Participant Handout

MODULE SIX: Financing

Overview of Financing for Sanitation

Market-based sanitation (MBS) aims to make products available that consumers want and can afford to purchase. However, there are consumers who cannot afford to pay cash. There are also entrepreneurs interested in expanding into sanitation products but lack access to financing or business development support. This module provides a better understanding of ways to implement MBS using financing, i.e., providing funds for individuals or businesses. We discuss typical financing mechanisms for sanitation, including subsidies.

Module 6 Objectives

As participants in this module, you will:

- Examine typical financing mechanisms used within MBS approaches
- Examine key factors when considering the use of subsidies

What is Financing?

Financing is the process of providing funds, typically for an individual or a business. It can be demand-side financing, such as consumer loans for households to purchase a latrine or supply-side financing, such as investment capital for a sanitation enterprise to grow its business. It is important to understand aspects of the business environment and broader context, such as what national policies exist on subsidies and financing.

Consumer financing can be very challenging for latrines and toilets since this is a non-income-generating product for a home to invest in. Unlike investment capital for a latrine entrepreneur, a sanitation loan is not directly linked to increased wealth. Therefore, many lending institutions are reluctant to offer consumer loans and, as a result, charge very high interest rates. The cost of managing small consumer loans can be so high that microfinance institutions (MFIs) are reluctant to engage in such programs. It is important to explore these ideas during market research (Module Three).

It can be fruitful to sync financing with seasonality. Many resilience food security activities work in agricultural-based rural economies. The affordability and willingness to pay may depend on seasonality and the flexibility of payment options available. Promotional activities should target the seasons when income is highest and people have cash at hand to purchase sanitation products.

There has been a lot of debate around the role of **subsidies** in sanitation. Implementers should consider four interconnected and overlapping elements when designing a subsidy program for market-based products and services: (1) form, (2) timing, 3) channel, and (4) amount.

Government policies, along with people's willingness and ability to pay, will have an impact on which financing mechanisms or approaches to subsidies you choose.

From a financial perspective only, there are two important factors that can influence willingness and ability to pay:

- **Affordability** is the relationship between the price of a product or service and the budget of its intended customers.
- **Liquidity** is the availability of cash to pay for products and services.

It is important to be clear about whether the challenge customers face is one of affordability or of liquidity. This will impact decisions made during program design and implementation.

In addition to consumer-side financing, projects can also consider business financing and support, which may take the form of:

- Subsidized training or business development services such as business planning, accounting, and auditing provided to enterprises involved in latrine sales, construction, and related services.
- Subsidized loans to small businesses allowing them to purchase start-up equipment and expand their operations.
- Subsidized hardware or sanitation supplies.
- Development of promotional materials and campaigns to generate customer demand for products sold by entrepreneurs.

Key Terms for MBS Financing

Business-side financing: Funding for a business when it is starting up or expanding.

Conditional cash transfers: Cash transferred to beneficiary, conditional on future performance of a measurable sanitation behavior.

Vouchers: Physical coupon for discounted (or free) specified hardware options or set cash amount redeemed at authorized businesses.

Purchase rebate: Paid to household that pre-finances toilet purchase, meeting prescribed criteria/quality after independent verification.

Microfinance institution: Organizations dedicated to providing financial services to low-income clients. They tend to focus on microcredit, though some MFIs also offer savings and remittance services. They are typically funded by external loans, grants, and/or investors and have staff members that regularly visit borrowers.

Village savings groups: When households group together, each putting aside small amounts of cash on a regular basis and taking turns getting the funds.

Non-income-generating loans: Loans for product purchases that do not generate increased income; latrines are a common example.

Willingness to pay (WTP): The maximum price at or below which a customer will agree to buy one unit of a product. According to the constructive preference view, consumer willingness to pay is a context-sensitive construct and thus potentially biased.

For more information and resources on MBS, visit:
https://www.fsnnetwork.org/PRO-WASH/Market-Based-Sanitation.

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