

Sustainable Economics for Water and Sanitation

1. Overview

The social, environmental and economic benefits of providing water supply and sanitation to people and businesses and of collecting and treating water after use are far more significant than is normally recognised. Water, sanitation and pollution alleviation are often seen as matters that are expensive and politically unattractive. This needs to be understood differently. These activities provide very significant direct benefits, as well as very substantial indirect benefits, to individuals, economies, and environment. They contribute significantly to national wealth, societal well-being and protection of natural capital. They also eliminate broad areas of avoidable direct and indirect costs, which hold back development.

Reliable and efficient water and wastewater services and pollution control systems are a clear indication of a stable and well governed society. These services enable people to enjoy productive and healthy lifestyles, to benefit from education and employment and to live in environments that are attractive and rich in biodiversity.

To deliver these benefits, these services have to be established and operated on a sound economic basis, where there is sufficient and predictable revenue to ensure that capital investment, operating costs and renewal and maintenance expenditure can be covered adequately over the long-term.

Sustainable economics of these public services can only be achieved when the communities that benefit contribute themselves to the costs. This can be done through cash flows based on tariffs charged to users, taxes levelled on the community, or some combination of the two. Additional financing from transfers from national or international budgets can be useful to provide temporary injection of funds, but it is not sustainable over the long term. These three mechanisms, Tariffs, Taxes and Transfers (the 3Ts) are the fundamental elements of sustainable cost recovery. When stable and predictable cash flows are established using these tools, additional repayable finance in the form of loans from international financial institutions or commercial banks can be mobilised. These processes combined are often referred to as “sustainable cost recovery (SCR)”. This is to be distinguished from “full cost recovery”, which may be socially or politically unattainable.

2. Key messages

- 2.1. The sustainability of all water and sanitation services is dependent on sound economics. This means having sufficient and predictable flows of cash to enable the costs of operation and maintenance to be covered, investments to be planned and their costs to be repaid.
- 2.2. Assuring the sustainable financing of water and sanitation infrastructure and operations is essential to ensure that all the other benefits and policy objectives generated by these services can be delivered to the service users. Sustainable financing must therefore be considered a pre-condition to all other policy objectives.
- 2.3. There are many economic justifications for ensuring adequate financing for the provision of water, and sanitation and de-pollution including:

- ✓ Reliable access to satisfactory water and sanitation services eliminates the "coping costs" that are necessary when the services are inadequate or unavailable. Studies show that coping costs can reach 20% of household incomes. Poor households are usually the most seriously affected and burdened by coping costs.
 - ✓ Water, sanitation and pollution prevention are powerful and effective tools for public hygiene and preventive health. They follow the principle that prevention is better than cure. Water-borne diseases are among the most common causes of death and disability and are almost entirely preventable. The WHO estimates that about half the hospital beds in the developing world are taken up by people suffering from water related diseases. The cost of providing and maintaining a hospital per bed is many times that of delivering a water and sanitation service. Water and sanitation investments are therefore very cost effective solutions for public health.
 - ✓ The loss of educational opportunity related to lack of adequate water and sanitation services is serious handicap in many cases. The costs of this are considerable to both individuals and the economy of a country as a whole.
 - ✓ Poor education and poor health that result from lack of adequate water, sanitation and pollution removal have serious implications for employment, productivity and purchasing power, and therefore directly affect societal wellbeing and economic performance.
 - ✓ Access to water and sanitation services has a positive impact on property values, while polluted water bodies reduce values. Clean water bodies and clean environments are more attractive and have richer biodiversity, which give rise to better human wellbeing and to economic activities, notably leisure and tourism industries.
 - ✓ The positive benefits of water, sanitation and de-pollution on the economy improve the tax revenue base for the government. The net benefits outweigh the costs by a considerable margin.
- 2.4. In the vast majority of cases it is a political responsibility to set the prices or cost recovery mechanisms for water, sanitation and de-pollution services. These cost recovery systems need to be set with a realistic relationship to the real costs incurred in delivering the services, irrespective of the nature of the service supplier (public, private or other).
- 2.5. Failure to ensure sustainable financing of water, sanitation and de-pollution leads directly to a vicious downward spiral of failing services and increasing costs to consumers, society, the economy and the environment.
- 2.6. Affordability must be tackled in a structured way, identifying affordability for both individual users, and for the community as a whole. SCR enables decision-makers to see the risks and benefits of alternative financing and subsidy policies and minimise adverse consequences of subsidy payments.
- 2.7. Setting water service prices for a whole community on the basis of "ability or willingness to pay" of the least affluent is a trap to be avoided. Prices should be set on the basis of covering the costs to provide services to the average consumer, with special provisions to support those who are truly unable to pay that price.
- 2.8. Without SCR the newly recognised right to water and sanitation is an empty promise. The misconception that the poor cannot pay leads to their exclusion by default and creates even greater costs for them. Failing to provide them a proper service for which they will pay less is unfair. There is no disconnect between SCR and extension of access to the poor.

3. Policy recommendations

- 3.1. Water services should be prioritised in public budgets, recognising the extensive benefits they provide
- 3.2. Water services should be paid for on a sustainable basis by the communities that benefit from them. Decision makers should determine how this is done by applying the principles of Sustainable Cost Recovery (SCR).
- 3.3. The policies and processes for setting and regulating cost recovery and charging mechanisms for water services should be applied on the same basis for all forms of service operator within the jurisdiction.
- 3.4. Specific provisions for assessing and targeting support to people who have difficulty to pay should be set up in ways that do not undermine the overall economic viability of the service provision to the whole community.
- 3.5. Specific policies are required to show to all stakeholders the objectives and processes used in deciding on a particular SCR scheme. These should be reviewed and adjusted periodically as conditions evolve.