Enhancing private investment for development

Policy guidance for development agencies

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INTRODUCTION

1. On current trends, many developing countries are not on track to achieve the Millennium Development Goals (MDGs) and need to find new, more effective means of reducing poverty. There is consequently growing demand among developing countries and their development partners for greater guidance on how to promote faster, more inclusive patterns of economic growth that will help make substantial inroads into sustainably reducing poverty and lead to achievement of the MDGs. One of the ways such pro-poor growth can be achieved is through the mobilisation of more domestic and foreign private investment.

2. The mobilisation of private investment is essential for development. While public expenditure – whether by developing country governments or through official development assistance (ODA) provided by developed country governments – is required, it has become clear that the demand for finance outstrips that which the public sector can provide. The *Report of the International Conference on Financing for Development* (United Nations, 2002), known as the Monterrey Consensus, recognised that a substantial increase in ODA and other resources – including private investment – will be required if developing countries are to achieve the internationally agreed development goals and objectives, including those contained in the United Nations Millennium Declaration. Mobilising investment in developing countries can contribute directly to economic growth. The challenge for developing countries and their development partners is to identify the best ways to influence the conditions that lead to increased levels of private investment.

3. This guidance document focuses on the role ODA can play in helping developing countries to mobilise private investment. However, enhancing private investment should not focus on attracting foreign direct investment (FDI) alone. While FDI to developing countries has increased significantly in the last 20 years, the bulk of investment is domestic (World Bank, 2004a, p.26). Mobilising domestic savings and creating conditions that stimulate greater levels of local private investments are consequently critical ingredients for success especially in many of the poorest countries. Indeed, increased levels of domestic private investment should contribute to attracting more foreign investment as well.

4. This guidance provides development agencies with practical frameworks, tools and processes they can use to help mobilise domestic and foreign private investment in developing countries. The guidance offered is drawn from the experience of bilateral and multilateral development agencies working around the globe. It encapsulates findings drawn from research, programme monitoring and evaluation and good practice reports. This includes documented OECD lessons and best practice reports such as the recently released report entitled, *Mobilising Private Investment for Development: Policy Lessons on the Role of ODA* (OECD, 2005a).

5. A fundamental objective of this guidance is to help development agencies pursue a more strategic and co-ordinated approach to the design and delivery of investment-enhancing ODA. As in other domains, investment-enhancing ODA requires an understanding of the broader dynamics affecting private investment levels in developing countries. While specific country contexts vary – and need to be taken account of when all ODA is being formulated – previous research and development experiences have identified ways in which domestic and foreign investment can be enhanced through development-supported reforms. By learning from the successes and failures of the past, development agencies can refine their approaches and apply their resources in ways that are more likely to produce desirable, long-term outcomes and impacts.

6. When undertaking investment-enhancing ODA, development agencies can draw from a range of general guidance that has been prepared to improve the design, delivery and effectiveness of development co-operation, including the *Paris Declaration on Aid Effectiveness*. However, this document focuses specifically on the methods development agencies can apply to mobilise private investment in developing countries. This encompasses a set of development fields that significantly influence private investment, as well as specific tools and processes development agencies can use to increase the levels of private investment in developing countries. Moreover, the ways in which private investment can be used to increase the rate and expand the inclusiveness of growth are given special attention.

7. This paper is divided into two parts. Part 1 describes what development agencies do to improve the conditions for private investment and pro-poor growth. Part 2 describes the ways development agencies support reforms that lead to increased private investment.

PART 1

WHAT DEVELOPMENT AGENCIES DO TO ENHANCE PRIVATE INVESTMENT FOR DEVELOPMENT

8. The first part of this guidance focuses on what development agencies are doing to improve private investment for pro-poor growth. It begins with Chapter 1 by examining the importance of private investment for economic growth and sustainable poverty reduction. This chapter contains a description of the approaches development agencies can take to orient their ODA to reduce the constraints on private investment and enhance contributions private investment can make to pro-poor growth. It also provides a framework for development agencies to understand the different levels they can work at and the kinds of interventions they can apply.

9. Chapters 2, 3 and 4 then examine the role of investment-enhancing ODA at the macro, meso and micro-levels respectively. Each of these chapters describe the development fields that development agencies tend to focus on at these levels, the kinds of instruments they use to support reforms and key issues that influence good reform practice at this level.

10. Chapter 5 describes a number of the challenges development agencies face when supporting the mobilisation of private investment for pro-poor growth.

CHAPTER 1

THE IMPORTANCE OF PRIVATE INVESTMENT FOR PRO-POOR GROWTH

11. Private investment is an essential ingredient for sustainable economic and pro-poor growth. This chapter examines the importance of private investment and the ways domestic and foreign investment can promote pro-poor growth.

12. There are three sections to this chapter. The first section concerns the link between private investment, economic growth and poverty reduction. Here, the importance of private investment for economic growth and sustained poverty reduction is highlighted.

13. The second section considers the approaches development agencies take to improving private investment for economic growth and poverty reduction. This section examines approaches to increasing the volume of domestic and foreign investment before describing the approaches to ensuring that this investment leads to a sustained reduction in poverty.

14. The third section looks at strategies for investment-enhancing ODA. This section presents a three-tiered framework for reform interventions at the macro, meso and micro levels.

1.1 The imperative of private investment for economic growth and sustained poverty reduction

15. Public resources, whether from developing-country governments or from ODA are not enough to address the development challenges and goals faced by poor countries. Thus, private sources of investment are required (United Nations, 2002). These are not only necessary to supplement public resources, but also to fuel the growth of national economies and the creation of more and better employment opportunities.

16. Increasing private investment levels is fundamental to poverty reduction. Without it, developing countries are unable to spur the growth of their economies or to sustain the reduction of poverty over the long-term. A high rate of investment is one of the key differentiating features of countries that have sustained high rates of growth. In high-growth countries, investment typically exceeds 25% of GDP, whereas it struggles to reach 20% in low-growth countries. Where investment is low, the productive capacity of the economy fails to increase. This results in lower rates of growth and job creation, and fewer opportunities for the poor to improve their livelihoods.

17. Private firms are critical actors in the quest for investment and economic growth. Whether they are large or small, domestic or foreign, private firms are at the heart of the development process. "Driven by the quest for profits, they invest in new ideas and new facilities that strengthen the foundation of economic growth and prosperity" (World Bank, 2004a, p.1). "It is the absence of broad-based business activity, not its presence, that condemns much of humanity to suffering" says the Secretary-General of the United Nations (quoted in Day *et al.,* 2005).

18. While private investment has been found to boost the growth of all economies – from the most to the least developed – it is the least-developed countries that appear to inhibit private investment the most (World Bank, 2004b, p.3). Thus, investment-enhancing ODA is vital to support developing countries wishing to make the reforms necessary to achieve greater levels of domestic and foreign private investment. Development agencies can work with developing country governments, the private sector and

civil society to assess the conditions for investment and identify the constraints and barriers to increased levels of private investment. They can facilitate the transfer of information and experience to guide these reforms and they can build the capacity of domestic agencies to sustain reform processes over the long term.

1.2 Approaches to improving private investment for economic growth and sustained poverty reduction

19. This section describes the approaches that governments and the development agencies that support them can take to improve private investment for economic growth and sustained poverty reduction. Two interests are highlighted. The first concerns the ways that the levels of private investment can be increased. The second focuses on the ways in which increases in private investment can contribute to the sustained reduction of poverty. Here, the interest is in reform efforts that ensure the poor are able to participate in, contribute to and benefit from economic growth that is spurred by increased private investment.

Approaches to improving private investment volumes

20. Governments are required to become more investment oriented if they are to increase the levels of private investment. They should come to understand the factors that influence the dynamics of private domestic and foreign investment. Because private firms make investment decisions, governments and development agencies should work closely with the private sector.

21. The *DAC Orientations for Development Co-operation in Support of Private Sector Development*, published in 1995, define the private sector "as a basic organising principle for economic activity where private ownership is an important factor, where markets and competition drive production and where private initiative and risk taking set activities in motion." It is markets, through the process of competition, that determine what is produced and consumed. Thus, while private firms are key investors, they operate within markets that set the rules of the game; these rules determine the choices investors make, balancing perceived risks and rewards.

22. The investment climate determines the contribution private firms make to economic growth and prosperity. However, it is public sector policies and behaviours that play a key role in shaping conditions for investment. Thus, improving government policies and behaviours that shape the investment climate drives growth. Private sector development requires the development of markets that comprise the interplay between public policies, laws, regulations, norms, etc. – as well as private actors. These elements create a market in which private investors make their choices (Sida, 2003, p.26).

23. Increasing private investment levels requires an understanding of the conditions that influence the flow of domestic and foreign investment – otherwise known as the "investment climate". This refers to "the location-specific factors that shape the opportunities and incentives for firms to invest productively, create jobs, and expand (World Bank, 2004, p.1).

24. There are three key elements of the investment climate. The first of these is the cost of investment, which can be affected by many factors. Some of the most common are the regulatory burden and red tape, taxes, levels of corruption, infrastructure services, labour market regulation, and the cost of finance. The second element in the investment climate is risks. Policy predictability, property rights, and contract enforcement affect investment risks. The third element is barriers to competition. This is affected by the regulations controlling business start-up and bankruptcy, competition law, and entry to finance and infrastructure markets. Thus, the components that comprise the investment climate cover a broad spectrum of development interests.

