

# **Responding to the Challenges of Aid for Trade (I):**

## **Enhancing the Role and Contribution of the private sector**

Draft, December 2009  
Olivier Cattaneo and Leen Solleveld

### **1. Context:**

In July 2009, on the occasion of the Second Aid for Trade (AFT) Global Review, the international community agreed on a series of objectives to move the agenda forward: (i) to enhance the role and contribution of the private sector in this initiative; (ii) to strengthen the regional dimension of AFT; and (iii) to improve the (impact) evaluation of AFT.

On the private sector engagement front, a few initiatives have been launched already. For instance, the World Bank has started engaging the dialogue with the private sector and developing pilot partnerships on aid for trade facilitation.

As part of the Global Trade and Financial Architecture (GTFA) project – that played a leading role in the early design and promotion of the AFT concept – an informal consultation with the private sector was initiated with a view (i) to discuss the concept of AFT, (ii) to take stock of existing efforts led or in partnership with the private sector, (iii) to identify potential areas for public private partnerships, and (iv) to explore interest/shape of private sector participation to the global AFT architecture. Individual firm interviews and a round table (Overseas Development Institute, London, September 2009) were organized to collect the views of the private sector and business associations.

This paper presents some of the conclusions of these consultations, challenges ahead, and prospects for an enhanced role and contribution of the private sector to AFT. It also suggests further steps to reconcile public and private sector approaches to the provision of AFT.

### **2. Main conclusions:**

The role and contribution of the private sector in the AFT initiative is largely understated and misunderstood

The AFT concept has not fundamentally changed the way official donors contribute to building trade capacity in the developing world. A number of activities financed by the Official Development Assistance (ODA) that do now qualify as AFT actually pre-existed the AFT concept and were just re-labeled or re-packaged to bolster AFT levels up. The private sector, obviously, did not have the same motives, and did not buy into the AFT frenzy. It remains that most companies established or trading with developing countries do contribute to building local capacities. These contributions are not labeled “AFT”, but rather called “value chain management” or “corporate social responsibility”. If the provider of this “aid” was public, then it would fall under the AFT umbrella: such contributions range from the owner of an SME dedicating some spare hours for training to the multinational investing in infrastructure.

In other terms, the private sector is no foul, and from its perspective, donors continue their “business as usual” even if new concepts are grafted. Logically, the concept of AFT lacks traction for the private

sector, and two parallel AFT tracks have developed: one led by business that is an inclusive part of their operations in the developing world; one led by donors, which is a subset of traditional aid. There is no apparent interest in merging the two tracks: the private sector and donors will continue to develop their own projects according to their respective strategic interests and competences. Nonetheless, bridges could be built by:

- Raising awareness – in the donor community of actions taken by businesses; in the private sector of AFT dedicated projects;
- Leveraging some private investments and initiatives by linking them to donor projects or helping consolidation of individual initiatives;
- Re-evaluating and thinking the business/donor dialogue and participation of the private sector to aid project cycles – from informal to formal, and from conception to evaluation.

With a view to build such bridges, first steps could involve:

- Stock-take of private sector initiatives that contribute to building trade capacity in developing countries;
- Identification and development by the donors of pilot partnerships with the private sector; and
- Stock-take of existing PPPs and lessons to be drawn for the global AFT architecture.

Due to potential conflicts of interest, it appears that the window for partnerships on AFT is very narrow, in particular since infrastructure projects for which the private sector competes represent the bulk of AFT. Truly “public goods” for which the private sector is ready to invest beyond individual action are seldom.

### **3. Aid for trade: a concept that is too vague to appeal to the private sector**

#### *Definition issues*

The private sector often does not relate to or understand the concept of AFT that is too vague and ambiguous. According to the WTO, AFT is defined as technical assistance, infrastructure, productive capacity, and adjustment assistance. Since the private sector represents a fair share of the productive capacity, does that mean that any form of aid that would help promoting its activities abroad or across borders would qualify as AFT?

The patterns of trade differ from sector to sector, country to country, and company to company. For instance, a few interviewed companies did not perceive themselves as doing trade, although they were established in over a hundred countries. Intra-corporate trade and global value chains drive an increasing part of global trade. Products/services do not always cross borders, however: foreign investment can lead to local production for the local market. On the other hand, the GATS and other instruments tell us that commercial presence is a form of trade. Plants/branches of foreign companies are commonly perceived as the symbol of globalization – and the target of anti-globalization (in the North) or “empowerment” (in the South) movements.

