



Water sector reform

Restructuring electricity, telecoms and water sectors:
comparisons of typologies, drivers, and reform paths

Dr Rolfe Eberhard, 23 August 2004

P•D•G

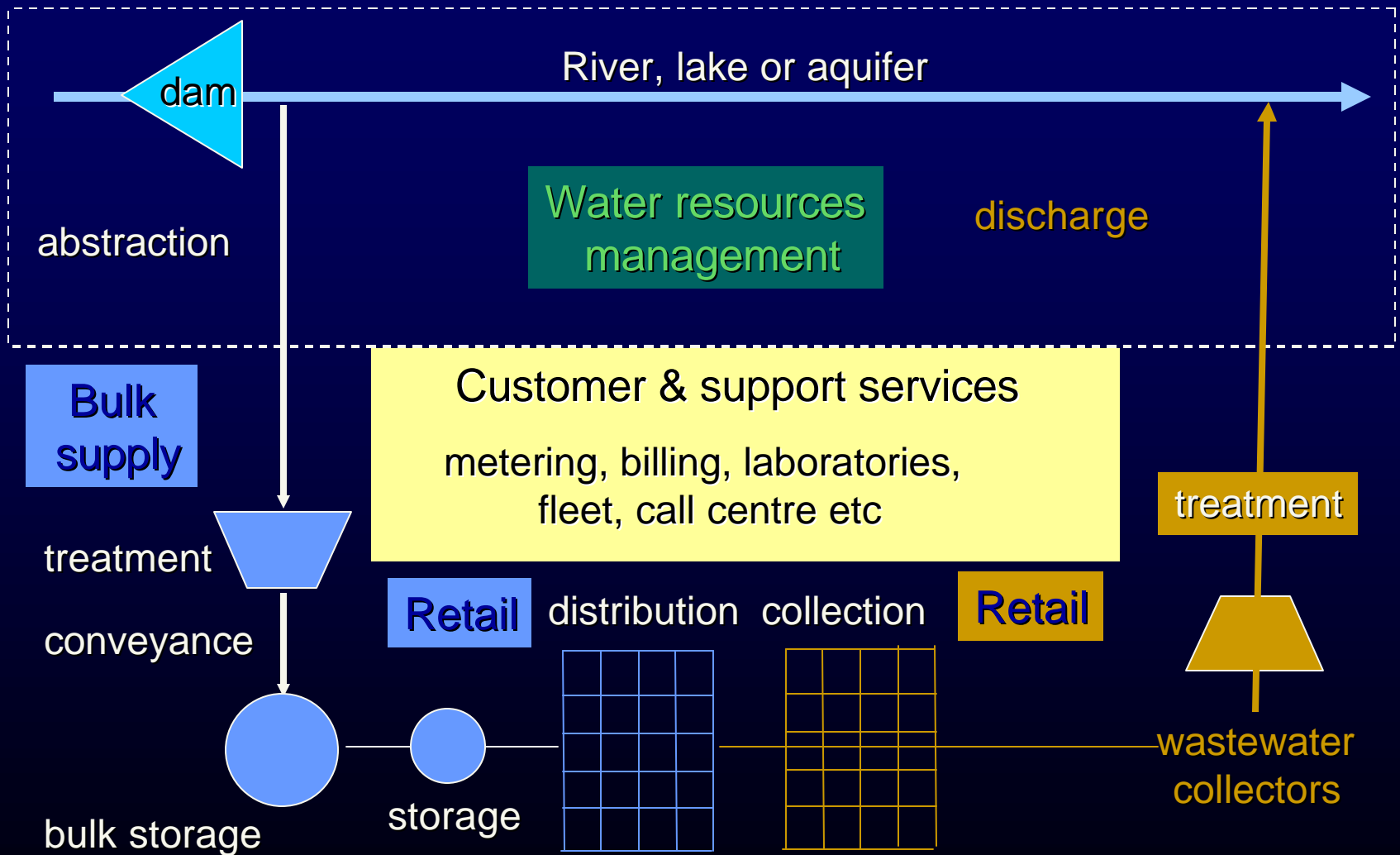
PALMER DEVELOPMENT GROUP

Outline

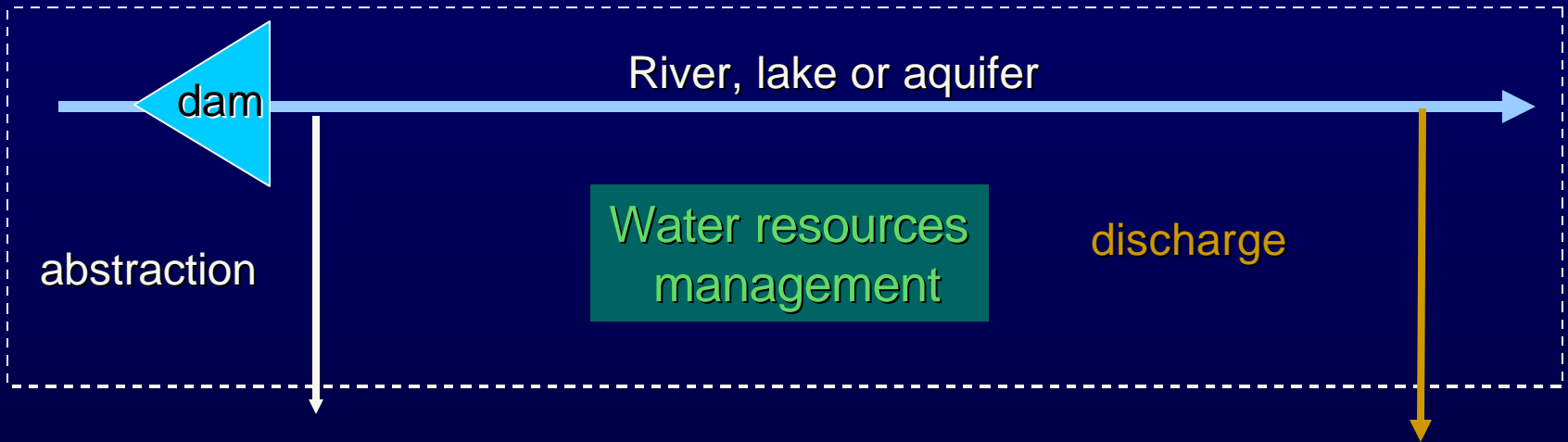
- Physical characteristics
- Industry arrangements
- Problems emerging
- Drivers of reform
- Reform models
- Reform steps



