WaterAid

Development
Finance
International

Financial absorption in the water, sanitation and hygiene (WASH) sector:

Lessons from five country case studies[1]

1. Introduction and background

1.1 Background to study

The Water, Sanitation and Hygiene (WASH) sector has already suffered major funding shortfalls in the context of the Millennium Development Goals (MDGs), and without significant change this is likely to continue under the recently-agreed Sustainable Development Goals (SDGs). Less than 10% of the 31 countries with available data on WASH (as analysed in the Government Spending Watch (GSW) 2015 report) are allocating the 1.5% of Gross Domestic Product (GDP), which the United Nations Development Programme (UNDP) estimated as necessary to reach the MDGs.[2] WASH budgets account on average for only 2.3% of government budgets and 0.9% of GDP, and these averages have been stagnant since 2011.[3]

Added to this allocation shortfall, the WASH sector suffers from the largest shortfall of actual expenditure compared to planned budget spending among all sectors studied in the GSW; over the 2011/13 period the WASH sector accounted for a 13% underspend (where actual expenditure data was available). Whereas this shortfall tends to not be as significant in other sectors, in WASH it is a major issue.

WaterAid therefore commissioned Development Finance International (DFI) to carry out detailed analysis of financial absorption in the WASH sector, through five country case studies. This note summarises the findings and recommendations highlighted across the studies, and compares them with broader analysis DFI has carried out in the GSW programme for 31 countries, drawing lessons for financing WASH post-2015.

The study focuses on 'financial absorption' – i.e. whether spending allocated to WASH (clean drinking water and sanitation facilities) has been implemented on schedule: it does not look at whether allocations are adequate, or on the impact of spending.

1.2 The five country case studies

The five countries chosen for this study were Ethiopia, Mozambique, Rwanda, South Africa, and Uganda. They were chosen for a combination of factors, the most important being significant progress in delivering higher WASH spending and results since 2000, so as to learn lessons from their success. Although Rwanda did not meet the water and sanitation MDG targets, it made good progress on both and it is one of very few to have performed well against the sanitation target. Rwanda is aiming for universal coverage by 2020. If it meets this goal it will be the first sub-Saharan African country to do so. Ethiopia and South Africa have met the MDG water target. Both Ethiopia and Rwanda have been hailed as low-income sub-Saharan African country WASH success stories – and it was hoped their stories would shed light on the connections between spending, financial absorption and good WASH outcomes. Both countries' successes have been seen as, at least in part, due to strong leadership and political will on WASH by the respective governments at senior levels.[4] Uganda has also met the water target, and Mozambique has made considerable progress towards achieving it.

The countries have also seen significant recent improvements in financial absorption and/or are already performing well. Since 2011, Ethiopia has improved from 66% to 98%; Uganda from 60% to 91%. Rwanda had very high absorption in 2011/12 and 2012/13 budget years (at 94% and 95% budget execution respectively), however, this fell in 2014/15 (to 84%), due to widespread institutional reform. This is expected to pick up again, though, and does mean they have very high average overall (at 91%). Mozambique has made some significant strides, i.e. at central level, budget execution levels for capital went up from 83% in 2011 to 93% in 2013, while some provinces have made dramatic improvement in the last few years going from an average of 43% in 2011 to 75% in 2013 (this overall average, however, masks some spectacular progress from very low to relatively high levels in certain provinces (see Mozambique study for more information). Finally, South Africa overall has high levels (at around 100% nationally) although this masks some provinces with lower levels.

Other key common elements across case studies which influenced their selection were: an active decentralisation process, to test the impact of decentralisation on absorption; availability of data on WASH spending, including at decentralised level; and availability of competent authors with connections to government sources and access to data.[5]

However, South Africa differs somewhat from the other countries: it is a middle-income country with virtually no Official Development Assistance (ODA) funding, and which therefore funds most WASH spending from its own tax and tariff revenue. It is included to act as an alternative perspective to assess domestic revenue spending in a country not skewed by aid levels in WASH, to assess problems with government structures, and to help other countries learn from maturity in WASH structures, especially of decentralisation.

