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DEVELOPMENT DISAGREEMENTS AND WATER PRIVATIZATION: BRIDGING THE DIVIDE

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Development Disagreements and Water Privatization:
Bridging the Divide

By

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Abstract

While trade liberalization was perhaps the archetype disagreement on development strategy in the 1980s and 1990s, in the 1990s and 2000s this role has been taken over by water privatization and the passions it arouses. What are the underlying reasons for disagreements on water, among those who proclaim to be for poverty reduction? This paper tries to understand the nature of the disagreements, and ascribes them to a combination of interpretation of the empirical evidence and, more importantly, differences in world view on how to assess what constitute good development outcomes, and on how to achieve them. It is suggested that the way forward lies in a clear understanding of the basis of disagreements, from which, perhaps, a new consensus can be fashioned on water privatization.

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1. Introduction: Development Disagreements

While some held the hope that the fall of the Berlin Wall would also lead to a new consensus on development strategies, things do not seem to have turned out that way. Sure, the fall of the wall also signaled the demise of full blown central planning as a serious development strategy. The converse of full blown market capitalism was, for a while, seen as the only viable alternative. Such was though to be the powerful message of 1989 that Fukuyama's phrase "the end of history" came to signify the start of a new beginning, with all past assumptions and experiences having to be reconsidered—in the economic as well as the political realm. But the reality of the last two decades has been messier than that. Leave to one side the politics. The full blown market based development strategies implemented in the 1980s and 1990s, in Africa and Latin America, cannot be said to have had the beneficial impact that was predicted for them. Growth did not recover. Poverty in Africa increased. Eastern Europe had an economic and social catastrophe. Asia had the notable success stories of China and India, but these cannot have been said to have been following the converse of central planning. And in Asia and throughout the world, capital flows liberalization, a tenet of the post Berlin Wall euphoria, led to the crisis of 1997.

Time moves on and passions dissipate. This certainly seems to have happened to some extent on the trade and capital flows front, where a weary consensus of caution has replaced the vehement discord of the 1990s and early 2000s. Partly as a result of the acceptance of facts on the ground by both sides, the "liberalize cautiously" mantra has provided a formula for discussion of country specificities and speed and sequencing.[1] The financial crisis of 1997 finally dented the proselytizing of those hell bent on this dimension of liberalization. The political realities of job losses in the North came to exert pressure on free trade agreements. And the short run costs of trade liberalization came much more into the policy-analytical discourse. At the same time, despite debates on nuances and precise interpretations of outcomes, it would be a strange sort of world view that would deny the importance of the "opening up" of China and India to trade and investment (while maintaining control over capital flows) to the upsurge of growth in those countries in the last two decades. Further, while inequality has undoubtedly increased in these countries, and growth could have been more pro-poor by a far greater margin, it would be a blinkered perspective to say that this growth has had no effect on poverty reduction in those countries.

In an area such as trade, then, cautious pragmatism has to some extent replaced the ideologies of yesteryear. But in the area of water privatization, passions are still raw, and the intellectual dispute leaves a bitter taste. Those advocating such privatization, however cautiously, are accused of putting profit before lives, of selling the national patrimony to multinationals, of bringing the market into the buying a selling of a human right. There are, no doubt, those who are motivated purely by profit. But on the other side are those, equally concerned about the poor, who argue that the current state run system is failing the most vulnerable, and who see privatization as a way of breaking the grip of political elites on heavily subsidized water—for their big farms and their swimming pools.

[1] There is a huge literature, but here are some recent examples: Rodrik (2001), Kanbur2001), Winters, McCulloch and McKay (2004), World Bank (2006a), and Kose et. Al. (2006)

Can the divide on water privatization be bridged? I think a first step is to understand the precise nature of the disagreements. Are they amenable to empirical resolution and if so, how? To what extent do they reflect unresolved methodological or philosophical divides which will have to be addressed in order to move forward? And what might be a practical process, at least for analysts, of attempting to resolve the differences? These are the questions to which this paper is addressed. Section 2 lays out the broad contours of the "water wars". Section 3 undertakes the task of understanding these disagreements, in the broader context of disagreements on development strategies more generally. Section 4 discusses the way forward and concludes.

