European network on debt and development

Conference report

The private turn in development finance:
Effective for development?

Organised by Eurodad and CRBM
Rome on 18-20 May 2011

Eurodad

The European Network on Debt and Development is a specialist network analysing and advocating on official development finance policies. It has 57 member groups in 19 countries. Its roles are to:

- research complex development finance policy issues
- synthesise and exchange NGO and official information and intelligence
- facilitate meetings and processes which improve concerted advocacy action by NGOs across Europe and in the South.

Eurodad pushes for policies that support pro-poor and democratically-defined sustainable development strategies. We support the empowerment of Southern people to chart their own path towards development and ending poverty. We seek appropriate development financing, a lasting and sustainable solution to the debt crisis and a stable international financial system conducive to development.
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Acknowledgements

Eurodad would like to thank its member CRBM for the invaluable support provided in organising this conference. We would also like thank the Gates Foundation, the European Commission and SOMO for their financial support.

The private turn in development finance: Effective for development?

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Introduction

The global financial and economic crisis has accelerated vast transformations in the current landscape of development finance. While ODA budgets are increasingly under threat, public development finance is increasingly being used to leverage private financial resources. This is taking place at a time when the patterns in private flows are swiftly changing – including through the increasing prominence of capital flows from emerging economies, and the changing landscape in global finance in the wake of the global crisis.

This context has, in the last two years, triggered the emergence of a new and controversial trend where private finance and the private sector in general are increasingly prominent in public development finance and policies. This comes from the perception that private sector development and – in particular – deepening developing countries' financial sectors is a key engine for "inclusive growth." Moreover, public development finance is increasingly using private financial intermediaries to (allegedly) reach out to poor and small businesses, and to leverage additional financial resources from private investors and financial markets in general.

Several concerns have been flagged about this trend which has been depicted by some as the ultimate financialisation of development finance, following a general trend which the global crisis has not yet managed to reverse. These concerns range – among others – from the lack of clarity on how this new turn in development finance will support positive development outcomes; its strong bias towards promoting Northern private capital flows; the absence of appropriate public regulation to manage their negative social and environmental impacts, including tax evasion and their potential to trigger higher debt levels in developing countries; or the abuse of financial intermediaries and new financial actors by development finance institutions to support private investments in the South.

In its 2011-2013 strategic plan Eurodad identified the issue of responsibility and development effectiveness of North-South private flows, and specifically private flows which count on some type of public support or guarantee, as a priority for the network in the coming years. The biennial International Conference which took place on 19 and 20 May 2011 in Rome provided a first opportunity to discuss thoroughly the concerns outlined above and lay the ground for future Eurodad work and positioning in this area.

The conference, co-organised by Eurodad member CRBM, gathered 101 participants from 31 countries, including 24 from the South. The main aims of the conference were to share knowledge and build capacity in order to increase understanding of the trends described above; identify common ground to position Eurodad future work according to priorities identified in the Eurodad 2011-2013 strategic plan; seek views from Southern partners; and identify linkages with other issues including those in the Eurodad work programme or covered by other CSO networks in order to forge wider alliances.

Some views from participants at the conference

“Extremely informative and interesting conference. You managed to give an overview of an extremely complex issue which was both frightening and constructive. Well done!”

“I have absolutely enjoyed every aspect of this conference, especially the content of the presentations and discussions. The organisation is also good. (...)”

“Innovative theme, diverse participation and discussion!”

“Congrats to the organisers for the attentions, logistics and the quality of the participants!”

“It was a very well organised conference. Liked the opening plenary most; Learnt a lot about the international financial scenario and the advocacy points for civil society. Major takeaway included understanding the issues of private finance in development and connecting with so many other people working on similar/related issues.”

“Energetic people! Impressing Eurodad staff, not only in Brussels but in Rome as well.”

“Congrats to the organisers for the attentions, logistics and the quality of the participants!”

Part 1

Plenary sessions

1 The old, the new and the ugly in the private sector of development finance

In the wake of the global financial crisis that started in 2007, private finance is increasingly prominent both in development debates and policies, and as a share of the overall amount of financial flows channelled to developing countries.

The two-day discussions at the conference identified several drivers behind this trend. On the one hand, aid levels are declining in several donor countries. Collins Magalasi from Afrodad pointed out that in developing countries "it is evident that there is a sharp reduction in external aid flows. However, at the same time, needs of developing countries are increasing as well as is pressure to developing country governments to meet the Millennium Development Goals (MDGs) by 2015." Moreover, there is a clear shift in the sectors prioritised by donor countries, shifting away from social development to an ever greater focus on private sector led growth. "According to some European governments' views, social investments have not led to self sustained growth in poor countries. This lack of progress has provided them with the excuse to shift their support towards private sector investments," said Sasja Bokkerink from Oxfam Novib.

