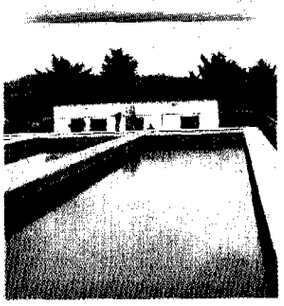
UN-HABITAT REPORT ON THE WATER SECTOR IN SMALL URBAN CENTRES: PAPER 2

Water Sector in Small Urban Centres

Analysis of Donor Flows to Water Supply and Sanitation Services

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1 Introduction

This paper presents an analysis of Official Development Assistance (ODA) flows to the water and sanitation sector, based on data gathered from the OECD Development Assistance Committee (DAC) and Creditor Reporting Systems (CRS) databases, as well as current knowledge in the sector. As part of this analysis, ODA flows to the health and education sectors, as well as to broader topics including governance and finance, are also considered. Where possible, policy implications and specific discussion about small towns is provided, however, there is a general lack of information about financing flows to small towns, due to the nature of the accounting systems used by donors (and reported to the OECD).

Historically, donors have used ODA to provide the majority of funding for water supply and sanitation activities in developing countries. They have done so through individual, ad-hoc, and sometimes competing programs, or through support to governments and other implementing agencies (such as I/NGOs). The growing acceptance of the Poverty Reduction Strategy Paper (PRSP) in recent years has created an opportunity for more coordinated development assistance as well as targeted poverty reduction in a way that reflects the demands and needs of countries. Current estimates to achieve the Millennium Development Goals (MDGs) for water and sanitation range from US$7.5 billion to US$70 billion annually[1], compared with the US$2-3 billion annually committed through ODA. Tracking donor flows, then, becomes all the more important, first to understand whether political commitments are consistent with funding decisions, and also to prime advocacy efforts for increased ODA, as well as analysis on the value for money created by ODA flows to the water and sanitation sector.

For example, in the water sector, the MDGs call for halving the proportion of people lacking sustainable access to safe water and basic sanitation has not translated into greater funding for the sector through traditional ODA financing sources (grants and loans). With Poverty Reduction Strategy Credits (PRSCs) driving national poverty alleviation strategies in most developing countries (PRSPs), how well a sector is profiled contributes to how the sector is prioritized, however even if a sector is prioritized, it does not always mean it would attract financing through the government budget.[2] This lack of attention suggests that the existing water sector finance and governance systems need to evolve – both to adapt to the current environment, and to create a new environment where the water and sanitation sector can attract the resources required to yield the economic and poverty reduction benefits so often attributed to it.

ODA to the water sector has typically been used to support infrastructure capital costs, and, as the data will illustrate, flows to the water sector continue to be biased towards larger infrastructure systems. Indeed, even the estimates costed at a global level to achieve the MDGs for water supply and sanitation tend to be based on initial construction costs.[3] However, the social and environmental benefits of these investments tend to be short-lived, because core principles of operations and maintenance, cost recovery to fund recurring and rehabilitation costs, and planning to meet present and future demand, are often overlooked. Because these principles require long-term investments in capacity building,

1 Fonseca, Catarina and Rachel Cardone, 2004.
2 WSP-Africa PRSP Benchmarking Review
3 Fonseca, Catarina and Rachel Cardone, 2004.

governance, business development skills, and the like, they tend not to attract traditional forms of donor finance.

While there is evidence of ODA flows supporting small utilities in small towns, the constraints to traditional ODA, outlined above, can be amplified. Other financing options are limited: while larger urban centers can assume loans (whether from the public or private sectors) for investments, and rural areas typically benefit from fully grant-based support, small towns fall into a 'middle ground'. Whether they serve as centers for rural markets that stimulate the establishment of a permanent population, or they are situated on the outskirts of larger urban areas, some of the challenges facing small towns regarding investments in water and sanitation include appropriate design of systems, sequencing of development, timing, and importantly, access to finance. The availability of branch banks in small towns that can provide products to domestic entrepreneurs is limited, due to a lack of capacity on the part of the banking sector. Opportunities for attracting finance through the national government may also be limited, particularly if the small town is not a municipality in its own right (a municipality may be responsible for several small towns, or a mixture of small town: rural, or small town: urban areas).

As key financiers for the water sector, donors have an important role in shaping sustainable water development, whether in urban, peri-urban, small town, or rural areas. To understand the recent history of ODA, this paper will consider ODA flows to the water and sanitation sector, looking at overall flows at a global and then regional level; this will be done by type of mechanism (grant/loan), and by comparing commitments with disbursements. It will then consider targeting of ODA flows, by sub-sector, to small towns, and to the poor, based on access data provided by the Joint Monitoring Program. To compare ODA flows to water relative to other expenditures, this analysis will track ODA flows to water supply and sanitation relative to health and education, by region and by income group (e.g. least developed countries, lower middle income countries, other low income countries, and upper middle income countries). To understand ODA flows to water supply and sanitation in relation to broader governance and economic development processes, such as the PRSPs, an assessment of ODA flows to governance and civil society, banking and finance, and business development is also provided.

The structure of this paper is as follows:

- **Section 2** outlines the OECD DAC and CRS databases, including their benefits and constraints.
- **Section 3** presents an analysis of ODA flows, using data from the DAC and CRS databases.
- **Section 4** provides some preliminary findings, as they relate in general to ODA, and more specifically for small towns.

This paper is complemented by another paper on *"Experiences in Innovation: Financing Small Town Water Supply and Sanitation Service Delivery"* which explores some of the innovative ways in which finance can be used to support and strengthen water sector development.

2 Overview of ODA flows to the water sector

2.1 Overview of the DAC

The OECD's Development Assistance Committee (DAC)[4] compiles statistics on development activities from OECD countries to developing countries. Data on the purpose of aid flows are gathered as commitments, which reflect project agreements, based on a calendar year. Donors report the face value of the activity at the date a grant or loan agreement is signed with a recipient, regardless of when disbursements are expected. Data on disbursements are also collected to monitor the implementation of activities. The OECD has two databases: the DAC, which provides aggregated information, and the Creditor Reporting Systems (CRS), which provides disaggregated details.

DAC statistics cover bilateral and multi-lateral aid to water supply and sanitation (Box 1 provides the details on what activities are covered by the water and sanitation category). For DAC countries, data on total aid commitments is available as of 1973, and is estimated to cover 85-90% of DAC countries' bilateral ODA for the water sector between 1990-1995, whereas from 1996 to the present, the data sets are close to complete. By contrast, information about disbursements has become more precise only in recent years.[5]

Box 1 OECD DAC Definition of water supply and sanitation

The DAC defines aid to water supply and sanitation as including the following sub-categories: water resources policy and administrative management; water resources protection; water supply and sanitation (large systems); water supply and sanitation (small systems); river development; waste management and disposal; and education and training in water supply and sanitation. According to the DAC classification, dams and reservoirs are considered primarily for irrigation and hydropower use, and are therefore classified under agriculture and energy sectors, respectively. The inclusion of waste management and disposal refers largely to solid waste-related activities, and does not represent a considerable portion of the total. Notably, in June 2004 the DAC Working Party on Statistics revised the sub-sector "water supply and sanitation – small systems" to "basic drinking water and basic sanitation", in order to allow for more targeted data collection relating to the MDGs in the future. As this report is based on data gathered through 2003, this new sub-sector is not included..

4 DAC members are: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Italy, Ireland, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, the United Kingdom, the United States and the Commission of the European Communities.

5 The OECD has recently published two reports on ODA to water supply and sanitation, from which this section draws heavily. These are cited throughout the text. For further information about the DAC and Creditor Reporting System (CRS), see http://www.oecd.org/dac/stats/crs/crsguide.

2.2 Constraints to tracking donor flows

While the OECD DAC and CRS databases offer insight into the world of donor financing, there are some constraints. First, and perhaps most importantly, the relationship between funding and access to water supply and sanitation is neither direct nor causal, meaning that improvements in access data may not be directly related to the amounts of ODA funding that are provided. Rather, the relationship should be seen as a way of identifying those countries and regions where additional financing is needed, and then provoking thoughts about how additional funding that can be targeted, should be targeted to achieve lasting poverty reduction impacts.

In considering this latter point, it should be noted that the DAC/CRS databases do not capture off-budget sheet commitments from donor agencies to the water sector, such as guarantee schemes, which means that more innovative funding schemes – which represent a new type of thinking about targeting ODA – are unaccounted for. From a technical perspective, accounting for these flows may be complex.

Further, the trend away from project-based donor assistance towards budgetary support – where ODA is deposited into recipient government accounts without rules on how it can be used – may also impact the potential for analysing ODA flows to specific sectors. Understandably, budgetary support places greater responsibility on governments to allocate and manage government functions, which may be appropriate in some countries, but not in all. Varied merits of this approach to ODA funding aside, this shift may result in a loss of focus in ODA reporting at a sectoral level.

Finally, and specifically for small towns, the DAC/CRS tracks large or small systems rather than urban or rural areas. For small towns, which tend to fall somewhere in between, there is no easy way to differentiate financial flows over time.

3 Data Analysis

3.1 Overall funding for the water sector

Overall ODA grant and loan funding for water supply and sanitation over the last several years is on the decline, compared with previous commitments throughout the early 1990s. Using a 5-year moving average (to account for variations caused by large commitments in a single year for multi-year projects) flows between 1999-2003 range between US$2.5 billion and US$3 billion.

Water and sanitation investments represent a declining percentage of ODA commitments relative to other sectors. As a percentage of commitments to overall social infrastructure and services (which includes health and education, governance and civil society, and population programs), water and sanitation commitments have dropped from 22% in 1999 to 14% in 2003. Compared with total ODA, water and sanitation commitments have dropped from 7% in 1999 to under 5% in 2003.

Considered from a regional perspective, the results are about similar:

- In **Sub-Saharan Africa**, average funding to the water supply and sanitation sector has declined somewhat, from US$603 million in 1999 to US$583, while total ODA flows to the region have increased every year, as have flows to total social sectors. The percentage of flows to water supply and sanitation relative to total ODA have fallen from 5% to 3% between 1999 and 2003; likewise for total social infrastructure spending, the percentage to water supply and sanitation has fallen from 17% to 10% in the same time frame.

- In the **Latin America/Caribbean** region, average funding to the water and sanitation sector averaged between US$300-500 million, with a decline from a high of US$477 million in 2000 to just $318 million in 2003. Compared to Sub-Saharan Africa, the total ODA flows to the region have increased, but at a slower pace, from US$5 billion in 1999 to just over US$6 billion in 2003. However, the percentage of flows to water supply and sanitation relative to total ODA have fallen from 8% in 1999 to 5% in 2003; likewise, compared with total social infrastructure spending, the percentage to water supply and sanitation has fallen from 20% to 11% in the same time frame.

