World Bank Conditionality in Water Sector Privatization

Cases from Ghana and the Philippines

June 2005
TABLE OF CONTENTS

Table of Contents ......................................................................................................................... i

List of Tables .............................................................................................................................. i

Acknowledgements .................................................................................................................... ii

Acronyms ................................................................................................................................... iii

1. Introduction .......................................................................................................................... 1

2. The Discursive Reform of Conditional Aid ........................................................................ 4
   2.1 The current culture of development-policy lending ...................................................... 4
   2.2 Selectivity and country ownership: a case for soft conditionality ................................. 6
   2.3 Conditionality in the World Bank’s water sector strategy ............................................. 8

3. Case Study: Ghana .............................................................................................................. 13
   3.1 Background .................................................................................................................. 13
   3.2 World Bank-funded water privatization ....................................................................... 17
      3.2.1 Rural community-based water supply ...................................................................... 18
      3.2.2 Privatizing the Ghana Water Company ................................................................. 19
   3.3 The role of the World Bank ......................................................................................... 23

4. Case Study: Philippines ..................................................................................................... 27
   4.1 Background .................................................................................................................. 27
   4.2 Experiences with water privatization .......................................................................... 30
      4.2.1 Metro Manila and the ‘corporate muddle’ of privatization ................................... 31
      4.2.2 Local government water privatizations ................................................................. 35
   4.3 The Role of the World Bank ......................................................................................... 37

5. Outlook on Conditional Water Privatization ..................................................................... 41

6. References ............................................................................................................................... 44

LIST OF TABLES

Table 1: Total Foreign Debt - Ghana - 1982-2002 ................................................................. 15
Table 2: HIPC Debt Relief Plan for Ghana - 2000 - 2009 .................................................. 15
Table 3: Ghana Water Company Tariff Rates - 1998-2003 .................................................. 22
Table 4: Total Foreign Debt - Philippines 1998-2004 (USD$ millions) ............................ 28
Table 5: Official Development Assistance in the Philippines - 1990-2002 ....................... 28
Table 7: World Bank Loans in Philippines Water Sector - 1990-2004 ............................. 38
ACKNOWLEDGEMENTS

The Canadian Catholic Organization for Development and Peace (CCODP) is pleased to acknowledge the contributors to this report.

The case study materials were prepared and reviewed in close collaboration with our partners in the Global South: Gyekye Tanoh and Yao Graham from Third World Network (Ghana case study), and Mae Buenaventura and her colleagues from Freedom from Debt Coalition (Philippines case study).

Nancy Alexander from Citizens Network on Essential Services shared her knowledge of the World Bank and water privatization.

Special thanks and acknowledgement are due to Marcia Chandra, graduate student in the Faculty of Environmental Studies at York University (Toronto, Canada), as principal researcher and lead consultant.

CCODP staff members Danny Gillis and Hélène Gobeil coordinated the preparation of the report and provided editorial oversight and supervision.

While all comments and inputs are considered valuable and gratefully acknowledged, the ideas and perspectives in this report are those of the Canadian Catholic Organization for Development and Peace (CCODP) and may not reflect the views of the above-mentioned persons or their affiliated organizations. CCODP assumes full responsibility for any errors or misrepresentations contained herein.
### ACRONYMS

<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
</tr>
<tr>
<td>ADR</td>
<td>Appropriate Discount Rate</td>
</tr>
<tr>
<td>APL</td>
<td>Adaptable Program Loan</td>
</tr>
<tr>
<td>BOT</td>
<td>Build-operate-transfer</td>
</tr>
<tr>
<td>CAS</td>
<td>Country Assistance Strategy</td>
</tr>
<tr>
<td>CWSA</td>
<td>Community Water and Sanitation Agency</td>
</tr>
<tr>
<td>CWSP</td>
<td>Community Water and Sanitation Project</td>
</tr>
<tr>
<td>DA</td>
<td>District Assembly</td>
</tr>
<tr>
<td>DBP</td>
<td>Development Bank of the Philippines</td>
</tr>
<tr>
<td>DFID</td>
<td>UK Department for International Development</td>
</tr>
<tr>
<td>DILG</td>
<td>Department of the Interior and Local Government</td>
</tr>
<tr>
<td>ERSO</td>
<td>Economic Reform Support Operation</td>
</tr>
<tr>
<td>ESAF</td>
<td>Enhanced Structural Adjustment Facility</td>
</tr>
<tr>
<td>FDC</td>
<td>Freedom From Debt Coalition</td>
</tr>
<tr>
<td>FFM</td>
<td>International Fact-Finding Mission</td>
</tr>
<tr>
<td>GWCL</td>
<td>Ghana Water Company Limited</td>
</tr>
<tr>
<td>GWSC</td>
<td>Ghana Water &amp; Sewerage Company</td>
</tr>
<tr>
<td>HDR</td>
<td>Human Development Report</td>
</tr>
<tr>
<td>HIPC</td>
<td>Heavily Indebted Poor Countries Initiative</td>
</tr>
<tr>
<td>IBRD</td>
<td>International Bank for Reconstruction and Development</td>
</tr>
<tr>
<td>IDA</td>
<td>International Development Association</td>
</tr>
<tr>
<td>IFC</td>
<td>International Finance Corporation</td>
</tr>
<tr>
<td>IFI</td>
<td>International financial institutions</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>IRA</td>
<td>Internal Revenue Allotment</td>
</tr>
<tr>
<td>ISODEC</td>
<td>Integrated Social Development Centre</td>
</tr>
<tr>
<td>JBIC</td>
<td>Japan Bank for International Cooperation</td>
</tr>
<tr>
<td>LBP</td>
<td>Land Bank of the Philippines</td>
</tr>
<tr>
<td>LGU</td>
<td>Local Government Unit</td>
</tr>
<tr>
<td>LWUA</td>
<td>Local Water Utilities Administration</td>
</tr>
<tr>
<td>MIGA</td>
<td>Multilateral Investment Guarantee Agency</td>
</tr>
<tr>
<td>MWCI</td>
<td>Manila Water Company Inc.</td>
</tr>
<tr>
<td>MWSS</td>
<td>Metropolitan Waterworks and Sewerage System</td>
</tr>
<tr>
<td>MWSS-RO</td>
<td>Metropolitan Waterworks and Sewerage System - Regulatory Office</td>
</tr>
<tr>
<td>NCAP</td>
<td>National Coalition Against the Privatization of Water</td>
</tr>
<tr>
<td>ODA</td>
<td>Overseas Development Assistance</td>
</tr>
<tr>
<td>OED</td>
<td>Operations Evaluations Department</td>
</tr>
<tr>
<td>PIDS</td>
<td>Philippine Institute for Development Studies</td>
</tr>
<tr>
<td>PPIAF</td>
<td>Public-Private Infrastructure Advisory Facility</td>
</tr>
<tr>
<td>PRGF</td>
<td>Poverty Reduction Growth Facility</td>
</tr>
<tr>
<td>PRSP</td>
<td>Poverty Reduction Strategy Paper</td>
</tr>
<tr>
<td>PSP</td>
<td>Private Sector Participation</td>
</tr>
<tr>
<td>PURC</td>
<td>Public Utilities Regulatory Commission</td>
</tr>
<tr>
<td>UN</td>
<td>United Nations</td>
</tr>
<tr>
<td>WDI</td>
<td>World Development Indicators</td>
</tr>
<tr>
<td>WSP</td>
<td>Water &amp; Sanitation Program</td>
</tr>
</tbody>
</table>
1. **INTRODUCTION**

1. A recent report jointly released by the World Bank, Asian Development Bank (ADB) and the Japan Bank for International Cooperation (JBIC) ranks infrastructure provision as the key challenge facing economic development and poverty alleviation in East Asia (ADB et al. 2005). The World Bank has further indicated its priority to support improvements to urban infrastructure in its Infrastructure Action Plan, setting out an intensively focused program in leveraging and directly investing in this sector (World Bank 2003c).

2. Particular attention is being paid to the role of water infrastructure in poverty alleviation, as well as economic development. The Bank\(^1\) estimates that an investment of USD $75 billion to USD $180 billion per year for the next 25 years in the water infrastructure of developing countries is necessary to meet poverty reduction goals (World Bank 2003d).

3. Recent studies and initiatives reflect a renewed interest by the World Bank and other international financial institutions (IFIs) in directly facilitating improvements in a sector that has largely been left to develop through market-oriented processes of water privatization, which the IFIs and the private sector advocated as the panacea to solving the growing crisis in access to services. Despite the documented failures of water privatization to meet expectations, and the cancellation of several large-scale water concessions with private utilities, the World Bank continues to pursue water privatization through a strategy involving enhancing the role of governments as facilitators, negotiators and financiers of private water utilities. These strategies are enveloped in discourse that lacks substantive and empirically-based debate regarding the purported benefits of private versus public, and fail to reflect citizen demands globally that water be kept publicly owned and operated.

4. Between 1981 and 1990, the World Bank was actively focused on providing water technology to developing countries during the United Nations-designated International Drinking Water and Sanitation Decade. However, progress was slow and the focus quickly turned to a direct goal of privatizing water services in accordance with the Bank’s restated economic goals. Ricardo Petrella, a leading water academic, believes the turning point to be in 1987, when a World Bank commissioned report was produced on private sector water participation, stating that the main obstacle to privatization was a political refusal on the part of governments (Petrella 2001).

5. Since then, almost all of the World Bank’s water lending projects have been conditional on some form of privatization, while little attention has been paid to enhancing the public sector. Between 1993 and 2002, World Bank loans to developing countries for infrastructure decreased by 50% while its investments in other sectors had increased, and the role of its financial institutions for enhancing private sector development – the International Financial Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA) - practically doubled (Kessides 2004). Huge and well-publicized water privatization projects were funded by the Bank throughout the 1990s. When these began to crumble in the first few years of the 21st century, the Bank changed strategy to address the principal issues of perceived risk and lack of economic incentives that had limited private sector investment. The principal limitation, noted by the companies themselves, was the unrealistic assumption that profit motivation would result in the private sector improving access to the poor.

---

\(^1\) The terms “World Bank” and “the Bank” are used interchangeably throughout this text.
6. The flight of several major transnational companies from their water utility investments in developing countries has occurred for three reasons: 1) the increasing number of high profile cancellations, signaling instability in the market; 2) reduction in investment interests, as investments in increasing access to the poor have proven to be less than lucrative; and, 3) an extreme shift in public opinion towards the supposed benefits of privatization after facing unsustainable water tariff increases and variable degrees of service quality (Hall 2003; Kessides 2005).

7. There are clear statements from water companies and proponents of water privatization that private investment in the sector is not attractive and that, where social goals are concerned, the private sector is unable to perform (Kessler 2004). A new environment of “precautionary investment” and a reduced desire by the private sector to assume the risks involved means that the World Bank must apply a new strategy for enhancing the quality of water infrastructure currently thought to be restricting economic growth in developing countries (Estache & Pinglo 2004).

8. Analyses of current World Bank strategies in the water sector indicate strongly that the ideology of private sector participation is overwhelmingly favored over publicly owned and operated utilities (Alexander 2002; Kessler 2004). Under the new rules of engagement, the Bank plans to encourage governments to increase incentives to the private sector through such measures as guaranteeing loans and foreign exchange risks, making regulation independent of government, transferring subsidies to the private sector for rewarding service performance, and being respectful of the profit-oriented needs of companies.

9. This hardly seems desirable for governments who not only still bear the financial burden of providing water for citizens, but now bear the risk of a private sector market that has proven to be unsustainable, unviable, and severely lacking in meeting social objectives. Yet water sector privatization is still occurring in developing countries in increasing rates, despite its poor track record.

10. Why are governments continuing to implement privatization programs instead of reforming their public water institutions to better serve social, environmental and economic objectives? Activists and NGOs monitoring the World Bank and other IFIs have identified donor aid conditionality as the principal factor for this phenomenon. Structural adjustment loans were used throughout the early 1990s to force governments to divest their centralized control over inefficient public utilities in the electricity, telecommunications, railway, and water sectors as part of macroeconomic restructuring to reduce budget deficits and ensure balance of payments of debt service (Vera 2000).

11. Although the use of structural adjustment loans has received intensive scrutiny by both civil society organizations and the IFIs themselves, studies demonstrate that utility privatization conditions continue to be a major tie to aid [Joyner 2004 (in ActionAid 2004)]. These conditions are no longer applied in the traditional forms they were during the 1990s, and the World Bank and International Monetary Fund (IMF) have undertaken measures to reform conditionality as a tool to ensure government compliance, including changes in official discourse as well as methodology.

12. The ‘new conditionality’ of water privatization is not easy to detect, as it is often structured through the use of financial loan instruments that are specifically tailored for each sector, and increased efforts to shelter conditionality from an increasingly observant and knowledgeable public. The attention currently being paid to government ‘ownership’ of public reform conditions also means that new forms of applying conditionality might be more
difficult to uncover, as IFIs find more discreet methods of applying pressure; for example, through technical assistance and advisory services.

13. In light of the experience with private sector participation in the water sector, the question remains as to why the World Bank continues to promote it as the solution to developing countries' problems. Perhaps more importantly, why are state and local governments of developing countries continuing to adopt private sector participation as the principal solution to meeting development objectives – as demonstrated in the cases of Ghana and the Philippines - despite previous failed and costly attempts, as well as strong public opposition?

14. The case studies in this report investigate the latter question, indicating that strong factors in the continued use of private sector ideology are both the 'hard' – ultimatum – and 'soft' conditions inherent in World Bank lending practices.

15. In both Ghana and the Philippines, intense structural adjustment programs throughout the 1980s left these countries highly indebted by the 1990s, when water privatization began to be ushered in as a solution to the 'water crises' (made worse through SAP conditions eliminating public sector spending).

16. In Ghana, water privatization has been explicitly tied to donor aid throughout the past decade, constituting a set of triggers within the Country Assistance Strategies and in achieving the completion point of the Highly Indebted Poor Countries Initiative.

17. In the Philippines, while the intense privatization program may have appeared to have been adopted freely by the government in the 1990s, the legacy of the structural adjustment programs and the increasingly high debt result in strong indications of non-traditional forms of conditionality.

18. These governments, faced with macroeconomic structural adjustments that have reduced public spending by the central government and increased responsibilities for infrastructure at the local level, are being encouraged to take up loans from the World Bank where the assistance and financial tools provided leave them no option but to lease their operations out to private bidders.

19. This report is primarily based on research of publicly accessible documents of the World Bank and related institutions, NGOs, and websites. The research was cross-referenced with local newspaper reports, as well as a critical review of academic journal articles. All financial figures, unless otherwise noted, are recorded in their original value as found in the referenced document.
2. THE DISCURSIVE REFORM OF CONDITIONAL AID

20. Conditionality is used by donor organizations to “increase the probability of prompt repayment of debt and sometimes even to ensure that the funds (including grants) do not support policies inconsistent with the values of the creditors” (Johnson 2005: 8). The 2000/01 World Development Report published by the World Bank stated that “aid has been shown to be more effective in promoting growth and poverty reduction in poor countries with sound economic policies and sound institutions – ineffective where these are lacking” (World Bank 2000:196).

21. Research throughout the 1990s to the present has generally concluded that the success of World Bank and IMF structural adjustment programs has been directly related to the policy environments of the recipient countries; that is, the degree to which the countries were willing to accept and implement the policies enforced by the lending institutions (Wasty & Johnson 1993; Killick 1997). Countries who had virtually been forced to accept conditions in return for aid generally did not commit significant resources to implementing the required reforms, while donors appeared to be reluctant to penalize them, resulting in a general agreement that the impacts on poverty alleviation have been minimal at best.

22. Since the late 1990s, however, there has been a flurry of reform on the use of conditionality through focused efforts to alter not only the process of achieving assurances of recipient compliance with loan conditions but to alter the discourse of conditional aid in order to facilitate public and government support for its application. The result has been an increased focus on ‘non-coercive’ measures of ensuring that countries are aware of and adopt World Bank-supported policy environments in exchange for aid.

