ELEVEN

Consumer-Driven Public Services

What traditionally are called "public services," although some are provided by private, usually regulated firms, are critical to the smooth functioning of a market economy. In Latin America, services to provide public transportation, roads, water, electricity, and telecommunications and to enforce government standards regarding sanitation, pollution and other environmental issues, food and drug safety and other consumer concerns, and public health, including control of endemic diseases, have all been plagued by problems of funding, access, and quality. With their buying power and privileged access to bureaucrats and regulators, higher-income households have never felt the need to use the democratic process to insist on the political accountability of those in charge of public service provision. One result has been the low overall coverage and poor quality of these services, on which poor and middle-income households are so dependent.

1990–2005: Top-Down Reforms

Access to infrastructure-based services—such as water, sanitation, electricity, and telecommunications—has improved in the region over the past fifteen years, particularly in urban areas. But public investment has been on a persistent decline since the 1980s, and the increase in private investment in the 1990s following the establishment of privatization programs had collapsed by 2002, as investors became weary of the uncertainties

caused by political fallout and unreliable government regulatory arrangements.[1] (In the case of utilities, the implosion of the power sector in core OECD markets, including the United States, forced many investors to pull out.) Overall, progress in providing infrastructure has been slow and uneven—especially when compared with that in East Asia and, more recently, in other middle-income countries and China, which once trailed the region (box 11-1). Poor infrastructure has been a key factor in the low ranking of most Latin American countries in indexes of global competitiveness.[2] It takes five days at the most for exports to pass through ports in Malaysia, compared with seventeen days in Brazil.[3] Logistics costs in

1. Electrical service reaches about 87 percent of the population in Latin America. In 2004, just over nine of every ten Latin Americans had access to an improved water source (up from eight in 1990) and 77 percent of the region's population had access to improved sanitation (up from 68 percent a decade earlier). There were close to fifty telephone lines (including fixed and mobile) for every 100 inhabitants in Latin America (up from six in 1990) (WDI 2006). At the same time, total infrastructure investment in telecommunications, power, and land transportation declined by 1.5 percent of GDP on average from the early 1980s to the late 1990s, with a sharp decline in public investment (from 3 percent of GDP in 1980 to less than 1 percent of GDP in 2001). Public infrastructure investment fell in all countries, with Argentina posting the largest drop, 2.7 percent of GDP, and Colombia the smallest, 0.3 percent, during that period. The substantial expansion of private investment post privatization (from US$12 billion in 1990 to US$74 billion in 1998) was not enough to offset the fall in public investment, except in Colombia and Chile. Moreover, by 2003–04, total private investments in infrastructure in the region had dropped to US$16 billion (Calderón and Servén 2004a; WDI 2006).

2. See, for example, the World Economic Forum's Global Competitiveness Index 2006–2007 (Lopez-Claros and others 2006) and the Latin American Competitiveness Report (Vial and Cornelius 2002).

3. World Bank (2005e); reference is to total time needed for cargo to pass through port, from ship call to the port exit gate. In China, exports take at most eight days to ship out and in India, about nine days. The delays in transport and delivery caused by inadequate infrastructure in the region erode the benefits of geographic proximity to the U.S. or other markets (Limão and Venables 2001). Clark, Dollar, and Micco (2004) finds that on average having bad ports is equivalent to being 60 percent farther away from markets. Across the region, ports are a key bottleneck for export firms. Brazil, Argentina, Chile, Colombia, and Panama all privatized port operations in the 1990s. Some have taken important steps to reduce inefficiency. In Brazil's Santos port, the average container handling cost dropped by 40 percent between 1997 and 2000 as a result of a reform to cut labor costs, remove excess staff, and streamline operations. But overall, port tariffs and time delays caused by transit problems, poor infrastructure, and inefficient customs services are still too high in the region. In the case of Brazil, reforms have stalled largely because of the lack of an appropriate regulatory framework or clear guidelines from the government to see reforms to completion; slow progress in undertaking major public investment works associated with port reform also is to blame (World Bank 2007c). In Colombia, port infrastructure also needs considerable investment in upgrading and expansion, especially port terminals and nearby facilities (Reis and others 2007).

the region are two to three times the costs in industrialized countries, largely because—given the region's difficult geography and relatively sparse population—the roads are inadequate.[4] Fifty-five percent of private sector entrepreneurs in Latin America rank infrastructure as a serious problem—the highest level in the world, shared only by the Middle East and North Africa—while only 18 percent do so in East Asia and the Pacific.[5]