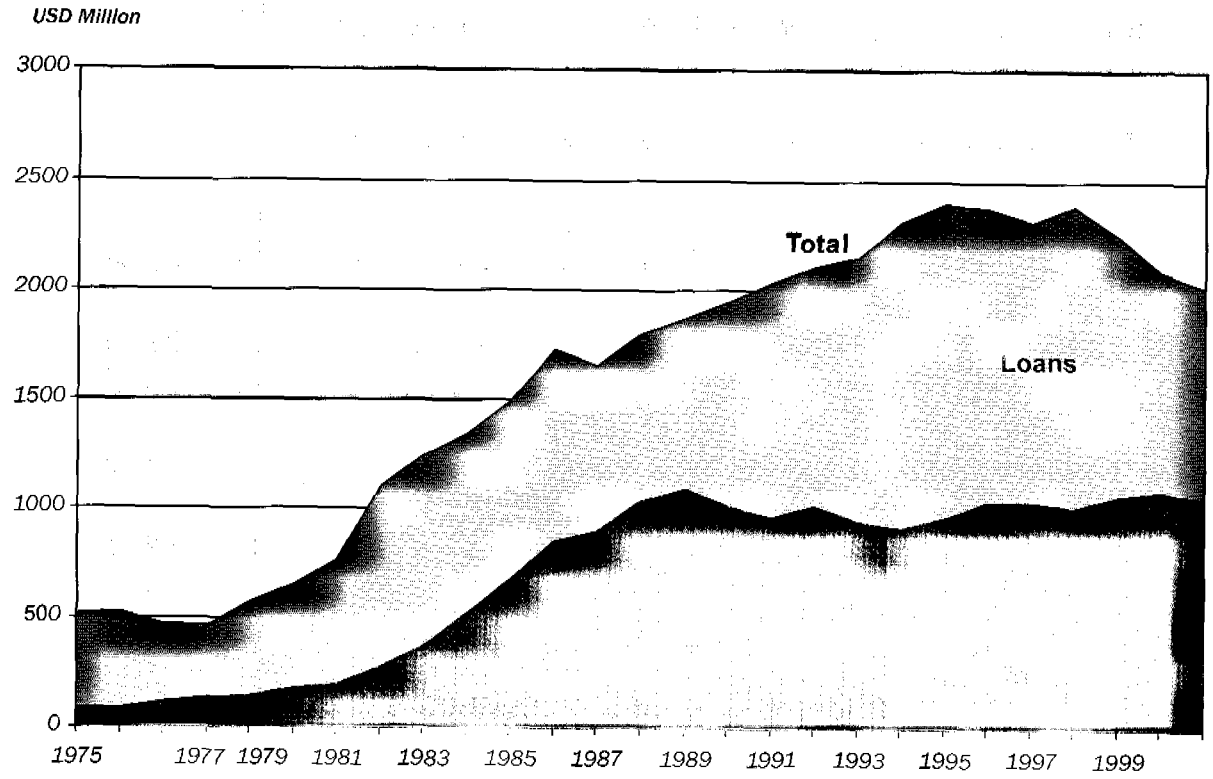
- In **Far East Asia**, average funding to the water and sanitation sector increased from US$652 million in 1999 to a high of US$795 in 2001; however commitments fell in 2002, and again in 2003, to a total of US$673 million. Water and sanitation sector commitments represent a somewhat stable percentage of total ODA flows, peaking at 9% in 2001, but falling to 7% in 2003. Compared with total social infrastructure funding, water and sanitation sector spending reached a high of 40% in 2000, but has fallen in consecutive years to 27% in 2003.

  By contrast to these other regions, **South and Central Asia** has seen an increase in average ODA commitments to the water and sanitation sector between 1999-2003, from US$499

million to US$515 million (noting a drop between 1999-2001 to a low of US$382 million). As a percentage of total ODA commitments, water and sanitation flows have dropped from 7% to 5%, and have also dropped from 21% to 18% of total social infrastructure flows.

Considering the balance between grants and loans over time, Figure 1 illustrates the long-term trends in ODA flows. As shown, grants and loans both rose considerably during the 1980s, perhaps reflecting the International Decade on Water Supply and Sanitation. In the 1990s, grant financing stagnated, while the volume of loans increased, leading to greater investments in the water sector. Between 1998 and 2001, however, loan financing drops off considerably. Notably, the loans that were provided for the sector had an average grant element of about 70%, which is the average for all sectors.[6]

Figure 1 Trends in bilateral grants and loans for water supply and sanitation from DAC countries, 1975-2001, 5-ye moving averages, constant 2002 price



Source: ERM, 2003.

6 OECD, 2004. "Aid for Water Supply and Sanitation", Report for Stockholm Water Week 2004.

3.2 Commitments and disbursements

The data presented so far reflects donor commitments, rather than actual disbursements. There are many factors that can prevent a commitment turning into a disbursement, such as changes in a donor country's policies, changes in international policy to which a donor may adhere, or activities by a recipient government, which can lead to the cancellation, withdrawal, or merely a delay in disbursement.

Although the OECD has tracked disbursement data since the 1970s, DAC members have only recently been able to provide data on their disbursements, largely due to bureaucratic, technical, and administrative constraints. In 2002, however, 90% of total bilateral ODA disbursements were reported, which should allow for better analysis and monitoring of commitments in the future. Using data from 2002, the OECD conducted a preliminary analysis of disbursements, using information from France, Germany, and Japan, and supported by other information. The agency's analysis suggests that disbursements to the water sector tend to peak about 4-5 years after the original commitment, while the process of disbursement tends to exceed 8-9 years.[7]

This lag time between commitments and disbursements has a considerable impact on water sector reform. For example, while sector strategies may be prepared for the longer term (e.g, a 10 year period), the PRSP and MTEF processes are normally prepared for a three-year period. At a broad level, the mis-match between PRSP/MTEF planning processes – on which donors increasingly rely for making ODA commitments – and the actual rate of disbursement would appear to disrupt, and even minimize, the development potential of these processes. Even if donors decided in 2005 to make commitments that bridge the financing gap for water supply and sanitation in its entirety, the funds wouldn't even start to be released until 2010, with gradual disbursements through 2013!

More specifically, the lag time between commitment and disbursement can stifle reform at the sovereign and sub-sovereign levels of government. For example, the PRSP process is meant to stimulate and improve planning processes at all levels of governance within a country. Premised on a demand-driven approach to development, activities reflected in the PRSP should be based on the needs and priorities identified by the country through active participation by a range of stakeholders (including NGOs, community-based groups, citizens/households, and government) with support from the international development community. Once the activities are identified and prioritized, they should be costed and budgeted through the national budget. The PRSP and MTEF are intended to coordinate donor flows to the government, and through the government, to support these activities. A lag time between commitments and disbursements can limit actual implementation of activities at the national government, creating a chain reaction that results in disruptions at the sub-sovereign level. An example is provided in Box 2.

7 OECD, 2004. Aid for Water Supply and Sanitation, page 11.

Box 2 Budget allocations and actual spending in Zambia

According to a study about financial flows to Zambia's rural water supply and sanitation sector between 1999-2001 conducted by WaterAid, the Government of Zambia typically manages to spend less than 25% of its actual budget – which is approved and authorized by Parliament – over the course of the year. There could be many reasons for this lack of disbursement, including re-direction of funds to other sectors, corruption, or lack of absorption capacity at sub-sovereign levels. Working to determine the cause for this variance, the study's authors found that absorption capacity was not the cause. One respondent noted that most of the machinery and personnel in one province were underutilized for most of the year, due to lack of funding. According to the head planner at the Ministry of EWD, the Ministry of Finance is responsible for disbursements; there appears to be a lack of communication between the ministries over why planned disbursements do not arrive on time, if at all. Interestingly, the study's authors found that some of the other ministries in the government do receive their allocated budgets on time. According to an official at the Ministry of Finance, this is because those agencies do not rely on donor counterpart funding, which is off-budget, and often delayed. As a result of donor delay and challenges within the Government of Zambia, available funding does not usually match planned expenditures, and the available funds require re-allocation, based on the Ministry of Finance's priorities. Ultimately, the work that goes into planning – which includes stakeholder engagement at all levels of governance – is not reflected in actual expenditures. Importantly, these types of challenges are not unique to Zambia; both WaterAid and the WSP have initiated studies on resource flows and financing at a country level in a variety of countries throughout Sub-Saharan Africa, which have yielded similar findings.

Source: Getting to the true nature of the problem: the case of financing rural water supply and sanitation in Zambia's poverty reduction strategy

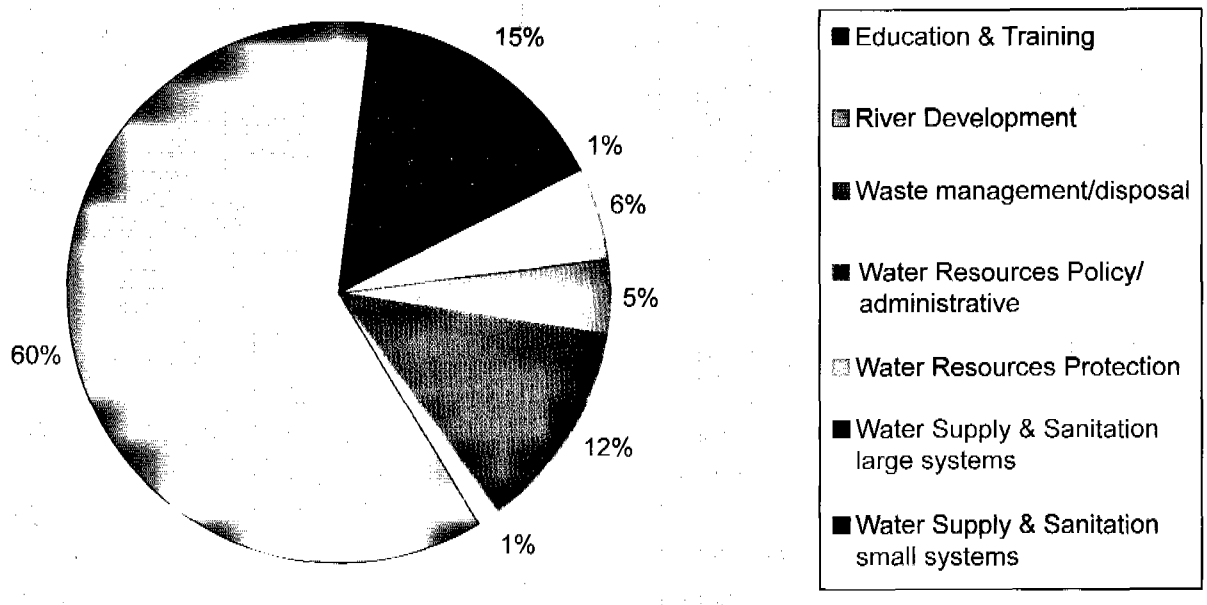
3.3 Targeting water supply and sanitation investments

Targeting by sub-sector

Adding to this general picture of ODA, the DAC and CRS databases also allow for some analysis of how ODA is targeted. Within the sector, ODA commitments predominantly are targeted towards large-scale systems, perhaps reflecting a bias towards urban utilities. **Figure 2** illustrates the split amongst different sub-sectors in 2003.

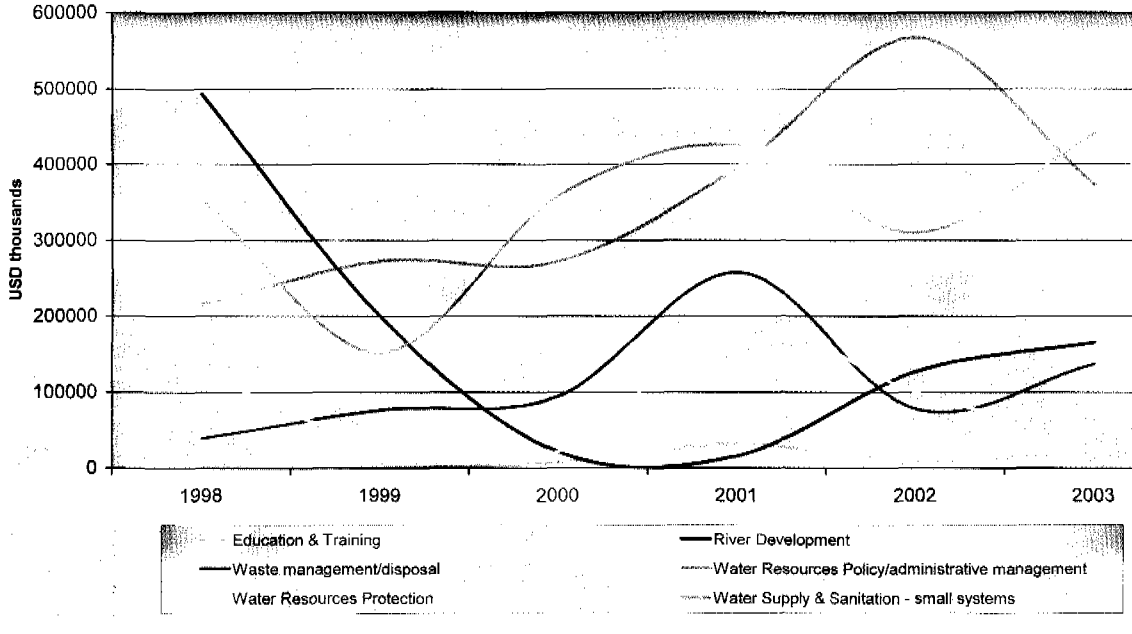
This picture has not varied considerably since 1998. Funding for large-scale systems tend to capture over half of commitments to the water and sanitation sector, and overall commitments to large-scale systems have tended to range between US$1 billion to US$2.5 billion per year. Notably, this range was reflected over a two-year period, where after the peak in 2000, commitments fell to US$1 million in 2002. In 2003, commitments rose to $1.8 billion.