25. Countries wishing to encourage positive investment decisions need to consider the risks, costs and rewards that influence these decisions and find ways to ensure the market for private investment performs competitively. While growth depends on private investment, private investment depends on a sound infrastructure and adequate human capital, both of which depend on an adequate level of national savings. Thus, aid-financed infrastructure development and human capital investments can make a vast difference in promoting investment, particularly foreign direct investment (United Nations Millennium Project, 2005, pp.45-46).

26. It is important to note that investment-enhancing ODA draws a lot from the experiences of development agencies that have supported private sector development. However, in contrast to the targeted approaches that many agencies have taken to private sector development (*e.g.*, financial and business development services), investment climate reform applies a broader, more systemic approach.

27. It is essential to engage with the private sector when identifying priorities for reform of the investment climate. In general terms, the private sector usually requires a stable and predictable investment climate. Moreover, issues such as transparency, reducing corruption, good public governance, strong rule of law, a sound macro economy, performing institutions and the right regulations are essential for sustainable investment and economic growth.

28. Reforming the conditions for investment requires a broad, systemic perspective on investment requirements and decisions. Annex 1 presents a brief overview of this range drawing from the perspective of various development agencies. These encompass elements that span the macro and meso levels of reform, outlined in more detail in Chapters 2 and 3.

Approaches to ensuring private investment contributes to sustained poverty reduction

29. Private investment alone will not reduce poverty to the levels set by the MDGs. The impact private investment and economic growth has on poverty reduction can be maximised through the reform of a specific set of policies laws and institutions. (See Annex 2 for the range of development fields that enhance the pro-poor outcomes of private investment.)

30. Private investment can contribute to sustained poverty reduction when there are greater opportunities for the poor to participate in markets, while also reducing their risks and vulnerability. Because there are many dimensions to poverty and its reduction – encompassing consumption and food security, health, education, rights, voice, security, dignity and decent work, as well as the influence of gender and environmental sustainability – there is a need for policies, strategies and institutions that focus on the full range of poverty experiences and causalities. However, when the conditions for private investment are considered, there is a specific set of approaches that can be applied to helping the poor maximise the opportunities that stem from increased private investment.

31. There are three areas that investment-enhancing ODA should focus on if it is to have the greatest possible impact on poverty reduction. The first is to improve the number, quality and variety of formal employment opportunities. As most employment is found in the private sector, this can only be achieved through reforms that make conditions for private investment more conducive to growth and to create policies and laws that enhance job quality.

32. The second area of reform that can lead to the reduction of poverty is the formalisation of informal enterprises. Poor investment climates encourage the private sector to act in an extra-legal manner and high levels of informality are an indication of a poor investment climate. The informal economy can stifle opportunities for growth and create barriers that restrict the full participation of the poor in the economy.

33. The third area of reform that can lead to the reduction of poverty is to improve the markets the poor operate in and the productivity of domestic enterprises, including informal enterprises. This can be achieved by increasing the assets of the poor as well as the competitiveness and terms and conditions of trade for domestic enterprises.

1.3. Strategies to improve private investment for economic growth and poverty reduction

34. There are a wide variety of fields development agencies can work within to reform private investment conditions for pro-poor growth. The selection of one or more fields to work in will involve the consideration of a number of factors, including:

- Investment climate assessment findings and agreement among key actors that these findings are accurate and present a priority list of starting points for reform.
- A perceivable demand for reform among key actors, especially government as well as the private sector.
- Recognised capacity of the development agency to add value to the reform required, as demonstrated by technical know-how, previous experience, sufficient funds, strategic relationships and trust among key actors.
- Practicalities of reform agendas – how specific reform requirements can be broken down into programmes within a defined period and with clear, measurable outcomes.

35. Most development agencies focus their limited resources on the issues they think matter and the ones they can do something about. Because not all elements of the investment climate satisfy these criteria equally, development agencies are required to prioritise and focus their attention on those elements that do.

36. If they are to maximise the development impact of their interventions, development agencies have to become more aware of the levels at which their interventions are designed and the partners they work with. While this does not suggest that development agencies must work at higher levels to achieve greater impact, it does mean that greater attention has to be given to the levels at which development agencies work, the synergies that can be created across these levels, and the kinds of interventions that are formulated at different levels.

37. There are three levels of reform activities: macro, meso and micro (see Box 1). A consideration of levels of intervention is important because it affects the strategic choices development agencies make when allocating ODA resources.

38. Investment-enhancing ODA often brings development agencies into contact with a wide range of possible programme partners. This range may be wider than in other areas of ODA, potentially encompassing political parties, the private sector, labour representatives and the media (see Box 2). The involvement of the private sector in investment-enhancing reforms – at all levels – is critical for success and sustainability. Thus, a number of agencies have developed programmes that build the capacity of private sector partners and facilitate their involvement in decision-making and consultative structures. Private sector involvement spans the domestic private sector in developing countries as well as foreign investors (who are often located in developed countries). Indeed, without the direct involvement of private sector in many investment-oriented reform programmes, the public sector and development agencies have neither the financial resources nor the technical and managerial expertise to make the changes that will significantly contribute to pro-poor outcomes and achievement of the MDGs.

Box 1: Overview of levels and intervention and relevant development fields	
Level of intervention	**Development fields**
Macro-level interventions	Macro-economic stability Budget and financial management, including debt stability Open and competitive markets Public-private dialogue
Meso-level interventions	Policy, legal and regulatory framework, includes: – Privatisation policies and programmes – Investment policies and laws – Taxation – Labour policies, laws and regulations – Competition laws – De-regulation/re-regulation and administrative reform Restructuring of state-enterprises Legal systems, including: – Rule of law – Contracts and commercial dispute resolution – Property rights Institutional reform Public and corporate governance Infrastructure and utilities development and management Trade capacity building and facilitation, including: – Strengthening trade-related institutions – Support in trade negotiations Financial services, includes: – Financial regulation – Mobilisation of domestic savings
Micro-level interventions	Investment promotion Private sector development, including: – Entrepreneurship promotion – Micro, small and medium enterprise development

Box 2: Actors affecting investment-enhancing ODA

– Business development service providers

– Financial service providers

– Government line ministries

– Investment promotion facilities (centres)

– Judiciary

– Local and district government authorities

– Local, community-based and civil society organisations

– Media

– National and provincial government departments

– Parliamentary and policy making institutions, including upper and lower houses, and committee structures

– Political parties

– Private sector, including multinational enterprises, domestic enterprises, firms of all sizes (from micro through to large enterprises), as well as different enterprises in specific sectors, women-owned enterprises, cooperatives, informal enterprises, agricultural and non-agricultural enterprises, urban and rural enterprises

– Private sector organisations, such as chamber of commerce, business associations, sectoral chambers or associations, regional and local chambers, and confederations

– Regulatory authorities

– Universities and academic research institutions

– Worker organisations

CHAPTER 2

SUPPORTING MACRO-LEVEL REFORMS FOR PRIVATE INVESTMENT

39. Development agencies can help improve the macro economic and political framework to generate greater levels of private investment for pro-poor growth. Indeed, there are a number of influences on private investment at this level that have drawn the attention of development agencies. However, because reforms at this level often involve broad, multidimensional interventions, not all development agencies can effectively support reforms at this level. Large multilateral agencies such as those in the World Bank Group have worked at this level in most developing countries for a long time. While bilateral agencies also work at this level, this is often with a narrower range of countries.

40. Multilateral development agencies are often seen as more neutral actors at this level, compared with bilateral development agencies that are more concerned with their own economic and political interests (White and Chacaltana, 2002). In either case, development agencies must respect the sovereignty of developing countries and recognise that macro-level development themes are steeped in the political dynamics of all countries.

41. Development agencies working at the macro-level tend to focus on a handful of critical development fields that affect private investment for pro-poor growth. There are four macro-level development fields that development agencies tend to focus on. To varying degrees, reform in each of these fields can be used to increase the levels of private investment as well the ways this investment can be used to sustain poverty reduction, such as through improving the access poor women and men have to markets.

42. The first of these is the promotion of **macro-economic stability**. Development agencies in this field help developing country governments to manage their economies better in order to improve the predictability of the national economy. Predictability is a key issue for many investors, especially foreign investors. "Economic and financial stability encourage investment and productivity, thus contributing to economic growth" (Government of Sweden, 2004, p.32).

43. The second macro-level development field is **budget and financial management**. ODA is used to help developing country governments manage their budgets more effectively. This often entails an emphasis on tax systems and revenues, ODA inputs and the management of debt.

44. The third macro-level development field for ODA is the promotion of **open and competitive markets**. This is undertaken to help developing countries become more fully integrated into the global economy and remove unfair or unnecessary barriers or constraints to domestic and foreign trade.

45. Finally, there is a significant interest in investment-enhancing ODA that supports better **public-private dialogue**. This can help establish high-level mechanisms that allow the private sector to present its views on macro-economic conditions and strategies.