Should one of the objectives of AFT be to increase the country’s attractiveness and readiness for foreign direct investment (FDI), i.e. to improve business climate in developing countries – or be limited to developing local capacities without foreign capital? Is AFT only about removing obstacles at the border, or also behind the border? Is AFT only about promoting exports or imports as well? FDI spill-over effects –technology and knowledge transfers, direct and indirect creation of jobs, local sourcing of inputs, sub-contracting, tax revenues, increased competition, etc.– are just as important to build local trade capacity. Neglecting this channel of trade integration would seriously hamper the chances of developing countries to export more – the learning process should not be neglected. It is however sometime rejected as part of

AFT as it could be seen as promoting foreign companies (and imports) rather than domestic companies (and exports).

Examples of trade capacity building through foreign private investment:

- Nestlé and Unilever have undertaken (with academics) to analyze the spill-over effects of their establishment in a number of developing countries.
- The case-study of Shoprite (distribution) in Zambia revealed that: in a first phase, the supermarket imported most products from ZA; in a second phase, local producers adjusted their production to meet the supermarket standards, and eventually most products were purchased locally; in a third phase, the most successful local products were exported to ZA and other countries.

Related is the issue of technology transfers. For instance, with regard the dissemination of clean technologies that is needed to adapt to/mitigate the effects of climate change, transfers of technology will be essential to the global trade integration of the developing world – financial aid alone will not suffice, and technology is in the hands of the private sector. Is the promotion of technology transfers part of AFT and trade capacity building? If not, AFT projects in the area are condemned to remain of marginal impact.

- The private sector has been very active in the Copenhagen negotiations, and continues to seek partnership models that would help the dissemination of clean technologies in developing countries. A number of governments in the developed and developing worlds are supportive of this initiative. This could become a promising area for partnership between the donors and the private sector.

Precisely defining the objectives of AFT could considerably expand or limit the scope of the concept and possible involvement/partnerships with the private sector.

#### **4. The articulation of the roles of the private sector and the donor community**

By establishing and producing in a developing country (or any country), a company aims to generate profit and incidentally to create jobs. This, in turn, creates more demand and more commerce. The contribution of the private sector to AFT could therefore legitimately stop here, and it would remain to the governments and donors to facilitate this virtuous process. Nonetheless, a few factors justify a further involvement in the AFT initiative: first, private companies will be associated to the building of capacity/infrastructure through government procurement and contracting; second, private companies have a stake in the development of infrastructure/business environment that supports their activity, and corporate strategies include value chain and corporate social responsibility management that overlaps with AFT. They have a potential role to play at all levels of AFT: diagnostic of problems, implementation of projects, monitoring/evaluation of results.

##### ***Public procurement and contracting: the business of AFT***

Donors, governments, and private sector have to work together on a number of projects -in particular infrastructure- that qualify as AFT. There, the private sector operates for profit, and not for public good. On one hand, partnerships on projects that lead to procurement/contracting risk creating conflicts of interest, or at least the perception of conflicts of interest. On the other hand, enhanced public-private partnership on projects (from conception to execution), including through co-financing, is likely to increase the chances of success of projects. It is very difficult to draw the line between partnership and conflict of interest, and therefore the prospects for pilot projects in this area should remain rather limited.

A number of points were raised by the private sector on the occasion of the meetings:

- Procurement rules

Many multinational companies see (abuses of) procurement rules as a main obstacle to trade – in particular the absence of transparency and corruption. A major request is to adopt transparent and uniform rules that would guarantee fair competition. The private sector is willing to inform this process by providing templates for reform, data and evidence on the cost and flaws of public procurement processes.

- This is a common request of the private sector. Negotiations on the transparency of public procurement are taking place in the WTO, but remain limited in scope.
- How could this request articulate with the donors' agenda on public sector reform and corruption? Could the private sector provide useful information or empirical evidence of abuses?

- Project conception

The private sector would appreciate an earlier involvement in the donors' project cycle. This already takes place in many sectors, on a more or less formal basis. This request is made, in particular, in sectors where technologies evolve quickly. For example, the private sector could finance project studies to develop rail corridors, electricity smart grids, high-voltage highways, telecom networks, etc. These studies could be elaborated jointly by several competitors, and precede a transparent and open procurement process. While making full sense, and despite safeguards, this cooperation could be seen as crossing the line of conflict of interest. More modestly, the private sector could be invited more often to share their knowledge of new technologies with the donors' engineers and project leaders to ensure the inclusion of the latest knowledge in the project studies.

- What could be done to improve closer involvement of the private sector in project cycles without creating conflict (real or perceived) of interest?

- Project financing

The private sector finds that the donors (and IFC in particular) are often too risk-averse. They would welcome a more frequent use of public funds to leverage private investment, and vice versa. Here again, the challenge is to avoid any conflict of interest. Also, the private sector recognizes that only very few projects in the least-developed countries have prospects of returns that would justify a private investment. Scope for partnership is therefore, here again, rather limited.

