Universidad de los Andes
Facultad de Administración

"Local institutions and water firms structure and governance: the case of Colombia"

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FIRST INTERNATIONAL FORUM
on regulation of water services and sustainability

Rome, January 21, 2209

The Cycles of Infrastructure Financing

- The approach to finance infrastructure investments, after two decades, is coming back in its pendulum swing from mostly private towards a more public participation
- Conceptual simplification has pushed the private alternative across the board, even in circumstances where (with hindsight) competition or independent regulation had little chances to flourish
- Challenge: avoid the return to the mistakes of *étatism* while recognizing the limitations of the purely private option. Proposal: *Contingent Contract Choice* (CCC)

The Cycles of Infrastructure Financing

- Proposal: *Contingent Contract Choice* (CCC)
- City size, income distribution, polity and politics dynamics, fiscal programming, role community governance and cultural beliefs, quality of civil service, contract enforcement
- Evolutionary approach. Use of Avner Greif´s ideas of self-enforcing and self-reinforcing measures to consolidate institutions and progressive traditions

A framework for infrastructure investment

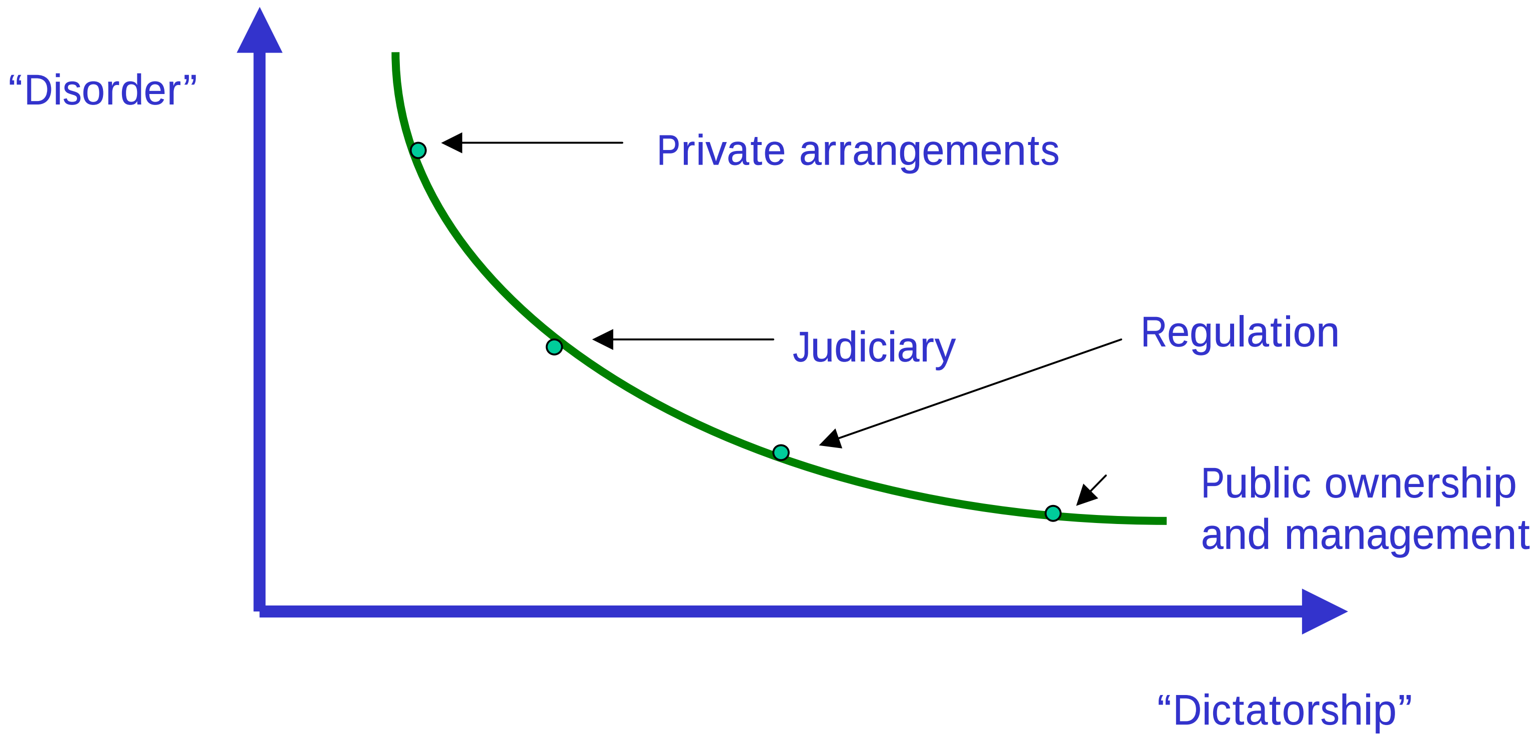
Basic conditions	*Short-term measures*	*Goals*
Project yields positive net social surplus	Economic evaluation consistent with potential impacts; comparison of alternative solutions	Sector plans linked to development policies; balanced maintenance vs. expansion decisions
Financial structure conforms to local context	Choice based on fiscal space, profitability and property rights defense efficacy (rule of law)	Effective sector fiscal programming and enabling business climate
Sector organization and governance evolving in the right direction	Self-*enforcing* measures needed for project success; mitigation of current weaknesses	Institutional achievements self-*reinforce* over time

