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PRIVATE SECTOR SUPPORT PROJECT: ECONOMIC ANALYSIS

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Executive Summary: Conclusions of Economic Analysis and Impact on Proposed Budget

I. Overall Conclusion

The purpose of the Private Sector Support Project is to develop effective programs that will work towards th overall goal of promoting private sector growth in Africa as well as yielding measurable results and benefits. These programs must also be able to provide quick and flexible technical assistance for rapid responses to changing conditions.

Sustainable economic growth and increased social benefits in Africa will come chiefly from new investment and wealth generated by a vibrant private sector and active capital markets. The Africa Bureau should continue its strong support for reforms of enabling environments in the region as an economically efficient manner to promote social well being, job creation, capital development, and technological transfer.

The key successes of the Africa Private Enterprise Fund (APEF) has been its ability to be flexible and innovative in response to rapidly evolving enabling environments in Africa and to provide technical support for governments on an ad hoc basis. In Africa, where political and economic change requires rapid response, the APEF ability to react to mission's needs has yielded considerable and measurable successes.

There has been less success in the areas of finance and venture capital development because most nations lack the basic policy and environmental prerequisites for developing credit markets. Africa Bureau resources are more efficiently employed in the promotion of enabling environments that will, over time, create the conditions for financial markets.

The emergence of an environment conducive private sector development is an evolutionary process that requires patience as well as an institutional capability, within A.I.D., to understand and to respond rapidly to changes. However, there exist poor enabling environments where A.I.D. assistance for private sector development goes for naught. In these circumstances, the agency must be as prepared to withhold or withdraw support where basic conditions no longer exist for growth.

There has been little assessment, on an organized basis, of the impact of changes in enabling environment in those Sub-Saharan African (SSA) nations that fall under "concentration" category or that have received substantial Africa Bureau assistance for private sector development.

II. Criteria for Program Design

Because of a dearth of funds, strong criteria should be used in project design to support private sector activity in SSA. Among these criteria are:

1. The government exhibits a distinct movement toward free market policies.

2. The activity reduces government involvement in the market place, replacing it with viable and competitive private sector institutions.

3. Support for foreign investment initiatives must first determine a viable enabling environment.

4. Government policies toward currency valuations, public and private sector debt and levels of taxation must be consistent and logical, meeting basic needs for private sector activity.

5. The activity does not sustain nonproductive enterprises, in the public or private sector.

6. The activity does not supplant one public sector subsidy with another.

7. The activity involves an increased role for the private sector, be it in dialogue on policy reform or in governing boards of regulatory bodies.

8. The activity focuses on development of African entrepreneurs.

9. Any transactional support should have clear benefit beyond the specific business transaction which is under consideration.

10. Assistance must work to improve the competitive environment and not undermine other private sector initiatives in similar sectors.

11. The activity mobilizes financial and management resources on a market basis (in investment finance, debt or equity).

12. The activity improves the position of business associations, microenterprise groups, networks and cooperatives.

III. Mission Support

The provision of technical assistance and business expertise to U.S.A.I.D. missions has been the most cost-effective use of Africa Bureau core funds for private sector development. This program should be maintained and strengthened.

A.1. Private Sector Strategy

The Bureau has worked to help missions to develop private sector strategies and to prepare project documents. These services were particularly valuable when missions were first venturing into private sector activities, a role that has diminished in importance. They have been mission-funded through buy-ins and should continue to be so.

A key component of this assistance, MAPS (Manual for Action in the Private Sector) should continue for nations undergoing basic reform. However, the number of nations where this may happen is likely to decline. Rather, some of the functions that MAPS performs should be expanded for missions in those nations with more advanced enabling environments and provided on an, ad hoc and as needed basis. These should include: 1) Updated analyses of the state of the private sector for nations where PSAs do not exist or where fundamental reform has shifted the scope of economic activity; 2) Continued efforts to strengthen domestic business leaders and associations, through national and regional meetings; and 3) General, ongoing assessment of Agency and mission private sector activities in light of political and economic changes to determine the viability of such programs.

A.2 Enabling Environment

The areas where the Africa Bureau has assisted in enabling environment reform includes the provision of TA for investment codes, trade regimes, tax codes and privatization efforts. These efforts represent a vital and efficient use of resources to spur free capital investment and flow of goods in the continent.

A3. Developing Private Sector Networks and Organizations in Africa

Support for the development of business associations and networks, through regional and sectoral meetings, TA and organizational support, is an important role in building private sector infrastructure as well as building support for private sector activities in African nations. The Africa Bureau has devoted considerable energy and technical support in this area, filling a vacuum left by other donor agencies. Its efforts to sustain networks has been particularly important in those nations, in West Africa, where the enabling environments are poor and where the private sector needs greatest support. It has worked to develop

contacts between businessmen and groupings in Africa and the United States. These efforts should continue and increase.

