

**Water Tariffs and Subsidies in Africa :  
Impact on Poverty, Expansion of Water  
Services and Sustainability of Utilities**

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**An oft repeated story...**

- Access to drinking water is a basic need.
- Access to safe water has tremendous direct and indirect impacts on poverty-related outcomes
- Thus, access should be provided to everyone at affordable tariffs.
- Basic starting point :
  - Drinking water is provided by utilities.
  - Thus, subsidies should be given to utilities so that they could pass it on to consumers.
- What is wrong with this line of argument ?

## Talk Outline

- Delivering subsidies to consumers: some difficulties
- Impact of utility subsidies on poverty, expansion of water services and sustainability of utilities
- Reforming subsidies to utilities
- Beyond utility subsidies

## Difficulties: Delivery (1)

A series of bottlenecks constrain the delivery of services (and associated subsidies) to the poor

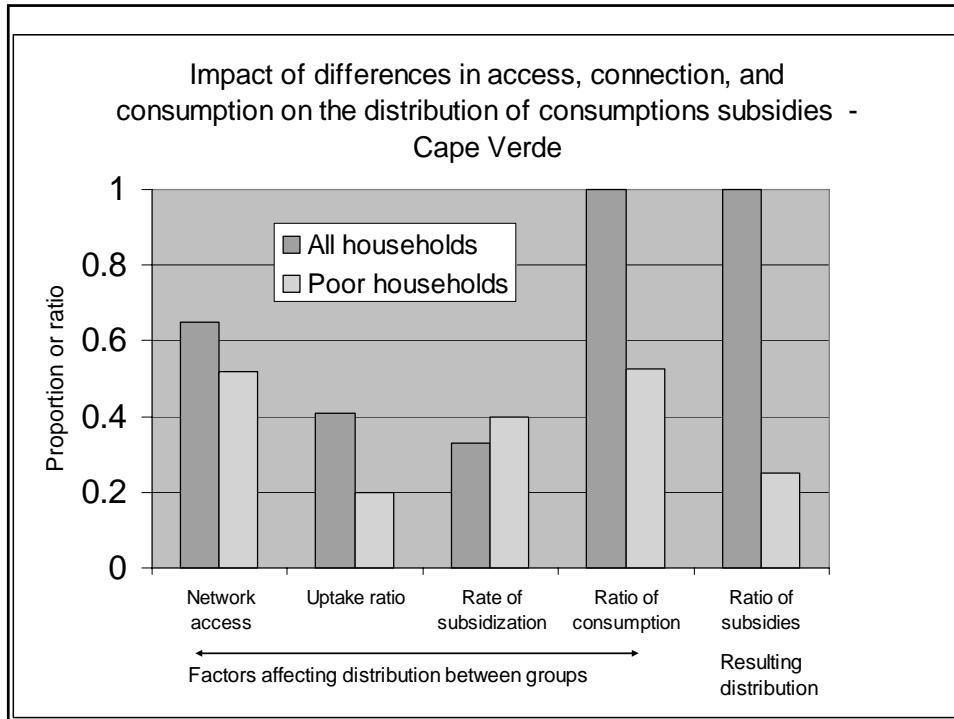
Case of consumption subsidies

Theoretical problems:

- Access to network
- Connected / not connected (given access) : relatively high (Figures WB report)
- Undifferentiated consumption level between poor and non-poor households (Figures WB report)

Practical problems

- Initial Block of tariff set too high : everybody is subsidized
- Shared connections mean paying the highest unit price (individual connection but also kiosks/ standpipes)



## Difficulties: Delivery (2)

As a result,

- Coverage of the poor population is often weak (high proportion of poor do not get subsidies)
- Targeting is also deficient (A large portion of subsidies go to high income households)

Alternative strategies :

- differentiated services (standpipes)
  - poor “self-select” into lower-quality service
  - highly (totally) subsidized. Does it work ? (India, Nepal)
- Administrative targeting (geographic ; means testing)
- Combination of administrative, tariff and quality targeting

## Difficulties: Financing Problems (1)

Financial support to utilities from government

### Risks :

- Government liquidity constrained
- Incentive problems
  - Utility : not to improve performances (subsidies are not passed on to consumers)
  - Government : delay maintenance (long-lived assets) and let service quality deteriorate

