European Centre for Development Policy Management
ecdpm

Discussion Paper

No. 131
July 2012

Common or Conflicting Interests?

Reflections on the Private Sector (for) Development Agenda

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www.ecdpm.org/dp131

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Acknowledgements

This paper was written by Dr. Bruce Byiers and Anna Rosengren from ECDPM. The authors would like to thank members of the Trade and Economic Governance team, with particular thanks to San Bilal, Melissa Dalleau, Quentin de Roquefeuil, Niels Keiser, and Paul Engel for useful comments and suggestions. Please send comments or queries to either author at bby@ecdpm.org and/or ar@ecdpm.org.

Acronyms

B2B	Business to Business
B4D	Business for Development
BCtA	Business Call to Action
BOT	Build-operate-transfer
BRIC	Brazil, Russia, India, China
CEO	Chief Executive Officer
CSR	Corporate Social Responsibility
EC	European Commission
ECDPM	European Centre for Development Policy Management
EEAC	European Environment and Sustainable Development Advisory Councils
ETTG	European Think-Tanks Group
EU	European Union
DANIDA	Danish International Development Agency
DCED	Donor Committee on Enterprise Development
DFI	Development Finance Institutions
DFID	Department for International Development
DGIS	Netherlands Directorate-General for International Cooperation
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
IFC	International Finance Cooperation
ITF	Infrastructure Trust Fund
MDGs	Millennium Development Goals
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
PCD	Policy Coherence for Development
PIDG	Private Infrastructure Development Group
PPPs	Public-Private Partnerships
PSD	Private Sector Development
PSI	Private Sector Investment
SIDA	Swedish International Development Cooperation Agency
SME	Small and Medium Enterprises
UK	United Kingdom
UN	United Nations
UNDP	United Nations Development Programme
UNICEF	United Nations Children’s Fund
USD	United States Dollar
USAID	United States Agency for International Development
WBCSD	World Business Council for Sustainable Development

Executive Summary

1. This Discussion Paper gives an overview of recent **donor commitments relating to the private sector and the questions these raise for development**, going beyond the rhetoric to thinking about the practical implications of such engagement.

2. **Commitments made at the Busan High Level Forum on Aid Effectiveness, G20 fora, in the European Union's Agenda for Change** and elsewhere all refer to **"leveraging" private sector activity and finance**, and improving the environment for businesses in developing countries.

3. It is useful to distinguish **between "private sector development" and engaging the "private sector *for* development".** While the **first is more focused on developing country *domestic* economies** and helping governments to design and implement policies to encourage economic transformation through investment, productivity growth, business expansion and employment; the **second relates more to donor engagement with *international* business activities and finance** to achieve development objectives.

4. This second area can be further broken down into i) engaging with **private sector *activity*** for development through encouraging productive investment, and ii) using public official development assistance (ODA) to leverage **private sector *finance***.

5. This represents a **broad agenda, raising a similarly broad range of issues** - to what extent **can the environment** in which very different firms operate genuinely **be affected through donor, developing country government and private sector initiatives?** And what are the political, financial, social, economic and reputational risks and potential benefits involved in investing in Africa either through finance or foreign direct investment (FDI)?

6. Although there are clear overlaps between the domestic and international private sectors, investment activities and finance, these **different forms of engagement operate through different channels, raising different questions and issues**.

Private Sector Development

7. The agenda for promoting **private sector development** is relatively well-established, with questions relating to how to **identify the true binding constraints to private sector development**, and **how to achieve and measure genuine policy impact.**

8. The high **costs of carrying out basic business transactions** in many developing countries have led to actions to improve the business environment. Other actions include **making credit accessible** to firms, particularly through Development Finance Institutions (DFIs), plus a range of multilateral and bilateral programmes and instruments such as **"challenge funds", equity funds and credit guarantee funds**. However, these have met with **mixed success.**

9. This relates partly to policy design and implementation, but also the **nature of firms** themselves. Even for similar firms, evidence suggests that **the conditions faced vary considerably within the**

same region, country, and sector, even where they formally face the same requirements and constraints.

10. A range of **basic management issues** may also determine firm success in developing countries. Relatedly, the **skills** required to run a **successful large firm** are different to those you need to work in a small firm, so successful firms often emerge from experience in other large firms having gained market knowledge and tested markets, etc.

11. It is also important to understand the **political economy of why some business sector reforms are undertaken or not in the first place**. Any process of economic transformation impacts on the **distribution of resources and therefore the interests of different groups**, thereby affecting reform processes.

12. All of this raises a number of **questions**. To what degree are the **formal and/or informal business environments** a genuine constraint to inwards investment? Given the differences across firms, ***who* genuinely benefits from regulatory reforms, and *why* are some potentially "easy" reforms not undertaken**? What are the **processes that can be used to engage the private and public sector** in dialogue to improve the business environment? What policies would genuinely **create linkages between local firms at the micro and small level with larger domestic and international** firms? How can we encourage greater **tax compliance while promoting firm growth** and investment? To what degree can and should **donors support industrial policies**?

Private Sector *Investment* for Development

13. While promoting the international private sector through public funds has the **potential to create jobs, raise productivity, produce spillovers of technology,** etc., there are clear **tradeoffs** that need to be made explicit and better understood, particularly in terms of commitments to **policy coherence for development and untied aid**.

14. **Some donors are more explicit than others**, but there is an apparent underlying **desire to use development finance to promote their own private sector**.

15. There is also **private sector interest in engaging with "the development sector"**. Quite apart from **seeking assistance** to target developing country markets, and despite generally **limited private sector participation in development policy discussions**, there is interest from businesses in the role that donors can play in **absorbing risk** and in **facing competition** from actors such as China, India and Brazil, among others.

16. Likewise, for donors the incentives goes beyond tied aid. The motivation is also to mobilize the European businesses so to make development more effective, which in the long run could ensure that the economic exchange between European firms and developing countries remains open, even with the emerging competition from the BRIC (Brazil, Russia, India, China) countries. A range of donor programmes therefore promotes **partnerships between donor country businesses and developing countries**.

17. The potential role of the private sector in achieving development goals through **businesses following their core business** is a key aspect of the surge in interest in engaging the private sector for development. In addition to pure economic interests, for some firms there is also a desire to

promote sustainable business, where the concepts of "good-will" and "business responsibility" act as strong incentives.

18. Many of the **benefits** of private sector activities apply **without development assistance**. The degree to which this occurs is likely to depend on a broad range of factors. For investments with public money, the starting **assumption must be that the investment would not immediately take place without the additional public funding**.

19. For future engagement it will be important to look **at particular donor programmes** and **draw general lessons from different cases in different sectors and countries** and the mechanisms at work that determine **development "success**" or 'failure".

20. An overriding concern here is the **lack of any commonly agreed guidelines for impact measurement guidelines.** Given the extensive ambitions and aspirations that are attached to this "new" developmental approach, it is important to understand whether these outcomes actually are realised.

21. There are also **challenges for private sector operators in collaborating with donor agencies**, including burdensome bureaucratic demands, high costs and slow pace in programme design and implementation. Are donors prepared to adjust procedures for working more closely with the private sector?

22. Further questions here relate to basic **definitional issues around when a private sector activity is "developmental"**, the **different impacts that different financing mechanisms and forms of collaboration** can have, the **factors most likely to accompany successful** partnership, and how to balance and **manage the risks** involved. Overall, it is a question of **how to ensure development and commercial interests are aligned.**

Private Sector Finance for Development

23. While development rhetoric makes frequent reference to **Public-Private Partnerships** (PPPs), there is **less analysis on the different forms these take and their related impact**.

24. Large **financing requirements** in areas such **as infrastructures and agriculture** combined with **declining ODA** have led to increased interest in involving private finance in development projects. However, this raises an additional set of questions to those raised by pure donor finance of private sector investment.

25. **An inevitable issue is the need for PPPs to be commercially viable,** with financial returns. As such, the majority of finance in existing PPPs goes to well-performing sectors such as telecoms, where commercial returns are likely to be high.

26. The need for financial return also impacts on the **level of risk private companies are willing to take, and therefore the balance of risk between partners in a project.** It is important to consider the **degree to which risk can be appropriately balanced between parties**, particularly where capacity levels, information available and interests may be quite different between developing country governments and private sector firms.

27. The issue of **risk and the contractual nature of PPPs** also point again to the business environment and need for a **robust legal environment**, while a great deal of technical know-how is also required for project preparation.

Key Issues Going Forward

28. The broad agenda implied by "engaging the private sector in development" heightens the **need for clarity on the potential implications of different focal areas, sources of finance, policy and financial instruments, policy objectives and ways of measuring impacts**.

29. There is a wide **array of stakeholders facing potentially very different incentives** depending on the precise **context of the project, the development objectives, the source of finance** etc. This is as important for policies on private sector development (PSD) in developing countries as strategies for engaging donor-country private sector.