Rural areas still lag substantially behind urban areas in access to basic services, and the poor are ill served everywhere or not served at all.[6] The

4. Part of the logistics cost gap reflects the higher value relative to weight of OECD products, but much of it reflects the region's poor transport infrastructure and resulting higher losses in transit, higher transport costs, and the need to maintain larger inventories, tying up capital (Fay and Morrison 2007; Guasch and Kogan 2005). In Brazil, transportation costs are very high, comprising one-third of firms' average operational costs, and mostly reflect the extremely poor conditions of the country's federal paved road network. Overall, of the 58,000 kilometer network—which handles more than 70 percent of the country's total goods—90 percent are single-lane roads with two-direction traffic and only 25 percent are considered to be in good condition. There has been no rehabilitation or maintenance work done for at least ten years and no investment for at least fifteen years. The rundown road system adds about a half-billion dollars each year to vehicle operational costs, mostly paid by the private sector (World Bank 2007c, 2005e; Beath 2006). In a 2005 study by the U.S. International Trade Commission, Mexico was shown to fall far short on a number of indicators of logistics quality, especially when compared with East Asia. Mexico's roads were found to be slow, expensive, and unsafe; railroads to be limited and costly; and airports and ports to lack the capacity to handle high volumes (World Bank 2006d). During the 1990s, Mexico spent almost double the amount spent by the United States on transport as a share of GDP. Escribano and others (2005) finds for a sample of Latin American countries that transport and energy deficiencies (measured as shipment losses and duration of power outages) hurt productivity and the probability of exporting.

5. World Bank (2004b). Firms surveyed in Latin America report waiting an average of twenty-six days to obtain an electrical connection; the average is twelve days in the East Asia and Pacific region and eight days in OECD countries. Latin American firms also report experiencing twice the number of electrical outages and nearly five times the number of water supply failures as do firms in the East Asia and Pacific region; they also wait almost thirty days longer to obtain a mainline telephone connection (World Bank Enterprise Surveys).

6. Access to electricity has become nearly universal in Latin American urban areas (the share of the urban population with access rose from 92 percent in 1986 to 97 percent a decade later) but reaches only some 60 percent of the rural population. In urban and rural areas of Peru, 92 and 28 percent of the population, respectively, had access to electricity in 2000. In Mexico's largely rural southern states (Chiapas, Guerrero, Oaxaca, Veracruz), electricity reaches between 50 and 65 percent of the population, while coverage is nearly universal in urban areas across the country (World Bank 2006d). The gap in access to water and sanitation in the region has narrowed in the last decade but remains large: 96 percent of Latin Americans in urban areas but only 70 percent in rural areas have a connection to safe water, while almost twice as many people in urban areas as in rural areas have access to improved sanitation (WDI 2006).

BOX 11-1. Latin America's Infrastructure Gap

In 1980, the coverage of productive infrastructure in Latin America was similar to or higher than coverage in East Asia. Today, East Asia's capacity to generate electricity is more than double that of Latin America, and its telecommunications network is nearly three times denser (figure 11-1). East Asia also leads in total road length, despite starting at lower levels in 1980. In addition, Latin America has lost ground to China and middle-income countries (MICs) in electrical power, roads, and telephone lines, despite being wealthier in per capita terms; only in terms of access to safe water and sanitation does Latin America perform comparatively well (table 11-1).[1]

TABLE 11-1. Latin America's Infrastructure Gap[a]

	Road network (km/km²)	*Paved roads (percent)*	*Telephone lines, total (per 1000 persons)*	*Access to electricity (percent of population)*	*Access to water (percent of population)*	*Access to sanitation (percent of population)*
Category	*2002*	*1997–02*	*2004*	*2000*	*2004*	*2004*
Latin America	0.008	27	497	87	91	77
China	0.189	91	499	99	77	44
MICs	0.062	54	485	90	88	71
East Asia	0.203	78	979	n.a.	96	n.a.

Sources: WDI (2006); Fay and Morrison (2007); ADB/JBIC/WB (2005).

a. East Asia data exclude Taiwan; for road network and paved roads, they exclude also Hong Kong and Singapore. Total telephone lines include mainlines and mobile phone subscribers per 1,000 people.