B. OPIC and Investment Promotion

The Africa Bureau's efforts at investment promotion in those nations that have basic flaws in the enabling environment do not yield sufficient results, given levels of effort undertaken. However, once the political atmosphere is ripe for reform, investment promotion in these some nations where promotion once failed can work, as in the case of the Uganda Investment Authority after 1990.

OPIC missions have generally utilized regional approaches, yielding minimal results in those nations where business environments are poor. Expenses have increases while yield has eroded. The continuation of OPIC missions at the same level as previous efforts is thus called into question.

C. Finance and Venture Capital

While a lack of capital and competitive financial markets is a key obstacle to business development, most efforts to promote financial instruments have not been successful, because, as market-conditions indicate, most of SSA lacks the prime conditions that usually attract and maintain capital. Efforts to explore creative financial mechanisms have not yielded beneficial effect and are not cost-effective. Work to expand micro-African financial institutions (such as tontines, La Financiere movement) into larger activity has not produced noticeable benefit. Venture capital efforts have been extremely slow, with minimal benefits given cost-expended. In some cases, venture efforts are working to subsidize other multilateral assistance in quasi-private sector activities rather than supporting local entrepreneur activity.

There does remain room for donor assistance in the financial arena. The Africa Bureau should continue to inform and pressure SSA countries to establish an attractive environment for financial instruments through continue dialogue, networking and cooperation with the IMF. It should assist in developing financial policy, independent monetary authorities and stock markets. Support should continue for networks of financiers, regional meetings of public sector authorities and seminars on financial techniques such as debt swaps or venture capital organizations. Where reforms are being undertaken, the Bureau should assist in developing financial skills.

D. Assessment, coordination and monitoring

Some on-going measurement of program success should be provided to determine progress, if any, towards the general goal of specific projects. The area of private sector development requires close monitoring by missions and the Agency alike with an active and flexible response to positive as well as negative developments. Ongoing programs should be withdrawn from nations where there has been erosion in enabling environments, as a means to reinforce policy reform. In addition, the Agency must coordinate closely and communicate with other, multilateral donors to which US funds are contributed its determination of where private sector development funds are not being used effectively.

IV. Impact on Proposed Budget

The economic analysis of the Private Sector Support Project PID concludes that increased effort should be devoted to provision of ad hoc support for missions, for regulatory change and for the development of unspecified, innovative R&D activities. Flexibility and the ability to adjust programs to meet rapidly changing conditions in Africa has been the key to the success of the Africa Bureau program. There has been less success in specific contractual areas of Venture Capital and Investment Promotion. Furthermore, given changing conditions, there should be additional adjustment in the areas of investment promotion, private sector studies (MAPS) and in assessment of the condition of enabling environments in Africa.

Consequently, this analysis suggests, in core funds, a 50% reduction in venture capital grants and a 25% reduction in OPIC participation, with all funds diverted to TA contracts for ad hoc usage. Professional staffing should increase, under the TA contract, by a factor of one. Similarly, in mission funds, there should be a 50% reduction in venture capital funds that should also be diverted for ad hoc usage.

In addition, it is recommended that a separate category be developed to evaluate private sector environments in SSA, both to determine the suitability of ongoing levels of effort by the Agency and the Mission, enforce conditionality agreements, and coordinate with multilateral and bilateral donors.

PRIVATE SECTOR SUPPORT PROJECT: ECONOMIC ANALYSIS

Preamble

Sustainable economic growth and increased social benefits in Africa will come chiefly from new investment and wealth generated by a vibrant private sector and active capital markets. This is particularly true given the leveling of multilateral and bilateral direct foreign assistance to the region. Many African nations have recognized this and are adjusting their policies to provide for a more effective enabling environment, that permits the private sector to flourish and social wealth to accumulate. However, the legacy of thirty years of statist rule is a dearth of capital, business skills and a lack of understanding of private sector requirements.