30. **Profit and developmental objectives can be obtained together**, but more needs to be understood about where the alignment of interests takes place and the **degree to which donor finance can genuinely tip the balance** towards developmental outcomes.

31. **Measurement of impacts is important**, but also the **need to understand some specific cases where donors and private firms have combined for developmental effects**.

32. **We need to recognise the limits of what either party can actually do.** Still, if aid can tip the balance that reinforces the international private sector as a positive force for development beyond its role in investing and creating jobs, then this is to be welcomed.

33. **There is clearly scope for further analysis and discussion among relevant stakeholders.** Potential themes for discussion might include:
    - Understanding distinctions between impacts from "inclusive business" and from "subsidized" business
    - The need to better analyse the issue of standards for measuring development impact
    - The extractive industry and its interactions with development objectives
    - The practicalities of infrastructures financing, particularly at the regional level
    - How to link FDI promotion from donor countries with developing country industrial policy
    - How to link international investments with the local private sector
    - Sharing bilateral donor experiences to improve private-public dialogue and engagement
    - Lessons on improving domestic private sector performance
    - The role the European Commission (EC) and/or European Environment and Sustainable Development Advisory Councils (EEAC) could or should play in involving the private sector
    - The political tradeoffs between tax incentives and aid-assisted investments
    - The degree to which we can embrace experiments and failures in using donor-country tax-payer money.

34. Ultimately**, private sector operators and development policy makers come at "development" from quite different angles.** They need to learn each other's language, and understand their respective starting points and ultimate goals before common ground and approaches can really be found.

1. Introduction

A striking aspect in recent development discourse is the surge in references to "promoting the role of", "engaging" or "partnering" with the private sector for development. Commitments made at the Busan High Level Forum on Aid Effectiveness, by the G8 and in the EU's recent Agenda for Change, range from involving the private sector in designing and implementing development policy, to "leveraging" private sector activity and finance, and improving the environment for businesses in developing countries. This represents a broad agenda, raising a similarly broad range of issues - what are the political, financial, social, economic and reputational risks and potential benefits involved in investing in Africa either through finance or foreign direct investment (FDI), and to what extent can the balance of who gains what be affected through donor, developing country government and private sector initiatives?

While the focus on "private sector development" is nothing new, the increased focus from donors on engaging the "private sector *for* development" is more recent. This distinction between the two broad agendas is important for analysis. The more traditional policy area of "private sector development" is about helping governments to design and implement policies to encourage economic transformation through investment, productivity growth, business expansion and employment in developing countries, therefore focusing more on the *domestic* economy (although FDI clearly also benefits). The second, more novel form, relates to engaging with *international* business activities and finance to achieve development objectives. This second area can be further broken down into i) engaging with the private sector for development through encouraging productive *activities*, and ii) using public ODA to leverage private sector *finance*, a distinction that emerges in several of the policy pronouncements discussed below.[1] These distinctions are illustrated in Table 1.

Although there are clear overlaps between the domestic and international private sectors, forms of engagement operate through different channels, raising different questions and issues. There is long-standing recognition of the private sector's role in investing, creating employment, providing useful and innovative goods and services, and contributing to public coffers through taxation. The questions associated with promoting private sector development are therefore relatively well established, if complicated to address, and relate to how to identify the true binding constraints to private sector development, and how to achieve (and measure) genuine policy impact. But overall there is a broad consensus on the need to design policies to make economies conducive to investment and private sector activity.

The implications of involving the international private sector to achieve development goals are less clear. While promoting private sector development in developing countries through improving the business environment is sometimes seen as relatively neutral and non-interventionist, benefiting anyone who happens to engage in business, active promotion of international investment or finance clearly has the potential to raise conflicts of interest between development and commercial interests. While the increasing emphasis on its engagement for development may reflect a change in attitude from suspicion to belief in its potential development impact, declining aid budgets in the current economic crisis also have a hand to play, raising quite different policy issues and questions. These relate to basic definitional issues around what are the different impacts that different financing mechanisms and forms of collaboration can have?

[1] Although it is useful to distinguish the separate areas here in order to establish clarity, this is not to say that policy should look at each in isolation. Indeed, the opposite is true and the synergies between the local business environment and private sector development, international investments and finance should be considered an overriding concern.

What factors are most likely to accompany successful partnership? How can one balance and manage the risks involved? And how can one ensure that development and commercial interests are aligned?

Table 1: Forms of Private Sector Engagement

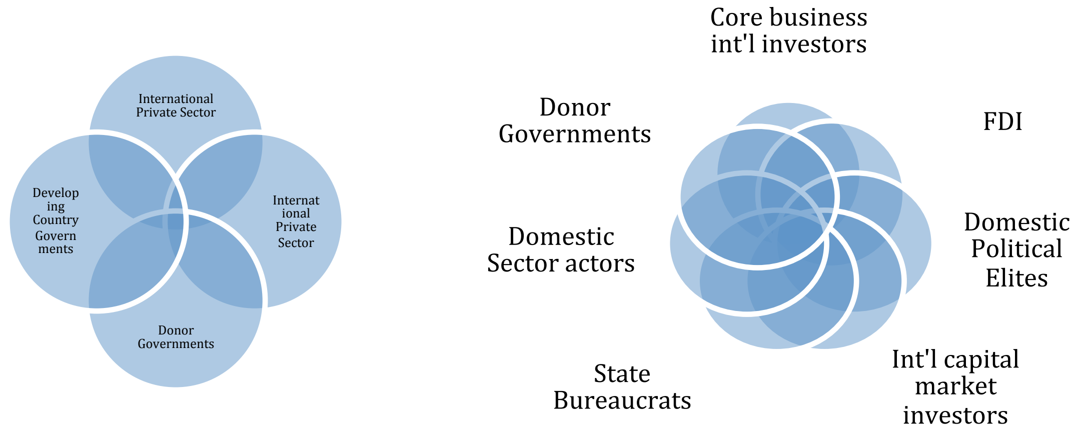
Private Sector Engagement			
	Private Sector Development	Private Sector *for* Development	
		Private Sector *Investment* for Development	Private Sector *Finance* for Development
Location	Domestic	Domestic/ International	International
Role of donors	Supporting the enhancement of the domestic business climate, credit etc	Encouraging private sector actors to make investments in developing countries by offsetting certain risks	Leveraging private sector to provide finance to development efforts
Types of Instrument	Challenge, equity and credit guarantee funds etc.	Challenge funds for Foreign Direct Investments, development-related grants and subsidies	Public-private partnerships, portfolio investment, private equity, private infrastructure funds etc.

There is also private sector demand for engagement with "the development sector". Quite apart from seeking assistance to target developing country markets, and despite generally limited private sector participation in development policy discussions, there is interest from businesses in the role that donors can play in absorbing risk, a key factor in countries that are characterised by high levels of economic, financial and political risk and high transactions costs. Donor assistance may also be effective in piloting specific private sector projects where the entrance costs are high with uncertain outcomes, thus opening the way for a range of commercial opportunities with development impact that might otherwise remain unexploited. Providing finance for large infrastructures projects in conjunction with donors may provide a degree of security. From this point of view, there are increasing questions from the private sector about how to get more involved.

While development objectives may be part of the story, the competition European firms face in Africa, from China, India and Brazil and elsewhere, also has a role. One European industry report on China states, for example, that in Africa "a broad range of industry sectors have been confronted with unfair competition, notably in infrastructure projects, energy, communication, transportation, but also in other sectors (cement, steel, machinery, agricultural equipment, metalworking, social infrastructure, etc.)" (BusinessEurope, 2011: 31). While an emerging players strategy of counteracting this by aligning development policy with industrial policy objectives may be an effective and justified response to this, the question remains the degree to which it is developmental or brings “developmental additionality”.[2]

This latter point relates to the need to be clear about tradeoffs, particularly with regards to donor commitments on untying aid and seeking policy coherence for development. This raises an additional set of questions. At what point does combining private with public funds become subsidy and tied aid, and to what degree is this acceptable? What development objectives are indeed better achieved through engaging the private sector than traditional aid? What are the opportunity costs of using donor funds to promote private sector activity? What degree of private sector failure is acceptable when using public money? The point where different interest and incentives align gets smaller and harder to identify the more actors are involved, something that Figure 1 attempts to illustrate. So how can one identify where interests indeed converge on developmental outcomes? These are all key questions that would benefit from further investigation and discussion among international and domestic private sector stakeholders, donors, and developing country governments.

Figure 1: How to identify align points of interest with a large number of actors?



Some of these issues, as well as further questions regarding the real outcome and impact of public-private cooperation, might be addressed by a coherent and comprehensive set of standards for impact measurements. The development of different forms of cooperation schemes should ideally be based on in-depth insights and knowledge on the actual affects, not only to ensure fruitful partnerships, but also to enable a better understanding of the participating actors and what factors are associated with “success”. Might a more standardised approach help to do this? While a number of different metrics exist, further discussion of what a standardised measure might look like could further enhance the role of the private sector in development.

