THE PRIVATE SECTOR AND DEVELOPMENT EFFECTIVENESS

- DISCUSSION PAPER FOR TUDCN MEMBERS -

THE ROLE OF THE PRIVATE SECTOR IN DEVELOPMENT EFFECTIVENESS Although this subject has been little explored until recently, the aid environment is undergoing profound change and is now seeking growing corporate involvement. This paper aims to identify the main issues and challenges related to the role of the private sector in development, to serve as a useful basis for discussion for the TUDCN, so that it can also define its position on the subject ahead of HLF 4.

The paper draws from a variety of sources, including official development institutions, trade unions, NGOs and consultants, etc. It is enriched by the first positions adopted by the various stakeholders, including members of the Network during the last general meeting.

1. Defining the private sector

Defining the private sector is an essential stage in reaching any understanding of current practices and the role the sector should be given in development policies. The efforts hitherto made to give it an official definition have, however, only resulted in a rather vague consensus. The OECD's very broad definition of the private sector, for example, includes "private corporations, households and non-profit institutions serving households", whilst others strictly limit it to the corporate and business world. The meaning given to the term in practice is nonetheless clear: it relates to private investors, i.e. **for-profit enterprises** - and, secondarily, **private foundations**. These long-standing privileged partners of official development policies seem set to see their role boosted in the future; they constitute what we understand here by "private sector".

An added difficulty lies in the fact that companies alone bring together a wide variety of actors whose interests, contribution and impact with regard to the development process differ. They range from large multinationals to micro-enterprises, SMEs to cooperatives, and even informal economy structures. In the context of development effectiveness, it is, moreover, important to distinguish between the role of domestic companies and foreign multinationals, as their interests can in some instances be conflicting[1].

2. The interest in studying the role of the private sector in development effectiveness

The private sector is an actor in the aid system

Growing private sector involvement is one of the main trends affecting development policies. Its impact is all the greater given that companies can be found at practically every level of the aid system, their involvement ranging from a being source of development financing to being a beneficiary of official development aid (ODA) or to managing a project within the framework of public-private partnerships.

The prioritisation of trade in the development strategies being witnessed today has its origins in the *Aid for Trade* initiative set up by the WTO in 2005. The latter covers aid to fund the technical assistance and infrastructure linked to trade and strengthening productive capacities; it represents around **a fifth of total ODA**[2].

Several bilateral and multilateral aid institutions have, furthermore, expressed their will to raise companies to the rank of privileged partners in their development policies. A group of bilateral aid agencies thus expressed their position in an official statement, as follows: "Rather than considering it simply as a donor, we choose to recognize the private sector as an ***equal partner around key development issues***[3]." A similar position is held by the OECD Working Party on Aid Effectiveness, which is counting on the signing of a joint statement with private sector representatives at the end of the Busan Forum.

[1] *The Role of the Private Sector in the Context of Development Effectiveness*, Penny Davies, 2011
[2] OECD/WTO (2011*), Aid for Trade at a glance 2011: Showing Results*
[3] Bilateral Donors' Statement in Support of Private Sector Partnership for Development (from development agencies of Austria, Denmark, Finland, Germany, Japan, Norway, USA, Sweden, Switzerland, UK), 2010

INVOLVING THE PRIVATE SECTOR: A PRIORITY FOR DEVELOPMENT INSTITUTIONS

The budgets allocated to ODA in the context of the global economic crisis are constantly under threat. Development agencies are therefore increasingly trying to base their actions on the contributions of third parties. But more than the financial constraints, what actually drives donors to seek private sector involvement is the **conviction that companies are more effective in promoting growth and fighting poverty.** In developing countries, achieving these goals hinges on creating jobs and income, stimulating innovation and technology transfers. For the Belgian Development Cooperation agency, and many similar institutions, **ODA alone is not sufficient to eradicate poverty but needs to be "used as leverage for creating sustainable and inclusive growth", and the private sector has a key role to play in this respect[4].**

Following the same logic, a large number of development experts, particularly those with a private sector background, contest the idea that ODA contributions should be increased. Noting that there has been no overall reduction in developing countries' dependence on ODA over recent years, they argue that the best strategy would be to redefine traditional aid instruments and to devote a larger part of the funds available to mobilising private investments. They have shifted from the logic that "more is better" to "less is more"[5].

Finally, this growing recourse to the private sector is also taking place in the name of implementing the Millennium Development Goals, most particularly those aimed at reducing extreme poverty and promoting global partnerships for development. In spite of this, **there is still no consensus between the agencies of the donor countries, companies and civil society organisations (CSOs) on how best to engage with the private sector in the context of aid efficiency**.