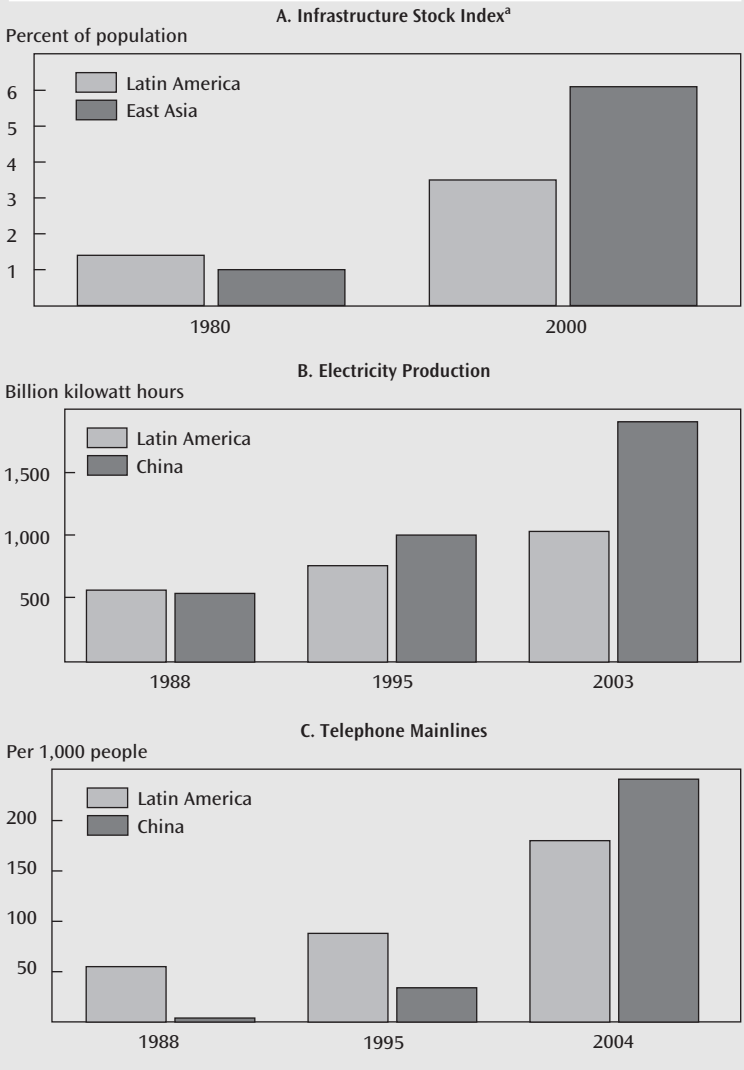
To catch up to the infrastructure levels of East Asia's median country, South Korea, the region would need to invest at least 2.4 to 5.0 percent of GDP a year over twenty years—which is at least twice the level that it invests in infrastructure today.[2] Calderón and Servén (2004b) estimates that eliminating the infrastructure deficit could increase GDP per capita growth rates in the region by almost 4 percent a year on average and cause decreases across countries of 0.05 to 0.13 in the Gini coefficients of inequality.

1. Latin America is also ahead of China and MICs in mobile phone subscribers per 1,000 people.

2. Total infrastructure spending in the region is currently less than 2 percent of GDP a year; it is 7 percent of GDP in China (up from 3 percent in 1998) and 15 percent of GDP in Thailand (up from 5 percent in 1998).

Sources: Fay and Morrison (2007); ADB/JBIC/WB (2005); Calderón and Servén (2004a, 2004b); Calderón, Easterly, and Servén (2003b).

F I G U R E 11-1. Latin America's Infrastructure Gap



Sources: WDI (2006); Fay and Morrison (2007).

a. The infrastructure stock index includes paved roads, electricity production, and telephones (mainlines and mobile) per worker. The index is calibrated so that East Asia had a value of 1 in 1980.

rich suffer least when public infrastructure services are deficient—their neighborhoods usually are the best served in the first place, and they can resort to private providers for some services. For middle-income and poor households, lack of access and low quality are much more costly, in terms of higher health and occupational risks and time and income lost, as when electricity is unreliable and roads and bus systems are bad.

