Sustainable Water Integrated Management (SWIM)

Expert Facility Activity No EFS-LB-2

Procurement of PPP in the Water/Wastewater Sector

Day 2 – Session 2.1:
The Creditworthiness Challenge as a Prerequisite for PPP

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What have utility success stories in common?

- ✓ Utilities have been able to set prices that recovered costs
- ✓ Effective management, empowered to do their professional job
- ✓ Accountable to external policy and regulatory authorities
- ✓ Their concrete impacts on poor people's access to services made sustainable by operational and financial viability

As a result, utilities have been able to raise commercial finance & contribute their own resources for investments to improve services

Importance of Creditworthiness

Creditworthiness is the ability and willingness to repay debts and to honour financial obligations fully and on time

Source: World Bank Utility Creditworthiness Academy, Johan Kruger (AfCap Consulting), 2016

Importance of Creditworthiness

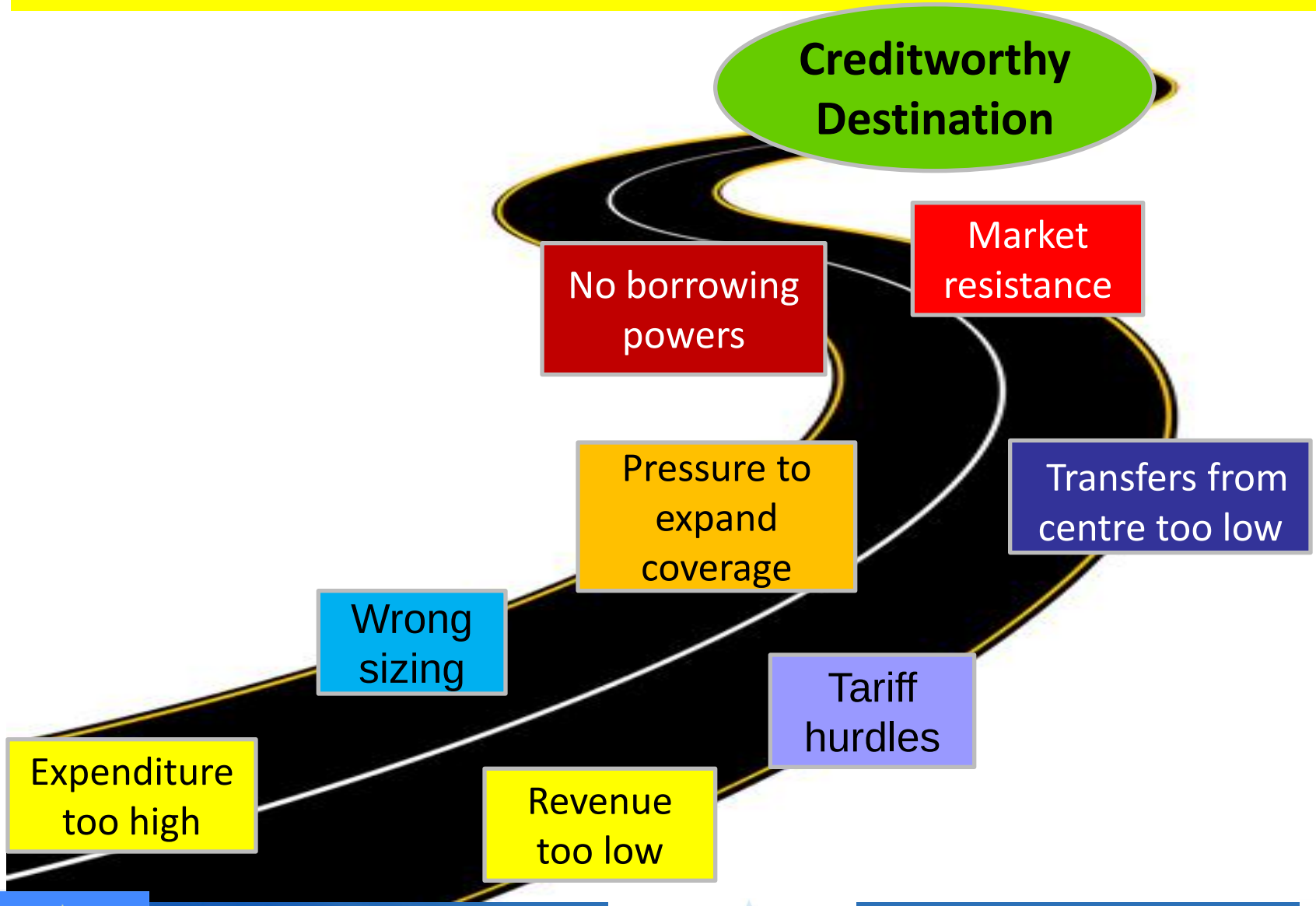
Creditworthiness means you are

worthy of credit

in the eyes of the potential lender or PPP operator

Often categorised by rating symbols

The road to Creditworthiness is full of challenges



Advantages of being creditworthy …

1. Creditworthiness requires more management discipline, leading to overall performance improvement
2. Creditworthy utilities can access more financing to accelerate provision of infrastructure
3. The higher the creditworthiness, the lower the price of debt and the more interested is the lender
4. Creditworthiness leads to less dependency and more autonomy
5. Results of peer comparison and benchmarking are improved