[4] Stakeholders meeting of the Belgian Development Cooperation, May 2011
[5] Draft Final Report to the European Commission: *The Role of Private Sector in Development*

3. Forms of private sector involvement in the aid/development system

Corporate involvement in the aid system poses a major challenge: how to align the aspirations of an actor motivated by maximising profits with development goals? This also begs the question of what we understand by "development" and how it is linked to the concept of economic growth.

A. Companies, aid beneficiaries

Donors never formally identify private companies as aid beneficiaries but as strategic partners in the efforts to support inclusive growth in developing countries. It is nonetheless clear that the direction taken converges with the interests of companies, some of which receive direct ODA subsidies. The civil society organisations (CSOs) that have addressed this issue have expressed their concern at seeing funds intended for development ending up in the hands of private companies.

Development cooperation supports the private sector in several ways:

- **Indirectly, by promoting an enabling environment for private sector development** and advocating the type of economic and fiscal reforms that encourage companies to invest**.** As indicated in the World Bank's World Development Report (2005), the aid allocated by the majority of the multilateral and bilateral development agencies to improving the business climate amounted, on average, to USD 21 billion a year between 1998 and 2002[6] (total ODA was USD 78 billion in 2002[7]).
- **Directly, by making expertise, training and development cooperation financing available to companies investing in developing countries.**

…A risky bias

One of the main problems posed by companies supported in this way by ODA is that, unlike other aid beneficiaries, they are not accountable for their impact on development. Making them accountable in line with principles of aid effectiveness (Paris Declaration, Accra Agenda for Action) is, therefore, a key challenge ahead.

Another issue underlined is the fact that the private sector entities supported within the framework of these policies are, first and foremost, multinational corporations from the North[8]. Moreover, whilst "tied aid" is a practice that is officially disappearing on the whole from development programmes, it is returning under a difference guise, Eurodad points out, as illustrated by the public-private partnerships programme of the German cooperation agency 'developpp.de', which is only open to companies from donor countries[9]. In cases where it is the large corporations from developing countries benefitting from the aid, the risk is that the ODA funds may be misappropriated, and never actually reach ordinary people, owing to the blurred distinction between the economic and political elite.

---

[6] *Promouvoir l'Investissement privé au service du Développement : le Role de l'APD*, OECD, 2006
[7] Source : OECD
[8] Eurodad Conference Report, *The Private Turn in Development Finance: Fit for Development?,* 2011
[9] *Ibid.*

Finally, official development institutions tend to promote private sector involvement in general, without considering the differences in the nature or the size of the private sector in question, or its specific impact on development. Although their programmes may take on board the national market and local companies, they do not, for instance, give them priority over the opening of markets to foreign investments and the export economy. Yet it is proven that their respective impacts on development are very different and that each requires specific provisions. As underlined by Charles Gore, "*a private sector led approach which does not pay attention to the nature of the private sector will inevitably fail*"[10].

B. Public-Private Partnerships

As with the "private sector", there is no clear consensus on what does or does not constitute a PPP. For the OECD, a public-private partnership consists in "arrangements whereby the private sector provides infrastructure assets and services that traditionally have been provided by the state, such as hospitals, schools, prisons, roads, etc". Nothing is said of how PPPs should be implemented, it is simply stated that "they should involve the transfer of risk from the government to the private sector"[11].

Formally, PPPs are established by a contract or a series of contracts in which the private partner agrees to deliver a clearly defined service. The public partner, for its part, focuses on the objectives the project should meet, the price and the quality of the service. There is a wide variety of PPPs that differ in terms of the form of collaboration, their size, the number of partners involved, their duration and their geographical reach.

The World Bank was the first multilateral institution to advocate PPPs for infrastructure projects in the 1990s, followed by bilateral aid agencies. In 1999, the UN followed their lead with the Global Compact, in a bid to secure the collaboration of global companies in the implementation of its social and economic rights policy. These non-binding commitments are, however, difficult to verify[12]. Finally, during the International Conference on Financing for Development in Monterrey (Mexico) in 2002, governments underlined the importance of PPPs in the context of stagnation or a fall in ODA, with a view to meeting the MDG.

PPPs have therefore seen substantial growth both in the North and the South, although developing countries constitute the main geographical area turning to PPPs. This trend can be explained in part by the shared interest of several actors in engaging in this type of partnership:

- **governments**, looking to make savings as well as to improve services in terms of efficiency, technical expertise, innovation and risk management;
- **companies**, looking to cover risks thanks to the use of public resources in a difficult economic climate;
- **international development cooperation**, which encourages PPPs in order to compensate for the fall in ODA. This is used to improve the quality of projects, to reduce certain risks and increase profitability.