46. Macro-level interventions typically involve working with national government agencies. In many cases this involves work with senior ministries such as the ministries of finance, planning or the office of the president or prime minister. It can also involve working with the national parliament, as well as with key social partners such as the private sector, organised labour and civil society bodies. Sometimes,

development agencies may work with opposition parties in an effort to get bipartisan support for macro-level reforms.

47. There are a variety of instruments development agencies use to support macro-level reforms. One of the most common is **policy development, research and analysis**. Development agencies will work with national government ministries and other national leaders to help them better understand the impact current policies and laws have on private investment levels.

48. Development agencies also support activities that help raise the **awareness** of politicians and senior public servants about policy alternatives and reform options. This often includes the exchange of information and best practices from other countries. These activities make government, the private sector and other macro-level actors more aware of the importance of an enabling environment for private investment, as well as activities that facilitate the sharing of information on how to improve the enabling environment.

49. ODA is also used at this level to support the development of new policy frameworks. This will often entail the use of **technical assistance** in the assessment of policies, the drafting of new policy frameworks and advising on strategies and implementation arrangements.

50. Investment-enhancing ODA is also used to **build the capacity** of central government ministries to carry out reforms or to manage the investment climate more effectively. This includes training programmes and management development programmes.

51. A common investment-enhancing ODA instrument at this level is the use of **budget and financial support**. The term “budget support” refers to the provision of funds which are integrated into government budgetary processes, while “financial support” refers to funds provided to government for more specific programmes. At the macro-level, it is more likely that budget support is used to bring about investment climate reforms.

52. Finally, ODA is often used to **facilitate dialogue** between the public and private sectors, or assist in negotiations between national governments and international agencies. Structured dialogue between the public and private sector can improve the quality of governance in three ways: by setting an example, by shedding light on the workings of institutions; and by improving the quality of advice the private sector gives to government (Herzberg and Wright, 2005, p.6).

53. When working at the macro-level, development agencies are advised to consider the following points:

- **Obtain political and bureaucratic support from the highest possible level.** The obstacles to reform that will be experienced can be overcome if there is strong, high-level support for reform.

- **Help key players to buy-in to the big picture of reform.** Many actors at the macro-level need to understand the broader vision of the importance of reform and how it will lead to major national economic and social development goals. The technical work to achieve this vision is often undertaken at lower levels.

Development agencies considering supporting macro-level reforms should reflect on the following questions:
• What other development agencies are working at this level? What reforms are they supporting and what is the purpose of these reforms? • Who are the main actors for reform at this level (*e.g.*, office of the president, parliament, ministry of finance, national federation of chambers of commerce, labour organisations)? • How can the development community in the country provide consistent macro-economic advice and complementary reform programmes? • What is the comparative advantage our agency brings to supporting reform at this level?

CHAPTER 3

SUPPORTING MESO-LEVEL REFORMS FOR PRIVATE INVESTMENT

54. Meso-level reforms affect the institutional arrangements for private investment. This is the most common level for investment-enhancing ODA. Working with the relevant policy communities, development agencies are active in a wide range of fields at this level.

55. The most common meso-level development field is the **policy, legal and regulatory framework.** This encompasses a wide range of policy, legal and regulatory domains depending on development interests and the identified need for reform.[1] Some of the most relevant aspects of the policy, legal and regulatory framework, include privatisation policies and programmes, investment policies and laws, taxation, labour policies, laws and regulations, and competition laws. It also includes de-regulation/re-regulation and administrative reform: The OECD (1997, p.6) describes regulatory reform as "changes that improve regulatory quality, that is, enhance the performance, cost-effectiveness, or legal quality of regulations and related government formalities". This can involve the revision of a single regulation, the scrapping and rebuilding of an entire regulatory regime and its institutions, or improvement of processes for making regulations and managing reform. Deregulation is a subset of regulatory reform and refers to complete or partial elimination of regulation in a sector to improve economic performance.

56. A major focus for development agencies in this field is the growing levels of informality in developing countries. Informality is often linked to weaknesses in the legal and regulatory framework. In addition, weak legal and regulatory frameworks often contain biases that disadvantage the poor. Another focus is reform of the legal system, which includes governance issues such as the rule of law as well as more specific concerns such as contracts and commercial dispute resolutions and property rights.

57. The **reform of institutions** is a focus for much investment-enhancing ODA. This deals with the capacity of government institutions to "own" and implement reform processes. Development agencies can stimulate debate around reform issues; they can also facilitate dialogue with private sector organisations, civil society and even the local media in these processes. The sequencing of reforms is also crucial and needs to take account of both feasibility and urgency of reform. An important sub-set of institutional reform includes is the support development agencies provide to improve the representation of the private sector.

58. **Public and corporate governance** is a development field at this level that is demanding more attention as a necessary requirement for investment-enhancing ODA. "Economic development stalls when

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1 In OECD work, "regulation" refers to the diverse set of instruments by which governments set requirements on enterprises and citizens. Regulations include laws, formal and informal orders and subordinate rules issued by all levels of government and rules issued by non-governmental or self-regulatory bodies to whom governments have delegated regulatory powers. Regulations fall into three categories: economic regulations (which intervene directly in market decisions such as pricing, competition or market entry or exit); social regulations (which protect public interests such as health, safety, the environment and social cohesion); and administrative regulations (such as paperwork and administrative formalities, the so-called "red tape" through which governments collect information and intervene in individual economic decisions). (Organisation for Economic Co-operation and Development 1997).

governments do not uphold the rule of law, pursue sound economic policy, make appropriate public investments, manage a public administration, protect basic human rights, and support civil society organizations—including those representing poor people—in national decision-making" (United Nations Millennium Project, 2005, p.31). Improving governance within public and private spheres has a significant influence on private investment. In the past, development agencies tended to separate their work in governance from private investment or economic development, yet it is clear that these fields of work are related and that there are benefits to linking these interventions wherever possible. Development agencies are increasingly recognising that improving the standard of corporate governance can have a significant impact on investment levels.[2]

59. Another major focus of investment-enhancing ODA at the meso-level is the **restructuring of state-enterprises**. This includes the privatisation and the restructuring of state-owned enterprises.

60. **Infrastructure and utilities development and management** have been long-standing fields of development for investment-enhancing reform. However, while the link between good infrastructure and increasing levels of private investment has become clearer, the DAC has noted that spending on infrastructure has declined in many developing countries and this has created a constraint for private investment (Hesselbarth, 2004). Recently, the Commission for Africa has called on development agencies to double their expenditure on infrastructure in Africa (Commission for Africa, 2005, p.13). However, the way development agencies undertake this work has changed. Growing attention has been given to improving the conditions for private investment into infrastructure development – and the improvement and management of utilities – in an effort to expand available resources for infrastructure and utilities, while enhancing the sustainability of these developments.

61. Development interventions in **trade capacity building and facilitation** have typically assisted trade-related organisations to become more effective, such as through the improvement of trade-related laws and regulations, the capture and use of trade information, the development and maintenance of trade networks and enhancing competencies in trade negotiations.[3] It also includes support to developing countries to improve their skills in trade negotiations.

62. Finally, ODA has been used at this level to improve access to **financial services**. While this includes financial services that are used by foreign and domestic investors, it also concerns financial services for the poor, which has become a critical focus for development agencies engaged in pro-poor growth. Meso-level financial service interventions include the reform of commercial banking regulations and improving the way domestic services are mobilised, while improving the quality of financial services is an important field of reform for the attraction of foreign investments.

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[2] For further guidance see the following OECD guidelines: *Guidelines for Multinational Enterprises* (2000), *Principles of Corporate Governance* (2004b) and *Guidelines on the Corporate Governance of State-Owned Enterprises* (2005b). In addition, Transparency International and Social Accountability International produced "Business Principles for Countering Bribery" in 2002. These principles serve as a guide for practical implementation the OECD *Convention on Combating Bribery of Foreign Public Officials in International Business Transactions*, the International Chamber of Commerce (ICC) *Rules of Conduct to Combat Extortion and Bribery*, and the anti-bribery provisions of the revised OECD *Guidelines for Multinational Enterprises* (Transparency International 2003). The United Nations has recently appointed a Special Representative to deal with the issue of human rights and transnational corporations and other business enterprises (Annan 2005). Benner (2005) claims that such initiatives create opportunities for business to work with the United Nations and that business needs a "core set of binding rules to credibly be able to counter accusations that its corporate responsibility initiatives are mere window dressing".

[3] See OECD (2001a). For an example of the way development agencies have contributed to trade-capacity building in three African countries, see United Nations Conference on Trade and Development and Japan Bank for International Cooperation (2005a, 2005b, 2005c).

63. Much of the work at the meso-level incorporates a "making markets work" perspective. This draws together all of the abovementioned development fields into a systemic model that describes the functioning of competitive markets for private sector development.[4] Special emphasis is given to the ways financial markets can be better regulated so as to improve access by poor women and men.

64. There are a variety of instruments development agencies use to support meso-level reforms. Among these, the most common are **capacity building** to improve the ability of government departments, regulators and other agencies to carry out reforms or to manage the investment climate more effectively.

