ICA Briefing Note
March 2009

Investment Climate Assessments - an innovative tool used to evaluate the competitiveness of the private sector and identify ways that firms can improve productivity - have been a key component of the World Bank’s development efforts around the world. ICAs will remain an important instrument for diagnosing barriers to private investment at the country level, and going forward the Bank plans to expand use of these assessments in the Africa Region.

The ICA’s strength lies in its standardized methodology, which allows for meaningful comparisons across countries. In particular, the ICAs have been instrumental in showing how indirect costs, such as electricity, transportation and red tape, plague Africa’s competitiveness by imposing a penalty of close to 30% of sales on African firms as compared to Asian competitors.

ICAs are the voice of the firms. The results of the ICAs have been widely publicized and discussed at the highest levels of governments (for example, at the President Investor Councils). As such, they have given a strong voice to all the key segments of the private sector, including formal and informal SMEs, large multinationals, exporters, firms located in Special Economic Zones, women-owned firms, firms with indigenous owners and owners of foreign origins, and firms listed on stock markets.

Demand for ICAs
Policy makers, the private sector and the donor community are all increasingly demanding ICAs. Policy makers demand an assessment of their investment climates as part of their private sector development strategies. In response, Country Directors express interest for an ICA and fund the analysis. In recent years, the Country Directors from Congo, Cote d’Ivoire, Guinea, Guinea-Bissau, Lesotho, Liberia, Madagascar, Mali, Mauritius, Senegal, Sierra Leone and Sudan set aside funds for investment climate assessments. In several cases, the government and the Country Director solicit funds from the donor community to fund both the survey and the ICA. The Governments of South Africa and Mauritius are themselves co-financing their enterprise surveys and their ongoing ICAs. ICAs are also increasingly demanded as a tool to measure progress over time (surveys can be conducted regularly using panel data) as well as to benchmark a country’s performance against others from within and outside Africa (the core survey is now standardized across the world). Funding is available within the Bank in the FDP anchor to pay for data collection for some countries under the Bank’s Enterprise Surveys Initiative. The Africa Region makes use of this funding when country demand coincides with the countries selected by the initiative.

ICAs as a tool for Re Engagement

KENYA: In 2003 the ICA was conducted as part of the first step in the Bank’s re-engagement with the country and was an important building block of analytical work supporting subsequent policy reform. Key constraints identified by the ICA were further analyzed by an Administrative Barriers Report that focused on regulatory and other impediments, and by a Competitiveness Report that examined specific policy constraints at the sector level through value chain analysis. These diagnostics together underpinned a major effort by the Government, supported by the Bank and FIAS, to improve the investment climate through simplification of the business-licensing regime, which identified some 1,300 redundant or overlapping licenses, and through measures such as the liberalization of the institutional framework for the coffee sector in 2007. An updated ICA was completed in 2008, and its findings are supporting the ongoing policy dialogue between the Government and the Private Sector Donor Group, which is co-chaired by the Bank.

2. An Enterprise Survey in Africa can cost between US$50,000 and US$125,000.
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Impact of ICAs
Policy makers have used ICAs to generate strong awareness of the need to improve on key areas of their investment climates. ICA dialogue often involves high-level policy makers and various stakeholders of investment climate reforms. Recent ICAs show traction around key policy issues – Kenya’s well-known regulatory guillotine, South Africa’s emphasis on skills and competitiveness, Mauritius’s regulatory reforms, Nigeria’s state-level investment climate reforms, and Burkina Faso’s business regulation reform. ICAs have fed into the policy content of the Bank’s operations and technical assistance, and often define investment climate pillars of country-level reform programs. The policy issues and reforms highlighted by ICAs across Africa have been associated with an aggregate of US$1,100 million of lending to African countries from 2002 to 2008. ICAs have spurred reforms in many countries, including those where the World Bank has historically modest lending programs, such as South Africa and Botswana.

Added Value of ICAs
ICAs are not the only diagnostic tool for improving the understanding of the business environment, but they bring an important new dimension to the process. For example, the Doing Business rankings are effective at inspiring and prioritizing needed reforms in the areas covered by the Doing Business indicators. Doing Business indicators only reflect symptoms of underlying problems, but cannot diagnose the actual problems nor identify the cure. The ICA complements the DB indicators by helping to prioritize reforms across a broader spectrum of investment climate issues.
ICAs (in conjunction with industry level analysis such as value chain analysis) can also identify the effect of investment climate constraints on real economic outcomes and firm performance. Because such analyses are fairly detailed, recommendations on constraints and priorities can be more precise.