This paper gives an overview of recent commitments relating to the private sector and the questions these raise, going beyond the rhetoric to thinking about the practical implications of such engagement. Although not exhaustive, it seeks to highlight prominent examples that raise issues for further analysis and discussion. Ultimately, the power of involving the private sector will lie in identifying where the interests of all stakeholders are genuinely aligned, and ensuring informed, wider stakeholder engagement within specific countries and sectors. To achieve this will require increased mutual understanding among stakeholders, greater understanding of where developmental and private sector

[2] Indeed, if the overriding goal is only to promote private sector development in developing countries, then the increasing involvement of the emerging players in Africa and elsewhere should also be welcomed by EU policy-makers to the degree that they contribute to development.

forces have been successfully combined in the past, and further, targeted, structured dialogue among private sector and development actors to avoid unrealistic expectations on either side.

The remainder of this paper is organised as follows. The following section summarises some of the main international commitments relating to private sector engagement in development. Section 3 then summarise the main issues and discussions relating to i) donor support to improving the business environment in partner countries, ii) some of the tools being used to engage with the private sector for investment and iii) issues relating to the combining private and public finances; while Section 4 concludes.

2. The Commitments

The new "conventional wisdom" that the private sector can play a greater role in achieving development outcomes is reflected in a range of international pronouncements on development policy. The Outcome Document from the Busan High Level Forum on Aid Effectiveness, the G20 Final Statement from Cannes in 2011, the 2010 Seoul Development Consensus for Shared Growth and the European Commission's recent Agenda for Change communication all highlight the need for more "private sector participation" for development (G20, 2011 and 2010; EC, 2011b).

In particular, the Busan Outcome Document states a commitment by all participants in the High Level Forum to:

> *"ensure a sound policy and regulatory environment for private sector development, increased foreign direct investment, public-private partnerships, the strengthening of value chains in an equitable manner and giving particular consideration to national and regional dimensions".*

It also refers to commitments to

> "*enable the participation of the private sector in the design and implementation of development policies and strategies", "further develop innovative financial mechanisms to mobilise private finance for shared development goals*".

And in terms of increasing engagement, the Busan Outcome Document refers to a need to:

> *"invite representatives of the public and private sectors and related organisations to play an active role in exploring how to advance both development and business outcomes so that they are mutually reinforcing" (*4th High Level Forum, Busan, 2011:10)

The European Commission's "Agenda for Change" refers to greater involvement with the private sector under five distinct headings that again relate to both "private sector development" and "private sector for development":[3] The specific relevant texts are presented in Box 1, highlighting again the different angles considered, but also the broad range of areas considered important for engagement.

[3] From the above five paragraphs, In terms of the three channels, domestic private sector development is discussed under points 1, 2 and 5, while points 2 to 5 also relate to the international (or perhaps more likely, the EU) private sector in terms of both finance and activity-related investments.

Box 1: Private Sector (for) Development commitments in the European Commission's Agenda for Change

1. "The EU should support the development of **competitive local private sectors** including by building local institutional and business capacity, promoting SMEs and cooperatives, supporting legislative and regulatory framework reforms and their enforcement..., facilitating access to business and financial services and promoting **agricultural, industrial and innovation policies**" (EC, 2011b: 8)

2. "In the same vein, crucial to developing countries' success is **attracting and retaining substantial private domestic and foreign investment and improving infrastructure**. The EU should develop new ways of engaging with the private sector, notably with a view to **leveraging private sector activity and resources for delivering public goods**. It should explore up-front grant funding and risk-sharing mechanisms to **catalyse public-private partnerships and private investment**." (EC, 2011b: 8)

3. "There is also scope for the EU to **work more closely with the private sector, foundations, civil society and local and regional authorities** as their role in development grows" (EC, 2011b: 3)

4. "**Public actors should forge partnerships with private companies, local communities and civil society**. Corporate social responsibility at international and national level can help avoid a 'race to the bottom' on human rights, international social and environmental standards and **promote responsible business conduct** consistent with internationally recognised instruments." (EC, 2011b: 7)

5. The EU should focus its support for **inclusive and sustainable** growth on:

- those sectors which build the foundations for growth and help ensure that it is inclusive, notably social protection, health and education;
- the enabling vectors for inclusive and sustainable growth, notably a stronger business environment and deeper regional integration;
- those sectors that have a strong multiplier impact on developing countries' economies and contribute to environmental protection, climate change prevention and adaptation, notably sustainable agriculture and energy (EC, 2011b)

More broadly, policies on Aid for Trade (AfT) also relate closely to issues of private sector development, particularly in relation to exports, and more recently, the use of blending with private sector finance for AfT projects. The AfT agenda emerged as an aid agenda at the World Trade Organisation (WTO) Hong Kong Ministerial Meeting of December 2005 based on a recognition and agreement from WTO members that to take advantage of improved market access, developing countries needed increased aid resources for investments in infrastructure, improved trade policy, and boosting productivity in key export and related sectors.[4] The priority areas therefore overlap with many of those being discussed more widely for engaging the private sector.

In addition to this proactive engagement in development policy by donor countries, there are clear overlaps with other policies. The EC's Agenda for Change recognises that "Development policy also helps address other global challenges and contributes to the EU-2020 Strategy", the EU's strategy for growth within the EU (EC, 2011b), suggesting that development policy might be used more proactively to promote EU businesses. The EU's SME Communication also talks of "Leveraging existing EU external policies to accelerate the international growth of European SMEs", while proposing that, "in line with the Joint Africa-EU Strategy, African countries in general should be invited to benefit from building on a strong partnership with EU SMEs (EC, 2011c). Further, in its most recent CSR strategy, the EC also puts forward

[4] Lui, Byiers and Van Seters (2012) provide an overview of some of the issues of applying "innovative finance" to Aid for Trade.

that "The search for synergies with the private sector will become an increasingly important consideration in EU development cooperation and in EU responses to natural and man-made disasters" (European Commission, 2011a: 15).

The above ambitions are also reflected at the level of individual donors. The UK Department for International Development (DfID) strategy document for private sector development states their ambition as: "*to bring private sector ideas, innovation and investment into the heart of what we do... In summary DFID's new approach to working with the private sector is to do more with private enterprise, extend the reach of our programmes with business into new areas and ramp up the value for money and impact of our private sector work"* (DFID, 2011b: 8). Value for money is a key underlying concern across a number of donors, with expectations that private sector engagement will provide more impact for donor money. DfID also states that it will "help sign-post business to partners, facilities and other Government Departments that may be of assistance" (DFID, 2011a: 2). This then suggests a facilitative role in bringing businesses into the development arena.

Some donors are more explicit than the EC or DfID, stating their expectation that development support also support their own private sector. For example, the Dutch government states that their policy framework and strategic plan is "*putting Dutch interest first, more so than in the past"* (The Netherlands MoFA, 2011: 1). In the description of Dutch Development Policy, it is moreover stated that "*Public-private partnerships, business instruments and economic diplomacy can lead to gains in both commercial profit and poverty reduction. A larger proportion of the development budget will be spent on instruments of this kind" (*The Netherlands MoFA, 2011a). Further, "*The Dutch government no longer plays the traditional role of financier, but sees itself as a full partner" (*The Netherlands MoFA, 2011b)

Similarly, Swedish Sida states that "it is in Sweden's as well as Sida's interest that Swedish businesses are suppliers in development assistance-financed calls for tender, in order to build reciprocal relations and to contribute to economic growth in partner countries as well as in Sweden." Sida staff are also urged to "*strive for cooperation with major companies since these tend to have a greater impact than small and medium-sized ones. In addition, many large companies are present and already working in many developing countries, which makes it possible for them to replicate new business models and approaches globally*". (SIDA, 2011: 9)

Danish development agency Danida also devotes special efforts to business cooperation with developing countries with a view to promoting Danish business. They state that "...*it is a strategic priority in Danish development cooperation to work for a stronger private sector. For Danida, it is important that Danish business participates actively in this endeavour."* (DANIDA, 2012: 1) While this declaration of interests might be commendable from the point of view of frank honesty, it nonetheless also raises some potential challenges for justifying that this meets development goals and other commitments on untied aid.

At the same time, most donors are committed to untied aid and ensuring Policy Coherence for Development (PCD). The European Consensus for Development of 2005 states Europe's "(…) *commitment to promoting policy coherence for development, based upon ensuring that the EU shall take account of the objectives of development cooperation in all policies that it implements which are likely to affect developing countries, and that these policies support development objectives.*"(European Parliament, EC and Council, 2005: 5). Further, Article 21 of Treaty on the European Union states that "*the Union shall ensure consistency between the different areas of its external action and between these and its other policies*", and Article 208 of the Treaty on the Functioning of the European Union, affirms that "*The Union shall take account of the objectives of development cooperation in the policies that it implements which are* *likely to affect developing countries*" (EC, 2011d: 10). More recently, the Busan Outcome Document again expresses the commitment to "accelerate our efforts to untie aid".

