SUMMARY REPORT

The Need for Long-Term Investments in the Water Sector

How to ensure high quality water services to future generations

28 April 2016
European Parliament, Brussels

Policy-makers and stakeholders were brought together by MEP Michel Dantin and MEP Dominique Riquet to discuss alongside representatives working in the domain of water the importance of ensuring long-term investments in the sector.

Dominique Riquet MEP and President of the Long-Term Investment and Reindustrialisation Intergroup underlined that water is a rare good and crucial for humankind. The various usage of water was highlighted stressing that both the global population and individual consumption continue to increase. It was said that different investments are needed such as infrastructure, research and development, which are justified firstly by the need to ensure access to this essential raw material. The importance of the water cycle was mentioned also underlining that investments are needed in order to ensure the continuation of for example agriculture. With regards to this it was said that much can be done in terms of technology and irrigaton also emphasising that the industry is an important investor. It was said that for citizen's it is essential to invest in networks providing fresh and drinkable water particularly mentioning the issue of leakage and the importance of progressing on such issues in cities. It was reiterated that investments are needed due to population growth stating that there is a big divergence between the consumption of water and the ratio used per person drastically varying throughout the world. It is also a geopolitical factor with water stress becoming an issue of security. It was said that water should not be seen as a free resource and due to its scarcity it is becoming more and more expensive calling water the oil of the 21st century.

Jan Busstra, Water Director, Dutch Presidency of the European Council highlighted that there are three action levels for investing in the water sector. It was underlined that at national level water is an essential resource, but particularly in the Netherlands it can also be a threat. It was explained that due to climate change a proactive approach has been taken with the development of the Delta Programme. It was explained that this programme provides the Netherlands with analysis of where the risks could take place with regards to water safety and water availability. The Delta approach provided input, which led to a national investment agenda. It was underlined that a key part of the success of such an agenda is the support provided by the different levels of government as well as the private sector and civil society. It was stressed that when elaborating on such an agenda the transboundary perspective must be taken into account. With regards to this level of action the importance of river basin management cooperation was stressed with attempts to make investment programmes in line with programmes upstream in other Member States. It was said that the impact on EU water legislation is of great importance mentioning that the REFIT programme and Horizon 2020 are good tools to provide further detail on how adjustments can be made. With regards to investments the EU Fund for Structural Investments and funds within the CAP are of great importance, and are used in the Netherlands to improve investments in water in the agricultural sector. It was stated that at the global level the adoption of the Sustaianble Development Goals further enhance the importance of tackling climate change and necessary actions to improve water availability. Further, the international financial institutions are becoming more aware of these global issues and more funding is becoming available for prevention. There is also an opportunity for individual states to act. It was said that the need to increase cross-border partnerships are needed such as the Delta Coalition that aims to make delta cities resilient. Further, the Green Climate Fund could be an important future tool.

Thomas van Gilst, Head of Water Management Division, European Investment Bank highlighted that the EIB is one of the largest lenders to the water sector allocating about four billion Euro per year to the sector. It was explained that the physical life of assets of water is long and that this requires long-term investments stressing that if the asset life can be matched with the maturity of the loan then the tariffs or charges to be paid will be lower ensure intergenerational equity. Long-term lending is in short supply, and often only available through large public or development Banks. The average EIB loan tenors in 2015 to the sector is long at 23 years on average and goes well beyod in exceptional circumstances if the useful economic life justifies this. Indeed a key criterion at EIB to justify loan duration is the Economic life. This can be shorter than expected physical life in the case of regulatory or market shifts, technical obsolescence, or poor maintenance standards, potentially causing an inability of the asset to generate the benefits justifying the loan repayment. It was poined out that the public regulators play an important role in ensuring that the factors determining the economic life keep it as close as possible to the expected physical life, in particular predictable regulation, and proper maintenance. This also ensures that more lenders or indeed investors are attracted to the sector. With regards to sources of funding it was said that grants are extremely scarce as well as equity also entailing demands on high returns. It was outlined that debts are abundant but not always for the needed tenors. He said that for EIB, the EFSI guarantee would allow for certain projects with a higher risk profile to nonetheless benefit from more attractive terms. This was the case for the recently approved Irish Water loan in a country with no track record of water regulation. In conclusion it was said that governments have an important role to play in ensuring proper regulation of the sector so as to allow long-term investments with lower consumer tariffs.

