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## Summary

**Strategic Financial Planning (SFP) for water is an approach that aims to place the financing of water infrastructure and services onto a more predictable and sustainable basis. SFP brings planning and financing - which are typically done separately - onto convergent tracks, so that spending ambitions are more compatible with available financial resources. This Tool defines the SFP framework, details its methodology, provides insights from in country experiences with SFP, discusses opportunities and challenges related to its implementation, and gives recommendation on how to best apply SFP in practice.**

## Defining Strategic Financial Planning

Strategic Financial Planning (SFP) is an approach and methodological framework to ensure that the financing of water and sanitation (WSS) infrastructure and services matches the policy ambitions. The SFP approach aims to foster a national policy dialogue amongst interested parties with the aim of developing consensus on what WSS services the country can or should afford in the next 20-30 years and how it will pay for them. More specifically, SFP provides a guiding framework to “who (users, taxpayers, industries) should pay for what (operating/capital expenses, water/sanitation, rural/urban/peri urban areas) and what should be the future service level. It determines how much money is needed and where it would come from” (OECD, 2009, 53). The outcome of an SFP is a report or plan with specific output that can support policy makers taking more informed financial and operational decisions.

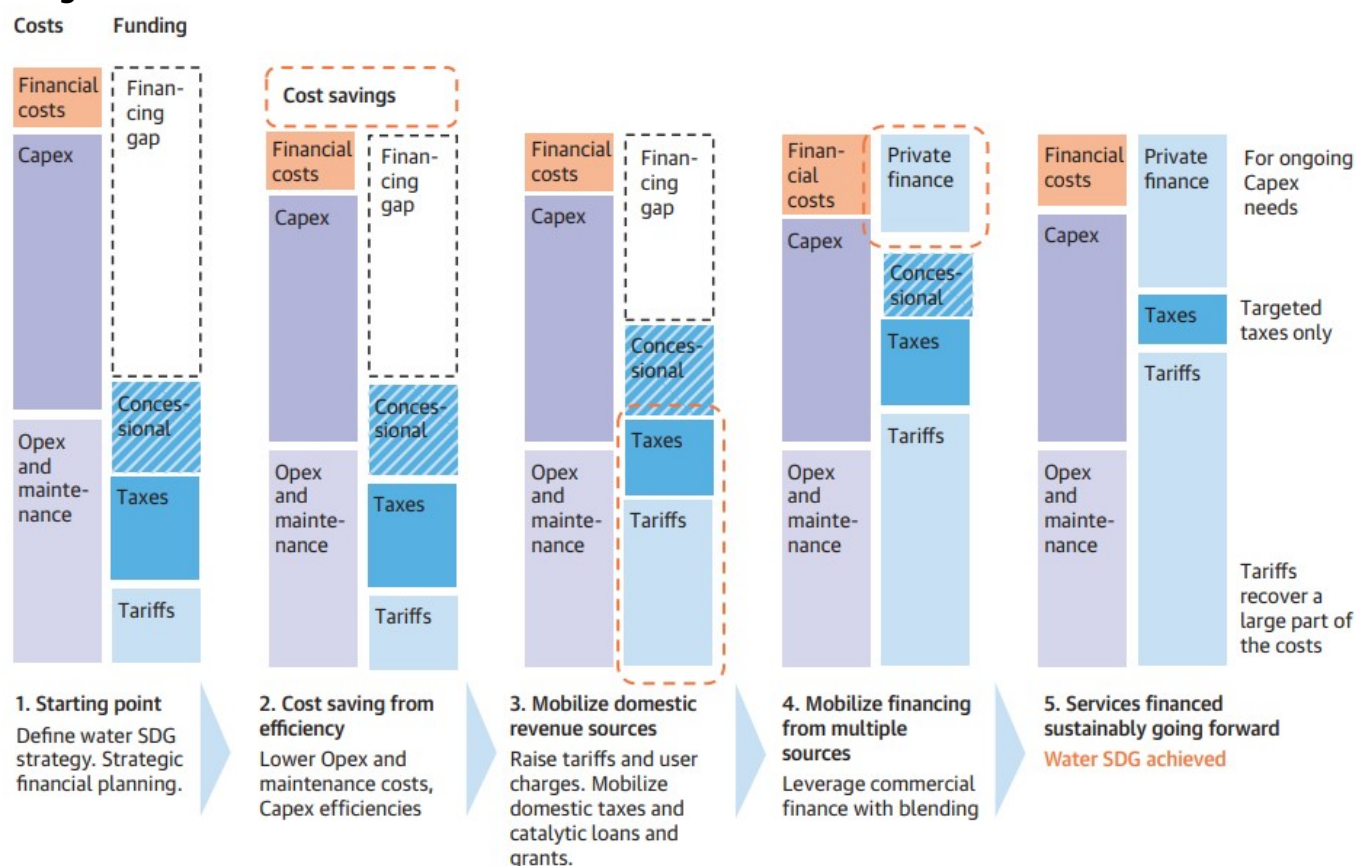
The objectives of SFP are (OECD, 2011):

- **Building consensus on goals:** providing a structure to enable a policy dialogue to take place, involving all relevant water stakeholders, with the aim of producing a consensus on a feasible

and sustainable WSS service delivery model.