Underpinning this turn, there is the perception that private finance should be leveraged to increase the amount of global finance flowing to developing countries, and the view that Northern private actors – ranging from financial institutions such as private banks or investment funds, but also multinational companies – are most effective in delivering development and in supporting private sector and financial sector development in poor countries. These widely-held official views were strongly contested by most civil society activists. Richard Ssewakiryanga, from the Ugandan National NGO Forum, asked: "How is it possible that the same institutions and

companies that took us into the global crisis are now being seen as the solution for taking us out?"

Indeed, as many participants at the conference highlighted, the track record of global private finance and Northern private sector investments in developing countries is extremely controversial. Several specific examples were put forward. Saviour Mwamba from the Centre for Trade Policy and Development, mentioned how most private investment and funds from International Financial Institutions (IFIs) in Zambia had overly focused on the extractive sector responding to profit-seeking interests of MNCs rather than in the type of investments which could deliver the best development outcomes for the Zambian people. These investments are well-known for having violated human rights, labour, social and environmental standards, and failed to pay their due share of taxes to the Zambian government. Moreover, "most of these investments only benefited the economic and political elites of our countries, rather than the majority of the population, let alone the poor," said Lidy Nacpil (Jubilee South, Philippines).

Numerous past experiences of private investments in the Global South show that at best private finance hasn't had a positive impact on the poor, and at worst it has had negative effects on human

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The private turn is not new; it is simply another tool to push for the financialisation of development and a second wave of privatisation.

rights, the environment and the poor. The lack of appropriate regulatory frameworks in developing countries – all too often the result of advice by donors and IFIs to de-regulate and weaken investment, trade, labour and tax policies among others – has prevented developing countries from reaping the benefits of foreign investments. The absence of public control over foreign finance and private investments has generated massive financial outflows (in the form of unpaid taxes, profit repatriation or debt service) and developing countries have been unable to channel these investments into strategic areas for national development, such as those outlined in national development strategies.

This trend is not new. "It is just an acceleration of an existing trend rolled over in the past two decades. The state and the democratic processes are being undermined, as it is the ability of the people to exercise public control over private interests. The result is rampant poverty and increasing inequality in the North and the South," said Nick Dearden from Jubilee Debt Campaign.

2 Blurring lines between public and private finance

There are new features in the current focus on private finance and private sector involvement in development which are distinctive from previous engagements in developing countries.

Firstly, private investments in the South are increasingly mirroring the developments that the financial system underwent in the last decade: the financial sector is attracting an increasing share of total foreign investments, gaining prominence in the sectoral distribution of financial flows to developing countries in what some observers call "the financialisation of the economy." Participants acknowledged that lack of access to credit has constrained the development potential in many developing countries and that this needs to be urgently addressed. However, they expressed serious concerns on the extremely unbalanced model promoted where foreign – instead of domestic – finance was systematically regarded as the only answer to developing countries' problems. "A functioning domestic financing system is needed, but it must be built on domestic resources if we will manage to reverse financial outflows that bleed developing countries' finances. Also, the type of global finance and private financial institutions which are increasingly investing in developing countries' financial sectors do not respond to the strategic needs of our countries, as outlined in national development strategies," said Beverly Keene from Jubilee South.

Secondly, increasingly sophisticated financial products and opaque investment funds are being used to channel private finance in the South, building on the financial engineering which characterised global finance in the last decade. "DFIs and IFIs are using ever more complex financial products which are hard to understand by civil society and activists. These institutions are not providing evidence that these are the best financial services and products to cater for the needs of the poor, and it is increasingly difficult for us to hold them accountable" said Iolanda Fresnillo from ODG in Spain.

And last but not least, development institutions are shaping up new roles for themselves as promoters of this private turn in development finance. The latter is of greatest concern for civil society groups which believe that development agencies and public institutions should be strongly guided by their development goals which often involve taming the negative effects of the market on the most vulnerable as well as engaging in counter cyclical policies – rather than simply following market trends.

Jesse Griffiths from Bretton Woods Project mapped out the different types of private flows which counted on some sort of public support or guarantee and explained the implications that this type of finance could have. There are different ways in which development agencies, Development Finance Institutions (DFIs) and IFIs support private financial flows to developing countries. They provide grants and concessional loans for private sector projects (which involve the use of ODA to subsidise the private sector). However, they

