

**Strengthening Private Sector Participation for
Infrastructure in the Pacific Region
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**Case Study:
The Water Service Concession
in Port Vila, Vanuatu**

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Sources: *A Case Study of the Privatization of Port Vila*, John Chaniel, UNELCO Vanuatu Ltd., 2004.
Beyond Boundaries—Extending Services to the Urban Poor, Asian Development Bank, 2002.

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The Pre-PSP Problems

- The urban water service in Port Vila under the Public Works Department was having problems:
- The Government was unable to collect sufficient funds to cover operating costs.
- Although water was metered and water charges were adequate, the level of collection was poor.
- As a consequence, the Department of Public Works had little or no funds to spend, not only on new works, but also on basic day-to-day operating needs.
- The network was deteriorating along with the quality of service, which was beginning to affect tourism and other industries.

The PSP Solution

- To address the problems, the Government decided to award a concession contract to a private operator.
- Aware of its weak institutional capabilities, the Government was prepared to delegate to the private operator all management, operating, and investment functions except for the ownership of assets.
- The Government also set the objectives of the concession
 - To improve the quality of service
 - To make the service financially autonomous
 - To allocate resources previously dedicated to the urban water sector to other sectors.

The Procurement Process (1)

- As a first step to implement the PSP solution, the Government in 1992 called a number of specialized companies to submit offers.
- UNELCO was selected as the potential operator.
- The operator conducted a detailed of the water utility carried out to collect data on the state of the network, the equipment and parts, the customer base, the water consumption, growth forecast, resources, etc.
- With these data, the operator prepared a technical and financial study to determine operating costs, investments and revenue.

The Procurement Process (2)

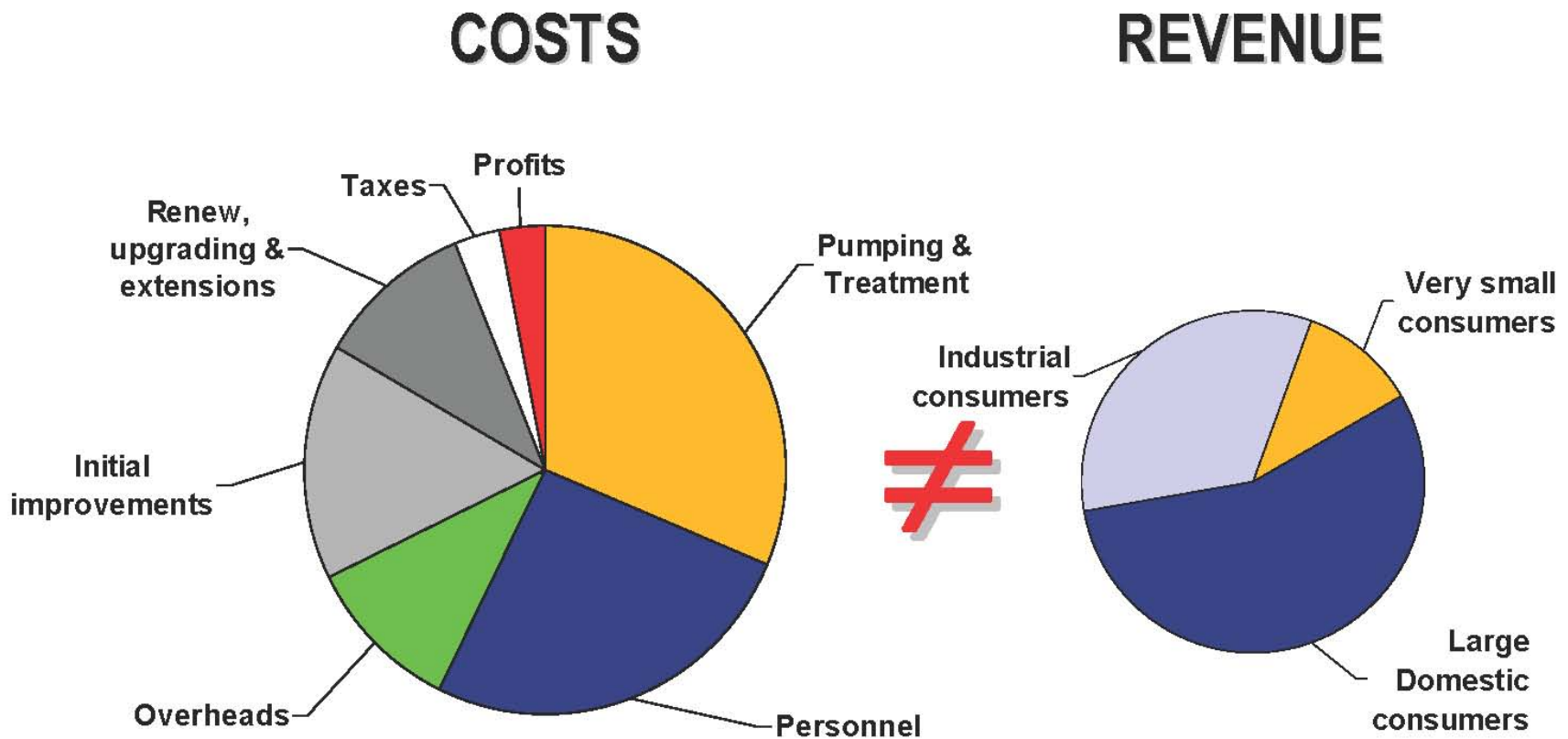
- The Government and the operator negotiated the key issues that have a significant impact on the selling price of water, such as:
 - amount of investments to initially improved the network and for future extensions
 - interest on loans
 - operator profits
- The Government wanted affordable prices for the consumers.
- In 1994, after two years of negotiations, UNELCO signed the concession contract to supply water to Port Vila.