1.3 Methodology

The overall objective of the study was to identify the main causes of low financial absorption in the water and sanitation sector, and key steps to achieve higher levels of absorption.

To identify potential case studies, DFI conducted an initial scoping analysis of data availability and progress in increasing spending and results; DFI and WaterAid then agreed the list of countries. DFI identified country authors for each study, who conducted a more detailed scoping of data availability, and chose two local government areas/districts (generally one with poor absorption and one with better absorption). Each author then interviewed sector stakeholders and analysed data and documents to answer the key research questions.

2. Key absorption challenges and enabling factors

2.1 Leadership is critical, translated into institutional reforms for improvements

The key factor in overcoming challenges and making progress has been strong leadership. In particular, in Ethiopia and Rwanda, political will has translated into positive actions – including action on increasing spending – at country level for delivering WASH. This seems to strongly suggest that the stronger the political leadership and priority given to the sector and MDG-related results, the greater the progress in terms of transparency, coordination, spending and results.[6] For instance, South Africa's highly decentralised system has huge disparities between well-performing municipalities, where leadership seems to play a key role, compared to low performers (where weak leadership is identified as an issue).

A number of the countries in the study are in a process of enacting institutional reforms and/or streamlining their funding mechanisms. Ethiopia has for some years now been in the process of setting up better coordination for financing in the WASH sector, and has recently set-up a sector-wide approach (SWAp), while also clearly setting-out clearer processes for agreeing and communicating the different actors' and ministries'/agencies' roles. Mozambique shows good progress in improvements to streamline the WASH sector and improve coordination. Rwanda is in the process of reforming the role of the water board, and defining the various institutional relationships in the sector.

2.2 Donor behaviour is the major blockage to high financial absorption in WASH

The most important absorption problem identified across all countries – except for South Africa as it receives virtually no aid for WASH[7] – is lower ability to absorb donor funds. In Rwanda, Mozambique, Uganda and Ethiopia, absorption of donor funding is significantly worse than government funding. Rwanda identified donor funds as by far the biggest issue preventing better absorption: in 2013/14 budgets this stood as 84% for domestic allocation to 60% for donor funds. Indeed, Rwanda made major efforts to overcome slow donor absorption by allocating higher levels of government funds to capital spending (finding 38% of central capital budgets and 56% of district budgets itself).

This was particularly true at the decentralised level: where government procedures and funds are predominant, absorption is higher, and in districts with high donor funds it is lower. For instance in the Amuru district, Uganda, donor funding performed 40-45% worse than government funding, bringing overall absorption down to 50-60%, whereas in Nakasongola, all funding for the water sector was from central government transfers, of which 95% were absorbed in 2013/14.

All four countries explain problems with donor absorption as being the result of:
- High transaction costs and coordination problems caused by **fragmentation** of donor activity into multiple small projects.
- The **inappropriate mix of capital and recurrent spending** caused by donor funds. Though this might appear at first sight as a 'misrecording issue', given that

all donor funds except sector budget support are classified as 'capital spending' regardless of the type of activity they support,[8] in fact the case studies confirm that a lack of recurrent spending is a crucial barrier to overall absorption (see 3.4 below).

- **Delays in disbursement**, because of cumbersome donor procedures for financial management such as long periods in processing disbursement requests, and demands for deposits by contractors.
- **Delays in procurement** because of complex donor procedures such as excessively low thresholds for international competitive bidding and long delays in giving non-objections or approvals at various stages of the procurement process.
- **Conflict between donor and government procedures**, in terms of planning and budgeting calendars, disbursement and procurement, which mean that project and sector managers suffer from confusion and duplication in accessing disbursements.
- **Knock-on effects of delays** in donor disbursements to decentralised agencies, which prevented them from following other procedures and applying for additional government or donor funds in the budget year.

Analysis in the GSW analysis confirms these findings. It shows that WASH has been the only sector to register large increases in donor funding since 2012, but this has left the sector highly dependent (75%) on donor funds, and with larger spending shortfalls than any other sector. If spending is to be accelerated post-2015, donors are going to need to simplify their procedures, and use government systems wherever possible, preferably by providing budget support.