2.1 THE CURRENT CULTURE OF DEVELOPMENT-POLICY LENDING

23. Traditional conditionality – or “ultimatum conditionality” (Mosley et al. (2004) – employed through structural adjustment loans throughout the 1980s and the early 1990s generally focused on short-term macroeconomic adjustments to improve balance of payments for foreign-assisted loans. The use of conditionality increased gradually, peaking in 1992 with an average of about 47 conditions per World Bank adjustment loan or credit (World Bank 2005b).

24. Until approximately 2002, each loan financed by the International Bank for Reconstruction and Development (IBRD) had between 27 and 40 legally binding conditions per agreement, while International Development Association (IDA) loans had slightly less – averaging 15 to 30 conditions per agreement. Since 2001, the average number of conditions has been steadily decreasing. By 2004, there was an average of about 20 and 12 conditions per loan, respectively. The change can be attributed to recent research and reforms on the use of conditionality, focusing on selectivity, streamlining, and ownership in order to improve aid effectiveness.

25. According to the World Bank, there are two reasons for applying conditions to loans, used as guides to ensure the Bank’s actions are accountable to both its donor and borrower countries, and based on economic rather than political or non-economic considerations (World Bank 2005b). The “development effectiveness rationale” ensures that aid is directly contributing to the development objectives of both the Bank and the recipient government. The “fiduciary rationale” ensures that the aid is used to directly contribute to the development objectives agreed upon within the loan agreement.
26. Conditions employed by the World Bank and other IFIs generally fall into three categories (ActionAid 2004). Prior actions entail policy or program changes that governments must – or be willing to - undertake before they can be eligible for IFI lending. Performance criteria refer to certain ‘trigger’ conditions that must be met in order to qualify for the further release of tranche funds. Outcomes are the intended goals of the loan and may not necessarily affect the release of funds but are used to judge the effectiveness of the overall aid program.

27. The World Bank recently reformed its structural adjustment program to reflect new policies for achieving aid effectiveness. The new guidelines (OP/BP 8.60), introduced in September 2004, officially renamed structural adjustment as “development policy lending” reflecting the new culture of “budget development” with the goal of supporting internally-induced reform rather than imposing prescribed policy models (World Bank 2005b). The new framework undertakes a programmatic approach, where performance and outcomes, rather than intended policy changes, are used as indicators of a country’s effective use of a loan.

28. From a critical point of view, the new terminology could be construed as a strategc way to diffuse the controversial and high-profile public debates that have arisen over the Bank’s use of structural adjustment, and the negative publicity it has garnered in response to the fact that many recipient countries were worse off than they had been two decades earlier.

29. The Bank employs several mechanisms to demonstrate accountability in loan procedures and legitimize both its conditions and actions to its Board and the public:

- **Country Assistance Strategy (CAS)** forms the strategic business framework and is meant to be a reflection and complement to the borrowing country’s own development objectives outlined in its Poverty Reduction Strategy Paper (PRSP).
- Annual report on the **IDA Country Assessment and Allocation Process** demonstrating the Bank’s choice of lending to countries based on their poverty index and Bank assessments of ‘good policy environments.’
- **Analytical and advisory services** produce diagnostic reports to support the monitoring and evaluation of outcomes for economic indicators, poverty assessments and environmental analyses.
- Ten **Safeguard Policies** are used to ensure that various non-economic principles are considered in policy and program development, including environmental assessments, indigenous rights, the uses of cultural property, and gender issues.

30. Currently, the World Bank and IMF are each undergoing internal conditionality reviews to assess how effectively these have been applied and to recommend reform to the processes involved. The IMF conditionality review was completed in early 2005, while the World Bank review is currently undergoing internal and public consultation processes with intentions to produce its findings in late 2005.2

31. There are two important focuses of this review called for by a joint committee of the IMF and World Bank. The first is a review of aggregate conditionality, as both institutions are concerned with streamlining conditions to produce more focused results. The other objective is to find ways in which the two banks’ lending strategies can be harmonized to minimize both overlapping and conflicting conditions. The World Bank is looking at the possibilities of redefining the term ‘conditionality’ to reflect the new discourse of development-policy

---

lending (World Bank 2005b). Terms that are being considered include “support for policy reform” or “results partnership.”

32. Processes of streamlining and harmonization, while theoretically working towards completing positive development objectives, need to be closely monitored. The streamlining of aid implies fewer and more focused conditions applied to each loan. However, it also implies that the conditions could be more intense in their objectives, pushing difficult-to-implement reforms and that they may also make it easier for donors to cancel aid if these conditions are not met to their satisfaction.

33. Harmonization of donor aid is desirable to prevent overlapping and conflicting programs and policies that often undermine the effectiveness of each loan (World Bank 2005b). There is a danger, however, of ‘cross-conditionality’, where donors align under similar policy and development objectives, making it difficult for borrower countries to access credit for alternative policies. It can also result in increased pressure for countries to adopt donor conditions or risk of losing all aid, as ActionAid (2004) noted for Ghana, where the UK Department for International Development (DFID), following the World Bank’s cancellation of loans, withdrew financing of seven million British pounds.

34. The World Bank and other donor institutions argue that these risks are minimized in the new culture of conditional lending, which places strong emphasis on selecting countries that have good policy environments, where the government and its citizens are favorable to reform; and on financing country-owned programs that have been developed free from external pressure and are expressions of a country’s favored strategy for enhancing development and poverty alleviation.

35. In this interpretation, the Bank’s CAS is intended to be based on and supportive of the recipient country’s own PRSP that has (ideally) been developed by a government operating as a legitimate representative of its citizens. These conceptual strategies of selectivity and ownership are intended to legitimize the Bank’s choices of loans and actions, and reduce or eliminate the need for conditions to secure compliance with loan agreements.

2.2 SELECTIVITY AND COUNTRY OWNERSHIP: A CASE FOR SOFT CONDITIONALITY

36. World Bank research on conditionality over the past few years has focused on efforts to increase borrower country ownership (World Bank 2005b). Country ownership, as defined by the World Bank and IMF, is assumed to exist based on two principles: 1) that representatives of the recipient country freely select the reforms to be implemented; and, 2) that the citizens accept the full responsibility for the outcomes of these country-owned reforms, thus legitimating and facilitating their implementation (Johnson 2005).

37. This means that citizens as well as foreign interests need to be convinced that the reforms being funded by the World Bank and IMF were designed by the (representative) governments and that the multilaterals are merely responding to the call of support for these internally-produced programs. It is suggested that, in the existence of full ownership by a recipient country, policy-based conditionality would not even be needed to ensure repayment of World Bank and IMF funds.

38. Efforts are also increasingly focused on the practice of selectivity, where recipient countries are chosen based on their level of poverty and ‘good’ governance, as a strategy to increase the effectiveness of aid. By selecting those countries thought to be operating under good policies, donor countries are assured more conducive environments for implementing requested reforms, maximizing usage of the funds and lessening the need to impose
conditions on loans. Thus, the use of selectivity can promote country ownership of programs as, theoretically, the countries themselves would already be implementing (or be preparing to implement) policies that are favorable to the donor.

39. The assumption that countries, whose socioeconomic conditions have led them to request aid and produce a PRSP, can fully own resulting programs of policy reform is highly controversial and arguably unrealistic. Buiter (2004) finds three principal reasons that a country with high debt might be willing to take part in the PRSP process: 1) a lack of access to private markets, meaning it needs external financial resources to finance development; 2) the need for expensive external expertise due to a lack of internal capacities or experience; and, 3) the need for external commitments to act as a signal to the market that a country is improving its domestic situation and on its way to progressive development. Selectivity essentially implies that countries whose policies do not conform to what is considered ‘good’ by the IFIs will have limited (or no) access to funding.

40. With greater focus on donor harmonization, the effect of not having the right policy environment would be compounded, as a country could risk losing access to any form of multilateral or bilateral aid. Thus, it would be reasonable to expect that countries, particularly those in high debt, would choose their reform programs strategically in order to gain access to foreign funds. While the World Bank claims that the PRSP process is intended to be proof of a country’s ownership of their reform program, it is highly doubtful that these policies arise free from indirect donor pressure.

41. Willem Buiter, chief economist at the European Bank for Reconstruction and Development, argues that country ownership is a useless term that cannot be said to reflect a people-supported or freely chosen policy regime (Buiter 2004). Indeed, the practice of governments agreeing to donor conditions in return for aid has mostly been undertaken ‘behind closed doors’ and without consultation with the public.3

42. Practicing selectivity to provide unconditional aid also poses problems for donors such as the World Bank, whose definitions of ‘good’ policies limit the range of possible recipients, leading to under-spending of aid budgets.4 A country may be selected as a recipient despite having the ‘right’ policies but having the possibility of developing these reforms with advice or direction from the donor agency. Thus, ownership becomes an ambiguous concept that can hardly be said to be fully free from donor pressure or be fully indicative of a country’s policy choices.

43. Mosley et al. (2004) assert that recent trends demonstrate that neither hard-core “ultimatum” conditionality nor selectivity have been methods favored by donors. Instead, an alternative method – the ‘new conditionality’ – has been applied, having three principal features:

- Multiple levels of commitment and withdrawal, where ‘good’ governments might receive support to policy reform, HIPC debt relief and social sectors, and ‘poor’ recipients might only receive social sector support or no support.

3 The ambiguity in ownership has not gone unnoticed by researchers of the World Bank or IMF. Johnson (2004) asserts that “the existence of constraints on the freedom to choose cannot be used to support an absence of ownership; indeed the impact of constraints on choice cannot be easily estimated” (p.4). He suggests key strategies to promote the ‘idea’ of ownership both internally and externally: the consultation of civil society organizations in order to obtain support and legitimize the idea that there is citizen support; and the use of safety-net programs, such as social funds, to “stave off social unrest and obtain political support for what could be a large portion of the population” (p.8).

4 Mosley et al. (2004) note that this would be undesirable for the donor institution who would risk losing influence in both the developing country and the donors’ own governments.
The increasing use of alternatives to government-to-government service provision where communities, NGOs and the private sector become significant actors to work around government.

Pressures exerted through social and political, rather than merely economic, investments to increase social capital, which is generally thought to lead to economic growth.

44. The ‘new conditionality’ described by the authors has occurred under conditions where “donors tended to initially tolerate short-term deviations from targets as trust was built up but later increased pressure on recipients to meet increasingly jointly agreed-upon targets. This tendency was often combined with invitations to recipients to frame their own definitions of pro-poor expenditure within the general context of Poverty Reduction Strategy Papers” (Mosley et al. 2004:229). Thus, through a process of building trust and dialogue, the World Bank can direct a country to the ‘right’ policy development choices, and then invite it to take ownership of proposed reforms through the PRSP, which then validates the proposals and conditions in the CAS.

45. The unilateral support for country ownership, both internally and externally, and the strong opposition to conditional lending that has grown in light of the last two decades of failed aid, means that IFIs such as the World Bank can no longer rely on direct conditionality as a tool for ensuring that governments agree to imposed reforms. Combined with the considerations on the limitations of ownership (outlined above), the use of indirect pressure – or soft conditions – to obtain desired reforms becomes a key factor in the ‘new conditionality.’ The World Bank can use its embeddedness in its analytical research and technical assistance services provided directly to recipient countries “allow[ing] the donor to influence policy without imposing conditionality, and hence without coercion” (Johnson 2005:11). The World Bank calls this type of assistance “additionality”, rather than conditionality, as these services do not constitute legally identified conditions (World Bank 2005b). In Ghana, for example, technical assistance accounts for an estimated USD$14 billion per year – one-quarter of its total overseas development assistance (ODA) (ActionAid 2004).

46. For countries whose socioeconomic conditions often place them in positions where they lack the technical experience and capacity to effectively develop and evaluate all reform possibilities, the reliance on World Bank expertise can inevitably produce reform programs that are inherently similar to the donors’ desired policies. The research produced by the World Bank, as well as the discourse employed in its public statements and strategy papers, also serve as soft conditions to advise recipient countries of the Bank’s position in terms of alternatives to its favored policies.

2.3 CONDITIONALITY IN THE WORLD BANK’S WATER SECTOR STRATEGY

47. In 2002, an estimated 14% of the World Bank’s loan portfolio constituted water-related loans (Alexander 2002). Since then, however, the Bank has embarked on a stronger program of investing in water infrastructure in developing countries as a solution to poverty alleviation and economic development, and investment directed towards the sector is

---

5 According to the World Bank’s definitions, conditionality “denotes the set of explicit conditions upon which the Bank disburses under development policy lending, and which are listed as legal conditions in the Bank’s Loan Agreements” (World Bank 2005b:4).
expected to increase. Thus, the adoption of ‘good’ policy reform and program implementation in the water sector are significant factors in securing World Bank financing.

48. Analyses of World Bank discourse and strategies identify ‘good’ policy as synonymous with private sector participation in water utilities, where public utilities are delegated a minor role, based on a perceived lack of capacity to improve access to water and sanitation services. Instead the public sector is reformed into facilitators, regulators and subsidizers for the supposedly ‘efficient’ private sector.

49. The principal feature of water sector reforms throughout the world is the significance given to full-cost recovery. Public utilities, particularly in developing countries, have traditionally been found to operate less than efficiently, with limited capacities to leverage financing for capital investments and high reliance on government subsidies that, in practice, are often applied regressively, benefiting the wealthy more than the poor. The private sector was proposed as a solution, based on its supposed ‘economies of scale’ resulting in lower overall tariffs, and its distance from politics, allowing the private sector interests to impose tariff collection where governments have been unwilling.

50. Kessides (2005) argues that the choice to impose cost-recovery is essentially a pro-poor policy, based on his view that those impacted by higher prices are the middle and high income classes. This assumption pays little attention to the proportional costs of higher tariffs relative to income – in developing countries, where the majority of the population lives with less than USD$2 per day, higher prices entail a significantly higher increase in the proportion of daily income spent on water. Most often there is a concurrent strategy to reduce government spending, entailing a reduction or elimination of progressive subsidies. Studies also demonstrate that the cost of infrastructure increases in poorer countries in response to economic and political instability (Estache & Pinglo 2004). The inability of the poor to pay for full-cost water seriously undermines the benefits to private sector participation in the water sector.

51. The private sector’s reliance on profit as incentive has meant that capital investments to increase access to the poor, who are essentially unable to pay, have been ignored. Although most private sector agreements have been negotiated on the basis of the winning company’s bid of the lowest tariff, tariffs have soared in response to macroeconomic instabilities affecting foreign exchange rates, inadequate or lack of technical capacity to regulate tariff increases, companies’ demands that they maintain an appropriate level of profit (though what is deemed ‘appropriate’ is often defined by the companies themselves), and governments’ fears of scaring off private investment by not conforming to private sector demands.

52. Tariff limits are intended to “generate an incentive for cost-reduction by limiting the amount by which the utility can increase prices; [however] if the price cap is renegotiated frequently, it becomes little better than standard cost-of-service regulation, which has proven difficult, as it requires that the regulator have enormous information about the firm’s cost structure and affects the firm’s investment incentives” (Clarke et al. 2004:7). On the other hand, the private sector claims that they should not have to bear the financial costs of inadequate regulation and unstable political climates, and that, without security of sustained profit, it is not worth the risk in investment. Thus, the poorer the country - the higher the risk - the higher the cost of capital – with the end result being higher tariffs.

---

53. Research further reveals how profit-oriented private companies can undermine the purported benefits of efficient resource allocation. World Bank researchers have argued that it is not uncommon for companies to represent their accounts with the minimum possible net profit, particularly in situations where there are tariff limits set by local regulators (Estache & Pinglo 2004). Through "creative accounting games", companies can end up declaring losses in host countries yet declare dividend profits at home. For example, consultants sourced from company headquarters overseas often get counted as an expense by the private utility in the developing country, however, are considered as revenue at headquarters.

54. The implication is that "the foreign company ends up having a guaranteed minimum return on equity, which in the host country is reflected in the revenue requirements used to assess the tariff level needed to cover the cost of capital, but is ignored in the revenue sources of the operator. In other words, the investors make money twice on this specific component of the deal" (Estache & Pinglo 2004:19). Thus, a high degree of competency is required by local regulators to monitor and evaluate private utilities, which is inevitably related to their ability to gain access to accurate information provided by the profit-motivated private sector.