Figure 2 Sub-sector ODA flows to the water sector, 2003



Other sub-sectoral categories receive an order of magnitude less funding than large-scale systems. **Figure 3** illustrates the variation in commitments within these other sub-sectoral categories.

Figure 3 Variation in water and sanitation ODA commitments by sub-sector



As seen above, there is some variation on a year-to year basis within each category, although there is less variation relative to each other. Water resources policy/administrative management, the second largest funding category after large-scale systems (capturing an average 13% of total water and

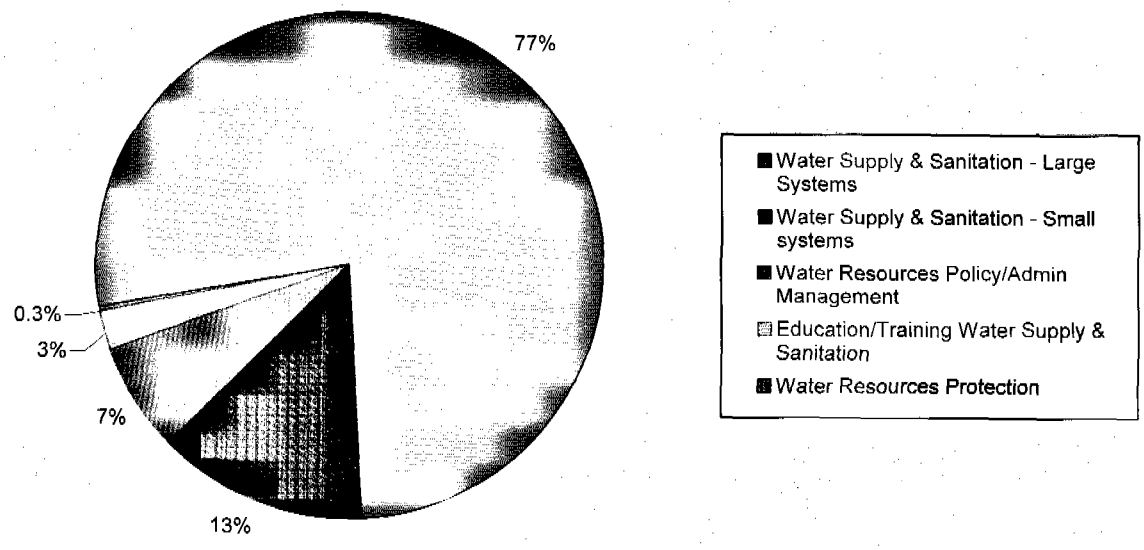
sanitation commitments), saw considerable increases in ODA commitments - from US$272 million in 2000 to US$567 million in 2002 – and then a decline, in 2003, to US$372 million. Small-scale systems, the third largest category (at an average 12% of total water and sanitation commitments) had greater variation over the last several years. Between 1998 and 1999, commitments dropped by nearly half from US$353 million to US$152 million. Commitments quickly rebounded in 2000, back to US$359, and have not been under US$300 million since. In 2003, commitments reached US$440 million. On the lower end of the spectrum, categories such as education and training have tended to remain a fraction (less than 1%) of total water and sanitation commitments, while activities such as river development and water resources protection have varied considerably.

Targeting to small towns

The OECD DAC/CRS databases do not differentiate between urban and rural areas, nor do they track funding flows to small towns. As a result, one must rely on working through each database entry to isolate those flows relating to small towns, based on voluntary text descriptions provided by the donors themselves. According to the OECD, the quality of input has improved substantially, allowing for an analysis of the 2003 data. Descriptions that included terms relating to villages, towns, provincial areas, municipalities, or decentralization were identified and then analyzed. Notably, the process is not an exact science, as it was not possible to deconstruct each funding entry to determine whether small towns benefited from each specific activity. However, it can be considered a best-guess, preliminary estimate.

Given these caveats, it appears that of the US$3 billion in ODA flows to water supply and sanitation in 2003, roughly US$360 million (or 13%) was allocated to small-town or related activities. Of the different sub-sectors, only river development and waste management/disposal did not receive ODA commitments. Otherwise, the commitments roughly correspond to the overall picture of sub-sectoral lending, as illustrated in **Figure 4.**

Figure 4 Estimated proportion of ODA commitments for water supply and sanitation in small-town or related activities, by sub-sector



Here, large systems accounted for 77% of total flows, followed by small-scale systems (13%) and water policy (7%). Education and training, and water resources training, by comparison, comprise considerably less of total allocations.

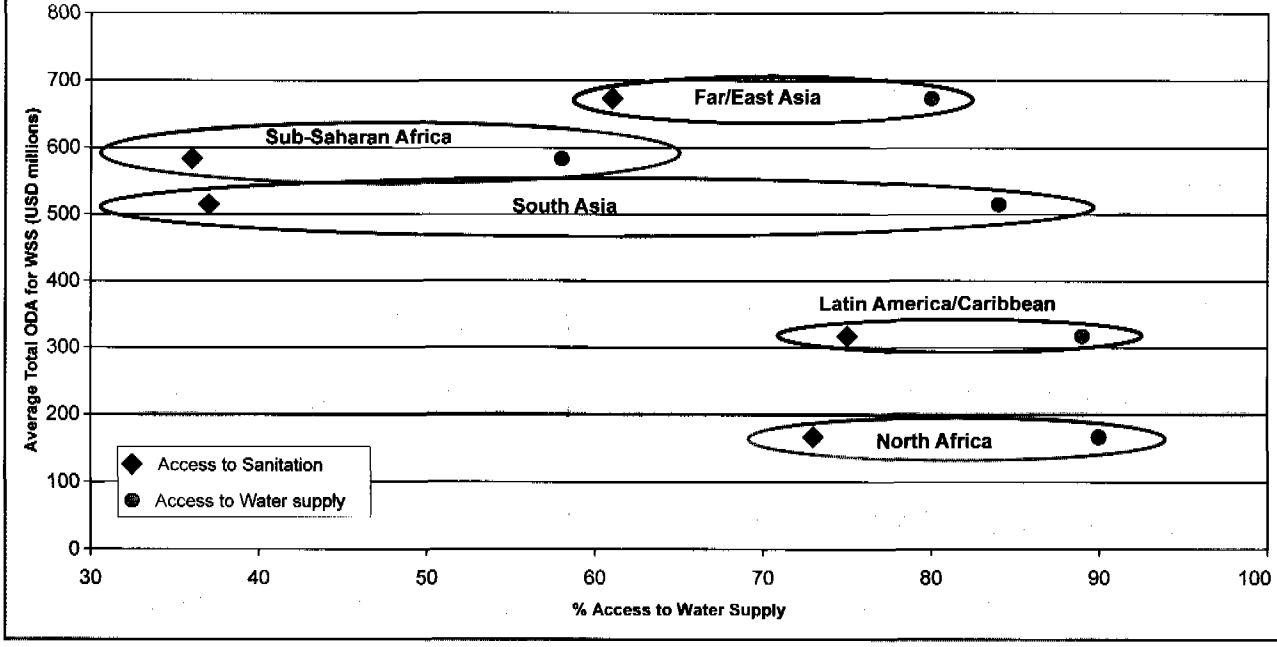
This split in allocation, which parallels the broader allocations of all water and sanitation commitments, suggests a bias towards infrastructure. In a recent report on small towns published by the World Bank,[8] considerable attention is paid to the fact that small towns often have utilities, but they tend to be over-designed, in terms of technical, operational, and financial capacity. Although further analysis is required, these preliminary findings suggest that ODA flows are not targeted effectively to meet the needs of small towns.

Targeting ODA for the poor

In addition to the challenges with tracking ODA flows for urban/rural/small towns, it is also difficult to determine whether water and sanitation commitments are targeted to the poor. From a broad perspective, it is possible to plot access data, provided by the Joint Monitoring Program (JMP), against funding flows, to determine whether funding flows are targeted to those areas lacking access.

According to the JMP, the regions facing the greatest challenges to achieve the MDG targets for water supply and sanitation are Sub-Saharan Africa and South Asia/East Asia. Notably, across all regions, access to sanitation lags considerably behind water supply, particularly in rural areas. **Figure 5** below maps access data by region with ODA commitments to water supply and sanitation, drawn from the JMP and CRS databases. Note that the pink dots represent access to sanitation, while the blue dots represent access to water supply. Importantly, this analysis is not meant to suggest causality between amounts of funding and access levels, as the amount of funding committed does not necessarily mean

Figure 5 Access to water and sanitation compared with ODA flows to water, based on average commitments, 1999-2003



8 World Bank Town Water Report, 2004

that it results in financial flows, or that such flows as may occur are timely or efficient. Rather, it should serve to illustrate where the needs are, and, by comparison, where ODA flows over the past few years have been directed. ODA flows are calculated in 2002 constant USD millions.

Overall, this analysis suggests that ODA commitments, at least based on an average of 1999 to 2003, reflect the regional needs to achieve the water and sanitation MDG targets. North Africa and Latin America/Caribbean regions have the highest levels of access for water supply and sanitation in both urban and rural areas, and receive, on average, the least amount of funding. By comparison, Sub-Saharan Africa, which has the lowest access for urban and rural water supply and sanitation, receives the second highest allocation of donor flows. Unfortunately, it is difficult to disaggregate investments between water supply and sanitation; otherwise further analysis between the two sub-sectors could be conducted. For example, it would be useful for policymakers to know whether funding in South Asia is more targeted to sanitation than to water supply, given the wide gap in access data between the two. Given the historic bias in ODA flows to water supply over sanitation, however, one can assume that ODA commitments continue to support water supply interventions over sanitation activities.

Importantly, data flows from other recent years reflect other priorities. For example, a 2004 OECD report[9] presents analysis suggesting that ODA commitments tend to be concentrated in just a few recipient countries. Of the total bilateral and multilateral commitments to water supply and sanitation from 2001-02, 53% of it was allocated to just 10 countries: India, Vietnam, China, Palestinian administered areas, Nepal, Senegal, Yemen, Jordan, Egypt, and Burkina Faso. Given that the bulk of countries considered off-track to achieving the MDGs for water and sanitation are situated in Sub-Saharan Africa, this suggests that ODA grants and loans are not always targeted effectively to those countries most in need.

