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Private sector in development: a trade union perspective

CSOPartnership for Development Effectiveness

Context

The increasing role of the private sector in development is very much linked to the agreement of the 2030 Agenda and governments commitment to meet the Sustainable Development Goals (SDGs). However, the implementation of the SDGs remains slow and unremarkable – the world is still replete with long standing challenges and issues such as poverty, marginalisation, and inequality.

In the context of Financing for Development, the Addis Ababa Agenda for Action highlighted the need for various sources for development financing to implement the SDGs. However, most emphasis is put on the private sector, to 'supplement' traditional, public funds.

Private financing is dominating the development cooperation discourse, and new mechanisms are being developed to support this including Blended Finance and the new guidelines for Private Sector Instruments (PSI). Both mechanisms are promoted by the Organisation for Economic Co-operation and Development (OECD), the consortium of mostly donor countries. The World Bank Group, on the other hand, is promoting an approach called Maximising Finance for Development (MFD) in an attempt to lure private sector investments and revive the global economy. This approach puts a focus on promoting Public-Private Partnerships (PPP) to funnel funds for infrastructure development. Governments have also been investing heavily on creating an enabling environment for private sector through various policy and legal frameworks, as well as spaces for consultations, dialogues, and lobbying (f. ex. ODA redefinition and efforts on ODA modernization).

Private sector in development: some introductory notions

→ **Private sector**: **Organisations that engage in <u>profit-seeking activities</u>** and have a majority of private ownership (i.e. not owned or operated by a government). This term includes financial institutions and intermediaries, multinational companies, micro, small and medium-sized enterprises, co-operatives, individual entrepreneurs, and farmers who operate in the formal and informal sectors.

It excludes actors with a non-profit focus, such as private foundations and civil society organisations.

→ **Private sector engagement**: The initiative to **engage the private sector in development projects aiming at obtaining development results**, which involve the active participation of the private sector, through the use of public resources such aid.

Private sector engagement can occur in any sector or area (e.g. health, education, private sector development, renewable energy, governance, etc.). Through private sector engagement, the private sector and other participants can benefit from each other's assets, connections or expertise witith the aim to achieve mutually beneficial outcomes.

Two very important concepts here for private sector engagement are financial and development additionality.

Private sector in development: some introductory notions

→ Some modalities for private sector engagement

- **Policy dialogue**: This includes policy-oriented discussions across sectors that aim to create or change policies or behaviour, including through the adoption of best practices and specific standards. Policy dialogue is characterised by varying degrees of formalisation and institutionalisation.
- **Technical assistance**: Mostly provided in the context of development finance, technical assistance includes the direct provision or funding for the provision of specialised advice and support to private sector actors.
- **Finance**: This includes transfers in cash, goods or services for which no repayment is required and transfers for which (re)payment is required to support specific projects, programmes or private sector entities. Finance includes **private sector instruments**, such as guarantees for example.

Private Sector Instruments: Blended finance

→ DAC members define blended finance as "**the strategic use of official funds including concessional tools to mobilise additional capital flows (public and/or private) to emerging and frontier markets**". Blended finance has three characteristics:

- leverage, the use of development or philanthropic funds to attract capital into deals (i.e. concessional finance);
- impact, investments that drive social, environmental and economic progress;
- and returns, in line with market expectations based on real and perceived risks.

→ For the EU, **blending** is an instrument for achieving EU external policy objectives, complementary to other aid modalities and pursuing the relevant regional, national and overarching policy priorities. Blending means the **combination of EU grants with loans or equity from public and private financiers**. The idea behind blending is that the EU grant element can be used in a strategic way to attract additional financing for important investments in EU partner countries.

→ For TUDCN, blending is **ODA which is used in combination with other forms of finance to catalyse private flows for development**. In general, catalysing or leveraging private flows for development often involves public finance in addition to aid. For example, an aid grant can be blended with a loan extended by a DFI to finance a private-sector project.

