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A Private Enterprise Strategy for Forestry Development: Principles, Mechanisms, and Challenges

By

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A PRIVATE ENTERPRISE STRATEGY FOR FORESTRY DEVELOPMENT: PRINCIPLES, MECHANISMS, AND CHALLENGES

Jan G. Laarman and George F. Dutrow[1]

INTRODUCTION

An increasing proportion of the U.S.A.'s economic aid to the developing countries emphasizes the building and strengthening of indigenous private enterprise. The promotion of private enterprise is included in the U.S.A.'s aid policy for forestry (USAID 1983). This paper reviews the arguments advanced for private enterprise as a means to realize economic growth in the developing countries, including economic growth in their forest-based sectors. It then describes the mechanisms of a bilateral aid project to strengthen private enterprise in those forest-based sectors. The concluding section discusses the challenges to meeting that objective.

The observations presented here stem from a project being carried out by the Southeastern Center for Forest Economics Research (SCFER) for the United States Agency for International Development (USAID). This project is titled "Private Enterprise Initiatives for Forestry Development." In the formulation and initial execution of this project, much has been learned that should be of practical value to other bilateral and multilateral organizations contemplating similar efforts.

The focus on private enterprise in programs of economic assistance to low-income countries is highly controversial. On the battleground of ideas, the U.S.A.'s attempt to "Reaganize the Third World" (Lubar 1981) has been scorned and praised, condemned and defended. Much of the argument is ideological, but there is also much of substance to be critiqued on grounds which are mainly analytical. Whether ideological or analytical, the views expressed here are those of the authors alone. They should not be ascribed to either SCFER or USAID.

PUBLIC CONTROL AND PRIVATE ENTERPRISE

Economists and policy-makers have extensively debated the question of state intervention in the industrialization of developing countries. At one extreme is the school of thought which supports pure laissez-faire as the most efficient means of allocating resources and advancing economic growth. This group argues that governments are political in nature, badly organized,

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and administratively inefficient in their control of economic enterprises. Market mechanisms and private enterprise, therefore, should be unbridled to permit capital and labor to flow to where they will be used most productively.

At the other extreme is the school of thought which contends that it is the private sector which is unimaginative, risk-averse, exploitive, and too traditional to conduct the kinds of undertakings needed for industrial development. Advocates of this position argue that the state should be the prime mover in this process through detailed central planning, combined with ownership and control of the industrial resources (World Bank 1979, p. i).

In reality, the industries of almost all developing economies comprise some mixture of private enterprise, public enterprise, and public control over private enterprise. The demarcation between public and private enterprise in the forest-based sector is explained by political ideology, historical circumstances, and economic constraints. In some developing countries the government owns and operates only the large capital-intensive establishments, e.g., pulp and paper mills. In others, government ownership and operation extend to even small sawmills. A variety of marketing boards, or their equivalent, set prices and quotas for forest products sales, especially for products which are imported and exported. Entry and exit from forest-based industries frequently depends on obtaining official licenses or permits. Reforestation on private lands may be subsidized, and timber cutting and wood-processing are likely to be taxed. In these respects the forest-based sector falls under the purview of the "closely controlled economy" (Bauer 1984, pp. 19-37).

Lal (1980) identifies many of the various reasons that governments offer in justifying their intervention: (i) to provide the lead in industrialization when private entrepreneurs are unwilling or unable to do so; (ii) to correct racial imbalances in entrepreneurship; (iii) to finance large-scale industries in economies lacking efficient private capital markets; (iv) to correct market failures that occur because of non-market costs and benefits, externalities, and high market transactions costs; (v) to provide control over the "base" sectors of an economy as a necessary condition for socialism, in those countries where this political consideration is relevant; (vi) to avoid the political consequences of concentrated private wealth; (vii) to control foreign-based enterprises, and to nationalize them when they are perceived inimical to a country's economic or political interests; and (viii) to extend state political power *per se*.

Critics of the closely controlled economy assail certain of the preceding arguments, e.g., extension of state power for mainly political purposes, as not related to the requirements of the industrialization process, and therefore not worthy as objectives. Critics also assail the effectiveness of government

controls as a means, e.g., use of state intervention to correct for market failures. They point out that government action for the solution of economic problems is frequently guided by less than perfect economic information, and other than public-spirited economic motives (Krauss 1983).