Based on the information presented above, the following can be concluded:

- ODA flows – both in terms of commitments and disbursements, are insufficient to bridge the financing gap at global, regional, and country levels, to achieve the MDGs for water supply and sanitation

- Even if ODA flows were sufficient in quantity, it is not clear that they are sufficient in quality. There is a lack of evidence that flows consistently reach those countries in greatest need; and even where funding does reach the poorest countries, there still appears to be a bias towards larger-scale infrastructure solutions over basic water and sanitation needs.10

Considered from a broader perspective, other trends in development tend not to be captured in discussion of ODA flows to the water supply and sanitation sector. For example, trends such as strengthening core governance functions through budgetary support and sector wide approaches, as well as thinking beyond traditional sources of finance to support more innovative ideas may have a positive impact on the water sector overall. A recent paper for DFID on the agency's contributions to achieving the MDGs for water supply suggested that given the key constraints facing the sector – which relate predominantly to public administration and financial management – it may be

9 OECD, 2004.

10 A recent report released by WaterAid, "Getting to Boiling Point" notes that in the countries where it operates, projects may benefit only 0.3% of the population, using inappropriate technology that ultimately breaks down without yielding long-term poverty benefits.

appropriate for donors to focus on improving the overall governance framework in a country to the point where things function, rather than continue to fund unsustainable projects and programs in an institutionally complicated water sector.[11] Some governance experts (representing water as well as livelihoods, health, and education) interviewed as part of that study also suggested that the tangled nature of the water sector's governance relative to health and education may be a core reason why funding has tended towards the latter two sectors in the PRSP process. In countries where this is true, there may be all the more reason for getting the governance framework 'right' before pouring ODA into water sector interventions that face little chance of having beneficial poverty reduction and economic development outcomes.

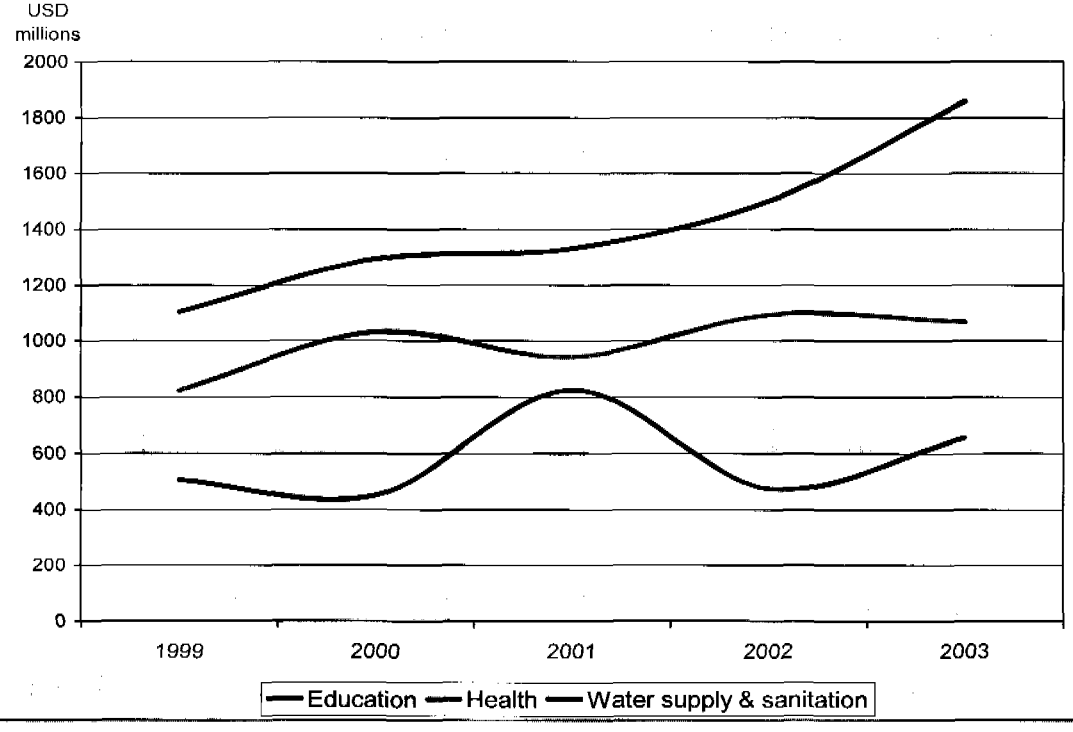
Section 3.4 builds on the proposition suggested above, and looks further into ODA flows, first to the health and education sectors, and then to broader governance and financial management programs.

3.4 Water sector flows relative to other sectors

ODA commitments to social infrastructure sectors

The water supply and sanitation sector is often compared with health and education, reflecting water's importance for social development and poverty reduction as well its role in stimulating economic development. Importantly, access to water supply and sanitation is critical for successful health and education service delivery. At a most basic level, health clinics require clean water and means to dispose of waste; access to water supply, and more specifically sanitation, have been shown to

Figure 3.4 ODA commitments to education, health, and water supply and sanitation in Sub-Saharan Africa, 1999-2003



11 ERM, 2005. "Meeting the Millennium Development Target for Water and Sanitation." DFID, London.

positively impact enrolment and attendance at school, particularly for girls. It may be useful to consider ODA flows, then, to the three sectors, and see how they compare. The following series of graphs show total ODA commitments to the water supply and sanitation relative to health and education by region.

Figure 6 ODA commitments to education, health, and water supply and sanitation in LAC, 1999-2003

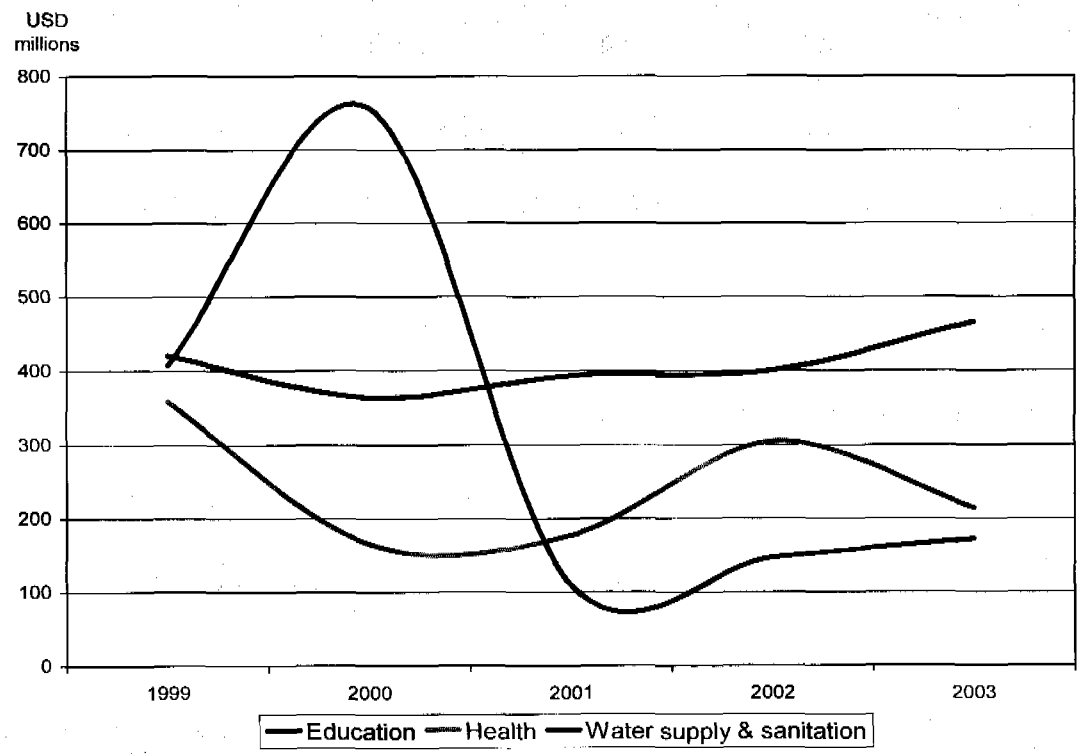


Figure 7 ODA commitments to education, health, and water supply and sanitation in Far East Asia, 1999-2003

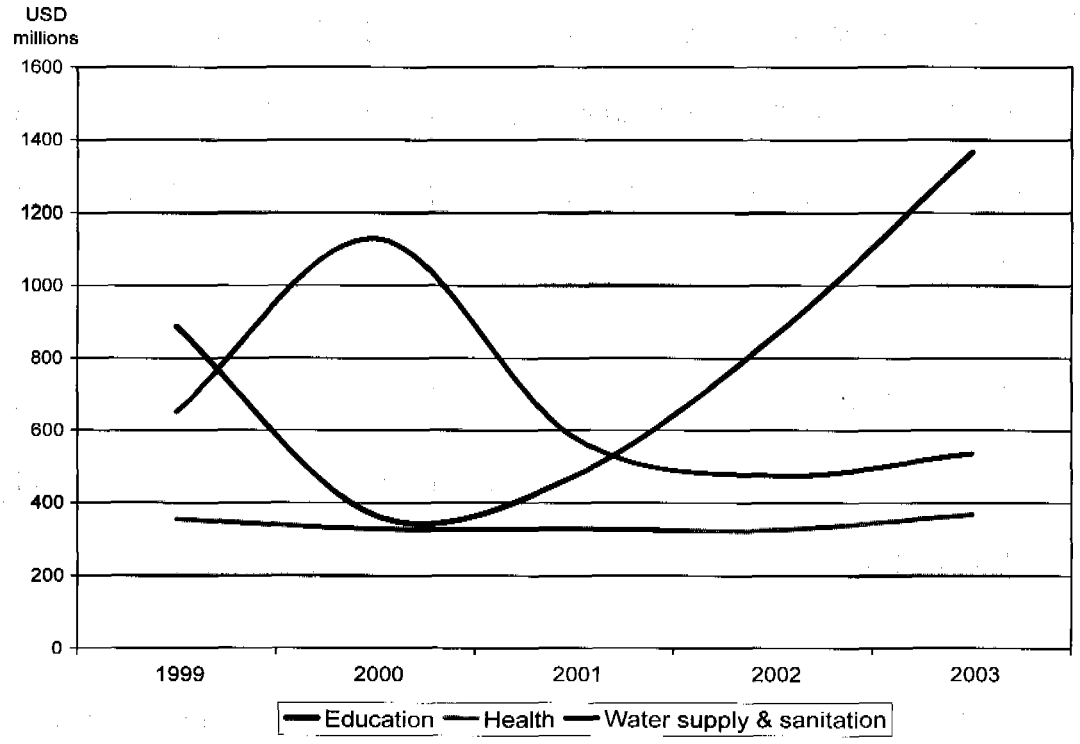


Figure 8 ODA commitments flows to education, health, and water supply and sanitation in South and Central Asia, 1999-2003