Lessons learned from the ICA data
There are certain conclusions that arise consistently in ICAs undertaken in most of Africa. These findings have informed our Africa Action Plan as well as our policy dialogue on private sector development. For example: High indirect costs and losses are dampening the productivity and competitiveness of manufacturers in Africa – often higher than labor costs at 20-30% and further widening its productivity gap with other regions. Poor port performance and slow customs procedures partly explain why manufacturing firms in Sub-Saharan Africa are less likely to export than firms in Asia. Firm level competitiveness can seriously be enhanced by improvements in the business environment; “Factory-floor” productivity in Africa is not that low compared with China, but when indirect costs such as power supply, transport, telecommunications and security are factored in, Africa’s productivity falls to very low levels.

3 For all projects with a significant PSD component, as categorized by the FPD Sector Board.
ICAs and competitiveness benchmarks

The Bank has vigorously supported a strong, consistently applied methodology for enterprise surveys to ensure a high-quality data base and the ability to compare results across countries. This was the basis for the original corporate decision to use central funding to pay for surveys and updates on a regular basis. Now the Bank has in place a strong, comparable multi-country enterprise panel data set. The Africa Region has drawn on these cross-country data by developing benchmarks for competitiveness for over 30 countries in the continent. This benchmarking exercise has been recognized in our contributions to the Africa Competitiveness Report (in partnership with the World Economic Forum). Recently, the African Union has expressed interest in a partnership, in which the Bank will be a key contributor. Due to the use of standardized core questionnaires and panel data, ICAs can also be used as monitoring devices to measure progress over time in addition to across countries.

ICAs as a tool for Reform

NIGERIA: The sub-national ICA has highlighted the cost impact of poor infrastructure on the competitiveness of enterprises and pointed out the deficiencies in access to finance. As a result of the analysis, the Federal Government has formally extended its PPP governance and financing platform to state-level institutions. States now can prioritize their reforms and redeploy development assistance with more accurate targeting for removal of key constraints to growth and competitiveness, without waiting for consensus on national-level policies.

ETHIOPIA: The ICA has been a crucial factor in maintaining a very challenging dialogue on the need to improve and open up the investment climate in Ethiopia. Extensive consultations have taken place with policy makers, the private sector, women entrepreneurs, and diaspora (the Ethiopia ICA gave special attention to gender and the diaspora). The ICA has highlighted the importance of improving access to finance, more open approaches to industrial policy and a more level playing field for all enterprises, particularly in the context of entry barriers posed by endowment-owned enterprises. A positive development has been a recent request by the Government (with its full support on data gathering) for a study on the role of endowment-owned enterprises and their economic impact. The ICA policy dialogue in Ethiopia illustrates both the difficulty and benefits of continuously engaging policy makers who remain reluctant to introduce major investment climate reforms.

BURKINA FASO: To set the stage for reforms, the ICA findings were used for the CAS progress report as well as for PRSP update. The ICA then fed into the investment climate component of the ongoing PSD Project and was used for the restructuring of the project to support reforms. For example, one-stop shop business registration resulted in a reduction of nearly a third the time required to start a new company. Company registration costs have dropped 60%. The ICA findings, along with the Doing Business Reports, stepped up the dialogue with the Burkina Faso Government on reforms, and the country is now one of the top five reformers in Africa.
The future of ICAs

ICAs will remain a key instrument for diagnosing impediments to the investment climate at the country level and for addressing reform priorities. Demand has been high for ICAs in the Bank; recent ICAs on India, Turkey, Bulgaria, Nigeria, and Kenya have been singled out for their quality and policy implications. Going forward, we would like to expand the ICA methodology in the Africa Region. In particular, we are exploring its use for diagnosing impediments to regional trade and integration and for initiating state-level investment climate reforms.

Regional ICAs centered on SADC, ECOWAS and COMESA zones, for example, would focus on the dynamics and impact of regionalization, the factors affecting competitiveness, regional cooperation, and trade. Regional ICAs would be able to shed light on the effects of macroeconomic, trade and tariff policies on exports.

Finally, sub-national ICAs have the potential to identify differences in the investment climate, and how these affect the performance of enterprises located in the major cities of the largest African economies. Selected cities would be able to compare their investment climate with other cities in the country. Accra, for example, would be able to compare itself not only with national economies of Kenya or South Africa, but also with those of Lagos, Dakar and other cities in African countries with large economies.