65. Investment-enhancing ODA at the meso level often involves the provision of **technical assistance** and advice. This includes the provision of expertise in the design of new legal and regulatory instruments. A significant feature of this work has been the inclusion of regulatory monitoring and impact units within senior levels of the government bureaucracy. While these units can also inform the design of strategies at the macro-level, they have been particularly useful for improving the legal and regulatory regime for private investment. The use of regulatory impact assessments has featured prominently in this context.

66. Development agencies have supported **advocacy** efforts among the private sector. This contributes to building a greater demand for reform of the investment climate. This can include the facilitation of structured dialogue between the public and private sectors, as well as programmes that strengthen the organisational capacity of **business membership organisations** and the extent to which they represent the private sector.

67. When working at the meso-level, development agencies are advised to consider the following points:

- **Recognise the connections between development fields at this level.** Supporting reforms at the meso level is a multidisciplinary task involving work in a variety of fields (*e.g.* enterprise, economic, governance, livelihoods and infrastructure perspectives). While some agencies focus their efforts on only a few of the above development fields, most apply their programmes in a number of fields.
- **Create incentives for reform within the bureaucracy.** Much of the focus of reform at the meso-level concerns change-management within bureaucratic government organisations or parastatal and regulatory agencies. Institutional self-interest and individual reluctance to change can hamper these processes. It becomes necessary to find ways to overcome this resistance and introduce incentives for reform. This can include the regular use of scorecards that measure and compare institutional performance.
- **Winning the "hearts and minds" of officials.** Similar to the issue of incentives, government officials and regulators have to have a change of heart and mind if they are to embrace the reform agenda. Individuals within these organisations should be assisted to see the big picture and to understand how their efforts can contribute to this.

[4] For more information on the "making markets work" perspective see: DFID (2000), Sida (2003), World Bank (2002).

Development agencies that are considering supporting meso-level reforms should reflect on the following questions:
• Is there support for meso-level reform by the senior levels of government? • How can consistency of reform efforts be achieved across different government portfolios? • Do government officials understand the need for reform?

CHAPTER 4

SUPPORTING MICRO-LEVEL REFORMS FOR PRIVATE INVESTMENT

68. While improvements at the meso level help, they are not enough to maximise the investment potential in developing countries. Strategies are also required to promote appropriate micro-level or supply-side responses to increase the capacity of local firms to take up the opportunities that arise from an improved investment climate and greater international linkages (OECD, 2004a, p.6). Development agencies often support micro-level reforms to help private investors make better use of emerging opportunities for private investment.

69. Reforms at this level typically include **investment promotion** programmes that recognise the specific constraints or barriers to investment are that often found in developing countries. Many development agencies have worked with developing country governments to establish promotional instruments for investment. This can include the design and application of investment incentives (*e.g.*, tax incentives), risk mitigation programmes, and guarantees. The OECD is developing a Policy Framework for Investment, a non-prescriptive checklist of issues for consideration by any interested governments engaged in domestic reform, regional co-operation or international policy dialogue aimed at creating an environment that is attractive to domestic and foreign investors and that enhances the benefits of investment to society. The Framework can serve as a reference point for investment promotion agencies and development agencies as they assist developing and transition country partners in improving the investment climate, as well as businesses, trade unions and non-governmental organisations (NGOs) in their dialogue with governments (OECD,2004a).[5]

70. A number of OECD countries have employed home country measures to promote foreign direct investment to developing countries. This is done on the premise that there are market and co-ordination failures that deter investment and cause the social benefits to FDI to be greater than the private benefits. A recent review of these programmes in the United Kingdom and the European Union has found that one-stop-shops for outward investors could be useful to reduce potential confusion among investors (te Velde, 2003).

71. A particularly significant source of private investment into developing countries is found in the diaspora. In Ghana, for example, the government's campaign to attract the large expatriate Ghanaian community back to the country is starting to bear fruit. Many of those that may be reluctant to return anytime soon are nevertheless building homes for themselves to which they can retire. Remittances from the diaspora have become an important source of revenue for the government (Games, 2003, p.37).[6] The

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5 The PFI is part of the OECD Initiative on Investment for Development, launched in 2003 in Johannesburg, South Africa. The Initiative supports the agreements of the Monterrey Consensus and includes three inter-related projects: i) the development of a Policy Framework for Investment; ii) drawing lessons on the use of ODA in support of countries' efforts to mobilise investment for development; and iii) sharing the OECD's experience with investment policy peer reviews as capacity building mechanisms. The Policy Framework for Investment is being developed by a Task Force through a partnership process involving OECD Member and non-Member governments, in co-operation with civil society and other international organisations (Organisation for Economic Co-operation and Development 2004a).

6 The number of diaspora Ghanaians is conservatively put at two million people who, in 2001, were estimated to be contributing around USD 400 million to GDP.

"diaspora effect" has stimulated the growth of high-tech and other industries in several East Asian countries and India. It has been estimated that remittances to developing countries currently amount to USD 75 billion annually. This is 1.5 times the value of ODA (World Commission on the Social Dimension of Globalization, 2004, p.96). Innovative schemes are needed to transform financial flows from the many diasporas into long-term productive investment in their home countries (Commission on the Private Sector and Development, 2004, p.40).

72. Micro-level ODA has often included support for **private sector development programmes**. Mobilising private investment – whether from domestic or foreign sources – requires a vibrant and competitive private sector. Because of this, many development agencies have supported programmes that endeavour to develop the indigenous private sector, often with an emphasis on micro, small and medium-sized enterprises. Included in these actions are programmes that encourage entrepreneurship – which can take development agencies beyond business development interventions and into the education system and those institutions that shape personal behaviours and attitudes.[7]

73. In recent years, development agencies have questioned the impact and sustainability of providing financial and business development services to support the start-up and expansion of the private sector, especially among micro and small enterprises. The Donor Committee for Enterprise Development (formerly the Committee of Development Agencies for Small Enterprise Development) has established guidelines for development agencies working in these fields. There has also been increasing attention paid by development agencies to developing the market for financial and business development services. Enterprise growth initiatives should occur at multiple levels (*i.e.*, at national, sectoral and enterprise levels) and micro-level interventions have an important place among a mix of other interventions working at higher levels (Snodgrass and Winkler, 2004).

74. There are a variety of instruments development agencies use to support micro-level reforms. Among these, the most common include the use of **capacity building** and **technical assistance** that improves the ability of programme partners to design, implement and monitor programmes.

75. A great deal of attention has been paid by development agencies in recent years on the **monitoring and evaluation** of micro-level programmes. Development agencies are eager to ensure their support promotes sustainability over the long-term and has significant impact on the target audience.

76. When working at the micro-level, development agencies are advised to consider the following points:

- **Limitations of scale and sustainability.** While there are many benefits for development agencies in working at the micro level, development agencies should remain aware that much of the work at this level is expensive, limited by scale and difficult to sustain in the long-term. As a result, it is important for development agencies to ensure they have a well-defined exit strategy and/or can complement their work at this level with reforms at higher levels.

[7] The International Labour Office in Geneva, for example, is currently undertaking a project to better understand the determinants of a culture for enterprise. This information will be used to improve the ways in which entrepreneurship can be promoted as a part of a process to create more and better jobs in the private sector.

- **Micro-level work can improve the functioning of markets.** One of the greatest benefits of ODA that is directed to the micro-level is the contribution this can make to improve the functioning of markets. However, to realise these benefits, development agencies need to identify the reasons for the failure of markets and design their programmes to address these specifically. In this way, micro-level interventions can facilitate the sustainability of increased investment well beyond the period of the development-supported programme.[8]

Development agencies that are considering supporting micro-level reforms should reflect on the following questions:
• Will the programme tend to perpetuate market distortions or will it help to find ways for markets to work more effectively? • Can micro-level programmes find synergies with reforms occurring at macro or meso levels? • How can the potential for sustainability and greater levels of impact be enhanced?

[8] For more information on how micro-level interventions can improve the market for business development services, see Committee of Development Agencies for Small Enterprise Development (2001), Gibson (1999) and Tomecko (2003).

CHAPTER 5

CHALLENGES FACING DEVELOPMENT AGENCIES

77. As development agencies consider ways to mobilise greater levels of private investment that helps promote pro-poor growth they are faced with a number of new challenges. These challenges can take development agencies beyond conventional development fields and require them to work with a broader range of actors than previously. Indeed, investment-enhancing ODA presents a new paradigm for many development agencies, which creates a number of new practical challenges that affect the practices of development agencies. Five of the most pertinent challenges are discussed in this chapter.