Blended finance

Table 1 — How aid can be used to leverage private finance

Mechanism/Instrument	Description – use of aid
Interest rate subsidies (blended loans/ concessional loans)	A grant is used to cover part of the interest payments. The project promoter thus receives a subsidised loan at below market interest rate.
Technical assistance for project design	A technical assistance grant is provided to a company to strengthen its design and increase the chances of accessing finance. It can also be used after finance has been granted in order to increase the chances of success. It is often combined with other forms of finance.
Loan guarantees	A grant is used to cover the losses of the lender in case of default so that it agrees to finance the project or to do so on better conditions.
Structured finance – first loss piece	Donors offer finance with a lower repayment priority than the debt issued by other financiers. In case of default, donors would absorb the losses first. Mezzanine loans are a form of structured finance.
Equity investment	A grant is used as a direct capital contribution to a company or investment fund, usually in order to send a signal to other investors or cover for first-losses and attract additional capital.

Private Sector Instruments: Public-Private Partnerships (PPPs)

→ PPPs are contractual **arrangements between the state and the private sector that entail a risk sharing between the two**. In this contractual agreement, the private sector provides infrastructure assets and services, that traditionally have been provided by government, such as hospitals, schools, prisons, roads, bridges, tunnels, railways, and water and sanitation plants. The partnership arrangement delineates partners' roles and responsibilities, risk sharing, and distribution of financial and nonfinancial benefits.

→ The term PPPs is currently being used to refer to anything from informal and short-term collaborations between non-governmental organisations, the private sector and/or government agencies; to more complex and long-term contractual arrangements in which the private sector participates in the supply of assets and services traditionally provided by the government.

→ PPPs are at odds with traditional procurement schemes, and are seen by trade unions and CSOs as a backdoor for privatisation of essential public services. Evidence shows that PPPs make public service provision more expensive, therefore undermining the inclusive development goal. However, PPPs are being more and more promoted to leverage funding for infrastructure development in developing countries.

Development Finance Institutions (DFIs) (1)

→ Unlike other forms of aid flows traditionally managed by aid agencies, leveraging or blending instruments generally involve **more specialised financial institutions**. The natural choice of donors has been to rely on DFIs to manage aid funds and blend them with other public and private finance.

→ National and international DFIs are specialised development banks or subsidiaries set up to support private sector development in developing countries. They are **usually majority-owned by national governments** and source their capital from national or international development funds or benefit from government guarantees. This ensures their creditworthiness, which enables them to raise large amounts of money on international capital markets and provide financing on very competitive terms.

→ It is very difficult to get an accurate picture for all DFIs, as not all donor countries report aid used for blending in the same way – which has lead to difficult discussions at the OECD – DAC on the matter. Different reporting practices make it very difficult to estimate the exact amount of aid being channelled through DFIs for blending purposes. With the modernization of ODA, **collaboration between DFIs and aid agencies is more and more increasing**.

Development Finance Institutions (DFIs) (2)

→ **Bilateral DFIs are either independent institutions**, such as the Netherlands Development Finance Company (FMO), **or part of larger bilateral development banks**, such as the German Investment and Development Company (DEG), which is part of the German development bank KfW. They are both among the largest DFIs worldwide.

→ The main bilateral DFIs include: OeEB (Austria), BIO (Belgium), BMI-SBI (Belgium), IFU (Denmark), Finnfund (Finland), AFD/Proparco (France), KfW/DEG (Germany), CDP/SIMEST (Italy), FMO (Netherlands), Norfund (Norfund), SOFID (Portugal), COFIDES (Spain), Swedfund (Sweden), SIFEM (Switzerland), CDC Group (United Kingdom), OPIC (United States).

→ **Multilateral DFIs are private sector arms of international financial institutions** (IFIs) that have been established by more than one country, and hence are subject to international law. Their shareholders are generally national governments but could also occasionally include other international or private institutions. These institutions finance projects in support of the private sector mainly through equity investments, long-term loans and guarantees. **They usually have a greater financing capacity than bilateral development banks** and also act as a forum for close co-operation among governments.

→ The main multilateral DFIs include: AFDB (African Development Bank), ADB (Asian Development Bank), EBRD (European Bank for Reconstruction and Development), EIB (European Investment Bank), IDB (Inter-American Development Bank), IFC (International Finance Corporation), ISDB (Islamic Development Bank)

DFIs – fit for purpose?

→ **DFIs were not built to manage and deliver aid flows**, there are important concerns about their ability to deliver results and achieve positive development outcomes.

→ **DFIs are ill-equipped to manage aid flows in line with existing best practices**. DFIs rarely show a good level of performance in any of these areas: Mandate & Eligibility; Participation of social partners; Standard on worker's rights and OFC; Monitoring; Transparency; Complaint mechanisms.