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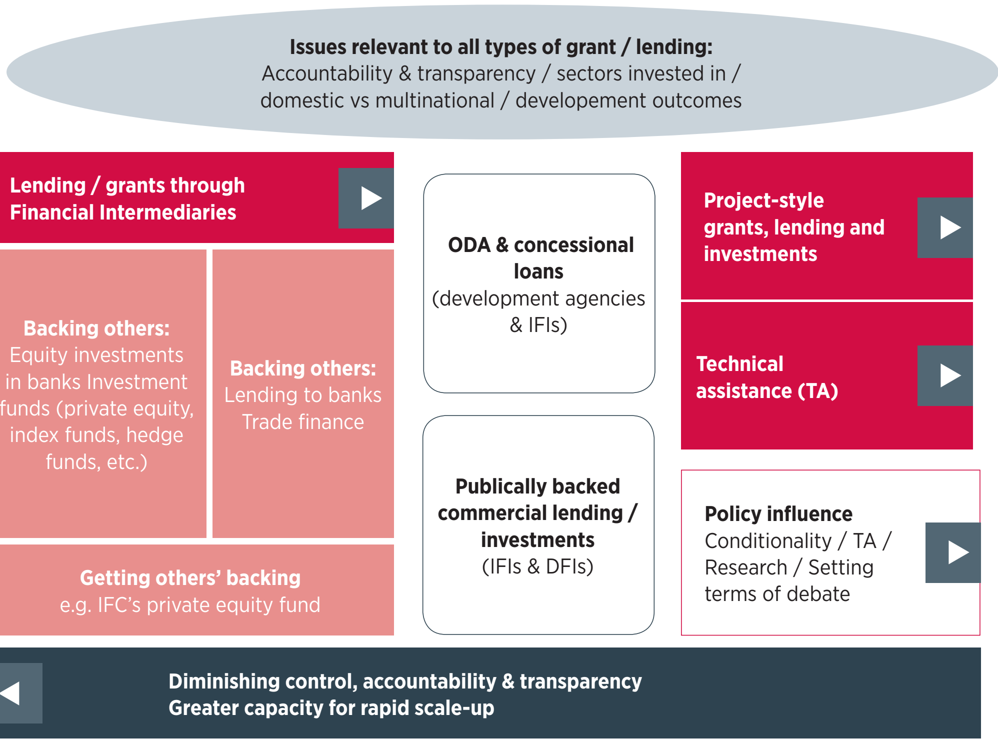
In the Netherlands, two thirds of all untied aid went to Northern private sector companies and private financial institutions.

also provide loans at commercial terms, equity investments, guarantees, and an increasing range of financial products such as quasi-equity, equity and debt funds, or structured finance. Increasingly, DFIs and IFIs are not only doing direct investments by using the abovementioned products, but rather they invest in financial intermediaries – such as commercial banks or investments funds, such as private equity and index funds.

Implications of these financing modalities include: "diminishing transparency and hence loss of public control and accountability over development finance as more money is channelled through intermediaries; increasing policy influence by private actors; and the capacity for DFIs and IFIs of rapid scale-up of their investments," Jesse Griffiths said.

On how private finance is influencing development policy, Collins Magalasi mentioned that "the private turn is not new; it is simply another tool to push for the financialisation of development and a second wave of privatisation." Savior Mwamba also expressed deep concerns on the lack of accountability of private investments – and particularly those that count on some type of support from development institutions – and on the possibility to reconcile development and profit-seeking goals (at least in the ways these investments have operated so far).



3 Current flaws in public support for private investments in the South

Many participants at the conference agreed that private sector and private finance are part and parcel of any economy and society. However, the devil – as always – is in the details. The private sector in general, and private finance in particular, is an incredibly diverse group with very different types of actors.

"When we talk about private finance and private investments, what are we referring to? It is important to differentiate between local and foreign investments, between big MNCs and small domestic cooperatives and social economy, and between global financial actors and – for instance – credit cooperative or national development banks," said Iolanda Fresnillo from ODG. Such differentiation is particularly relevant when it comes to deciding what types of private actors deserve public support because they face real constraints to financial access, to ensure financial inclusion for the poor, and to identify the private sector that is best placed to contribute to the development model and can deliver for the poor. "There needs to be a nuanced approach to private sector investments. Not all actors in the private sector are the same," said Seamus Finn from Jubilee USA.

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The failure to establish public control over private flows is leading to the recurrent and very unfortunate situation whereby public institutions bear the risks and private actors enjoy the profits of these investments.

The problem identified recurrently throughout the discussions was that the type of private sector which is mostly supported by public development institutions is biased towards promoting large investments from Northern MNCs and global private finance institutions, which promote commercial interests from the North rather than the goals of equitable and sustainable development that development institutions are mandated to support.

Sasja Bokkerink from Oxfam Novib highlighted the risk of ODA and other sources of public development finance being used to subsidise Northern companies, thus making aid more responsive to commercial interests from donors than to poverty eradication goals. "In the Netherlands, two thirds of all untied aid went to Northern private sector companies and private financial institutions," she said. "The problem is that private investments obviously respond to profit seeking goals and do not have a mandate to target poverty reduction. Furthermore, private investments – and particularly those which count on some sort of public support – are largely unaccountable for their development results," she added.

This is even worse when global investors turn to developing countries as "they need higher returns to offset higher risks premiums. It is naïve to think that, without proper regulatory frameworks hardly existing in some developing countries, much of this will trickle down to benefit the poor," said Bernard Anaba from ISODEC in Ghana.

Representatives from Southern civil society organisations emphasised that, besides Northern companies, big firms from developing countries also benefit from support and subsidies from development institutions. This is problematic because the lines between economic and political elites in developing countries tend to be blurry and all too often Northern support to these companies does not translate into real profits for the broader population.