2. The Water Wars

There is by now a huge literature on water privatization. The term "water wars" referred originally to the famous protests in Cochabamba, Bolivia, in 2000, when the government sold the municipal water supply of that city to an international water company. There have been other water wars of this type, with tragic loss of life. The street battles have been reflected in water wars of another type, among policy analysts, between those broadly supportive of water privatization and those opposed. This literature has ranged from the prosaic and academic to the populist and polemical. Much of the debate has taken place on the web. I want to pick out two recent contributions to represent the alternative perspectives that I will examine in depth—Shiva (2005) and Segerfeldt (2005a). I pick these not only because they are by prominent protagonists, but because they present the positions cogently and intelligently, even though they do so in somewhat polemical vein.[2]

Vandana Shiva (2005) provides a recent, trenchant, account of the water wars from the Indian perspective, and is worth quoting extensively and reading carefully:

"On 13th June 2005, 5 farmers were shot dead in Tonk during a protest demanding their share in the water from Bisalpur dam, which is diverting water from villages to the city of Jaipur under an ADB project for water sector "reforms" in the State of Rajasthan currently ruled by a BJP government….Yet the Congress government in Delhi is determined to create another Tonk in Muradnagar, with its demand to divert 635 million litres of Ganga water per day to the Sonia Vihar Plant, which has been privatized to Ondeo Degrement a subsidiary of Suez…..The real politics of water is not Congress vs. BJP. It is World Bank/ADB and other aid agencies creating water markets for global water MNCs while robbing the Indian people both hydrologically and financially….[T]he World Bank started to push the Delhi government to privatize Delhi's water supply….The contract between Delhi Jal Board….and the French company Ondeo Degrement (subsidiary of Suez Lyonnaise des Eaux Water Division—the water giant of the world), is supposed to provide safe drinking water for the city….On December 1, 2004, water tariffs were increased in Delhi. While the government stated this was necessary for recovering costs of operation

[2] Some other contributions (a very small selection) from the web are Obando (2003), Public Citizen (2003), Barlow and Clarke (2004) on one side, and Moore (2003), Bailey (2005), and Galiani, Gertler and Shargrodsky (2002), on the other.

and maintenance, the tariff increase is more than ten times what is needed to run Delhi's water supply. The increase is to lay the ground for the privatization of Delhi's water, and ensure super profits for the private operators….The tariff increase is not a democratic decision, nor a need based decision. It has been imposed by the World Bank. The Delhi Jal Board cites the justification for increase in tariff as based on a study done by Price Waterhouse Cooper under the World Bank study on privatization….The tariff increase hides significant increases through changes in categories….”Piaos”, a core part of India's culture of the gift of water, must also now pay for water. How will they give water to the thirsty? Cremation grounds, temples, homes for the disabled, orphanages which paid Rs. 30 will now pay thousands of rupees ….The World Bank driven policies explicitly state that there needs to be a shift from the social perception to a commercial operation. This worldview conflict lies at the root of conflicts between water privatization and water democracy. Will water be viewed and treated as a commodity, or will it be viewed and treated as the very basis of life?....The common argument for privatization and price increase is that higher costs will reduce water use. However, given extreme income inequities, a tariff increase that can destroy a slum dweller or poor farmer is an insignificant expenditure for the rich. Privatization as dictated by ADB and he World Bank thus means that water will be diverted from the poor to the rich, from rural areas to urban/industrialized areas…..The government's priority for commodification and privatization of water was clearly stated by the Planning Commission Deputy Chairman, Montek Singh Ahluwalia….While Mr. Ahluwalia argued that rich farmers are the real beneficiaries of free water, it is the rich who can afford to pay. The poor peasant, already struggling under the burden of debt, driven to suicide, will be wiped out if she/he is denied access to water and made to pay for a resources that is their common property….The Deputy Chairman stated that “chasing short term benefits that accrue from vote bank politics, instead of seeking long term gains that flow from prudent economic policies, has become the bane of our decision-making process.”….What Mr. Ahluwalia is calling “short term benefits that accrue from vote bank politics” others call democracy. What he refers to as “prudent economic policies” are the World Bank/IMF/ADB paradigm of water privatization which has already led to the killing of farmers in Tonk and could leads to many more water wars….Water is a commons, a public good. Privatization is the enclosure of the water commons. Water privatization aggravates the water crisis because it rewards the waste of the affluent, not the conservation of resource prudent communities. Sustainable and equitable use needs water democracy, not water privatization.”