2.3 Insufficient recurrent spending is the second most important issue

The issue of an inappropriate capital to recurrent mix was the second most important concern. As discussed above, this is largely linked to overreliance on donor funds, which are almost all capital investment and therefore skew funds away from managing projects and running costs (meaning many projects cannot be sustained over the long term). Mozambique, Rwanda, Ethiopia and Uganda all highlight this. In Uganda, high levels of capital spending in some provinces did not allow enough recurrent spending to facilitate absorption. In Mozambique there was too little recurrent finance to pay decent wages, especially in remote provinces. Low levels of recurrent funds also had a perverse double impact as there were no funds to pay for the inspection, which delayed verification of the work, delaying subsequent tranches of disbursement.

It is not only highly donor-dependent countries who struggle to absorb capital spending. For South Africa's eight underspending provinces, average capital budget absorption was only 72% – largely the result of inadequate allocation of recurrent resources for municipal planning, and shortfalls in decentralised revenue generation.

However, broader GSW analysis confirms that there is a close link between the degree of dependence on donor project-based funding in a sector, and inadequate recurrent spending. Across 32 countries, the WASH sector budget contains 83%

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investment spending. This is validated by sector experts who have for many years complained about a lack of recurrent spending to maintain water and sanitation facilities once constructed, and emphasises the need for adequate recurrent funding from government resources – and for donors to fund recurrent spend through budget support.

2.4 Low capacity is the third key problem, especially at decentralised level

Low absorption also reflects weak capacity (due to inadequate recurrent spending) hampering implementation of capital spending, particularly in decentralised agencies (or newly created private agencies). Lack of recurrent budgets has left gaps in staffing capacities, (especially in Ethiopia), and made it hard for the public sector to attract and retain good quality staff in rural areas (Uganda and Mozambique).

For instance, in Amuru district, Uganda, the water department is supposed to have five staff but currently has only one full-time staff member and two other staff seconded by other sectors, with other additional responsibilities. In South Africa, the civil engineering capacity (expressed as civil engineering professionals per 100,000 people) in local government is too low to deliver, operate and maintain local government infrastructure in a sustainable manner. From 20 engineers per 100,000 people in 1994, this has dropped to three per 100,000 people, a ratio that is, as one official document put it "clearly indicative of a crisis".

Broader lack of capacity in the sector is also raised across all studies. In South Africa there is insufficient and weak capacity in all planning and implementing agencies. The case study of Ethiopia raises a major concern about weak capacity among private sector operators. Capacity constraints are worsened by multiple different agencies for rural and urban services in Ethiopia and Rwanda, especially if private agencies draw capacity away from the public sector by paying higher wages.

2.5 Government procedures can also be problematic

Government procedures can also be problematic – although much less so than those of donors, as evidenced by much higher government-funded absorption rates. Three key issues emerge:

- **Procurement and contracting delays** due to of bureaucracy and slow information flows.
- **Underestimation of costs by private companies** when bidding for contracts. Subsequent cost overruns (and resulting demands that government find more funds) have brought projects grinding to a halt in Uganda, Ethiopia, and Mozambique.
- **Slow fund releases from central government**, and unclear information to decentralised agencies about when funds will be transferred or in what amounts, leading officials to halt projects.
- **Cuts in spending during the year** when there are shortfalls in donor flows, and central or (in decentralised cases) local government revenue, or when other emergency spending needs arise.

2.6 Decentralisation and privatisation create opportunities, but pose major risks

The jury is out on whether decentralisation and/or privatisation can increase absorption. The theory is that decentralisation improves absorption by enhancing local accountability, but the South Africa study shows that this happens only when there is strong implementation capacity, openness to accountability and supply of comprehensible information to the public, and citizen/CSO will to hold government accountable. Equally, private sector involvement is supposed to enhance efficiency, but this will not happen unless there is high management and implementation capacity, full transparency and accountability, and very careful design of contracts to share costs and risk between the government and private sector: even then, it can easily result in higher costs and reduced access for poorer consumers. Lack of capacity in private sector actors is highlighted as a major concern in Ethiopia; a problem of underbidding is flagged in Rwanda—Rwanda is midway through moving to a decentralised Public Private Partnership (PPP) model from a more community-based model, and this might need following more closely in future.