Additionally, the operation of closely controlled economies is faulted for introducing excessive political leverage over economic life. The preoccupation with politics only intensifies the stuggle for political power, together with the search for government-conferred privileges. These privileges include lavish subsidies for favored firms, restrictions to protect the businesses of personal colleagues from competition, and privileged forms of employment for relatives and friends of influential officials. Hence the economic prospects of large numbers of businesses and workers come to depend directly on who is in the government at any particular time (Kreuger 1974).

The answer, then, is that governments of many of the developing countries need to "take a few steps back" (i.e., away from intervention) and permit a greater play of market forces (World Bank 1979, p. ii). Those who advocate reduced intervention argue as follows (Schultz 1980; Bauer 1984):

(1) that the economic interests of politicians, civil servants, and their associates do not necessarily coincide with the economic interests of the poor;

(2) that state control has extended into economic activity for reasons completely unrelated to the more justifiable objectives of intervention, e.g., to address market failure;

(3) that to "assist" industrialization—through subsidies, tariff protection, special pricing arrangements, and the like—is only to retard its long-run growth and development;

(4) that among the poor is found a great majority of persons who are exceptionally responsive to economic incentives and market prices, spending much time and energy to earn or save even small amounts of produce or money;

(5) that material progress has much less to do with endowments of capital and natural resources than with personal and cultural aptitudes, attitudes, ambition, and resourcefulness; and

(6) that it is the "competitive growth regions" of the Pacific Basin (Peninsular Malaysia, Singapore, Rep. of Korea, Taiwan, and Hong Kong) which lead the developing world in material growth—all relying extensively on private markets and minimal government controls.

DEVELOPMENT ASSISTANCE, FORESTRY, AND PRIVATE ENTERPRISE

In the past few years various bilateral and multilateral sources of development assistance have come to be strongly influenced by the preceding views. Both the World Bank and the International Monetary Fund have increasingly adopted "policy-based lending" and "conditionality," referring in part to having governments reduce their overall spending and their intervention in markets (Francis 1984).

Much bilateral aid from the U.S.A. now conforms with principles and policies defined in USAID's "Private Enterprise Initiative." This document stresses helping governments to identify and remove policy, legal, and other barriers that inhibit market efficiency and hold back private investment. Another emphasis is the building of management and technical skills needed to run businesses. A third is feasibility studies to identify and evaluate specific investment opportunities. The final focus is the strengthening of financial institutions and private capital markets (Hageboeck and Allen 1982).

Selected components of the U.S.A.'s program of bilateral aid for forestry are guided by the preceding themes. In 1983 USAID began a five-year project to strengthen private forest-based enterprises in selected countries of Latin America and the Caribbean Basin. Activities supported by this project are as follows: (i) on-site technical assistance, recommendations for marketing strategies, and studies of investment feasibility for forest-based businesses; (ii) applied research and seminars on subjects such as wood products manufacturing, product grading and standards, export marketing, and wood for low-cost housing; (iii) workshops on business management and finance applied to the forest-based sector; and (iv) research addressing government policy reforms in order to improve the business climate for private forest-based enterprises.

Objectives are to use relatively small amounts of USAID funding to act indirectly as educator, demonstrator, and matchmaker (or "information broker"). That is, the project provides information, not capital. Premises for this position are as follows: (i) large amounts of both public and private funds are being invested in forest-based enterprises, but often ineffectively; (ii) in many cases effectiveness increases dramatically by amending government policies that interfere with market incentives; (iii) in other cases effectiveness increases by enhancing an entrepreneur's information and professional contacts in marketing, finance, and technology choice. Clearly, neither policy dialogue nor the enhancement of decision-making information requires large expenditures of capital. Furthermore, the proponents of USAID's private enterprise philosophy contend that small amounts of public funds should only facilitate, not displace, capital expenditures forthcoming from private sources (Hageboeck and Allen 1982, pp. viii-ix).

Project implementation requires a careful combination of public and private partners. Project management is under the direction of a small team of forest economists employed in the public sector, representing universities and federal agencies. These university professors and agency civil servants assume the role of "trusted agents," whose motives and objectivity are typically respected in communications with host-country governments. But recommendations to the forest-based businesses in questions of finance, markets, and technology are more appropriate when made by private consultants and specialists from forest-based companies. To encourage this form of public-private partnership is a major goal of the U.S.A.'s economic aid program (USAID 1982, p. 2) and of this project.