The alternative perspective I want to examine is provided by Segerfeldt (2005a)[3], which is also worth quoting extensively and reading carefully:

“Ninety-seven percent of all water distribution in poor countries is managed by the public sector, which is largely responsible for more than a billion people being without water. Some governments of impoverished nations have turned to business for help, usually with good results. In poor countries with private investments in the water sector, more people have access to water than in those without such investments. Moreover, there are many examples of local businesses improving water distribution. Superior competence, better incentives and better access to capital for investment have allowed private

[3] This is an op-ed piece based on a volume, Segerfeldt (2005b).

distributors to enhance both the quality of the water and the scope of its distribution. Millions of people who lacked water mains within reach are now getting clean and safe water delivered within a conventional distance….The main argument of the anti-privatization movement is that privatization increases prices, making water unaffordable for millions of poor people. In some cases it does, in others not. But the price of water for those already connected to a mains network should not be the immediate concern. Instead, we should focus on those who lack access to mains water; usually the poorest in poor countries….They usually purchase water from small-time vendors, paying an average of 12 times more than for water from regular mains, and often more than that. When the price of water for those already connected goes up, the distributor gets both the resources to enlarge the network and the incentives to reach as many new customers as possible. When prices are too low to cover the costs of laying new pipes, each new customer entails a loss rather than a profit, which makes the distributor unwilling to extend the network. Therefore, even a doubling of the price of mains water could actually give poor people access to cheaper water than before….True, many privatizations have been troublesome. Proper supervision has been missing. Regulatory bodies charged with enforcing contracts have been non-existent, incompetent or too weak. Contracts have been badly designed and bidding processes sloppy. But these mistakes do not make strong arguments against privatizations as such, but against bad privatizations. Let us, therefore, have a discussion on how to make them better, instead of rejecting them altogether. Greater scope for businesses and the market has already saved many lives in Chile and Argentina, in Cambodia and the Philippines, in Guinea and Gabon. There are millions more to be saved."

I believe that most if not all of the main points in the water privatization discourse are encapsulated in these two quotes, from two well known sources on the two sides of the debate. We would do well to study these to identify the nature of the disagreements as a starting point in the process to see if a reconciliation is possible and, if so, how to get it. The next section begins the task of understanding the disagreements.

3. Understanding Disagreements

Let us try to enumerate the disagreements on water privatization as evidenced in Shiva (2005) and Segerfeldt (2005a). We should note at the outset that as actually implemented, "privatization" is of many types—this is implicitly if not explicitly acknowledged in the two quotes. But the central thrust is clear. It is to move from primary state control in the provision of water services to a greater role for private investors, market pricing, and the profit motive. Given this broad definition, how can people with same objectives, of helping the poor and reducing poverty, differ so much? It is useful to consider the disagreements under two broad headings—consequentialist and deontological. In a consequentialist based argument, the only thing that matters are outcomes and their evaluation. The evaluations can be empirical, looking at actual outcomes, or theoretical, looking at outcomes predicted by a particular form of reasoning (a model of the world). Disagreements can arise on the value judgments used in the evaluation of outcomes, on the actual outcomes (in the empirical frame), or on the model (in the theoretical frame). In the extreme form of a deontological argument, consequences are beside the point. What matters is an assessment of the process, and disagreements can arise over different frameworks for such an assessment. Let us take each of these categories in turn.