55. The private sector continues to be advocated by the World Bank as the principal solution to resolving the huge investments needed to improve water supply and sanitation access to the world’s poor, as called for by the UN Millennium Development Goals. However, the new strategy entails a stronger role for the public sector to facilitate private investment and ‘share’ the risk. The World Bank has published several sector strategies providing details on innovative financial instruments and tools the public sector can use to convince the private sector to operate their public utilities. Some examples include automatic tariff adjustments, independent regulatory boards, government guarantees for foreign loans, leveraging of domestic financing, and public subsidies to award performance and provide incentives to improve services to the poor (World Bank 2004e).

56. There is also general consensus that the prospects of the private sector for improving sewage and sanitation infrastructure are limited, and that the public sector should be prepared to provide the capital investments necessary. This requires heavy investments in technical assistance to develop the capacity of the public sector to manage these new roles effectively. As Kessler notes, “while the use of subsidies to support struggling public sector utilities was invariably characterized as fiscally irresponsible, using public resources from the same government to lure hesitant private firms becomes an innovation in development assistance” (2004:9). This same conclusion can be extended to the entire set of public sector ‘solutions’ for private sector participation in water infrastructure, as they are some of the same conditions that would be necessary to produce effective public water utilities.

57. Recent World Bank research based on a comprehensive study of private and public utilities has demonstrated that there has been no difference in the degree of performance improvements or service coverage to the poor between the two management models (Clarke et al. 2004). Kessides notes that “the fact that state ownership is flawed does not mean that privatization is appropriate for all infrastructure activities and all countries” (2005:89). Thus, the idea that private sector participation is the most logical solution for the water sector in developing countries does not appear to be based on empirical evidence, since experience has demonstrated that it has been both as disastrous and as beneficial as public utilities.

58. The study by Clarke et al. (2004) failed to compare or analyze the full costs and benefits of managing the utility both privately and publicly. It would be useful to provide
evidence whether all the public sector inputs necessary to sustain private sector participation (e.g. subsidies, regulation, legal fees from costly lawsuits) are less than all the inputs necessary to improve public sector management of water resources. In order to effectively and critically evaluate the options in water sector reforms, studies need to focus on information that demonstrates the maximum possible social and economic benefits, particularly in terms of alleviating poverty.

59. Why are state and local governments of developing countries continuing to adopt private sector participation as the principal solution to meeting development objectives, despite previous failed and costly attempts as well as strong public opposition? World Bank and other IFI conditionality play strong roles. And despite strong public statements and structural policy changes regarding the use of conditions in loans by the IFIs, the ‘new conditionality’ requires an increased reliance on soft conditions to push for desired ‘good’ reform, including water sector privatization.

60. The use of soft conditionality – or “additionality” – can provide strong enough indication to developing countries in need of assistance that there exist almost no opportunities to improve public sector water utility performance from World Bank loans. This is primarily evident in the discourse inherent in the Bank’s public statements and research, which frequently criticize public utilities while ignoring the failures of private utilities on almost the same grounds.

61. An internal evaluation of the World Bank’s performance in water and sanitation indicates that not only was performance poor, but it was “unclear to what extent [the Water & Sanitation Program] contributed global knowledge and best practices [since the early 90s] that were independent of the prevailing Bank’s views on private-sector development – either to the Bank’s own operational policy dialogue and advice to its client countries, or directly to the Bank’s clients” (OED 2004:28).

62. While the Water & Sanitation Program (WSP) provides in-kind technical assistance to developing countries, its performance has never been independently evaluated. The Public-Private Infrastructure Advisory Facility (PPIAF), which provides free Bank-executed technical assistance to facilitate private sector involvement in sectors including water, has a very good evaluation process of its outcomes. Yet the OED report concludes that there is no significant evidence that the poor, who are declared ultimate beneficiaries, are benefiting from these programs and projects.

63. A recent policy guidance document prepared to advise World Bank staff on public and private sector roles clearly indicates the options that are available to present to developing countries making use of the Bank’s technical assistance for water reforms (World Bank 2004e). While the document attempts to provide some balance by discussing the possibilities for public sector utilities, it is careful to be clear that the extent to which a public sector utility can access Bank financing “will depend on an assessment of its financial strength and past operational performance” (World Bank 2004e:15). Meanwhile, if a private sector utility is considered by the government in question, the same document offers a comprehensive list of possible support in the form of grants, tools and advisory services that the government willing to reform can access. It also includes assurances of coordination at all World Bank levels to ensure success of the privatization reform process. Aside from WSP, these advisory services include the PPIAF, IFC and MIGA, which provide advice for private sector involvement.

64. One section of the document discusses past experience with public sector utilities, outlining their deficiencies, yet the discussion of the private sector offers no similar critical analysis. There is no attempt to qualify or quantify the motives for advocating private sector
participation or explain how it will “generate an outcome that yields the highest benefits to consumers” (World Bank 2004e:21).

65. A brief review of World Bank-produced research within WSP reveals almost no research on reforming public utilities, providing strong indication that Bank staff may not have the experience to advise and support governments wishing to retain public sector utilities. Yet, though it is clear that any significant level of support is only available for private sector participation, the Bank’s guidance policy for the sector indicates that the choice of which strategy to employ is completely the responsibility of the reforming government; this thus serves as a qualifier to its commitment to support government-owned programs.

66. Yet, as noted above, governments in positions wherein they need foreign assistance, debt relief and technical advice, are likely to conform their strategies to match those supported by the donor institutions – particularly in the current climate of increased harmonization and selectivity resulting in limited alternative sources of financing. With such clear messages from the World Bank’s strategies, research, communications and discourse, it is highly unlikely that there is much freedom in choice – it is either privatize or lose access to desperately-needed funds.
3. CASE STUDY: GHANA

67. By World Bank estimates, Ghana is one of the few countries with the potential to achieve positive results in Africa, due to its economic potential and strong social capital, as well as its “ambitions to achieve middle-income status within one generation, driven by private sector-led growth” (World Bank 2004c:1).

68. In the early 1980s, Ghana was considered to be one of the most promising African countries for economic and social development, prompting the World Bank and IMF to embark on an ambitious structural adjustment program. Privatization of the Ghana national water utility has been a prime objective for over a decade. However, despite the World Bank’s claims of country ownership, prior to 2001, the government did very little to facilitate water privatization of its urban water utilities. Rural communities, however, underwent small-scale community-based privatization efforts. A new government in 2001 was forced to apply for enhanced debt relief from all its donors, a significant portion of which was owed to the World Bank. Backed into a corner, with water privatization as one of the main conditions, the government has reinstated the privatization project, expecting bids in 2005.

3.1 BACKGROUND

69. By 1981, when a military coup was staged by Jerry John Rawlings, placing the country under authoritarian rule, Ghana was in financial disarray with non-functioning institutions and collapsed infrastructure. Beginning in 1965, Ghana had been approaching the World Bank and IMF for support; however, there had been little success, primarily due to internal opposition to IFI participation and lack of compatibility with World Bank and IMF philosophies, in some cases leading to government overthrow (Boafo-Arthur 1999).

70. The Rawlings administration prompt agreements with the World Bank and IMF for structural adjustment support, which initially received popular support, proved to have disastrous results. The fiscal austerity measures imposed by the IFIs created huge unemployment, drastic devaluation of the cedis and reductions in public sector spending for education and infrastructure (Jeong 1995). Mounting public opposition, particularly from labor unions, led the government to implement democratic elections in 1992 in which Rawlings won majority rule. It was not until late 2000 that the Rawlings government was voted out of office, and John Agyekum Kufour became President of a country that was now in the deepest debt it had been in after almost twenty years of World Bank structural adjustment. Within months, the government announced that it had requested debt relief through the Heavily Indebted Poor Countries Initiative (HIPC).

71. In 1992, after the elections resulted in political unrest damaging the macroeconomic stability the IFIs had worked hard to create, the IMF withdrew its support. This lasted until 1995, when the Rawlings government instituted an ambitious medium-term fiscal plan under a new ESAF arrangement. The elections in 1996 created havoc again, however, and this time both the World Bank and IMF withdrew their funding until the government had managed to limit domestic expenses and had reduced the inflation rate by 50% (IDA/IMF 2002).

72. Once convinced that the government was committed to completing previously delayed reforms, the World Bank approved the Economic Reform Support Operation (ERSO

---

7 World Bank support for Ghana is currently fully financed through IDA.
8 There was much opposition to the results, however, with many claiming that the elections had been rigged (Jeong 1995).
in 1998, calling for an intense divestiture program of the state’s public assets, including liberalization of the cocoa sector. By the end of 2000, 255 state-owned enterprises had been fully or partly privatized, and further drastic reforms had been undertaken to reform the public sector.

73. In May 1999 the IMF’s ESAF (from 1995) was replaced with a Poverty Reduction Growth Facility (PRGF), and the World Bank approved another adjustment loan (ESRO II) based on continued privatization reforms in the cocoa, energy and banking sectors (IDA/IMF 2001). By 1999 the macroeconomic situation appeared to have been stabilized once again. However, later that year, falling prices for gold and cocoa (the major exports of Ghana), and rising petroleum prices created conditions of trade shock, resulting in a build-up of foreign debts, high depreciation of the exchange rate, and high inflation through to 2000.

74. The World Bank blamed the poor ability of the economy to recover on the country’s delay in adjusting fiscal and monetary policies called for by the structural adjustment loans. After the government tightened public spending and increased the VAT rate, a second review of the PRGF was completed in August 2000, but the government was unwilling to implement some of the measures. By the time of the national elections in December, the IFIs had pulled out of the financing it had earlier promised. The Rawlings government had been offered the HIPC status earlier in 1999, however, according to the World Bank, the government had not felt it was in their best interests at the time (IDA/IMF 2001).

75. The new government came into power in 2001 and soon after applied for HIPC debt relief by agreeing to a package of fiscal measures that included doubling petroleum prices, raising taxes, decreasing public spending, and implementing water and electricity tariff increases, prompting a third review of the PRGF and a one-tranche adjustment loan from the World Bank (ESRO III).

76. The structural adjustment loans implemented from the 1980s have sponsored the stabilization of macroeconomic factors at the expense of investments in social and structural sectors, and have not reduced Ghana’s susceptibility to external shocks, resulting in only higher debts as the government continued borrowing. In general, there have been factors of progress in terms of some macroeconomic indicators such as annual growth rate, services and inflation; the latter was reduced to 9.2% by the early 1990s from 122% in 1983 (Boafo-Arthur 1999; IDA/IMF 2001).

77. However, at the same time, socioeconomic indicators proved to be harmful for the general population, particularly the poor, due to huge wage cuts, reductions in employment, and limitations on public spending in order to service the debt. Real wages dropped by 50% during the 1980s, and extreme devaluation of the cedi relative to the dollar from 2.75 in 1983 to 390 in 1991 resulted in high interest rates and limited opportunities to obtain credit (Jeong 1995).

78. By 2000, Ghana’s debt to export ratio was 160%, while its debt service to export ratio was 20.8% (Moss & Chiang 2003). Ghana owed money to 34 creditors in 26 countries. By the time the Kufour government came to power, Ghana had a total public foreign debt estimated at USD$3.8 billion (in 2001 net present value) – a debt service equivalent to 558% of government revenues, 152% of exports, and 77% of GDP.9

79. In 2002, Ghana’s external debts amounted to USD$7,338 million, 60.5% of which was owed to multilateral donors. The IDA/World Bank accounted for 78.1% of the

---

9 To qualify for the HIPC Initiative countries must meet the minimum thresholds of 250% debt service to government revenues, and 150% of debt service to exports.
multilateral loans – or almost half of Ghana’s external debts (Table 1) – making it the single largest and most influential lender in the country.

**Table 1: Total Foreign Debt - Ghana - 1982-2002**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total foreign debt</td>
<td>1,484</td>
<td>4,460</td>
<td>6,734</td>
<td>7,338</td>
</tr>
<tr>
<td>World Bank</td>
<td>256</td>
<td>1,718</td>
<td>3,178</td>
<td>3,476</td>
</tr>
<tr>
<td>World Bank/total foreign debt (%)</td>
<td>17.3%</td>
<td>38.5%</td>
<td>47.2%</td>
<td>47.4%</td>
</tr>
<tr>
<td>Total debt service</td>
<td>111</td>
<td>318</td>
<td>314</td>
<td>211</td>
</tr>
<tr>
<td>World Bank</td>
<td>17</td>
<td>35</td>
<td>63</td>
<td>32</td>
</tr>
<tr>
<td>World Bank/total debt service (%)</td>
<td>15.3%</td>
<td>11.0%</td>
<td>20.1%</td>
<td>15.2%</td>
</tr>
<tr>
<td>Total debt/GDP</td>
<td>36.8</td>
<td>69.6</td>
<td>126.8</td>
<td>119.3</td>
</tr>
</tbody>
</table>

Source: World Bank (2004c)

80. After obtaining the HIPC Decision Point, the World Bank agreed to provide interim debt relief in the amount of USD$98 million, and promised to forgive 67% of Ghana’s outstanding and incurred debts from 2000 to 2020 (IDA/IMF 2002). The HIPC Completion point\(^{10}\) was reached in July 2004, after Ghana had complied with all but one of the conditions that the government had agreed to meet.

81. As of March 2005, Ghana has received USD$2,186 million in debt relief (in net present value) (IDA/IMF 2005). Of the total commitment of USD$1,445 million in debt service reduction, USD$139 million has been delivered. Table 2 (below) outlines the debt relief plans of the World Bank and IMF.

**Table 2: HIPC Debt Relief Plan for Ghana - 2000 - 2009**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>WB debt service before HIPC relief</td>
<td>56</td>
<td>63</td>
<td>65</td>
<td>76</td>
<td>87</td>
<td>99</td>
<td>132</td>
</tr>
<tr>
<td>WB debt service after HIPC relief</td>
<td>56</td>
<td>63</td>
<td>32</td>
<td>31</td>
<td>39</td>
<td>46</td>
<td>63</td>
</tr>
<tr>
<td>World Bank debt relief</td>
<td>-</td>
<td>-</td>
<td>33</td>
<td>45</td>
<td>49</td>
<td>53</td>
<td>68</td>
</tr>
<tr>
<td>IMF debt service before HIPC relief</td>
<td>39</td>
<td>68</td>
<td>17</td>
<td>22</td>
<td>40</td>
<td>48</td>
<td>23</td>
</tr>
<tr>
<td>IMF debt service after HIPC</td>
<td>39</td>
<td>68</td>
<td>8</td>
<td>5</td>
<td>23</td>
<td>23</td>
<td>22</td>
</tr>
<tr>
<td>IMF debt relief</td>
<td>-</td>
<td>-</td>
<td>9</td>
<td>17</td>
<td>17</td>
<td>25</td>
<td>1</td>
</tr>
<tr>
<td>Debt service paid</td>
<td>533.2</td>
<td>242.6</td>
<td>267</td>
<td>161</td>
<td>140.9</td>
<td>135.1</td>
<td>-</td>
</tr>
<tr>
<td>Debt service/exports (%)</td>
<td>21.9</td>
<td>10.1</td>
<td>10.2</td>
<td>5.2</td>
<td>4</td>
<td>3.5</td>
<td>3.2</td>
</tr>
<tr>
<td>Debt service/govt revenue</td>
<td>78.1</td>
<td>25.7</td>
<td>39.1</td>
<td>17.1</td>
<td>13.5</td>
<td>8.7</td>
<td>6.3</td>
</tr>
<tr>
<td>Debt service/GDP (%)</td>
<td>10.7</td>
<td>4.6</td>
<td>4.3</td>
<td>2.1</td>
<td>1.6</td>
<td>1.3</td>
<td>1.2</td>
</tr>
</tbody>
</table>

Source: IDA/IMF 2005

Note: The 2006-2008 columns were not included here for simplicity. The World Bank and IMF each continue to contribute debt relief during these 3 years.

\(^{10}\) As of April 2005, completion points had been reached by 15 of 27 countries that had achieved HIPC debt relief decision points (IDA/IMF 2005).
82. Out of 177 countries, Ghana is ranked 131st based on the Human Development Index (UN 2004b). The 2002 population was 20.5 million, growing at a rate of 2.1% per year. GDP per capita in 2000 was USD$290. According to Ghana statistics, poverty has decreased from 51.7% to 39.8% for the country, although the average masks the geographic unevenness of poverty – urban poverty was reduced from 27.7% to 19.4%, while rural poverty remains high at 49.5% down from 63.6% in 1991 (IDA/IMF 2002).