Matjaž Malgaj, Head of Unit "*Marine Environment and Water Industry*", DG Environment, European Commission outlined that the legal and policy framework in the EU is long in its standing and pretty comprehensive. It was stressed that the issues that are most relevant for the sector and investment needs must be seen in this holistic framework. It was also said that interaction is crucial in order to secure sufficient supply while protecting the environment. It was stated that the legal framework has led to a strong water industry in Europe, which is well placed to offer their services and provide solutions in international markets. It was said that when looking at investment needs there are various categories to be examined. He explained that the needs could be classified in three categories. First and most known is large urban infrastructure, which is essential to allow for access. Second are investments in securing water quality and quantity supply; these include green infrastructures to prevent flooding and water retention and increased efficiency in industry and agriculture. Last but not least are investments in innovation, which in turn makes investment in previous categories more efficient and cheaper. Although the latter is sometimes more risky than in some other sectors, investments in innovation have therefore great long-term return potential. It is important to see this in the context of fully applying other instruments, such as the Nitrates Directive and Industrial Emissions Directive, which would reduce some of most relevant pressures and by make it easier and cheaper to manage water systems and supplies. There is no complete systematic overview across the three categories but data provided by Member States and companies provide some insights of what is needed. For example information reported under the Urban Waste Water Treatment Directive demonstrate high needs in Member States concerning investments in new and renewal of existing infrastructure and suggest that investmenst are alerdy planned in the EU 28 of between €22 and €25 billion per year. The issue of renewal was especially highlighted as it involves a hidden cost which must be made more transparent. It was said that all levels play an important role here and the EU recognises the need to ensure that instruments are available. It was also stressed that it is pivotal to apply cost recovery so that sectors and consumers are using and pay for that usage. This will increase efficeny and can be done by fully taking into account the need to protect vulnerable groups. EU structural funds and EFSI were pointed out as helpful tools and the need for capacity building in some Member States recognized. Improved governance and administrative cooperation between all levels, which were already mentioned buy some previous speakers, will play an important role delivering the results needed.

Xavier Leflaive, Water Team leader, OECD Environment Directorate emphasised that investing in water is a development issue and also contributes to sustainable growth. Investing in water storage or other water-related infrastrucuture in particular is crucial to compensate for variations in water availability and ensure reliable flow. It was said however that not all investments are equally beneficial. The most benefitial investments combine investments in infrastructure, institutions and research. They are properly sequenced investments. Investment sequences must be designed in a strategic way and must be adaptable for future changes and shifting priorities. In order to make such investments happen, more work is needed to ensure best use of available resources, allocate risks and rewards, and make investments in other sectors (e.g.urban development, agriculture, and energy) water-wise. The investment needs must be minimised, essentially by avoiding building future liabilities, by tapping alternative water sources, and exploiting the potential benefits of green infrastructures. In addition, best use should be made of available finance, through asset management (it is most often easier to finance a new wastewater treatment plant rather than putting money into maintenance and renewal), well-designed tariff structures, and combining the 3Ts (Taxes, revenues from Tariffs, and Tranfers from the international community). It was explained that the 3Ts are the ultimate sources of finance for water and sanitation services, as other sources of finance (such as loans and equity) have to be repaid by a combination of the 3Ts. It was also explained that in order to make investments materialise, risks and returns need to be allocated in an appropriate manner. Financers tend to believe that the risks are too high in the water sector and the returns are too low. Therefore, policy-makers should consider how to allocate risks and returns so that water investments are made attractive to financers. There is no shortage of savings or money globally to cover water-related investments but rather a gap on making this money available. . It was concluded by reflecting on how to select projects that contribute to sustainable growth and how to ensure that investments in such sectors as urban development or energy contribute to water security and sustainable growth.

