AfDB

Water & Sanitation Department

Policy Brief

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# Financing water security for economic growth in Africa

The African Union Summit of Heads of State at Sharm El Sheikh in 2008 agreed on several key conclusions:

- the importance of making the case for investing in water infrastructure by demonstrating its benefits to national economies;
- the urgency of preparing national plans for the development of water infrastructure, containing estimates of cost, indications of phasing, and other aspects of implementation;
- the need to prepare financing strategies and develop all feasible sources of funding for this infrastructure.

This Policy Brief contains suggestions about how these Ministerial conclusions can be translated into policies implemented by African Governments.

## Making the case

The relative neglect of water in public budgets and the low priority it receives in public investment allocations shows that the economic contribution of water in all its forms[1] is not fully appreciated. Water is the lifeblood of the economy - a medium essential for all life and livelihoods, as a key raw material for economic sectors and a binding constraint on their future growth. To promote this mindset amongst policy-makers:

- Planning and development departments should review the economic implications of future water scenarios, using state of the art methodologies[2] for assessing the economy's exposure to water risk, and a means of comparing different ways of mitigating this.
- In presenting bids for budgetary and investment allocations for major programmes, all sectors should be required to state their estimated impact on water, both as passive agents (water risk exposure) and as active contributors (water impact, or water footprint).
- Proposals for major new investments, by private companies or other sponsors (including sovereign wealth funds and non-OECD partners) should include a full assessment of their water risk and impact (including footprints where feasible).
- Sponsors of projects for the development and management of water resources or the provision of water services should include a full economic justification, using economic values of these services, where feasible.

## Planning, costing & capacity building

The prior work of the African Infrastructure Country Diagnostic (AICD), which continues as the Africa Infrastructure Knowledge Programme (AIKP)[3], should be given a strong national focus in order to assist Finance Ministers and national planners:

- African governments should capitalise on the existing work of the AICD/AIKP by estimating investment requirements for water in its various forms, and determine priorities and sequencing as part of the same exercise.

[1] Not just household water and sanitation, but also water services for agriculture, industry and other economic sectors, strategic water storage, flood control, environmental protection, etc.
[2] such as that produced for the 2030 Water Resources Group by McKinsey & Co, Charting our water future: economic frameworks to inform decision-making (2009).
[3] Now hosted by the AfDB, alongside the Infrastructure Consortium for Africa.

Implementing and funding complex infrastructure programme will require some reinforcement of Governments' institutional and human capacity. Two specific aspects in water financing that cause difficulty are the preparation of complex water infrastructure finance packages, and problems arising in existing PPP projects that are running into difficulties. Consideration should be given to creating new facilties as follows:

- A facility to assist governments and other public authorities in the preparation of complex water infrastructure financing contracts, drawing on resources of existing agencies and other related bodies.
- A "trouble-shooting" service available to governments, municipalities, utilities and other public agencies to assist with resolving problems arising in the execution of existing contracts in the water sector, especially those in PPP ventures. This could involve existing agencies, and co-opt expertise from other successful public water authorities, private water companies, the financial sector and management consultants.

## Financing strategies and development of funding sources

The cost of national water infrastructure plans is likely to exceed the sums potentially available. The approach recommended for dealing with this problem is in three steps: firstly, minimising (shrinking) the gap, secondly, enhancing the revenue stream from the "3Ts" (tariffs, taxes and transfers) and, thirdly, using this to leverage repayable funding sources, making intelligent use of risk-sharing and mitigation instrtuments.

To shrink the financial gap, government finance departments could:

- Insist on improved internal efficiency from the water sector in such areas as loss reductions, energy efficiency and bill collection rates as the quid pro quo for public financial allocations.
- Ensure that state enterprises and public institutions such as schools and hospitals have sufficient funds to pay their water bills.
- Address the reasons for underspending of financial allocations made to water institutions and service providers.
- use the iterative financial planning processes employed in Strategic Financial Planning in order to reduce funding gaps to realistic and affordable levels.

Governments can develop revenues from the "3Ts" by:

- Avoiding across-the-board subsidies for water tariffs and user charges and targeting subsidies to specific policy aims and hardship cases.
- making more use of medium term (3-5 year) commitments to water entities receiving budgetary allocations, to improve the predictability of their funding
- Working with donors to improve the rate of disbursement from existing aid commitments and meeting their pledges on ODA predictability and alignment under the Paris Declaration and Accra Agenda.
- tap into climate change funds for the adaptation of water infrastructure

Repayable sources of finance can be leveraged by:

- Encouraging the funding of water from local sources, by promoting the growth of local capital markets.
- In countries with sufficiently strong fiscal prospects, preparing municipalities and utilities for bond issuance, through actual or "shadow" credit rating, the corporate reforms that this entails, and through the uptake of guarantees and other forms of credit enhancement.
- Building project finance for major infrastructure around loans from IFIs and blending other sources using platforms such as the EU-Africa Infrastructure Trust Fund.
- engaging non-OECD partners earlier and more fully in planning and financing infrastructure in order to optimize their contribution to national water programmes.
- promoting private management, operation and lease contracts for water supply, sanitation and wastewater projects, containing performance-related rewards, as an alternative to full private concessions, where the latter are not feasible.

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