The following section looks in more detail at the three areas of I) promoting private sector development, ii) leveraging international private activity for development, and iii) leveraging international finance for development.

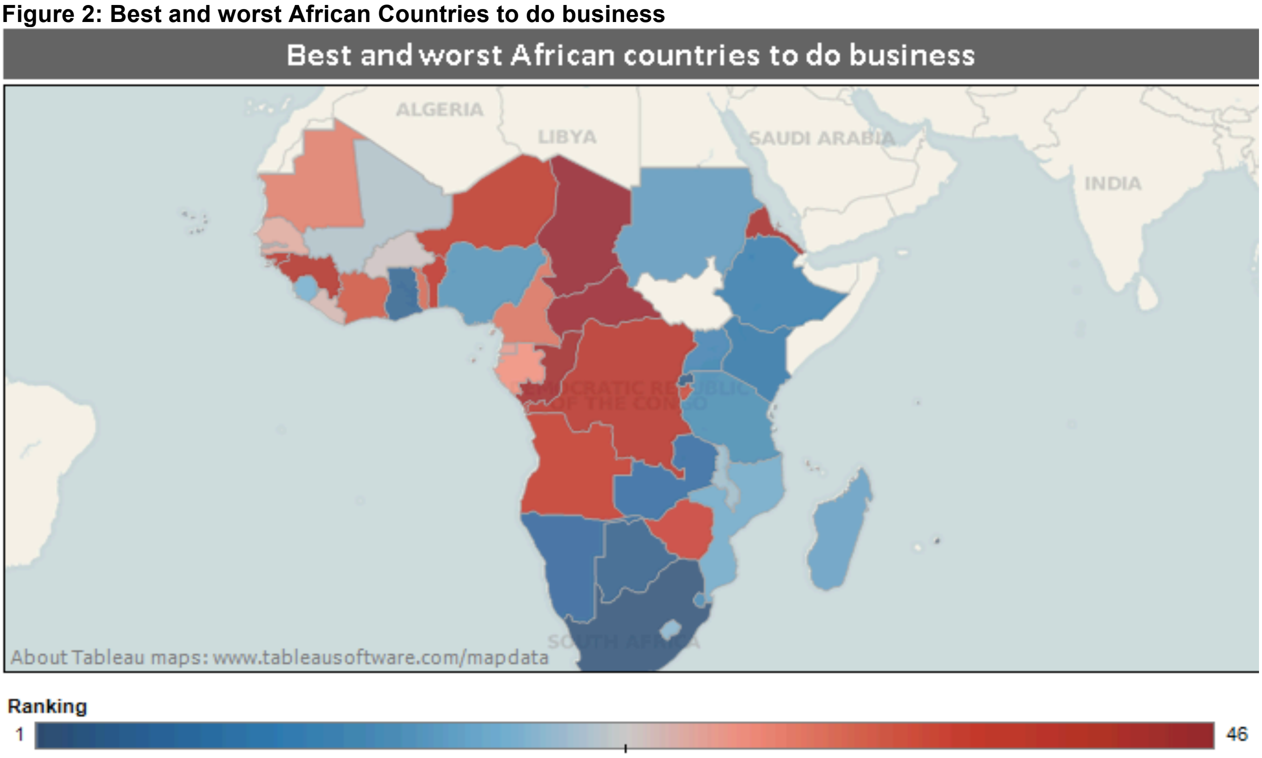
3. Actions & Issues

3.1. Private Sector Development

While economic growth is not sufficient for poverty reduction, it is nonetheless necessary, leading to broad consensus on the need to promote private sector development. Given that economic growth is not sufficient for poverty reduction, some highlight instead the need for economic transformation (Africa Power and Politics Programme et al., 2012). That is, growth must be accompanied by transition towards higher productivity activities and employment creation if it is to impact on poverty. Much of the emphasis on private sector development therefore stems from the premise that poverty reduction requires expanding job opportunities, growing incomes and demand, increasing supplies of goods and services, and tax revenues to finance public goods, all of which can be achieved through an expanding private sector. Although questions remain regarding the true binding constraints to private sector development and how to achieve (and measure) genuine policy impact, there is a broad consensus on the need to design policies to make economies conducive to investment and private sector activity.

As reflected in the commitments mentioned above, the high costs of carrying out basic business transactions in many developing countries have led to an emphasis on policies to improve the business environment. The focus has often been on regulatory reforms to lower the costs of doing business in developing countries through indicators such as the World Bank's Doing Business survey index. Although this may be imperfect in design, it has drawn attention to the procedures faced by businesses in different countries and received broad support across stakeholders. Maps such as that in Figure 2 highlight where reforms have been successful and to a degree put pressure on governments to at least keep up with neighbouring countries in order to attract investments and expand their private sector.

Figure 2: Best and worst African Countries to do business



Ranging from 1 = very good, to 46 = very poor business climate
Source: Kim, K. 2012, *Best and Worst Countries to Business in Africa,* The Global Post 4/06/2012
http://www.globalpost.com/dispatch/news/regions/africa/120523/best-and-worst-countries-do-business-africa-interactive

However, the effects of efforts to improve the business environment have met with mixed success. This may partly relate to the design and implementation of policy reforms, but also to this distinction between promoting growth and transformation. In response, the Donor Committee on Enterprise Development (DCED) is developing a standard for measuring the impact of business environment reforms (DCED, accessed 4/6/12) The focus aims to be both in terms of individual donor projects, and the contribution of specific reforms to enterprise growth, while the outputs will go someway to understanding what policies have worked where and to some degree, why.

But beyond the way reforms are designed, much of the issue of impact will relate to the nature of firms themselves. While firm ownership, nationality or sector are frequently blurred, it is nonetheless useful to distinguish between the many different types of firms that government policy is intended to promote in order to understand potential policy impacts. Some useful distinctions might be made between:

- agricultural smallholders,
- large-scale agricultural producers,
- micro/informal operators,
- commercial traders,
- manufacturers/processors,
- suppliers of international value chains
- extractive sector firms,
- national (monopoly) service providers,
- pure international (enclave) investments.

This incomplete list of categories highlights the likelihood that different types of firms operate in different ways and therefore face different constraints. But even for similar firms, evidence suggests that the conditions faced by firms vary considerably within the same region, country, and sector, even where they ostensibly face the same requirements and constraints (Pritchett and Hallward-Driemeier, 2011).[5] So even in “unfriendly environments” there are firms that successfully start up, survive, grow, and make profits in spite of (or because of) regulatory barriers and may even actively oppose reforms to lower the costs of new firm entrance. Understanding why this occurs and the characteristics associated with performance within this environment may then be as important as easing the regulatory barriers to doing business.

In this light, in addition to regulatory reforms, much emphasis is placed on making credit accessible to firms. While this can take the form of donors providing finance through Development Finance Institutions (DFIs), sometimes alongside funds raised on capital markets, to commercial banks and other intermediaries, a range of multilateral and bilateral programmes also provide instruments such as “challenge funds”, equity funds and credit guarantee funds for developing country private sector firms (Kwakkenbos, 2012; Perry, 2011). These work on the basis of competitive, commercial proposals, with investments selected on the basis of the greatest expected return.

However, there are a range of challenges here related to the degree of additional impact of such programmes. Very often, only relatively successful firms are in any case able and eligible to apply for such programmes while smaller firms either do not meet the criteria or have the capacity to meet requirements.

5 Pritchett and Hallward-Driemeier (2011) compare Doing Business (“de jure”) data with reported data from enterprises (“de facto”) on certain business procedures, such as the time taken to get a construction permit. They find enormous differences in the average "de facto" conditions compared to the "de jure" estimate from Doing Business estimates. They also find enormous dispersion in the "de facto" conditions suggesting enormous variations in conditions faced by firms.

Further, depending on the workings of the financial sector and potential investment returns from the private sector, donor funds channeled through the regular banking system often find themselves financing government bonds, not SMEs, while that which does reach firms often goes to firms domiciled in developed countries and tax-havens (Kwakkenbos, 2012). While this may not be problematic in itself, as much as it contributes to the economy and employment, it does also raise the possibility of high levels of profit repatriation and therefore limited development impact. Further, the assumption of such interventions is that firms are credit-constrained, something that may not be the case with firms also subject to issue of weak demand as well as weak initial business project design.

