Proposal to nationalize all water gains support

Bachelet appears to back proposal to nationalize water via the Constitution

When we first reported it (April 28 – our note Senate group tables bill to nationalize water), we thought this initiative by a group of lawmakers aiming to give the State total ownership of all Chilean water resources would get little support, since the government has enough controversial proposals on the table, and would not want to foment further resistance from an already hurt business community. It now seems the State is supporting the proposal: Chile’s new president Michele Bachelet bolstered it with a mention in her first State of the Union address last week – promising changes to the Water Code, to make the resource a fiscal asset.

Main change: replacing water rights with concessions

The draft law in its present form would give the State absolute, exclusive, inalienable, non-terminating ownership of all water sources – including glaciers/snow – subject to statutory exceptions, while allowing mechanisms of private commercial operation. This would mean elimination of Item 24 of Article 19 of the Constitution, and replacement of today’s modus operandi (water use rights), with the legal institution of concessions. This concept frees the State from the burden of expropriation, while giving it control. The law would define water as a fiscal good – requiring the State to define and regulate its distribution, quantity, and quality to satisfy individual and collective needs. We see complex mechanics: as an example, the government would be responsible for dictating a balance between industrials, agriculture and individuals.

How to prioritize: when, how, who?

The proposal mandates authorities: (i) to prioritize water consumption; (ii) to provide potable water, and sanitation services; and (iii) to provide integral management of water basins and aquifers to improve efficiency. While these last two points would seem to imply the government establishing itself as a service provider, we think it likely that the State will leave that responsibility to the private sector – as it does now. Prioritizing water consumption is a tougher question – as Chile enters its 5th year of severe drought. In a dry year, we can imagine the government favoring, for example, the well-being of individuals at the expense of industries – and this type of value judgment having strong economic consequences for individual industries or sectors.

Losers? Water already scarce for mining

As we see it, this reform gives the government the legal power to dictate water distribution, with limited social damage – and indeed, with this, to boost its political capital. In an adverse scenario such as drought, we would expect industrials and the mining sector to be on the losing side, and they would have limited power to ask for a larger water allocation. On the other hand, companies think long-term when planning investments, and since variables of this type seem hard to forecast (uncertainty in budgeting), possibly this move might stimulate increasing investment in desalinization – though for the moment this is more of an alternative for those that can afford to pay.
Axes of the proposal

1. **The proposal has a constitutional nature:** It seeks to place in Chile’s constitution the concept of all water as a national asset for public use, in whatever form it occurs – liquid, gaseous, or solid (as in glaciers, ice and snow); and it seeks to give the State the power to direct or reserve flows – including surface flows or groundwater – in accordance with the overall interests of the nation. These interests would include, for example: national security; public utility; public health; and the preservation of the environment.

2. **Structure of rights; revocation / forfeiture:** It will aim to create legal structures and procedures for creation/constitution, specification, recognition, transfer – and also waiver, abdication, termination, and revocation/loss, of any rights to use of water that can be held by individual interests.

3. **Each basin a legal entity with a manager:** The proposal introduces the concept of an entity with the responsibility of manager for a specific water supply basin. This responsibility would include: strengthening the asset; and ensuring that river basins receive integrated management. Each river basin would be a public body, with its own legal identity, and assets. The organization, and other functions and duties, of these corporations would be established by law. There will be a need to decide on reallocation of existing powers and existing skills.

4. **Geography and resource availability:** Under the proposal, a specific law would lay down a framework governing use and commercial operation of water rights throughout the country, in accordance with the wide geographic and climatic diversity of the country’s various regions – with pointers for balance between use and availability in each case.

This is a wide-ranging idea – with, in our view, some interesting basic concepts; but with the usual potential risk of errors associated with efforts to decide matters of environmental planning – or any economic planning – by central or local government decisions. It has the added complication that water is becoming a key economic resource, and one that is – not only in Chile but perhaps increasingly in the rest of the world – the subject of strong and growing competition, and need. And this is without going into the political difficulties facing any regulator with discretion over allocation of public assets – and their potential for differentiated damage between sectors.
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<th>BTG Pactual Rating</th>
<th>Definition</th>
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<th>IB Services *2</th>
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<tr>
<td>Buy</td>
<td>Expected total return 10% above the company's sector average.</td>
<td>55%</td>
<td>46%</td>
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<td>Neutral</td>
<td>Expected total return between +10% and -10% the company's sector average.</td>
<td>41%</td>
<td>46%</td>
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<td>Sell</td>
<td>Expected total return 10% below the company’s sector average.</td>
<td>4%</td>
<td>0%</td>
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<th>12-mo rating</th>
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