The challenge is not only to increase investment in infrastructure. It is more fundamental: to create and sustain public competence in regulating the nonfinancial sector. There has been some progress in infrastructure services regulation since the 1990s in countries like El Salvador and Peru, but an unstable, unpredictable (politicized and capricious) regulatory environment is still a problem in many large markets, including Brazil and Argentina. And most governments have not yet tackled seriously such issues as pollution control, public health, food and road safety, and other consumer protection concerns.[7]

Privatization: Also a Victim

Until the late 1980s infrastructure services typically were state run—supplied at subsidized rates by large public sector monopolies that had no commercial incentive to price services adequately or to serve their consumers well. Most state-run telecommunications, water, sanitation, and electricity companies were left unable to expand and innovate because they charged inadequate prices, and the quality of services deteriorated visibly. That ended up undermining social welfare and the lot of the poor—who always are last in line for any subsidized service.

Privatization of telephone and electricity services (and to a lesser extent of road, ports, and airport services) swept through Latin America in the

7. An IDB study (2004b) ranked enforcement of consumer protection laws in Brazil as excellent; in Mexico, Argentina, Panama, and Peru as satisfactory; and in Ecuador, Venezuela, El Salvador, Nicaragua, and Paraguay as largely ineffective. Bolivia and Honduras lacked a consumer protection system altogether. In examining data for Europe and Latin America, Gilardi, Jordana, and Levi-Faur (2006) finds that the tendency to establish regulatory agencies is much weaker in social sectors (pharmaceutical, food safety, environment, and so forth) than in economic sectors (utilities, finance, competition), especially in Latin America.

1990s.[8] Privatization has been less extensive in water, sanitation, urban public transportation, and public health services.[9] In many respects privatization has been a success, resulting in improved financial and operating performance in most firms and better quality and enhanced availability of services to consumers.[10] It also has relaxed the bottlenecks

8. We use the term "privatization" to refer to both privatization and public works concession schemes. The accumulated revenues from privatization in eighteen Latin American countries reached 6 percent of gross domestic product in the 1990s. By the end of the decade, the region accounted for fully 56 percent of total privatization revenues across the developing world (more than half of all the privatizations were of high-value infrastructure or utility firms, in contrast to those in other regions outside the OECD states). From 1990 to 2001, private investment in the region in infrastructure alone totaled US$360.5 billion, US$150 billion more than the next most attractive region, the East Asia–Pacific area (Nellis 2003; Harris 2003).

9. Public ownership remains the norm in most of the region in the water and sanitation sectors but not in the electric sector. In most countries, privatization of water services has been less successful technically and still less politically than privatization of other services. Violent protests erupted against the privatization of water services in Cochabamba, Bolivia, where the concession was cancelled. Popular unrest also led to the cancellation in 2005 of Bolivia's La Paz and El Alto water concessions. By 2005, more than one-third of Argentina's water and sanitation concessions had been cancelled or were in the process of being cancelled (World Bank Privatization Database, http://rru.worldbank.org/privatization). In the state of São Paulo, Brazil, sharp increases in rates, poor service, and complaints of corruption in the privatization process prompted the government to try to reverse the shift toward water concessions back to state delivery of services (IDB 2003b). More successful water concession arrangements in recent years have involved small-scale providers under contract to municipal governments, as in Paraguay and parts of Bolivia. Cartagena, Colombia, has adopted innovative mixed capital firms in which the city government has the majority stake in utilities companies, with responsibility for securing financing for infrastructure projects, while private operators, with a minority stake, are responsible for the management and operation of the company, working under a contract with clear performance and expansion targets (Luis Alberto Moreno, "Water Works," *Wall Street Journal,* March 9, 2006, p. A19; Guasch 2004; Kariuki and Schwartz 2005).

10. Case studies in Chong and López-de-Silanes (2005) based on a large sample of privatized firms in Argentina, Brazil, Chile, Colombia, Mexico, and Peru show a median gain in firm profitability after privatization of around 14 percent, efficiency gains of almost 70 percent, and output increases of more than 40 percent. In Argentina, the number of phone lines more than doubled after privatization. In Chile, the waiting time for a new fixed phone line dropped from 416 days in 1993 to fewer than six days in 2001, while the waiting list dropped from a peak of 314,000 people in 1992 to only 32,000 by 2001 (Fischer, Gutiérrez, and Serra 2005). In more cases than not, privatization also freed the state from a heavy administrative and unproductive financial burden, closing the door to widespread corruption and mismanagement by publicly appointed state company employees (Nellis 2003). Andres, Foster, and Guasch (2006) analyzes the impact of privatization on the electricity sector in the region, separating the short-term from the long-term results. The study finds that changes in ownership generate significant improvements in labor productivity, efficiency, and product and service quality—and that most of those changes occur in the transition

that service supply shortages used to create. Furthermore, enhanced access resulting from privatization often has benefited the poor.[11] In Argentina the privatization of water services in poorer areas was associated with a reduction in child mortality of as much as 24 percent. The poor have benefited even in sectors, such as telephone services, in which privatization has led to price increases, because often they had no previous access to services at all (the pre-privatization price was, in effect, infinite). Increasing access made them better off.[12]