Beyond these issues external to the firm, research suggests that there are a range of basic management issues that determine firm success in developing countries. Bloom et al. (2009) carry out randomised control trials on firms in India with support provided to a group of firms to apply managerial practices related to basic quality control, inventory control and operational efficiency. They find that "improved management practices led to significantly higher efficiency and quality, and lower inventory levels, substantially increasing plants' productivity and profitability." (Bloom et al, 2009: 620)

It may also be that the skills required to run a successful large firm are quite different to those you need to work by yourself or with a single employee. Most medium sized firms in Ethiopia and Tanzania emerge from other medium sized firms, often in a different activity, not from successful small firms that grow (Sutton, 2011). As such, they are the ones capable of negotiating the market conditions, testing markets, and building on existing experience from, for example, operating as traders before branching out into manufacturing. While this offers more challenging policy prescriptions than regulatory reform, the basics of firm management and the mechanisms of success for existing firms in a complicated regulatory environment may be key to understanding how to promote the private sector more broadly.

It is also therefore important to understand the political economy of why some reforms are undertaken or not in the first place. Any process of transformation impacts on the interests of different groups. Whitfield and Therkildsen (2011) propose a framework resting on three propositions: i) political survival is a key motivation of governments; ii) keeping the coalitions required to stay in power leads to the choice of policy and how they are implemented; and iii) implementation also relies on an ability to create "pockets of efficiency" in the bureaucracy. (Whitfield and Therkildsen, 2011) To use this then requires an understanding of the institutional and political factors that drive private sector policy reforms, and that ensure that economic benefits flow to the wider population through employment, better governance and provision of public services.

While this is clearly an area that requires further examination, the framework that sees political elites motivated to ensure their political survival through policy choices has motivated other potentially related work. Besley and Persson (2011) suggest a model where political survival motivates investment in the legal system and taxation to reap the benefits of growth through taxation, while Collier (2009) discusses cases of active weakening of state institutions and the military to reduce the risk of being militarily dislodged from office (Besley and Persson, 2011). As proposed in a recent paper, in all cases it will be important to understand the interests and contexts of three main actors: the ruling political elite, state bureaucrats, and sector actors (from firms, farms, and households) (Africa Power and Politics et al, 2012). Understanding how a business-friendly regulatory environment emerges out of these actors' interactions is therefore of prime importance.

There may be some competing narratives here, then, that can be examined through studies of individual cases. This would examine where certain sectors of the private sector have successfully benefited from policy reforms. Further, the cross-comparison of this type of information with a more technocratic analysis of business environment reforms as discussed above may be singularly informative.

More fundamentally, what does a focus on economic transformation or "inclusive" growth imply? One interpretation is that the focus should be on raising employment opportunities for all. To what degree is this compatible with encouraging integration into global production networks and "defying" comparative advantage, as proposed by economists such as Chang?[6] What are the tradeoffs to be made, and should, for example, a large capital-intensive investment such as the Mozal aluminium smelter in Mozambique nonetheless be assisted or encouraged with development assistance for its demonstration effect for other large investments? This then goes considerably beyond moves to simplify business procedures towards more prioritised industrial policy and donor support to international companies, the topic of the next section.

All of this raises a number of questions. To what degree are the formal and/or informal business environments a genuine constraint to sustainable, long-term investment? Given the differences across firms, *who* genuinely benefits from regulatory reforms, and *why* are some potentially "easy" reforms not undertaken? Do lessons from emerging countries and from history offer any actionable policy conclusions? What are the processes that can be used to engage the private and public sector in dialogue to improve the business environment? What policies would genuinely create linkages between local firms at the micro and small level with larger domestic and international firms? How can we encourage greater tax compliance while promoting firm growth and investment? How can we assist firms in expanding their markets, either domestically or into international markets and value-chains? How much can donors genuinely do in certain political contexts? These are issues that related to the broader question of state-society relations, and institution building that relate to the "development question" more generally.

While promoting private sector development in developing countries can impact on domestic and foreign firms alike, the "private sector *for* development" agenda places particular emphasis on international firms.

3.2. Engaging the Private Sector *for* Development

While there is some consensus on the importance of private sector development in developing countries, there is considerably less clarity on what it means to engage with the international private sector for development. It may be that there is a need for more of the private sector mentality of "innovate or die" in the development world, while the blending of aid and investment, frequently employed by the Chinese in developing countries, is also pushing Western policy-makers to think along similar lines. However, there are also some concerns that should be addressed.

As mentioned, a distinction can usefully be made between engaging with international private sector "finance" and "activity" in addressing the above areas. Promoting *productive investments* ("activity") through support for foreign direct investment, linkage programmes between international and local enterprises, credit guarantee funds, equity investment, and other support for "inclusive", "bottom of the pyramid" or "core business" models targeted at local consumers, is likely to have different implications to encouraging the participation of private sector *finance* in development projects through portfolio investment, Public-Private Partnerships (PPPs), private infrastructure funds, and blending of grants and

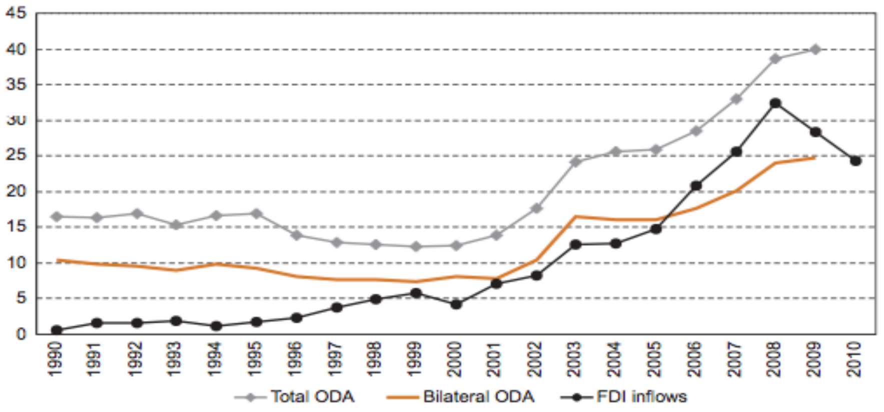
6 See the written debate with Justin Lin (Chang and Lin, 2009).

loans to governments.[7] The remainder of this paper does not go into detail on each of these but summarises some of the main issues relating to the two broad types.

Private Sector *Activities* for Development

The main issue in looking at how donor finance can combine with private sector *activities* is that of how to define development, and development additionality. What is required for a private sector investment to be considered developmental? At what point is it simply business, and at what point should it attract public money in the form of donor support and thus subsidy? And is subsidising activity "more developmental" than finance given the commercial presence and therefore potentially higher local engagement in the local economy? As can be seen in Figure 3, FDI has increased substantially during the last decades and surpassed bilateral ODA just before the outbreak of the financial crisis.

Figure 3: FDI inflows and ODA flows to LDCs, 1990-2010 ($bn)



Source: UNCTAD, 2011

Note: Data for 2010 are estimates

The potential role of the private sector in achieving development goals through businesses following their core business is a further key aspect of the surge in interest in engaging the private sector for development. Going beyond corporate social responsibility (CSR) and "good behaviour" principles such as those laid out in the UN Global Compact, there is increasing discussion of "inclusive business", or business aimed at the "bottom of the pyramid".[8] Broadly put, "inclusive business entails creating a net positive development impact through a financially profitable business model" (Wach, 2012: 8). This approach ultimately suggests that the core business should provide stakeholder value rather than mere shareholder value.

Ashley (2009) identifies four main types of "inclusive business". There are: i) commercial businesses selling goods and services that are needed by the poor and have high development impact; ii) large

[7] Kwakkenbos (2012) provides a concise list and description of different instruments. See also Dalleau and Bilal (2012).

[8] The then principles of the UN Global Compact relating to human rights, labour, the environment and anti-corruption are: 1: Businesses should support and respect the protection of internationally proclaimed human rights; 2: Businesses should make sure that they are not complicit in human rights abuses; 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining; Businesses should ensure 4: the elimination of all forms of forced and compulsory labour; 5: the effective abolition of child labour; 6: the elimination of discrimination in respect of employment and occupation.; 7: Businesses should support a precautionary approach to environmental challenges; 8: undertake initiatives to promote greater environmental responsibility; 9: encourage the development and diffusion of environmentally friendly technologies; 10: Businesses should work against corruption in all its forms, including extortion and bribery. UN Global Compact, "The Ten Principles": http://www.unglobalcompact.org/AboutTheGC/TheTenPrinciples/index.html

companies that have a significant impact on poverty in their daily operations and that attempt to increase their developmental impact through supply and distribution chains, or through research and development; iii) commercial domestic small and medium sized companies that, through their embeddedness in the local economy, have local economic development as an explicit driving force; iv) social enterprises that uses market mechanism and commercial models of delivery, rather than the traditional non-profit model of delivery (Ashley, C. 2009: 3) Because "inclusive businesses" target developing country as part of their core model, when, where and how to support each of these types of businesses with donor funds while avoiding unnecessary subsidy is a major challenge.