In earlier work, I tried to understand the nature of disagreements on broad macroeconomic policy, distribution and poverty in a consequentialist mode (Kanbur, 2001a). I set to one side differences in objectives--how outcomes are evaluated--and concentrated on disagreements linking policies and outcomes. I asked the question—how can people with the same objectives differ so much about policy when they have the same objectives and, to a large extent, the same data? I argued that the answer lay in different perspectives that people bring to the discussion, along three dimensions—aggregation, time horizon and market power. Dividing the main protagonists into two for simplicity and clarity, I characterized one as the "Civil Society tendency" (CS) and the other as the "Finance Ministry tendency" (FM). I suggested that the latter has a world view that is more aggregated, with a longer time horizon, and a tendency to ascribe competitive structure to markets.

On aggregation, the CS world view is more "worm's eye" than "bird's eye". Thus, for example, national level poverty statistics will be deployed by FM, and these will naturally aggregate gainers and losers. On the other hand, CS will focus on the losers, especially the poorest losers. It is cold comfort for a poor person who has been made poorer because of a policy, to be told that other people, even other poor people, have been made worse off.[4] On time horizon, the CS view worries more about the immediate negative impacts of a policy on the poor as opposed to the FM perspective that often emphasize the medium term benefits, for poverty, of the same policy. Trade liberalization is a classic case, where the short term costs on those displaced have to be set against the longer term benefits from greater openness. Publications like World Bank (2006a) have eventually conceded the importance of the former in the poverty debate, and the discussion has shifted much more to compensation and safety net mechanisms, as compared to the trade liberalization mantras of the 1980s and 1990s. Finally, on market structure, the CS perspective sees market (and political) power everywhere it turns, whereas the basic economic models that underpin the FM analysis are competitive in nature. As argued in Kanbur (2001), this is another dimension explaining the benign (or supportive) and cautious (or opposing) stances taken by the two sides on major issues of economic policy reform. With a non-competitive market structure, the argument that benefits of policy reform are likely to be appropriated by a powerful elite hold greater sway.

I believe that the above framework for understanding disagreements in the consequentialist mode is a useful one to apply to the water privatization debate. For a start, the CS/FM divide is clearly seen in the debate set up by Vandana Shiva (2005) between herself and Montek Ahluwalia, the effective head of the Indian Planning Commission, and former Finance Secretary to the Government of India. More substantively, however, there is clearly a disagreement between her and Segerfeldt (2005a) on the actual outcomes of water privatization. For Segerfeldt (2005a), privatizations have come "usually with good results," despite problems in some cases. For Shiva (2005), it is quite the opposite. This is generally the case among many Civil Society organizations. Thus Public Citizen (2003), in

[4] I have developed this argument in greater detail in Kanbur (2005).

a report entitled "Water Privatization Fiascos," presents no fewer than five case studies from developing countries Argentina, Bolivia, The Philippines, Indonesia and South Africa) to illustrate the title of the publication. Yet Segerfeldt (2005a) argues that "the market has saved many lives in Chile and Argentina, in Cambodia and the Philippines, in Guinea and Gabon." It cannot escape notice that there is an overlap of countries in the two lists. How can it be that such opposite conclusions are drawn from the same experience?

To explore this issue, let us consider the specific case of Argentina, and compare the analysis of Public Citizen (2003) and Galiani, Gertler and Schargrodsky (2002). Here is how the latter summarize their conclusion, based on state of the art econometric analysis:

"In the 1990s Argentina embarked on one of the largest privatization campaigns in the world including the privatization of local water companies covering approximately 30 percent of the country's municipalities. Using the variation in ownership of water provision across time and space generated by the privatization process, we find that child mortality fell by 8 percent in the areas that privatized their water services; and that the effect was largest (26 percent) in the poorest areas. We check the robustness of these estimates using cause specific mortality. While privatization is associated with significant reductions in deaths from infectious and parasitic diseases, it is uncorrelated with deaths from causes unrelated to water conditions."

Public Citizen (2003) on the other hand says the following of the Buenos Aires privatization in 1993:

"During the first eight years of the contract, weak regulatory practices and contract renegotiations that eliminated corporate risk enabled the Suez subsidiary, Aguas Argentinas S.A., to earn a 19% profit rate on its average net worth….According to Fernando de la Rua….(speaking in March 1999 when he was Mayor of Buenos Aires): "Water rates, which Aguas Argentinas said would be reduced by 27% have actually risen 20%. These prices have increases, and the cost of service extension, have been borne by the urban poor. Non-payment for water and sanitation are as high as 30 percent, and service cutoffs are common with women and children bearing the brunt with health and safety consequences."