A recurrent criticism made of PPPs, often resumed as "private gain, public pain", stems from the fact that the risks are often unequally shared between the private operator and the public, which finds itself having to bear

[10] *Short Course on Key Issues on International Development*, *Building Productive Capacities in LDCs as a Means to Reduce Poverty*, Charles Gore, 2007
[11] OECD Glossary, www.oecd.org
[12] Eberlein Christine, *" Comment concilier rentabilité et développement ? Une ONG s'interroge",* Annuaire suisse de politique de développement, Vol. 24, n°2, 2005

most of the burden. Doubts have also been expressed concerning their ability to foster the creation of quality jobs[13].

The view that PPP implementation around the world has had mixed results is shared by the partnerships' critics and supporters alike. The former nonetheless insist on the need to draw from the "best practices" and success stories. The success of PPPs relies on careful risk sharing and a solid enabling environment created by capable states, which represents a challenge in itself. PPP failures are deemed to be owed to unequal risk sharing, the lack of competitive and transparent procurement, or poor contract enforcement and follow-up mechanisms.

In the context of aid, in addition to the dangers posed by tying PPP contracts to be executed in developing countries to companies from the North, as referred to above, there is also a risk that projects will be designed to meet the donors’ and service providers' expectations, based on agreements between the aid agencies and the companies and involving little or no consultation with the population concerned[14].

C. Private financing for development

Private foundations

The large private foundations, mainly from the United States, have been influential in steering aid development policies since their very beginnings. They are progressively claiming a more prominent role. The phenomenon is particularly visible in the area of global public health, where large foundations work with states to help them tackle epidemics, such as HIV/AIDS. Their involvement in global public health is not without consequence, contributing to issues of governance[15].

Acclaimed for their large networks, their flexibility and limited red tape, private foundations also enjoy the advantage of being free from the constraints of political cycles. A new trend, "philanthrocapitalism", has recently emerged, contending that the principles governing the business world and the business models can be effectively applied to transforming society and resolving its problems. A closer look, however, needs to be taken at foundations' real impact on aid effectiveness, and especially at the source of the assets accumulated, which are often the fruit of returns from operations in developing countries, the export of profits and non-productive or speculative financial operations.

Private development aid is not without its perils, as illustrated with the criticism levelled by doctors and NGOs against certain foundations for their closeness to the major pharmaceutical companies and the purchase of products protected by patents rather than the promotion of generic medicines. The closeness of foundation with lobbies promoting private interests can be found in numerous sectors providing goods and services of public interest, such as agri-business, water or telecommunications. The growing involvement of philanthrocapitalists is also leading to a form of division of labour in the area of cooperation that, combined with the disengagement of governmental authorities, is favouring the privatisation of development cooperation.

---

[13] Danis Gabriel, *Les partenariats public-privé (PPP) : mythes, réalités et enjeux*, 2004

[14] Eurodad submission to the WP-EFF, *Public-Private Partnerships: Fit for development?*

[15] BERTHO Michelle, *Les fondations privées américaines et le développement au XXIe Siècle. L’exemple de la lutte contre le sida*

Finally, whilst it is true that philanthropic contributions can generate resources, limiting companies to a charitable philanthropic role has been decried in a UNDP report: "Because it lies outside the traditional business model, the benefits are measured in intangibles—such as reputation, risk reduction and license to operate—rather than the bottom line. It represents mainly short term, unquantifiable and unaccountable financial contributions."[16]

FOREIGN DIRECT INVESTMENT

International institutions such as the World Bank, the IMF or even the OECD have actively promoted foreign direct investments (FDI). The Monterrey consensus[17] also presents FDI as one of the main ways of financing developing countries' growth.

The impact of FDI on development is still, however, a highly controversial issue, especially in countries with economic and political weaknesses. Although the social impact of foreign investments can be positive, in terms of the transfer of skills to local companies or salaries (higher than the local average), many NGOs, trade unions and other CSO have highlighted the risks accompanying an influx of foreign investments in fragile states, such as the perpetuation of human rights violations, destructive environmental practices or tax evasion by multinationals. Links have also been established with a deterioration in workers' living conditions, in terms of health, rights at work and pay levels. When investments stagnate or are withdrawn, as seen since the beginning of the financial crisis, states that are over-dependent on FDI are left even more vulnerable.

4. ELEMENTS OF A TRADE UNION POSITION

A range of fundamental issues first need to be addressed in order to define a position on the role of the private sector in development; the ITUC, TUAC and members of the TUDCN have already adopted policy positions on a number of these matters. These will therefore serve as a basis for the deliberations of Policy Working Group.