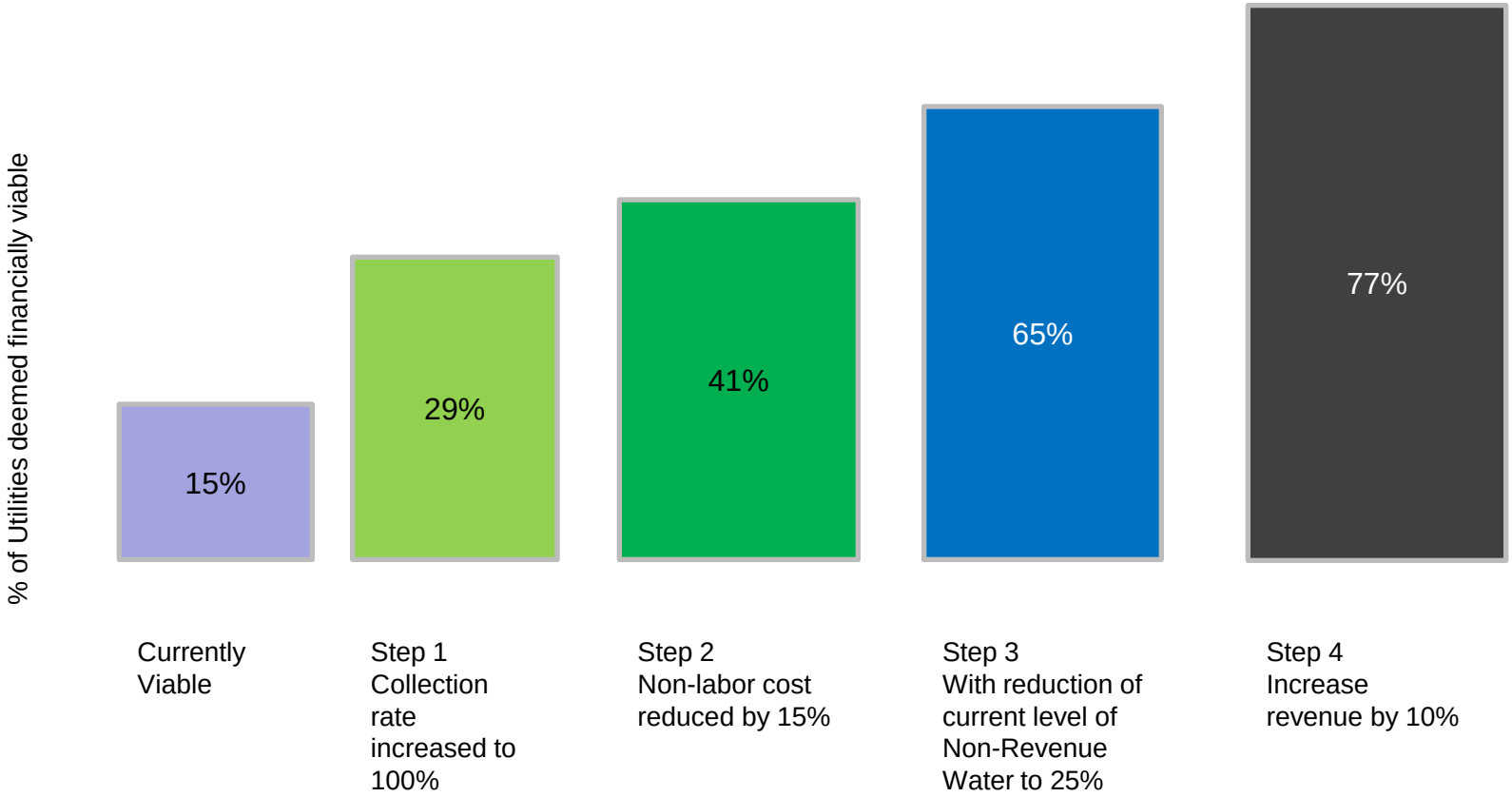
Ways to reduce the cost of borrowing …

- ✓ **Become more creditworthy to reduce risk premium**
- ✓ **Have a transparent long term capital investment and funding plan**
- ✓ Approach right funders for right project
- ✓ Acknowledge areas that need improvement and have a reasonable plan
- ✓ Provide collateral
- ✓ **Utilize Blended Finance**
- ✓ Utilize available Viability Gap Funding
- ✓ Utilize credit enhancements like guarantees

… on Governance

- ✓ Creditworthiness requires a paradigm change in utility corporate governance
- ✓ Shift from being a government department to an entity which is managed as a business
- ✓ Proceed towards development of a shadow, and eventually a formal credit rating