Cross-subsidies, e.g. industry pays for households

### Risks :

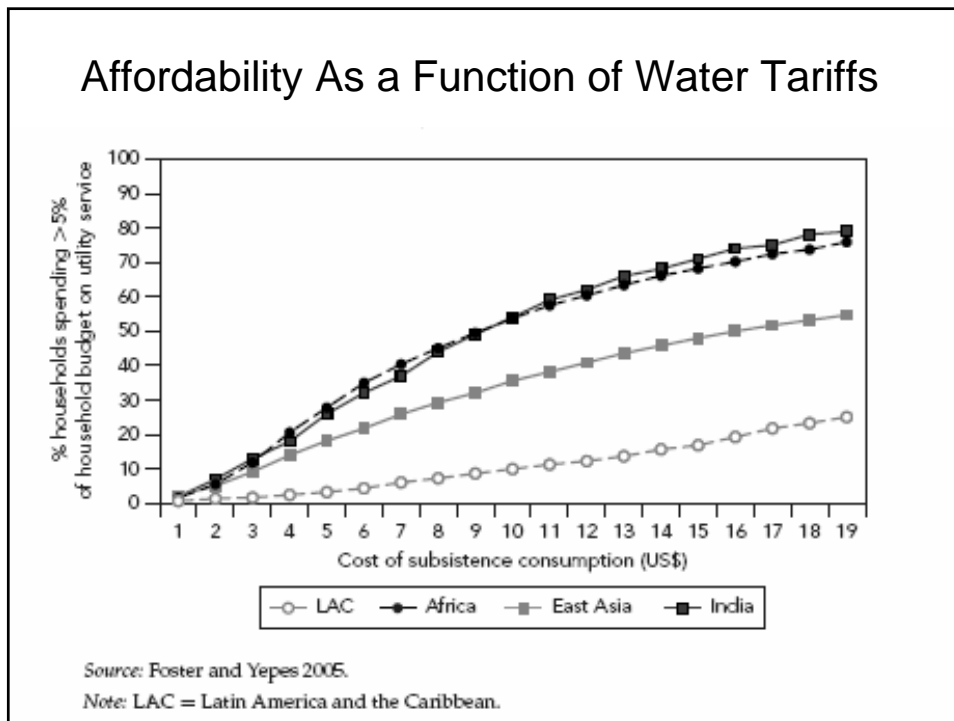
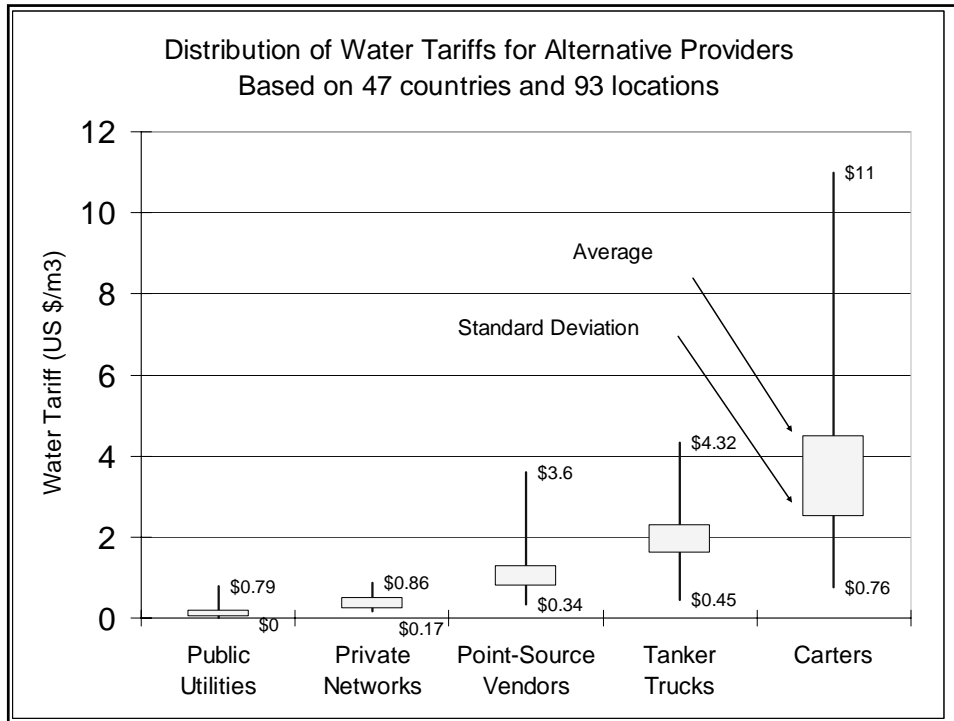
- Few net contributors
- Shrinking base of net contributors if possibility of alternative provision (Cote d'Ivoire)

## Impact of Utility Subsidies : Poverty (1)

- Expenditures for W&S represent between 3 – 5 % of total expenditures of poor households : not “too high”

BUT ....