The fact that investments supported by public development finance are supply- rather than demand-driven was yet another problem highlighted by most participants. "Excess liquidity in the North and in global financial markets is driving the new wave of private financial flows to the South. It is not driven by the needs of countries and their peoples," said Beverly Keene from Jubilee South. "The current situation should remind us of the excess of liquidity channelled to developing countries in the 1970s which triggered the dramatic debt crises of the 1980s. We do not seem to learn the lessons of the past," she added.

The fact that these flows are mostly driven by strategic interests from the North and by global investors is also evidenced by the destination of these flows. Magalasi provided figures of publicly-supported private investments in Africa which are heavily concentrated in resource rich countries and extractives sectors. This does not necessarily respond to the strategic development priorities of some recipient countries and their national development plans, let alone the needs of the poor people in these countries.

4 Losing public control over development finance

Underlying the flaws of current private investment in the South is the failure to establish strong public control over private finance, both in the North and in the South.

Development agencies, DFIs and IFIs fail to support private investments in ways which target the types of investments that would contribute to sustainable and equitable development. In a nutshell, instead of disciplining private flows to strengthen their responsibility and development outcomes, all too often they just follow the market or even respond to commercial interests of Northern countries and global finance.

In developing countries, decades of deregulation and the push by donors and IFIs to shrink the roles and responsibilities of the state have left developing country governments and, most importantly, their peoples disarmed of the necessary tools to control foreign investments and to shape up alternative sources of development financing which draw on domestic and regional finance. “The South must take proactive decisions on which kinds of foreign investments we want. However, the problem is international in their nature, as most of these funds flow in from rich countries” said Nacpil.

Paul Quintos from IBON (Philippines) mentioned how in practice the failure to establish public control over private flows is leading to the recurrent and very unfortunate situation whereby public institutions bear the risks and private actors enjoy the profits of these investments. “Public-Private Partnerships are a clear example of how this socialisation of losses and privatisation of profits is enshrined in a flawed partnership between the public and private sectors. The losses are then passed on to taxpayers, while private participation in service delivery all too often also translates into increased prices for the consumers,” he said. The citizens end up paying more and paying twice.

Sanya Reid Smith from Third World Network also mentioned the specific case of investment contracts and investment agreements systematically biased towards investors’ rights, which fail to deliver outcomes that contribute to the equitable development in impoverished countries.

After years of financial liberalisation and deregulation, development finance has ended up subsidising financial capitalism in what John Christensen referred to as “socialism for the rich.” Governments and the people do no longer have a say in what type of development model they want and what are the most effective ways to use public resources to contribute to equitable and sustainable development.

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Public-Private Partnerships are a clear example of how this socialisation of losses and privatisation of profits is enshrined in a flawed partnership between the public and private sectors.

5 Reclaiming development finance for sustainable and equitable development

Several participants strongly felt that at the heart of it all is the development model that we think can deliver best development outcomes, and which can deliver for greater equality and poverty eradication. "Not all investment is good for growth, and growth is not always good for development. This assumption needs to be further challenged" said Ane Schjolden from the Norwegian Forum for Environment and Development.

"The discussion we need to bring up is that of a different economic model which can deliver social and economic justice," concluded Julian Oram echoing the sentiment of many in the room. This must be a highly political discussion backed with strong social and political action. Many also felt, however, that technical expertise and discussions are much-needed to help increase CSOs' understanding of current trends in the private turn of development finance, and inform campaigns and political action.

First and foremost a distinction needs to be made between the types of global finance and investments that are currently absorbing most of public support for investments in the South, and types of companies and institutions that are needed to support effective development – such as Small and Medium Enterprises in developing countries, cooperatives, social economy or ethical financial institutions. Several participants felt that the latter deserves support by development institutions; however, this does not respond to the current business model of development agencies, DFIs and IFIs.

Most participants insisted on the need for development to be an endogenous phenomenon, driven by the political will and resources in developing countries. For this purpose, it is most important to stop the financial outflows from developing countries, in the form of ineffective aid which never reaches the ultimate intended recipients, tax evasion and avoidance by multinational companies, other types of capital flight and illicit financial flows, or illegitimate debt repayments. For this purpose, stricter global regulation is needed, but also greater policy space and bolder political measures by developing countries to manage foreign capital inflows to ensure they respond to the country's needs and to dampen down their damaging effects.

Regarding Northern private finance investing in the South, Ane Schjolden posed the question: "Should private capital flows be curbed or should we work for controlling these flows and mitigating their damaging impacts?" Anna Thomas from ActionAid responded that "assuming that private investments will continue to happen, we have to make sure that developing countries get the most out of it."

With regards to public support for these private investments, some participants felt strongly about opposing any role or financial transfer by IFIs and DFIs to the private sector given its poor track record and unproven development impact. However, others felt that private investments supported by public development institutions were likely to continue flowing regardless of our positioning. "The expansion of the private sector has become an unavoidable reality. At the African Development Bank, this type of operations will reach 50% of their portfolio by 2020" said Karim Trabelsi from l'Union Générale Tunisienne du Travail. Therefore, these groups felt that CSOs should call for these funds to support, for instance, smaller domestic companies and social economy, instead of big Northern multinationals and global banks and investments funds. Along the same lines, some groups also felt that CSOs should call for strengthened transparency and accountability of these flows; to ensure their responsiveness to developing countries national development priorities; and to ensure that they comply with highest development, environment, social and labour standards and human rights.

