



## ADB-OECD Expert Meeting

***For a beneficial private sector participation in the water and sanitation sector, lessons learnt from Asian country experience***

***Manila, March 5<sup>th</sup> 2008***

# SUMMARY REPORT

On 5 March 2008, the Asian Development Bank and the OECD held a joint Expert Meeting on: *For a beneficial private sector participation in the water and sanitation sector, lessons learnt from Asian country experience*. The expert meeting aimed to advance the debate on private sector participation in the water and sanitation sector by providing a forum for participants to discuss and better define the key elements of a beneficial partnership. After the NEPAD/OECD Investment Initiative roundtable organized in Lusaka in November 2007, the ADB/OECD expert meeting was the second opportunity to discuss the draft OECD guidance on private sector participation in water and sanitation infrastructure, building on the experience of Asian countries. The meeting brought together high level participants (see list of participants in Annex 2) and led to fruitful discussions.

The meeting was organized into 3 sessions (see programme in Annex 1):

1. Session 1 provided a broad overview by introducing the application of the OECD *Principles on Private Sector Participation in Infrastructure*<sup>1</sup> to the water and sanitation sector and by sharing past experiences and trends within the sector.
2. Session 2 focused on two main areas highlighted by the OECD *Principles* as crucial for beneficial partnerships. Panel discussion A focused on the development of a conducive institutional and regulatory environment and Panel discussion B discussed the roles and responsibilities of various stakeholders.
3. Session 3 highlighted the access to financing as a major constraint to the development of the sector and to further involvement of the private sector. It aimed to draw attention to the financial innovations that could help lift the constraints on financing and facilitate private capital flows to the water and sanitation sector, based on the experience of the ADB.

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<sup>1</sup> [www.oecd.org/daf/investment/ppp](http://www.oecd.org/daf/investment/ppp)

## **Main highlights from the discussion**

### ***The regulatory framework***

A sound regulatory framework was highlighted as the key element for a successful partnership and in general for improved governance in the sector. Unpredictability of the regulatory framework and multiplicity of government agencies responsible for implementation and oversight are leading to dilution of responsibilities and unclear reference point for private actors. Remedies include regulatory reform and clearer and better defined allocation of roles across existing government bodies.

Some participants however stressed that regulatory bodies have often been overburdened with too many governance roles. There is a need to refocus regulatory functions around the key activities of: 1) tariff/price setting, 2) subsidies for the poor, 3) efficiency and performance incentives, 4) quality and environmental standards, and 5) consumer protection. Quality and availability are important elements of regulation that should be jointly considered with tariffs setting. Regulation cannot substitute for appropriate design of contractual arrangements, which remain the basis for the relationship between the public and the private sectors.

Regarding tariffs, several participants highlighted the usefulness of regular rebasing exercises as components of long-term contracts. Given the long-term nature of private water and sanitation contracts, these would give the parties an opportunity to reassess the situation, take stock of present circumstances, and agree on a way forward. It raises the issue of the appropriate capacity on the part of the public partner to develop sound tariff strategies and to participate in the rebasing exercises.

Participants agreed that a good regulatory framework and a robust long-term water policy should apply to the overall sector, regardless of ownership of operators. Standards and requirements set by regulation should notably be the same for all and incentive-based rather than punitive. Some participants however underlined that the involvement of private actors has probably helped raise expectations and put pressure on private operators to provide higher level services than required by minimum standards.

Cambodia and China experiences illustrate how high level political commitment can contribute to driving reform. At the same time, participants agreed on the need to shelter the sector from undue political interferences. They underlined the importance of third party and professional technical advice to bring credibility to regulatory decisions, while stressing that the independence of third party should be strictly respected through appropriate financing.

### ***Information and benchmarking***

Participants insisted on benchmarking as a source of information to compare performance of water and sewerage providers, as a strong tool to drive efficiency and as an incentive towards greater transparency. Benchmarking involves developing a set of performance indicators that show how providers fare relative to each indicator i.e. coverage, non-revenue water, average tariff, collection efficiency. The ADB, through its Water Utility Data Books, has regularly

conducted benchmarking exercises in the region. Consumer satisfaction surveys are also a good way to assess utility performance as shown in the Manila experience where academia has been a partner to both concessionaires and the government in the conduct of annual public assessment surveys.