Nonetheless, privatized infrastructure programs have been plagued by corruption and the failure of regulatory agencies to protect consumers from price gouging in some cases and in other cases to protect newly private firms from government restriction of legitimate price increases.[13] As a result, privatization has been an especially unpopular reform.[14] Also to

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period around the privatization process. The improvements in the post-privatization period—beyond two years after the change in ownership—are much more modest.

11. Birdsall and Nellis (2003); Nellis and Birdsall (2005). Analyzing results from the water sector in Colombia, Barrera-Osorio and Olivera (2007) finds that in addition to increasing the frequency of service, privatization in urban areas increases access to and quality of service and also improves health outcomes for the lower quintiles. But in rural areas, the positive effects of privatization on the frequency of service and on health indicators are outweighed by negative impacts on access and prices.

12. Galiani, Gertler, and Schargrodsky (2005) finds that in Argentina, child mortality fell 8 percent on average in municipalities that privatized their water services. The effect was largest in the poorest municipalities that privatized, where child mortality fell 26 percent. Evidence of a pro-poor impact of private sector services also was found in Chile and Bolivia, where 25 to 30 percent of network expansion targeted the lowest 20 percent of the income profile (World Bank 2003b). In Argentina, Gonzalez-Eiras and Rossi (2007) finds some evidence of lower child mortality related to food poisoning and lower frequency of low birth weight in provinces that privatized their electricity service than in provinces with public distribution networks—though the evidence is less conclusive (possibly due to the low number of cross-section observations). Instances of price increases in privatized firms often are necessary if the firm is to modernize, meet demand, and operate without subsidies. Under state ownership, many Latin American governments set utility prices so low that they did not cover costs, which led to scarcity, rationing, and starving firms of investment capital.

13. In Colombia, scandals and allegations of corruption followed the privatization of the electricity sector (TermoRío case). In Argentina, the obscure bidding process in privatization programs raised suspicions of corruption and political favoritism (Ayala and Millán 2002; Chong and López-de-Silanes 2003). In Argentina's Tucuman province, opportunistic behavior by the local government, popular protests, and poor performance led to cancellation after two years of a thirty-year private concession for water and sanitation provision (Nellis 2003; Guasch 2004).

14. Latinobarómetro (2006) shows that between 1998 and 2003, support for privatization among Latin Americans surveyed dropped from 46 percent to 21 percent (falling across all countries and income groups). Satisfaction with privatized services rose 12 percentage

blame are a few cases that have gone very wrong, such as the privatization of water services in Cochabamba, Bolivia.[15] Along with instances of price increases, job losses—even when small relative to overall employment—have added to the sense of frustration, reinforcing the perception among Latin Americans that privatization has been unfair, generally making the rich richer and the poor poorer.[16]

A central problem was that the region's approach to privatization was shaped heavily by fiscal considerations, since sales help shore up government revenues and may permit retirement of government debt.[17] Often that meant that insufficient emphasis was placed on ensuring that markets would be competitive after privatization and that consumers would be protected from abuse. Sales were made to single firms, for example, or regulation of natural monopolies became inadequate after they were in private hands.[18] The lack of accountability reflected the reality that privatization policies were never embedded in a broader vision of social policy. In most cases it meant that opportunities to share the gains of privatization more fairly with the broader public were lost or ignored.[19]

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points among respondents in 2004–06 as economies picked up steam, but the average figure, 30 percent, remains low. For an overview of the arguments and evidence on the unpopularity of privatization in Latin America, see Nellis (2003); Nellis, Menezes, and Lucas (2004).

15. See Nickson and Vargas (2002) and Kohl (2004) on the case of Cochabamba, Bolivia.

16. Privatization often had a short-term effect on employment—labor had to be shed for the privatized enterprises to restore efficiency and profitability. But in most cases the number of workers laid off due to privatization was small relative to the entire workforce and tended to be offset in the medium term by the increased job creation produced in part by privatization and liberalization (McKenzie and Mookherjee 2005).