Physical components of system



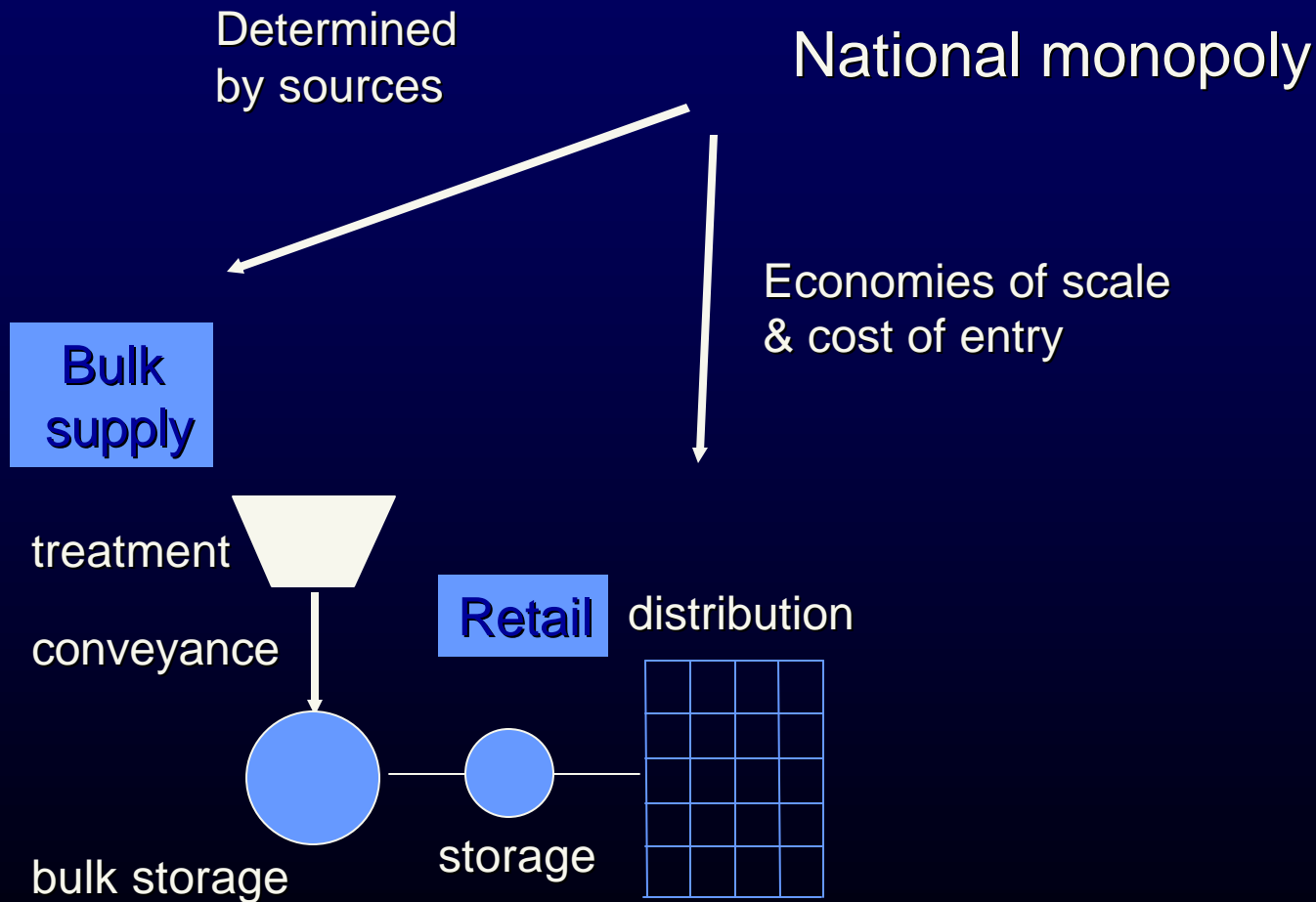
Characteristics of industry



National or regional regulatory function

- water resource management
- allocations (licences, trade, rights)
- discharge control (permits, pricing)

Characteristics of industry



Characteristics of industry

National monopoly

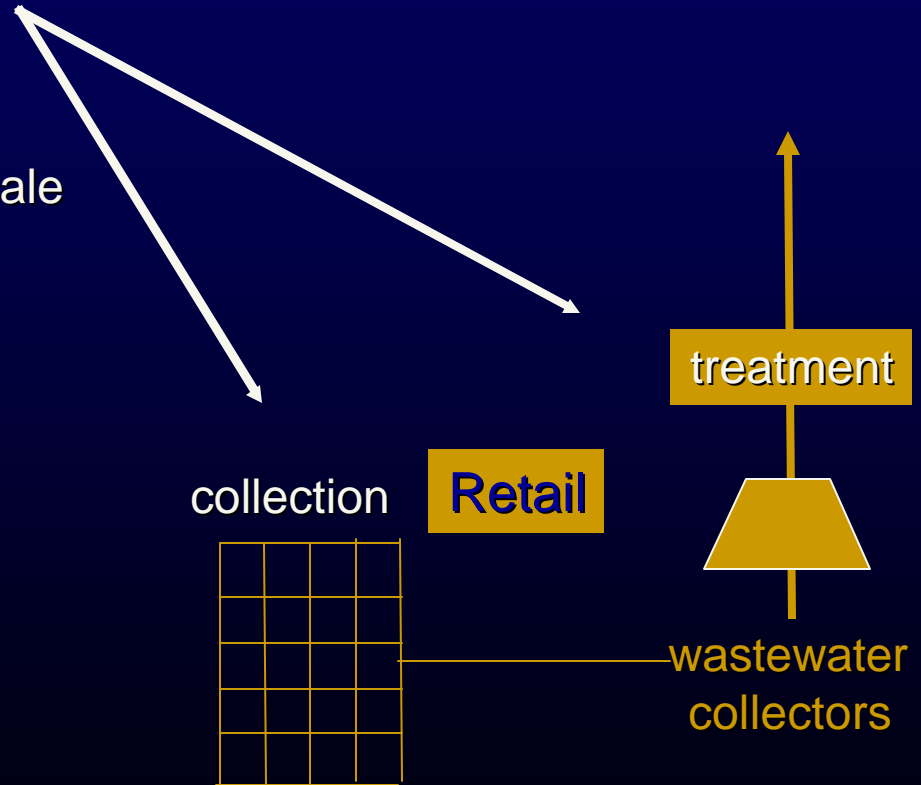
Economies of scale
& cost of entry

collection

Retail

treatment

wastewater
collectors



Characteristics of industry

Customer & support services
metering, billing, laboratories,
fleet, call centre etc



Some services can be competitive
e.g. metering, fleet

Industry arrangements

- diversity a key characteristic

- Wide diversity of institutional arrangements
 - municipal delivery (small to large scale)
 - utilities (city, regional, state-wide)
 - contracts

- Ownership
 - predominantly public ownership
 - National, regional or local (municipal)
 - private ownership
 - in perpetuity: rare (e.g. UK)
 - time limited: BOT, concessions, leases, management contacts

- Regulation follows industry structure
 - Independent dedicated water regulators rare



Industry arrangements

- historical trends related to ownership

- Early networks developed by private initiative
 - London, New York, LA etc; regulation non-existent or ah hoc.
- Taken over by local or national government to protect public interests (public health)
 - Delivery by public sector still the norm today
- Limits to public sector delivery (?):
 - **Ideological** (UK, Thatcher) – government debt
 - **Necessity** (low income countries) - capacity & financing; donor conditionalities
 - **Preference / persuasion** (Eastern Europe & low income countries – World Bank, donors)
- Long standing tradition of private involvement
 - French contracting model