Greater availability of information facilitates healthy competition among operators (including across public and private operators). Transparency on contractual arrangements is also necessary so the public will be aware of the goals and objectives in inviting the private sector in the provision of water and sanitation.

### ***Roles and responsibilities***

Participants posit that Governments should provide an environment that will allow for viable water and sanitation operators. It involves developing a clear regulatory framework, but also effective implementation of regulations and contractual provisions. In that context, clarifying roles and responsibilities is needed, including disentangling of functions, notably between oversight and service provision. Appropriate allocation of roles and responsibilities goes in tandem with clear identification of risks, rewards, rights and recourse across the various parties.

The service functions should be the responsibility of operators. Some participants pointed out the need to strengthen operators, be they public or private. This is precisely the objective of the WOP (Water Operators Partnership) program, a platform for mutual cooperation among water operators and utilities<sup>2</sup>.

The experience of Manila Water shows that when the regulatory framework establishes effective incentives, the private companies can also contribute to improving substantially level of access and service. However, the participants highlighted the difficult trade-offs that reaching the poor involves. The private sector has to comply with contractual arrangements and is driven by ensuring an adequate return on capital. Where affordability is low, installing new connections may require establishing subsidies, with the risks of misallocation and that the less profitable customers are excluded – in that context, subsidizing connections rather than consumption may help reach out to the poor more efficiently in areas where connection rates are low. Furthermore, if there is a clear necessity for private companies to be in line with the development goals set by the government, countries cannot afford to leave the connection and provision for the poor to purely corporate social responsibility actions. This raises the issue of the opportunity to set universal service obligation as a contractual arrangement and of its concrete application through investment programmes.

International financial institutions also have a role to play in assisting governments to package projects for private participation. However, after the Manila and Jakarta contracts packaged with the help of the IFC and with assistance from the World Bank for policy, regulatory and institutional reforms in the late 90's, there have been very few projects in the region involving private sector in water and sanitation.

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<sup>2</sup> [www.adb.org/water/operations/partnerships/GWP-water-operators.asp](http://www.adb.org/water/operations/partnerships/GWP-water-operators.asp)

## ***Financing***

Participants agreed that tariff setting was the cornerstone of a sound financing strategy as it determines future revenue streams and therefore both internal investment capacity and ability to contract a loan from financial institutions. The development of sound, bankable proposals remains a key parameter and an area where greater capacity building is needed. A closer collaboration between public and private actors in developing funding proposals could help bridge the capacity gap. But building demand also requires institutional reforms, cultural change and political will, all necessary elements to develop the capacity of utilities.

Serious challenges also persist on the supply side of financing. Some participants stressed the limited capacity on the part of financiers to assess risks and rewards. Participants also agreed on the limits of traditional instruments (on-lending by local governments for instance constrained by political considerations that may lead them to favour shorter-term expansive financing, but fully under their control) and the need to develop innovative forms of financing (involving credit enhancement, bonds linked to contracts). There is an active role to play for ADB in the area of risk mitigation instruments and in terms of financing for low income communities (such as setting up subsidy mechanisms targeting connection fees). New financial instruments launched by ADB include non-sovereign lending (allowing state-owned companies and local governments to borrow), local currency financing (dealing with the currency risk), and multi-tranche financing (allowing for single approvals for large scale projects with interest payments for disbursed amounts only). However, financial viability of projects remains a major constraint.

The specific case of sanitation was highlighted. In that sector, tariff structures rarely reflect the cost of operating and maintaining the sewerage network and connection costs reach prohibitive levels. At the same time, the Bandung experience has shown the limitation of spreading the connection costs to all – even to the unserved - making it difficult to justify future additional charges for new connections. This urges regulators to look into tariff structures to provide operators incentives for sewerage connections and public authorities to consider subsidies that would target connection fees. Participants pointed out that innovative financing instruments and concessional funds will be necessary to make sanitation and sewerage services viable. More projects – public or private – are needed in the sector if the sanitation related MDG is to be reached.