5.1. Working with the private sector

78. Most other forms of ODA are designed around partnerships with government agencies or with civil society organisations such as non-government and community-based organisations. Investment-enhancing ODA draws the private sector closer into the development processes. Since private investment is based on the decisions of private domestic and foreign investors it makes sense to ensure these actors are more closely involved in the design and implementation of programmes. While this implies the importance of giving a voice to the private sector and establishing effective public-private dialogue, it also creates new opportunities for the private sector to participate more directly in a range of development activities. Given the right policy frameworks, the private sector can enhance the effectiveness and scope of investment-enhancing ODA as investors, operators and service providers.[9]

79. Some development agencies engage the private sector directly in an effort to design and deliver interventions that increase private investment for pro-poor growth. Initiatives such as the Global Reporting Initiative and the IFC's Sustainability Framework track private sector contributions to sustainable development, while the World Economic Forum's Global Governance Initiative scores corporate efforts towards the MDGs. These initiatives reflect an understanding that private investors can do more than provide philanthropic support to poverty reduction projects and can in fact contribute resources through strategic investments. The UN Growing Sustainable Business (GSB) initiative, for example, focuses on business-led enterprise solutions to poverty. Such solutions challenge the often-perceived unquantifiable risk and additional costs to business when dealing with the poor, causing potentially interested investors to place opportunities on the "too complicated" pile. The GSB describes its "value proposition" to business as helping address these challenges at relevant points in the investment cycle in order to reduce the risks and costs associated with private investment (UNDP, 2005).

80. The Commonwealth Business Council has promoted the role of governments and businesses in improving the business environment both separately and in collaboration with others. A recent manifestation of this is the Abuja Manifesto on Business – Government Partnerships for Removing Practical Obstacles to Wealth and Job Creation (see Box 3).

81. In many cases, investment-enhancing ODA requires a balance between working with the public and private sectors. While private sector partners are critical, the importance of public agencies cannot be forgotten. Governments are mostly in charge of reform processes and remain critical programme partners.

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[9] See Sida (2003, p. 21).

Box 3: The Abuja Manifesto: Government Partnerships for Removing Practical Obstacles to Wealth and Job Creation

Agencies such as the Commonwealth Business Council have promoted the role of governments and businesses in improving the business environment both separately and in collaboration with others. A recent manifestation of this is the Abuja Manifesto on Business – Government Partnerships for Removing Practical Obstacles to Wealth and Job Creation which states that:

Governments will:

- Set clear targets and realistic plans for investment in and provision of essential services such as infrastructure, education, health and water.
- Ensure a legal framework with timely enforceability of all contracts.
- Create a good business climate focused on predictability and simplicity of regulations rather than offering elaborate incentives to investors.
- Offer transparency of public fiscal affairs.
- Implement a continual program to lighten the regulatory burden on business, for example by making it faster and more affordable to start a company, employ staff, register assets or clear customs.
- Address constraints on competitiveness in national economies in order that domestic business can compete internationally and benefit from trade liberalisation measures.
- Improve public access to government services and the efficiency of these services by embracing an e-government strategy.
- Set mechanisms for regular consultation between the public and private sector at the highest levels.

Business will:

- Implement best practices for Corporate Governance and citizenship to meet high standards for each company and ensure widespread adherence.
- Integrate into the business model a work plan for investment in the workforce, local communities and the supply chain.
- Ensure that business activities are sustainable and avoid undue external costs on stakeholders or on society as a whole.
- Pay taxes and other revenues to the public treasury in accordance with the provisions of the law.
- Invest in ICTs to improve productivity and make increased use of e-commerce.
- Organise itself for constructive and cohesive dialogue with government in business policy formulation and assessing priorities.

Together governments and businesses should:

- Explore best practice on private sector participation in the provision of infrastructure and other public services.
- Implement common standards on Codes of Ethics and systems to eliminate corrupt practices in public and private organisations.

Source: Commonwealth Business Council (2003)

5.2. Balancing foreign investor demands with those of domestic investors

82. Many development agencies have established relationships with the investors from their own countries. It is common to see some degree of liaison between European investors, for example, and their embassies and national development offices located in developing countries. Such relations can be very useful for development agencies; they provide insights into how foreign investors experience the investment climate and business environment in a given country. However, it is important for development

agencies to look beyond the experiences of foreign investors, to understand the demands of the domestic private sector as well.

83. There are three reasons for development agencies to pay greater attention to the domestic private sector. First, domestic resources are much larger than actual or potential external resources. Second, there are vast informal domestic resources that can be tapped (*e.g.*, the potential value of land) that generally exceed the value of potential foreign investment. Third, unleashing the domestic resources in an economy is likely to create a more stable and sustainable pattern of growth (Commission on the Private Sector and Development, 2004, p.9).

84. Development agencies need to balance the views of domestic and foreign investors, rather than take a one-sided approach. This should include examining the impact the investment climate has on domestic and foreign investors to ensure there is a level-playing field.

5.3. Recognising diversity among private investors

85. Differentiating between domestic and foreign investors' demands and interests already demonstrates an understanding that not all investors are the same. The investment climate affects different kinds of investors in different ways. Thus, development agencies need to consider who are the winners and losers in any given situation. This will help to better understand the influence the investment climate has on private investment, as well as how reform measures will be welcomed or resisted.

86. A good illustration of this diversity can be found when the influence of gender is considered. Research has shown that macro-economic approaches to development are not gender-neutral but are actually gender-blind because they fail to examine the different ways men and women experience the investment climate (Klassen, 2004). The achievement of pro-poor growth therefore depends on understanding and responding to gender differentials in economic reform processes (Pinder, 2005).

87. Another example development agencies often face in this field concerns the experiences of micro and small enterprises in the investment climate. While it is acknowledged that in most developing countries the private sector is dominated by small enterprises, the question arises as to whether special attention should be given to small enterprises compared with large enterprises (Hallberg, 2001). Should the investment climate favour micro and small enterprises or should it provide a level playing field for all enterprises regardless of their size – or whether they are domestic or foreign? Naturally, the vast majority of small enterprises are domestic. While the special needs of small enterprises are acknowledged, most development agencies agree that biases favouring smaller sized firms can become disincentives to growth. Small enterprises may represent entrepreneurial endeavour, but there is no beauty in this kind of smallness. Many small enterprises can have low revenues, provide poor working conditions and insecure employment. Thus, development agencies are often required to help address the specific concerns of micro and small enterprises, but also to take a broader, economy-wide perspective of the private sector and ensure that the investment climate does not discriminate against enterprises on the basis of size.

5.4. Responding to informality

88. One of the greatest concerns for development agencies is the growing level of informality in developing countries. This refers to firms that are not registered with the government as well as the unreported activities and workforce of registered firms. The root causes for the increasing size of the informal economy in many development countries are overly stringent and expensive government

regulation in the labour, product and land markets and an ever increasing tax burden imposed on an ever shrinking formal sector.[10]

89. The size of the informal economy reflects some important aspects of the investment climate and business environment and can provide a focal point for development intervention. A large informal economy is not conducive to growing private investment. It distorts markets, reduces tax revenues and excludes many people from basic protections.

90. The growth of the informal economy is often a response to overly cumbersome regulations and laws, and corrupt and/or inefficient regulators. Thus, many enterprises – especially those that are small enough to remain hidden from official eyes – choose to avoid registering their business or their employees. As a result, the informal economy becomes a depository of people who are not absorbed in gainful, productive formal sector employment.

91. The informal economy in many developing countries is large both in terms of number of actors and in terms of contribution to GDP. It can provide a safety net for the unemployed, especially those from disadvantaged groups (*e.g.*, women, the handicapped, children, people living with HIV/AIDS). However, while it is highly dynamic, adaptable and resilient, the informal economy is generally characterised by low returns, low ability to enhance productivity and poor, sometimes appalling, working conditions. Indeed, the informal economy is a major source of livelihood of the poor.

92. The informal economy represents an important point of focus for investment-oriented ODA. Addressing the problems of the informal economy has the potential to have considerable impact on the incomes and welfare of poor and marginalised households.

93. Formalising the informal economy brings a number of benefits for private investment. It builds investor confidence by reinforcing the social contract between citizens and the state, and strengthening the reliability of agreements between firms; it broadens the tax base, reduces the cash economy and provides more resources for intermediation by the formal financial sector. Ultimately, the formalisation of the informal economy creates higher quality, better paid, more sustainable employment.

94. However, few development programmes specifically encourage the informal economy to formalize. Development interventions generally aim at creating a better business environment for small enterprises with the belief that the results will help the informal economy as well as the formal enterprises. Generally, development agencies do not differentiate between the formal and informal economies in the design and implementation of their interventions. Those development projects that do specifically seek to assist informal enterprises to grow have focused on training for entrepreneurs, provision of business advice, facilitating access to finance, granting property rights and addressing market access issues, rather than on removing regulatory and administrative barriers.

5.5. Improving governance

95. In the past, many development agencies separated their support for improved governance in developing countries from their support for economic development and investment. However, in recent years it has become clearer that there is a strong link between governance, economic development, investment and pro-poor growth (Jütting, 2003). Thus, investment-enhancing ODA opens opportunities for greater synergy between these to fields of intervention.

96. There are divided opinions regarding the purpose of reform in public governance. While there is general agreement on the demand for public governance reform to improve private investment, the

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[10] Palmade and Anayiotos (2005) claim that the Russian Federation, Sub-Sahara Africa, Latin America and Central Asia have the highest levels of informality, with the greatest increase since 1990.

direction this reform should take will vary from one country (and its political economy) to another. Reforms that reduce informality can be seen as contributing to a reduction in the scope for government interference in the economy. Less laws and regulations mean less opportunity for poor public governance to undermine investment, while focussing enforcement efforts on the main offenders. However, an improvement in quality of laws and regulations, rather than a simple quantitative reduction, and support for improving the institutions that enforce them is also an important reform agenda. By improving the accountability and transparency of public institutions, laws and regulations can, in the long-term, serve the interests of both domestic and foreign private investors.