- **Generating scenarios for a financial strategy:** illustrating the impact of different objectives and targets in a long-term perspective.
- **Fostering institutional coordination:** linking sector policies, programmes, and projects in relation to WSS.
- **Matching financial needs with investment flows:** facilitating external financing by providing clear and transparent data on financing requirements (Fig. 1).

## Image



**Figure 1.** Representation of the Financial Needs Assessment and Projected Investment Flows for Realising Water Sector SDG 6. Source: World Bank (2017).

The SFP framework may be applied to support municipal, regional, or national planning of WSS. While it is traditionally used in the context of urban and peri urban WSS, SFP can also be applied to other sub-sectors of water management, e.g., rural, industrial, agricultural, and environmental uses of water. In the context of the SDGs, the SFP approach might also play an important role as a tool to generate a financial strategy to achieve the development goal set for the water sector (Tool D2.01). SFP is not only concerned with matching financial needs with investment flows, it can also be used as a framework to improve efficiency in the provision of WSS.

## Methodology for Implementing SFP

SFP was initially implemented as part of the OECD's WSS work in transitioning economies (Eastern European, Caucasus & Central Asia region - Armenia, Georgia, Moldova and the Kyrgyz Republic) and some African countries (Egypt, Lesotho, and Uganda). The SFP methodology is based on solid financial modelling that structures the process of consensus-building in the following steps:

1. Assessment of current financing gap
2. Discussion of policy options that could help to close the financing gap
3. Development of alternative scenarios to improve water services
4. Identification of most appropriate scenario and associated policy mix.

Based on the learnings from OECD's experience, building a financing strategy using the SFP framework requires the following elements (OECD, 2009):

- **Scenarios:** 10-20 years or even longer of investment and service plans for the sub-sector (e.g., water supply and sanitation, irrigation, wastewater), including estimated costs for capital investment and recurrent operation and maintenance (O&M).

- **Projections:** feasible sources of finance for both the initial capital investment and the recurrent costs of operating services. These would typically include cost recovery from tariffs and other user charges, subsidies from government budgets (including those originating from external donors), contributions from non-governmental organisations, loans on commercial terms from banks and export credit agencies, private equity, loans on concessional terms from international financing institutions (IFIs) and other sources, etc.
- **Comparisons:** The financial requirements implied by the above scenarios would be compared with projections of finance likely to be available. In the event of a financing gap appearing, a process of iteration would take place involving revisions to both the spending and financing scenarios. Spending plans would be adjusted to make them realistic (e.g., less ambitious targets, more cost-effective options, demand management programmes, more attenuated implementation periods), while more rigorous assumptions would be made about financing sources (higher tariffs, greater engagement with donors and IFIs, use of financial engineering and innovative financing sources, etc.).
- **Iteration:** it would continue through several rounds until the spending scenarios were compatible with feasible sources of finance.

## Insights from Practical Country Experience

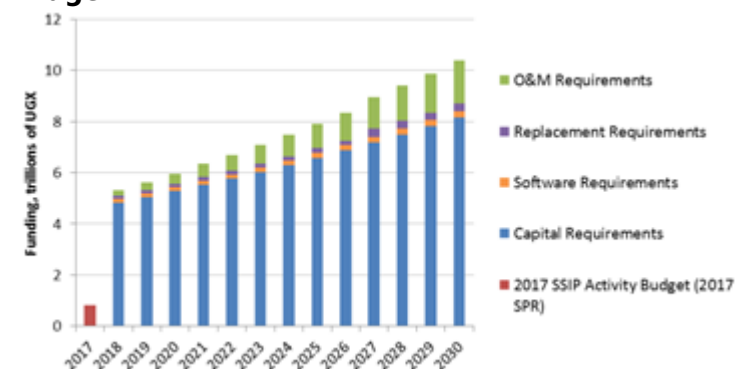
Several countries put in practice the elements of SFP in their own way (e.g., Senegal, Mozambique), but some (e.g., Kyrgyzstan, Armenia, Moldova, Lesotho, Egypt) have undertaken SFP more systematically, involving stakeholder dialogues and modelling exercises to underpin the processes described above. Here are few insights on how the SFP process was applied in two different countries:

- **Colombia:** A recent case that highlights the importance of SFP is Colombia's Strategic Vision for the Water Sector 2018-2030. Even though this strategic planning process did not fully apply the SFP methodology, it used its most important elements: an approach to build consensus on the goals among key water stakeholders; a methodology to calculate and close the financial gap to achieve those goals; and a document that compiles results and serves as a reference for policy makers. An interesting feature of this process is the financial scenarios built under different regulatory restrictions. This exercise helped the government to propose a financing strategy to close a financial gap of US \$4 billion, if the country wants to achieve its SDG compromises in 2030. This financing strategy also proposes to work on the optimization of

different economic mechanisms (such as direct subsidies, concessional loans, etc.) and the use of innovative financial mechanisms such as “municipal bonds”, backed-up by revenues from tariffs, or “coaching funding” where WWS providers with strong financial and technical capacity lend resources to small providers, conditioning repayment to financial performance of the latter.

- **Uganda:** Another recent practical example of SFP is the “Water and Environment Strategic Investment Plan 2018-2030” of Uganda. to guide annual investments in the sector out to year 2030. Spearheaded by the Ministry of Environment and Water, the plan aims to guide the annual investments needed until 2030 to meet the sector's targets across 24 indicators measuring the key activities of the sector (Strzepek et al., 2018). The SFP exercise created projections based on external trend and indicator trajectory assumptions and summarised budget requirements into four cost categories (Fig. 2). An interesting exercise with the Ugandan SFP is that business as usual scenarios were run across the 24 water indicators to reveal which sub-sector would miss their targets, thus informing where to prioritise limited future investments.

## Image



**Figure 2.** Annual Environment and Water Sector Budget Requirements in Uganda 2018-2030. Source: Strzepek et al. (2018).

## Opportunities and Obstacles

Experience so far shows that the following positive outcomes can be expected from SFP. From a technical perspective, experts believe that SFP can solve many of the problems in WSS, such as (OECD, 2009):

- Greater dialogue between the water community and the Ministry of Finance.
- A more widely shared understanding of the issues amongst stakeholders, leading to greater consensus on realistic spending targets.
- Outcomes from SFP can be incorporated into mainstream governmental budgetary and planning frameworks, such as the annual Budget, the Medium-Term Expenditure Framework and Poverty Reduction Strategies (Tool D2.01).
- An improved coordination between WASH actors and stakeholders, specifically improving the link between policy and projects and bringing the two into closer alignment.
- Linking sector planning more closely into the budget system, delivering better and more predictable public budget resources for WSS.
- It can support an informed debate about tariff policy for the sector and ensure that

considerations of affordability are sufficiently factored into these debates.

- In developing countries SFP is an essential part of building the case for external support through ODA or loans from IFIs.

Nonetheless, implementing SPF can be considerably challenging due to a lack of:

- Financial and engineering technical capacity in terms of access to data and/or the skills to transform this into useful information.
- Political willingness for reform, ownership of the process, and engagement of key stakeholders within the public administration (Ministry of Finance; Municipal/Regional Finance Departments).
- Buy-in and coordination with local authorities. Indeed, most of the cases related to successful stories of SFP implementation come from countries with nationally centralised WWS governance systems. Yet, in many countries local authorities (e.g., municipalities) play a great political, administrative, and financial role in WSS services (Tool B1.02). Therefore, when applying this tool in countries with decentralised WASH governance structures, engagement of local authorities and regional governments becomes a key step in the process, which is often not so easily obtained.