### ***Call for greater capacity building***

Participants stressed the need for greater capacity building in the following specific areas:

- To develop understanding of the key elements of a public/private partnership and the roles and responsibilities of parties throughout the PSP process.
- To develop an informed involvement of civil society, communities and consumer associations.
- To support regulators and governments by professionalizing technical capacities to avoid politicization of tariff setting and adjustments.
- To facilitate access to funding.

# ANNEX 1 – AGENDA

## I. Background

Water and sanitation is a key sector where much effort is needed: with over a billion people without access to drinking water and 2.6 billion lacking basic sanitation, developing the relevant infrastructure constitutes a major challenge. Halving the proportion of people without access to drinking water and sanitation by 2015 would require investments of some 30 billion USD per year, which is twice the current spending level. To meet these tremendous needs, many countries have sought the involvement of the private sector.

Within the framework of its new horizontal project on “Sustainable Financing to Ensure Affordable Access to Water and Sanitation”, the OECD addresses the economic basis for sustainable water service provision and sound water management. Along with special focuses on pricing, innovative financing business models and realistic financing strategies, the project aims to develop practical guidance to optimise private sector participation in the development and management of water and sanitation infrastructure. The guidance builds on the newly released OECD *Principles for Private Sector Participation in Infrastructure* and is developed through multi-stakeholder dialogues and reviews of specific country experiences. The Manila expert meeting follows a similar roundtable organised jointly by the NEPAD and the OECD in Lusaka, Zambia on November 27/28<sup>th</sup> 2007<sup>3</sup>.

## II. Objectives and expected outputs

The overall aim of the expert meeting is to advance the debate on private sector participation in the water and sanitation sector, by providing a forum for participants to help guide the ADB and OECD in their efforts to develop a better understanding of the key elements of a beneficial partnership. Expected outputs from the Roundtable will include a first draft of guidelines, taking advantage of the new *OECD Principles for Private Sector Participation in Infrastructure* for the water and sanitation sector derived from the experience of Asian countries, in order to foster the mobilisation of additional and beneficial private sector involvement.

<b>08:00 - 08:30</b>	<b>Registration</b>
<b>08:30 - 08:45</b>	<b>Opening Session</b> <b>Chair and Welcome Remarks</b> <ul style="list-style-type: none"><li>• Arjun Thapan, Director General, Southeast Asia Regional Department and Chair, Water Committee, ADB</li></ul> <b>Introduction of Participants</b>

<sup>3</sup> [www.oecd.org/daf/investment/africa](http://www.oecd.org/daf/investment/africa)

**SESSION 1: SETTING THE STAGE OF PRIVATE PROVISION OF WATER AND SANITATION INFRASTRUCTURE SERVICES IN ASIA.**

The purpose of this session is to take stock of past experiences in involving the private sector, both domestic and foreign, in the development and management of water and sanitation infrastructure in Asian countries. It will be an opportunity to share experiences on the recent developments in the nature of private sector involvement and of the typical bottlenecks that are holding back private investments.

The session will address the following questions:

- What have been the strengths and weaknesses of past experiences of private sector involvement in water and sanitation infrastructure development?
- What have been the key developments in the nature of the co-operation between the private and the public sector in developing water and sanitation infrastructure?
- What preliminary conclusions and guidance can be given on the respective roles of the private sector and government agencies, and on the mechanisms to ensure successful partnerships for the benefit of all?

**08:45 – 10:00**

**Presentation:** *The OECD water Project and the guidance to ensure successful private sector participation*

- Céline Kauffmann, Water Investment Project Manager, OECD

**Presentation:** *Stock-taking of private sector involvement in the water and sanitation infrastructure sector of Asian countries.*

- Jenny Dato, Consultant, OECD

**Questions for clarification**

**10:00 – 10:30**

Tea and Coffee

**SESSION 2: APPLYING THE *PRINCIPLES* TO THE WATER AND SANITATION SECTOR**

High capital intensity, large initial outlays, long pay-back periods, immobility of assets and low rates of return, which characterise water infrastructure investments generate high risks, especially when in a context of poor initial information and a weak investment environment. These features limit the scale of private investment in water and sanitation infrastructure.

