

OECD – GIZ Conference: Closing the gap for water in line with SDG ambitions: the role of blended finance

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“Bridging the bankability gap”

- Christopher Gasson

Before we can talk blended finance, or even concessionary or any other type of finance, we need utilities that are good investment prospects. Christopher Gasson, Publisher of Global Water Intelligence outlines a strategy.

Around 80% of ODA finance to the sub-Saharan urban water sector goes to the top 3% of utilities according to an analysis by Global Water Intelligence. It reflects the fact that the vast majority of utilities are simply not considered to be bankable. That is to say that have a tendency to destroy rather than create value through the way they operate.

It gives rise a perverse situation in which there is potentially plenty of money available for investment and almost unlimited demand for that investment, but very little capital actually being deployed. It also suggests the most effective strategy for value creation in the urban water sector is in delivering bankability to weak and underperforming utilities.

William Muhairwe’s 2ML was established on the principle that there are three main reasons why utilities fail to perform: Management, Management and Leadership. On that basis he has introduced a utility Performance Improvement Programme to help the CEOs of struggling utilities turn around the fortunes of their organisation within 100 days. It has been applied successfully in Sierra Leone, Ghana, Rwanda and Nigeria. In each case the turnaround in performance has rapidly attracted donors and lenders looking to support the continued turnaround story.

It shows that it can be done. The next challenge is to see how it might become on a larger scale. That is why we are proposing a Water Performance Fund. This would part-finance utility turnarounds on a success fee basis, then support ODA lenders to ensure that the performance improvement continues in the long term. The benefits of this approach are as follows:

- 1) **It improves the effectiveness of ODA funding:** at the moment ODA funders have the choice between putting money into high performance utilities which could probably access commercial funding anyway or putting money into non-bankable utilities and see it wasted. The Water Performance Fund will create a pipeline of bankable utility projects which enjoy a high probability of success without the risk of crowding out commercial finance.

2) **It is results oriented:** most ODA funded technical assistance and capacity building at utilities is carried out on a fixed fee basis. Delivering the project to spec is more important than the broader outcome of achieving bankability and longer term performance improvement. The Water Performance Fund is incentivised to deliver success to its clients (the utilities) and their stakeholders.

3) **It can deliver success at scale:** SDG 6.1 is never going to be delivered on hand pump at a time. It is going to be delivered by industrialising the process of improving access to water. By systematising the process of making utilities bankable, and deploying this expertise across the world, we can deliver change at scale.

The Fund would work as follows. First it would raise \$20 million in equity from ODA funders and impact investors. This capital base would fund its working capital – ie the work it does on developing and delivering projects before it receives success fee payout. Then it would begin to develop the business. This would involve locating utilities which favourable conditions for turnaround (this would mean looking for leaders who can deliver change and politicians willing to support it), and negotiating performance improvement programme contracts with them. These programmes would be part financed by the client and part financed by the Fund. The success fee would be related to milestone achievements (such breaking even in terms of cash flow or bringing capital into the utility) and cover the cost of the programme. The next stage would be to secure further funding for the utility and to monitor and manage the on-going performance of the utility on behalf of the lenders and donors in exchange for a performance related management fee.

The objective is to build an organisation which can close the bankability gap for 20 utilities serving a total of 10 million people per year. By 2030 it would have had an impact on more than 100 million people. It would start in Africa but spread to all other regions where weak utility performance impedes investment. Although ODA funding will be required in the early stages of utility performance improvement, it would create a strong platform for the development of blended finance and eventually fully commercial finance within the sector.

Christopher Gasson is a Publisher at Global Water Intelligence.