life. The private contractor wanted to invest his own money but he was only given a six month contract as in India particularly, and all south Asia, the politicians were very wary of PPPs. If there were no service and management contracts in Asia, all that would be left would be a massive amount of BOTs. BOTs do not serve the poor. Generating extra water to put into the leaky bucket does not help. Using BOTs for waste water treatment, in Asia or now in Mexico, Puerto Vallarta, serving tourist areas does not help the poor either. It might meet the needs of some people selling artefacts on the beach to help the tourists there, but it is not development, it is not getting clean water and sanitation to the poor. So be wary of all the BOT and that type of PPPs. Getting to the heart of the matter; how are PPP serving the poor? This slide is courtesy of Business Partners in Development's first study tour to Buenos Aires . The slide shows one of the slum areas from where the Argentinian footballer Maradona came. In comparison with other parts of the world, one can say that this is not really low-income housing. But this is the local context. Through various means, the Aguas Argentinas, part of Ondeo, part of that partnership, was serving 146,000 poor people through special projects by 1998 and according to their reports an additional 114,000 (?) by 2000. Through participatory development, through using NGOs, working with communities, they are doing the business which governments had been failing to do. A private operator in partnership with NGOs was trying out alternative approaches, adapting technical standards, and breaking government rules – giving pipes to illegal housing areas, which is everything that governments and government engineers always refused to do. There are good reasons for doing it, there are political reasons for being seen to meet the needs of the poor to get other price reviews through the regulator. But it is being done.

The universal cross subsidy has made a difference, as there are reasons for which the rich should pay. They have been enjoying the benefits of clean water for a very long time. In Manila, Ondeo and Manila Water are also trying to adapt technologies. The critical factor is using NGOs for social intermediation and having reduced connection fees. The poor can pay for water, but they cannot afford the ridiculous connection fees that have been 100 or 150 dollars. Reducing connection fees

by providing a simple supply, allows people to make their own provision from those meters to their houses, whether by hose pipes or carrying. We have held focus group discussions with the poor showing that their water bill has reduced by 90% when they got the new connection. International operators and actually their local partners would now say that they are taking much more responsibility, as the local companies are making a difference. Some customers can now enjoy the luxury of a daily shower because of the high pressure. Now households have spare time to go to the shopping malls – I didn't realise in all my talk about health and hygiene, that the ultimate goal of all this is so that people can go shopping. The key aspect of that in development terms is giving people choice. People now have choice to spend their lives and do the things they want to do. Also to attend focus group discussions without having to worry about returning home without water for the day's use. People have more time available, so can take an hour to do household chores, and no longer have to queue for water when it becomes available, no more waking up at 3 am, or paying a fortune to vendors. These are real improvements. Using simple technologies, putting galvanised iron pipes around a slum, and people use their own plastic pipes to make their own connection. Furthermore, the poor are pleased to have those meters, as it gives them legal representation in a way. They now have a bill with their name on, with where they are from. It makes a difference.

There are similar experiences in other places. All the tricks of participatory development have been used and service has been delivered very quickly, whereas most of the development projects that I have been involved with span over years and often do not deliver. Here the discussion started in August 1999 and by October 1999 even the poorest had water connections. It is not rocket science, it is the simplest technology, but it means they do not now have to use the hand pump and polluted groundwater. In this particular low-income housing site, people have meters and they are pleased to pay a tariff. It is not very good quality, but it gets the job done.

There is the danger of contamination with the pipes going across this little drainage canal but it is fully pressurised, which was not previously the case.

More benefits mentioned were mothers having more time to care for their children, attend to their meals, more leisure time, and houses being made out of permanent materials. It is making the difference.

But what is the private sector bringing? Is it capital for investment, is it private management with incentives or does it appear to be foreignisation rather than privatisation that is making the difference? 70% of the major contracts are international, probably a little higher now. Not all of them are success stories. As I mentioned, the PPP in Kampala did not work, but at some level the big multinational companies are honing the political power to make a difference.

There are some simple management theories of Kurt-Lewin and others about force field and quasi-stationary equilibria, saying how it is necessary to unfreeze before change can occur. And at some level this privatisation is needed to do the unfreezing of the existing system. Lewin also writes about the driving forces and the restraining forces. Everywhere I work I find these restraining forces are incredibly powerful. The international companies also need to be powerful enough to change the 'force field' to put pressure on politicians to overcome these ever-present restraining forces, otherwise no progress is made. Contingency theory segments organisations into mechanical, craft and organic.

