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Assessing the Sustainable Development Potential of The Commission's New Proposal for Establishing a European Water Facility for ACP Countries[1]: A Critical Review and Alternative Suggestions

The Commission's January 26th proposal for the establishment of a European Water Fund is both welcome and commendable. The assessment that follows is intended to provide some constructive feedback on this proposal in hopes that the Water Fund (WF) will be administered in ways that genuinely contribute to the achievement of the Millennium Development Goals of halving those without access to safe and affordable drinking water and sanitation by 2015. It is our hope that the modalities for establishing the WF are still malleable and open to suggestions from the public. Toward that end, this paper begins by highlighting those aspects of the proposal that we feel may ultimately constrain the ability of the WF to meaningfully support sustainable development projects in the water service sector that directly benefit the poor. This review is then followed by alternative suggestions for how the proposal's 'flexible funding approach' might be expanded so as to support the successful realization of more local community based approaches to water service management.

Critical Review

1) Subsidizing the International Private Sector: a Sound Strategy for Sustainable Development?

The Commissions proposal regarding the "key principles" that should guide the use and function of a European Water Fund are rather narrowly constructed and could undermine its potential for genuinely contributing to the sustainable development of ACP countries. According to Section 4.1 of the proposal:

> The Water Facility will assist countries to establish their institutional and regulatory framework in order to attract additional [READ: private] financial resources. The flow of private capital to the water sector has been limited, particularly for Africa…a major challenge remains how to make the private sector to participate more actively. Commercial loans are often too expensive to raise finance to the water sector…due to the range of risks that are perceived to exist and the uncertainty of gaining an adequate return on investment. Therefore…a combination of different financing layers such as grants, soft loans, loan guarantees, revolving funds, micro-credit finance for small scale actions, etc, may be needed to address financing gaps. The proposed Facility should give a flexible answer to a variety of situations.[2]

The major assumption here is that the only way to improve access to safe drinking water and sanitation for the poor in ACP countries is to attract international (preferably European)[3] private sector investment. To that end the Commission appears to be structuring the purpose and function of the WF more around the needs of international capital rather than those of the local poor. Thus large portions of the fund will be used on projects designed to attract and subsidize the entry of the international private investors into the water and sanitation service sectors of ACP countries. Therefore projects most likely to be funded through the WF are those that will facilitate this goal by (1) helping to create a more enabling environment for foreign capital through the administrative restructuring of ACP governments' institutional and regulatory frameworks and/or (2) projects geared toward providing stronger guarantee systems for reducing private sector risk.

[1] See Communication from the Commission to the Council and the European Parliament, *Communication on the Future Development of the EU Water Initiative and the modalities for the Establishment of Water Facility for ACP Countries*, Brussels, 26 January 2004 COM(2004) 43 final.
[2] *Ibid*. Section 4.1 pp.13-14.
[3] According to section 5.2 (2) of the proposal "Each proposal would ideally include a European partner. This could be the EIB and/or a European Development Finance Institute, or a private company…" *Ibid*. p.17.

Used in this way, the WF will do more to boost the profit margins of trans-national water corporations than it will to secure sustainable access to safe drinking water and sanitation to the poor in ACP countries. Water and sanitation services managed by private companies are by definition commercially driven. As a result, these companies are often only interested in investing in those areas of developing countries that they feel will provide the best chances for the biggest returns on their investment. They are not interested in piping and supplying water to poorer areas where people cannot afford to pay the full cost for water services. Nor are private sector investors generally keen to cut into their profits by engaging in basic life-line or cross-subsidization schemes designed to subsidize the cost of water services to the poor. In other words, private companies will manage the delivery their services only in ways that most efficiently minimize cost and maximize profit. The consequence of this, of course, is that the poor are increasingly cut-off rather than connected to water and sanitation services that are managed by the private sector and governed by the laws of the market.

Thus the responsibility of ensuring that safe and affordable water is available to the poor is once again ultimately laid at the feet of the national governments. Only now the problem of finding the resources for cross-subsidization schemes is compounded by the fact the most profitable sources of revenue in the water and sanitation sectors will be siphoned off by TNCs. The government is now left with one less recourse with which to subsidize the cost of water and sanitation services delivery to the poor. As a result, ACP governments will either have to go deeper into debt in order to provide safe and cheep water to the poor, or contend with the catastrophic social and economic costs to the health care system, labour force, and national economy when large sectors of the poorer population get sick and/or die as a result of this basic need going unmet.

So while the WF may be able to provide the right incentives to attract international private sector participation in the public water and sanitation services of ACP countries, these incentives will do little to improve affordable access to safe drinking water and sanitation for the poor, or to ease the debt burden of developing countries.

2) Liberalization, Good Governance and Flexible Funding?

Section 4.2 of the proposal, entitled "Activities to be funded under the Water Facility," betray a strong bias toward projects geared to promote market liberalization and public-private partnerships in the water service sectors of ACP countries.

> To stimulate the private sector investments, the Water Facility can contribute to Public Private Partnerships (PPP) or Private Sector Participation (PSP) initiatives, both at international and local level through the development of new financial tools. There are numerous innovative ways to leverage private and commercial funding and the Commission is presently in discussion with Member States, (EIB), European Development Finance Institutions (EDFI) and International Finance Institutions (IFI) on how to achieve the best results.[4]

To that end, the 'good governance' conditionality requirements for receiving support from the WF are narrowly defined by the Commission in terms of openness to, and progress toward market liberalization principles of maximum cost recovery, and market oriented institutional reforms that will attract and benefit private sector participation.