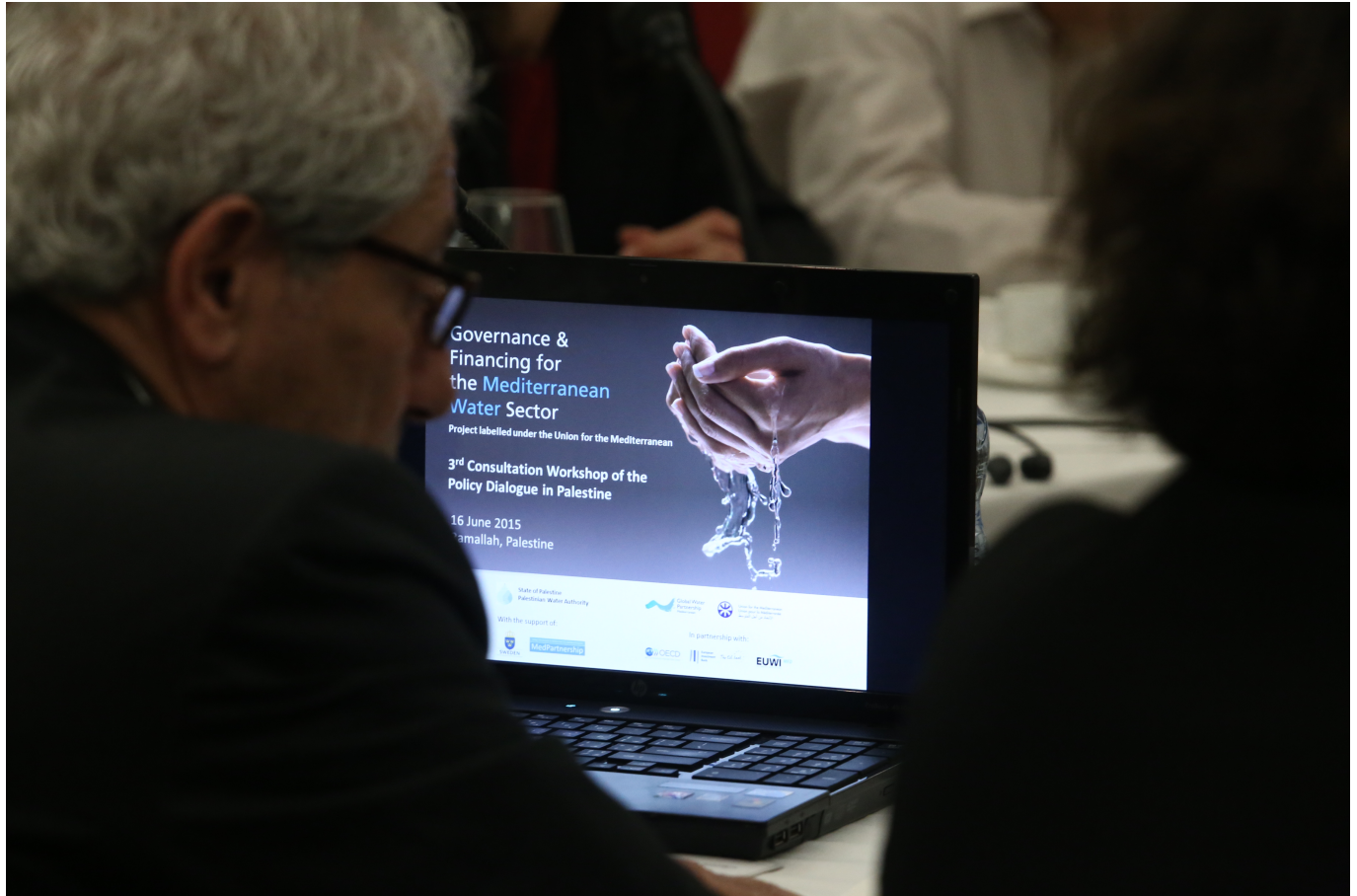
## **Key Considerations and Recommendations**

The key enabler for a successful implementation of a SFP process is to establish a broad multi-actor platform (Tool B3.05) for dialogue that, on one hand, considers water stakeholders' views and, on other hand, gives legitimacy to the decisions made in relation with the options for the water sector in the long-term. The following lessons for policymakers have emerged, if the full benefits of SFP are to be realised:

- SFP must be championed at an influential level, and fully owned by the government, in order to give it the necessary credibility and impetus.
- Time and care should be taken to engage stakeholders in dialogues about water investment and spending ambitions, and about the trade-offs involved in interactions between spending and financing scenarios.
- If the process is supported by the use of formal modelling, this should be credible and endorsed by stakeholders, including the Ministry of Finance and Municipal/Regional Finance Departments (when SFP is applied to local or regional governments).
- It is important to tie up SFP to the new trend about designing and implementing Integrated

National Financial Frameworks (INFFs) for advancing the Sustainable Development Goals (Tool D2.01). At the national level, any country implementing an INFF should take advantage of the experience in SFP for the water sector, that is, using its tools to establish a financial strategy to achieve SDG 6 targets.

- The OECD has sponsored the production of modelling system FEASIBLE. The FEASIBLE is a computerised tool for developing spending and financing scenarios, enabling iteration of the two to produce a compatible outcome (EUWI & GWP, 2007).



## Thematic Tagging

Private Sector Urban Water services

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