Setting the Price of Water (1)

- In the negotiations, the Government and the operator collaborated to define a tariff structure based on the projected costs, profits, and volumes of sales that would:
 - be affordable to the consumers;
 - allow the operator to fulfill its obligations; and
 - allow the operator to make a reasonable profit.
- The Government opted to favor the low-income consumers and to charge more to the large domestic and industrial consumers (cross-subsidization).
- A structured fixed-tariff system was established to enable affordable rates for all types of consumers.

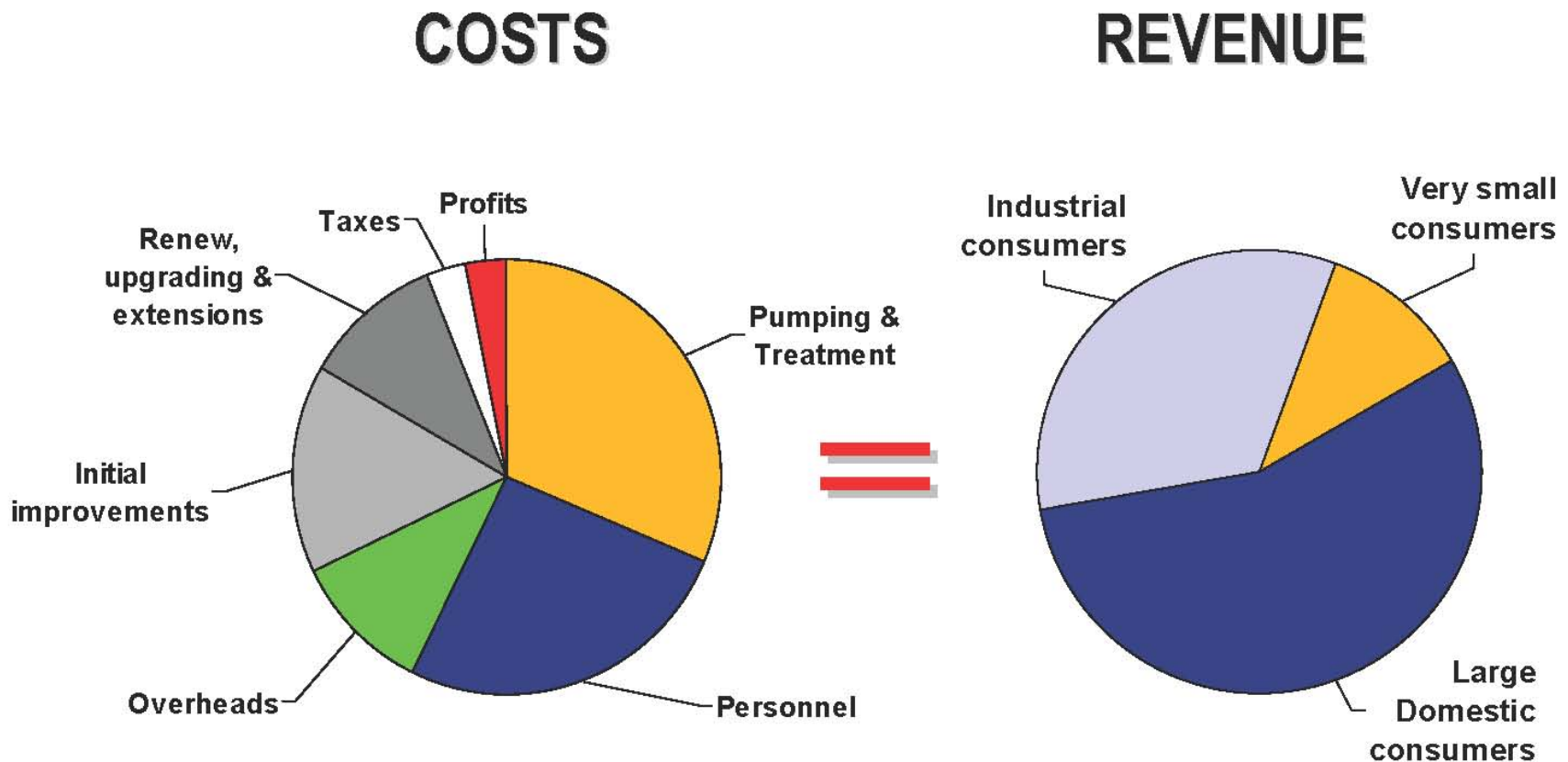
Setting the Price of Water (2)

At the start of negotiations, the expected revenue based on the existing tariff was not enough to cover planned operating expenses.



Setting the Price of Water (3)

- Negotiations went on until agreement was reached on the cost and tariff structures that would match costs and revenue.



Key Terms of the Concession Contract (1)

- The duration of the contract is for 40 years.
- The operator is responsible for the operations, renewal, upgrades, maintenance, and extension of the network within the geographical limits of the concession area.
- The Government facilitates access to new areas for extension of service.
- The price of the water is adjusted based on formula that reflects increases in the underlying costs.

An investment of US\$11.6 million was anticipated over the life of the contract, with US\$580,000 per year for the first 5 years.

Key Terms of the Concession Contract (2)

- The operator guarantees the sustained quality, quantity, pressure, and continuity of service as specified in the contract.
- Failure to meet service targets would result in penalties to the operator.
- The Government retains ownership of the assets.
- At the end of the contract, all assets are returned to the possession of the Government or a new contract is signed.

Regulatory Arrangement

- A self-regulatory system is provided in which the Government monitors the operator's activities.
- The performance of the contract is controlled by the Government; periodical technical and financial reports are provided by the operator.

Some Service Improvements Achieved

- After close to 10 years of operation, the concession delivered improvements in service:
- Before the contract, water supply was often interrupted; by 2003, water was supplied 24 hours a day.
- Unaccounted for water was reduced from 50% to 23%.

Annual losses of up to US\$440,000 in 1991, had been turned into a reported surplus of US\$12,000 in 2000.

Key Success Factors

- Some of the factors that contributed to the initial success of this concession include:
- Initial acceptance by the Government of its own weak institutional state.
- The contract was well designed, tailored to satisfy the particular needs of the concession area and with good provisions for tariff indexation and clear definition of service targets.
- Selection of a suitable concessionaire.

Thank You