> Priority will be given to support for countries that are well advanced in their sectoral policy reforms. The Water Facility will assist partner countries in the elaboration of good, sustainable projects designed around the principle of maximum cost recovery…the WF can assist other countries to reform the water and sanitation sector, strengthen their institutions and build up capacity in the sector to create the enabling environment for investments.[5]

This narrow focus on only those countries and projects which demonstrate the best chances for attracting private sector participation in public water and sanitation services undermines the otherwise positive potential that lies in the proposal's flexible funding approach to the improvement of water service management in the South. Flexible and innovative funding schemes should not be limited only to the

[4] *Ibid*. Section 4.2 "Activities to be Funded Under the Water Facility" p.15.
[5] *Ibid*. p.14.

promotion of PPP or PSP. As argued above, "the effect of using aid to promote PPP, or requiring privatization as a condition for aid, is to tie that aid firmly to giving business to EU based companies."[6] Such policies, in both economic and political terms will do more to benefit European trans-national water companies, than they will to deliver safe and affordable water to the poor. Providing risk guarantees for corporate investors tells us little as to the specific needs of the poor for improving their access water, or local communities and municipalities for improving their capacity to deliver a better service to more people.

Indeed the Commission's proposal says very little about supporting public-run utilities and basically ignores the European Parliament Resolution passed just last September on Water Management in Developing Countries, which calls on the Commission to support local public authorities in their efforts towards establishing innovative, participatory, democratic systems of public water management that are efficient, transparent and regulated and that respect the objectives of sustainable development in order to meet the population's needs.[7] The lip service that the proposal pays to the support of community based projects is at best vague. Section 5.2 on 'Investment projects and related TA' mentions that "special arrangements will be developed for the co-financing of smaller community based projects," but does elaborate as to what those "special arrangements" might be or how the WF might go about developing the capabilities to assist in the development of such projects. In fact, in the case of Africa, the proposal suggests that the responsibility for supporting community-based projects should be offloaded to the African Water Facility to manage.[8] Therefore, the European Water Facility, it seems, is only to be used for supporting those projects that will guarantee profit returns for European trans-national water companies.

We would urge the Commission to reconsider this position and to gear its 'flexible funding approach' more directly and precisely toward supporting public utilities and/or local community based projects that may be more capable of addressing the needs and concerns of the poor in ACP countries in their struggle to gain sustainable and affordable access to safe drinking water and sanitation.

Alternative Suggestions for Supporting Sustainable Development in the Water Services

Below are a few alternative suggestions for ways in which the European Water Fund could be used to promote sustainable water and sanitation service management in ACP countries. A few suggestions are as follows:

1. Supporting Public-run Utilities
   The WF could be used to support projects geared toward supporting public-run water and sanitation utilities that are already in place in many in ACP countries. Where asked for and where it is needed, funding for technical assistance, infrastructure development and extension, skills training, etc. could all serve to improve ACP government's ability to ensure affordable access to safe drinking water and sanitation to the poor.

2. Community Based approaches to Water Service Management
   The WF could be used to support community-based projects designed to develop more participatory models of water service management. Support for democratic decision making models and/or participatory budgeting processes may serve as a better application of WF resources because projects will be designed, and monies will be spent in ways that best reflect the needs and priorities of local citizens and that best conform to their social, economic and environmental conditions.

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[6] David Hall, "Financing Water for the World: an Alternative to Guaranteed Profits" PSIRU, University of Greenwich, March 2003, p. 9.

[7] European Parliament resolution on the Commission communication on water management in developing countries and priorities for EU development cooperation (COM(2002) 132 - C5-0335/2002 - 2002/2179(COS)).

[8] See Section 5.1 (3) of the Communication from the Commission on the Furure development of the EU Water Initiative and the Modalities for the Establishment of a Water Facility for ACP countries. *Op. Cit*. p.19,

3. Public-Public-Partnerships

    Based on the needs outlined by local communities and municipalities, the WF could support the creation and maintenance of Public-Public Partnerships (PUPs) between public utilities in Europe and those in ACP countries. European-ACP PUPs could engage in information sharing, skills training and technical assistance projects, while regional PUPs among ACP countries might be supported to engage in wider infrastructure development partnerships.

4. WF as a source of Cheep Loans for Capital Investment for Local Communities

    The WF could act as a source of cheep loans for local authorities and/or communities to use for capital investment in their own water and sanitation service sectors. Many local municipalities and communities in ACP countries are unable to secure loans from private banks for capital investment. The WF could function in some cases as development bank geared toward providing low cost loans to public providers for their water and sanitation development projects. Such loans would, of course, be most effective and attractive if they were to come without the usual privatisation and liberalisation conditionalities that characterize so many World Bank and other IFI loans.

These are but a few suggestions as to how the Commission's proposal for a European Water Fund might be better applied in the current struggle to meet the MDG goals. Providing sustainable and affordable access to safe drinking water and sanitation should centre more directly on listening to and meeting the needs of local communities rather than those of private industry. Gearing the WF to support only those projects that embrace strategies for profit maximisation, private sector participation and market liberalisation in water services will do little ensure that those who cannot afford to pay for the full cost for water service delivery are able to get it. Therefore it is our hope that the Commission will revise its current proposal and show more genuine flexibility and openness in its approach to funding water development projects such as those outlined in this paper.

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