The general sentiment among participants at the conference was that in the absence of strong public control and regulation private finance – be it from the North or from domestic sources – could not live up to high standards of responsible finance and it could not deliver positive development outcomes. Stronger global and national regulation is needed, and this is an area where global CSO cooperation must be scaled up and strengthened. In order to achieve these, various proposals were made including strengthening the developmental role of the state, as well as the ability of CSOs and affected communities to have a say in what type of private investments are needed to respond to development needs. Justin Fong from Moving Mountains in China mentioned some experiences in his country and region in how "the state can play an active role in determining development, and not be just assisting the market forces." There are several cases where not only the state but also other public sector actors, such as community groups, have successfully delivered positive economic, social and development outcomes. "We need to de-construct the myth that the public is always less efficient than the private sector" said Pooja Parvati from Centre for Budget and Governance Accountability in India.

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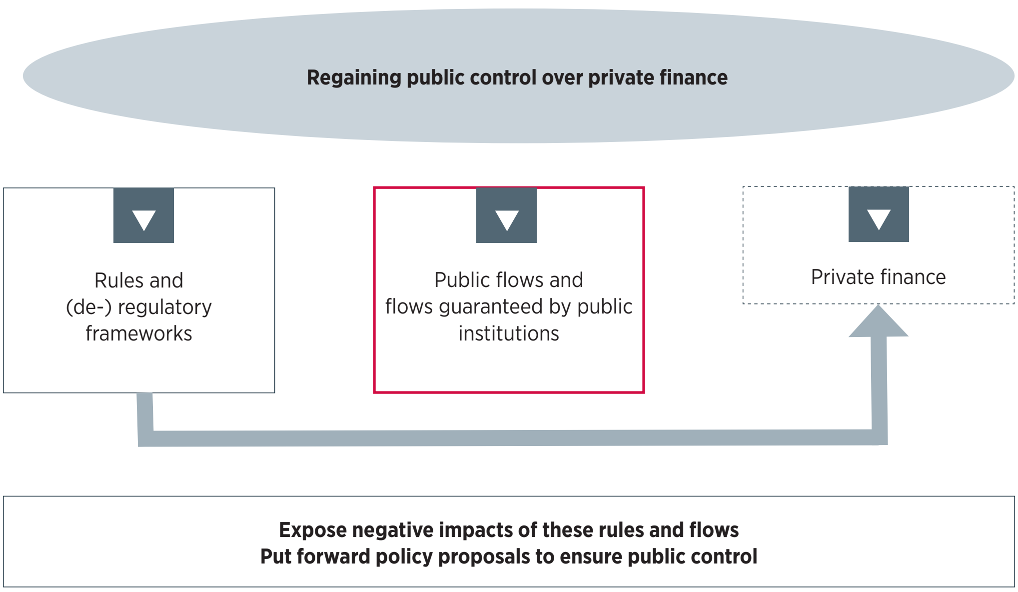

6 The road ahead: challenges and priorities for civil society

Between the call by some to strongly reject the current development paradigm and unfettered market deregulation that underpin a good deal of current development policies, and the perception by others on the need to engage in debates to mitigate its worst effects, Lidy Nacpil highlighted: "There are some reforms that help changing the system, but not all reforms do that. What we need to do is to stop and to make it difficult for private capital to cause damaging effects in our countries. Different groups can take different strategies, as long as we all work towards the same objectives."

All participants agreed that coordinated action is needed to expose current business models and flawed DFI and IFI support to the private sector, and to scale up pressure to discontinue support for companies and financial institutions that have negative development impacts. Further efforts also need to focus on unveiling MNCs and private financial institutions negative impacts on development and scaling up public pressure against these practices.

Participants also felt strongly about the need to reclaim public control over private finance and over public development finance. To this effect, it is crucial to strengthen coordinated action by Northern and Southern CSOs. While Northern CSOs can pressurise Northern and Northern-dominated global institutions to stop pushing further deregulation of global finance, Southern groups need to push their governments to stop entering into agreements that further disarm them from exercising control over private financial flows.

Specific actions were mentioned to advance the above-mentioned goals. Just to mention a few: legal action against MNCs where cases of violation of human right or responsible financing standards were identified; Southern CSOs pushing their governments to reject multilateral courts for investment arbitration or signing loan or investment contracts which do not yield positive development outcomes; or change the burden of evidence by calling development institutions to provide evidence that the private sector interventions they support deliver positive development outcomes.

Above all, the need to build broader coalitions and reach out to a broad range of activists, social movements, trade unions, from the North and the South was identified as the key to advance CSO demands on this area.