CHALLENGES TO THE PRIVATE ENTERPRISE APPROACH

The objectives and delivery system of the project "Private Enterprise Initiatives for Forestry Development" are unconventional and largely untried in USAID's current portfolio of forestry projects. As with any new undertaking, a series of constraints must be overcome to make the venture succeed. These constraints are reported here for the benefit of other bilateral and multilateral organizations which are planning or beginning similar projects.

(1) In the views of many world leaders and opinion-makers, the U.S.A.'s government is considered naive for lecturing the developing countries on the virtues of free enterprise. The Reagan Administration is rebuffed for providing a simplistic answer to a multifaceted problem, and for substituting political ideology in the place of useful assistance measures (Horton 1984).

Whether these critics are right or wrong is not a fruitful subject for present discussion. But the implications are that a USAID-funded private enterprise project must operate in a highly charged political environment. Influential personalities in the forest-based sector and elsewhere already have formed opinions about the U.S.A.'s current approach to foreign aid.

The practical upshot of this for project administration is to direct project activities through and for believers in the private enterprise strategy, and to attempt to convert unbelievers through persuasion and on-the-ground demonstrations. Most of the unbelievers are found in the government sector, for the private sector is understandably sympathetic to project aims and approaches.

(2) The question of "policy reform" is obviously a sensitive one. It can easily be perceived as external interference in internal politics. To a very real extent, it is. For this reason leading officials of a host country's forestry agency are likely to resent the intrusion of an external team

which tells them how to change their policies, programs, and legislation to allow markets to operate more freely.

However, there are many ways in which a project can concentrate on technical and analytical tasks to support policy education, avoiding the delicate position of giving policy advice *per se*. Project team members can be reminded that the choice among policy alternatives always belongs to the officials of the host country governments. The most a foreign assistance project can do is to provide objective and analytical information to help these officials become better informed for policy-making.

(3) A project like the one described in this paper can be perceived as conflicting with other interests of the donor country. For example, privately-financed forest products associations in the U.S.A. are intent upon expanding exports. These associations are spending large sums of money to promote wood products exports to the Caribbean Basin and elsewhere. Not only the U.S.A.'s private sector, but also agencies of its federal government (e.g., the U.S.A.'s Foreign Agricultural Service) are aggressively promoting wood products exports. Yet a leading objective in "Private Enterprise Initiatives for Forestry Development" is to evaluate possibilities for import substitution of these same products.

Some of these conflicts have to be accepted as inevitable, given the plurality of foreign interests of a large country like the U.S.A. Also, it is not difficult to identify and affiliate with constituencies in the U.S.A. for which conflicts of interest do not exist. For example, along with its trade associations which promote wood products exports, the U.S.A. has others which focus on wood products imports, including imports of tropical hardwoods. Groups like the importing associations and others are readily able to endorse project objectives.

(4) The promotion of private enterprise in the forest-based sectors of developing countries strikes many environmentalists as patently inadvisable. Some blame much of tropical deforestation on the inability of governments to check the forces of private enterprise in the forest. Is not USAID encouraging more of the same by funding this project?

The response must be to carefully select activities for the project that appeal to profit-making instincts at the same time that they are resource-conserving or wood-extending. Examples are private enterprise approaches to seedling nurseries and reforestation, feasibility studies of thin-kerf sawmills, and expansion of wood preservation treatment. From an environmentalist's viewpoint, an example of a less appropriate project activity is the testing of new logging systems for virgin stands of tropical hardwoods. Clearly, highly subjective value judgments enter this activity screening. However, it does seem technically possible and certainly worthwhile to identify common ground where the goals of both forest-sector industrialists and environmentalists coincide (at best) or do not clash (at worst).

(5) The world's forestry development circles have just recently entered the era of "social forestry" and "community forestry." To many, a project like "Private Enterprise Initiatives for Forestry Development" implies a trickle-down approach that abandons village-level forestry and reverts back to the tenets of industrial forestry. Here there are false impressions to rectify.

The project's domain is forest-sector markets and entrepreneurs, wherever they are found. This definition ranges much more widely than to encompass only the most prominent wood-processing firms in a country. A small land-owning farmer surely epitomizes the "private entrepreneur." When project activities can be identified in which small farmers are the target beneficiaries (e.g., in agro-forestry marketing and smallholder fuelwood production), there is every reason to proceed with them.

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