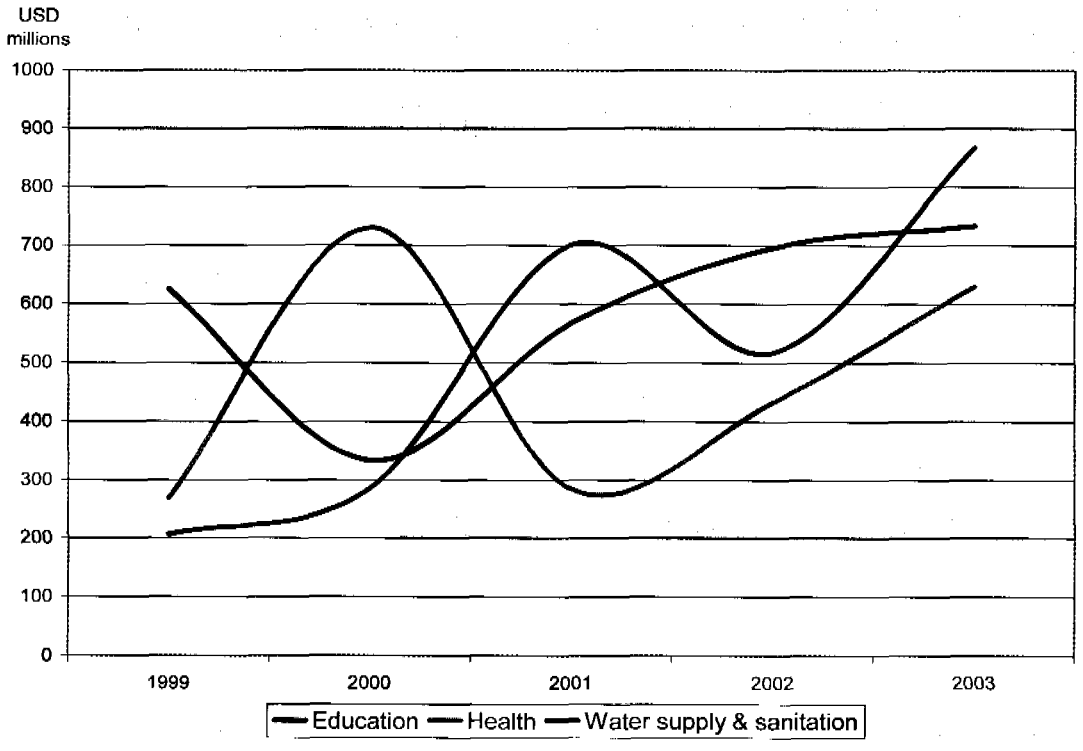
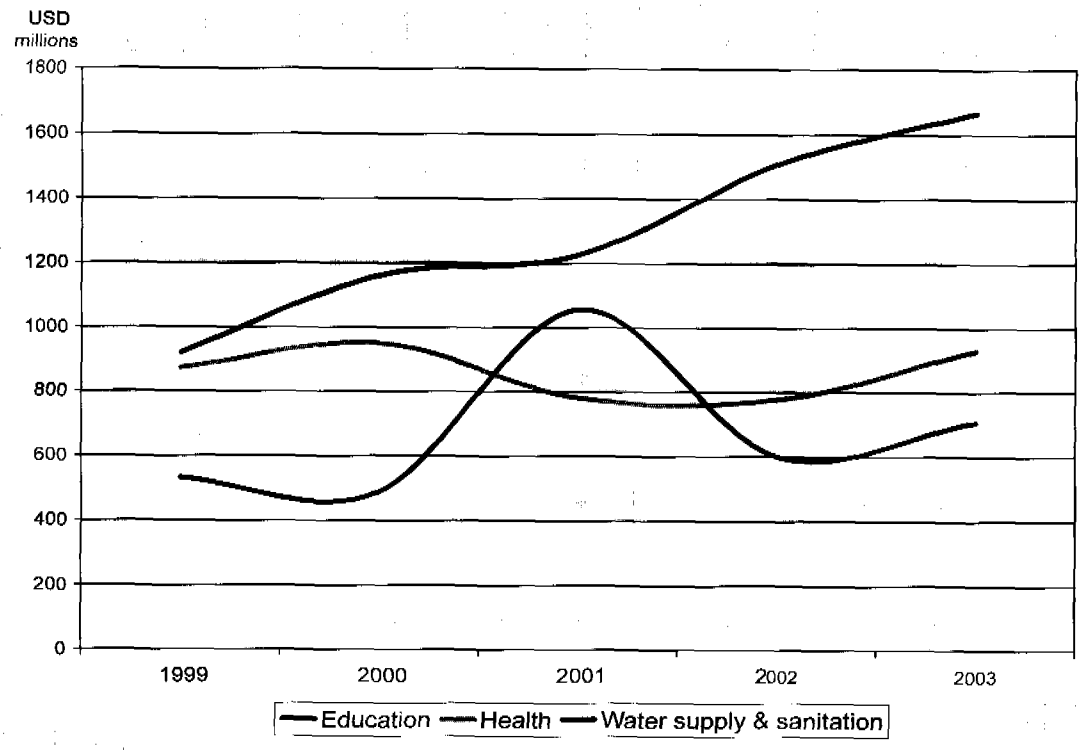


Figure 9 ODA commitments flows to education, health, and water supply and sanitation in South and Central Asia, 1999-2003



These graphs illustrate some interesting points. To begin, looking at average ODA commitments (between 1999-2003) across regions, water and sanitation and health received roughly the same amounts – about US$2 billion per year. By comparison, the education sector received US$3.2 billion per year over the same period. Further, while education commitments appear to be consistently increasing each year, flows for health and water supply and sanitation show considerably more variation. Finally, there appears to be some relationship between the health and water sectors: where commitments to health increase, commitments to water appear to decrease. This finding is suggestive, as more statistical analysis would be required to determine any correlation in these trends. Regional breakdowns, based on average ODA commitments between 1999-2003 are provided below:

- In **Sub-Saharan Africa**, the education sector received, on average, nearly three times more in ODA commitments than the water and sanitation sector; the health sector received nearly twice as much. Within the five year period, annual commitments to education have increased, while commitments to health and water supply and sanitation are more variable.

- In the **Latin America Caribbean region**, average commitments to education are also higher than health and water supply and sanitation, although the gap is not as large: education received US$409 million, water and sanitation, US$318 million, and health, US$243 million. Looking across the five years, funding for water supply and sanitation fell considerably between 2000 and 2001, from over US$750 million to under US$110 million, and then have gradually increased since. By contrast, commitments to education have remained fairly consistent, while commitments to health have been consistently variable.

- In Far **East Asia**, by contrast, average commitments to health (US$339 million) lag considerably behind both education (US$789 million) and water supply and sanitation (US$673 million). Over the five year period, flows to education have increased nearly four-fold since 2000. By contrast, commitments to the water sector dropped by over two times between 2000 and 2003. In the health sector, commitments have been fairly consistent, ranging between a low of US$324 million in 2002 and US$366 in 2003.

- In **South and Central Asia**, average commitments to education, water supply and sanitation, and health ODA commitments are nearly equivalent, at US$591 million, US$515 million, and US$468 million, respectively. A five year analysis indicates that commitments to education have more than doubled between 2000 and 2003, with consistent annual increases. Commitments to health have varied considerably each year, with large declines following large increases. For water supply and sanitation, the trend has largely been positive, with commitments on the rise since 1999 (excluding a dip between 2001-2002). By 2003, commitments to the water sector actually surpassed health and education.

This regional portrait helps to paint a broader picture of ODA flows to those sectors identified as key for poverty reduction. By comparison, the next series of graphs compares ODA commitments to education, health, and water supply and sanitation in least developed countries (LDCs), Lower Middle Income Countries (LMICs), Other Low Income Countries (OLICs), and Upper Middle Income Countries

Figure 10 ODA commitments to education, health, and water supply and sanitation in Least Developed Countries, 1999-2003

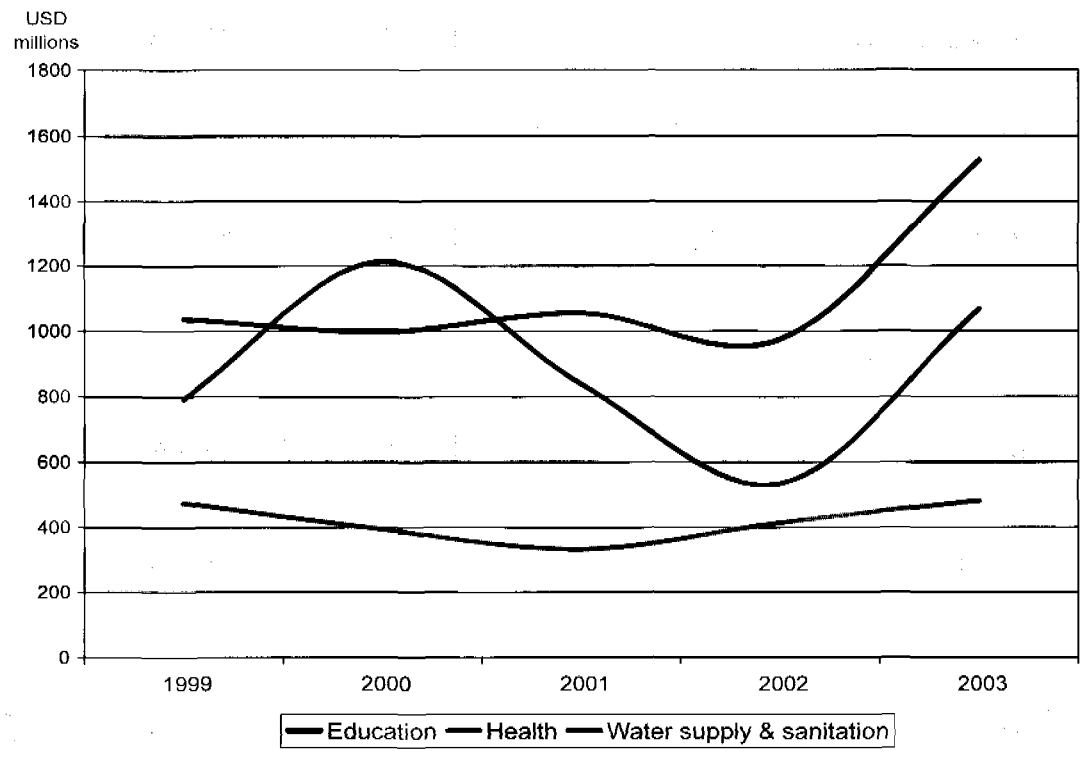
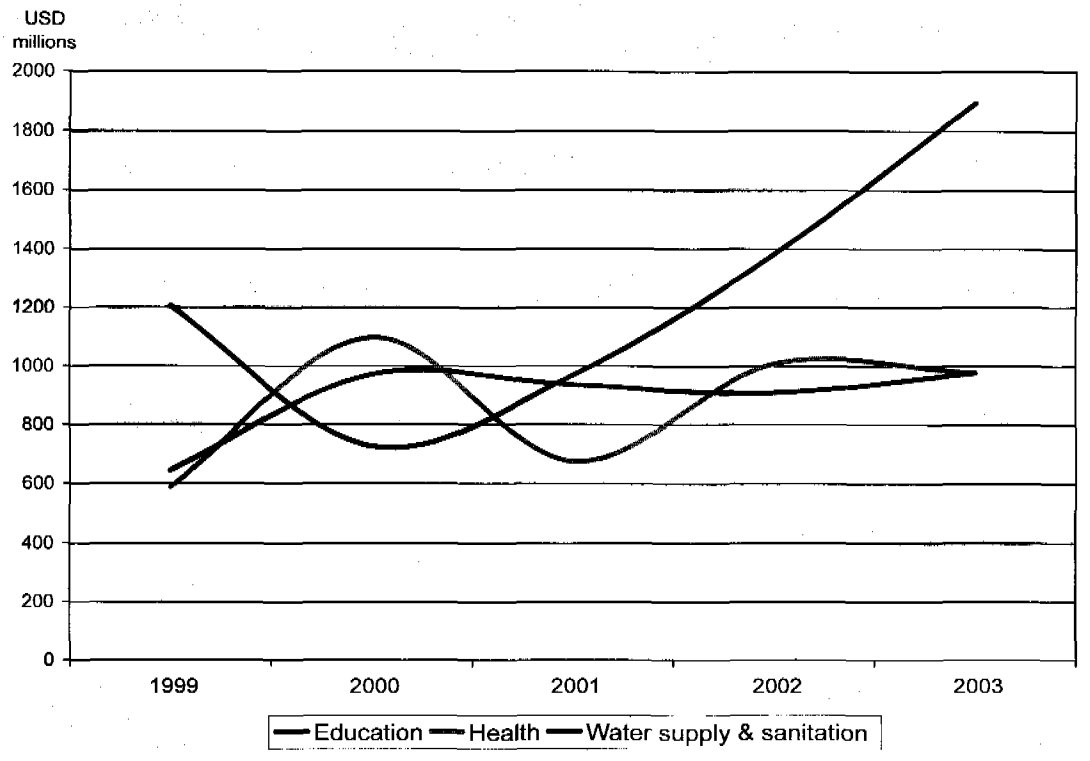
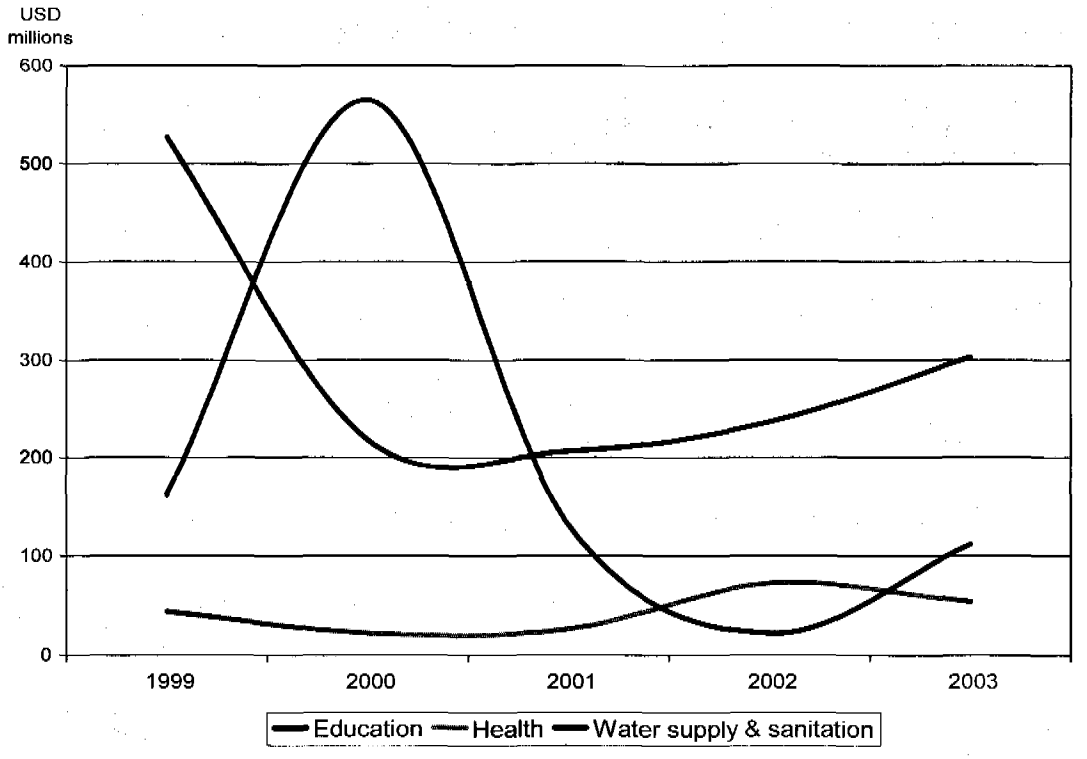