Operating Efficiency and the Impact on Financial Viability



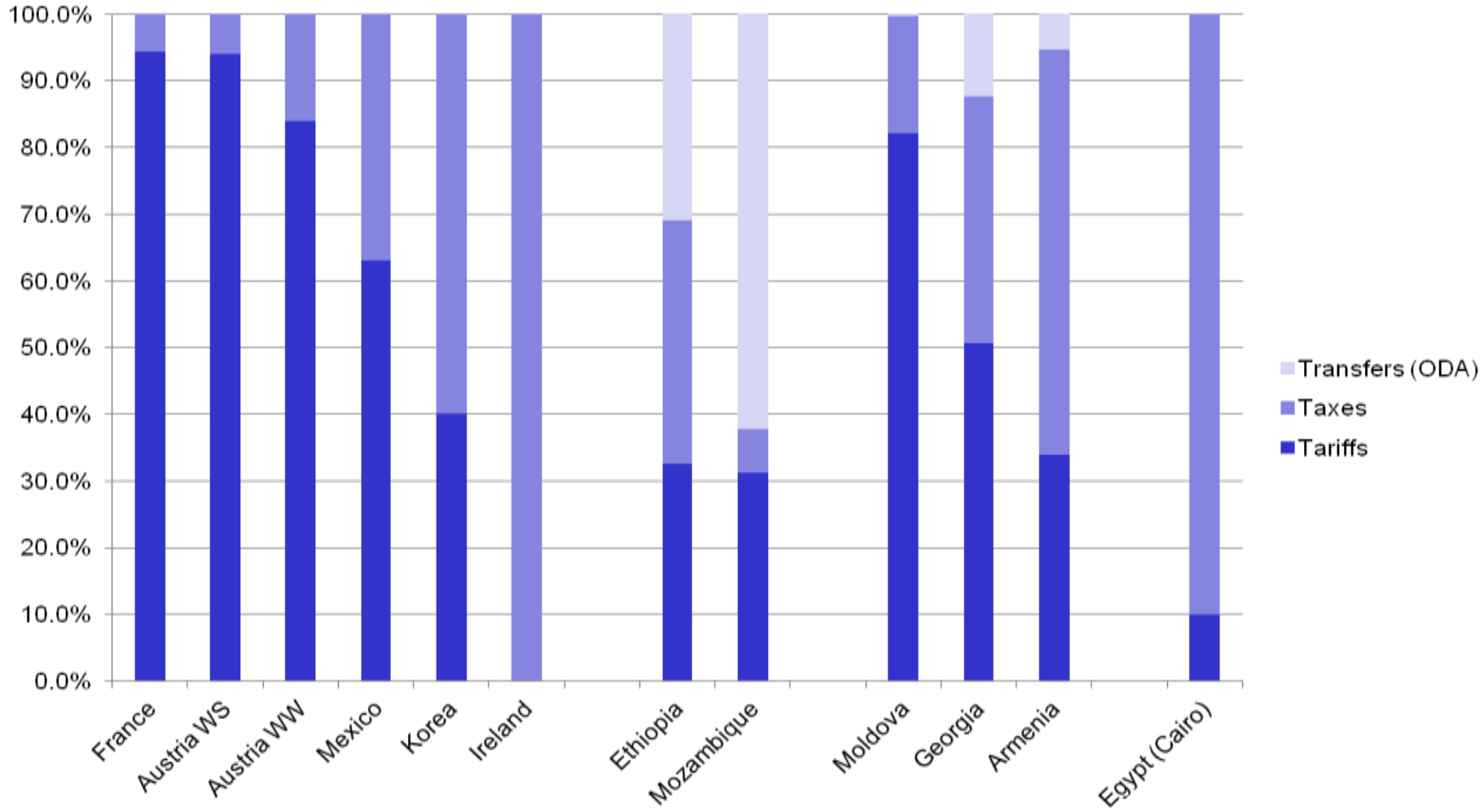
Note: Sample 690 utilities operating in selective emerging markets
Note: Financial viability is utilities with an operating ratio > 120%

Source: IBNET 2016

Resources available to meet Revenue Requirement

Type	Advantages	Disadvantages	Uses
Transfers	- Free money! - World Bank loans only provide resources to the extent of concessionality	- Very limited quantities - Often unreliable	- Targeted OBA - Financing CAPEX - Occasionally for OPEX
Taxes (Local Govt. Grants)	- Additional to what consumers can pay - Can be targeted to social needs	- Often unreliable - Paid by taxpayers (who may also be poor)	- Targeted subsidies - Funding CAPEX - Operating subsidies - Bail outs
Tariffs	- Could grow automatically as service expands - Reflects value of service - Promotes accountability + customer orientation	- Raising tariffs can reduce affordability - Raising tariffs is unpopular	- Covering O&M - Providing return on capital/debt service - Generating surplus for investment in assets

The 3Ts in selected countries



Source: OECD, Stockholm Water Week, August 2011

Inappropriate mix of the 3Ts …

Increased investment risk is often caused by an inappropriate mix of the 3Ts to recover costs

- Cash flows cannot support investment
- Vicious cycle of inadequate investment, declining service and unwillingness to pay for poor service
- Explains the limited attractiveness of the sector

Source: Managing Water for All: An OECD Perspective on Pricing and Financing, Key Message for Policymakers, OECD 2009

Credit enhancement

Means of improving your creditworthiness by the utilization of third party support, collateral or other financial instruments essentially to reduce or migrate risk or components of risk

Where risk mitigation can make a difference

- Adequately Creditworthy – Do Not Require Risk Mitigation
- Near Creditworthiness
- Marginally Creditworthy, but Reforming
- Non Creditworthy and Low Performing

Risk Mitigation Instruments Could Be Effective

Thank you