In addition, the case studies show major risks of both decentralisation and privatisation. The initial effects of both have been to add another layer of complexity, disperse limited capacity across a larger number of agencies, and create management units with very limited capacity. Privatisation has the potential to be a barrier to transparency in contracting and financing when accompanied by less detailed reporting to government and parliament, and has increased costs by raising salaries of managers and having to pay profit needs/financing costs of private implementing agencies. These risks are higher in the poorest and most remote areas, raising major problems for reaching the most marginalised under the SDGs.

There is nevertheless a tendency to look to the private sector to fill WASH coverage gaps, which is likely to intensify with greater pressure on public sector resources post-2015. Yet the world must not lose focus on the need for a huge scale-up of public funding – both government spending and aid –given the types of risks and problems privatisation and private funding can cause, especially for meeting the needs of the poorest and most marginalised.[9]

3. Data and information issues

3.1 Tracking WASH spending is becoming more complex

All our country studies struggled to access comprehensive information, with differing degrees and explanations for problems. Given that the countries were chosen for their relatively high availability of data on absorption, this highlighted a key set of lessons, especially for less transparent countries.

One important reason – backed by broader GSW analysis – is lack of uniformity in how governments organise the WASH sector institutionally. Water, sanitation and hygiene activities are often located across two or more institutions, and in multiple different agencies for rural and urban services. In addition, WASH spending is often

located within ministries that deal with broader issues (water in infrastructure, and sanitation in health). These factors can make identifying absorption levels difficult, especially because governments often break down planned budgets in ways that identify WASH, but do not repeat this disaggregation for actual spend. 'Water spending' may also cover many non-MDG related activities such as waste water management, dams and infrastructure projects for industrial water or energy, rather than providing clean water and sanitation to the poor.
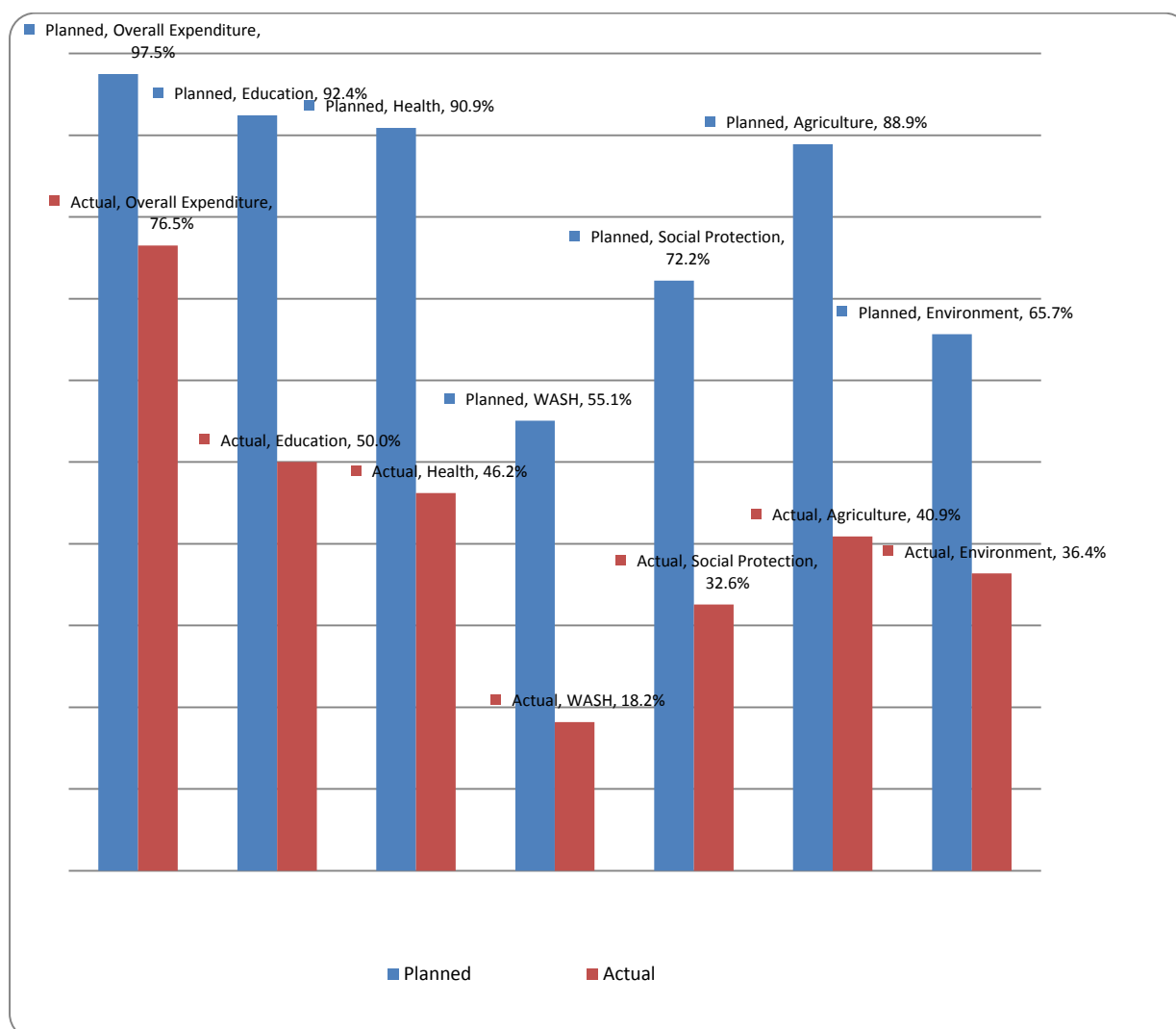
This was a problem in all the country studies, hampering analysis. In Ethiopia, WASH is implemented mainly by the Ministry of Water and Energy, making disaggregating actual water spending hard. Meanwhile, sanitation is spread across the Ministries of Health and Education, with the Ministry of Water, Irrigation and Energy coordinating at Federal level. In Mozambique, WASH is in the Ministry of Public Works and Housing (MOPH). In Rwanda it sits in the Ministry of Infrastructure (MININFRA), while the Ministry of Health has a role in sanitation. In Uganda, WASH sits within the Ministry of Water and Environment. Country authors managed to separate out water spending at national level. However, data disaggregation proved most challenging in the district/local level analysis: and this could worsen in future as decentralisation accelerates and if delivery is switched to state-owned enterprises (e.g. water and sewerage corporations), or private corporations through PPPs.

