



The World Bank Group

***Local Governments: Facilitating
Framework and Enabling
Policies for Accessing Debt
Finance***

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New Roles in Urban Infrastructure

National Govt.

- *inter-govt. finance framework / flows*
- *standards, rules of the game*
- *monitoring, capacity building*
- *capital grants*

Local government

- community representation
- core non-revenue services
- local tax administration
- sets service objectives within natl. standards, regulates utilities/ concessions

Muni. enterprises

- provision of revenue-earning services
- should be business-like: management autonomy, financial self-reliance, rational “make-or-buy” decisions

Private sector

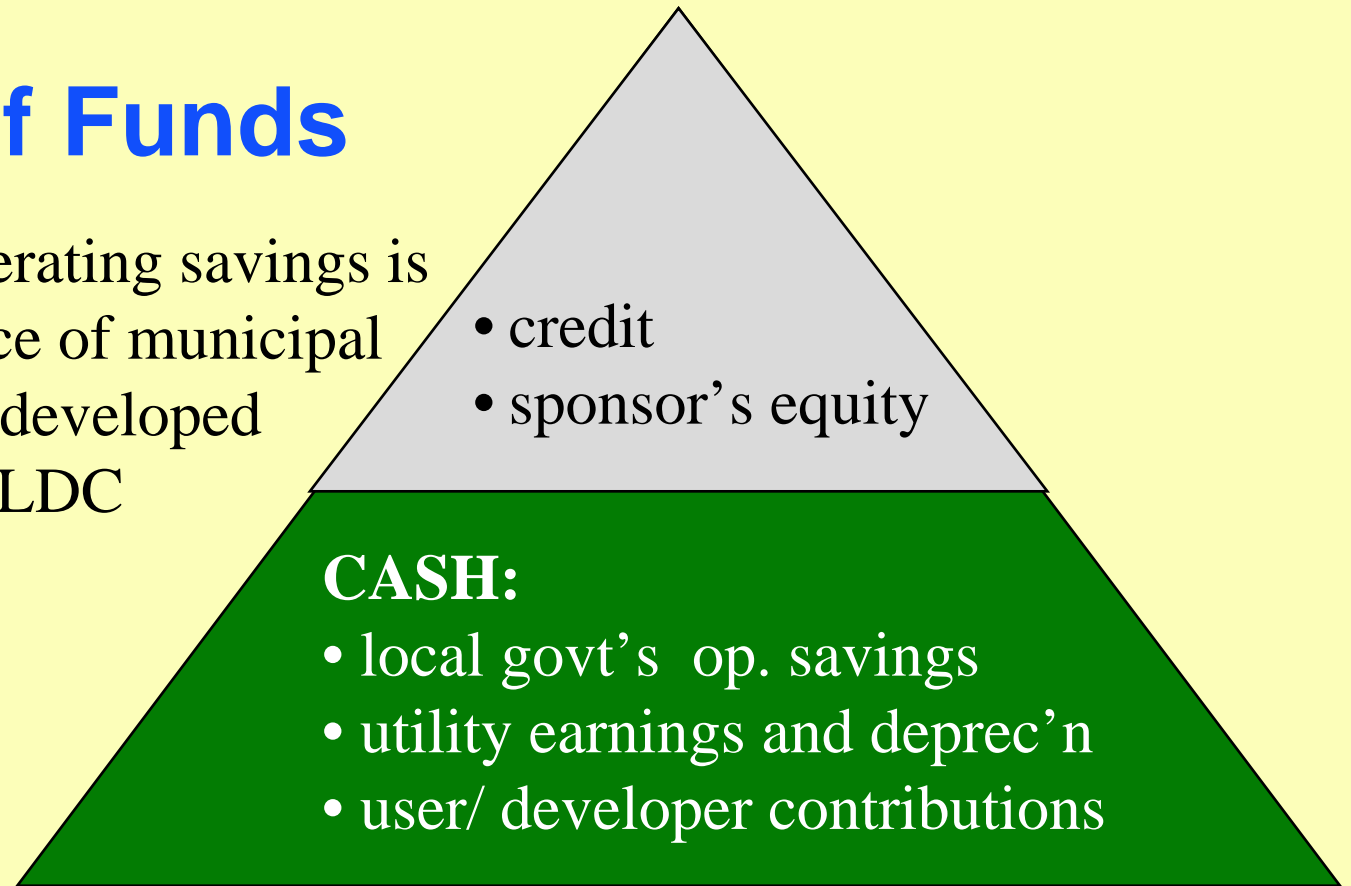
- provides goods, works, services, finance to LG and enterprises
- runs / develops services under municipal concessions and BOT

*Users,
NGOs,
Developers*



Sources of Funds

- Cash from operating savings is the main source of municipal investment in developed countries and LDC



- A sufficient and steady cash-flow is also the basis for credit and private concessions



Municipal Access to Credit

Local credit-worthiness

- cash flow
- collateral
- capacity

limited
invest. from
cash & grants

sustained
market
financing of
viable projects

Financial sector dev't.

- macro stability
- bank regulation, securities market
- market depth, diversity, competitiveness



Segmenting Municipalities

Creditworthy Local Govt.

social / environmental projects

- GFI loans
- MDF loans
- commercial bank loans, general obligation bonds

- BOT /concessions
- revenue bonds
- commercial bank loans
- GFI loans

revenue-earning projects

- Grants and TA

- BOT / concessions
- GFI loans and TA
- limited MDF loans and TA

Non-creditworthy LGs



MDF performance & design issues

Frequent MDF Shortcomings

- politicized lending
 - allocation
 - forgiveness (contagious)
- interest rate subsidies can undermine emerging commercial alternatives
- government provision of credit fails to initiate relationships between local borrowers and “real-world” lenders
- bias against concessioning

Better MDF designs

- external audits, prudential oversight, management autonomy
- affiliated to Min. of Finance not Min. Interior or Public Works
- explicit, simple eligibility criteria
- automatic transfer intercept for loan recovery
- unbundling loans from grants
- unbundling TA (“information intermediary” role) from finance



Do's

- think access to debt finance
- “speak to” financial market participants
- involve the financial sector in allocating credit and sharing risks, to the extent possible
- work out underlying cash flow, collateral and capacity issues
- unbundle subsidies from debt finance
- look into specifics of “market failure”, seek minimal govt. intervention that addresses it
- design a strategy for market sustainability

Don'ts

- think only about flow of IFI funds
- create ad-hoc, state-run financial arrangement to meet real-sector capital needs
- solve a fiscal problem by tweaking financing instruments
- unfocused, supply-driven municipal management TA
- prefer fake loans to subsidies
- copy an instrument without reading the prescription
- create agencies / funds without worrying about what they might grow into



Balancing goals, looking for win-win

Better incentives

- “drop dead”
- strict fiscal federalism
- incentive regulation of utilities, competition, “merchant” plants

- better pricing
- service concessioning
- risk allocation to most able party
- rating-driven discipline
- standard disclosure, GAAP
- listening to users

More money

- central micro-management of local revenue sources, utility rates
- unfunded recurrent spending mandates
- murky chart of accounts

- explicit or implied sovereign guarantees, MDFs
- BOT with guaranteed traffic, “cost-plus” utilities
- unrestrained pledging of transfers
- tax exemption on muni bonds