Pierre Menet, **Advisor within the Department for Institutional, International and European Relations of Caisse des Dépôts** underlined the need for a framework favoring long-term investments in the water sector. It was explained that investments in the water sector in France are considerable and still represent €6.5 billion in total per year. It was also said that 70% of investment costs for the water budget are allocated to the water networks. It was stressed that public operators are the biggest investors concerning sanitation and drinking water. Further, it was said that the sector is essential for both indirect and direct job creation. With regards to investments it was recommended to invest in either debt and/or equity on territorial projects. Moreover it was explained that Caisse des Dépôts look for significant additionality of new assets to be financed. It was explained that they act for the general interest and aim to operate as market economy investor. It was said that one relevant additionality criteria is the risk of renewal providing the example of water pipes. It was underlined that even though additionality criteria are taken into account, an appropriate risk approach cobined with a long view is recommended when consideringa project. It was stressed that close attention is given to the risks and their clear allocation among the investors, the industrial sponsor and the public contracting authority. It was emphasised that this allocation will allow for a long-term commitment of investors and more efficient financing schemes. It was also said that it is important to know how to distribute the risks as it will have an impact on the global cost. It was said that this is essential as it can make a huge difference given the (very) long term maturity of the funds to be committed in terms of Net Present Value. It must also be recognised that the various players are bearing different levels and nature ofrisks. It was concluded by stressing the importance of the Euroepan Fund for Strategic Investments (EFSI) stressing that long term investment challenges in the water sector are aligned with the additionality criteria requested by the Juncker Plan. Further, it was said that the Plan is particularly appropriate for small and medium sized projects as they can be pooled and finance through Investments Platforms enhanced by EFSI.

The debate with the audience highlighted the need for smart investments in e.g. high efficient technologies, which help reduce greenhouse gas emissions. The importance of grey and green infrastructure was also raised as they play an essential part in climate mitigation and adaptation. The need to reduce harmful substances was also mentioned. The case of Ireland was highlighted emphasising the need for certainty and how to fund or not fund investments in water also asking who should sit on national water boards and commissions. In response to this it was said that it is a political issue that needs the support of the public. The trade offs or balance between tariffs, transfers, and taxes will remain political and it is crucial to ensure that they are well informed. With regards to water boards not one model can be replicated, but it is important that the public is represented as well as people who understand the finances behind the issue. It was also pointed out that involvement of the private sector and NGOs is crucial. It was said that the price of water was previsouly highly debated in France and it was underlined that it is important for citizens to understand what the costs represent and that it is the infrastucture they are paying for, not the water itself. The need to better consider public–private partnerships was raised calling for a regulatory framework, which is well adapted to public tenders. Support was also reiterated to ensure that rewards are correctly calculated within the investment. The issue of desalination plants was raised underlining that the process is becoming more efficient asking whether it would be considered in future water production. In response to this it was outlined that it is an energy intensive industry and that focus is firstmost on tackling overuse and leakage as well as encouraging better management. It was reiterated that a strong regulatory framework can stimulate innovation and promote investments. The use of best available technology was also stressed. The potential of market failures and risk allocation were underlined mentioning that one reason for this is because of its monopoly regime. It was however said that the water market is not necessarily a monopoly with new developments bringing about competition. Water as a tradeable commodition was also mentioned with the panellists agreeing that there is at the moment no political support moving water in that direction. The main emphasis is to see water as a common good. It was also said that tradeable water rights exist in some countries at the local level. With regards to risk allocation it was said market investors will not be enough to absorb long-term risk schemes and the need to standardise risks is will lower the level of source risks. The need for international investors was also raised pointing out that the regulatory framework in the US is easier for investors to understand and the need to standardise risks is important in order to attract investors.

Michel Dantin MEP and Chair of the "*Agriculture and Water Management*" Working Group of the EP Intergroup on "*Climate Change, Biodiversity, and Sustainable Development*" concluded the meeting by reiterating the need for long-term investments in the water sector. It was said that linking current EU water legislation is of utmost importance to ensure that investments are made at the relevant scale and context. It was also said that the EU and Member States must reflect on the geographical distribution of water and the importance of governance bodies was mentioned. The role of wetlands was also raised stressing that they represent great reserves and help mitigate climate change. Furhter, as climate change continoues to exasberate extreme weather a global vision is needed. A solid regulatory framework is essential but it must also be aligned with the amount of investments needed. It was said that financial opportunities must be seized underlining the importance of local engineering to find solutions for investments to provide good return. Furhter, it was reiterated that all actors must collaborate as water is foremost an issue for the territories.