

New financing instruments

The rapid growth of cities is accompanied by huge challenges, particularly in relation to infrastructure and public services. It is estimated that 900 million people do not have access to safe drinking water, while 2.5 billion people live without proper sanitation facilities. Many cities are unable to meet the swiftly growing and constantly changing demands placed upon them. The public structures and facilities needed to play an active role in shaping municipal development are often simply not there. Above all, though, there is a lack of essential funding.

The absence of financial resources is only one aspect of the problems making it difficult to plan development. Many local governments do not have the necessary capacity to make effective use of available resources, collect taxes, manage their budgets professionally or assign the separate parts of their budgets unambiguously to specific areas of work. However, funds must be allocated to urban development and implementation of the associated measures if the necessary infrastructure and the public services required for a growing city are to be established.

To the same extent as globalization is changing the face of cities and the global market is exerting an increasing influence on urban development, new opportunities are also opening up for municipalities. Wherever international businesses are investing, creating jobs and recruiting highly qualified employees, they often also show an interest in improving the local quality of life. In megacities in particular, the private sector can become an important partner for municipal authorities. Given the scarcity of urban funds, innovative forms of finance such as public-private partnerships open up new avenues for implementing urban infrastructure projects.

Where it proves possible to finance urban development schemes, the positive effect extends well beyond the monetary and infrastructural dimension. In most cases, municipal commitments bring further investment from the private sector in their wake, thus contributing to economic growth. Quality of life is always enhanced if, for example, improvements are made to the population's access to clean drinking water, hygiene, health and protection of the environment, and more efficient use is made of natural resources.

In recent years, the mobilization of domestic capital has also constantly grown in importance as a new form of financing for local authorities below state level. For this instrument to be used, however, the appropriate legal and regulatory framework has to be in place, as well as the political environment. Loans must be guaranteed by commitments on the part of the city government, for example (payment or purchase guarantee, non-callability of the loan during a certain period etc.). For the city government, in turn, the examination of its creditworthiness can act as an important incentive to improve its performance, increase transparency and predictability, and strengthen local democratic decision-making processes.

A main objective of German Development Cooperation is to put local governments in a position to make the most effective and efficient use of their available resources. Support in developing a coherent regulatory mechanism that includes both decentralization and the search for alternative financing instruments is one of the core activities of German Development Cooperation at local level. This is the basis on which Germany finances a wide range of investments in the infrastructure sector and development of the finance sector. The German Government provides loans and subsidies to promote projects ranging from water supply and wastewater disposal systems, housing and road construction to public transport systems. The aim is for the relevant goods and services to be provided at the lowest possible political level.

Urban Development Fund (India)

Tamil Nadu is one of the largest and fastest-developing states in India. The existing infrastructure has long since failed to meet the needs of its rapidly growing population and economy. Vital public services such as water, wastewater, electricity, roads and public transport need to be developed. However, neither the state nor local bodies are able to shoulder the necessary investment. This

would require the cooperation of banks and the private sector, but those responsible decline, saying that it is too risky.

Support comes from development banks such as KfW. Its involvement reduces costs, lowers the level of risk, helps in the search for new financial resources and makes it easier for domestic banks and private donors to commit themselves. German Development Cooperation is helping Tamil Nadu mobilize private capital to develop its local infrastructure and to advance the development of the money market in the state as a whole. Above all, it is strengthening the refinancing capacity of the public Tamil Nadu Urban Development Fund (TNUDF). This has the task of promoting the development of urban infrastructure in small and medium-sized towns and cities in particular.

The fund was established by the Government and three private banks in 1996 as a public-private partnership, endowed with the equivalent of EUR 65 million. By 2012, sewage systems are to be installed in a further 100 towns and cities using money from the fund. There has already been a significant decline in the occurrence of diseases primarily attributable to contaminated water.

Drinking Water and Wastewater Management Project LiWa (Peru)

The Federal Ministry of Education and Research (BMBF) is promoting ten projects within the framework of its priority area "Research for Sustainable Development of Megacities of Tomorrow". One of these is the project "Sustainable Water and Wastewater Management in Urban Growth Centres Coping with Climate Change – Concepts for Lima Metropolitana (Peru) – LiWa". LiWa is investigating the sustainable planning and management of two crucial lifelines: water and sanitation. During the preliminary phase, the relevant stakeholders were identified and initial contacts were established. Among other things, the project is developing and analyzing options for designing the tariff structure to take account of economic, environmental and social criteria.

This also involves identifying various options for water pricing and carrying out the relevant economic analyses. This is designed to help the municipal authorities overcome problems with water quality and quantity. Researchers are examining various options to determine whether they are suitable for covering the cost of water supply, meeting distribution-policy goals and overcoming institutional, political and economic obstacles. They are also analyzing whether changes need to be made to the institutional framework in order to reform water pricing.