17. Privatization has brought a positive flow of funds and reduced public debt to governments in Latin America through price rationalization, retirement of accumulated debt, elimination of subsidy flows, and increased tax revenues from more profitable and productive private firms (Nellis 2003; Macedo 2000).

18. Privatization of public utilities has in many cases left consumers defenseless vis-à-vis the new owners of the formerly state-run enterprise. Typically, consumers have been poorly represented, creating a lack of transparency and the perception of abuse, which work against the long-term sustainability of privatization reforms. There have been instances, as in Argentina, in which the privatized firms did not honor some of the commitments that they made to the government, such as investing a percentage of their profits in modernizing infrastructure, improving customer service, shortening service installation times, or extending coverage to certain areas. Uruguay's energy sector regulatory body, Unidad de Regulación de Energía y Electricidad, was established only in 2000, five years after the start of sector reform and the establishment of a services concession system (IDB 2003a, 2003b).

19. Nellis and Birdsall (2005) includes a number of country studies that illustrate this point. They note that when distributional issues have been considered, it has generally been in the context of greasing the wheels of the process to make it politically more palatable (as

An exception, for a while, was Bolivia. There some of the expected benefits of privatization were initially distributed to citizens in the form of future pension benefits or stock holdings, creating more shareholders in the market economy through a kind of popular capitalism. But that program fell afoul of Bolivia's fiscal problems in the late 1990s. Meanwhile, privatization in Brazil, though clearly leading to more efficient and competitive production, failed to provide for any improvement in the distribution of wealth and income (box 11-2).

The perception of unfairness has slowed privatization and even begun to reverse its contributions to improving efficiency and the access of the poor to services. In Mexico, energy remains a state-run business, limiting the new investment that private owners would bring. In Argentina, the current government has limited tariff increases to well below inflation, putting a stop to new investment and continued extension of services to poorer neighborhoods.

What's Needed Now: A Bottom-Up Approach

The key reform for the future is a radical rethinking of the culture of service delivery. In infrastructure services, continuing private involvement and ownership are essential if a government hopes to secure adequate investment and avoid the past problems of state-owned enterprises. But to avoid corruption and guarantee a good regulatory environment also requires the government to make an active commitment to ensuring transparency and providing information to consumers regarding privatized firms.

In some countries, improving infrastructure and other consumer services may require expanding public budgets.[20] But above all, it is a matter

when employees of enterprises to be privatized are given special deals on obtaining shares in the new firm or when the sellers oblige the new owners to accept post-privatization conditions such as service guarantees for less-profitable markets or to commit to maintaining certain levels of investment or numbers of employee for a specified time). See also Birdsall and Nellis (2003).

20. Recent research by the World Bank estimates that the annual financing requirement for infrastructure in the region for the next ten years is about 3 percent of regional GDP (Fay and Morrison 2007; Fay and Yepes 2003). Assuming that the public sector supplies half of that amount, it would need to devote 1.5 percent of GDP a year to infrastructure. That would be an increase of 0.7 percent of GDP from the average level of public infrastructure spending in the region from 1996 to 2001.

BOX 11-2. Privatization and Popular Capitalism

Letting Taxpayers Hold the Bag in Brazil

Since the early 1990s, Brazil has privatized more than 115 state-owned enterprises, transferring more than US$71 billion worth of equity capital to private owners. From an efficiency point of view, reflected in the improved profitability of privatized firms, privatization has been a success. But its impact on income and asset distribution has been less positive.

To be sure, equity concerns were never at the heart of the program's objectives. Although democratization of capital was initially stated as a goal, the Brazilian government—facing a fiscal crisis when the program peaked in 1997 and 1998—focused instead on using privatization to promote foreign investment and maximize revenue from sales. To get higher prices, it auctioned most of the state-owned enterprises in large, controlling blocks of shares to big foreign and national corporations. In the few cases in which room was made for democratization of capital, the beneficiaries were mostly middle-income workers of former state-owned enterprises participating in manager-employee buyouts and workers covered by pension funds of former state-owned enterprises that participated in the auctions. Worse, the program did not reduce public debt, which actually increased sharply from 1994 to 1999, due in part to external shocks. Taxpayers, including the poor, are now bearing the costs of higher public debt.