Part 2

Break-out sessions

Interactive plenary sessions at the conference were combined with break-out sessions which allowed for in-depth discussion on the implications and linkages of the private turn in development finance with other issues in the Eurodad work programme (aid effectiveness, developing countries' debt, capital flight and responsible financing). Below are the summaries of the specific discussions, challenges and policy proposals identified during these sessions.

1 Aid effectiveness and the private sector

In the mid of the 2000s, progress towards the MDGs was supposed to be driven primarily by ODA. However, lately aid is increasingly seen as a catalyst for mobilising private capital flows. Additional to this civil society has started to deal with other financial inflows and outflows to developing countries play a significant factor in their positive and negative developemnt. Since ODA represents only a small share of world GDP and the financial flows to developing countries, other development finance flows needs to be development effective as well.

In Europe, new centre-right governments are advocating for business-friendly approaches to development cooperation – including the EC's new approach to "inclusive growth", and the OECD's focus on the private sector as a development actor in the aid effectiveness process. Bilateral donors such as Germany, Sweden and the Netherlands are increasing the share of ODA set aside for Public-Private Partnerships (PPPs) or for full implementation through private actors.

The private sector has different roles in development cooperation: Private firms are contractors in aid-funded projects; partners in Public Private Partnerships; recipients of ODA; and they also become increasingly important providers of aid, e.g. in form of philanthropy.

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Aid indeed has the potential to contribute to job creation and private sector development. Unfortunately predominantly in the North, what is not the intention of development aid.

Private companies as aid contractors

Most relevant to development is their role as contractors: At least one third of ODA goes to private firms through the procurement of goods and services needed for development projects. Whereas the aid effectiveness agenda foresees to untie aid and procure more locally in order to improve the developmental impact, more than 60% of aid-funded contracts still go to Northern firms. "Aid indeed has the potential to contribute to job creation and private sector development. Unfortunately predominantly in the North, what is not the intention of development aid," said Bodo Ellmers from Eurodad.

Public Private Partnerships

Paul Quintos of IBON stressed that the new trend towards PPPs was driven by the perception that private sector can deliver more efficiently, but also by fiscal constraints of governments. This is matched by the fact that the financial crisis has made the private sector become risk-averse and seek risk-mitigation through PPPs. In this light, PPPs are "private gain – public pain". Civil society is concerned with the development model they promote and how to align the private profit motive with public welfare. Norayda Ponce of Social Watch highlighted that in Guatemala PPPs have created very little jobs, and those are of questionable quality from a decent work perspective. Another limitation of PPPs has been their high volatility over the past twenty years, which made them an unpredictable source of development finance.

The extent to which aid effectiveness principles apply to PPPs seems to vary. The selection of projects is often donor-driven, consisting of an agreement between aid agency and the private firm with little to no consultation of affected citizens which are supposed to be the ultimate beneficiaries. Hence, PPPs are often supply driven.

Particularly striking is that some PPP programs such as Germany's developpp.de programme are only accessible for firms from donor countries. Thus, PPPs become a new case of tied aid and a subsidy of foreign investment of transnational corporations, to the detriment of private sector development in developing countries: Local firms are excluded from the business opportunities and risk-mitigating benefits that PPP programmes offer.

Transparency is also an issue since the project lists, conditions, and rationale for project selection are not publicly disclosed in all cases. This makes it difficult for citizens to monitor such projects.

Applying aid effectiveness principles to the private sector

The aid effectiveness principles of Paris and Accra were primarily developed for government-to-government aid, and private finance is of a very different nature. There was however consensus that private finance needs to be development effective too. Aid effectiveness principles can give guidance, together with existing frameworks on responsible financing, corporate accountability and social responsibility, human rights treaties and decent work conditions. Participants thought, however, that the private sector needs to be held to account under aid effectiveness principles, at least in all cases in which they receive aid monies. Further discussion is needed on the question whether the private sector should have a separate process to develop its own development effectiveness principles, as CSOs did with the Open Forum that resulted in the Istanbul Principles.

There was also no clear view if private firms should receive aid funds, with some participants arguing that some private actors such as cooperatives or smallholders actually do need and deserve support.

What next?

Participants agreed that there is a need for CSOs to engage because the issue of aid and the private sector is already on the official agenda. There is however a need for additional research and evidence gathering. We lack evidence and a deeper understanding on the quantitative relevance of ODA-backed PPPs, the procedures of selecting and implementing them, and their developmental and poverty impact. Such evidence is needed to put our advocacy and campaigns on a firm footing.

On private sector development, CSOs need a clear position on what private sector we want, and what development cooperation can and should do to assist the development of such a private sector.

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2 Publicly-supported private capital flows

The breakout group on publicly supported private investments addressed a variety of CSO concerns regarding the turn to the private sector by development agencies, including how public development institutions mobilise private capital flows (so-called leverage); to the roles foreign investment should play; and the types of financial mechanisms being employed by development finance institutions (DFIs).

DFIs are the main vehicles of public finance for the private sector and raise several major concerns in terms of their development impact. Chief amongst civil societies concerns were issues of accountability and additionality.