A framework for infrastructure investment

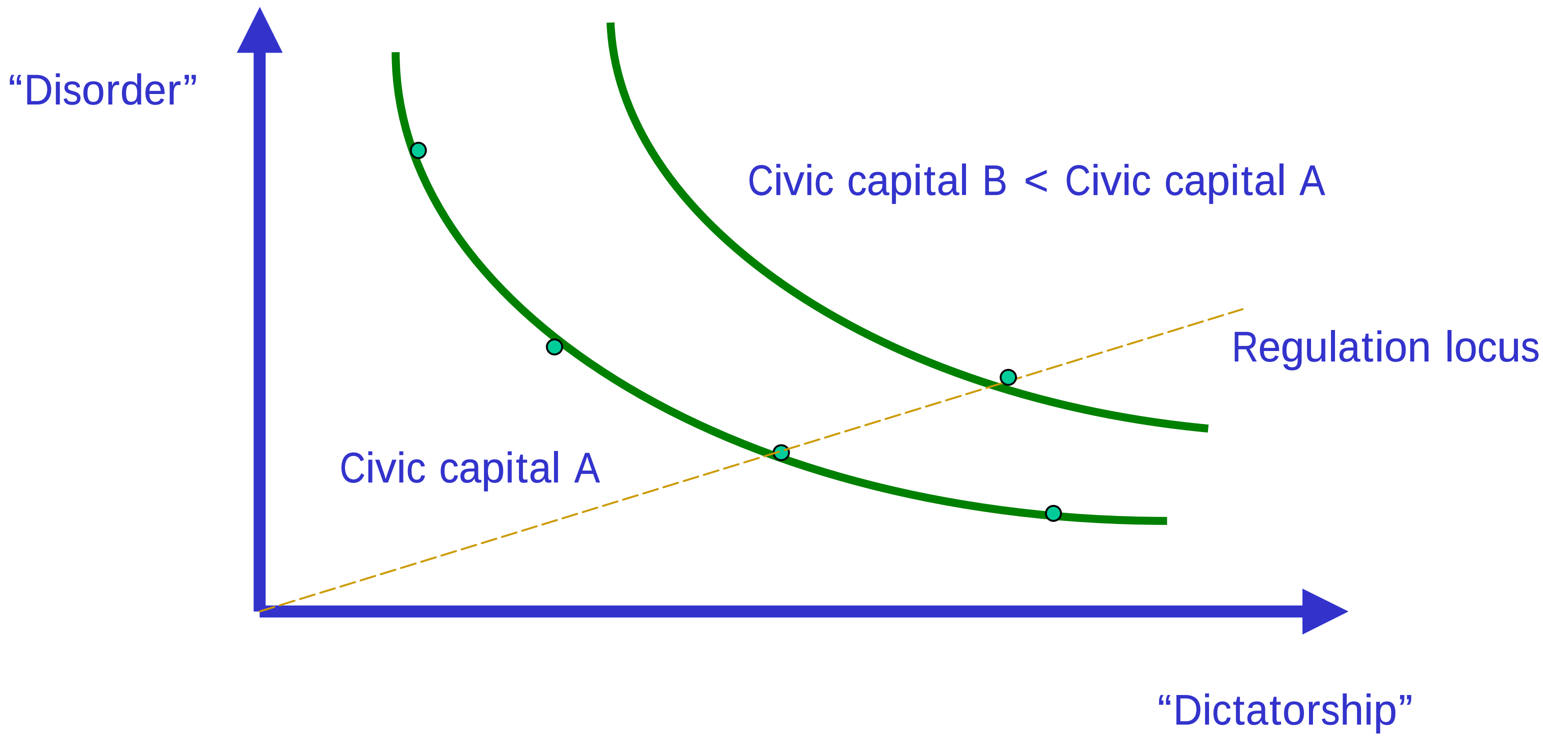
- *Plain vanilla* variety of PPP: private sponsors respond to high-powered incentives and governments honor payments schedule (including guarantees)