In the 1970s and 1980s, economic and trade liberalization swept through Eastern Europe, Latin America and Asia, yielding impressive results. Korea, Taiwan, Mexico and Chile became beacons and models for other nations: Thailand, India, Argentina, Colombia and others. But despite high levels of assistance, efforts at private sector development in Africa did not yield similar results. Net resource flows to SSA in the 1980s totalled more than $100 billion, yet the region's economy grew at a mere 1% a year, with real per capital incomes dropping by 40%. In the first two years of the 1990s, Real GDP is declining 1% per year. Political instability, natural and public health disasters, corruption, excessive government regulation and the lack of a dynamic business sector were exacerbated by inappropriate development strategies focused on government-sponsored growth. Today, SSA is marked by low productivity, shortages of capital and credit, shortages of goods and services, high public sector debt and a sharp decline in infrastructure. Beyond this, the continued high rate of population growth, malnutrition, and low health standards maintain a constant economic pressure on the continent.

Perhaps the greatest indicator of failed policies in Africa is the erosion of agricultural production and food distribution. Nations that once were food exporters, such as Zambia and Cote d'Ivoire, have lost their agricultural capability. Government attempts at maintaining food costs deprived farmers of profit and thus, production declined. The key lesson is that those same factors that worked against agriculture worked against all sectors of business in Africa. The state piled on disincentive after disincentive and thirty years of statist ideology has imbued Africans with a profound distrust of the profit motive and individual entrepreneurship.

Africa is beginning to change. Governments and elite groups are adjusting their visions and ideologies under the combined pressures of international donors, especially A.I.D., and popular African

discontent against failed, statist policies and ideologies. But Africa is a Gordian knot of entrenched groups, traditional practices, xenophobia, donor confusion and inexperience. Unraveling the old system while creating growth economies is not easy.

Today, an irregular business environment exists throughout sub-Sahara Africa, with different understandings, traditions, and regulations. The challenge is complex and multifaceted, ranging from promoting a general business environment favorable to large firms and financial institutions to developing microbusiness support for small scale agriculture, women in development and tradespeople. Most international donors now accept that an effective business environment must emerge with a strong physical, institutional and human infrastructure, with a consistent and logical macroeconomic policy framework and with a microeconomic incentive structure. Expressed in other terms, roads, computers and trained African managers must emerge in countries with legal structures that promote enterprise and without informal barriers to trade and investment and with markets that accurately reflect cost, demand and supply to allow farmers, entrepreneurs and other producers a fair return on their labor.

Lessons Learned

The challenge is to achieve maximum results, in the most efficient manner possible, without wasteful experimentation or counterproductive programs. Programs must be developed that are effective for the overall goal of promoting private sector in Africa as well as yielding measurable results and benefits. They also must be able to provide quick and flexible technical assistance for rapid response to changing conditions.

The PSSP builds on the experiences of its predecessor project, the APEF as well as other multilateral and bilateral programs which have paralleled APEF initiatives. Above all, there is a recognition that, in Africa, the growth of capital, technological advance, modernization and, ultimately, job creation and social well-being, depends upon changing thirty years of statist rule and mentality.

The emergence of an environment conducive private sector development is an evolutionary process that requires patience as well as an institutional capability, within A.I.D., to be flexible and to respond rapidly to changes. However, there exist poor enabling environments where A.I.D. assistance for private sector development goes for naught. In these circumstances, the agency must be prepared to withhold or withdraw support where basic conditions no longer exist for growth. Not a small number of nations have not fulfilled commitments to reform or have done so in name only, without the withdrawal of support by donor agencies. Assistance must be applied to shore up effective reforms. Alternatively, donors must be willing to take difficult decisions

and reduce or withdraw assistance rapidly, when governments and agencies fail to follow commitments to reform. In effect, rapid withdrawal of assistance programs is a positive initiative to support implementation of private sector reforms.

While political reasons for maintaining support may override economic concerns, the continuation of private sector support programs in nations where political and regulatory resistance is strong is wasteful of the scarce resources in the African Bureau. For example, attempts to provide assistance to promote foreign investment in nations where fundamental restrictions against foreign capital exist cannot work. Financial institutions cannot develop in a regulatory climate that is unpredictable, with interest rates, currency valuations, tax levels and regulations changing frequently and without notice or with an openly hostile legal structure. Even with substantial foreign assistance, credit markets will not open up when I.M.F. agreements prohibit any expansion of credit.

The implication of this analysis is that:

1. The area of private sector development requires close monitoring by missions and the Agency alike with an active and flexible response to positive as well as negative developments. This is a particularly difficult role for missions to undertake because of the long work that program development entails and understandings made with local authorities, all of which must be readjusted given the failure of local authorities to fulfill commitments.

   The PSSP must devote greater resources to support missions and monitoring private sector reforms to ensure effective use of funding as well as to provide some understanding of the level of impact for the Agency. In the end, this will provide an efficient use of resources, eliminating wastage and promoting strategic implementation of funding.