The two panel discussions will build on the *OECD Principles for Private Sector Participation in Infrastructure* to identify the specific investment environment conditions and governance arrangements conducive to beneficial private sector involvement in the water and sanitation sector. It will aim to clarify the roles and responsibilities, but also the constraints faced by public and private actors and more generally of all the stakeholders involved in the sector.

**PANEL DISCUSSION A: TOWARD A CONDUCTIVE INSTITUTIONAL AND REGULATORY FRAMEWORK TO MAKE CO-OPERATION WORK**

10:30 – 12:00	<p><b>Panel discussion bringing together experts from the water and sanitation sector, including representatives from government, regulatory agencies, private sector.</b></p> <p>This panel discussion aims to identify the specific investment environment conditions and governance arrangements conducive to beneficial private sector involvement in the water and sanitation sector. The discussion will address the following questions:</p> <ul style="list-style-type: none"> <li>• What is required to enhance the enabling institutional environment in order to facilitate the participation of the private sector in the water and sanitation sector?</li> <li>• What are Government’s motivations in considering PSP in the water and sanitation sector?</li> <li>• What are the minimum requirements of the private sector for involvement in projects?</li> <li>• How to build capacity of Government and regulators to address contractual obligations and more importantly to deal with extraordinary circumstances?</li> <li>• How to build consensus at all levels to achieve common objectives?</li> <li>• What are the communication mechanisms that the governments can put in place to facilitate the communication and understanding across partners?</li> </ul> <p><b>Facilitator:</b></p> <ul style="list-style-type: none"> <li>• Anand Chiplunkar, Senior Water Supply and Sanitation Specialist, ADB</li> </ul>
12:00 – 13:30	Lunch
<b>PANEL DISCUSSION B: RESPECTIVE ROLES AND RESPONSIBILITIES OF PARTNERS</b>	
13:30 – 15:00	<p><b>Panel discussion bringing together experts from the water and sanitation sector, including representatives from government, regulatory agencies, private sector.</b></p> <p>Access to safe drinking water is a basic human need and a source of significant positive externalities, notably for public health. In the face of tremendous infrastructure needs, the partnership between the State and the private sector should involve setting the right environment, but also good faith and committed participation from all involved partners. It requires a clear understanding of the roles and responsibilities, but also of the constraints faced by the public and private actors and more generally of all the stakeholders involved in the sector.</p> <p>The session will address the following questions:</p> <ul style="list-style-type: none"> <li>• What are the key responsibilities of the different government agencies?</li> <li>• How does private sector see the role of government in ensuring the success of the partnership? What can be expected from Governments in terms of addressing private sector concerns?</li> <li>• What can be expected from the private actors in terms of responsible business conduct? How can private sector participants better align their actions with public authority poverty reduction objectives? How can the private sector better interact with the general public, notably consumers and communities, to promote mutual understanding and better outcomes?</li> <li>• How better involve users and communities?</li> </ul> <p><b>Facilitator:</b></p> <ul style="list-style-type: none"> <li>• Mai Flor, Water Governance Specialist, ADB</li> </ul>
15:00 – 15:30	Tea and Coffee

### SESSION 3: DEVELOPING THE UPTAKE OF FINANCIAL TOOLS

Strengthening the overall investment environment takes time. However, innovations, notably in the finance area, can help to mitigate risks in the context of an imperfect investment climate. For instance, new developments in investment guarantees and risk mitigation mechanisms make sub-sovereign financing a viable option, and are helping to attract investment and mobilise private sector resources in the water and sanitation sector.

The session will address the following questions:

- What can be drawn from past experiences with the use of these instruments in Asian country contexts?
- How can they be further developed, notably drawing on other developing regions experiences?
- What can donors do to support the development and adoption of risk management practices suited to the specificities of the sector in Asian countries?
- How to mobilise the appropriate development and use of investment guarantee and risk mitigation mechanisms to attract investment in the water and sanitation sector?