- The EASSy initiative is a good illustration of project co-financing by the donors and a consortium of private operators that will largely benefit trade in Africa. A key feature of the project, that avoids the creation of conflicts of interest, is the open access (as opposed to the capture of operation concessions by the participating firms).
- Infodev had developed jointly with Alcatel-Lucent a number of pilot projects on the dissemination of telecoms in developing countries (e.g. in Senegal, mobile access to the market price of crops). This partnership has stopped, and Alcatel continues the projects on its own (e.g. in Haiti, on the traceability of coffee, Madagascar, wifi access).
- What lessons should be drawn from these successes/failures?

- The business of AFT

AFT is a business in itself: indirectly (through donors' procurement) and directly (when trade capacity building projects are directly delivered by the private sector to the government without donors' intermediary). Some companies, like SGS, are providing services (on a commercial basis) very similar to the ones provided on a non-commercial basis by donors (sometimes with, sometimes without donors' support to the government). Obviously, this cannot be counted as AFT (at least not by the provider of the services, but eventually by the contractor if a donor), but sharing lessons and data could increase the efficiency of AFT delivery.

- Would it be possible to gather data from companies that are in the “AFT” business with a view to help monitoring/evaluating AFT projects.

### *What really matters to the private sector: refining the scope of AFT and partnerships*

According to the above, the private sector is often associated to the delivery of AFT, but on a commercial basis. This rules partnerships in a number of AFT projects out. Is it nonetheless possible to identify projects that are targeting public goods and for which private companies are ready to invest resources/knowledge/time without hopes of higher returns than their competitors? The private sector is already investing a lot in building capacities in the countries where they invest, but does it independently of the donors. There is not necessarily an interest in renouncing to this unilateral “aid” (that is faster, more targeted, and more efficient), but some public goods are such that cooperation with donors could help or be necessary. When asked about what really matters to trade, private companies give answers that strikingly differ from what is usually showcased and promoted in Geneva as AFT.

Infrastructure is probably the first priority for many companies but partnerships in this area are difficult due to the risk of conflict of interest in procurement. Some rare examples of AFT in this area exist: e.g. Lafarge building a power station for its own use and offering additional capacity to supply other consumers.

It is interesting to hear that the public goods the private sector values most and, in its view, best contribute to improving trade environment and facilitating trade are quite remote from what would usually qualify as AFT – and actually would not be reported as AFT. Examples include:

- Cost of AIDS and other pandemics

In some countries, in particular Sub-Saharan Africa, pandemics are a major cost for business operation, hence competitiveness and trade integration (e.g. cost of staff turnover, absenteeism, etc.). For a number of companies, tackling the issue of pandemics is essential to developing the attractiveness of certain countries. A number of projects in this area are already led by the private sector.

- Cost of road insecurity

Road accidents are humanly and economically costly, both for governments and private sector companies using the road to transport their merchandise and do trade. A pilot project is developed by the World Bank and Total – supported by a group of about thirty other companies, transporters, and governments – that will secure a trade corridor in East Africa. Potentially, this pilot could be replicated in the other 20 trade corridors identified in Africa.

- Cost of staff insecurity

Ensuring the safety/security of employees is a major concern of companies establishing operations in some sensitive developing countries. The capacity is a key determinant of the decision to invest, or maintain operations and trade with a country. The private sector is ready to invest, jointly with donors, and in cooperation with local governments, in the training and hiring of security forces in major economic development zones and trade corridors.

- Education and training

Lack of qualified personnel (e.g. engineering) is a well-known obstacle to economic development and trade integration. The cost of expatriates increases operations costs and affects both competitiveness and scaling-up prospects. A number of initiatives have already been taken by donors and the private sector to

remedy this situation – more partnerships could be envisaged to multiply the effects of the private sector's engagement (e.g. sponsoring of chairs in universities or other schools).

This observation raises fundamental questions regarding the definition and potential impact of AFT. It suggests that what matters the most for the promotion of trade would not necessarily fall into the AFT category as defined by the WTO/OECD and the donor community.

### ***The participation of the private sector to the global governance of AFT***

No surprise then that the private sector has expressed so far little interest in participating to the global governance of AFT and the private and public AFT tracks have remained parallel. Nonetheless, beyond the areas for participation that have been sketched above (mainly focusing on the implementation of AFT), the private sector could participate up- and down-stream the donors' interventions. In particular, the private sector is in a better position to provide diagnostics of countries' trade environment (e.g. by providing data on trade costs) and to evaluate the impact of AFT projects on their operations.

A few other mechanisms of formal cooperation have been envisaged, such as a high-level business advisory group, but lacked traction so far.