2. Support for private sector development will tend to be considerably stronger in Eastern and Southern Africa rather than in Western Africa where traditional and ideological antipathy towards effective enabling environment and Structural Adjustment reforms is greatest.

3. Support for private sector development will tend to concentrate in a few nations, where policies are progressing, and will not be region-wide in nature. However, care must be taken to maintain contact and communication with other African nations, through missions and other, multilateral donors, to be able to

respond to rapid changes in regulatory climates.

4. While the tendency in the Agency is to delegate more actions to field missions, the wide degree of levels of private sector development and enabling environment reforms suggest that this core program is critical in providing efficient and ongoing support. In addition, because global business conditions and capital flows change rapidly, a knowledgeable, centralized font of information on competitiveness provides an efficient use of Agency resources.

5. The Agency must coordinate closely and communicate with other, multilateral donors to which US funds are contributed its determination of where private sector development funds are not being used effectively.

Determination of Impact

Some on-going measurement of program success should be provided to determine progress, if any, towards the general goal of specific projects. This will be subjective as well as objective. While any exact measurement of programs to support private sector development is difficult to develop, some statistical basis does exist to determine the viability of the enabling environment taken together with periodic monitoring. The formation rate of new, non-farm businesses is a good indicator of how well private sector reforms are being implemented. In addition, the level of foreign direct investment (FDI) and the relation between the level of public sector to private sector investment are also important. To be sure, mitigating circumstances may bias statistical results. Natural disasters, such as epidemics or drought, or political turmoil, may delay the impact of private sector reforms.

In the past, monitoring and understanding of private sector reforms has been carried out on an ad hoc basic, leading to misunderstandings at the mission level and misapplication of resources. An effective and efficient monitoring program can easily ascertain the impact of private sector reforms and determine where programs should continue and where they should be reduced. Progress should be assessed in areas such as policy reform and implementation, reduction in tax and tariff levels, growth of non-trade, private lending for business growth, formation rate of non-farm business, the level of foreign direct investment (FDI), the relation between the level of public sector to private sector investment and other subjective and objective indicators.

Close, two-way communication with missions, World Bank and other active organizations is critical to develop common understandings of policy and implementation flows in African nations as well as areas of opportunity for effective program development.

An effective monitoring program is also an efficient strategy to reduce expenditures in programs that are failing because of poor regulatory or business environments.

General Criteria

Because of the complexities of different African economies, differences in cultural and political values as well as different levels of private sector development, an understanding and implementation of criteria for assistance, for both PSSP as well as in U.S.A.I.D. missions, should be used in deciding on donor assistance in support of private sector activities. These criteria should include:

1. The government exhibits a distinct movement toward free market policies. The activity is undertaken in a country where there is has been shown a substantial commitment to reform and where serious policy reforms are underway or about to begin. Whereas many African nations have had a long history of agreeing to liberalization reforms, many have not fulfilled their commitment. Furthermore, donor attempts to use carrot-and-stick approaches to nations that have not shown any tendency to reform have generally failed. Attempts to support business groups in nations where an enabling environment does not exist have also not succeeded.

2. The activity reduces government involvement in the market place, replacing it with viable and competitive private sector institutions. Policies aim at reducing government presence in business, such as privatization, should be supported. But equally as important is a determination that such reforms insure the development of competitive business that will insure continued provision of services. The continuation of what had been a public monopoly in private hands does not yield economic benefit.

3. Support for foreign investment initiatives must first determine a viable enabling environment. While some benefits may result from supporting foreign investment promotion to nations with poor enabling environments, such a use is not cost-effective and penalizes those nations where reforms have been enacted.

4. Government policies toward currency valuations, public and private sector debt and levels of taxation must be consistent and logical, meeting basic needs for private sector activity. Frequently, nations agree to regulatory reform but impose confiscatory fiscal or currency policies that render reforms useless. This must be

carefully monitored, especially in West Africa where a long history of unrealistic currency valuations has distorted business activities, rendering new formal investment extremely difficult.

5. The activity does not sustain nonproductive enterprises, in the public or private sector. Donor assistance should not shore up public sector firms. Neither should it try to support privatization or other business efforts where self-sustainment cannot be clearly established. This is particularly true for financial schemes. In nations where financial institutions are unable to provide loans, because of I.M.F. credit strictures or because of the perception of high risk, donor assistance should be limited until a viable financial market can be established.

6. The activity does not supplant one public sector subsidy with another The replacement of domestic, public sector subsidies by multilateral or bilateral donor subsidies does not work towards development of a viable free market activity and is an inefficient use of funds.