97. Improving governance in order to achieve greater levels of private investment toward economic development and pro-poor growth often entails what has been described as the "governance agenda" for investment-enhancing ODA. The following topics are most commonly found on this agenda:

- **Drivers of change and the demand for reform.** Analysing the causes of change in a given country with a view to identifying the obstacles to reform and the ways change processes can be strengthened.

- **State and capacity building.** Helping state institutions perform their functions more effectively

- **Improving public-private dialogue.** Creating the conditions necessary to improve dialogue between the public and private sector

- **Improving governance in the private sector.** A response to the importance of corporate governance.

- **Designing reforms according to state capacity and country context.** Developing a better understanding of the kinds of challenges different countries face managing their economies and reforming their investment climate.

98. A major governance issue that directly affects the conditions for private investment is corruption. Corruption cannot be effectively addressed in isolation from other problems. Instead, reducing corruption requires a multi-pronged strategy. Critical is to reduce opportunities for corruption by cutting back on officials' discretionary authority, to increase accountability by strengthening mechanisms of monitoring and punishment and to reward favourable performance in decisions on pay and promotion.

99. One of the greatest contributions the governance perspective offers development agencies working to enhance private investment levels has been to better understand the kinds of challenges different countries face managing their economies and reforming their investment climate. Setting priorities for reform requires a broad frame of reference that recognises the political and economic context in which reforms are formulated. Establishing basic political legitimacy and order is an essential first step for countries with collapsed states. This task inevitably must take precedence over other important, but less urgent, reforms such as public expenditure management, civil service reform, and decentralisation of public services (Mason, 2002, pp.17-18). Some countries may need basic institutions to ensure some degree of political stability, basic physical protection of citizens, and initiatives that increase the legitimacy and authoritativeness of government, laws, and public policies. Other countries have enough institutional coherence to think more about expanding public services to their poor majorities, diminishing the most development-averse forms of corruption and setting up systems for better management of public resources.

PART 2

HOW DEVELOPMENT AGENCIES CAN HELP INCREASE PRIVATE INVESTMENT FOR DEVELOPMENT

100. This Part describes the ways development agencies can support reforms that lead to increased private investment. It begins with Chapter 6 which presents a four-stage framework that development agencies can use when designing and implementing investment-enhancing ODA. Chapters 7, 8 and 9 examine the ways development agencies can assess the conditions for private investment, design programmes that lead to increases in private investment for pro-poor growth, and implement these programme. Chapter 10 describes the issues development agencies face when measuring the outcomes of reforms and evaluating programmes, looking at monitoring programmes, as well as measuring outcomes, results and long-term impacts. Chapter 11 provides a conclusion to this guidance.

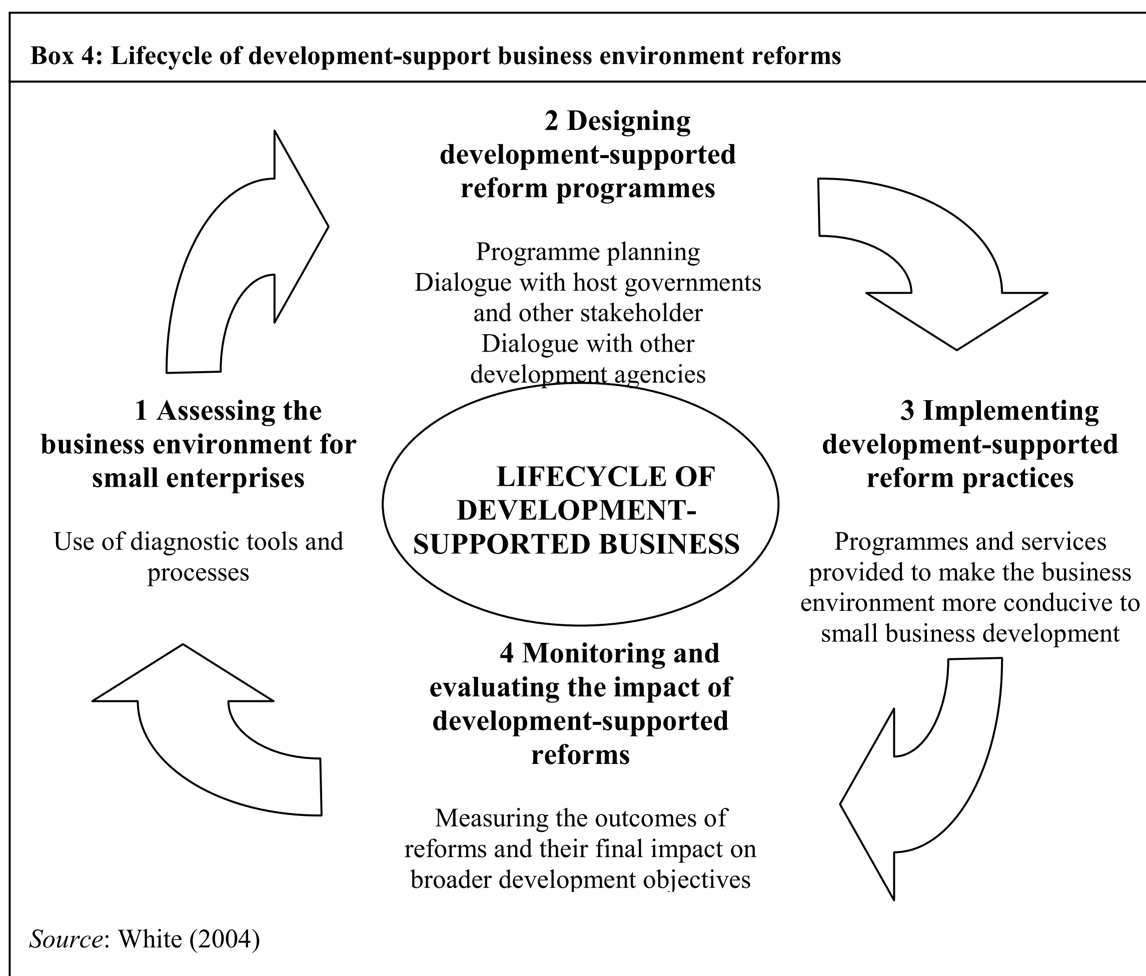
CHAPTER 6

FRAMEWORK FOR THE DESIGN AND IMPLEMENTATION OF INVESTMENT-ENHANCING ODA

101. Development agencies can benefit from a systematic approach to the design and implementation of investment-enhancing ODA. Such an approach connects anticipated outcomes and impact of ODA with interventions that address specific constraints or barriers to private investment. While instruments such as the logical framework (used by many development agencies) are relevant to the design and implementation of investment-enhancing ODA, development interventions that support investment climate reforms can benefit from a framework that connects all elements of ODA.

102. The Donor Committee for Enterprise Development has found that many agency interventions in business environment reform can be categorised into four programme cycle stages (see Box 4). These stages can be used to systematise development considerations in the design of short, medium and long-term interventions in line with the different challenges and priorities found in developing countries.

Box 4: Lifecycle of development-support business environment reforms



Source: White (2004)

103. It should be recognised that the links between each of these lifecycle stages are critical. How assessment of the investment climate informs the design of reform programmes, for example, should be given careful consideration by development agencies. Often a range of factors other than those found in the assessment of the investment climate influence the design of a reform programme (*e.g.*, political factors or development competencies).

Stage 1: Assessing the conditions for private investment

104. Development agencies use a variety of diagnostic tools and techniques to assess the conditions for private investment (*i.e.*, the extent that the investment climate enables or constrains private investment). These tools contribute to a better understanding of the obstacles to investment and private sector development.

Stage 2: Designing development-supported reform programmes

105. While development agencies can support reforms that enhance private investment in developing countries, it is clear that host governments and, to varying degrees, other stakeholders, should be the main drivers of the reform process. Thus, development agencies must look for ways they can add value to domestic reform processes rather than drive them (*e.g.*, by promoting international best practices without applying a one-size-fits-all approach to reform). However, there are also a number of other issues to consider when designing reform programmes, such as how to co-ordinate with other development agencies, how to ensure reforms are sustainable over the long term and how to keep programmes on track over what is often a long period of time.

Stage 3: Implementing development-supported reform practices

106. Supporting reforms that improve private investment in developing countries is a time consuming and complex matter. Development agencies are required to work at a more political and institutional level than they may have in the past; they work closely with host governments who are usually the leaders and managers of reform efforts, while also engaging other programme partners, including the private sector. Development co-ordination and collaboration is also important if reform efforts are to be consistent and effective.

Stage 4: Monitoring and evaluating the impact of development-supported reforms

107. Most development agencies struggle to find ways to better assess the impact of their work. However, in recent years, there has been a growing body of experience that has helped development agencies to measure the impact that their programmes have on changing private investment in developing countries.