Creating Stakeholders in Bolivia: A Good Idea Run Aground

Bolivia's privatization program in the 1990s put income redistribution at the heart of its objectives. Under the model adopted in 1995, private purchasers of state-owned firms committed themselves to doubling the net worth of the companies in exchange for half the shares. The government distributed the remaining half to the Bolivian people in the form of life annuities (initially set at US$250), beginning at age sixty-five. (The annuity represented 27 percent of Bolivia's per capita income.) The idea was to create stakeholders in the future of the firms and the market economy. Subsequent fiscal pressures eventually prompted the government to lower the annuity amount and to decree that only citizens who were fifty-five years old or older at that time would qualify for a life annuity when they reached age sixty-five. All others would receive shares in the privatized firms instead. In 2002, then President Sanchez de Lozada promised to return Bonosol to its initial level, but lower-than-expected dividend flows from capitalized firms made that impossible. The performance and popularity of the program was further undermined by inadequate regulation, prolonged economic recession, and

(continued)

BOX 11-2. Privatization and Popular Capitalism (*continued*)

a couple of high-profile failures among foreign firms (like Brazil's VASP). By 2006, the idea of "capitalization" was being eclipsed in the key energy sector by the newly elected president's decision to renegotiate contracts with foreign holders of privatized entities.[1]

1. It is not clear whether the Bolivian state enterprise YPFB (Yacimientos Petrolíferos Fiscales Bolivianos), which took a majority stake in the countries' main gas and oil production companies, will maintain pension payments. The government has claimed that it does not have sufficient funds to pay the existing yearly pension to the elderly beyond 2007 ("Out of Gas," *Economist,* August 17, 2006; Matthew Cowley, "Gas, Oil Takeover Pits Bolivia against Brazil, Foreign Cos," *Wall Street Journal,* May 2, 2006; "Bolivian May Day Brings Higher Hydrocarbons Revenues and Higher Expectations," Andean Information Network/Red Andina de Información, May 4, 2007.)

Sources: Barja, McKenzie, and Urquiola (2005); Birdsall and Nellis (2005); Macedo (2005, 2000); Barja and Urquiola (2001); Graham (1998); Valdez (1998).

of creating a market in which public financing is combined with a radical new style of management, one that focuses on greater consumer choice and voice. The government then assumes two major roles. The first is to empower citizens and community groups with effective regulation and information about standards and prices. The second is to ensure, through voucher-like subsidies and cash grants, that the poor have the buying power to demand good-quality services. User participation and voice and firm accountability are crucial in particular for sustaining an adequate quality of services at the local level. In the end, however, civil society and grassroots advocacy cannot substitute for the fundamental role of government.[21]

We set out below policies and programs to look for in infrastructure services; the same logic and spirit can be applied to all regulatory services.[22]

21. See Fiszbein (2005) for more on this point.

22. The general benefits of the policies and practices that we suggest depend heavily on well-functioning legal and economic institutions that promote and monitor transparent market operations. The more careful and extensive the preparation devoted to the institutional underpinnings of private participation, the better the results, in terms of both efficiency and equity (Nellis 2003). See also the discussion in Guasch and Straub (2006).

First, Focus on Competition and Information

- In designing privatization and concession contracts and transactions, avoid the mistakes of the 1990s. Maximize competition wherever and whenever possible. When the lack of exclusive rights or other forms of monopoly privilege look like a deal breaker, negotiate hard to make the period of exclusion as short as possible.
- Build more transparency into privatization operations by opening bids on television and using independent monitors to vet transactions and certify their openness and honesty. Make full disclosure regarding access, pricing, user rights, and performance benchmarks a legal part of contract provisions with private providers.[23] Encourage monitoring and publication of information on service quality by consumer groups, nongovernmental organizations, and the press.[24]

Second, Make Special Efforts to Reach the Poor

- When auctioning service contracts, obligate private operators to extend access to poor neighborhoods.[25]
- Use connection subsidies, given directly to poor households.[26]
- Include provisions in contracts that give service operators incentives to tap the labor of the poor in delivering services. In Argentina, the low-income population in some neighborhoods is providing the

23. A review of urban water utilities in Latin America in the early 2000s concluded that giving consumers little information about the process of reform and tariff setting while limiting their opportunity for comment weakens the regulatory process and the credibility of reform, thereby making rate changes, however justified, difficult to implement (World Bank 2003b).

