ANNEX 6: SOURCES OF FINANCING

Sources of financing can vary and depend on the investor and the location of the future WWTP. The investor depends on its sources, but since we are generally talking about expensive investments, the investor relies on the co-funding from the state, commercial and development loans, and development grants (EU, various foreign donors, and national development banks). The location impacts the WWTP construction, mainly where the area is located in an environmental (protected area) and resource important location (water sources). The matrix of relevance is presented below.

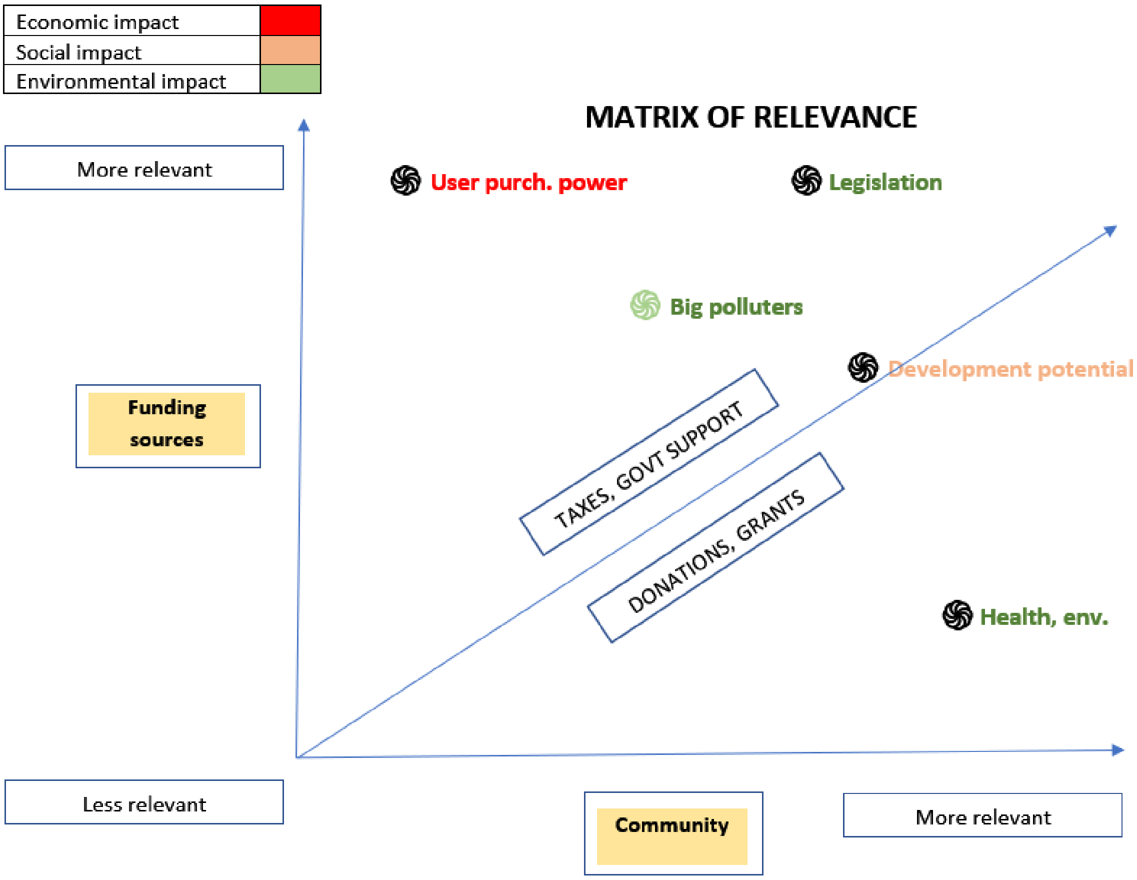

Figure 1: Example of matrix of relevance for financing RBs

A sustainable water sector financing structure must consider how services are organised and other aspects, such as providing services, degree of private sector participation, regulatory framework, financing, tariff setting, and ways to address affordability chosen technological solution. The financing structure for water and sanitation projects is chosen on a case-by-case basis.