**15:30 – 17:00**

**Presentation:** New Financial Products of ADB

- Elsie Louise Pfleider Araneta, Principal Innovation and Efficiency Initiative Specialist, ADB

**Panel discussion:** Experience of the ADB in non-sovereign lending? What are the needs, the bottlenecks, the promising tools and practices? How can the development partners be of help?

**Facilitator:**

- Paul van Klaveren, Water Supply and Sanitation Specialist, ADB

**CONCLUDING SESSION: SUMMARY, NEXT STEPS AND CLOSING REMARKS**

## ANNEX 2 – List of participants

<b>CAMBODIA</b>		
Mr. Sem Bun Heng	Deputy General Director	Phnom Penh Water Supply Authority
<b>FRANCE</b>		
Mr. Jack Moss		AquaFed
Mr. Dominique Lebastard	Head of the Economic Department	French Embassy, Philippines
<b>INDIA</b>		
Mr. Dhruva Purkayastha	General Manager and Head	Infrastructure Group, ICRA Management Consulting Services Ltd.
Mr. Pradeep Singh	Vice Chairman, Managing Director	IDFC Projects Limited, IDFC Developers
<b>INDONESIA</b>		
Mr. Thierry Krieg	Managing Director	PT PAM Lyonnaise Jaya (PALYJA)
Mr. Nugroho Tri Utomo	Head of Sub-directorate, drinking and Washed Water	Directorate of settlements and housing, BAPPENAS
<b>MALAYSIA</b>		
Mr. Faizal Othman	General Manager	Ranhill Utilities Berhad
Mr. Lee Kon Yew	Executive Director President	National Water Services Commission South East Asian Water Utilities Network
<b>PHILIPPINES</b>		
Mr. Ramon Alikpala	Executive Director	National Water Resources Board
Mr. Antonino Aquino	President	Manila Water Company, Inc.
Mr. Jaime Ladao	President	Dun and Bradstreet, Inc.
Mr. Rogelio L. Singson	President and CEO	Maynilad Water Services, Inc.
<b>PRC</b>		
Mr. Pan Wentang	General Manager and CEO	Beijing Capital Group
Mr. Liu Yanjun	General Manager	International Department, Beijing Capital Group
Ms. Mo Li	Senior Engineer	China Academy of Urban Planning and Design
<b>VIETNAM</b>		
Mr. Nguyen Huu Nam	Manager, Appraisal Department	HCMC Investment Fund for Urban Development
Mr. Vuong Duc Hoang Quan	Deputy General Director	HCMC Investment Fund for Urban Development
<b>ADB</b>		
Ms. Elsie Louise Pfleider Araneta	Principal Innovation and Efficiency Initiative Specialist	Special initiative Group, Regional and Sustainable Development Department
Ms. Gyongshim An	Urban Development Specialist	Urban Development Division, South Asia Department
Mr. Stephen Blaik	Water Supply and Sanitation Specialist	Pacific Operations Division, Pacific Department
Mr. Anand Chiplunkar	Senior Water Supply and Sanitation Specialist	Energy, Transport and Water Division, Regional and Sustainable Development Department
Ms. Mai Flor	Water Governance Specialist	Energy, Transport and Water Division, Regional and Sustainable Development Department
Ms. Kathie Julian	Principal Urban Development Specialist	Social Sectors Division, Central and West Asia Department
Ms. Joanna McLean Smith	Young Professional	Social Sectors Division, Central and West Asia Department
Ms. Mary Jane Carangal san Jose	Economic Officer	Economic Analysis and Operations Support Division, Economic and Research department
Mr. Paul van Klaveren	Water Supply and Sanitation Specialist	Social Sectors Division, Southeast Asia Department
<b>OECD</b>		
Ms. Jenny Dato	Consultant	Water Investment Project, Investment Division
Ms. Céline Kauffmann	Economist/ Project Manager	Water Investment project, Investment Division