24. In some cases having a modern, technically savvy ombudsman or agency might make sense. The person or agency would be a watchdog for poor and working-class consumers, and it would accountable to an elected body.

25. On this point, see Estache, Foster, and Wodon (2002); Estache and Quesada (2001); Briceno-Garmendia, Estache, and Shafik (2004).

26. See Komives and others (2006); Nellis (2003); Estache, Foster, and Wodon (2002). Latin America has a long history of distortive, poorly targeted subsidy programs, which have tended to benefit mostly the urban middle class rather than the poor (Estache, Gomez-Lobo, and Leipziger 2001). In Mexico in 2003, subsidies for electricity consumption absorbed 1.1 percent of GDP, about the same amount as total public investment in infrastructure that year, with the bulk of subsidies going to non-poor consumers and more economically developed regions (World Bank 2006d).

labor to establish and maintain water connections. By involving consumers in poor communities in setting standards and mapping infrastructure networks, one of Manila's water concessionaires has helped reduce the costs of providing water to the communities by 25 percent.[27]

- Eliminate regulations that undercut what would be viable markets in poor communities.[28] In Yemen, the government now allows poor communities to tap into already available electrical lines and to manage service distribution and pricing. In other developing countries, eliminating the state telephone monopoly has created a good rental market for mobile phones in poor neighborhoods. In Paraguay, independent small-scale water providers are reaching poor households in isolated neighborhoods at prices that are competitive with those of public utilities.[29]

Some of these "pro-poor" contractual obligations have costs, which governments must allow private providers to recover through the rates that they charge.

Third, a Political Strategy

- Minimize the losses of laid-off workers. Make special provisions in privatization schemes to compensate laid-off workers without compromising the government's fiscal position or generating excessive political pressure. This step is politically important. Although the number of job losses due to privatization in Latin America has been small relative to the total number of jobs, job loss has a high political

27. World Bank (2003b).

28. See Trémolet and Hunt (2006) for an in-depth discussion on this point based on case studies from Bolivia, Vietnam, South Africa, and Zambia in which existing regulations were eliminated or adapted to facilitate the expansion of water services to poor consumers.

29. Small-scale water providers serve about 25 percent of the urban population in Argentina, Bolivia, Colombia, Guatemala, Paraguay, and Peru. They range from fixed networks (piped delivery) to mobile providers (tanker trucks) serving individual households and institutions. In Santa Cruz, Bolivia, cooperatives are the only water suppliers for the city's 1 million people. The aguateros in Asunción, Paraguay, have invested more than US$30 million to provide service to 75,000 households, and they have fully recovered both operating and investment costs (Solo 2003; Kariuki and Schwartz 2005).

cost and helps fuel much of the opposition to reform. During Uruguay's state restructuring and modernization program in the early 1990s, special funds were set aside to cover the costs of severance, early retirement, or transfer of redundant employees. The reforms took place without strikes or labor protests.[30]

- Develop a strategy to deal with public opinion. In some settings it may be necessary to minimize the negative public perception of privatization in order to preserve the political possibility of deepening or extending privatization or other efficiency- and growth-oriented reforms.[31] In Peru, a campaign to inform the public that privatization of electrical service would be undertaken through a transparent process and that rate increases would be regulated increased support among citizens from 21 to 60 percent.[32]

Governments will always have fundamental responsibilities to protect the environment, public health, and consumers as well as to provide the infrastructure and services necessary to run a modern state. In all these areas, public policy and practice need to become more consumer driven and the government must become more accountable to citizens than to bureaucracies and interest groups. At the same time, the constant scrutiny of citizens is critical if the government is to be held to account for its performance.

30. The approach in Uruguay emphasized incentives and voluntary participation instead of job cuts. The special funds also helped provide limited technical support, business training, and small loans for civil servants who opted to start their own businesses in the private sector. Many of the laid-off employees received training and assistance in finding private sector employment, and many now provide services to the government—at lower cost—as private contractors (Constance 2002).

31. Public campaigns should explain choices; detail the government's priorities within sectors, between sectors, and between policy instruments; and address concerns regarding privatization strategy, regulatory strategy, and social policy. To ensure public perception of transparency, sales of state-run enterprises could be addressed separately in public campaigns. Too often, impending privatizations have been used by political rivals to create dissension and confusion among the population, as in Bolivia.

32. World Bank (2003b).