BUT neither ownership nor industry structure is critical to success

- Both public and private ownership can be successful
- Industry structure can be diverse

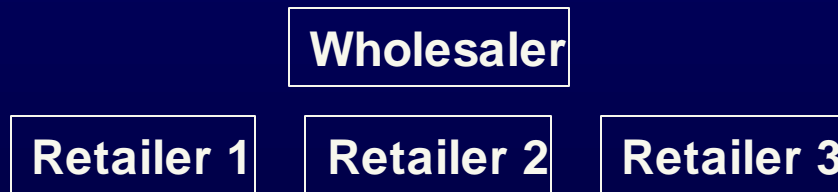


The four most success utilities in Australia have different industry structures ...

Source: Professor John Langford

Melbourne

Horizontal disaggregation
Comparative competition



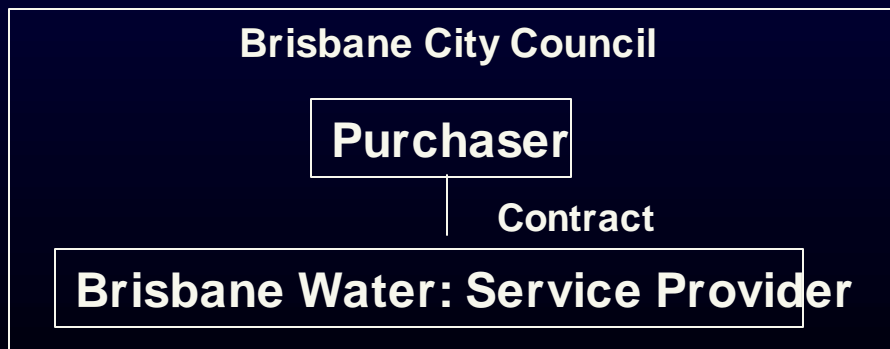
Hunter

Vertical integration



Brisbane

Internal Service Contract



Adelaide

External Service Contract



Problems emerging

“Government opportunism is the main problem for poor performance of utilities, even publicly owned utilities. Governments cannot credibly commit to financial sustainability in the water sector.”

Body of knowledge for regulators, 2003

Problems emerging

- Municipal delivery:
 - Fragmentation of delivery (diseconomies of scale)
 - Poor access to & use of technology
 - Unable to attract necessary skills
 - Unable to manage effectively
 - Inadequate investment
 - Poor management of assets
 - Impossible to regulate (absence of ring-fencing)

- Inefficient large public utilities
 - Scale may be too large (e.g. Brazil state utilities)
 - Poor governance arrangements
 - Ineffective regulation (lack independence)
 - Inefficient investments & asset management

- Grant seeking behaviour

- Risks and costs related to private concessions
 - Foreign currency risk (e.g. Buenos Aires)

Drivers of reform

- Macro-economic reform
 - Macro-economic crises cuts government grants
 - Grant/financing conditionalities (Australia)
- Access to capital (and MDG)
 - Utility reform often a specific condition for accessing finance directly for that utility
- Crises
 - Collapse of infrastructure (??)
(interruptions, sewerage in streets, health risks)
 - Debt
- Standards driven reform (e.g. EU)
- Desire for efficiency improvements (??)

Reform models

- Structure: not critical, can be diverse
- Ownership: not critical, can be diverse

BUT, for reform to be successful, the following essential principles must be respected:

- (1) Economies of scale and resource logic
- (2) Governance
- (3) Financial self-sufficiency & full accountability
- (4) Professional management & operational autonomy
- (5) Effective regulation
- (6) Performance benchmarking (public accountability)
- (7) Strategic asset management

Outcomes

Generic

- Professional management
- At scale
- Full accountability
- Industry best practice
- Financial sustainability

This means:

- Separation of provision from government
- Ring-fenced
- Effective independent regulation

Reform steps

- Process will depend on where constitutional responsibility lies (national or local levels)
 - Mandatory versus voluntary reform
- Clarify ownership
 - National versus local; public versus private
- Define governance arrangements
 - Sound corporate governance, expertise-based
 - Weaning water from government
- Accounting reform and ring-fencing
 - separate audited accounts essential
- Develop regulatory capability *beforehand*
- Leadership
 - Vision, strategic decision making
- Incentives
 - Especially important where local responsibility exists

Questions

- Drivers for reform
 - Are these the most significant?
 - Are they sufficient for reform to take place?
- Ring-fencing
 - Is this essential?
- Do services need to be aggregated? (regionalised)
- Should services be made arms-length from LG?
- Who should own utilities?
- What role for private sector?



Thank you

P•D•G

PALMER DEVELOPMENT GROUP