83. The most densely populated regions of the country are the Upper East Region, and along the coast between Accra and Kumasi. The Northern Region and northern half of Brong Ahafo are much less densely populated, with the rural population scattered across the landscape. The savannah region in particular (Northern, Upper East and Upper West region) has been virtually neglected experiencing little impact on poverty levels; in fact, the percentage of the population living below the poverty line in the Upper East region actually increased from about 66.9% in 1991 to 88.2% in 1999.

84. There have been substantive improvements in average levels of access to water services within the country. In 1992, water supply coverage was 28% in rural areas and 76% in urban areas; sanitation coverage was about 29%. By the end of 2001, rural water supply coverage had increased to 41%, although in urban areas it had decreased to about 70% (IDA/IMF 2002), reflecting high rates of urban migration with a slower rate infrastructural improvement.

85. Yet, these average figures mask the high levels of inequality between the rich and poor regarding access to these services. Clarke & Wallsten (2002) demonstrate that, in 1998, 64.75% of households whose male head had secondary education had access to piped water, compared with 25.6% of those households whose male heads had no education. Data such as this collected over time might produce stronger indications of whether improvements to basic water services access have been favoring poor communities, thus enhancing health and poverty alleviation.

86. Health issues are a significant problem in Ghana, although there have been some measures of improvement over the past decade. Infant mortality fell from 85 to 57 per 1,000 live births between 1991 and 2002, and life expectancy rose three points, to 58 years of age.

87. Water-related diseases – particularly cholera and guinea worm – continue to plague various regions of the country. Reported cases of individuals with cholera increased from 254 to 3,525 cases between 1998 and 1999 (FFM 2002). Ghana is second only to the Sudan for the highest reported cases of guinea worm, constituting 5,436 (35%) of the total reported cases in Africa between January and June 2003 (CDC 2003). Outside of Sudan, Ghana constituted 75% of the total number of cases during the same period, with a large number originating in only 15 districts, particularly in the northern regions.

88. Although the total number of reported cases has increased significantly over the years, it is noteworthy that this has most likely been a direct result of increased surveillance efforts that effectively increase monitoring and reporting, particularly in rural areas, where the disease can often go untreated due to lack of health services. Since mid-2002, the CDC reports that there have been enhanced surveillance, investigations and interventions, with the mobilization of about 6,000 village-based personnel.

---

The human development index (HDI) measures average achievement in three basic aspects of human development – a long and healthy life, knowledge, and a decent standard of living (UN 2004b).
89. Although general access to safe water services appears to have increased, the continued persistence of these diseases indicates both a geographic unevenness in investment, and a need to pursue higher degrees of health and water service improvements, particularly in the regions most affected.

3.2 WORLD BANK-FUNDED WATER PRIVATIZATION

90. Ghana’s water services have traditionally been managed as a national utility. Rural water supplies have been mainly groundwater sources – wells, boreholes, and simple community taps or distribution networks - while about 50 urban areas are supplied by an integrated distribution system.

91. In 1958, the Water Supply Division became an entity responsible to the Ministry of Works and Housing, headquartered in Kumasi. The Ghana Water and Sewerage Corporation (GWSC) was established in 1965 and, until 1994, was responsible for the provision, distribution and conservation of both urban and rural water supply, as well as sewerage systems.

92. In 1994, at the suggestion of World Bank consultants, responsibilities for the urban and rural service provision were separated, with rural areas covered under the autonomous Community Water & Sanitation Agency. There was also a separation of water supply and sewage services, in order not to burden the former with the fiscal responsibility for costly improvements in sanitation. The GWSC was converted to a limited liability company – Ghana Water Company Limited (GWCL) – a few years later. The Public Utility Regulatory Commission (PURC) was created in 1997 as an independent body responsible for regulating and overseeing water services provision, including setting water tariffs and approving drinking water quality.\(^\text{12}\)

93. The National Community Water Supply and Sanitation Policy and Strategic Investment Program has recently been adopted under the principles of demand-driven service expansion and community ownership, with requirements that communities make upfront capital contributions of 5% to construct the facility (UN 2004a).

94. The Water Resources Commission, made up of technical representatives of stakeholder groups, was set up in 1996 to manage the country’s water resources and coordinate the various government policies and sectors. It has recently begun implementing a comprehensive communications strategy to promote sustainable use of water resources.

95. Between 1969 and 1989, four World Bank loans invested USD$51.5 million into the GWSC to improve supply and sewerage networks, provide institutional strengthening, technical assistance, and to install rural solutions to infrastructure, such as hand-pumps.

96. The Water Sector Rehabilitation Project - begun in 1989 and completed in 1998 – was funded by various partners, including the World Bank (25%), and sought to rehabilitate 34 urban water supply centers and rehabilitate 57 of the non-operating urban water systems (there were an estimated 208 of these), as well as improve the institutional operations of the GWSC (World Bank 1999).

97. The project was rated unsatisfactory in meeting development objectives; the satisfactory elements included a staff reduction down to 3,000 employees (from 4,500) and tariff increases. In 1986, the government had withdrawn its subsidy support for the GWSC through a law instituting cost recovery. Tariffs were instituted in rural areas for the first time, at

---

\(^{12}\) PURC also regulates the electricity sector. Information can be found on its website: www.purc.com.gh.
and urban tariffs increased by about 5%. Until 1994, tariffs had been increasing at a rate of about 20% per year.

3.2.1 Rural community-based water supply

98. In 1994, there were distinct efforts to privatize Ghana’s water system. The first step came through separating the non-revenue generating rural operations from the potentially lucrative urban operations. Local politics divide Ghana into five cities, 36 towns, and 110 district assemblies (DAs). The recommendation to divide responsibilities for servicing these areas was made by the World Bank in order to “commercialize” the GWSC so that it could begin to generate enough revenue to cover its costs.

99. To assist the rural sector, the Bank implemented community-based water systems in 30 small town centers, and installed 1,000 new water points through a USD$21.96 million loan for the Community Water Sanitation Project (CWSP) (World Bank 1999). The effort promoted the use of the private sector for goods and service provision, while advocating for greater community participation through a requirement of 5% upfront financing. The intention was to provide a demonstration of the benefits of the National Community Water Supply and Sanitation Policy that World Bank consultants had proposed, and that had initially been instituted.

100. The Second CWSP was initiated in 1998 and completed by the end of 2004. Forming the first part of a 9-year USD$80 million APL, the objective was to expand rural water and sanitation service to about 550,000 people in Brong Ahafo, Ashanti, Upper East and Upper West regions, with waterpoints, piped systems and sanitation facilities. The project explicitly identified the private sector as the provider of all goods and services, with the government acting as a facilitator.

101. The construction would take place as a demand-driven approach, with communities committing 5-10% of the project costs. In 2000, the World Bank funded a PPIAF TA grant to investigate the feasibility of PSP in the rural water supply sector through three pilot projects (PPIAF 2003a). Effectiveness is measured in the short-term by local private sector involvement and in the long-term by improvements in service coverage. The recommendations included: establishing sinking funds for sanitation and major capital investments to encourage the PSP process; and provide incentive taxes, as well as soft credits and bulk imports of supplies.

102. There were three significant problems with the rural aspect of the water supply system. The CWSA, which until 1998 had been serving as a department of the GWSC, was now an autonomous agency funded by the government in order to facilitate the CWS projects. A significant problem was financing, as it had been almost 90% dependent on foreign public sector funding. The increase in counterpart funding requirements by bilateral and multilateral donors, together with the decrease in the Government’s allocations, had caused it to owe significant debts by 1998, and the situation worsened through to the HIPC relief.

103. There was also a dubious reliance on the DAs to be able to effectively manage and coordinate responsibility for the water supply systems. Decentralization had began in 1988 when the government passed the Local Government Law establishing the new DAs, that took over the devolved central government activities and became responsible for health, infrastructure (except water) and community development.

104. Yet, despite intending to promote local participation and decentralized decision-making, there was a lack of any real local gains in these areas, owing largely to the central
government’s lack of willingness to devolve power to local governments (Mensah 1998; Mohan 1996). A World Bank loan for the Local Government Development Project (begun in 1994) to invest in roads, storm water drainage and waste management, focused on building capacity of DAs and support of central government for new local responsibilities. In the 2003 final report, the World Bank found that “the government lacked the commitment to proceed decisively with decentralization” and “issues relating to leadership, accountability and full devolution of power in DAs are almost absent in the local Government administration” (World Bank 2003b:12). Mohan (1996) found that the DAs lacked participatory decision-making structures and by 1996 there was little direct community involvement. Thus, at the same time that the loans were passing off added responsibilities to the DAs, there was a demonstrable lack of both technical capacity and decentralized responsibilities that would have made them accountable.

105. The third issue is the aspect of `willingness-to-pay` in these rural communities. The World Bank’s appraisal document decided that, based on their research methods, the expected costs to the community of financing these projects (5-10%) would be desirable and affordable. However, it also noted that the first CWSP had encountered problems in securing the funds from community members, although there is no analysis given as to why (World Bank 1999). There is not enough data to determine whether the absence of counterpart funding in some cases was due to a prohibitive cost or whether it was a lack of the DAs to enforce this commitment.

106. The CWSP Adaptable Program Loan (APL) was postponed after the first tranche in light of the HIPC developments in 2004. The World Bank decided to focus efforts on the urban growth issues raised as a focus of the PRSP, and financed two major projects – the Small Towns Water and Sanitation Project and the long-awaited (at least by World Bank technicians) Urban Water Project.

### 3.2.2 Privatizing the Ghana Water Company

107. The GWSC was separated from the rural operations in order to commercialize and capitalize on the (paying) urban market. World Bank research demonstrated that the GWSC had been generating sufficient income to cover operating costs between 1988 and 1992 – despite being cut off from government funds in 1988 –but was unable to generate a positive net income to pay for debts incurred, particularly in the 1980s structural adjustment policies. After 1992, GWSC began to incur debts through government loans.

108. A program was proposed aimed at tariff increases, increased water production from physical rehabilitation, increased water sales due to service coverage and population increase, and non-revenue water reduction to 42% from 54% World Bank 1994). With these improvements, it was anticipated that by 1997 the GWSC would be operating at a water tariff of 2,234.8 Cedis – 50% higher than its 1993 value. The benefit to the water utility was phenomenal -- projected net annual income for 1997 was 27 billion Cedis – an increase of 14,000%. These projected figures, guaranteeing such a large profit from providing water services, would have made the utility extremely attractive to private sector investment.

109. As part of the restructuring proposed for the GWSC in the early 1990s, the Minister of Works and Housing and World Bank engaged a consulting firm (Halcrow) to complete a Private Sector Restructuring Study (Martey 2001). The proposed restructuring of the GWSC had the following objectives:

- Increase access to water supply for consumers
- Ensure sustainability of the sector
- Achieve cost recovery
- Improve efficiency in the management of the sector
- Ensure affordability and quality of service to consumers

110. The Halcrow consultants presented seven options at a 3-day workshop in Accra in February 1995, where actors from the private sector, multilateral and bilateral agencies, and various government departments were invited. The workshop ended with the selection of a “lease arrangement for a self-contained system from source to end-user” as it was considered to provide the most “flexibility” (Martey 2001).

111. NGOs were reportedly invited to the workshop, although no members of the country’s largest labor unions were present, and only two international NGOs participated (FFM 2002; Weissman 2002). Nevertheless, the presentation at the workshop enabled the World Bank and government to declare that “Ghanaians” had demonstrated support for the project.13

112. Not until 1998 was the Business Framework completed (by Louis Berger of France), defining the institutional and legal arrangements. The urban water system was proposed to be divided into two regions: Business Unit A covering 28 systems in Greater Accra, Volta, Northern Upper East and Upper West regions; and Business Unit B covering 51 systems in Central, Eastern, Western, Ashanti and Brong Ahafo regions.

113. By late 1998, a number of studies had been commissioned to prepare for the bidding (with USA-based Stone & Webster consultants). Preparations included trips throughout Africa, the UK, and France to see privatization in action. After 1998, however, the project did not get very far. Government was reportedly causing delays by making changes to the Business Units and contracts (Martey 2001). A strong opposition was developing from labor unions and organized groups against the privatization, and the Rawlings government appeared to be backing down from privatization, even though the bids had already been called [Larbi 1998 (in Batley 2004)].

114. By 2000, the government had renewed plans to implement the restructuring program. Azurix, a subsidiary of the collapsed Enron corporation, had reportedly been negotiating with the government to operate the water utility since 1995 (Adam 2005). The project was financed by the World Bank with a USD$100 million loan. The loan, however, was cancelled shortly afterwards, with the Bank accusing Azurix of paying a USD$5 million bribe to senior Ghanaian officials, and withdrawing its funding, citing “transparency” as the central issue (Bayliss & Hall 2001). Ghana was asked to refund USD$800,000 for the project appraisal costs, and DFID cancelled a USD$30 million rural water project being planned as a complement the World Bank loan.

115. Although the contract was re-tendered and five companies made pre-qualifying bids, the project was again stalled with the expected national elections later that year. At a November 2000 donors’ conference, donors indicated willingness to finance USD$400 million over a 5-10 year period. However, after the elections, the new government was faced with an out-of-control debt burden and entered into agreements for HIPC debt relief. As part of the World Bank and IMF adjustment measures, the government increased the water tariffs by 98% in May 2001 (Table 3 below).

116. A strong opposition, headed by the Integrated Social Development Centre (ISODEC) in Ghana, led to the formation of the National Coalition Against the Privatization of Water

---

13 The Water Sector Restructuring Secretariat, a position within the Government funded by the World Bank, responded publicly to the FFM by arguing that “Ghanaians selected the PPP lease option” (Weissman 2002).
(NCAP), which is hosted by the Ghana Trades Union Congress and includes numerous groups from labor unions, students, women’s groups, health organizations, communities and NGOs. These participants met at a national water stakeholders’ workshop in 2001 to discuss the water sector privatization plans, and deemed the plans incapable of providing universal access, especially to the poor (Adam 2005). The public opposition is credited with pressuring the government to stall the privatization project.

117. By April 2002, the lease arrangements for the GWC were still under review. The contract proposed leasing the two urban water systems to two operators, who would be responsible for providing the water supply, rehabilitating and renewing pipes, maintaining assets, billing and collecting tariffs, and expanding service coverage. The lease required the concessionaires to each invest USD$70 million over 10 years; however, the international lenders indicated willingness to loan USD$500 million to the companies at no interest (Adam 2005).

118. The FFM noted that there was no provision for a performance bond, and that the investment prioritization formula favored areas already serviced (FFM 2002). In addition, the estimated amount that the deal was expected to bring in amounted to USD$140 million, while the total needed for rehabilitation and expansion was estimated to be at least USD$1.3 billion, leaving the government with a huge amount to finance (through more foreign loans), regardless of privatization.

119. The companies rejected the lease arrangements, citing disincentives and the high infrastructure investment requirement. Although this requirement was later reduced to USD$30 million, it was still deemed excessive by the companies, and was completely dropped. However, as a result and condition of the country achieving HIPC Completion, the government formally instituted plans to privatize the GWCL in June 2004, with the announcement of a USD$103 million World Bank Urban Water Project. Initially proposed as a loan, in January 2005, the project was converted into a full grant.

120. The project proposes to change the lease into a management contract with a private operator for 80 regions, for a period of up to five years. The operator is to be paid an operating fee directly by the World Bank for the first four years; in the last year, 25% of the management fee will be derived from commercial operations that will have benefited from significant capital investments. Key features of the contract (World Bank 2004d) are:

- System Expansion and Rehabilitation - USD$98 million – includes increasing water supply, extending service to poor areas, and reduction of NRW
- PSP Development - USD$6.5 million – supports the payment of a private operator
- Capacity Building and Project Management - USD$7.7 million – training and technical assistance
- Severance Program - USD$11.0 million – financing up to 2,000 layoffs at the GWCL.

121. It is clear that the World Bank is fully financing the investments in capital infrastructure. The management contract requires the private operator to invest USD$500,000, with the Bank funding USD$98 million over the course of the five years. The private operator will be able to realize all its anticipated profit and will receive bonuses for achieving performance objectives.