- This structure will only deliver under very stringent conditions (not generally observed in Colombia):
  - Sufficient public funds to make government payments credible
  - Strong judiciary, regulation and dispute resolution mechanisms that minimize chances of *ex post* opportunistic behavior

A framework for infrastructure investment



A framework for infrastructure investment



Contingent Contract Choice

- Based on Vives, Paris, Benavides (2006). Assume that *fiscal space*, *project profitability* and *rule of law* are the conditions dictating the fundamental risks of a project. For simplicity, restrict such conditions to take only two values, High or Low
- Proposal: (i) profit-sharing arrangements to minimize expropriation risk and the overcosts of renegotiation; (ii) plain vanilla PPP where the efficiency-fiscal tradeoff applies; (iii) mobilization of non-cash resources when fiscal space is insufficient and projects are non-profitable
- A larger menu of “contract flavors”

Contingent Contract Choice

Case 1: High fiscal space credibility

Project profitability	Low (Rule of law)	High (Rule of law)
High	- PPP_C: profit-sharing	- Pure privatization or concessions -PPP_A: public guarantees
Low	- PPP_D: construction contracts - Civil works contracts	- PPP_B: classic PPP with recurrent public payments/subsidies

Rule of law

Contingent Contract Choice

Case 2: Low fiscal space credibility

Project profitability \ Rule of law	Low	High
High	- PPP_C: profit-sharing	- PPP_C: profit-sharing
Low	- PPP_F: public/community procurement (matching efforts)	- PPP_E: concession revenue supplemented by land use rights

Contingent Contract Choice

- Universidad de los Andes is aimed at designing a comprehensive “solution package” to mobilize resources and attain stable governance. Challenge: almost 2,000 widespread firms, most of them located in poor municipalities; regulatory measures need to be supplemented. *Focus: small and rural communities*
- Package would include: (i) risks identification map; (ii) simplified engineering design templates; (iii) matching risks and financial structures; (iv) management models, governance and incentives. Role of checks and balances

Path to sustainable investment

Basic conditions	*Short-term measures*	*Aspirations*
Project yields positive net social surplus	Economic evaluation consistent with potential impacts; comparison of alternative solutions	Sector plans linked to development policies; balanced maintenance vs. expansion decisions
Financial structure conforms to local context	Choice based on fiscal space, profitability and property rights defense efficacy	Effective sector fiscal programming and enabling business climate
Sector organization and governance evolving in the right direction	Self-*enforcing* measures needed for project success; mitigation of current weaknesses	Institutional achievements self-*reinforce* over time

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