Linking Cities And Domestic Finance

Rajivan Krishnaswamy

March 2013

Rabat
Why Do Cities Need Debt?

• Huge infrastructure backlog in environment amenities - water, sanitation and solid waste management.

• Globally, 900 million people in urban slums, an estimated 1 billion do not have access to adequate water and 2 billion to sanitation.

• Regional trends - Africa has 38% of its population unserved by safe water and 40% by sanitation, Asia 19% and 52%, Latin America 15% and 22% respectively.

Cities, need to be empowered to leverage budgetary resources with domestic capital and invest in infrastructure.
Meanwhile, cities across the developing world are coping with the impact of three major historical trends:

- **First**, globalization, requiring quality infrastructure to attract investment, stimulate growth and employment.

- **Second**, decentralization, increased responsibility, often not matched by devolution of powers – regulatory, financial and administrative.

- **Third**, the continual flow of poor people with limited access to basic infrastructure.
Urban Finance Framework: A Suggested Typology

- **Type 1** – The domestic debt markets are yet to mature and the devolution framework weak – Assist cities in loan-grant blends while improving the devolution system- Nepal, Andhra Pradesh, Bangladesh

- **Type 2** – Debt markets are constrained by fiscal space, but devolution more secure-work with domestic financial institutions to lengthen maturities and reduce transaction costs-Vietnam, Philippines

- **Type 3** – Markets begun to mature, and devolution secure, provide instruments to link city financing with domestic markets, especially for small and medium cities- Mexico, South Africa
Can We Begin with an Agenda?

Given these trends:

- Need for proactive cities to develop urban infrastructure rather than passive service providers.
- This transformation requires empowerment - authority to raise resources, create and maintain infrastructure and pay for their costs over time. Where is Bangladesh?

Urban reform agenda should include:

- City level Investment plans with pricing policies
- Rational Devolution.
- Sustainable financial structures which link domestic capital markets with city financing needs.

Survey of global trends indicate the need for policy actions which are based on partnerships between cities, national governments and their development partners.
Urban Finance: 
The Traditional Situation

Traditional Financing:

- City get debt/grants from governments/government owned financial institutions/Multilaterals on basis of guarantees.
- Project Implementation by Parastatals/Cities with no clear duties and responsibilities for servicing debt or asset maintenance.
- Under investment in Urban.
- User charges rarely covering even O&M.

Usually resulting in:

- Drying up of institutional sources based on state guarantees on account of ceilings on national liabilities.
- Limited low cost / equity / grant type funds.
- Excess supply of commercial funds including multilateral.
- Little impact on growth or urban poverty.
Since the 1990’s, innovations towards sustainable financing by leveraging domestic capital. Some stylized facts:

- Larger cities with medium-term investment plans have repeatedly accessed local markets, establishing a credit relationship with the private sector – Joburg, Ahmedabad, Ho Chi Minh City. Casablanca (?)

- Smaller and medium cities mobilized domestic capital through intermediaries – South Africa-INCA, India-TNUDF. Columbia –Findeter,

- Serious efforts to provide a greater domestic market orientation for municipal intermediaries – CAIXA-Brazil, MDFO-Philippines, FEC-Morocco (?).
Viable urban financing strategies usually need:

• Rational and predictable devolution largely formula based as in South Africa, Zambia. Tamilnadu Maharashtra

• Legal frameworks for borrowing, such as The Municipal Finance Management Act (MFMA) in SA, Urban Local Bodies Act (Tamilnadu), Master Trust Structure (Mexico).

• Strong domestic financial intermediaries working with cities such as DBSA, INCA in S. Africa, TNUDF in India

• Fiscal space allowing affordable long term interest rates for financing city infrastructure.
What Can Cities Do?

• Accounting – Modified Accrual/ Dues to and Dues by

• Clear Statement of Subsidies in Utility Accounts

• Clear Demand, Collection and Balances- Arrears and Current

• Rate Explanations
Systemic Access for Small and Medium Cities-An example from India

- Umbrella Crd Enhanc.
  - Sov. Govt. Transfer Payments
  - Sov. Grant
  - Reserve Account
  - Revenue Intercept

- WSPF
  - Partial Credit Guarantee
  - Technical Assistance
  - Bonds
  - Funds
  - Market Rate
  - Long term

- MLA
- Investors
- Local Govt. Project
  - Principal & Interest payments
  - Trustee

If necessary
Water and sanitation pooled fund

What does Commercial Finance Assess?
• Stable Revenue Streams from devolution and own sources
• Demand driven Medium term Investment Plan, Commitment by cities to tariff and collections
• Strength of the Credit Enhancement

What do Cities and National Governments Get?
• Systemic Access to Commercial Finance
• Leveraging of scarce state grants
• Maintenance of Assets built into budgets
• Disclosure of Investments and Pricing

The Role of Development partners...
• The use of a DCA Partial Credit Guarantee as a market making tool
The terms of the issue are:

<table>
<thead>
<tr>
<th>Mode</th>
<th>Private Placement Issue</th>
</tr>
</thead>
<tbody>
<tr>
<td>Issuer</td>
<td>Water and Sanitation Pooled Fund (WSPF) a trust, which pools infrastructure needs of 14 small cities</td>
</tr>
<tr>
<td>Issue Size</td>
<td>Rs. 30.41 Crores USD 10 million approx</td>
</tr>
<tr>
<td>Coupon</td>
<td>9.20% p.a.</td>
</tr>
<tr>
<td>Tenor</td>
<td>15 years (With a put and call option at the end of 10th years)</td>
</tr>
<tr>
<td>Redemption</td>
<td>In 15 equal annual instalments</td>
</tr>
<tr>
<td>Payment of Interest</td>
<td>Annual payment of coupon on a diminishing balance method.</td>
</tr>
<tr>
<td>Security</td>
<td>Unsecured Issue</td>
</tr>
</tbody>
</table>
## The Cities and the Investments

### LIST OF POOLED PROJECTS

<table>
<thead>
<tr>
<th>S.No.</th>
<th>Particulars</th>
<th>Project Cost</th>
<th>Loan amt sanctioned</th>
<th>Loan disbursed</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Water Supply Schemes:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>Ambattur Municipality</td>
<td>336.56</td>
<td>67.32</td>
<td>67.32</td>
</tr>
<tr>
<td>2</td>
<td>Tambaram Municipality</td>
<td>182.00</td>
<td>109.20</td>
<td>109.20</td>
</tr>
<tr>
<td>3</td>
<td>Madhavaram Municipality</td>
<td>325.00</td>
<td>195.00</td>
<td>105.75</td>
</tr>
<tr>
<td>4</td>
<td>Rajapalayam Municipality</td>
<td>85.00</td>
<td>51.00</td>
<td>51.00</td>
</tr>
<tr>
<td></td>
<td><strong>Adjacent Urban Areas - AUA</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>(I) Alandur Municipality</td>
<td>427.00</td>
<td>403.00</td>
<td>403.00</td>
</tr>
<tr>
<td>6</td>
<td>(ii) Pammal Municipality</td>
<td>378.00</td>
<td>357.00</td>
<td>357.00</td>
</tr>
<tr>
<td>7</td>
<td>(iii) Ankapathur Town Panchayat</td>
<td>188.00</td>
<td>178.00</td>
<td>178.00</td>
</tr>
<tr>
<td>8</td>
<td>(iv) Ullagaram Town Panchayat</td>
<td>298.00</td>
<td>281.00</td>
<td>281.00</td>
</tr>
<tr>
<td>9</td>
<td>(v) Porur Town Panchayat</td>
<td>579.00</td>
<td>547.00</td>
<td>547.00</td>
</tr>
<tr>
<td>10</td>
<td>(vi) Maduravoyal Town Panchayat</td>
<td>146.00</td>
<td>138.00</td>
<td>138.00</td>
</tr>
<tr>
<td>11</td>
<td>(vii) Valsaravakkam Town Panchayat</td>
<td>189.00</td>
<td>179.00</td>
<td>179.00</td>
</tr>
<tr>
<td>12</td>
<td>(viii) Meenambakkam Town Panchayat</td>
<td>17.00</td>
<td>16.00</td>
<td>16.00</td>
</tr>
<tr>
<td></td>
<td><strong>Under Ground Drainage:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>13</td>
<td>Madurai Corporation</td>
<td>1407.00</td>
<td>500.00</td>
<td>325.00</td>
</tr>
</tbody>
</table>

**Total**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th>Rs. In 100,000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>4557.56</td>
</tr>
</tbody>
</table>

### Notes

- **S.No.**: Serial Number
- **Project Cost**: Cost of the project in Rs. 100,000
- **Loan amt sanctioned**: Amount sanctioned for the loan in Rs. 100,000
- **Loan disbursed**: Amount disbursed for the loan in Rs. 100,000
### The Investors

**Water and sanitation pooled fund**

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Subscribers</th>
<th>No. of Bonds allotted</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Karnataka Bank Ltd.</td>
<td>2000</td>
</tr>
<tr>
<td>2.</td>
<td>ICICI Bank Ltd.</td>
<td>1000</td>
</tr>
<tr>
<td>4.</td>
<td>Metlife India Employees Provident Fund Trust</td>
<td>5</td>
</tr>
<tr>
<td>5.</td>
<td>City Union Bank Ltd.,</td>
<td>25</td>
</tr>
</tbody>
</table>
Beginnings of a New Market...

WSPF bonds have created an active secondary market
Bonds sold by original holders to following entities

1. The Karnataka Bank Ltd
2. The Tata Engineering And Locomotive Company Ltd Superannuation Fund
3. The Tata Engineering And Locomotive Company Ltd Provident Fund
4. Credit Capital Investment Trust Company Ltd Trustees Taurus Mutual Fund A/C Libra Bond Fund
5. The Tata Engineering And Locomotive Co. Ltd Employees Pension Fund
6. The Baghat Urban Co Operative Bank Limited
7. The Indian Hotels Co. Ltd Employees Provident Fund
8. Trust Capital Services (India) Pvt. Ltd.
9. Digital Globalsoft Limited Provident Fund Trust
10. Staff Provident Fund of Nicholas Piramal India Ltd
11. City Union Bank Limited - Mount Branch
13. Metlife India Employees Provident Fund Trust
14. Advanta India Management Staff Provident Fund
Alandur Wastewater Treatment
Drinking water in Madhavaram
Intermediation – Design Issues

Choices between Com Bank Approach or Capital Market
• Com Bank strongly capitalized and capital market thinly

• Ownership – Government, Private or Municipal?

• Loans and Grants: Tied or Untied?
Questions/Comments?

Thank You