122. The current annual GWCL budget is insufficient to meet actual needed level of investment required to provide a safe and accessible water supply (Adam 2005). Since the private operator will not be responsible for making capital improvements, the only option for cost-recovery is through tariff increases. At the end of the five year contract term (or earlier,
if deemed feasible), the management contract will be converted into a lease contract and re-bid. Thus, after all the large capital investments are made, NRW is reduced, staff is trained, debts rendered manageable and the GWCL is commercially ‘efficient’ (having attained profitability), the well-functioning utility will be turned over to the private sector. Although there is mention of public sector options, there is no attempt to qualify whether and why involvement of the private sector would even be necessary at this point.

123. Table 3 below demonstrates tariff rate increases that have been implemented between 1998 and 2003. In the basic lifeline category for metered domestic use, there has been an increase of 600% in tariff rates between 1999 and 2003. The largest increases, however, have gone to public standpipe connections, found in the poorest neighborhoods, where the price per 1,000 litres has gone up by 775%.

124. These figures do not reflect the more recent tariff rate changes, which, according to the Third World Network, were increased by 96% in 2003 and 140% in 2004, and are set to increase again in 2005. Since 2003, these increases have been based on automatic tariff adjustments linked to the foreign exchange rate and requiring quarterly reports to the IMF.

Table 3: Ghana Water Company Tariff Rates - 1998-2003

<table>
<thead>
<tr>
<th>Consumption categories for Metered Domestic (in 1,000 litres)</th>
<th>1998</th>
<th>1999</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>% Change 1999-2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cedis</td>
<td>Cedis</td>
<td>% Change</td>
<td>Cedis</td>
<td>% Change</td>
<td>Cedis</td>
<td>% Change</td>
</tr>
<tr>
<td>Metered domestic - based on categories of consumption</td>
<td>400</td>
<td>500</td>
<td>25%</td>
<td>990</td>
<td>98%</td>
<td>3,000</td>
</tr>
<tr>
<td>1,000</td>
<td>1,300</td>
<td>30%</td>
<td>3,600</td>
<td>177%</td>
<td>4,500</td>
<td>25%</td>
</tr>
<tr>
<td>1,400</td>
<td>1,820</td>
<td>30%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unmetered premises - Flat rate per month</td>
<td>5,200</td>
<td>6,500</td>
<td>25%</td>
<td>9,900</td>
<td>52%</td>
<td>22,000</td>
</tr>
<tr>
<td>Boreholes, wells, hand pumps - Flat rate per house per month</td>
<td>1,000</td>
<td>1,500</td>
<td>50%</td>
<td>3,000</td>
<td>100%</td>
<td>4,000</td>
</tr>
<tr>
<td>Premises without connection (public stand pipes) - per 1,000 litres</td>
<td>250</td>
<td>400</td>
<td>60%</td>
<td>1,000</td>
<td>150%</td>
<td>3,000</td>
</tr>
<tr>
<td>Reconnection fee</td>
<td>5,000</td>
<td>10,000</td>
<td>100%</td>
<td>15,000</td>
<td>50%</td>
<td>20,000</td>
</tr>
</tbody>
</table>


125. A significant condition of the World Bank grant is that increases in water tariffs be adjusted according to an automatic adjustment formula linked to foreign exchange, in order to make the investment attractive to foreign investors. This measure had in fact already been implemented in 2002. However, in January 2004, the PURC failed to implement the

automatic adjustment formula to increase prices, which prompted the IMF to deem Ghana non-compliant for a USD$39 million PRGF disbursement (IMF 2004). According to the IMF document, the situation arose when the Minister of Works and Housing apparently put the automatic adjustment on hold in response to concerns that the poor would be adversely affected, considering the concurrent increase of electricity tariffs by 10%.

126. The government subsequently implemented the water tariff increase, and reportedly assured the IMF and World Bank that the government ‘oversight’ would not occur again. Its renewed commitment to the Urban Water Project served as an indication to the IMF and World Bank that the government was serious about implementing full-cost recovery as well as PSP, and the lenders waived the non-disbursement penalty. The debts of the GWC were planned to be settled with IMF support by the end of June 2004 to “make transparent the true cash flow” situation (IMF 2004).

127. The Urban Water Project is questioned for its legitimacy as an option to improve the conditions of water access by the poor. Of principal significance are the assumptions that PSP will and is the only option that can improve efficiency. Yet the major factor affecting the GWCL is its high debt burden, limiting its ability to invest in the utility.15 With the new World Bank loan, as well as IMF commitments, a high amount of the debt service will be reduced or eliminated, although the World Bank admits it is unlikely that historic debts will ever be completely eliminated (World Bank 2004d).

128. Furthermore, the manner in which the loan was ushered through without civil society consultations virtually de-legitimized the participatory process that had developed over 2002 and 2003 due to pressure from NCAP, the FFM and other groups. The project document describes the consultative process that had been undertaken in 2003; however, by the time the new loan agreements were announced, there was no indication of civil society participation. In fact, many of the same groups cited by the World Bank as having been consulted have issued strong statements against the Urban Water Project.

129. In January 2005, the Board of the World Bank announced its approval to convert the credit into a full grant. Although the original five bidders – Suez, Vivendi, Saur, Biwater, and Bechtel – have been involved in the bid process, the latter two have withdrawn, reportedly due to organized protest in their home countries.16 Thus, although there is a strong push for water privatization by the World Bank and the government (according to the PRSP), there is also a strong movement that has developed both within Ghana and internationally that has succeeded in politicizing the privatization of water and pressuring the World Bank.17

3.3 THE ROLE OF THE WORLD BANK

130. The World Bank, together with the IMF,18 has played a decisive and concrete role in the water privatization efforts of the Ghanaian government. In July 1988, the World Bank produced a report Ghana: Reviving the Urban Sector, which proposed a comprehensive agenda on decentralization, urban management, and institutional development (World Bank

---

15 This is confirmed by discussions in the Project Appraisal Document (World Bank 2004d).
16 Public Citizen claims it was responsible for pressuring Bechtel, while the World Development Movement claims responsibility for BiWater.
17 An indication of the significance of this pressure on the World Bank is found in the 2004 Appraisal Document for the Urban Water Project, where the FFM report and letter to Public Citizen are included in the list of official documents.
18 At least until 2001, when the IMF announced it would no longer be participating in utility privatization, and instead would focus on macroeconomic adjustments.
2003, ICR of LGDP). The Bank promoted these principles in a series of loans aimed at decentralizing (the authoritarian) government, and restructuring the water sector.

131. In 1994, a report stated that the “GWSC is interested in learning more about approaches to reducing unaccounted-for-water through private sector involvement” (World Bank 1994:15), indicating the strong advisory role that Bank had in directing options for the sector. The Bank has played a key role in the design of the water sector – separating rural water services into the CWSA, and away from the more profitable urban sector, arguing that the urban “should not have to pay” for the rural – where most of the country’s poor live.

132. The Bank also created the PURC and the Water Sector Restructuring Secretariat in the mid-1990s. The latter was a position within the government that was funded through the World Bank. It is estimated that the World Bank has spent about USD$14 billion per year on technical assistance (ActionAid 2004). Thus, it is possible to conclude that the privatization project that began in Ghana was a product of World Bank advice and assistance, which is and has been overwhelmingly in favor of water privatization.

133. There is evidence to demonstrate, as well, that even though the government appeared to have been in favor of water privatization through agreeing to loans, it was seriously reluctant to implement the program. For example, a paper presented at the World Water Forum in 2001 by the Area Director of the GWSC noted that although the quick support in terms of funding from the World Bank, JBIC and DFID was positive, he laments that “governments must be seen to be committed to privatization to enable funding to be promptly availed by donors” (Martey 2001:77), indicating frustration at the lack of government commitment in Ghana.

134. The government’s own comments on the final report of the Local Government and Development Project stated that, throughout the course of the project, “the decisions of the funding agencies tend to override those of the DAs and agencies” (World Bank 2004b:22) indicating World Bank ‘bullying’ of water privatization projects. Various World Bank documents, as well as the HIPC documents, noted that the government was slow to implement recommended reforms and macroeconomic adjustments, a common feature of failed World Bank adjustment loans that have been blamed on poor country ownership.

135. It is apparent, however, through review of World Bank documents, that hard conditions through structural adjustment loans were needed to force the government to commercialize the water sector in Ghana. Two major water tariff increases are directly linked to approval of World Bank ERSO loans in 1998 and 2001. The HIPC review document states that the reforms requested in order to “support Ghana’s progress in completing previously delayed reforms – in particular, increased tariffs aimed at restoring financial viability to the public utilities and the passage of the VAT law – IDA approved a one-tranche adjustment credit, the Economic Reform Support Operation (ERSO) in 1998” (IDA/IMF 2001:4; emphasis (italics) added).

136. The HIPC Completion point indicators included a reduction in public spending and borrowing, private sector involvement in infrastructure, transferring funds and responsibilities to the District Assemblies – as well as a strong focus on reducing poverty from 40% to 32%. The joint report stated that “the two key areas of structural reform where the staffs consider that completion point conditions would be appropriate are the cocoa sector and pricing reforms in the energy and public utilities sectors... the importance of putting in place a rational pricing regime lies in its potential benefits both for macroeconomic stability and for improved supply and service delivery” (IDA/IMF 2001:13).
137. The 2004 CAS states that the IMF PRGF approved on May 12, 2003, was a direct response to the government’s achievement in implementing automatic water and electricity tariff adjustments. In 2002, the PRGF review had been unsuccessful due to the government’s failure to implement these measures on time (World Bank 2004c). By the time the HIPC Completion point was reached, Ghana had met all condition triggers except for automatic tariff adjustment in the petroleum sector.19

138. The World Bank’s CASs strongly indicate that loans were also conditional upon water privatization. The 2001-2003 CAS was built around the government maintaining conditions where there was little improvement in public sector privatization for infrastructure, low public sector borrowing, and liberalization of the cocoa export.20 One of the primary objectives was to “redefine the role of the state in the provision of public services” (World Bank 2004c).

139. In the first year of the CAS (2001) the base case lending scenario was USD$195 million; however, if the government achieved high-case lending triggers involving no public borrowing, and progress in implementing private sector participation, the country would gain a USD$100 million dollar loan for Urban Water Restructuring. Thus, the total lending for 2001 would increase by 56% to USD$305 million. This loan was to be granted at the completion of the bidding process for a lease arrangement of the GWCL but was put on hold twice, as noted above, when Azurix was accused of bribing Ghanaian officials and when, after re-tendering, the interested bidders rejected the agreement as it stood.

140. In addition, IFC planned support for infrastructure privatization did not materialize due to the “unfavorable environment” attributed primarily to slow sector reform (World Bank 2004c:28). Financing of the water system was important at the time, as the GWCL had incurred deep debts due to the economic crisis and reduced government spending, and very few improvements in water infrastructure had been made in the previous five years.

141. The most recent CAS endorsed in 2004 (for the period 2004-2007) appears to have strong conditionality for water sector privatization. By the time the CAS was endorsed, Ghana had attempted to implement four major economic policy and private sector operations, only one of which was rated satisfactory (World Bank 2004c).

142. The CAS reports on the largely failed use of funds that had been made available in relation to private sector participation, infrastructure and public services provision, and particularly notes the failed effort at water sector reform where the IFC had promised funds. In the base case lending scenario, Ghana will have access to almost USD$1,055 million over three years. The primary conditions are that the government show progress on macroeconomic management, poverty reduction and public finance management. A significant trigger to move into the high case lending scenario (USD$1,370 million) would be to “show satisfactory progress on an agreed IDA portfolio improvement plan… including acceleration of project implementation and disbursements (a trigger in the base case)” (World Bank 2004c:44).

143. The water privatization plan, having been in limbo for 10 years due to “slow” government efforts, is inevitably one of these projects. For 2005, if Ghana managed to maintain the base case scenario, it would receive a USD$100 million loan for Urban Water,

---

19 However, this was allowed as a new regulatory regime was being implemented for 2005 that would completely remove the government from having any influence over petroleum prices – the companies would have the freedom to decide prices (IDA/IMF 2005).

20 This information was compiled in a CNES website document as the 2001-2003 CAS was not available: [www.servicesforall.org/html/countries/ghana.shtml](http://www.servicesforall.org/html/countries/ghana.shtml) [accessed April 15, 2005].
a USD$125 million loan for the poverty reduction strategy and USD$25 million for SME development – a total of USD$250 million, more than the low case lending scenario of USD$65 million. Progress with these portfolios – in implementing and disbursing the loans - would mean that, in 2007, Ghana could reach the high case scenario, where it would receive USD$170 million more than the base case lending scenario. These provisions give the government strong incentive to pursue the privatization plans in earnest.

144. Yet, while there is strong evidence that water privatization is a condition of the loans, the World Bank would argue that it is only responding to the PRSP developed by Ghana indicating their desire to pursue the privatization option in the water sector as a means of increasing access by the poor. However, the reality is that the current government is in a position from which it could not possibly oppose privatization.

145. Having been in power for only three years, the current administration is not necessarily responsible for the actions of the government that preceded it. The Rawlings administration, which lasted for almost two decades, had negotiated private sector participation and the structural adjustment loans that had left the country with such high debts in 2001 that the incoming government had to apply for debt relief. Such high debt can create conditions where a country is forced to make short-term policy decisions, disregarding long-term sustainability. As Moss & Chiang write: “this can lead to non-selective borrowing, including agreeing to conditions that might otherwise be rejected… Not only do governments that are facing continual short-term crises tend to make poor policy decisions, but this trend over a period of time damages the development of public institutions able to make strategic choices, finance initiatives on a sustainable basis, and monitor their implementation” (2003:9).

146. Thus, it would be difficult to make conclusions about the government freely making the decision to pursue water privatization. In fact, within the CAS, the World Bank notes that the earlier two years in trying to implement public sector reform had experienced implementation delays due to “weak government ownership.” Considering the discussion above regarding options other than privatization, the discourse produced in the advice, research and financing options of the World Bank do not lead to the conclusion of guaranteed financing for failing public utilities. It would be reasonable to conclude that the government would step up its “privatization platform” in order to gain access to financing it desperately needed.

147. It is also doubtful whether water privatization efforts of the Rawlings administration could be considered “country ownership”, as it was achieved under an authoritarian government for the first decade of structural adjustment. After 1992, when true efforts at water privatization began to materialize and democracy had been reinstituted, there were significant challenges to the Rawlings regime, particularly by labor unions. Although World Bank analysts in 1996 concluded that the success of the structural adjustment programs throughout the 1980s and early 1990s in Ghana was directly attributed to the sense of country ‘ownership’ (Obeng 1996), it has become evident that not only was the discourse of supposed local government and democratic decentralization not a reality (Mohan 1996), but by 1998 it was evident that the World Bank-funded program was far from being a success.

148. At present, the privatization of the GWCL appears to be going as planned; however, strong civil society opposition, within Ghana and internationally, is constantly challenging the state and the World Bank to show more transparency in negotiations, loan conditions and the privatization process. The existence of such a movement indicates the precarious level of ownership that exists in the PRSP process and the staunch resistance to water privatization.
4. CASE STUDY: PHILIPPINES

149. Since the 1960s, the Philippines has been strongly influenced by IMF and World Bank structural adjustment lending that has failed to lead to substantial structural improvements. By the 1990s, the country was in huge debt and was unable to provide funding for its state-owned water utilities, which were already in extreme states of disinvestment. A series of legislation ushered by the Aquino and Ramos administrations paved the way for water privatization, leading to what was dubbed as the ‘world’s largest water privatization’ when the Manila Waterworks & Sewerage System (MWSS) was divided into two main concessions in Metro Manila and sold to two separate private sector bidders, facilitated to a great degree by the World Bank.

150. Although deemed to be a success and replicated as a model in other countries, by 2002 it was evident that there had been some serious mistakes made when one of the concessionaires issued its notice of termination after failing to obtain its desired tariff increases. By this time, tariffs had been increase substantially, the concessionaire had stopped paying its concession fees, and the debt that it had agreed to pay continued to be as high as 5 years earlier.