7. The activity involves an increased role for the private sector, be it in dialogue on policy reform or in governing boards of regulatory bodies. Profitability should not be the sole criteria for support; Increased private sector intervention and resources in regulatory boards is an evolving step towards creating a vital enabling environment.

8. The activity focuses on development of African entrepreneurs. While support for investment from foreign capital should be strong, a chief focus should be placed on African entrepreneurship to lay the basis for creation of a vital African business sector. This is a diverse group. Generally speaking, entrepreneurial talent in Africa derives from agriculture small- and large-holders; microentrepreneurs such as truckers, smugglers, craftsmen, and marketwomen; government-linked private suppliers; government managers of parastatal firms who must be retooled to operate in a market economy; offshore Talent who left their nations or sent their capital abroad and who will return, and bring with them sophisticated knowledge of management and commerce; and African managers of multinational firms.

9. Any transactional support should have clear benefit beyond the specific business transaction which is under consideration. There should be a clear demonstration of broader implications for policy, social benefits and lessons learned from transactional support. In most

cases, this indicates that businesses and transactions must be substantial in nature. Businesses should have other, private sector funds (as opposed to those multilateral funds channeled through financial institutions) that will indicate confidence in the enterprise as well as having some logical basis for a profitable rate of return. Assistance should not be in the form of direct subsidies to businesses. Examples of broader implications are the impact of tax or tariff reform upon a specific sector, the viability of newly privatized firms if startup costs are supported, or the competitiveness of local products in regional African markets.

10. Assistance must work to improve the competitive environment and not undermine other private sector initiatives in similar sectors. Transactional assistance should insure that funds are not subsidizing attempts to eliminate competition, nor to subsidize competition against other private sector enterprises, nor to support one sector against another. Support for private bus lines, for example, may work against private taxi owners, or, support for private food stores may work against local, open markets.

11. The activity mobilizes financial and management resources on a market basis (in investment finance, debt or equity). Where support for financial institutions is provided, it must be used to mobilize existing resources. However, before any support for financial development is provided, projects must determine how the investment environment has changed (reduced interest rates, reduction in IMF credit ceilings, improved operating environments because of tax reductions or altered currency valuation etc.) to allow for effective development of financial instruments.

12. The activity improves the position of business associations, microenterprise groups, networks and cooperatives. Support for business and cooperative groups to represent their interests before the government, while not yielding immediate results, is a critical element in securing a continued and effective enabling environment. In those nations where enabling environments are particularly poor, strong support for fledgling organizations is an effective strategy to further private sector development. However, it should also be recognized that the private sector in Africa is not one group but a collection of different, frequently competing sectors. Support should be provided to those effective organizations that represent these competing sectors, to provide them strength within government as

well as in public opinion circles.

Program Issues

A. Mission Support

The provision of technical assistance and business expertise to U.S.A.I.D. missions has been the most cost-effective use of Africa Bureau core funds for private sector development. This program should be maintained and strengthened.

Under this role, the Africa Bureau has provided rapid TA on an as-needed basis and has been able to adjust its focus with changing global and regional economic conditions. It has given guidance and networking with private sector experts and business groups for mission officials who have lacked private sector experience or who have been living in Africa for many years. Core expertise has been provided in developing and implementing private sector strategies and programs.

The Bureau has provided effective and timely short-term assistance on an as-needed basis for missions that required expertise in specific industrial sectors, in private sector reform or in privatization. In Mozambique, where war relief was the central concern of the mission, the Bureau provided guidance on establishing a Foreign Investment Code to lay the basis for growth in the rich mining and agricultural sectors for the post-war era; in Zambia, rapid political changes altered the mission's focus from agricultural assistance to a privatization program in industry and commerce, the Bureau assisted the mission in providing TA for the new privatization agency in a timely fashion. In South Africa, where the Bureau's program was limited, it assisted in assessing the possibility for developing black entrepreneurship in the post-apartheid era. Similar, ad hoc assistance took place in Togo, Ghana, Zimbabwe and other nations.

Through this program, the Bureau has provided communication between and among the missions on new strategies being developed by other offices as well as new business and financial trends emerging in the global and African economies. This communication has been on an ad hoc basis and should be more formalized, especially if the monitoring role is expanded. It has also provided the Agency with invaluable information as to mission needs and the changing economic developments in each African nation.

The Africa Bureau has been instrumental in providing long-term PSA technical assistance for missions in ten countries -- Burundi, Zimbabwe, Gambia, Cameroon, Zaire, Ghana, Swaziland, Lesotho, Kenya (regional) and Ivory Coast (regional). This broad program will be narrowed somewhat in line with the growth of mission capability in some of these countries (Zimbabwe, Ghana) and negative private

sector policies in others (Kenya, Cameroon).