- Expenditures on water are highly variable
- can be very high for those with no access to public connections
- Even households with private connections often rely on other water sources



## Impact of Utility Subsidies : Poverty (2)

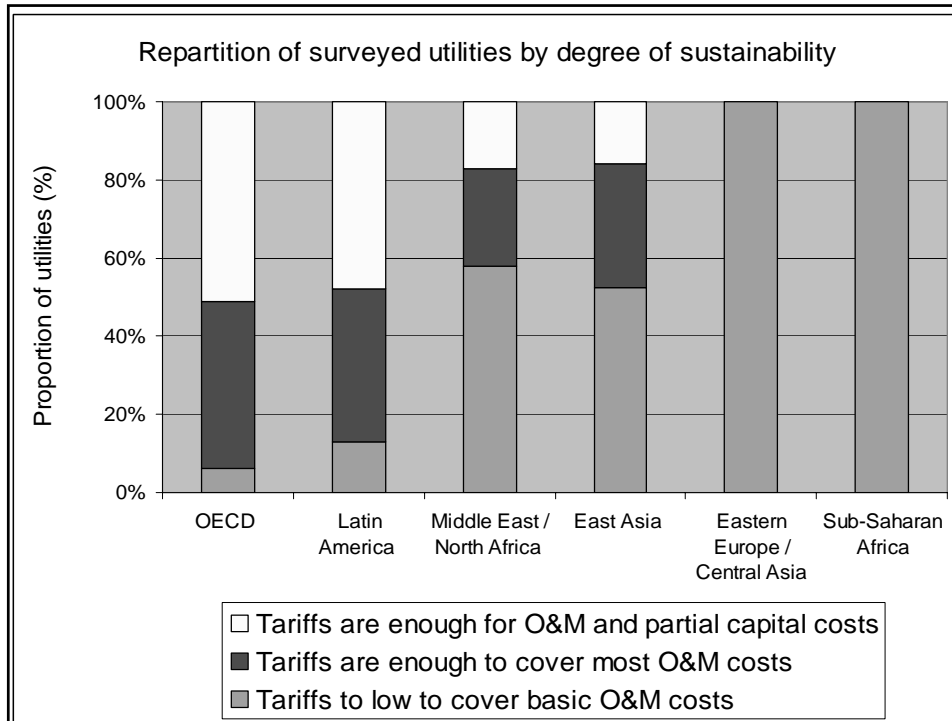
In conclusion :

- Due to limited coverage of public networks (especially in Africa), water subsidies through utilities are not a good way to redistribute income
- However, potential need for targeted consumption subsidies, stronger in Africa
- In practice, due to limited coverage of public networks, subsidies concentrated on utilities leave most of the poor aside.
- Connection subsidies are rare, although their social return would often be very high
- Alternative service quality : problem of the middleman (e.g. Kenya, standposts)

## Impact of Utility Subsidies : Sustainability of Utilities

Structural tendency to underfinancing by governments, combined with reluctance to make people pay “too much” for water, results in :

- Declining quality of service
  - people / industries have to secure consumption from other providers
  - higher rates for industrial customers may lead industries to opt out
  - further undermines the financing base of the utility
  - more rapid degradation of the assets
- Low incentives to efficiency improvement for utilities
  - higher efficiency => less transfers ?
  - for regulator / government : difficult to sort out efficiency issues from subsidy issues



## Impact of Utility Subsidies : Expansion of Water Services

- General low cost recovery of water utilities precludes expansion of networks (structural deficit does not allow for new investment)
- No incentives to extend network
  - more connections => more losses
- Regulation may impose uniform tariff (e.g. Universal Service obligations (USO)).
  - May make marginal areas unprofitable (sub urban and peri-urban land : where urban expansion is concentrated !)
- Connection subsidies more recent, less frequent than consumption subsidies

## Reforming Utility Subsidies

### 1) Know your (potential) customers !

- Who needs subsidies ? WTP estimates show that proportion of households needing subsidies may be lower than what current tariffs imply
- Collect data and information:
  - Who are the recipients of current subsidies ?
  - What factors are limiting take-up in connected areas ?
  - How do households not connected to the network cope ? How much do they spend on water ?
  - How can current subsidies be reformed to decrease leakage and increase coverage (simulations)?

## Reforming Utility Subsidies

### 2) Separate subsidies from finance

Social concerns are highly legitimate, but

- Responsibility to assist poor customers belongs to government, not utility
- Sustainable tariffs are the best guarantee to sustained services and investment by utilities
  - Better management of existing assets
  - Attracts additional investment
- Make subsidies more transparent (consumer versus utility) and efficient (targeted versus across-the board)
- Provides better incentives for utilities and governments
  - Utilities : improve efficiency and sustainability
  - Government : financially assume subsidies
  - Links with output-based aid
- Overall recommendation in other fields (e.g. housing)



## Beyond Utility Subsidies

Crucial benefits provided by access to safe water; yet only a fraction of population covered by public networks.

- Policies should be focused on increasing access.
  - How to finance network extension ?
  - How to incorporate alternative providers in the global picture?
- Shift the bulk of subsidies from utility subsidies to subsidies encompassing other forms of provision
  - Connection subsidies
  - Differentiated services
  - Alternative providers

**THANK YOU !**