4.1 BACKGROUND

151. At a growth rate of about 2% (in 2001), the Philippines has one of the fastest growing populations in East Asia, increasing at more than twice the average for the region (WDI 2005). In 2002, it had a population of 78.6 million with 60% living in urban areas (UN 2004b). The rate of rural to urban migration has doubled over the last 25 years enhancing pressures on already limited urban resources and infrastructure.

152. Out of 177 countries, the Philippines is ranked 85th on the Human Development Index. Although considered to be a ‘medium development’ country by the United Nations Development Programme, it has quite a distance to catch up with the region. There is a high degree of poverty with 36.8% of the population living below the National Poverty Line between 1999 and 2001; 46.4% of the population made less than USD$2 per day (UN 2004b). The richest 10% control 36.3% of income while the poorest 10% control only 2.2%.

153. Rising public debts and a lack of infrastructure investment have been blamed for the relative underdevelopment of the Philippines compared to its neighbors. Corruption is also a significant factor contributing to the mismanagement of public resources – Transparency International rates the Philippines in the bottom third of 145 countries.21

154. In 2004, the Philippines had a staggering total foreign debt of USD$54.8 billion, up from USD$46 billion in 1998 (Table 4). Approximately 69.1% of this is public debt owned by government institutions and enterprises (Bankgo Sentral 2005).22 Multilateral lenders accounted for 15.4% of the foreign debt in 2004, while Japan was the largest lender accounting for almost 27%. Although the World Bank, through the IBRD, only represents 6% of the total, it is one of the most significant single lenders along with the ADB and the JBIC; these three also represent most of the public sector debt.

---

21 Based on the Transparency International’s Corruption Perceptions Index, the Philippines had a value of 2.6 out of a possible 10 in 2004. In 1999, it had a value of 3.3 (PPIAF 2000a). The Corruptions Index is accessible online at: www.transparency.org [accessed May 3, 2005].

22 Total public debt includes Bangko Sentral, government banks and non-banking public debt.
<table>
<thead>
<tr>
<th>Year</th>
<th>Multilateral</th>
<th>IBRD</th>
<th>IMF</th>
<th>ADB</th>
<th>Japan</th>
<th>Other</th>
<th>Total Foreign Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>10,058</td>
<td>4,298</td>
<td>1,562</td>
<td>3,490</td>
<td>11,887</td>
<td>24,201</td>
<td>46,146</td>
</tr>
<tr>
<td>1999</td>
<td>10,245</td>
<td>4,071</td>
<td>1,822</td>
<td>3,536</td>
<td>14,205</td>
<td>26,547</td>
<td>50,997</td>
</tr>
<tr>
<td>2000</td>
<td>9,665</td>
<td>3,626</td>
<td>2,031</td>
<td>3,324</td>
<td>13,136</td>
<td>28,405</td>
<td>51,206</td>
</tr>
<tr>
<td>2001</td>
<td>9,553</td>
<td>3,251</td>
<td>1,948</td>
<td>3,160</td>
<td>11,986</td>
<td>30,361</td>
<td>51,900</td>
</tr>
<tr>
<td>2002</td>
<td>8,970</td>
<td>3,322</td>
<td>1,675</td>
<td>3,271</td>
<td>12,927</td>
<td>31,748</td>
<td>53,645</td>
</tr>
<tr>
<td>2003</td>
<td>9,031</td>
<td>3,446</td>
<td>1,193</td>
<td>3,710</td>
<td>14,478</td>
<td>33,886</td>
<td>57,395</td>
</tr>
<tr>
<td>2004</td>
<td>8,440</td>
<td>3,317</td>
<td>755</td>
<td>3,730</td>
<td>14,528</td>
<td>31,878</td>
<td>54,846</td>
</tr>
</tbody>
</table>


(1) Other includes bilateral lenders except for Japan, banks, suppliers and bondholders.

155. Official Development Assistance ODA to the Philippines has been decreasing over the past decade (see Table 5 below), while the country's debt service has been increasing and remains extremely high relative to average ratios for the region and other developing countries.

<table>
<thead>
<tr>
<th>Year</th>
<th>Total ODA (USD$ millions)</th>
<th>ODA per Capita (USD$)</th>
<th>ODA (% GDP)</th>
<th>Total Debt Service (% GDP)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>595.7</td>
<td>9.22</td>
<td>2.9</td>
<td>8.1</td>
</tr>
<tr>
<td></td>
<td>1999</td>
<td>7.33</td>
<td>7.1</td>
<td>0.7</td>
</tr>
<tr>
<td></td>
<td>2001</td>
<td>7.1</td>
<td>3.9</td>
<td>0.3</td>
</tr>
<tr>
<td></td>
<td>2002</td>
<td>2.9</td>
<td>1.5</td>
<td>0.7</td>
</tr>
<tr>
<td>Philippines</td>
<td>55,150</td>
<td>8.8</td>
<td>6.5</td>
<td>1.2</td>
</tr>
<tr>
<td>East Asia &amp; Pacific</td>
<td>7,724</td>
<td>-</td>
<td>-</td>
<td>8.8</td>
</tr>
<tr>
<td>Developing Countries</td>
<td>26,070.9</td>
<td>8.51</td>
<td>6.5</td>
<td>1.2</td>
</tr>
<tr>
<td>‘Medium Development’ Countries</td>
<td>'Medium Development Countries'</td>
<td>5.35</td>
<td>6.5</td>
<td>1.2</td>
</tr>
</tbody>
</table>

Source: UN (2004b) and WDI (2005).
(1) Philippines is categorized as a Medium Development country according to the UNDP (HDR 2004).

156. An increasing population, together with higher public debts and misguided investment priorities, has created extreme strains on government spending towards infrastructural improvements, particularly in health and water. While there have been significant advances in increasing the population with sustainable access to improved sanitation from 74% in 1990 to 83% in 2002, improvements in access to a safe water supply have been relatively negligible with 86% of the population in 2002 compared to 87% more than a decade ago. By 1994, public investment in infrastructure had fallen to 0.08% of GNP making water and health the two least invested public sectors (World Bank 1995).²³

²³ In 1983, prior to the fiscal crisis, expenditure on infrastructure was 0.34% (World Bank 1995).
157. The privatization initiatives in the Philippines have marked a process of over twenty years of government attempts to manage public spending and take control of the foreign debt. President Corazon Aquino succeeded Ferdinand Marcos in 1986, restoring the Philippines to democratic rule, and inheriting a USD$26 billion debt in the process. Faced with IMF and WB emphasis on debt repayment, the government opted for the ‘model debtor’ strategy for fear of economic retaliation by foreign creditors (Bello 2005). Until the end of her term in 1992, President Aquino laid the groundwork for private sector development in the country, believing it to be the answer to the cash-strapped centralized government.

158. In 1986, Proclamation 50 was approved that launched a program of privatization and set up the Committee of Privatization. Over 122 government enterprises were privatized, generating almost USD$2 billion in revenues (Dumol 2000). The Aquino administration was also responsible for enacting the “BOT” – build-operate-transfer – Law, establishing a concrete process for development and bidding of BOT schemes. These two initiatives essentially “opened the door to privatization”, creating an environment conducive to WB/IMF lending ‘ideology’ and setting the stage for the incoming President Ramos in 1992 to pursue more concrete privatization of huge public infrastructure.

159. A principal initiative of the Aquino administration was the adoption of the Local Government Code in 1991. This legislation essentially decentralized financial autonomy to local government units (LGUs), where they were granted opportunities to raise revenue and assume debt in order to invest in local infrastructure and socioeconomic development. The Code provided for four sources of finance: 40% of internal revenue allotments (IRA) from national government tax proceeds; local taxation; credit financing, where debt service cannot be more than 20% of LGU income; and the ability to engage in BOT schemes (PPIAF 2000b).

160. However, along with these financial tools to invest in the welfare of local residents, the LGUs were also downloaded responsibility for infrastructural investments that had formerly been responsibilities of the central government. A 1995 report by the Philippine Institute for Development Studies (PIDS) found that the IRA transfers were not sufficient to cover the increased level of activities that LGUs were required to undertake, and few LGUs had the capacity to mobilize local resources (Manasan 1995).

161. In addition, many local governments already owed huge debts to the government’s financial institutions - a 1985 estimate was P2.1 billion (PPIAF 2000a). The PIDS study also found that in 1993, there were negative net transfers in 20% of municipalities. This investment ‘vacuum’ has largely been unresolved and has been the focus of intensive World Bank funding to build local capacities, although these efforts are usually directed towards improving the abilities of the LGUs to commercially manage and oversee private sector development.

162. At the start of the new Ramos administration, the Philippines was faced with an electricity crisis throughout 1992 and 1993, to which government responded by facilitating private sector investment through BOT arrangements aimed at eliminating the ‘brownouts’ (electricity shortages) (Dumol 2000). Fuelled by the success of these reforms and riding on the public’s support, the Ramos administration began to look at privatizing the heavily

---

24 Many of President Aquino’s officials came from the private sector (Dumol 2000).
26 P= Philippine pesos
indebted and poorly performing public water utility in Metro Manila – the Metropolitan Waterworks and Sewerage System (MWSS).

163. Beginning in 1993 with the convening of several ‘Water Summits’ to discuss the impending water crisis and the fatal state of the country’s utilities, the government instituted the Water Crisis Act, permitting the Executive full authority to negotiate BOT contracts and privatize MWSS, as well as allowing for the reorganization of utilities (reduction in personnel) and introducing the criminalization of water theft.27

164. Mark Dumol, a key actor in the Ramos administration at the time, makes clear the lack of public debate or accountability the MWSS privatization process afforded Philippine citizens:

> The Water Crisis Act… turned out to be extremely important for the MWSS privatization. In one sentence, almost as an afterthought, the law gave the President the authority to privatize MWSS. This authority was strong because it did not prescribe any particular procedure for privatization. We were free to create our own procedure.28

165. Between 1992 and 1997, foreign direct investment in public water utilities increased from USD$15 million to USD$150 million as a result of the policies of the Ramos administration. The “world’s largest water privatization” was completed in January 1997 when MWSS was divided into two utilities and leased to two private sector companies, who, from then on, continuously challenge the ideology that public resources are better managed in a market-based economy.

### 4.2 EXPERIENCES WITH WATER PRIVATIZATION

166. The water supply and sanitation sector in the Philippines is managed by four systems with unique legal and managerial responsibilities:

- The Metropolitan Waterworks and Sewerage System (MWSS) in Manila covers eight cities and 29 municipalities with a population of 11.3 million in 2000 (PPIAF 2000a). Since being privatized, MWSS continues to operate as an autonomous government corporation, overseeing its two concessionaires as an (ineffective) regulator. Aside from the regulatory, legal and financial issues that have arisen out of the privatization, there is substantial preoccupation with the huge tariff increases that have occurred, as well as the inability to reduce non-revenue water losses (NRW) – currently greater than 50%.

- Water Districts are formed by local governments, existing in over 500 municipalities ranging from less than 100,000 to almost 300,000 residents. Although these Water Districts operate autonomously from the municipality, the local mayor often directly appoints the Board. The Local Water Utilities Authority (LWUA) acts as a special lending agency; by 1998 it had financed P12.3 billion for water utility infrastructure. Until 2002, the LWUA retained regulatory control over the water districts including approving tariff rates. After 2002, however,

---

27 According to Esguerra (2003), the legislation was introduced with very little discussion, largely a result of its timely introduction as a strategic response to the El Nino phenomenon damaging agriculture.

these responsibilities were passed on to the National Water Resources Boards, and the LWUA retained control of water rates only in those districts where it had financial exposure so that it could ensure the recuperation of its loan interests (Jamora 2002). In general, almost 80% of Water Districts have been suffering from financial gaps and inabilities to invest in coverage expansion.

- There are an estimated 1,000 Local Government Units (LGUs) operating smaller water utilities as a function of the municipality since the Local Government Code endowed them with the abilities to raise financial capital. LGUs are overseen by the Department of Interior and Local Governments (DILG).

- Small-scale private utilities exist throughout Manila and many provinces, serving an estimated one million people (in 2000). These are often set up as part of condominium or suburban developments, generally in economically well-off areas. Informally, however, there are a number of small-scale private vendors selling to local markets where there is a lack of coverage, such as in Manila’s slums. It has been estimated that the urban poor can pay as much as 4 to 13 times more for water than for households that have piped water (David & Inocencio 1996).

167. There are currently intensive programs sponsored by multilateral lenders, particularly the World Bank, to privatize Water Districts and LGU water utilities. A few significant cases of the privatization experience in the Philippines are outlined below.

4.2.1 Metro Manila and the ‘corporate muddle’ of privatization

168. In 1995, water service coverage in Metro Manila was one of the lowest for the major Asian cities, with only about a 67% water supply coverage and 10% sewage connection. The MWSS was considered inefficient, providing only 16 hours per day of service, with approximately 9.8 staff per 1,000 connections (David & Inocencio 1996).

169. Non-revenue water amounted to an estimated 65%, the highest relative to its country neighbors. A large number of unconnected households were paying up to 11 times as much from private vendors for water that had been stolen from illegal connections to the MWSS service. In addition, forced to borrow from multilateral lenders through the national government, the MWSS had incurred approximately USD$880 million in debt – in 1998, its debt service burden was approximately USD$100 million (Dumol 2000; Esguerra 2003).

170. The government appointed the IFC to design the bidding process for privatization and draw up a 25-year concession contract, completed in November 1996 at a cost of USD$7.2 million - USD$6.2 million as a consultancy fee, and an additional USD$1 million as a bonus upon successful completion of the bidding process. The key objectives were to improve quality and efficiency, expand services, end inefficient government subsidies and reduce water tariffs (Esguerra 2003).

171. Manila was divided into two areas for two separate concession contracts: Zone West included old Manila and the southern zone of Cavite, representing 60% of the population and the highest concentration of poverty in the city. The wealthy area of Makati and expanding suburbs of the eastern part of the city made up Zone East. This arrangement was proposed for three reasons: 1) to promote competition; 2) to provide comparative performance benchmarks; and, 3) to provide a safety net where one concessionaire could easily take over if a contract was terminated (Dumol 2000). The two concession contracts were awarded in February 1997 and began operations later that year.
172. The West Zone was awarded to Maynilad Water Services Inc. – a consortium\(^{29}\) of BenPres Holdings (Philippines) and Suez (France) – that had proposed a 43.4% tariff reduction. The East Zone was awarded to the Manila Water Company Inc. – a consortium of Ayala (Philippines), Bechtel (US) and United Utilities (UK) – that had proposed a 73.6% tariff reduction. Of the four bidders, Manila Water was by far the ‘winner’ with a substantially lower bid; however, the lease contracts stipulated that the concessions be owned by two different companies.

173. It had earlier been agreed that, as the West Zone utility had a higher population and could therefore expect more revenues, Maynilad would assume 90% of the MWSS debt, leaving 10% for Manila Water.\(^{30}\) Aside from the concession fees, features of the agreement included coverage supply service targets of 98.4% for the West Zone and 94.6% for the East Zone by 2021, and a commitment to invest USD$7 billion in infrastructure over the course of the concession. The companies were required to post a USD$200 million performance bond as insurance to MWSS in case they failed to meet their contract obligations. The MWSS Regulatory Office (MWSS-RO) was established to monitor the concessionaires, implement tariff adjustments, and deal with customer complaints. An automatic tariff adjustment would be allowed at the discretion of the MWSS-RO at five-year intervals.

174. Dumol (2000) reports how, in order to prepare for privatization and help drive the bids lower, water tariffs were increased by 38% - from P6.43 to P8.78 per cubic metre – in August 1996. The employee base was reduced by 30%. There were also significant “visible” capital investments made in order to foster public support for the tariff increase and demonstrate to the bidders that the government had the “courage” to make difficult fiscal choices. Thus, the economic situation of the utility was already an improvement over when it made the decision to privatize.

175. By the end of 2000, Maynilad reported expected losses of P2.7 billion. Although the company blamed the Asian financial crisis for the devaluation in the peso, there were clear indications as early as 1997 that it was already in an unsustainable situation - 1997 revenue was only P751 million or 43% less than the company had originally estimated (Esguerra 2003). Maynilad was unable to obtain loans, particularly a USD$350 million loan offered by the ADB, and, in October 2000, applied for automatic accelerated relief and deferment of its concession fee payments to the MWSS, as well as reduced coverage targets as called for by the ADB. These requests were not granted, and Manila Water suspended payment of its concession fees.