Figure 11 ODA commitments flows to education, health, and water supply and sanitation in Low Middle Income Countries, 1999-2003



This set of graphs also reveals some interesting trends that complement the regional trends

Figure 12 ODA commitments to education, health, and water supply and sanitation in Other Low Income Countries, 1999-2003



discussed above. To start, low income and least developed countries received the bulk of ODA commitments for water supply and sanitation, health, and education, compared to middle and upper middle income countries. Low income countries average nearly US$3 billion in commitments per year, compared with US$2.8 billion in least developed, US$2.4 billion to lower middle income, and US$540 million to upper middle income countries.

Within these categories, education received the highest commitments overall (US$3.9 billion), followed by water supply and sanitation (US$2.6 billion) and then health (US$2.2 billion). Further analysis of ODA commitments between 1999-2003, based on income group, is provided below:

- In **Least Developed Countries,** commitments to education have increased annually, and have nearly doubled between 1999-2003 from US$920 million to US$1.6 billion. By contrast, commitments to health have remained fairly consistent within a band of US$750 and US$950 million, although annual commitments rise and drop considerably. In the water and sanitation sector, commitments doubled between 1999 and 2001 to US$1 billion, then fell by half again between 2001 and 2002, only to rise to US$707 million in 2003.

- In **Lower Middle Income Countries,** annual commitments to the education sector remained fairly consistent, at US$1 billion, until 2003, when commitment increased by half, to US$1.5 billion. By contrast, the education sector appears to fluctuate between US$400 and US$500 million. Within the five year period, annual commitments to the water sector have seen the largest variation, with flows jumping from about US$800 million in 1999 to US$1.2 billion in 2000, falling to a low of US$500 million in 2002, and then recovering in 2003 to US$1 billion.

- Other **Low Income Countries**, which, as noted above, received the majority of ODA, show consistent commitments to water supply and sanitation over the five-year period, wavering just above and below US$1 billion. By contrast, commitments to education have increased by over two- and-a-half times since 2000 to US$1.9 billion, with increased commitments each year. Commitments to the health sector, by comparison, vary by year, with peaks at about US$1 billion, and lows of around US$600 million.

- In **Upper Middle Income Countries**, commitments to the education sector are higher than health and education, and, since 2000, commitments have risen annually to about US$300 million in 2004 (note that this is still lower than the high of US$527 million in 2000). By comparison, commitments to the health sector have varied nearly every year, for example swinging from a low of US$22 million in 2000 to US$72 million in 2002. In the water sector, which saw a trebling of commitments between 1999 and 2000 to US$565 million, commitments fell just as quickly, dropping to US$22 million in 2002.

By comparison, commitments to high-income countries (graph not shown), for water supply and sanitation, health, and education total just US$20 million in total, between 1999-2003.

Some of the year-to-year variability expressed in the water and sanitation and health sectors, both at the regional and income-based analyses, can likely be explained by larger projects that get 'booked' in a single year, although they may be multi-year programs. It is not clear at this point whether the education sector differs with regards to the types of investments made; further analysis may be required. Further, these analyses do not include multi-sectoral allocations, meaning projects that have a health and water

supply and/or sanitation component, for example. As a result, the figures for total spending may be underestimated.

Still, it is clear that while the education sector receives annual and increasing commitments, commitments to the health and water sectors are more varied. Also, aside from the rapid increase in water sector commitments in South and Central Asia, overall commitments to water pale in comparison to education, and in Sub-Saharan Africa, to the health sector.

ODA commitments to broader governance and financial management

The somewhat flat level of commitments to the water sector has been attributed in recent years to the lower priority countries place on the water sector relative to other investments through the PRSP process.[12] The PRSP process has emerged as an important process to stimulate realistic planning and budgeting at a country level, as well as coordinate ODA flows amongst different development agencies. One of the core premises of the PRSP is that the process be country-driven, with governments leading the process, participation from civil society and the private sector, and support from donors. It was originally intended as a means to reduce debt burdens in Highly Indebted Poor Countries (HIPC), and it generally understood that the governance frameworks at the national and sub-sovereign levels in these countries were too weak to embark on the process without substantial support from the donor community. Importantly, there is increasing awareness of the need for PRSPs to be MDG-focused, incorporating a longer-term vision within the three-year planning process.

Decades of water sector experience have shown[13] that sustainable access to water and sanitation services depends strongly on the capacity, and interest, of government to provide these services (whether directly or through creating an enabling environment for others to do so). Therefore, improvements in the broader governance environment may lead towards more sustainable water sector reform. A recent DFID study on the MDG for water supply and sanitation[14] analyzed key elements of governance in 12 countries in Sub-Saharan Africa and Asia. Though preliminary and qualitative in nature, the study found strong evidence that those countries with the strongest governance frameworks also tended to be the most likely to achieve the MDGs for water supply and sanitation.

In addition to governance frameworks, the other core challenge facing the sector relates to financing. As seen throughout this paper, ODA flows to the water sector, which historically have constituted a majority of the funding for water and sanitation, are insufficient to achieve the MDGs. A current trend is to promote 'leveraging' additional finance into the sector by looking beyond traditional grants and sovereign loans. This includes the development and growth of domestic capital markets, support for domestic private sector entrepreneurs, use of different types of finance (including equity, guarantees, and commercially-based debt). Still, the potential for leveraging is often limited, due to constraints relating to legal and regulatory banking frameworks, governance of the financial sector, and capacity within the sector to manage and expand business using different products and services. Hence, ODA could be targeted to reform both the financial sector within countries, and also the business environment for domestic, private entrepreneurs to operate. In turn, these types of efforts could create an enabling environment for 'leveraging' water-related investments.

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12 WSP Benchmarking Study, and Water Supply and Sanitation in PRSP Initiatives, by the WSP-Africa.

13 Including the MDG Task Force on Water Supply and Sanitation's Final Report, "Health, Dignity, and Development: what will it take?"

14 ERM DFID study: Meeting the MDGs – what will it take? April 2005.

The next set of graphs depicts ODA commitments between 1999 and 2003 to governance and civil society, the banking and financial sector, and business and other sectors in order to determine, broadly, whether ODA is focusing on these categories, and where. **Box 2** provides the definition of these categories, according to the OECD DAC/CRS.

Box 2 DAC/CRS definitions

The DAC defines aid to Governance and Civil Society as including the following sub-categories: Economic and development policy, public sector financial management, legal and judicial development, government administration, strengthening civil society, post conflict peace building, elections, human rights, demobilization, free flow of information, and land mine clearance. Likewise, the Banking and Financial Sector includes financial policy and administrative management, monetary institutions, formal sector financial intermediaries, informal/semi formal financial intermediaries, and education/training in banking and financial services. Business and Other Sectors refers to business support services and institutions, and privatization. There are other relevant sub-categories which may be interesting to analyze: SME (small and medium enterprise) development falls under the Industry sector, while statistical capacity falls under *Other Social Infrastructure and Services*.

Figure 13 ODA commitments to governance and civil society, banking and financial services, and business and other services in Far East Asia, 1999-2003

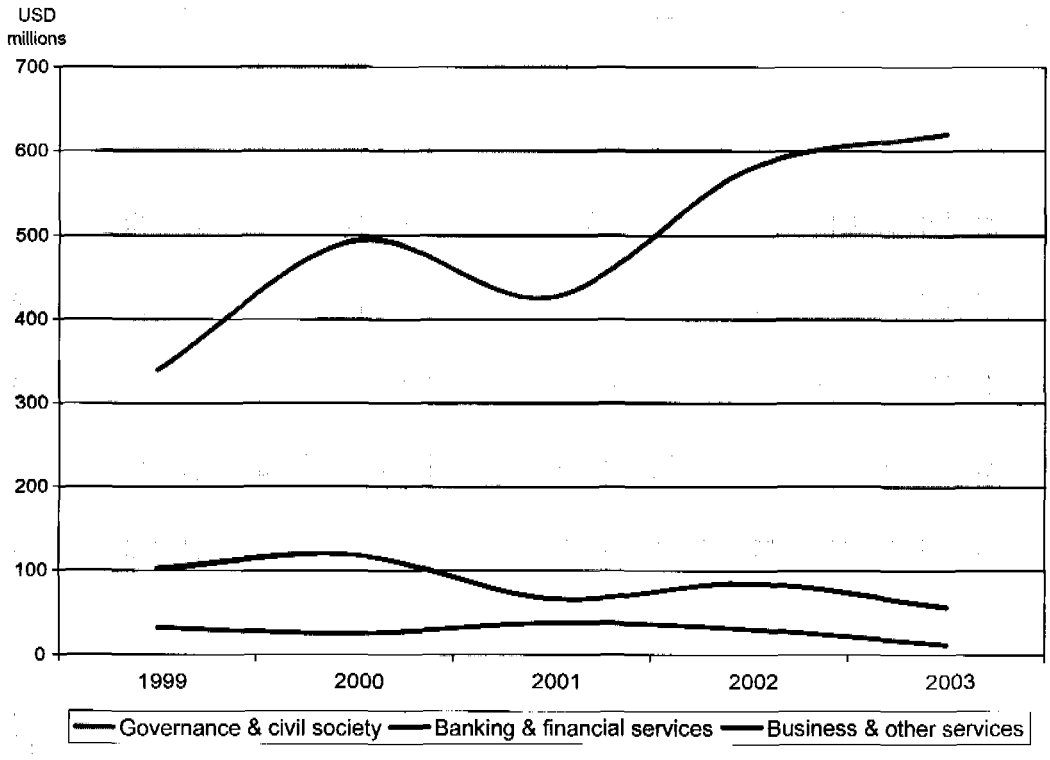


Figure 14 ODA commitments to governance and civil society, banking and financial services, and business and other services in LAC, 1999-2003