3.2 Disaggregating spending on sanitation is a top priority for action

Spending on sanitation is even more difficult to disaggregate (especially if it occurs in non-WASH ministries such as education and health). This was a problem flagged in Uganda, South Africa and Ethiopia. GSW has found that across 124 countries, disaggregating spending on sanitation is almost impossible, at least in part because governments do not have specific plans and budgets to improve sanitation. This was why the African eThekwini conference in 2008 committed to separating out budget lines for sanitation and hygiene to improve tracking (as well as to higher spending on sanitation), but there is virtually no evidence of progress, even in the best performers – Rwanda and South Africa.

3.3 Overall actual spending data availability for WASH

It is these issues that make WASH the sector with the lowest data availability in the GSW 2015 database (see Figure 1): only 18% of 67 countries have full information on actual spending on WASH.

Figure 1: Availability of data by sector, 2012/14 planned and actual

Figure 1: Availability of data by sector, 2012/14 planned and actual
- Planned, Overall Expenditure, 97.5%
- Planned, Education, 92.4%
- Planned, Health, 90.9%
- Planned, Agriculture, 88.9%
- Actual, Overall Expenditure, 76.5%
- Planned, Social Protection, 72.2%
- Planned, Environment, 65.7%
- Planned, WASH, 55.1%
- Actual, Education, 50.0%
- Actual, Health, 46.2%
- Actual, Agriculture, 40.9%
- Actual, Environment, 36.4%
- Actual, Social Protection, 32.6%
- Actual, WASH, 18.2%
- Planned
- Actual