- **What form should public and democratic regulation of the private sector's activities take?**

Given that private firms are primarily driven by the search for profit, they are not able to fully contribute to development without being subject to regulation. Without regulation, their activities may have negative repercussions for development. A fundamental aspect of the trade union position is, therefore, that it is **not up to companies to unilaterally decide on the terms of their contribution to development.**

1. STATES CAPABLE OF ASSERTING THEMSELVES…

… vis-à-vis private finance: Governments in both the North and South must try to establish solid public controls over private finance. This is especially the case in developing countries that have been pushed by donors and

[16] UNDP, *Unleashing Entrepreneurship: Making Business Work for the Poor*, 2004
[17] The Monterrey Consensus is a document that emerged from the International Conference on Financing for Development in Monterrey held in Monterrey, Mexico in March 2002.

international financial institutions to limit the role and responsibilities of the state, and have not developed the tools needed to control foreign investments and massive tax evasion. It is essential that they build their capacity to channel investments towards key sectors, in line with their national development strategies.

...in public-private partnerships: PPP projects must take into consideration all the stakeholders, which are not simply limited to the company and the users but also include the workers and local communities[18]. PPPs can lead to employment contracts switching over from the public to the private sector. In such cases, the state must ensure respect for labour rights, in such a way as to limit any transfer of potential risk from the state and the company to the workers (wage cuts, changes in working conditions, rescinding of collective agreements). In addition, as underlined by the ITUC, a PPP project should not lead to a redefining of society's expectations of it, to suit the partners' ends. These expectations should be considered in the same way as they would be if the private sector was not involved.

2. THE PRIMACY OF DECENT WORK

Regardless of the nature of the enterprise concerned (multinational, local, SME, micro-enterprise), attention must first and foremost be given to the **quality of the jobs created, based on the ILO's decent work agenda**.

3. SOCIAL DIALOGUE

The international trade union movement must assert its role as a social partner within the framework of a **global social dialogue, and promote governance based on collective bargaining**. Interaction with employers' organisations on the issue of the private sector's role in development has been limited thus far and a scaling up of the exchanges in the future would be beneficial.

• Integrating the principles of development effectiveness in companies' core business

Over and above philanthropic activities, **the need for companies to progress towards greater sustainability within the framework of their core business** is recognised as the most effective way for the private sector to influence development. This idea is shared by most of the stakeholders, including the donors and the CSOs.

4. FROM CSR TO CORE BUSINESS

The term Corporate Social Responsibility (CSR) broadly refers to the decision made by companies, on their own initiative, to integrate social and environmental concerns into their business activities and their relations with their stakeholders. The ITUC insists on the fact that **CSR must not substitute government action** and that promoting CSR is not an adequate response to flaws in national and international governance. CSR policies should, furthermore, ensure greater involvement of the workers, who are often not consulted or even informed about these practices within their companies, even when they directly concern them. CSR policies need, therefore, to be conceived in alignment with promoting social dialogue in the medium term.

Because CSR is a voluntary commitment and rests on the principle of free choice, the ITUC has called for it to be redefined, in line with society's legitimate expectations of the private sector and existing standards on

[18] TUAC, *Comments & Marked Up on OECD Principles for the Use of Public-Private Partnerships*, 2011

companies' conduct, such as the international standards enshrined in the ILO Conventions. For the ITUC, "CSR, which is about what business does and about what it wants to do, must not be confused with what society wants business to do."[19]

Integrating the principles of development in companies' core business also requires a clear definition of the concept, given the blurred distinction between the responsibilities of businesses and CSR.

5. RESPECT FOR THE INTERNATIONAL PRINCIPLES REGULATING MULTINATIONALS

There are two authoritative international instruments on the social responsibilities of multinationals, which set out the standards they should respect. They are the **OECD Guidelines for Multinational Enterprises** and the **ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy**. These texts are the fruit of multilateral agreements that go beyond the self-interest of companies.

In addition, the ITUC supports and calls for respect for the **United Nations guiding principles on business and human rights** and the **implementation of the recently published "Protect, Respect and Remedy" framework**, aimed at making businesses accountable.

6. PROMOTING THE SOCIAL ECONOMY

Social economy organisations are business models integrating development principles within their core activities, both through their form of governance and the goods and services they produce. They are able to play a crucial role in development by contributing to the creation of socially inclusive growth and employment. This therefore raises the question of their promotion within the aid system.

- ## Should ODA finance the private sector?

The question remains as to whether companies should continue to benefit from ODA finance or whether these funds should be directed towards local companies or social entrepreneurship. In any event, it is fundamental that companies benefitting from aid strive to respect the principles of the Paris Declaration and the Accra Agenda for Action.

Stéphanie Genteuil, ITUC

August 2011

[19] *Trade Union Guide to Globalization*, ICFTU, 2004