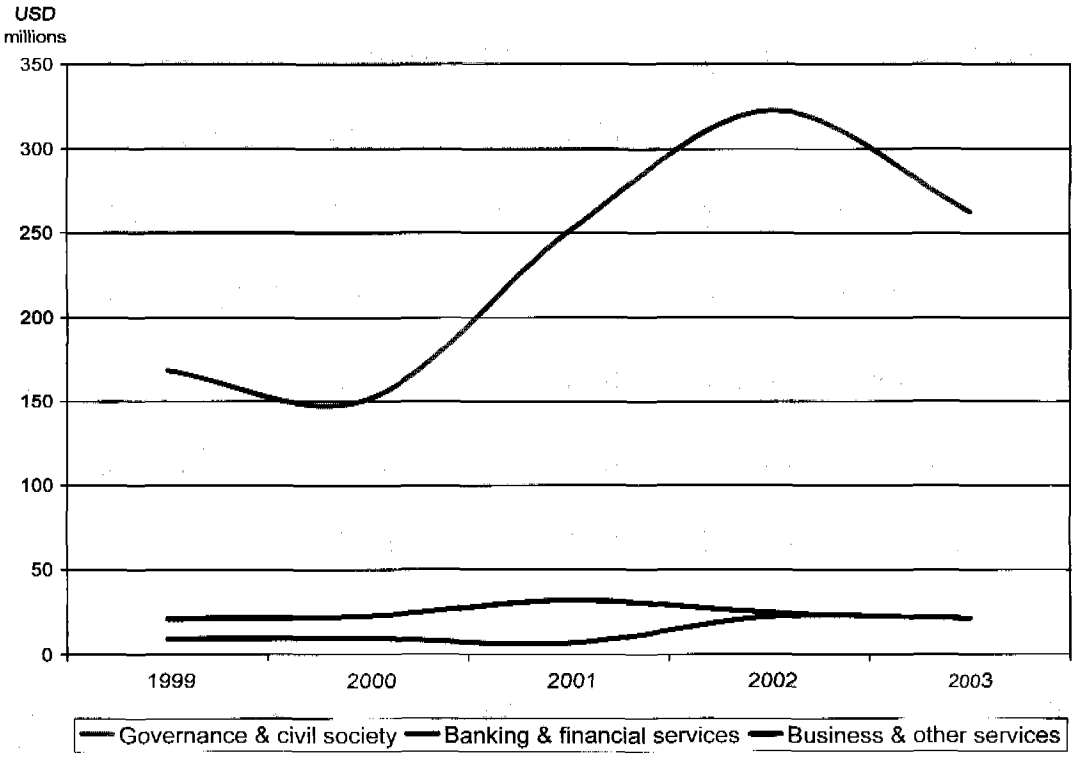
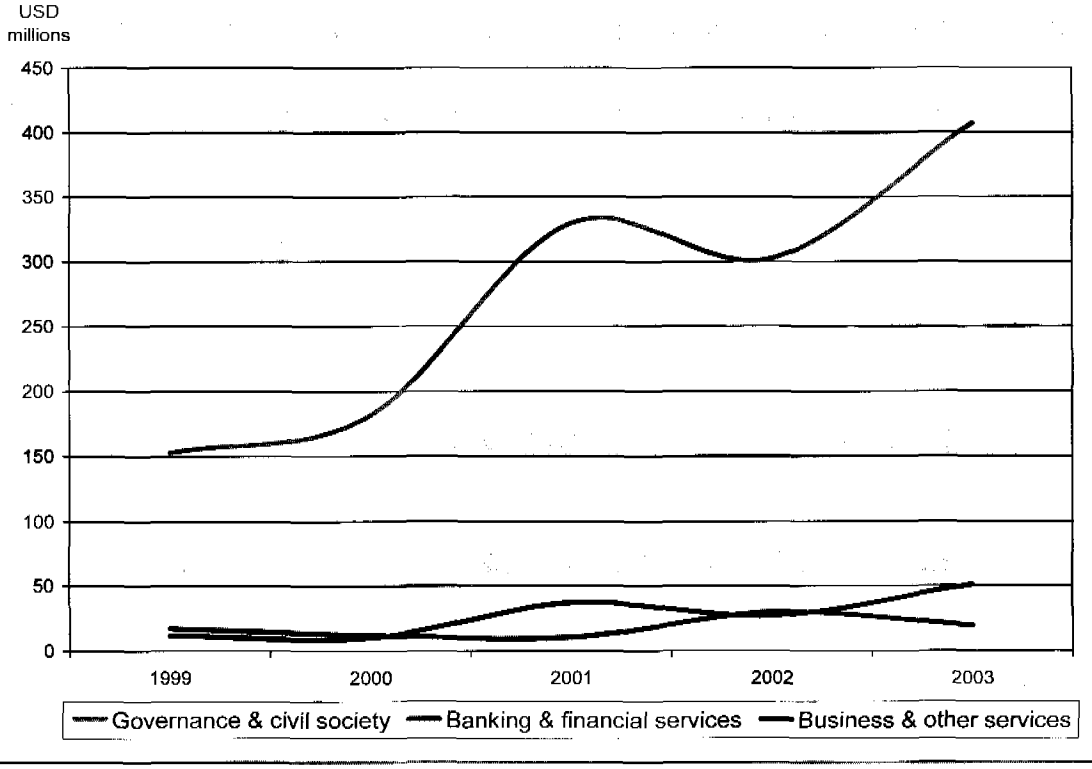


Figure 15 ODA commitments to governance and civil society, banking and financial services, and business and other services in South & Central Asia, 1999-2003



Overall, average ODA commitments between 1999 and 2003 to governance and civil society interventions (US$1.4 billion) overwhelmingly exceed commitments to banking and financial services (US$97 million) and business/other services (US$254). Comparing regions, Sub-Saharan Africa received, on average, US$606 million per year between 1999-2003, followed by US$564 million in South & Central Asia, US$319 million in Far East Asia, and US$269 million in Latin America/Caribbean. On an annual basis, annual commitments to governance and civil society interventions have also increased considerably. South & Central Asia's commitments increased five-fold, from US$157 to US$796 million. Commitments in Far East Asia increased by over two and half times, from US$152 to US$407 million. By comparison, Sub-Saharan Africa saw a near doubling in commitments from US$340 to US $620 million over the five-year period; commitments in Latin America/Caribbean rose from US$168 million in 1999 to US$323 million in 2002, but fell in 2003 to US$262 million.

Considering ODA commitments by income base, the data shows the following:

- For **governance related activities:**, Lower Middle Income Countries received the most, at US$711 million per year on an average basis between 1999-2003. This was followed by Least Developed Countries, at US$549, then Other Low Income Countries (US$455). Upper Middle Income Countries and High Income Countries, by comparison, received US$78 million and US$2 million, respectively.

- Funding for governance was an order of magnitude higher than that for **banking and financial services.** In this category, Other Low Income Countries received the most, at US$43 million, followed by Lower Middle Income Countries (US$36 million), Least Developed Countries (US$27 million), Upper Middle Income Countries (US$3 million) and High Income Countries (US$200,000).

- Commitments for **business and other services** was more varied; Lower Middle Income Countries received US$252 million, followed by Other Low Income Countries (US$116 million), Least Developed Countries (US$45 million), and Upper Middle Income Countries (US$20 million).

The (overall) increase and quantity in ODA commitments towards governance and civil society strengthening may reflect prioritization as a result of the PRSP process, or could reflect a more general trend towards improving governance, particularly in South & Central Asia and Sub-Saharan Africa. However, it should be noted that as with previous analyses presented in this article, there may not be a direct relationship between the quantity of funding and the quality. Further, the types of interventions supported by the "governance and civil society" category include public financial management; hence the relative lack of attention to the financial sector and business environment could be a function of sequencing, or a bias towards public sector expenditures, given the nature of traditional ODA (whereby funding is disbursed to, and through, central government).

4 Preliminary findings and topics for further research

This analysis shows that ODA flows to the water supply and sanitation sector will be insufficient to cover the projected costs to achieve the water supply and sanitation MDG targets. This is because ODA flows are insufficient relative to estimated needs, and because the nature of ODA poses constraints, including a lag time between commitments and disbursement, administrative and transaction costs at both the donor and recipient government level to manage programs and interventions at the sovereign, and increasingly sub-sovereign levels; and the political dynamic associated with allocation of funds across regions and sectors.

Compared with other sectors, ODA commitments to water supply and sanitation are at par with commitments to the health sector, often facing wide variations from year to year. By contrast, commitments to the education sector increased substantially between 1999-2003, in all regions, and across all country income levels. It is not clear at this point whether the education sector differs with regards to the types of investments made; further analysis may be required to understand whether there are lessons learned which can be applied to the water and sanitation sector.

Learning from other sectors

The data analysis in this report illustrates strong annual increases in ODA commitments to the education sector, while the water supply and sanitation, and health sectors are more variable. These findings, while preliminary, support previous findings. For example, the Global Monitoring Report 2005 notes that low-income countries' spending on health and education increased considerably between 1990-2002, largely as a result of the MDGs. One possible reason for this rapid increase is the emergence of global programs.

In the education sector, there is a single global partnership – the Education for All Fast Track Initiative (FTI), which partners donors and recipient governments 'to ensure accelerated progress towards the Millennium Development Goal of universal primary education by 2015'.[15] Through FTI, developing countries commit to put primary education at the top of their development agendas, and donors commit to coordinated, predictable, transparent, and increased ODA.

By comparison, there are well over 70 such global programs, including the Global Fund to Fight AIDS, Tuberculosis, and Malaria (GFATM), which have had a considerable impact. In particular, for HIV/AIDS funding, an estimated 80% of public spending globally came from external grants.[16] These programs, both within the donor community and out of private philanthropy, have targeted global awareness of

15 Education For All Fast Track Initiative website: http://www1.worldbank.org/education/efafti/
16 Global Monitoring Report, 2005.

health issues. The abundance of private initiatives have managed to raise awareness within the donor community to the need for health sector funding, and, interestingly, tend to focus more on low-income countries with pro-poor initiatives than donors themselves (considering total ODA commitments).

Best practice norms in the education sector suggest that 20% of the recurrent budget, and 4% of GDP should be focused on education, and half of that should focus on primary education (page 92). Further, through the Abuja Declaration (2000), African governments agreed that health expenditures should increase to 15% of their budgets (the average is 8%). Notably, research conducted by the World Bank indicates that even this amount increase in budget prioritizations will not, on its own, bridge the finance gap in these sectors.[17]

The clarity of the agenda for the education sector, and the multi-targeted approach in the health sector, could provide lessons for the water sector. To start, similar agreements and best practices for the water sector do not exist. While there are partnerships for water and efforts towards collaboration, these tend to be at a regional or country level, for example, through Sector Wide Approaches (SWAps). Private contributions for water and sanitation are not clearly tracked and tend to be highly decentralized. This may reflect the nature of the sector, or result from a lack of clear leadership for the sector.[18] However, these types of initiatives and guidelines may help to improve political awareness of the need for water sector expenditures, including infrastructure, but more importantly, the capacity and technical investments required.