Additionality

The additionality of public sector investment in private enterprises was brought to task by Oriana Suarez of Latindadd. She noted that in Latin America public investments in the private sector differed little from private investments and were primarily focused in the extractive industries. As there is no lack of capital available for extractive industries it is unclear what development role public finance plays in these investments. The International Financial Corporation and other DFIs claim that their added value to development is that they bring access to financial instruments that would otherwise be unavailable in developing countries. In Latin America this is clearly not the case. This point was expanded on by Nick Hildyard of The Cornerhouse who noted that "decades ago an Indian company could not raise money on capital markets," now, however, not only can they raise private capital but are even providing it to other developing countries. This raises the question of what role are DFIs playing in these markets if they can no longer be considered "frontier financiers."

The type of additionality that DFIs claim to have was picked up on by Jesse Griffiths of the Bretton Woods Project. He pointed out that their main argument lies on their ability to leverage funds from the private sector for development purposes. With some DFIs claiming leverage ratios of 1:25, for every €1 of public money they can leverage €25 of private money, this implies a huge influx of cash for development purposes, most of which does not come from the public coffers. The reason DFIs can leverage this kind of funding is because they are either implicitly or explicitly backed by governments which reduces the amount of risk associated with the investment for the private sector. This risk is then passed on to the public sector which can be positive in frontier markets which would otherwise not have access to finance, but as previously pointed out, most of DFIs investments are in countries that already have access to external capital. With all the risk transferred to the public sector, what would happen in the face of another financial crisis?

Accountability

One of the largest challenges with publicly backed investment in the private sector of developing countries is that the private sector has no development mandate. Getting the private sector to align with development principles is quite challenging for DFIs. Jeroen Kwakkenbos of Eurodad pointed out in his presentation that DFIs have a tremendous amount of difficulty in demonstrating development effectiveness and are particularly weak when it comes to monitoring and evaluation. DFIs are themselves aware of this difficulty. The initial stake by DFI's can be swallowed by private investment altering the focus of the project from development to profit. Confidentiality agreements between investors further complicate accountability issues.

Peter Lanzet pointed out that the DFIs themselves can be quite opaque as they tend to be structured more along the lines of a bank than of a development institution. This lack of transparency is highly problematic as it makes accountability almost impossible. Furthermore the reliance of the private sector on tax havens and secrecy jurisdictions in the interest of remaining competitive in the marketplace is a further complication in determining accountability and whether they are appropriate vehicles for development. The usage of opaque financing instruments such as the European Financing Partners (EFP) and the IFC Asset Management Company (AMC) further obscures accountability as well as blurs the line between public and private sector investment.

What next?

Participants in these break-out groups concluded that publicly backed private flows have serious issues in demonstrating development and financial additionality and clear accountability. A discussion was held on how to respond to these new challenges and what actions to take. In this discussion it was mentioned that other institutional models such as the Bank of the South need to be given a closer look as effective alternatives. Clear rules on responsible investment need to be established where control lies within developing countries rather than external to them. This control would allow developing countries to align private sector investment with national development priorities.

Such rules could be included in agreements between IFIs or DFIs and private investors or financiers, as well as used as indicators to measure the development impact of these investments.

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Clear rules on responsible investment need to be established where control lies within developing countries rather than external to them.

3 Developing country debt and commercial lending

The debt group kicked off with a mapping exercise where posters on the wall soon made it clear that the sovereign debt and debt creating mechanisms are more complex and perhaps less transparent than ever. Key questions asked were: What new mechanisms used by DFIs and IFIs to support private sector investments are debt creating? What are the main drivers behind new indebtedness?

One of the main complicating matters is the financialisation of economics and of development finance. Wiert Wiertsema made a strong call for stricter regulation of financial markets, including for pension funds and other institutional investors investing in developing countries. "The question is: will these new funds also become new debts? Will the debt created through these instruments be legitimate or illegitimate?" he asked, referring particularly to massive infrastructure projects funded by private investments.

Another hot topic was how to tackle the high levels of private debt and the indirect mechanisms allowing private debt to turn into public debt liabilities. Although the use of sovereign counter guarantees for private debt has become rare, there is a high risk that private debt turns public once a financial crisis hits. Domestic debt is another issue that requires more attention as the levels for this type of debt are getting alarmingly high, especially in highly indebted poor countries.

The complex situation triggered the question of whether current debt campaigning needs to adjust to new challenges. "The debt movement has generally been very focused, and that has been a strength" said Lidy Nacpil from JSAPMDD. "However, now we need to draw a broader picture, including issues that are around and linked to debt, for example private investments" she added.

For some, financialisation and the socialisation of private debt in both Southern and Northern countries provide the grounds to revisit the concept of illegitimacy of debt. "The crisis within the EU is an opportunity to talk about debt and to challenge the system as such" said Beverly Keene of Jubilee South, calling for a deepening of our analysis of how these new developments relate to the reproduction of a model of accumulation and concentration of wealth.