Mission assessments of the Bureau have been favorable; chief criticism has focused on the Bureau's inability to provide specific commercial information for the missions' use. However, this was not an expressed role for the Bureau. Rather, the criticism is a sign of success. While the Bureau has endeavored to answer queries and network missions with commercial experts, it did not have the capability to perform such specific functions.

A.1. Private Sector Strategy

The Bureau has worked to help missions to develop private sector strategies and to prepare project documents. These services were particularly valuable when missions were first venturing into private sector activities, a role that has diminished in importance. They have been mission-funded through buy-ins and should continue to be so.

A key component of this assistance has been MAPS (Manual for Action in the Private Sector) studies. These are designed to help identify the structure of the business sector, facilitate reform as well as to develop a dialogue between government officials and entrepreneurs who have heretofore lacked a political voice. The MAPS, developed by the PPC/Policy Bureau, occurs over a period of four to six months during which time the private sector is surveyed to establish its size and scope and to obtain insights into its attitudes and views. Where does business exist and where does government limit entrepreneurship?

This MAPS process involves local consultant and survey firms who are then trained to undertake MAPS surveys so that missions and the private sector in the country can have local, experienced firms able to undertake MAPS updates. It brings together various segments of the private sector, some of whom have a history of antagonistic relationships, to discuss shared constraints. It also engages the AID mission to learn how to find significant private sector actors and to engage in a dialogue with the private sector.

The MAPS program is a critical, learning tool for nations where reform of the enabling environment sector is just emerging and should continue to be employed in those nations where private sector reform is being undertaken for the first time. To date, it has succeeded in eleven African countries in identifying the structure of the business sector, as well as to develop a dialogue between government officials and entrepreneurs. Missions have come to understand the environment in which they work.

MAPS should continue for nations undergoing basic reform. However, the number of nations where this is may happen is likely to decline. Rather, some of the functions that MAPS performs should be

expanded for missions in those nations with more advanced enabling environments and provided on an, ad hoc, as needed basis. These should include:

1. Updated analyses of the state of the private sector for nations where PSAs do not exist or where fundamental reform has shifted the scope of economic activity.

2. Continued efforts to create strength among domestic business leaders and associations, through national and regional meetings. In addition, sectoral organizations should be encouraged to develop, through networking of Associations with their international or US counterparts, such as chambers of commerce, trade associations, industry groupings and financial associations.

3. General, ongoing assessment of Agency and mission private sector activities in light of political and economic changes to determine the viability of such programs. Coordination with international agencies, in Washington, as to their views and plans with specific nations.

A.2 Enabling Environment

Governments' commitment to reform their enabling environment and to enact Structural Adjustment Programs (SAPs) are the keys to developing a successful business climate. If fulfilled, job employment will increase, capital investment will expand, new technologies will flow into countries and reliance upon donor agencies for subsistence will decline.

While the Agency supports SAPS, its major impact is on assisting in the development and implementation of reform of the enabling environment through provision of technical and financial assistance and conditionality. However, political resistance is strong against reform, especially in the bureaucracy and allied private groups. Even though governments agree to reform, informal barriers are frequently stronger than legal restrictions. [illegible] be cost-effective, the Agency must monitor continuously the wil[illegible]gness of nations to continue these reforms.

The areas where the Africa Bureau has assisted in enabling environment reform includes the provision of TA for investment codes, trade regimes, tax codes and privatization efforts. These efforts represent a vital and efficient use of resources to spur free capital investment and flow of goods in the continent:

Reform of investment codes is key to developing an environment that allows domestic as well as foreign capital to invest in African nations, rather than hide or export capital abroad. Property rights must be guaranteed and investors must be given confidence that the

environment for their capital is safe. Investment reform lays the basis for a long-term process that informs African leaders what capital requires to invest in their nations, to create jobs and lay the basis for growth. Revision of foreign investment codes frequently leads to revision of domestic investment codes, because local entrepreneurs complain, rightly, that they are working at a competitive disadvantage. Furthermore, as the benefits of new capital are discerned in the form of job creation and technological replenishment, countries are more willing to relax restrictive requirements. Africa Bureau efforts have been successful in Mozambique and Uganda.

Investment promotion in nations that have basic flaws in the enabling environment is useless, even if some partial reforms have been undertaken. Mission efforts throughout the 1980s at sponsoring trade & investment centers confirm this lesson in areas where there is minimal infrastructure (Cape Verde), where the business environment is inefficiently corrupt (Kenya), where repatriation of capital and profits is difficult (Cameroon), or in case of other major risks or impediments to operating and profit potential(Uganda).