I would like to suggest that NGOs have the ability to function as 'craft' organisations relating directly to the poor but craft organisations can deliver services of variable quality. Private operators appear to have the ability to unfreeze existing behaviour patterns. Other presentations have made the point that it is the same people working in these companies before and after privatisation. They need to be unfrozen, we then have to implement an efficient 'mechanistic service' changing from a relationship-based management to rules-based management, which are very important for a conventional mechanistic water company. However, to serve the poor it is necessary to develop and integrate the 'craft' or 'organic' elements - using some ideas of contingency theory. It appears that international private operators can limit the restraining forces. The French ambassador has already written to the Argentine

Government on the behalf of the French utilities in Argentina. That power does seem to have some effect.

However, for the rest of the world, which may not have the chance of these international operators, there seems to be a gamble. The challenge is to go from second rate public service provision at the moment to go to a first rate experienced foreign operator. There are not many of them which have all these skills of participatory development as well. As the market expands, it is quite likely to go to an inexperienced private sector operator, or to seek to 'buy in' and/or a national private operator, but the result is a third rate performance, as is happening in Kampala at the moment. That is a real gamble to governments – deciding which way to go.

Nehru suggested that it is better to have a second rate thing made within one's own country than a first rate thing that one has to import. That is part of the whole development debate, deciding how to go forward. There does appear to be a degree of concentration; this figure's international market in Asia on middle and low income countries, Ondeo are reporting capital expenditure 45% of the market (?). And just to make it quite clear, of course it is not their own capital that they are spending, but that of the World Bank and ADB, the old sources of finance really that are being leveraged by this new foreign management. Apparently Vivendi say that Ondeo is a generation ahead of them in learning how to meet the needs of the poor as part of these concessions. There is a sense that the French water companies, in particular Ondeo, with their own R&D department are ahead of the game. From my own knowledge and experience, they appear to be doing better than many others. The key question is how national private enterprise, or national public direct providers, can capture these qualities to promote reform. Only 4% of the populations of MLICs are served by PPPs at present. There is a long way to go before we have any fear of being taken over by the private sector. How can the partners become pro-poor? Our ADB study will produce some results very shortly on the website.

In conclusion, I would say that PPPs are giving benefits, so although perhaps they should not be necessary, it seems that they are at the moment. As we have seen in regard to regulation and privatisation in the UK, there is no perfect model to follow. The

process is always adapting as we go along. It does require very expert contract preparation if the needs of the poor are to be met. I hate the terminology of the success fees going to the IFC for 5 million dollars while signing the contract. I believe the success fee should come after 5 years when the poor are being served under the contract. The only time that I have seen a representative of a French company look worried is when I talk about open book accounting. I do not see why this should not be introduced with PPPs. Again international auditors use international auditing standards. Perhaps international standards of auditing are not so good after all as was seen in the case of Enron - and this therefore makes open book accounting even more necessary to meet the needs of the poor. We have to use the special skills of NGOs, we have to remember affordability and willingness to pay. There is no willingness to pay for sewerage and waste water treatment. Subsidies still have a part to play. International donors may well have a part to play to subsidise opex as well as capex to meet the needs of the poor. It is a job that can be done and should be done. We do want to use labour intensive technologies. The poor need jobs. I am not convinced about subsidising job creation for the sake of it, but we should be very aware of labour intensive technologies. Regulating wisely, using customer committees, generating competition perhaps through comparative competition wherever possible, there is much benchmarking competition going on at the moment.

In big cities there is 20% PPP, compared to only 6% for small towns and secondary worldwide, so that represents quite a lot of England and France and the USA. There is a long way to go.

As a final point: at the moment India has four thousand urban local bodies, none of which have a PPP. Apart from a few service contracts, the population gets water on average for two hours on alternate day. The Minister of Urban Development and Poverty Alleviation signed up to the change management forum in December. India wants to change, yet is resistant to PPP, which is their decision, so it is looking at change management ideas. They are trying to send the message that perhaps change can come. But the real question to us all is whether it can happen enough without the private sector's driving force for change. The private sector should not be necessary, but it does appear to me that it is, to try this change. In low income countries, only 1.7

billion available investment is reported, which is insufficient to meet the needs of the poor. . As usual, it all tends to go to the rich. If the rich can benefit from privatisation, then so can the poor.

Please note, this presentation was delivered to an audience who were able to see a series of over 60 slides, complete with photographs, tables, graphs and quotations.