



United Nations

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Backgrounder

Supplying Water – For a Price

Supplying water and sanitation for the world's people is a huge task – and an expensive one. Whether these essential services are best carried out by governments or the private sector is a much-debated question among policy makers, experts and citizen groups. Some background to this debate and key positions are outlined below.

Providing safe drinking water and sanitation to those lacking them requires massive investment – estimated at \$14-30 billion per year in addition to current annual spending levels of \$30 billion worldwide. As with other infrastructure services such as electricity, telecommunications and transport, most developing countries rely on public sector utilities to finance and operate water and sanitation services. But because of financial and human resource constraints, the results are often low productivity and inefficient service and coverage. According to the World Bank, technical inefficiencies in power, water, roads and railways alone were estimated to have caused losses of \$55 billion a year in the early 1990s – equivalent to one per cent of the GDP of all developing countries, a quarter of their annual infrastructure investment, and twice the annual development finance for infrastructure.

In the late 1980s, urged by international lenders, countries around the world began turning to the private sector, both to take over the operation of existing infrastructure enterprises and to finance new infrastructure assets. It was argued that private sector financing and management expertise could improve the quality and quantity of infrastructure services. Private financial resources could be tapped and services expanded, while reducing the burden on scarce public resources.

In developing countries, water and sanitation services are often subsidized, traditionally through direct

payments to utilities, and are paid for by general taxation. The current investment in water and sanitation in developing countries is about \$15 billion annually. According to the World Bank, governments are responsible for close to 75 per cent of financing and the private sector for about 11 per cent, with the remaining 14 per cent of financing coming from external support agencies.

Popular belief generally holds that water is a common good and basic need that can best be provided by the public sector at very low cost. As a result, the full cost of supplying water is seldom charged to consumers. Even where tariffs are charged to industrial users, they are usually based upon average costs and ignore the real costs of externalities such as wastewater disposal, as well as the “opportunity costs” such as the benefits lost by not pursuing alternative uses of water. One result is that much water is undervalued and wasted, even as the world faces greater and greater water shortages. Without compensation for the costs incurred, developing country governments usually cannot afford to expand their services to all in need, and the poor who are not serviced are often forced to take arduous treks to fetch water and risk becoming sick from unsafe supplies.

Some proponents argue that privatization of water and sanitation services can address some of these problems. Currently the private sector manages the water system for only 7 per cent of the world population. That

figure is expected to more than double by 2015. Private water management is estimated to be a \$200 billion per year business at present, which World Bank projections show could reach \$1 trillion a year by 2021.

Growing Criticism

However, the growing involvement of the private sector comes with growing criticisms. Just as when water and sanitation services were managed by the public sector, there are reports of privately-run services wrought with unsafe contaminants, leaky pipes that go un-repaired for weeks, and, notably, price hikes that put poor people in a position of having to choose between food and water. In Cochabamba, the third largest city in Bolivia, prices increased by 35 per cent after a private consortium took over the city's water system in 1999, resulting in protracted street protests. The contract with the private water supplier was rescinded less than a year later.

Even attempts by some developing country governments to adopt private sector approaches have served as painful lessons. When the South African government tried to end water subsidies in 2000, the result was that millions of poor people were forced to use water from polluted rivers and lakes, causing one of the country's biggest cholera outbreaks ever.

These cases reinforce two common perceptions – that private sector participation enriches a few at the expense of many, and that water flows to those who can pay. Critics say that private companies, in their attempt to make attractive bids for long-term contracts, often underestimate the cost of maintaining a water system. Once the contract has been won and operations begun, they resort to cutting staff and maintenance costs, raising prices, or both, to turn a profit. Other detractors of privatization argue that water is a human right and everyone should be ensured equal and adequate access on a

non-profit basis. It should not be managed by for-profit enterprises.

Finding Solutions

However, no matter who manages this key resource, water supply and sanitation will inevitably have to be paid for by someone, whether consumers or taxpayers. Some experts argue that private enterprises, which in many cases are in a better position to identify gaps and provide needed services, have an important role to play. But working with the private sector does not mean that a government would, could or should simply hand over the management of its water resources to the private sector, and let the profit motive run its course. Rather, it implies a dialogue among government, the private sector and all users, to come up with equitable and environmentally sound solutions.

A spectrum of relationships could evolve, with many different options for the role of the private sector. Governments could transform their role from the exclusive financiers and providers of infrastructure services to facilitators and regulators of services provided by private firms. Contracts would have to be well designed, with the right balance of minimum standards and penalties, as well as incentives. In all cases, the government must be engaged in both oversight and overall regulation.

Better pricing of water by governments is another proposal considered to be a potential solution. Developing pricing schemes that meet social, technical, economic and environmental concerns is a major challenge. One option being tested in some countries is for governments to pay part of the water bill for poor households that meet certain criteria under a direct subsidy approach. Beyond the basic minimum, consumers would have to pay increasing tariffs per unit used. This would be an alternative to allowing the price of water to fall below economic costs indiscriminately.