→ DFIs do not have adequate systems in place to **guarantee the ownership of development projects** by developing countries' governments and stakeholders

→ Current practices and systems used by the DFIs **cannot generally guarantee a minimum level of accountability** when using aid funds or other public resources

Existing business accountability mechanisms

→ In a globalised economy, a large number of instruments have been created **to offset the dominant power of market dynamics**. Many have underlined that the enforcement of social and environmental standards are needed as companies take excessive advantage from the lack of institutional constraints.

→ As matter of the fact, several international standards act together on the global scene with the aim of keeping all governmental and non-governmental actors compliant with **a minimum set of fundamental standards**, mitigating the democratic deficit of the global governance.

→ Such instruments are normative or procedural with the attempt to introduce transparency and accountability in the way private actors behave (e.g., Global Report Initiative, Global compact, OECD Guidelines, etc.). They operate **triggering relationships between business, trade unions, stakeholders, local authorities, states, and international organisations**.

Existing business accountability mechanisms

- ILO Declaration of Principles concerning Multinational Enterprises and Social Policy
- OECD Guidelines for Multinational Enterprises
- OECD Guidelines on Due Diligence
- United Nations Global Compact
- United Nations Guiding Principles on Business and Human Rights
- Transnational Company Agreements (TCAs)-Global Agreements

Ongoing (not agreed): Binding Treaty for TNCs and other enterprises and Human Rights.

Issues at stake, challenges and policy trends within key institutions

OECD-DAC

→ ODA modernisation & private sector instruments reform

→ Total Official support for Sustainable Development (TOSSD)

→ Principles and Guidelines on blended finance

→ CRSs reform and donor support to decent work

OECD GPEDC

→ Principles and Guidelines on Private Sector Engagement in Development Cooperation

Arenas of action: DAC high-level and senior-level meetings, national delegations to the DAC (minister of international development), national governments, meetings of the GPEDC, including senior and high – level meetings.

Issues at stake, challenges and policy trends within key institutions

European Union / External Investment Plan (EIP) / European Fund for Sustainable Development (EFSD+)

→ Encourage investment in partner countries in Africa and the EU Neighbourhood region, promoting inclusive growth, job creation and sustainable development and so "tackle some of the root causes of irregular migration".

→ The Plan will encourage private investors to contribute to sustainable development in countries outside of Europe.

→ With a contribution of €4.1 billion from the European Commission, the External Investment Plan is expected to leverage more than €44 billion of investments by 2020. To enhance the firepower and the efficiency of the new Fund, the Commission wants EU Member States and other partners to contribute.

→ The EFSD+ will ensure world-wide coverage for blending, guarantees and other financial operations. The External Action Guarantee will have a capacity of €60 billion to guarantee the EFSD+ operations, as well as macro-financial assistance and loans to third countries. The European Commission intends to pay particular attention to the EU Neighbourhood, the Western Balkans and Africa as well as countries experiencing fragility or conflict, least developed countries and highly indebted poor countries, or regions with critical infrastructure and connectivity needs.

Arenas of action: European Commission, national governments, MEPs, national and European DFIs, European Investment Bank (EIB), EU Policy Forum on Development

Issues at stake, challenges and policy trends within key institutions

United Nations/ILO

→ Accountability of private sector in SDGs

→ FfD discussions on blended finance, domestic resource mobilisation, tax justice

→ Talks for a UN Treaty on Business and Human Rights

→ ILO: resolution on contribution of supply chains to decent work & SDGs / Discussion on effective development cooperation (2018 ILC)

→ Promotion of decent work (SDG 8) and social dialogue as drivers of sustainable development

Arenas of action: SDGs regional and global forums, UN Development Cooperation Forum, Financing for Development Follow-Up Forum, ILO ILC

Key asks

→ Claim same access and space to policy-making that private sector enjoys, in the spirit of social dialogue;

→ Ensure that private sector is subjected to strict eligibility and reporting criteria to benefit from ODA; as well as adheres to Development Effectiveness Principles and to the SDGs;

→ Ensure financial and Development additionality;

→ Condition future ODA allocation to performance and compliance with business accountability mechanisms

→ Mandatory global frameworks for business accountability, including risk analysis on social, economic and environmental levels, highlighting risks identification, mitigation and avoidance, including grievance mechanisms in place;

Thanks for your attention!

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