176. A government committee was set up to negotiate with the company, resulting in a Memorandum of Cooperation reportedly giving it a 72% rate increase. Due to popular pressure, the Arroyo administration withdrew the agreement, and a 2001 amendment was negotiated to the original Concession Agreement, permitting the company to recover foreign exchange losses and increase water tariffs.

177. Maynilad continued to refuse to pay the concession fee. A rate rebasing exercise in 2002 granted the company an increase of P26 per cubic metre and extended the deadline for compliance in paying the concession fee. However, Maynilad, unhappy that its original request for P34 per cubic metre tariff had not been granted, filed a notice of early termination in December 2002 and attempted to sue the MWSS for USD$300 million – money it claimed to have invested in the utility.

---

\(^{29}\) According to law, Philippine companies must retain ownership of 60% of BOT schemes.

\(^{30}\) In reality, the ratio was 80:20 as debt that came in after the deal was closed was loaded in the East Zone (Dumol 2000).
178. The dispute was carried to the International Court of Arbitration in Paris, where the termination was denied validity and Maynilad was ordered to pay the MWSS the P6.77 billion it owed in concession fees. After filing a Petition for Rehabilitation, Maynilad and the MWSS negotiated a proposal for Amendment No.2, approved in April 2005.\textsuperscript{31} The amendment permitted the MWSS a partial draw on the performance bond of USD$50 million with the rest – roughly USD$70 million -- transformed into equity, giving the MWSS direct shares in the company. The total amount of USD$120 million was roughly equivalent to the concession fees owed to MWSS by Maynilad. Although the MWSS Board apparently supported Amendment 2, it was later withdrawn, reportedly due to widespread criticism that it constituted a ‘bailout’, as well as recognition of the implicit risks to the financial position of MWSS in taking on the debt-laden company.

179. In 2004, Maynilad made a new proposal - the Rehabilitation Plan. Currently, the agreement gives MWSS a full draw of the USD$120 million performance bond, accounting for 60% of the money it is owed. About USD$60 million worth of Maynilad equity will become available for new investors in order for the utility to secure loans to cover its new performance bond.\textsuperscript{32} The MWSS committed to securing a USD$100 million World Bank loan for Maynilad to cover the capital investments it claims it will be unable to make over the next few years.

180. Manila Water has also had its share of disputes with the MWSS, particularly in 2001 when it petitioned to have the appropriate discount rate (ADR) – an interest rate charged to consumers – increased from 5% to 18% (Esguerra 2003). The rate was finally approved by the MWSS to 9%, raising rates by almost 40% by the end of 2001.

181. By March 2002, the tariffs in the West Zone were P15.46 and the East Zone P6.75, increases of 135% and 128% respectively from the pre-privatization rates (Esguerra 2003). In the West Zone, the prices increased from P6.58 to P15.46 over the course of one year. Six additional charges were also placed on the per-unit pricing, including a 10% value-added tax (VAT). According to Inocencio (2003), by the end of the first quarter of 2001, the cost per cubic metre for individual connections was USD$0.06, while the cost for community managed water connection was USD$0.16. Public taps serving about 50 households each - of which Maynilad operated 402 and Manila Water operated 533 - ranged from USD$0.43 to USD$0.86. Thus the distribution of charges as a percent of income has still been heavily burdened on the urban poor.

182. The problems in Manila’s water privatizations have been largely attributed to the unsustainable tariff reductions that the utilities proposed in the bidding process – a concept understood as ‘dive bidding’. There is strong evidence indicating that IFC consultants were aware that the Maynilad bids were based on several issues that would make the bid unrealistic, including optimism that it could reduce NRW by 50% and that it would be willing to operate at a cumulative loss of USD$496 million for the first ten years (Solon & Pamintuan 2000).

183. Similar observations were made for Manila Water, even though its proposal was very similar to the two losing bidders. Research by PIDS indicated that Maynilad had underestimated its tariff structure and that the IFC consultants had misinterpreted demand (David 2000). The research also concluded that the coverage targets did not include those households that had well sources, or community taps, or were serviced by a private providers, as well as being ambiguous about industrial and commercial targets. Thus, the

\textsuperscript{31} Reported in Business World, April 27, 2005.

\textsuperscript{32} Manila Water, in consortium with the IFC and a foreign investor are reportedly interested in buying the Maynilad shares. DMCI (a shareholder in Subic Water) is also reportedly interested.
coverage levels represented by the utilities were overestimating achievements in access to the poor.

184. An open letter by Vipul Bhagat, the IFC Country Manager to the Philippines, outlined the following objectives for the MWSS public-private partnership over the term of the 25-year concession:

- Increase capital investments and operational efficiencies to expand service coverage;
- Create competition and enable performance to be benchmarked;
- Ensure 24-hour water supply;
- Improve sewerage services;
- Reduce non-revenue water to an acceptable level; and
- Relieve the government of the financial burden needed to improve MWSS facilities.

185. An important function of the original concession agreement (not mentioned by Bhagat in his letter) was the reduction of water tariffs (or their maintenance at an appropriate and affordable level). Yet, according to the FDC, over a period of eight years – 1997 to 2005 – the tariffs had increased by 500% in the West Zone and 700% in the East Zone. Table 6 outlines the progress in the targets that were intended to be achieved through the MWSS privatization.

<table>
<thead>
<tr>
<th>Year</th>
<th>MWSS</th>
<th>1997</th>
<th>7.15</th>
<th>67</th>
<th>10</th>
<th>65</th>
<th>9.8</th>
<th>16</th>
<th>-</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2001</td>
<td>3.9</td>
<td>89</td>
<td>1</td>
<td>48.3</td>
<td>3.6</td>
<td>21</td>
<td>50,549</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2002</td>
<td>4.3</td>
<td>90</td>
<td>-</td>
<td>53.5</td>
<td>3.4</td>
<td>17</td>
<td>61,370</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2003</td>
<td>4.4</td>
<td>90</td>
<td>-</td>
<td>60.7</td>
<td>3.7</td>
<td>21</td>
<td>63,730</td>
<td></td>
</tr>
<tr>
<td>Manila Water</td>
<td>2001</td>
<td>5.5</td>
<td>82</td>
<td>4</td>
<td>66.3</td>
<td>4</td>
<td>21</td>
<td>63,910</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2002</td>
<td>5.7</td>
<td>84</td>
<td>7</td>
<td>68.7</td>
<td>3.7</td>
<td>21</td>
<td>63,730</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2003</td>
<td>5.7</td>
<td>84</td>
<td>-</td>
<td>64.7</td>
<td>3.7</td>
<td>21</td>
<td>63,730</td>
<td></td>
</tr>
<tr>
<td>Maynilad</td>
<td>2001</td>
<td>5.5</td>
<td>82</td>
<td>4</td>
<td>66.3</td>
<td>4</td>
<td>21</td>
<td>63,910</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2002</td>
<td>5.7</td>
<td>84</td>
<td>7</td>
<td>68.7</td>
<td>3.7</td>
<td>21</td>
<td>63,730</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2003</td>
<td>5.7</td>
<td>84</td>
<td>-</td>
<td>64.7</td>
<td>3.7</td>
<td>21</td>
<td>63,730</td>
<td></td>
</tr>
</tbody>
</table>


(1) Sanitation coverage targets were intended to be 38% and 43% for 2001.

186. What remains to be quantified is how ‘efficient’ the privatization process has been, compared to what it would have cost to improve MWSS as a public utility. While there have been improvements in coverage and water supply, these have largely been funded through increased loans and not through cost-recovery, invalidating one of the primary reasons advocated for privatization of water utilities.

187. Manila Water’s cumulative borrowings to 2004 were USD$130 million, while Maynilad was reported to owe approximately USD$180 million. Yet, in 2003, Manila Water

33 This letter was written in May 2004 to the Freedom from Debt Coalition in response to criticism of the IFC and World Bank’s actions. The letter was published in several newspapers as well as the FDC website: [www.freedomfromdebtcoalition.org/main/pages/000247.php](http://www.freedomfromdebtcoalition.org/main/pages/000247.php) [accessed April 14, 2005].

34 This value was reported as P10 billion and converted to USD$ based on the exchange rate at the end of 2004 – USD$1:P56.17.
announced a net income of USD$21.5 million (P2 billion), an increase of 116% over 2002 (GWI 2004). A recent Business World report indicates that Maynilad is expected to realize net income of P1.9 billion by the end of 2005 and P2.7 billion in 2006. Meanwhile, the government and MWSS have had to pay the high costs of legal battles, administration and capacity-building for regulation.

4.2.2 Local government water privatizations

188. Subic Freeport and Olangapo City had their water utilities privatized beginning in 1995, through a World Bank loan that foresaw the development of increased demand in the area with the development of the Subic Industrial Park (World Bank 2004a). The Subic Bay Freeport Project was initiated in June 1994 with a USD$40 million loan intending to develop the necessary infrastructure to attract industry to the area. Foreseeing increasing demands and potential revenues, the World Bank also proposed a second loan of USD$60 million in November 1996, focused partly on preparing for bulk water transfer to the region. The water portion of this loan was dropped in early 2002 (reducing the loan to USD$36 million), when conflicts with Olongapo City made negotiation on water rights difficult (World Bank 2004a).

189. The Subic Water & Sewerage consortium is formed by BiWater Internationa(UK) – 30%; DMCI (Philippines) – 40%; Olangapo water district – 10%; and Subic Bay Metropolitan Authority – 20% (PPIAF 2000a). Subic Water was entitled to increase water tariffs twice per year and in 2001, the water tariffs had reportedly increased by 465% in five years, to a 2001 rate of P34.2 per cubic metre. Despite receiving further World Bank loans, the company reported losses of P146.8 million (based partly on high operating costs due to mismanagement, as well as exorbitant foreign consultancy fees), and had only invested 30.8% of their agreed capital investments, resulting in negligible change to the NRW rate of 44%. The Subic Water Resources Board chairman was quoted stating that “Government must help by providing subsidized loans to investors with stakes in utility firms.”

190. The most significant direct privatization program of the World Bank is the four-phase LGU Urban Water and Sanitation Adaptable Program Loan (APL). It is explicit about being a water privatization program for local governments in developing design-build-lease contracts for private participation.

191. The loan is designed to be released in four segments of USD$180 million over 12 years, with approval of the subsequent phase predicated on successes in the previous segment. The first phase (1998 to 2002 - USD$23 million) was planned to create 35 privately operated water utilities as a ‘test’ phase in selected well-performing LGUs. APL 2 (2001 to 2006 - USD$30 million) plans to reach at least 40 LGUs. APL 3 (2004 to 2008 - USD$100 million) and APL 4 (2006-2010 - USD$130 million, and USD$100 million from other sources) plan to improve local opportunities to leverage private financial investment and enter a further 130 LGUs in PSP concessions. By the end of the APL, an estimated 20% of local government water utilities in the Philippines will have been privatized.

192. The first APL selected 35 LGUs as pilot cases for PSP based on their potential to achieve the objective of “providing practical demonstration, through a reasonably large sample of LGUs, that appropriate technical and financial designs, pricing rules and institutional incentives, water supply systems, regardless of size, can be viable and sustainable” (World Bank 2004b: 6; emphasis (italics) added).

---

193. This first phase proved to have unsatisfactory results, as about 79% of the USD$23.3 million loan was cancelled when many of the LGUs that had initially shown interest dropped out. The final report on the loan indicates several reasons for the high dropout rate -- the overall reason being little interest in PSP and the availability of credits from other government programs as well as the LWUA without PSP requirements.\textsuperscript{37}

194. Only nine LGUs in three municipalities – Laguna, Isabela and Bukidnon - followed through with the BOT loans, constructing the water supply systems that would be bid to private operators on concession agreements. However, as of February 2003, only two LGUs water systems were operating under concession to the private sector.\textsuperscript{38} At least five LGUs were unable to find interested private operators to bid on their systems and were undertaking operations and maintenance themselves. Both Magdalena and San Mateo LGUs started off with private concessions; however, these were later dropped. In Magdalena, the bidder – a subsidiary of BenPres Holdings – backed out after 40 households refused to connect to the new system as the old system, though less frequent, was much cheaper than the P20.54 the private utility would be offering for 24-hour service (Capistrano & Gutierrez 2003).

195. Intended to produce a sample of functioning local-level privatized water utilities, the project was considered to be less than successful, having liquidated only 27.4% of the original appraised loan. On the other hand, the DBP spent almost 40% of its counterpart contribution to cover the expenses of the LGUs that completed feasibility studies and subsequently dropped out (World Bank 2004b).

196. The seven water utilities that were unable to find private investors to take on part of the World Bank loan in exchange for the water utility concession are now burdened with having to pay the loan back themselves. While their water systems appear to be operating successfully as public utilities, revenues are not sufficient to cover the debt service on the loan, thus placing the public system at risk. One of the privatized systems in Bukidnon, operated by Benguet Corp. under a 15-year concession, reportedly suffered losses of more than P200 million in 2002 and 2003.\textsuperscript{39}

197. The World Bank’s report on this project concludes that the public utilities built through the loan were operating successfully, yet does not use this information to question the viability or purpose for private sector participation. The financial analysis of the project does not include details for the privatized utilities, as there was not enough information yet for the two utilities in Bukidnon nor in San Mateo in view of the “6-month gap in financial data while the system was under private sector management” (WB 2004b:10), making cost-benefit analysis impossible by either internal or external studies.\textsuperscript{40} Analysis of these systems may have provided useful and educational insights into effective public sector management. As of March 2003, the seven remaining utilities to be privatized under the first APL were redrafting their lease contracts with World Bank advisors to be re-offered for bidding under more ‘favorable’ terms.

198. The second part of the APL (totaling USD$30 million) had already been granted in 2001 before the APL1 completion report was published; thus there has been little

\textsuperscript{37} This loan was funded through the Development Bank of the Philippines.

\textsuperscript{38} In Bukidnon one LGU is operated by DCMI (of Subic Water) under a 15-year concession agreement.


\textsuperscript{40} However, as promoting public operation and management was not an objective of the World Bank loan, the lack of this “benchmark” was not even considered a factor in the project’s evaluation.
information for the additional 40 LGUs projected to benefit from PSP to evaluate feasibilities or alternatives. In La Union, the Bank is experimenting with output-based aid where, based on studies demonstrating that low income households tend to use less water, poor households will be exempt (for the first time) from paying the minimum water use rate and will pay for actual usage (Yamamoto & Hunt 2005). Subsidies will be transferred through a World Bank loan to the municipality, which will pay the private operator based on service targets, essentially transferring the cost reductions onto poor consumers. The IBRD will finance more than USD$4 million for the USD$11 million project - USD$1.5 million to the private operator; USD$2.3 million to the La Union government for OBA payments; and USD$360,000 to refinance the LGU's outstanding debt to the LWUA.

199. The La Union case demonstrates well the amount of funding required to attract a private operator, and also highlights an important question: why involve the private sector at all? The point of having PSP is so that the market economy will provide for the efficiencies that the public sector apparently can not afford. Yet the local government is asked to take on additional loans just to pay for a service that it might operate itself under the same conditions.

200. In addition, the local government body will have to learn how to regulate the utility, and develop the capacity to ensure that the subsidies are distributed based on accurate assessments. Including social cost-benefit analysis, it might be worse off to privatize. The project has already been delayed for almost two years due to public protests and union issues arising out of the dissolution of the water district, demonstrating that there is a strong local demand for keeping the utility public.

4.3 THE ROLE OF THE WORLD BANK

201. The examples noted above provide evidence that PSP in the Philippine water sector is a strong feature of the current investment development environment. The Manila water privatization was hailed by the Philippine government and the multilateral donors, including the World Bank, as a huge success for the “world’s largest water privatization.” In fact, a Philippine official boasts about his role in serving as a representative for the Philippine water privatization in South Africa in its pre-privatization period (Dumol 2000).

