



Financing water: risks & opportunities

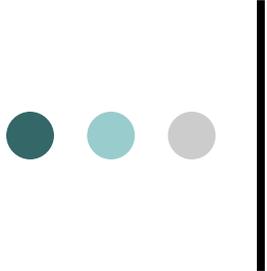
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Water-a risky business

- “Sutton & East Surrey [a UK water co.] has just changed hands and is now owned by Deutsche Bank. The Company said yesterday that it was facing ‘persistent drought’ and this was its biggest challenge” (“The Times”, May 2006)
- “Eminent domain issue hits RWE plans for American Water. For Germany’s largest utility company, RWE, expectations of soaring profits in the US water business are beginning to evaporate following spirited opposition to foreign ownership by local communities.” (Platts Global Water Report, July 2006)



Water-a risky business (contd.)

- “British business pays the third highest water costs in the world ...At \$1.90 per 1000 litres, Britain’s water costs less than Denmark and Germany, both about \$2.25...The US had the lowest costs at 66 cents per 1000 litres. ...The study found British business was paying 7.8% more for its water than last year and 32.3% more than in 2001...” (“Daily Telegraph”, 11 Aug 2006).



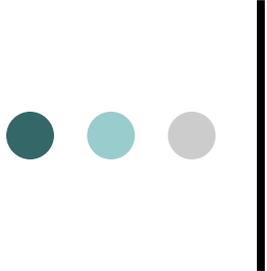
Water-related risks (WRRs)

- Commercial:
tariffs, cash flow, credit, market
- Political
expropriation, interference, devaluation
- Regulatory, legal, contractual:
laws, regulator, contract enforcement
- Water resource:
scarcity, reliability, pollution, flooding
- Reputational:
compliance, activism, ethics, hostility



Banks' exposure to WRRs

- Client categories:
 - Infrastructure & service providers*
 - Suppliers of equipment & materials*
 - Water –intensive*
 - All businesses*
- “..strong economic and market conditions and intense competitive pressures have encouraged financial firms to extend their risk-taking. This has pushed the financial system as a whole further up the risk spectrum” (Bank of England, July 2006)
- Basel II



How WRRs arise: Fray Bentos

- Two large European paper companies recently stated their intention to build a pair of huge pulp mills on the outskirts of Fray Bentos at a cost of US\$1.8 billion, which would be the largest ever private investment in Uruguay. The plans have aroused strong protest on environmental grounds, not least from Argentina, which borders the river on which the mills would stand, and which fears contamination of the river water. A Dutch bank, which is a leading advocate of the Equator Principles, decided to withdraw its support for one of the promoter companies, and Argentina has filed an official complaint before the International Court of Justice. The bank's action followed sustained pressure from international environmental campaigners. A second bank, which has also subscribed to the Equator Principles, is considering its position, pending an environmental impact assessment by the IFC, which is also planning to invest in the project.

(Source: "Financial Times", 12 June 2006)



How banks influence clients

“..few institutions are as well placed to encourage social responsibility as banks are. By integrating social, environmental and corporate governance objectives into their operations banks can have a huge influence on those they lend money to.”

(David Cameron, M.P., Leader of the UK Conservative Party, speaking at the *Financial Times* Sustainable Banking Awards ceremony on June 12, 2006)

Influence can be exerted through:

- portfolio selection
- relationship banking
- advisory services
- due diligence
- voting power
- Step In rights
- UN PRI



Sustainable banking

“Sustainability issues are very important for most banks. It started out being done for defensive reasons, to protect their brand, but more and more people tend to see this as a business opportunity.”

(Interview with Lars Thunell, Vice President of IFC, in *Financial Times* Special Report, June 12, 2006.)

- The Equator Principles
- Win-win projects & opportunities
- Water scarcity & pollution as drivers



WRRs: moving the agenda on

- Footprints, watertrails, water balances
- Sustainability indicators & diagnostic tools
- Rating & benchmarking
- Risk assessment & testing models
- Mainstreaming WRR assessment