Trade reform is required to spur exports and exports are not possible until nations become globally competitive. Almost all substantial growth among donor concentration nations, apart from donor funds, is from exports. To become competitive, all African enterprises must lose their traditional tariff, currency and legal protection from imports. Many African nations tax imports and exports. Their governments obstruct trade through burdensome procedures in ports. Poor maintenance in the transport sector, despite high taxation, works against trade. Government-supported cartelization of trade (shipping and trucking) further works to undermine the ability of nations to export. It is not surprising to find that the more vibrant sector of the economy is in informal trade (contraband) that thrives across many borders to circumvent government controls and inefficiencies. The Africa Bureau has achieved notable regulatory reform Uganda, Burundi and Swaziland. Attempts at reform in Togo floundered because of political unrest.

- A predictable and fair and competitive tax code is required to provide confidence for new domestic and foreign investors. African leaders must come to understand that a reduced tax burden decreases the level of informal activity, bringing more economic activity within the formal sector, increasing state revenues.

- Privatization symbolizes a political will to take strong steps and end monopolies and favored treatment to quasi-corrupt elite groups and workers in bureaucracy and government-linked contractors who do not perform work for value, thereby taxing the productive sector of the nation, the farmer, the worker and the private sector. When successful, privatization

reduces government spending and fiscal deficits, improves services to the general population, reduces patronage and burdensome taxation of the populace, frees-up resources for more productive, social and infrastructure uses, and improves the overall competitiveness of national bureaucracies in the face of global competition. African Bureau efforts have been successful in Tanzania, Uganda and Zambia.

A3. Developing Private Sector Networks and Organizations in Africa

Support for the development of business associations and networks, through regional and sectoral meetings, TA and organizational support, is an important role in building private sector infrastructure. The Africa Bureau has devoted considerable energy and technical support in this area, filling a vacuum among donor agencies. Its efforts to sustain networks has been particularly important in those nations, in West Africa, where the enabling environment is poor and where the private sector needs greatest support. It has worked to develop contacts between businessmen and groupings in Africa and the United States.

While measurement of the economic benefit in this area is difficult, the program plays a critical economic as well as political role in building support for private sector activities in African nations. The lack of sophisticated business networks in Africa is a key restraint to private sector growth. In the developed world, business associations represent individual industrial and agricultural sectors, provide up-to-date information on current business trends and opportunity and represent their sector to government and international associations. In Africa, the small and medium entrepreneur community works in isolation from other businessmen, neighboring countries and from the world economy. Because of hostile operating conditions, most businessmen work in secrecy, too insecure to cooperate with their compatriots.

The basic need for African entrepreneurs is to break out of the isolation in which they worked by establishing a strong network. African business must be kept aware of the impact of the rapidly changing African environment. Markets and sources will radically shift as government subsidies and protectionist policies are abolished and liberal import regimens are established with low or no tariffs. Above all, the entrepreneur sub-culture must develop confidence in its operating environment.

In an effective African business environment, a broad band of associations, representing competing sectors and interest groups, would address obstacles to private sector development by representing the interests of its membership to government and other industries with regard to the substance of policy and the process of regulation, providing members with information on policy, regulatory and market environments, facilitating access to

credit, supplying technical assistance and training and establishing industry standards.

After initial Africa Bureau efforts, missions in Cameroon, Kenya, Ghana, Guinea, Swaziland, Tanzania and Uganda are working with business associations and groupings to strengthen their ability to participate in policy dialogue through studies, publications and the promotion of fora where such exchange can occur (see below, business associations).

B. OPIC and Investment Promotion

The Africa Bureau provides assistance in developing the investment and trade potential in Africa through technical assistance in legal and regulatory reform, in promotion, in develop of market information and in establishing linkages with US firms. These efforts have been done on an ad hoc basic, using outside consultants, as well as through cooperation with the Overseas Private Investors Corporation (OPIC) and the Foreign Investment Advisory Service (FIAS).

The Africa Bureau's efforts to promote investment, including revision of investment codes, sponsorship of US investment missions and support for new investments through financial intermediaries has shown that investment promotion in nations that have basic flaws in the enabling environment yields minimal results, even if some partial reforms have been undertaken. However, once the political atmosphere is ripe for reform, investment promotion in these same nations where promotion once failed can work, as in the case of the Uganda Investment Authority after 1990.

Investment sites must have a clear competitive advantage, especially because their locale is in Africa. Investors prefer to keep their money in safer havens with greater predictability. However, they will invest if the risk/reward ratio is beneficial. Accurate information must be provided to facilitate outside investment interest and follow through.