Within the framework of EU co-financed projects, the primary sources can be[1]:

- Union assistance (the EU grant);
- national public contribution (including, always, the counterpart funding from the OP plus additional grants or capital subsidies at central, regional or local government level, if any);
- project promoter's contribution (loans or equity), if any;
- private participation under a PPP (equity and loans) if any.

[1] https://ec.europa.eu/regional_policy/sources/docgener/studies/pdf/cba_guide.pdf

The main sources of financing of WW projects in EU are illustrated in Figure 2.

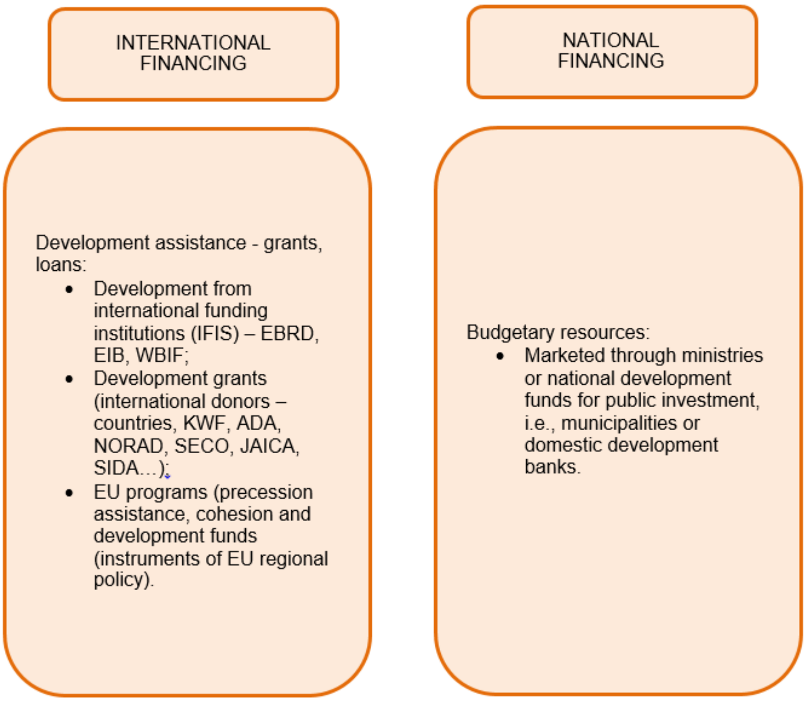

Figure 2: Main sources for financing of WW projects

The main sources of revenue are threefold: tariffs paid for water and sanitation services by water users, subsidies (e.g., from taxes), and transfers from national sources or grants. This is the so-called 3T (tariffs, taxes, transfers) concept[2]. All loans, bonds and equity investments must be serviced and repaid from the future revenue stream from these sources.[3]

Financial instruments used in wastewater sector can be divided into[4]:

- **NON-REPAYABLE INSTRUMENTS** (represent the ultimate source of financing in the water sector):
  - **Tariffs** are the foundation of the future cash flow and the main source of funding of operation and maintenance costs. They should also contribute to investment costs.
  - **Tax-funded subsidies** are used to supplement tariff revenue. They are applied to support specific groups of customers and can be provided in the form of grants and (soft) loans from the national level.
  - **Transfers** are usually grants from official development aid donors, national and international donations.

- **REPAYABLE INSTRUMENTS** (public and private loans, bonds, equity, etc., can help cover upfront investment costs and thus enable the government to leverage available sources of revenue and reduce financing costs):

[2] The concept is described in the OECD (2009b); this section is based on this concept.
[3] https://europa.eu/capacity4dev/file/29929/download?token=z83vjfHt
[4] https://europa.eu/capacity4dev/file/29929/download?token=z83vjfHt

- **Short-term loans** can be used to cover working capital requirements and to cushion cash flow. They are usually available from local banks.
- Financial institutions provide **long-term loans** on better terms for the development of water infrastructure.
- **Microfinance** can be a source of finance for local and community projects. It is typically used for schemes with a short pay-back period.
- Local water utilities can issue **bonds** by entering the capital markets.
- **Private equity** is a potential instrument for water utilities with sound finances, good cash flow, and good credit. It is used where investors share the risks of the project in return for the prospect of sharing in its profits.
- **Levers** are used to magnify the ability of future cash flow to attract repayable sources of finance.