One major international initiative in this area is the Business Call to Action (BCtA). Supported by a number of donors, the BCtA challenges businesses to develop inclusive business models and to "engage low-income citizens as consumers, producers, suppliers, and distributors of goods and services" (BCtA, 2010: 2). In the opening speech of the "Business Call to Action" meeting in 2008, that hosted more than 80 of the world's leading CEOs, Gordon Brown and Kemal Davis (head of UNDP) clarified that "By signing the Declaration, CEOs and Chairmen are committing their company to take action through their core business in a transformative and scalable manner that will enhance growth and help meet the MDGs" (Ashley, 2009: 2) The Business Call to Action support member companies with linkages, advice and assistance in their pro-development activities, with 45 companies from a wide range of countries are currently involved in the project. Some of the target goals are, among others, to create 35.700 jobs, provide financial services to 18 million people and to improve access to clean water for 750.000 people (BCtA, 2010: 2).

Other donor-led examples include GIZ's DeveloPPP.de idea competitions. The PPP stands for public-private partnerships which are jointly financed, planned and implemented by development organisations and international companies. Here, European business sectors prepare public-private partnership proposals to compete for GIZ funding. They also have what is called the Africa Facility, a cooperation instrument for the promotion of development partnerships with companies based in Africa (GIZ, 2011).

Further, DfID has several challenge funds, among them the Responsible and Accountable Garment Sector, the Food Retail Industry Challenge Fund and the Haraket Challenge Fund. For example, the Food Retail Industry Challenge Fund provides up to US$ 401 000, on a cost-sharing basis to companies that are food retailers in the UK and that, in their work, promote supply chain development and livelihood improvement for African farmers. Other multi-donor challenge funds are e.g. the African Enterprise Challenge Fund and the Ghana's Business Sector Advocacy Challenge Fund (DCED, accessed 29-05-12)

As another example, The Netherlands has a Private Sector Investment Programme (PSI), which provides grants to partnerships between Dutch and local companies from developing countries. PSI contributes with 50 % to 60% of the project budget, with payment based on achieved results during the project period.[9] PSI is a tender programme and the eligibility criteria are that: i) a local company is an investment partner; ii) the investment is innovative for the developing country; iii) the investment is the first stage in a series of investments leading to growth of sales and employment after the project period; iv) the risks are high and commercial financing is not available; the project is commercially feasible, and; v) the project has significant positive impact on the local economy (Adam Smith International, 2009: 16). Further, a DGIS Development Cooperation Matchmaking Facility targets small- and medium-sized companies in emerging economies with the goal to stimulate joint investments together with Dutch companies.

[9] Standard PSI (50%): Africa, Asia, Central and Eastern Europe and Latin America. PSI Plus (60%): Sierra Leone, Afghanistan, Burundi, The Palestinian Authority and Southern Sudan.

The Danish Danida Business-to-Business programme (B2B) supports the establishment of mutually beneficial and long-term partnerships between companies from developing countries and Danish companies. This aims to develop the private sector in Danida's programme countries and in South Africa through creating linkages between local and Danish companies in which the local companies can get access to Danish technology and knowhow. The incentives for the Danish companies are that they "*...obtain access to new markets, products and production opportunities"* (Adam Smith International, 2009:19). Here, eligibility criteria include demonstrated improvements in the internal and external labour environments, job creation (especially for women) as well as other related CSR benefits such as e.g health, labour right and education benefits. A further PPP programme aims at promoting and supporting CSR partnerships and strengthening the competitiveness of developing countries' enterprises. To be eligible, the project must be consistent with the UN Global Compact principles.

Other mechanisms that exist are in partnerships between donors and private sector companies. An example is the multi-stakeholder cooperation between USAID, UNICEF, Bill and Melinda Gates Foundation and Unilever, that actively engages in promoting hand washing with soap so to reduce the risks for viruses that spreads diarrhea and respiratory infections. Apart from the broader developmental goals that this has the potential to achieve, it also provides an opportunity for Unilever to get access and recognition at new markets (Adam Smith International, 2009: 19).

For investments with public money, the starting assumption must be that the investment would not take place without the additional funding. How can a development policy-maker identify where this is the case? How can one identify the tipping point at which a commercially unviable investment becomes viable with financial assistance? Is aid then simply a subsidy and can we justify that in the current context of untied aid? Or does a dollar invested in a private venture provide considerably more benefit than it would do in building a school?

It is therefore important to understand what drives the development aspect of these investments in the first place. In some cases it is a lack of qualified staff; in others it is the potential for accessing larger markets while serving a social purpose. But what role does the aid genuinely play in these kinds of ventures? Is it a safety net, a "turbo-booster", or just a little extra cash to provide breathing space? The companies operating in developing countries as part of their core business, aiming at the so-called "bottom of the pyramid" include well-known multi-national companies. While this is not out of pure altruism, it serves to illustrate that "developmental gains" do not necessarily require public money. In these cases, what may be more important are reputation gains (and risks).

Clearly, some of the benefits of private sector activities apply with or without development assistance. The degree to which this occurs is likely to depend on a broad range of factors. These include: the sector - production, trade, extraction, services; the nature of the target market - local or foreign, intermediate or consumer; the size of the local market; the original purpose of the investment; the scale of the investment; the labour/capital intensity; the political process behind the investment; the competitiveness of the labour market; the tax incentives offered; the effectiveness of the tax administration; the nature of the contract/concessions; the reputational risk of the firm; trade preference margins to developed markets; the legal/regulatory environment; local ability to supply quality inputs regularly and cheaply; local political risk; local business environment; local crime rates; the fixedness of the investment; negotiating power of the firms vs. government; degree of regional market integration & preferential trade arrangements; profitability of the sector within a country; concern for development of the firm in question; political contacts; local market knowledge. All of these will impact on the developmental impact, the profit-risk balance, and the reputational pressure to ensure that business procedures are in line with developmental goals.

While some of these aspects relate to the country in question, others will be determined to the characteristics of the investment. To draw lessons it will be important to look on a case by case basis to draw general lessons from different cases in different sectors and countries and the mechanisms at work that determine development "success" or 'failure". For example, a major global brand such as Unilever, Philips or Gap is considerably more subject to reputational risk than a medium-sized European cement factory investing in Africa. In the latter, the issue may be more related to getting skilled workers through relationships and training with universities. Is this developmental? Does building a road to your factory or schools and hospitals next to it count as development? Should this receive public money? Under what conditions does providing an equity share in a local investment make sense to an investor? And what benefits are genuinely obtained from this?

Indeed, it is fundamental to recognise that businesses themselves are interested in promoting a better image in the local community and internationally. CSR Europe points visitors to a tool for companies to measure their "socio-economic footprint", that aims to help firms to "engage with local communities, enabling them to "maximise their positive impacts and manage negative impacts effectively" (CSR Europe, 2010). Business benefits being "looked for" include: "recruitment and retention, improved productivity, enhanced reputation, license to operate, stakeholder relations and employee engagement" (Business in the Community, 2012). Although this might be viewed cynically as firms simply eager to use development as a ladder to further profit and reputational gain, either through appeasing local communities or receiving favourable press, it nonetheless remains important that some (especially big) firms see engagement in development related issues as in their own interest. It also highlights the need for more objective measurements of development impact and analyses by outside parties from the companies themselves.

At a practical level, there are therefore a lot of questions to be addressed from a donor point of view, but also from the private sector. A report from 2011 highlights some of the challenges for private sector operators collaborating with donor agencies. These include: burdensome bureaucratic demands and high costs; slow pace in programme design and implementation; diverging languages and operational procedures; opposing or diverging objectives; and on occasion, hostility (UNDP, 2011). The same study highlights the frequently poor outreach to the private sector so that firms are often unaware of available support and programmes.

Similarly, in a report from an inclusive business dialogue held at the UN Summit on the MDGs in 2010, the following challenges were presented by the participating private sector: i) fear of failure: companies need to be willing to take some risks but also to be able to end a project that is not successful; ii) constraints on staff: the project might cause some constraints on the staff and they will need sufficient training, support and innovative room for maneuver; iii) profit pressure: many companies might run into situations where they have to balance between pressure for short-term profits for the shareholders, and long-term value creation; iv) practical challenges: new partners will pose new challenges related to issues such as language, payment systems, time horizons and risk management; v) financing: companies might find it challenging to find sufficient funding for their private sector engagement; vi) attitudes**:** breaking new barriers and introducing new business models always runs the risk of facing misunderstandings, scepticism and suspiciousness. (UN Global Compact, 2010)

As with the domestic private sector, it is important to also recognise the heterogeneity of the international private sector. Quite apart from their origins, and potential roles between finance and production, their sectoral and size distinctions may also have implications for their underlying purpose, development potential and ultimate impact. Distinctions might also be made depending on their role in global production networks as leaders or suppliers, the nature of their "home" country, and the characteristics of their target market.[10] Much is made in CSR circles of improving the supply-chain, again with reputation risks often in mind. This is also likely to be important in determining the degree to which private and developmental objectives can align.