ODA and different country income levels

Given the rates of poverty and focus on the MDGs for the poor, ODA funding levels in least developed and low- income countries should be substantially higher than those for more middle-income countries. Broadly this is because the latter are more likely able to attract more commercial or near-commercial sources of finance, perhaps with incremental types of ODA, such as equity and guarantees, while the former likely require substantial ODA simply for the government to operate.

The data presented in this paper illustrates that, in terms of sectoral funding, LDCs, LMICs, and OLICs do attract greater amounts of ODA than UMICs and high-income countries. However, as reflected in the regional analysis, there is variation amongst the education, health, and water sectors, with an apparent prioritization for education. LMICs received the bulk of governance and civil society expenditures, and more than twice as much for business and other services than other categories. In contrast, OLICs received the most for banking and finance, compared with LMICs, LDCs and UPMIs. Further investigation into the types of activities such funding supports (outside the water sector) within these income-based groupings, and how these work to stimulate, support, or scale up development efforts, may prove useful entry points for more targeted water sector reform.

17 Global Monitoring Report, 2005.

18 For example, within the UN system alone there are at least 10 organizations and departments focused on water, each with a unique perspective.

The importance of an MDG-based PRSP

The PRSP/MTEF process calls for a demand-led process, where countries prioritize sectors for reform and funding. Building on this concept, donors are supposed to increase coordination of their funding flows, and provide funding through the government budget, to increase the effectiveness of their ODA. One of the key constraints to this process is that as a result of the prioritization process, there may be sector ceilings which 'cap' the amount of funding allowed in the national budget every year. This results in budget ceilings that 'cap' funding at sub-sovereign levels, also on an annual basis.

Because a country's PRSP, and subsequent targeting and release of ODA from donors, is dependent on the World Bank and IMF for approval, the latter have the power to reject the funding mix proposed by countries. As a result, the sector ceilings proposed by a recipient government may be drastically reduced, dampening the longer-term effectiveness of stakeholder engagement and planning processes that created the sector budget in the first place.

For this reason, an MDG-based PRSP would be a significant improvement. Rather than consider funding for a three-year cycle, an MDG-based approach would consider the full range of investments required until 2015. Once the cost to achieve the MDGs in total is determined, the country, along with development partners, could engage in a real discussion about the types of finance mechanisms that might be applicable, given the policy environment; what reforms may be needed between now and 2015, and in what sequence they would be most effective; and whether investments in other sectors could have crossover benefits to achieve other MDGs. The Global Monitoring Report 2005 notes that most of Sub-Saharan Africa is off track to achieve most of the MDGs, not just water and education; the report also notes that a financing gap exists for all sectors. While this may lead to greater competition for limited ODA flows, an MDG based approach provides increased opportunities for collaboration to identify all sources of finance which could be harnessed for economic development and poverty reduction, whether public, private, NGO, or user based. The importance of considering the multi-dimensional nature of poverty is critical to achieving the MDGs; mobilizing ODA flows, both through increasing absolute quantities of aid, and through increased aid effectiveness (getting more bang for each buck) should be paramount.

Sequencing reform

The increased interest in programmatic lending and sector wide approaches may be a useful way to intensify coordination of donor flows at a sovereign level, as well as build support for governance functions. Depending on the country, and the structure of its PRSP, it might make sense to focus on core governance issues – including institutional arrangements, legal and regulatory functions, and monitoring and evaluation – before focusing on specific water sector reform. However, shifts in donor flows should be planned and sequenced. The impact of a shift in funding from isolated, off-budget projects to support core governance issues may lead to an effective collapse of water and sanitation services in rural or urban areas. Existing projects and programs, even if they do not fit within an agency's current policy paradigm, should continue to be supported so as to become operationally and financially viable over time.

Commitments vs. Disbursements

The MDGs offer a limited time frame to accomplish a great deal, with regards to macro-economic policies (broad poverty reduction), gender health, education, environment, trade, and so forth. For the water sector, which is still considered an 'infrastructure' sector, both at the donor and recipient levels, there is a risk that the limited time available may lead to supply-side thinking – in other words, using funds to roll out massive infrastructure projects. Unfortunately, this approach has been tried before, and has been demonstrated not to achieve sustainable solutions. Institutional, governance, and financial reforms are needed in most regions; this requires a longer-term, and more incremental, approach. It also requires consistent and stable funding, of the type provided through ODA.

Flexibility of ODA flows

On the bright side, these needed reforms are important as core governance functions, no matter what the sector, or which MDG goal one considers. Donor funding that is more flexible to adapt to local circumstances may be better value for money, from a sustainability perspective, than pre-planned projects that may or may not be feasible, given circumstances. For example, several years ago the EDF was primed to fund a large dam in Africa. However, the application form for funding was inadequate, and the potential costs to support the types of studies needed to support the project were deemed too much to address the potential project risks. As a result, the EDF funded an institutional strengthening project, so that the government could develop the project preparation skills needed to apply for funds in the future.19 This principle of flexibility should also be applied cross-sectorally, to support better use of limited funding.

Predictability of ODA flows

The issue of predictable finance has become a key issue for aid harmonization. In practice, development agencies within donor countries must propose budgets on an annual basis, complicating the ability to parallel national planning processes at a recipient country level. In an environment where governance frameworks, including public financial management, are critical for success, the predictability of aid flows is imperative. This includes matching the amount committed with that which is disbursed and making payments according to a set schedule. Predictability is also important at a recipient country level; for example in the water sector, longer-term contracts and programs grounded in tariff reform have often been started, and even implemented, only to fail because of a new political administration promising free water.

Uses of ODA

Donor flows tend to operate on a five-year basis, and in the water sector, tend to support capital costs of large-scale water systems (often with some level of co-finance from communities). At the same time, the policy, governance, technical, and financial constraints to functional recovery of operations and main-

19 ERM, 2005a.

tenance fees lag, resulting in over-designed systems that communities – whether in urban, peri-urban, small towns or rural areas – do not use.

Accepting the reality of ODA flows to water supply and sanitation, staff within donor agencies should consider ways to increase development impact with less funding, while advocating recipient countries for prioritization of water and sanitation through the PRSP process. Within their own agencies and internationally, staff should advocate for additional funding, while demonstrating the value for money from their water and sanitation programs.

Allocation and targeting of ODA

According to the Global Monitoring Report 2005,20 public expenditures provided outside of ODA are on the rise, largely as a result of economic development, throughout Asia and Latin America, but not in Sub-Saharan Africa. Likewise, economic development has been linked, broadly, in those countries where legal and regulatory issues are consistent, where laws are enforced, and where policies are in place to stimulate business development. While increasing ODA flows to support governance may not be the answer (note that Sub-Saharan Africa receives the most funding relative to other regions, but boasts the worst performance), new thinking on how to improve governance efforts, possibly drawing from the approaches used in other countries, may be appropriate. For example, secondments from donor agencies into government agencies at the sovereign or even sub-sovereign levels, or strengthening of non-governmental organizations as advocates for governance reform may be useful, and cost-effective, approaches.

Looking beyond ODA

As outlined in Section 1, the ODA analyses presented in this article relate to traditional grant based and concessional loan-based finance. Over the last few years, a number of agencies have shifted to support new programs and initiatives that focus on leveraging other forms of finance, whether from users, domestic private sector, the international private sector (both private utilities as well as industry and commercial business), and the domestic financial sector. These initiatives also work to apply other types of finance, including guarantees, equity, and more commercially-oriented debt mechanisms to the water sector. Due to the nature of the DAC and CRS databases, and for technical and accounting-based reasons, these activities are not captured in this analysis. Further information about these issues can be found in a complementary paper *"Experiences in Innovation: Financing Small Town Water Supply and Sanitation Service Delivery"*.

Other sources of finance

In addition to the application of ODA in new ways, other forms of finance are not even tracked. For example, international and domestic non-governmental organizations (I/NGOs) tend to construct substantial amounts of infrastructure and provide capacity building programs around the world,

20 Global Monitoring Report, 2005

but tend to operate under the radar screen of broader government. Because of the nature of these organizations, administrative overhead is kept to a minimum, which leads to a lack of record-keeping about financial flows, and impacts. In some countries, this may reflect the lack of governance function; in others, perceived conflicts of interest may be the cause. One of the findings from the recent DFID study on the water and sanitation MDGs was that as the PRSP process develops, new opportunities open for NGOs that may traditionally have been service providers to become advocates for governance reform, which may help to address this disconnect.

Specific suggestions for small towns

Small towns face specific challenges in the context of ODA flows. Some important challenges, along with suggested policy implications, include:

- Inclusion in the planning process. Most countries use an urban/rural split to differentiate different needs within the water sector. Small towns tend to border between urban:peri-urban, or urban:rural, which places them at a disadvantage with regards to understanding their unique qualities and constraints. From a governance perspective, small towns can either be municipalities, or be a part of a larger municipality. Because of this lack of clarity, their planning and financing needs are particularly important, and often missing. Governance processes, including water strategies, PRSPs, and MTEFs, should include the needs of small towns to the best extent possible.

- ODA flows to small towns should be used creatively, to tap into other possible sources of finance available, including existing commercial and industrial business, micro-finance centers, NGOs, and consumers for networked water supply, sanitation, and drainage solutions, both to extend the impact of ODA as far as possible, but also to engage these different stakeholders in the planning, implementation, financing, and oversight of interventions.

- Likewise, ODA should be used to support the sustainable operations and financing of existing small utilities, whether through management models or finance mechanisms, and particular attention should be paid to tariff reform and cost recovery. Smaller utilities tend to carry high debt levels – a result of over-design from previous donor interventions – which minimizes their ability to extend services to meet demand, or operate without considerable and ongoing subsidies from government and donors.

- Finally, ODA support for the purposes of strengthening small-scale domestic providers of water and sanitation services, through improving the business development environment, the domestic private sector, and relations with utilities, is highly appropriate.

Low income countries, and countries with weak governance structures remain highly dependent on ODA grants and loans to fund their budgets. Building on the principles above, of increasing aid flexibility, predictability, and sequencing, within the framework of an MDG-based PRSP process, would go a long way at improving governance structures to support more market-based solutions. By contrast, the challenges of disbursement delays, frequent changes in donor policy, and cutbacks for varied reasons all create an unstable governance environment, which can have a substantial impact at the national, sub-sovereign, and human level.

Topics for further research

This paper has sought to highlight trends in ODA flows, and specifically place water supply and sanitation ODA flows within the context of broader development issues, including health, education, governance and financial sector reform. Importantly, success in meeting the MDGs will require considerable additional attention to the water sector, but this must also be taken in the context of other MDGs and other funding flows. With this in mind, further research on the following topics would be useful:

- How real is the shifting nature of donor funding towards more market-based mechanisms? Has this shift impacted donor agencies' mandates, and in what ways?
- Are there best practices to increase the effectiveness of ODA flows with regards to activities – for example, what are the various costs and benefits of providing infrastructure over training and secondment programs in different countries?
- How does the trend towards decentralization of government functions impact traditional sources of ODA, and how can donors adapt to provide appropriate types of support, and develop appropriate relationships?
- Are the grants and loans provided through ODA at a country level targeted to those most in need? How does programmatic lending impact this targeting?
- In light of the above, how can the international community fill the gap caused by declining commitments and, eight years hence, disbursements?

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