Two more opposing descriptions of outcomes could hardly be possible. According to one analysis, the privatization was an unmitigated disaster. According to another, it saved children's lives. And these are the views taken by the CS and FM tendencies. Can they be resolved? One possible route is to consider aggregation, time horizon and market structure. The impact effect of the price increases, emphasized by Public Citizen 92003) with the quote from de la Rua, would indeed have been to hurt all current users of water services—by definition. Some of these would have been poor households. But what of the longer term? If connections increased because of the increased profit, and if some of these connections were to poorer neighborhoods, then previously underserved poor households would have got clean water, and this could have led to reduced child deaths, as is claimed by Galiani et. Al. (2002). Both perspectives are in some sense right. The short term pain to poor households is highlighted by one. The greater long term gain to other poor households is highlighted by the other. There is no easy resolution between these two competing perspectives on evaluation. In addition, there is the market structure issue. There is a basic mistrust of non-competitive market structures, and a great fear that market power will increase once granted, among the CS tendency. The "natural monopoly" issue with water is well recognized by the FM tendency, who do say that regulation will be necessary as a result, but in general they seem to be more fearful of government failure than market failure. For the CS tendency, as seen in Shiva (2005) the answer is not in privatization combined by regulation, but in state ownership combined by democratic control. The counter to this, as in Segerfeldt (2005) is that as a matter of fact state ownership is failing the poor because of elite capture. Paradoxically, then, privatization, which is feared by CS as the route to concentration of power, is seen by FM as the route to breaking the power of the political elite who are diverting state services to their own end!

All of the above is in a consequentialist mode of thinking where the only thing that matters is the outcome. But there is another strand to CS critique of water privatization which is more deontological in nature. This is alluded to by Shiva (2005) when she talks about the cultural role that "gift of water" plays in India. A bolder statement is found in Obando (2003):

"Water is a fundamental and inalienable human right and a common good that every person and institution of this plane should protect. This resource is, like air, a heritage of humanity and must be declared that way. Water is not a merchandize and no person or institution should be allowed to get rich from the sale of it. It should not be privatized, marketed, exported or transferred to a few multinational companies, which today already control 90 percent of privatized utilities. For the GATT, NAFTA and FTAA, water is a commodity, an investment, a simple service for commercial use and profit."

Leaving to one side the concern about monopoly market structure, which has been discussed above, this perspective is fundamentally opposed to the buying and selling of water. This is difficult for economists with their "consequentialist gene" to comprehend. Why take such a position? Why not base the argument on the consequences of alternative arrangements—state, market, or in between? The answer can perhaps be found if we pose the following question. On this argument, why not leave the market for child sex to a consequentialist decision? Or the market for human slaves? Reflection on this will reveal that there are some commodities, the trading of which cannot be countenanced no matter what the consequences. Indeed, the consequences may be harmful, but that is not the point. The argument stops well before we get to those. At the very least the argument is at a different level.

I have addressed this issue in earlier work under the heading of "Obnoxious Markets" (Kanbur, 2004). Why and how exactly is the market for apples different from that for slaves? Somewhat paradoxically, I tried to understand this deontological question by examining consequences:

"Certain markets evoke popular discomfort, distrust and even outrage. Trade in arms,

drugs, toxic waste, child labor and body parts, for example, elicits these reactions to different
degrees. This paper asks—what is it about some markets that brings about these responses? It is argued that three key parameters—extremity, agency and inequality—have a bearing on our intuitive reactions and serve to differentiate markets. The more extreme are the likely outcomes of a market, the further is the agent who acts in the market from agents who bear the consequences of those actions, and the greater is the degree of inequality in market relations, the more likely it is that the operation of the market will provoke discomfort. At the extreme, when outcomes are potentially extreme, agency is minimal and market relations are highly unequal, the market in question may deserve the label "obnoxious".