Although agreeing that we face a complicated scenario with new roles for new institutions, Njoki Njehu underlined that the development impacts of debt creating flows are still the same and that we have to stick to the principle of justice. "It is the same game, but with new actors" she said. "Lines are not straight and there is a lot of grey area. What matters is what we do in this grey area. For us, the value of justice is consistently present regardless whether this is a new or old area" she added.

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One of the key challenges for the future is the imperative of building competent and motivated debt movements in the South.

What next?

The South North Platform for Sovereign, Democratic and Responsible Financing, the Afrodad borrowing charter, and the Eurodad responsible financing charter were mentioned as existing campaigning tools that could be applied to new debt instruments.

Participants also addressed the question of how to build alliances with Southern governments and empower them to stand up against dirty deals. Debt audits and an institutional independent procedure for debt resolution were also identified as initiatives that should be continued.

“One of the key challenges for the future is the imperative of building competent and motivated debt movements in the South” said Collins Magalasi from Afrodad.

4 Towards tax justice: addressing international and national issues

The main focus of the discussion lay around domestic resource mobilisation which was seen as the primary method of raising the necessary resources for national governments to fulfil local needs. John Christensen from Tax Justice Network warned of the increasing perception that governments are inefficient while the private sector is implicitly efficient. "We have to challenge this idea," he said. "Evidence suggests that massive market failures continue excluding poor people from markets; this is even more the case when the roles and responsibilities of the state are dramatically reduced."

Foreign investment and tax exemptions

Private equity has become an important share of foreign investment in developing countries. Private equity expects very high rates of return (often around 30%) and benefits from tax exemptions in several jurisdictions. The rise of private equity has been one of the reasons behind the race to the bottom on national tax policies, as countries compete to attract foreign investment. In some cases tax rates have turned "negative" as companies are receiving high subsidies. Pooja Parvati from CGBA stated that in India 8% of the GDP is being given as tax exemptions mainly to the corporate sector.

Panellists recalled that evidence shows that foreign investment decisions are not driven by tax exemptions only. In fact, FDI goes to stable countries that have infrastructure, natural resources and a cheap labour force.

Loopholes in the global tax system

"The loopholes in the global tax systems are to a great extent linked to the way Multinational Companies (MNCs), banks and private equity firms are allowed to operate" say Christensen. Large MNCs often have a network of hundreds of affiliated companies in different countries. In some of these countries, MNCs conduct substantive economic activities, but this is not always the case. For instance, all too often they have affiliates in secrecy jurisdictions for the purpose of shifting profits generated by the company in order to benefit from very low or close to zero tax rates and from a veil of secrecy that allow them to hide the real identity of the investors. An unofficial paper of the UK government found that 80% of FDI flows through offshore jurisdictions.

Another tax planning strategy followed more recently by MNCs is the registration of intellectual property rights offshore so the earnings derived from them can go untaxed. Moreover, abusive transfer practice strategies are used with intellectual property rights, management fees and other intangibles where it is harder to identify accurate market prices to regulate these transactions. Private equity is also involved in these type of activities, for instance, when a fund buys a company, strips it of all its intellectual rights, and sells it again.

The weaknesses of the existing OECD guidelines on transfer pricing are well known by private investors, which continue exploiting the loopholes to dodge taxes.

National and global challenges

Participants agreed that in order to move the tax justice agenda forward it is necessary to address both national and global regulation. At the international level, it is important to call for greater transparency and to push for the imposition of stricter rules on foreign investment. However, panellists stressed that no country should be over-reliant on external capital flows to finance its development. Therefore, countries should prioritise increasing the share of resources mobilised domestically.

At the national level, it is essential to strengthen local tax authorities to allow them to fight against tax avoidance and evasion. Civil society should be involved in these debates. Parvati mentioned CSO advocacy in India to support reforms to the tax policies to make them more progressive and the proposal to tax private equity. Santa Ana highlighted the possibility of imposing taxes on short term portfolio investments to prevent exchange-rate crisis and to attract longer term investments.

What next?

Participants identified several areas where further research and action should be taken.

More research is needed to deepen CSO understanding of investment vehicles such as private equity, as well as some investment activities such as mergers and acquisitions, to better grasp the tax loss these activities represent for the public purse.

Participants also called for a clear set of guidelines that prevent public institutions lending or investing in companies that are registered in offshore jurisdictions, or which do not comply with country-by-country reporting standards.

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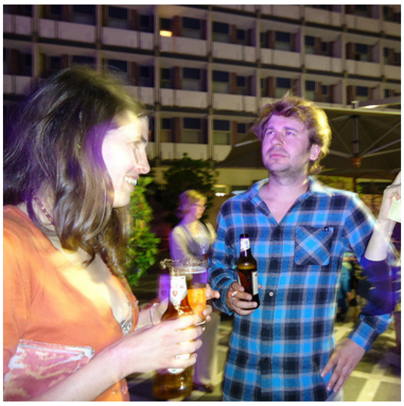
The loopholes in the global tax systems are to a great extent linked to the way Multinational Companies (MNCs), banks and private equity firms are allowed to operate.

... and we also had fun!



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