OPIC missions have generally utilized regional approaches, yielding minimal results in those nations where business environments are poor. While it is true that missions yield some political benefits as well as illustrating to African nations the requirements for investment, the benefits for increasing foreign investment is questionable in nations with poor operating environments. In addition, an independent assessment of OPIC missions, done for the Africa Bureau, raises questions as to cost justification, a markedly increase expense for more recently accomplished missions over prior missions.

In the eighteen months since OPIC and AID entered into a joint program of investment missions, more than 91 US firms visited ten

African countries; of the 91 companies that participated on the missions 35 have notified OPIC of plans to "pursue investments." But major questions exist as to how much of these data relates to trade rather than investment and whether these investments would have been accomplished without OPIC mission. If, indeed, interest in foreign investment is increasing, such missions would better be provided through private sector organizations and business groups.

Furthermore, OPIC investment missions have taken place in African nations where enabling environment reform has taken place. The number of new SSA nations where reforms will have similar impact in the future is unlikely to be large. The key issue is whether Africa Bureau efforts yield greater results in policy reform rather than in developing investment missions and whether investment missions should be financed on a per nation rather than region basis to avoid high costs and poor enabling environment. The continuation of OPIC missions at the same level as previous efforts is thus called into question.

C. Finance and Venture Capital

While a lack of capital and competitive financial markets is a key obstacle to business development, most efforts to promote financial instruments have not been successful, because, as market-conditions indicate, most of SSA lacks the prime conditions that usually attract and maintain capital: a sufficient rate of return and predictability. Inflation and high taxation erodes the value of money. Financial markets are very small and the size of their potential business does not merit investment of resources. Private capital needs to understand what are and will be the general rules of the game in both government regulation and implementation as well as in markets. Capital abhors political and economic uncertainty and a climate of unpredictable corruption. Trust is critical. Only after this basis is established will capital markets begin to look at Africa seriously and invest in both production and markets.

Most African banks lend to large customers and for trade. They are reluctant to lend to small business and take local currency risk. The loans on their books weakens their credit worthiness. In many countries, the World Bank and the I.M.F. impose stiff credit and liquidity ceilings, limiting loans to 3%-10% of asset capitalization; Banks prefer to use their scarce resources for established, less-risky and favored clients. Beyond this, high interest rates and closing fees are too high for small and medium-sized entrepreneurs to support, especially in areas with small markets. These businessmen also lack collateral for many loans.

Expressed in other words: even though a dearth of finance is a prime reason for the lack of African development, donor assistance

generally lacks sufficient pull to attract private capital because basic investment conditions for profit and security are not adequate.

There does remain some room for donor assistance. The Africa Bureau should continue to inform and pressure SSA countries to establish an attractive environment for financial instruments through continue dialogue, networking and cooperation with the IMF. It should assist in developing financial policy, independent monetary authorities and stock markets. Support should continue to be provided for networks of financiers, regional meetings of public sector authorities and seminars on financial techniques such as debt swaps or venture capital organizations. Where reforms are being undertaken, the Bureau should assist in developing financial skills.

However, efforts to explore creative financial mechanisms have not yielded beneficial effect. Attempts to provide support for financial instruments to serve as an underpinning for financing of the growing entrepreneurial class, which currently lacks access to credit, while well-meaning are not cost-effective. Work to expand micro-African financial institutions (such as tontines, La Financiere movement) into larger activity has not yielded noticeable benefit.

Venture capital efforts have been extremely slow, yielding minimal benefits given cost-expended. In some cases, venture efforts are working to subsidize other multilateral assistance in quasi-private sector activities rather than supporting local entrepreneur activity.

D. Assessment, coordination and monitoring

The Africa Bureau has provided periodic assessment of its performance. But there has not been any general monitoring of ongoing private sector activities in Africa, where enabling environments are effective and where they are not. This has not been within the mandate of the Africa Bureau, to date. However, some ongoing monitoring mechanism should be established to provide the Agency and missions with guidance as to current and future programs. Enforcement of conditionality provisions is critical for maximum economic usage of assistance funding. In those nations and areas where enabling environments are not succeeding, assistance should be reduced and negotiations with government officials begun. In those nations where success is greatest, additional help should be provided.

Coordination should be increased with other donor agencies at Agency and mission levels. In those nations where there has been policy slippage, the Agency to take a strong position with multilateral donors to alter policy. The reverse is also true.

Similarly, coordination is critical to avoid overlap of donor activities as well as competition between multilateral or bilateral donors for specific projects.