A basic question put by the private sector at a recent private sector event was about who in the Commission to speak to about development related projects (Byiers, 2012). Is there someone they can make proposals to? Who can act as a sounding board? How should they "get involved" from Europe? Interestingly, the implications of the drive in development policy towards partner country "ownership" has meant that EU delegations, not Brussels, have most of the authority for working with partner country governments to design and implement development programmes. As such, most opportunities for the private sector may actually exist in the partner countries, with EU-based companies losing out.

In response, the EC has responded with a consultation on "a new EU Platform for External Cooperation and Development". "This Platform would look at how grant funds could be best used to in combination with loans and other forms of funding ("blending") from public and private organisations in order to support investments in line with EU external action and development objectives. The tasks of the Platform could include providing guidance to existing blending mechanisms and financial instruments, to streamline agreements, and promote cooperation and coordination between concerned parties" (EC, 2012). This may go some way to answering private sector concerns but will nonetheless need to be informed based on existing knowledge and experience of engagement with the private sector for development ends.

While the PCD agenda is clearly relevant for donors engaging with private sector activities, further commitments exist in this regard. According to the Policy Coherence for Development workplan 2010-2013, "*socially and environmentally responsible behaviour by foreign (and national) enterprises is particularly important, not only to ensure the sustainability of their own business activities over the longer term, but as a demonstration of good practice to host governments and local business. The Commission encourages European companies to adhere on a voluntary basis to internationally recognised guidelines for corporate social responsibility (CSR), for their business operations both within and outside the EU*." (EC, 2010:9). The question will be, how to make sure that any aid money to businesses goes beyond CSR.

Strikingly absent among the issues broached above, and in surveying some of the literature, is the absence of attention to developing country governments as stakeholders. To what degree are governments consulted as to the specific areas into which they would like to see any subsidised investment flow? In the case of PPPs, some suggest that discussions are primarily donor and private sector led, with a "questionable level of ownership by the partner country"(Kwakkenbos, 2012:10)

Neither does there seem to be any commonly agreed guidelines for impact measurement guidelines. Given the extensive ambitions and aspirations that are attached to this "new" developmental approach", it is important to understand whether these outcomes actually are realised? Many donor agencies have not yet conducted a major evaluation of their PSD activities. The Norwegian development agency, Norad, published an evaluation in 2010, finding among other things that "*Overall, over the last decade the PSD support has had mixed performance.... On the one hand, it has been effective in*

[10] An interesting discussion of Global Production Networks (as opposed to the more linear "value chains") can be found here: http://www.sed.manchester.ac.uk/geography/research/gpn/gpnwp1.pdf along with other papers here: http://www.sed.manchester.ac.uk/geography/research/gpn/gpnwp.htm.

*mobilising Norwegian enterprises in the development cooperation, especially small and medium enterprises (SMEs) and the Norwegian resource base in hydropower. On the other hand, it has not been provided in a comprehensive and coordinated way, or assured synergies. Nor has the support been effective in promoting trade and addressing the economic marginalisation of the poor countries" (*Norad, 2010:xvi). In light of the stated aims to provide economic opportunities and increased trade and job creation, from this evaluation it seems that the greatest beneficiaries so far have been the Norwegian companies. The evaluation further states that: "*The weakness in policy coherence is not due to poor performance by the various implementing organizations, but an apparent gap between policy and implementation (Ibid).* This difficulty in balancing profit and development could possibly act as a barrier in the formulation of comprehensive, coherent and efficient donor strategies for PSD.

Several large international companies evaluate their own business initiatives for development. Four main methods are being deployed by companies in their reports on activity impact in developing countries. These are:

- Livelihoods impacts and stakeholders views of initiatives assessed by the company e.g. SABmiller assesses supply chain benefits of the poor.
- Enterprise and poverty impact of the value chain as a result of the initiative e.g. Unilever/Oxfam assessment in Indonesia of the global value chain.
- Economic contribution to GDP and/or multipleir effect of the initiative e.g. Unilever assessment of economic footprint in South Africa.
- Using a scorecard of indicators e.g. Barclays Bank, Diageo reporting on company performance internationally. (Adam Smith International, 2009: 32)[11]

The purpose and use of these reports and assessments are not always clear. For example, the World Business Council for Sustainable Development (WBCSD) have outlined a " Measuring Impact Framework Methodology" intended to provide companies with tools to better understand their own contribution to development and thus be able to hold more informed and "more convincing" discussions with their stakeholders (WBDC, 2010). The question is whether an impact assessment should strive to find as positive results as possible, to be presented to potential consumers, donors or stakeholders, or if it should rather try to assess the real impact in the local communities and in that, also try to highlight potential problems, weaknesses and fault lines. Clearly this is an area where commercial and developmental interest may not be fully aligned.

While there are clear overlaps between promoting private sector engagement for development through investment activities and finance, there are nonetheless some distinguishing issues.

Private Sector *Finance* for Development[12]

Large financing requirements in areas such as infrastructures have led to increased interest in involving private finance in development projects. While Ghana and Gabon both succeeded in raising funds on private capital markets in 2007, and Senegal in 2009 and 2011 (US$750m, US$1bn, US$200m and US$500m respectively), many African countries have no access to such markets, and for those that have there are risks in terms of debt sustainability.

[11] Alternatively companies report their activities by using fixed international indicators, e.g. that provided in the Global Reporting Initiative. However, since they are easily understood by the broader public they have some important advantages. The primary indicators are: i) labour practices, including child and forced labour; ii) community investment; iii) anti-corruption actions; iv) investment and procurement practices, and; v) environmental good practice *Ibid.*

[12] This section draws on Lui et al. (2012) and Dalleau (2012).

Combined with declining ODA, this leads to increasing interest in using aid to leverage private sector finance through "blending" (**Cheikh et al, 2010).** Private sector involvement in the form of portfolio investment, private equity, private infrastructure funds, Public-Private-Partnerships (PPPs), etc. are therefore increasingly regarded as a potential mechanism to release public debt pressures on African governments already engaged in efforts to mobilise more domestic public resources. Moreover, as they bring on board private sector expertise and technical know-how, PPPs in particular, might also help ensure more efficient project design and service delivery, and help spread the risks that large-scale infrastructure projects may entail.

However, combining donor finance with private finance raises an additional set of questions to those raised by pure donor finance of private sector investment. These relate to the degree and balance of risk, the complexity of putting legal conditions in place to allow Public-Private Partnerships, capacity to negotiate deals to arrive at an appropriate balance of risks between public and private partners, the difficulty of ensuring government development priorities can be met through profit-oriented projects, and ensuring value for money.

While development rhetoric makes frequent reference to Public-Private Partnerships (PPPs), there is less clear analysis on the different forms these take and the impact they can have. A recent report details a sliding scale of private involvement and risk ranging from 'publically owned enterprise' to 'privatisation' (BMZ, 2011). In between are the different PPP models including performance based contracts service, operate and management (O&M) contracts, leasing and affermage, build-design-operate (BDO) models, build-operate-transfer models (BOT) and build-own-operate models (BOO).[13] As Table 2 illustrates, these all have different implications in terms of the source of investment and the allocation of the risk burden between public and private, and therefore also on potential development outcomes.

Table 2: Characteristics of alternatives forms of PPPs

	Operation & maintenance	Ownership	Investment	Commercial risk	Duration (years)
Management support	Public and private	Public	Public	Public	1-2
O&M	Private	Public	Public	Public	3-5
Leasing	Private	Public	Public	Semi-private	8-15
Concession	Private	Public	Private	Private	20-30
BDO	Private	Public	Public	Private	20-30
BOT / BOO	Private	Public / private	Private	Private	20-30

Note: Operation and Management (O&M), Build Design Operate (BDO), Build Operate Transfer (BTO) and Build Own operate (BOO)[14]
Source: OECD, 2005

There are some cases of large-scale projects that are gathering momentum, particularly in infrastructure. This is above all because of the sheer volume of finance believed to be required to meet African infrastructural needs, and the estimated drag on productivity that current gaps are estimated to create. At the same time, the sector has traditionally had a high level of private sector involvement in the

[13] Affermage is a construction where the private sector is remunerated via fees paid by governments rather than from tariff revenues collected from customers. See OECD (2005) for a more detailed description of these different models.

[14] The private O&M is responsible for the daily maintenance and service of the facilities, and may also in some cases be in charge of the operational procedures. The BDO is responsible for the design, construction and operation of publicly owned facilities for a fixed period of time. The BOT designs, finances and builds government owned infrastructure. BOO is similar to BOT, but in this case the private investor holds the control and ownership of the project (OECD, 2005).

delivery of projects through government procurement, while complex structured financing arrangements are more common or expected in large infrastructure projects, alongside other supporting financial products such as risk guarantees. Public-Private Partnerships are also seen as a more likely model for large infrastructure investments than perhaps for other areas.