202. Between 1990 and 2004, there have been 15 World Bank loans to the Philippines which were all or partly focused on water and sanitation, totaling almost USD$772.6 million (Table 7), almost all containing some reference to private sector participation.41

203. The MWSS privatization may not have been a direct project of the World Bank; however, the Bank financed USD$117 million in 1996, demonstrating their support in furthering water sector privatization in Subic Bay and Manila. The USD$57 million loan to the MWSS was implemented to improve capital investments in sewerage and sanitation infrastructure at the time the bidding processes for MWSS had begun. This served the desire to provide a ‘signal’ to the bidders that financing for capital investments had been secured (guaranteed by the government), facilitating the privatization process and increasing the chances for lower bids (Dumol 2000). After privatization, financing of Manila water projects was absent for a period while the Bank allowed the market economy to work

41 PPIAF technical assistance has amounted to at least an additional USD$360,000 on projects to advise on regulation and the use of new financial instruments such as OBA, however, complete figures were not attainable from information available on its website.
its ‘magic’, although there were other foreign lenders who pursued more intensive funding in this sector.42

<table>
<thead>
<tr>
<th>Year</th>
<th>Projects</th>
<th>Loan Amount (USD$ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>1</td>
<td>85</td>
</tr>
<tr>
<td>1992</td>
<td>1</td>
<td>68</td>
</tr>
<tr>
<td>1996</td>
<td>3</td>
<td>167</td>
</tr>
<tr>
<td>1997</td>
<td>1</td>
<td>56.8</td>
</tr>
<tr>
<td>1998</td>
<td>3</td>
<td>83.3</td>
</tr>
<tr>
<td>1999</td>
<td>1</td>
<td>27.5</td>
</tr>
<tr>
<td>2001</td>
<td>1</td>
<td>30</td>
</tr>
<tr>
<td>2002</td>
<td>3</td>
<td>250</td>
</tr>
<tr>
<td>2003</td>
<td>1</td>
<td>5</td>
</tr>
<tr>
<td>2005</td>
<td>2</td>
<td>9.9</td>
</tr>
</tbody>
</table>

(1) The two 2005 projects are still in the appraisal stage – May 2005.

While it is apparent that the government in the Philippines has been highly favorable toward PSP, undertaking intensive private sector development strategies and “leading Asia” in opening its infrastructure markets (PPIAF 2000a), it is still questionable whether the Concession Agreement with Maynilad would have continued to exist without the influence of the World Bank and other multilateral lenders.

The ‘corporate muddle’ of Maynilad and the subsequent bailout by MWSS, permitting a series of tariff increases, is not surprising after considering a few influential factors. With an impending privatization of the national electricity utility, the new government of President Gloria Macapagal-Arroyo, in attempting to demonstrate that the country’s environment was conducive to utility privatization, may have been careful about its public relations for investment climate (Esguerra 2003).

The World Bank exercised strong leverage, along with the ADB, by canceling a USD$200 million loan to the energy sector in 2000, when the portfolio reviews of the Estrada government demonstrated that the government had failed to meet several conditions of an ADB structural loan. Under pressure to recover from the extreme debt left to her administration, and the lack of foreign lenders, President Arroyo would have had little choice but to ensure the MWSS entered into agreements favoring Maynilad, despite the obvious failure of its service provision. The USD$800 million loan that Maynilad had inherited had been mainly contracted through the Philippine government carrying sovereign guarantees. The government would have been liable for the loans and could not have afforded to repay them if Maynilad continued to default.

The World Bank’s 2003-2005 Country Assistance Strategy for the Philippines differed from the previous CAS in its lack of reference to private sector development as one of its focal areas, most likely a response to several high-profile cancellations, including Maynilad, and huge public protest that had erupted in response. However, the CAS is replete with references indicating that utility and infrastructure privatization has been high on the agenda “directed towards development objectives.”

42 For example, the ADB was poised to offer a USD$350 million loan to bail out Maynilad in 2000 provided it was released from meeting its service targets.
208. The base case lending scenario of USD$1.1 billion depends on the government’s ability to decrease the public debt, increase tax revenue, and increase the environment for private investment. Maintenance of the base case scenario into 2003 was dependent on progress of three loans that had been approved totaling USD$135 million, including the second APL for the LGU privatization. Failure to maintain the investment climate would mean the loss of a USD$200 million public sector reform loan (reducing the lending scenario by half), providing much needed funds to help service the huge public debt. An improvement of the private investment climate would mean an increase in USD$200 million of loans in 2003 towards public sector reform, as well as the City Development and Investment Project that promised to enhance infrastructure, governance and finances within the major failing cities of the Philippines.

209. To date, all the loans through 2003 have been approved in full, except for the first tranche of the Public Sector Reform adjustment loan. This loan is in the “pipeline” of projects waiting approval at an August 2005 Board date and proposes a USD$50 million loan — only half of the base case scenario value. One of the possible triggers may have been the recent announcement of an increase in the VAT tax rate from 10% to 12%, increasing public revenues. Another may have been the success of the LGU APL in enhancing the local government private investment environment.

210. The 2003 CAS states that the “Bank’s objective for the next three years is to strengthen decentralization and partnership with LGUs through assistance at both local and national levels to improve rural, urban and metropolitan governance” (World Bank 2003:28). As LGUs are often the implementing agencies for sub-loans, the Bank views them as “key partners” in urban and rural development, and plans to enhance their ability to mobilize financial resources and efficiency in delivering basic public services.

211. The final report of the first LGU APL noted the frustration felt by Bank staff at the high number of cancelled projects, due to the ability of the LGUs to find non-conditional funding elsewhere in government institutions or programs, and the inability of the DBP to impose penalties on those that backed out of loan agreements (World Bank 2004b). The report also highlighted that the government had acted very little in terms of implementing the necessary reforms that would give incentive to LGUs to participate in the World Bank project. This had reduced the LGU loan to only 25% of its potential to mobilize PSP in local water infrastructure, an objective that had become central to the Bank’s infrastructure development strategies (PPIAF 2000a; World Bank 2004b).

212. By 2002, the first APL had resulted in only four out of 35 projected privately-operated water utilities – two of which were cancelled — a significant failure in terms of reducing the perception of risk for private investment and encouraging the remaining 160 LGUs to participate in the program over the next nine years.

213. Two PPIAF technical advisory grants worth USD$75,000 each had been awarded in early 2002 to improve the effectiveness of the LGU loan. The first was to propose a Contracts Administration Unit that would build local capacity for regulation and oversee the administration of the design-build-lease contracts. The other TA was to design an output-based aid scheme to be used in future LGU contracts. Based on these facts, it is likely that the structural reforms necessary to trigger a move in the lending scenarios may have been partly based on the success of the government in ensuring a more predictable and less rewarding incentive for LGUs to look to the DBP and World Bank to finance their water infrastructure expansions — “putting the squeeze on.” There is an obviously strong effort on

---

43 See the PPIAF website: [www.ppiaf.org](http://www.ppiaf.org) [accessed April 11, 2005].
44 This is being tested out in La Union province through the LGU APL2 program.
the part of the Bank to ensure that these loans are mobilized to their full potential and for their intended use as PSP incentives.

214. It is possible to argue, however, that while the hard conditionality that was employed in the Ghana case is not as conclusive for the Philippines, the use of soft conditionality clearly is -- particularly in the cases of those LGUs and water districts resistant to PSP\footnote{Evidence in the media, NGO reports, and the APL 1 Final Report indicates that there are a number of these.}. Cash-strapped local governments suffering from intensive pressures on the national government to reduce public spending and grant subsidies have few resources from which to draw on to improve their largely failing water systems. By 1997, the Development Bank of the Philippines and the Land Bank of the Philippines had outstanding loans to municipalities amounting to an estimated P12 billion (PPIAF 2000a).

215. The legal capacity and ability of LGUs to raise financial capital, and the large investments needed to improve local infrastructure in order to stimulate economic development, lead the Bank to consider investments in local infrastructure as one of its primary “partners” in local development (World Bank 2003). This has led to enhanced measures to improve the ability of the LGUs to access World Bank funds for infrastructure investment.

216. The results of the first APL for this purpose, however, proved to be a failure -- not only because of the low number of utilities that had made use of the funds, but also because only two of nine utilities that had used the loans to build new water systems were successful in bidding out to the private sector. Although the Bank admits that these utilities were fully operational, it challenges their sustainability in employing full-cost recovery while having to pay back the loan. Yet, there is no evidence to suggest that a private utility would not have the same fate - Maynilad has certainly proved that paying back loans is not as high a priority as making profits, and that there is a strong possibility that the IFIs and government could be pressured into bailing them out.

217. The World Bank’s response is to provide innovative financial means for the private sector to be unburdened, including the use of output-based-aid, community-driven development so that the poor can be serviced by NGOs or themselves, and government guarantees to manage the risk for loans.

218. These same financial tools are not available to utilities choosing to remain publicly operated. Instead, these have to implement principles of full-cost recovery without access to World Bank loans, government subsidies (that are being eliminated through World Bank adjustment policies), or technical assistance grants from the IFI or PPIAF. As the APL loan demonstrates, there is no attempt to quantify and compare the costs and benefits of each strategy, despite there being clear ‘benchmarking’ opportunities. The ideology of private sector participation continues to dominate over realistic goals of poverty alleviation and public accountability.
5. OUTLOOK ON CONDITIONAL WATER PRIVATIZATION

219. The increasing capacities of civil society organizations to produce research and critically analyze World Bank policy and discourse have contributed to global knowledge and solidarity against water privatization. This increased public exposure challenges the Bank to find new ways of facilitating private sector participation in water utilities in the face of popular opposition and government resistance.

220. Mosley et al. (2004) have argued that the World Bank and other IFIs are operating somewhere between traditional conditionality and full country ownership without conditions, in what the authors call ‘new conditionality’. The new conditionality is characterized by a balance between appearing to provide space for country ownership and ensuring that countries with ‘poor’ policies adopt the Bank’s selection of ‘good’ policies. This can be achieved through more concrete efforts to promote Bank-funded and provided technical assistance and advice, research production and dissemination, and discursive strategies aimed at directing countries to one or limited options.

221. The World Bank is committed to water sector privatization, as evidenced by various indicators: speeches by Bank executives; research focused on private sector policies and facilitating investment in infrastructure; and, availability of financing, grants and technical assistance for private sector projects. There is a decided lack of strongly conclusive research examining whether private utilities are more efficient, sustainable, and capable of meeting social goals than public utilities. In instances where water privatization is advocated by the World Bank as the most viable option for improving the utility, there are no published studies published indicating how this conclusion was reached. The World Bank’s policy guidance on evaluating public and private sector options gives no indication of how (or even if) Bank staff compare and contrast all the possible options (World Bank 2004e). The policy guidance does not include any discussion comparing the drawbacks of both models (and all or any other options). There is an almost explicit assumption that the option chosen will be to privatize.

222. The Bank affirms that only already ‘well operating’ public utilities will be supported, yet Bank privatization projects and loans consistently support inefficient and corrupt private utilities through increasingly transferring the risks and costs back onto the public sector, and financing the capital investments that the private companies had promised to undertake in order to win the utility.

223. Under the current implementation measures for water sector privatization, governments need to guarantee multilateral loans for the private utility to invest in capital improvements (from which they will not profit); provide subsidies to finance coverage to the poor (which governments are prohibited from providing to public utilities); re-train their remaining employees (after extreme retrenchment of staff) to become effective regulators (when these same personnel are assessed to be ineffective operators); and link water tariffs to automatic adjustments based on the exchange rate (to mitigate financial risk for the foreign operator investing in the risk-prone economy).

224. Clarke et al. (2004), although not advocating public sector water utilities, argue that “the same governance and institutional factors in a country that exacerbated problems in the water sector in the first place can cause problems under private ownership” (2004:5). Nevertheless, the World Bank provides almost no comparative research or opportunities to the public sector to develop the capacity to become viable.

---

46 In fact, Mosley et al. (2004) refer to Ghana as one of the countries considered to be under the regime of `new conditionality`. 
225. For countries such as the Philippines and Ghana, characterized by intense structural adjustment policies implemented by controversial governments, and followed by even higher debts and economic crisis, there are few options for any level of government to find alternatives to water privatization in order to access World Bank financing. Ironically, it is the result of Bank-led structural adjustments that required retrenchment of public employees, reductions in public investment, divestiture of public assets, and implementation of cost-recovery policies, that have created a virtual vacuum in water sector investment and spending over the past decades.

226. Thus, it is no surprise that these public utilities are failing in terms of improving services and management. The World Bank has not recognized or acknowledged its role and responsibility in constructing the current situation; rather, the Bank argues that the problems are inherently due to the nature of the public sector, thus legitimating its position on preferential options for privatized utilities. Governments are forced into weak bargaining positions where their administrations require huge sums to finance high debt service - money that only the IFIs have the capacities to provide. There are few indications of any real options available to governments; hence, it is impossible to conclude that their identification of water privatization strategies in the PRSP represents legitimate country ownership. The depth of indicative country ownership must be critically questioned, given that the PRSPs are developed in contexts of high debt, with objectives of obtaining World Bank financing, and in face of growing civil society opposition to water privatization.

227. In both Ghana and the Philippines, World Bank loans have carried explicit conditions of privatization. In Ghana, over the past few years, the HIPC process has included both IMF and World Bank conditions leading to the facilitation of water privatization. The Urban Water Project (as a lease contract rather than an operating contract) had, in fact, been promoted by the Bank since 1995 but the government’s repeated failure to demonstrate its commitment to implementing the privatization process meant the project was postponed until 2004. Concurrent with the announcement by the World Bank of intentions to finance a USD$103 million loan for private sector participation in the water sector, Ghana achieved its HIPC Completion Point, granting it more than USD$1 billion in much-needed debt relief.

228. In the Philippines, the issue of conditionality is more controversial, as the Ramos government appears to have been strongly committed to water privatization and private sector participation. What was considered to be the “world’s largest water privatization” demonstrated itself to be a failure by 2002. The experience has resulted in extremely high tariffs, increasing public debts (as the government has had to ‘bail out’ the private sector), and a lack of accountability on the part of the private utilities to maintain service levels.

229. There have also been high legal and social costs associated with the ongoing controversy, particularly with Maynilad. While there have been some modest improvements in water service coverage and connections under the privatized model, these have come at huge external costs that have failed to be quantified in superficial discourse over the benefits of the private sector. The Arroyo government initially seemed hesitant to continue promoting the private sector utility; however, faced with an impending electricity privatization and the need to ensure a risk-free environment, as well as the extremely high debt requiring assurances of future World Bank funding, it is not necessarily surprising that the Arroyo administration discursively appears to support the Manila concessionaires.

230. The influence of local elites on privatization-centered policies in Manila is noteworthy – the Lopez family, which has an interest in Maynilad, controls a significant portion of land and services in the West Zone. Understanding the influential role of the local elite may help explain the level of perceived government ownership in the water sector.
231. There are increasing indications that the World Bank is more directly facilitating water sector privatization with local governments. In the Philippines, the Bank’s appraisal of its LGU privatization project indicated severe frustrations with the central government’s lack of action in ensuring that the LGUs would look to the Bank for financing and remain committed to contracts. Recently, the National Economic Development Authority of the Philippines (NEDA) announced that the IFIs were looking at the possibilities of directly funding local governments, rather than having money funneled through the national government.47

232. This approach gives the World Bank more influence over local politics and policies, as well as promoting water sector privatization from the ‘inside out’ – by starting with pressure at the local level - in order to avoid hard conditionalities at the national level. The strategy circumvents national governments’ reluctance to privatize, while avoiding large-scale public scrutiny. This encourages the practice of applying conditional lending without hard conditionality, and will be most effective in areas where resources are low. The strategy further contributes to the identification of new allies and support for water privatization as opportunities open up for private sector involvement by the local elite and other local actors, particularly in areas where resources are low or incomes are extremely polarized.

233. These new relationships can serve to enhance inequalities and redefine local power dynamics, where the economic benefits are concentrated in limited hands and negative externalities continue to pile up on the poor. Thus, the ‘new conditionality’ as practiced by the World Bank involves the creation of new actors within countries and outside national governments that can act as key figures in applying internal pressures to privatize, as well as legitimize government announcements of water privatization as representative of ‘what the people want’.

47 Business World, April 15, 2005.
6. REFERENCES


Fletcher, Kevin. 2005. Increasing Public Sector Revenue in the Philippines: Equity and Efficiency Considerations. In *IMF Working Paper WP/05/22*, Report No.: International Monetary Fund, Fiscal Affairs Department,