4. Recommendations

In the post-2015 framework, WASH will grow dramatically as the global goals are made more ambitious, to provide access to WASH for all (which implies higher costs to reach marginalised groups, especially in informal settlements and urban slums), and ensure sustainable water management given increasing water scarcity. There can be no doubt that, overall, vastly more investments are required for the sector.[10] According to the Sustainable Development Solutions Network (2014), World Health Organization (2012) and UNCTAD (2014), between $22 and 30 billion extra will be required annually to ensure universal access to safe drinking water and adequate sanitation during 2015-30, with sanitation accounting for the vast majority of these investment needs.[11]

As spending needs increase dramatically, absorption constraints could become even more serious unless the problems raised in this report are tackled. The main

recommendations to achieve this (in order of urgency based on the scale of delay they cause) are:

1. Donors must work with governments to improve absorption of their funds, including:

- Moving from small projects to multi-donor sector programmes and budget support coordinated by governments, to cut waste and transaction costs for institutions managing WASH spending.
- Rebalancing their (donor) projects and programmes to provide more recurrent funding (including through budget support).
- Using government procurement and financial management systems, which work more rapidly.
- Accelerating disbursements using donor procedures by setting maximum deadlines for all stages of financial management and procurement, and raising thresholds for competitive bidding.
- Ensuring timely flows of information to government institutions on commitments, procurements and disbursements, so as to make compliance with procedures simpler.
- Encouraging increased spending on financial and procurement management capacity, especially at decentralised and State-Owned Enterprise level, to ensure these agencies process funds rapidly.

2. Donors and governments must provide higher amounts of recurrent funding, by:

- Donors allocating a higher share of their funding to recurrent support, through sector programmatic or budget support.
- Governments and donors increasing allocations for staffing in planning, maintenance and inspection functions.
- Governments increasing wage levels for these staff, especially in remote or poorer regions.

3. Governments and donors must work together to improve capacity, by:

- Improving weak human resource capacity and skills at different stages of the delivery chain (planning, engineering, management and monitoring of implementation, maintenance and inspection) – which is in turn dependent on higher recurrent spending.
- Paying particular attention to increasing capacity in decentralised (especially in poorer regions) and privatised agencies, and in private contractors to plan, budget and implement on schedule.
- Examining closely the potential impact of decentralisation and privatisation on capacity across the sector resulting from duplication of functions, and wage distortions.

4. Governments must improve their own procedures to accelerate absorption, by:

- Accelerating procurement and contracting procedures and information flows among agencies, by improving institutional structures, and clarifying roles and responsibilities across the chain.
- Scrutinising private company cost estimates more closely to avoid overruns.
- Accelerating funds releases from central government to decentralised or private actors.
- Establishing contingency reserves in budget allocations to offset revenue shortfalls and avoid in-year spending cuts.

5. Governments and donors must maximise opportunities and minimise risks of decentralisation and privatisation, by:

- Ensuring that all decentralised and private agencies have high levels of capacity.
- Making all agencies more transparent and accountable to citizens for service delivery.
- Designing contracts with private entities carefully to ensure that costs are minimised, access of the poorest is maintained, and risks are fully shared between government and private sector.
- Continuing to focus on public sector funding and implementation of programmes designed to expand access to WASH, to increase equity and universal coverage in the 2030 Agenda for Sustainable Development.

6. All parties must improve transparency and accountability of spending data on WASH, by:

- Governments and international organisations collaborating on a capacity-building programme to make WASH spending more identifiable and easier to track across all government budgets.
- Clearly separating out water from other infrastructure; sanitation and hygiene from health; and the different types of 'water' spending ('expanding access to WASH', 'water infrastructure', and 'water sustainability/conservation').
- Separating sanitation and hygiene spending from broader water spending, in order to accelerate progress in this sector, for which the MDG target has been missed by such a wide margin.
- Improving availability of actual spending data by applying these same classifications to mid-year and end-year budget implementation reports, and by accelerating the verification and auditing of sector spending reports.
- Investing in monitoring and tracking spending in decentralised and private agencies.
- Ensuring that the same standards of transparency, reporting and accountability apply to private agencies, PPP contracts and state-owned enterprises as to central government agencies.