Using these criteria, I then looked at a number of markets and concluded that "Each Obnoxious Market is Obnoxious in Its Own Way" (one of the section titles). I argued that markets for child prostitution or body parts were furthest along the spectrum to being "obnoxious", while those for soft drugs might not be quite so far along.

Where do water markets fit into the spectrum? Water transactions, or at least a lack of water, can lead to extreme consequences. In this, it is like transactions in toxic waste or body parts. In terms of agency, the market for child labor is problematic because it is not entirely clear that the agent making he decisions, the parent or the household, necessarily has the full interests of the child at heart. The agency issue, is not quite so sharp in the case of water, I believe. The inequality issue can be introduced by again considering child labor. Many economists chide opponents of child labor by saying that their actions actually make poor children worse off, since they cannot now bring in income and may be forced to worse forms of income earning (like child prostitution). But this is to miss the point of the visceral reaction against child labor. From this perspective it is not that child labor can earn income and therefore reduce poverty, it is rather a reaction against a state f the world where children have to work to relive their poverty. Translating into the water world, it is not so much that charging for water may in the long run lead to more investment and thus make poor people better off; it is rather the very fact of poor people having to pay for a life giving resource that jars. Taking all of these considerations into account, we might be able to unpack and understand the fundamental reaction against water privatization from some CS groups. It goes beyond consequences. It flows from the same body of argument that says there should not be markets in some commodities, period.

4. The Way Forward

It should be clear that the nature of the disagreement has to be understood before we can devise a way forward. It is not possible to easily bridge the deontological divide between those who are simply against markets for water for the same reason they are against markets for slaves, and those who wish to make a decision based on an assessment of outcomes of creating markets versus not. At least, I do not see an easy way forward if that is the divide. But if, as is mostly the case, the divide is one over assessing consequences, then in principle the divide can be bridged.

For some, “it is unlikely that this controversy will be resolved” (McGranahan and Satterthwaite). Others (UN-Habitat, 2003; UNDP, 2006) are taking a middle road, arguing that it all depends on the context and how privatization is done. The question can also be changed to “how to ensure that both private and public operators can be made to provide better services to low-income areas” (McGranahan and Satterthwaite, 2006). Certainly, the rhetoric of organizations that were once hard charging on water privatization is much curbed. The comprehensive World Bank (2006b) document on water privatization talks of presenting possible options instead of a “single best approach” (pxiii), and acknowledges that in the process of privatization the government “may want to protect some vulnerable groups (such as the poor)” (p.47). All of this is worthwhile and represents progress compared to a few years ago. But one cannot skirt around the basic disagreements. The World Bank (2006b) document, admirably open though it is compared to earlier statements from the institution, is essentially about different ways of privatizing. And the statements of Shiva (2005) and Segerfeldt (2005a) are from two years ago, not twenty or ten years ago. These disagreements persist, and will reappear sooner or later, perhaps in a different guise, despite attempts to smooth over them or get around them by avoiding them. They must be addressed.

In light of the way I have described the nature of disagreements over water privatization, it should be clear that I view bridging the divide as a process rather than a one-shot outcome. It will involve disciplined and respectful dialogue where analysts from both sides take seriously the claims of the other and examine the issues with the aid of a common information base on actual cases and situations. It will also involve a willingness to understand the other side’s perspective on the matter, and to question one’s own presuppositions. Since I am an economist, my writings have usually exhorted economists and those in the FM tendency more generally) to be more open and more humble about their findings and frameworks. From the trenchancy of some of the writing on the Civil Society side, I suppose one could make an exhortation in that direction as well.

Specifically, it would be a useful to consider a well thought out, well planned out, and well organized forum where thoughtful proponents of the two perspectives on water privatization could come together to examine empirical evidence case by case—starting, for example, with the case of Buenos Aires. The objective initially would be not so much to arrive at an answer, but to understand the different methods of analysis and different ways of formulating questions. After a few such meetings, we would be in a position to judge whether the divide can be bridged. That, to me, would be a good start.

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