108. Each of these four stages is addressed in further detail in the following chapters.

CHAPTER 7

ASSESSING INVESTMENT-ENHANCING ODA

109. Assessing conditions for private investment and measuring the influences these have on investment decisions can be a complex and difficult task (see Box 5) Development agencies tend to draw on existing assessment tools and expertise to help identify those fields where reform is most needed.

Box 5: Five main challenges to measuring the investment climate

1 The multidimensional nature of the concepts being measured (*e.g.*, stability, corruption, regulation and access to telecommunications services) and how they can interact in different ways.

2 Some dimensions are inherently difficult to measure, *e.g.*, competitive pressures and policy-related risks. Sensitive issues such as corruption may be underreported.

3 Differences in perspectives across firms and activities because they are affected in different ways by the investment climate *e.g.* they may be greatly affected by poor export infrastructure or relatively indifferent to it.

4 Differences within countries where, for example, local government policies, infrastructure provision and law enforcement may vary.

5 Gaps between policy and practice.

Source: World Bank (2004a)

110. There are two kinds of approaches to assessing the climate for private investment. The first is where development agencies develop standardised instruments for assessment. Development agencies have been found to use a variety of diagnostic tools and techniques to assess the investment climate (see Annex 3). While the focus of these tools may vary, most contribute to a better understanding of the obstacles or constraints to investment and private sector development. The second approach to assessing the climate for private investment is where development agencies rely on the expertise of their field staff and consultants to undertake assessments, rather than apply a standard instrument.

111. The decision to design and apply a standardised assessment tool appears to be guided by various interests. Firstly, a standardised assessment tool reduces the risk of subjectivity in assessments, particularly subjectivity of the personnel who are undertaking the assessment. Secondly, a standardised assessment tool produces results that can be compared across different countries. These are tools that apply common sampling frames, indicators and benchmarks to compare countries and even local conditions. Thirdly, standardised assessment tools can be used to promote comparisons over time so that improvements or declines can be measured. Fourthly, tools of this kind can help national stakeholders do their job better. Through the use of standardised assessment tools, stakeholders can develop the skills and techniques required to monitor and assess the investment climate themselves. Fifthly, standardised assessment tools encourage assessments to focus on specific aspects of the investment climate, rather than be distracted by broader or more general concerns. Finally, a standardised assessment tool can be a cost efficient means of assessment. Although an initial investment is required to produces the standardised tools and techniques for assessment, the later cost of undertaking assessments can be reduced because consultants and other assessors can follow the assessment protocol rather than create a new one every time (White, 2004).

112. Development agencies can also develop their own assessment tools. This is usually done to address the unique nature, interest or purpose of a particular assessment. Non-standardised assessments can be used to supplement the information from standardised assessments produced by other agencies. In some cases, specialised assessment tools are developed through collaboration between development agencies, developing country governments and/or the private sector in an effort to develop a common reform agenda.

113. Because of the wide range of factors affecting conditions for investment, it is often necessary to focus assessments on a selection of key indicators. Once a broad assessment has been carried out, it may be necessary to go deeper into specific sectors or localities. Rather than focus on the full range of issues affecting private investment conditions, development agencies can pay particular attention to the conditions found in specific sectors. Usually, the sectors selected are chosen because of their strategic position within the national economy (*e.g.*, textiles in South Asia, information technology in India or furniture manufacturing in Africa). In addition, development agencies may select other areas of focus such as foreign investors, the small enterprise sector, enterprises in the informal economy or agricultural or rural investment climates.

114. Investment-enhancing ODA is mostly found at the national level. However, there is growing awareness among development agencies that reform at sub-national levels, such as in specific provinces or localities, can yield valuable results. Indeed, there appears to be a growing trend among development agencies to adopt a two-pronged approach in their reform assistance strategies, combing national-level reform efforts with provincial or local efforts.

Questions to consider when assessing the conditions for private investment

- What assessments have already been conducted?
  - What information can be drawn from these?
  - Is it necessary to undertake further assessments? What are you trying to understand? Why is this important? Have any other agencies (including the actors within the country) identified this as a concern?
- What are government's investment climate reform priorities?
- What are the private sector's (domestic and foreign) investment climate reform priorities?
- If further assessments are required, can existing assessment tools be used, or is a new assessment tool required?
- Who will undertake this assessment (a foreign consultant, local consultants, local development staff, an assessment team containing a combination of these)?
- Who will view the information collected and conclusions reach through this assessment? Will it be released to the public for comment? Will government and the private sector be invited to comment?
- How will this assessment inform the design of future reform programmes?

115. There are a number of lessons that have been learned in the assessment of investment-enhancing ODA. These are described below.

Apply systematic, regular, common sense approaches to assessment

116. Assessing the conditions for private investment is not a once-off activity. It is important to identify trends over time and to determine whether these are leading toward an improvement or deterioration of the investment climate – including the levels of investment. Every country should conduct a systematic inventory of its rules and regulations to eliminate all those that cannot be justified (Palmade and Anayiolos, 2005). This implies a common sense approach to assessment: if it can't be justified, it should be removed. This is consistent with OECD principles of good practice.[11]

Use standardised assessment tools, but be prepared to modify them

117. It makes sense for development agencies to draw from the results of investment assessments that have already been done and, where necessary, to apply standardised assessment tools. However, development should consider the possibility of modifying these tools if required to meet specific needs and circumstances.

Dig deeper into strategic sectors

118. There is a point when general investment climate assessments are no longer enough. It then becomes important to assess the conditions for private investment in some of the key sectors of the economy (*i.e.*, those sectors that provide a significant contribution, or have the potential to contribute significantly). In addition, it is important for assessments to include the use of gender analysis tools to determine the extent to which the investment climate is influenced by social relations between men and women and the inequalities in power that underlie gender-differentiated outcomes in private investment.

Go beyond the national level and into sub-national assessments

119. Another way to dig deeper with investment climate assessments is to go beyond the national level and to examine sub-national areas. This kind of assessment can help to identify some of the factors that contribute to the regional disparities in investment levels that are often found. These assessments usually focus on sub-national government authorities such as provincial or local government authorities.

Build the analytical capacity of host governments

120. Development agencies are paying greater attention to the capacity of partner governments to undertake their own analysis and to monitor the progress of reforms. Regulators must be trained to conduct regulatory impact and other forms of assessments so that they clearly understand the methodological and data collection processes and the role regulatory impact assessment (RIA) plays in assuring regulatory quality.[12] Governments should be supported in their efforts to assess the investment climate. This implies the need for capacity building programmes for government as well as private sector organisations.[13]

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11 . OECD (1997)

12 See Rodrigo (2005).

13 See Tsikata (2001, pp. 15-16) on development experiences in Ghana and Tanzania.

Communicate and debate assessment results

121. Assessment results should be made public in an effort to engage key actors in discussions concerning the priorities and importance of reform. Through such discussions, development agencies can form mutual agreements with potential programme partners.

Identify the barriers and obstacles to reform

122. Development agencies should recognise that there will be resistance to reform programmes. Groups who have a vested interest in the status quo and will resist – either passively or actively – any efforts that threaten these interests. Businesses that have established and grown within a corrupt administrative regime may, for example, be very comfortable with this set up and resist reforms that remove corruption, thereby opening the market for new entrants.

Integrate regulatory impact assessments into the formulation and review cycle

123. Regulatory impact assessments are an approach to business environment assessments that have proven successful in developed and developing countries. RIAs are another way in which assessments can dig deeper into the issues that affect private investment. RIA examines and measures the likely benefits, costs and effects of new or changed regulations. It is a useful regulatory tool that provides decision-makers with valuable empirical data and a comprehensive framework in which they can assess their options and the consequences their decisions may have. RIA recognises the need to assess regulations on a case-by-case basis to determine whether they contribute to strategic policy goals. In any regulatory decision, the problem should be clearly defined and government action justified. RIA can be used to ensure policy makers, legislators and regulators are well informed (Rodrigo, 2005).

CHAPTER 8

DESIGNING INVESTMENT-ENHANCING ODA

124. Development agencies should – in collaboration with developing country governments and the private sector – prioritise their development goals based on the country-specific conditions in which the capacity for reforms are assessed. Rather than attempting to implement the full spectrum of the good governance agenda, for example, development agencies should focus on those that are most pressing and will help countries to move the next level of reform requirements (Grindle, 2002).

125. The design of investment-enhancing ODA will focus on different priority areas according to the country context. In fragile states, for example, it is likely that development support would best be focussed on supporting state-building and strengthening, establishing the rule of law, establishing and maintaining political stability and enhancing economic stability and predictability. In less developed countries where the state is operating relatively well, development agencies are more likely to support the development of open and competitive markets, as well as the management of public debt. In comparison, in developing countries that are showing healthy signs of economic growth, investment-enhancing ODA would best focus on supporting the reform of the policy, legal and regulatory framework for the private sector and improvements in tax regimes.

126. Objective assessments of the investment climate do not necessarily determine the nature of the programmes development agencies design. Development agencies are influenced by a number of different factors when designing their reform interventions. Setting priorities for investment-enhancing reforms and the design of reform programmes are also affected by other factors such as political interest and the competencies of development agencies. The OECD (2003a, p. 9) describes how cutting red tape is firmly on the political agenda of most OECD countries, but is rarely based on an understanding of the real costs of regulatory burdens.