7. Conducting further analytical work to improve absorption post-2015

In conducting this work, several key areas emerged for further analysis:

- An 'equity-based' analysis of allocation and absorption, examining urban-rural and poverty-related issues. Some studies (Mozambique, South Africa) pointed to much lower absorption in rural and poorer areas, which requires more analysis to overcome post-2015 constraints.
- Conducting more work to understand the enabling factors driving positive outcomes (the Terms of Reference of the current study perhaps focussed excessively on identifying problems and barriers).
- In-depth work in a number of districts to understand local-level barriers to absorption in more detail (funding levels for the current study did not allow widespread district visits/interviews).

8. Applying similar lessons to other countries

Finally, it is important to remember that these countries were chosen as positive examples, because they have resolved most problems of central government-funded absorption, but continue to face problems in donor-funded absorption, and are now potentially facing growing problems around decentralised spending. The analysis of their experiences therefore reinforces messages from other reports and in other sectors that 'leaving no one behind' in a context of growing decentralisation, will require even greater investments in planning, management and engineering capacity.

However, as pointed out in earlier DFI reports to WaterAid (and the GSW 2013 and 2015 reports), most other countries are still facing much bigger, first-order problems in absorbing centralised spend, and especially donor-funded spend given their higher donor dependence. To improve performance in countries that have made less progress towards the MDGs, each country needs a comprehensive diagnosis across the same range of problems discussed above. They (especially fragile/conflict-affected and least developed countries) are likely to need more support with government procedures and capacity, but the most important solutions are likely to remain the same in all countries – especially donors providing more sector recurrent/budget support, using country systems, reducing fragmentation and improving their own procedures.

Endnotes

[1] This overall report was written by Jo Walker and Matthew Martin. The country case studies were written by Girma Aboma (Ethiopia), Manuel Lobo (Mozambique), Eugene Dusingizumuremyi (Rwanda), Len Verwey (South Africa), and Imelda Namagga (Uganda).

[2] Government Spending Watch is a programme by Development Finance International, which tracks budget allocation and actual spend in seven sectors across 67 low- and middle-income countries. This includes tracking on the WASH sector (as well as education, health, social protection, agriculture, gender and environment). From these 67 country budget trends there are some clear trends in WASH which we have identified. For more on this see pages 27-28 of the *Government*

Spending Watch 2015 report, available at http://www.governmentspendingwatch.org/news/110-financing-the-sustainable-development-goals-lessons-from-government-spending-on-the-mdgs.

[3] For more information on WASH specific findings see http://www.governmentspendingwatch.org/research-analysis/water-and-sanitation.

[4] For instance, the *UN Water Global Analysis and Assessment of Sanitation and Drinking-Water GLAAS 2014 Report* identifies strong leadership, coordination and implementation as key for both countries in their report. *See WHO 2014 UN-water global analysis and assessment of sanitation and drinking-water (GLAAS) 2014 report: investing in water and sanitation: increasing access, reducing inequalities.*

[5] A WaterAid country programme was also an important factor, though South Africa was included to provide comparative lessons for the southern African region.

[6] This confirms the findings of the *UN Water Global Analysis and Assessment of Sanitation and Drinking-Water GLAAS 2014 Report* which identifies strong leadership as crucial to successful attainment of the MDGs.

[7] There is a tiny amount of donor financing in South Africa's WASH sector but it is not significant enough to impact on trends.

[8] This is in line with budgetary practice across the world, largely because donors do not report to governments on breakdowns between capital investment and recurrent spending transactions within projects.

[9] UNCTAD (2014) report suggests that a maximum of 20% of WASH funding post-2015 could come from the private sector; SDSN (2014) suggests that this is more likely to be 10% given the lower profitability of expanding access to the most marginalised

[10] WaterAid 2013, WHO and UN Water 2012, World Bank 2011.

[11] SDSN (2014) suggests a range of needs from $22-24 billion a year. WHO (2012) estimates a total need of $535 billion to be spread out over 20 years. UNCTAD (2014) projects a much higher investment gap for access to water and sanitation of some $260 billion a year, but this appears to include a lot of investment in large-scale water infrastructure, such as dams.