Indeed, the G20 Cannes statement highlights the need to focus private sector engagement on infrastructures, agriculture and promoting a conducive environment for Public-Private Partnerships (PPPs). An example of this in practice is given by the Private Infrastructure Development Group (PIDG). This is a multi-donor organisation funded by Ireland, Austria, The World Bank, IFC, Germany, Switzerland, the UK and Sweden. The PIDG has set up several instruments and facilities that provide a wide range of financial, practical and strategic support mechanisms with the aim to increase investments into development promoting businesses and ventures (DFID, 2012). Another example is the EU-Africa Infrastructure Trust Fund (ITF), which combines its own grants with non-concessional loans from the development banks of EU member states for regional infrastructure projects in Africa, with African governments also playing a project role in the selection process. For the most part, the grant element has been applied as either technical assistance or an interest rate subsidy. ETTG research finds that 1 unit of grant in this form can leverage 5-6 units of loan (from the lead development banks) and 15 units of other finance (ETTG, 2011).

At the 2008 and recent 2012 G8 Summits, donor countries also committed to support agriculture. Further, in November 2011 the first Grow Africa Agricultural Investment Forum was held in Dar-es-Salaam, Tanzania with the theme of 'Scaling up Public-Private Collaboration for the Transformation of African Agriculture'. (Grow Africa Agricultural Investment Forum, 2011) The aim of the event was to 'expand partnerships, integrate best practice and catalyse investment' within 'a new paradigm of public-private collaboration for transforming African Agriculture'. However, with specific proposals still at an early stage it is as yet too early to say whether the Grow Africa initiative can deliver on its initial promise. It will be of particular interest to see how 'Public-Private Partnerships' in agriculture develop beyond the dialogue and policy levels (e.g. working together to identify potential investment areas), for example into contractual arrangements seen in sectors like infrastructure.

Notwithstanding, and despite the relative newness of engaging private sector finance in development projects, 'results to date with PPPs have been mixed, with lessons yet to be learnt and applied" (OECD, 2011). In particular, experience with management and affermage contracts has apparently been disappointing with expected efficiency gains not materialising as contract incentives could not overcome deeper institutional weaknesses (Gantsho, 2010). Indeed many governments are either lacking capacity or hesitant to fully embrace the idea and establish the conditions for success, with specific issues for example in the pricing of basic services (OECD, 2011). This begins to point to some of the constraints being faced.

An inevitable key constraint is the need for PPPs to be commercially viable, with financial returns. According to one analysis of World Bank's data on private participation in infrastructure projects, the majority of finance goes to well-performing sectors such as telecoms, where commercial returns are likely to be high (Jones, 2009). Updating this analysis shows that the situation in recent years has continued this trend, with close to four-fifths of completed projects over the 2005-10 period (by value) being in the telecoms sector, and only 7 per cent in energy (PPIAF, 2011). Clearly this raises questions about the degree to which public and private interests are compatible.

The need for commercial return, also impacts on the level of risk private companies are willing to take, and therefore the balance of risk between partners in a project. While risk is confronted daily by the private sector and incorporated into their decisions and planning, this is arguably less so in the development community. At the same time many of the projects associated with PPPs, in particular for infrastructure, are projects entail a high level of inherent commercial or political risk. While it may therefore make sense to encourage innovative approaches that alter the commercial terms of a project to offset some of that risk, it is important to consider the degree to which this can be appropriately balanced between parties. This is of particular importance where capacity levels, information available and interests may be quite different between developing country governments and private sector firms.

Apart from the capacity to negotiate contracts, the issue of risk and the contractual nature of PPPs also point to the need for a relatively robust legal environment. Poorly defined land tenure and property rights, unclear regulatory requirements and procedures, as well as hurdles to establish legal relations between governments and the private sector, may limit the possibilities of infrastructure projects getting off the ground and/or their financial/commercial viability in the long run. Partly in response, a number of initiatives are currently underway to strengthen the regulatory framework in Sub-Saharan African countries including the drafting of 'PPP laws'. Without strong regulatory institutions, implementation and enforcement mechanisms in place, there is little legal recourse for governments to take if a project does not deliver, while private sector companies may refuse to carry more risk precisely due to a perceived lack of legal protection.

While this requires government capacity to carry out reforms, a great deal of technical know-how is also required for project preparation. Identifying viable projects, conducting feasibility studies, and bringing them to a bankable status is a process requiring considerable preparatory work, which, apart from raising capacity demands, also frequently implies large upfront sunk costs. These typically range from 6 to 9 per cent of total project costs in infrastructure, for example (if not more in the case of PPPs). A number of project preparation facilities and support services have recently been set up to meet this challenge. However, African countries and regions still often lack both the resources needed to roll out services on such a large scale and the local professional expertise on those legal and financial structures that is required for initiating and managing such projects.

But underlying discussions of PPPs is the assumption that a lack of finance is the binding constraint. In some sectors such as infrastructures, this ostensibly seems to be the case with infrastructure gaps in Sub-Saharan Africa estimated at approximately US$93bn a year (Foster and Briceño-Garmendia, 2010). However, recognising that "when people change the way they use resources, they change their relations with each other", political will and specific interest groups may also affect the degree to which additional finance really resolves the issue (Leftwich and Hogg, 2007). Given the cross-border nature of many infrastructure projects, basic issues of political will to promote regional integration may also represent barriers to pushing such projects forward. Combined with issues of capacity and the need for commercial return then, the potential for achieving developmental goals through private sector engagement is far from simple.

4. Conclusions

The increasing rhetoric on engaging the private sector for development implies a very broad agenda. This heightens the need for clarity on the potential implications of different focal areas, sources of finance, policy and financial instruments, policy objectives and ways of measuring impacts. As the overview provided in this paper shows, there is a wide array of stakeholders facing potentially very different incentives depending on the precise context of the project, the development objectives, the source of finance etc. As was raised at the outset such a broad agenda involving such an array of stakeholders raises a range of questions - what are the political, financial, social, economic and reputational risks and potential benefits involved in investing in Africa either through finance or FDI, and to what extent can the balance of who gains what be adjusted through aid/blending/loans? Indeed who are we talking about when we discuss the “private sector”?

If development is the overarching goal, then the focus has to be on how to raise employment and productivity in developing countries and to gauge the impact of any additional donor dollar. If aid can tip the balance that really turns EU private sector into a positive force for development beyond its role in investing and creating jobs, then this is to be welcomed. This goes to underline that measurement of impacts is important, but needs to go beyond corporation self-assessment for CSR purposes. Even issues of local ownership, strategically taken as part of risk management, need to be considered from a more concrete development perspective, based on some clear criteria.

While it is perhaps healthy to have some honesty about the desire to benefit developed country firms, development commitments imply that the implications must be studied in more depth. Profit and developmental objectives can be obtained together, but more needs to be understood about where the alignment of interests takes place and the degree to which donor finance can genuinely affect the risk-balance faced by investors, financiers and recipient countries. Developing countries may not always be well placed to avoid carrying all the downside risk in terms of financial deals or indeed welcoming FDI. Similarly, development finance should not simply be a channeling of funds to the EU private sector in the hope that some finds its way to improving welfare in developing countries.

We may also need to understand the limits of what either party can actually do. There is an expectation from some in the private sector that donors such as the EC could or should help resolve “governance” problems for EU companies in developing countries. But development policy-makers and researchers have for decades been, and still are, grappling with how to use development finance and trade policy to promote the effective rule of law and to create more effective states in general. Indeed, this is the development question. The EC is limited in how much it can do with its existing tools, something the private sector must understand. Nonetheless, greater engagement and understanding from both sides may reveal novel ways of addressing governance and other issues through collaboration.

Given all of the above there is clearly scope for further analysis and discussion. Potential themes for discussion might include the EU private sector involvement in, and developmental aspects related to:

- Understanding distinctions between impacts from “inclusive business” and from subsidised business
- The extractive industry and development drivers
- Infrastructures and financing, particularly at the regional level
- Linking FDI promotion from donor countries with developing country industrial policy
- Linking international investments with the local private sector
- Sharing bilateral donor experiences to improve private-public dialogue

- Lessons on improving the investment climate for *new* investors
- The role the EC and/or EEAC could or should play in involving the private sector
- The political tradeoffs between tax incentives and aid-assisted investments
- The degree to which we can embrace experiments and failures in using donor-country tax-payer money.

Ultimately, private sector operators and development policy makers come at "development" from quite different angles. They need to learn each other's language, and understand their respective starting points and ultimate goals before common ground and approaches can really be found.

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This publication benefits from the generous support of ECDPM's core and institutional funders: The Netherlands, Belgium, Finland, Ireland, Luxemburg, Portugal, Sweden and Switzerland.

ISSN 1571-7577

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