127. The successful design of investment-enhancing ODA is not determined by the amount of funds that are spent. Key to a more strategic involvement by development agencies in this field is the design of interventions that match demand and are suited to the specific country context. For example, a major component of much of investment-enhancing ODA is technical assistance. The World Bank (2004a, p.192) found that many technical assistance projects in this area are relatively small in size, averaging USD 1.1 million each between 1998 and 2002. Despite the small amount of resources this kind of intervention consumes, the relative impact can be significant.

128. Annex 4 describes the main mechanisms development agencies have used to provide investment-enhancing ODA. One of the mechanisms not referred to in the annex involves the setting of conditions for development assistance. Development agencies often set conditions for their assistance in order to reduce programme risks and to maximise the impact and sustainability of the programme. Policy conditions – often bundled with financial and technical support – have sometimes helped reform-minded governments advance their reform agendas. However, where conditions have been externally imposed on programme partners, effectiveness and sustainability is often reduced. It is important for development agencies to build collaborative arrangements with programme partners and where either partner requires conditions, these should be mutually agreed upon. External partners should have a shared view of the partner country and co-ordinate their development co-operation and other actions and policies. Assistance should support the

development of sustainable national or local institutions – both public and private – addressing the barriers to adequate performance.

129. Similarly, programme milestones or benchmarks should be designed in collaboration with programme partners. Indeed, conditions and milestones should be designed hand-in-hand. Conditions work best when they are focussed on outcomes rather than initial (programme planning) promises.

Questions to consider when designing investment climate reform programmes
• Are there government reform programmes or intentions (*e.g.*, statements) that your agency can support or add value to? • Is there a clear domestic demand for the reform programme you are designing? • How can you ensure your programme gains high-level political support by the government and the private sector? • Where do you expect resistance for this reform programme to be found? Who will the reform hurt? • How can you ensure there is local ownership for this reform and for its sustainability over time? • What outputs will the programme produce and how will these create the desired outcomes and development impact? (Referring to the logical framework for investment climate reforms.) • Are the timeframes you are setting for creating desired outcomes and development impact realistic (investment-enhancing ODA is often best structured over a longer timeframe that many other ODA programmes *i.e.*, well beyond the typical three-year programme cycle)?

130. There are a number of lessons that have been learnt in the design of investment-enhancing ODA. These are described below.

Focus on policy and institutional reform

131. Development agencies should focus on the policy and institutional determinants of investment and growth when designing their interventions (Burnside and Dollar 2004). Attention should be given to the "institutional fit" of reform programmes, ensuring programmes are "well adapted to local conditions. Indeed, advisers from development countries very often propose solutions that bear a striking resemblance to those adopted in their home country – regardless of where they are recommending them. It may be understandable that advisers will be influenced by the approaches they are most familiar with, but the uncritical transplant of models from other countries can lead to poor or perverse results" (World Bank, 2004a, p.192).

Sequence reform interventions

132. Development agencies are advised to pay attention to the sequencing of their interventions in support of greater levels of private investment. Often development agencies prefer to balance programme risks and returns with interventions that address immediate priorities and work toward a long-term vision associated with pro-poor growth and levels of private investment. Thus, sequencing interventions, by building on success and trust between the development and programme partners, is important. This requires regular monitoring and revision of programme strategies. Moving from analysis to reform, finding appropriate starting points for reform, and establishing a mutually agreed upon sequence of reform

interventions is a major challenge for investment-oriented ODA. Reform is a multi-layered interdisciplinary process that spans a substantial period of time. Beginning with achievable changes and building on success is critical. This view is supported by the findings of the World Bank Operations Evaluation Department's evaluation of investment climate reforms in which it was found that reform programmes that were "meaningful, co-ordinated, and sustained were more likely to be successful" (World Bank Group 2004, para. 2.17).

Co-ordinate investment-enhancing ODA interventions

133. Sound co-ordination increases credibility with the host country and improves efficiency and effectiveness of development efforts. From a reform point of view, co-ordination contributes to consistency. There are a number of ways to improve development co-ordination, which recognise that development agencies often find it easier to agree on policies and priorities, but harder to agree on implementation. However, once a track record of success has been achieved, development agencies seem to become more willing to modify their own procedures in the name of successful co-ordination and collaboration.[14] A sector-wide approach to development coordination should also be considered.[15]

Package programmes across more than one level

134. Development agencies should look for ways to combine various kinds of interventions. While this might increase the complexity of programmes, there are often complementary characteristics of this approach that can create important benefits.[16] For example, firm-level interventions (at the micro-level) while often more costly than other interventions, can be the right choice in high-risk situations. Demonstrating success at this level can build trust and prove competence, which might then help the development agency to work at higher levels. Work at this level can also help to identify the externalities that confront the private sector, which can then be the focus of the next stage of development support.

Connect reform programmes to broader development strategies

135. Where possible, reform programmes should be closely connected to broader national development strategies such as private sector development, competitiveness or poverty reduction strategies (*e.g.*, Poverty Reduction Strategy Papers), including annual short or medium-term budget plans. This can help programme partners to see the relevance of investment climate reform and the contribution this makes to broader social and economic roles.

Combine national and local level reforms

136. Development agencies have indicated that developing programmes that deal with national reforms while also targeting specific local areas for reform can provide a useful means of observing how national reforms are experienced at the local level.

Recognise the importance of branding and good public communications

137. Because successful reforms involve political and social processes, it is important to pay attention to the way reform messages are communicated. Some development agencies have found it extremely useful to develop a public brand for reform campaigns. This helps key actors as well as the general public to understand the purpose of the reform and how it will improve their lives. Such campaigns should make

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14 See Disch (1999).

15 See Mbugua, Ronge et al. (2004) for experiences from Kenya.

16 See Snodgrass and Winkler (2004). For more guidance on development harmonisation and co-ordination see OECD (2003b).

use of terms that convey action, urgency and the importance of reform.[17] Social marketing and public awareness reform campaigns can also encourage the business community as well as government regulators to understand the importance of reform and the processes that are underway.

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[17] Herzberg and Wright (2005, p. 26) stress the value of certain key words: "business" implies private sector advocacy; "voice" implies private sector frustration; while "bulldozer" conveys private sector impatience. They cite the Bosnia "Bulldozer Initiative – 50 economic reforms in 150 days" and the Nigerian "Better Business Partnership" as examples.

CHAPTER 9

IMPLEMENTING DEVELOPMENT-SUPPORTED REFORM PRACTICES

138. While the implementation of all forms of development programmes can benefit from general guidelines and best practices, the implementation of investment-enhancing ODA differs in some important ways. Much of this is due to the institutional and policy making dynamics that influence the success of ODA.

139. Successful investment-enhancing ODA is more than simply about *where* to provide support (*i.e.*, which development fields are the most appropriate); it is also about *how* ODA instruments and mechanisms are used to promote sustainable investment-enhancing reforms. The following lessons have been learnt in the practice of investment-enhancing ODA. These lessons provide a set of practices that improve the implementation of investment-enhancing ODA.

A higher level of development engagement

140. Investment-enhancing ODA often requires development agencies to work at a higher-level than they may have previously (*i.e.*, the macro-level instead of the meso-level, or the meso-level instead of the micro-level). This requires development agencies to develop a new set of skills and competencies. Rather than focus on specific interests (*e.g.*, financial services, investment promotion or entrepreneurship), development agencies are required to balance these interests against a competing range of other interests that need to be incorporated within macro and meso-level reforms. Thus, development agencies need to ensure they have the skills and capacity to work at these levels and can keep their eye on the big picture while focussing on the details of reform.

Co-ordinating reform efforts

141. Development agencies should work together to ensure their calls for reform are harmonised and that their different programmes complement each other. The *Paris Declaration on Aid Effectiveness* places a high degree of importance on the need for development agencies to harmonise their programmes and coordinate with one another. "Effective aid calls for improved aid co-ordination by working collaboratively, undertaking joint tasks, and combining skills and resources. While maintaining high standards of accountability and transparency, DAC Members can simplify and harmonise administrative and financial requirements, adjust to local procedures where these are adequate and help partners improve their administrative capacity and performance. We will undertake best efforts to work collaboratively, streamline our administrative requirements where possible, and co-ordinate our approaches and actions with those of our partners".

Dealing with the political process of reform

142. Implementing successful investment-enhancing ODA requires a sensitivity to and understanding of political processes. Reform creates winners and losers. In some cases, successful reform will mean that those who have often lost will win, or that those who lose have loud voices. Thus, reform will involve conflict and sometimes this conflict will be public and controversial. Those who are potential losers in the reform process will resist change wherever possible. Development agencies need to be prepared for this

and to develop strategies to counter such resistance. Similarly, supporting the demand for reform and building political commitment is essential.

Building effective relationships with programme partners

143. Development agencies should invest in building strong and trustworthy relationships with their programme partners. While this might sound like common sense, there are a number of barriers to effective relationship that often arise (see Box 6).

Box 6: Barriers to effective relationships between development agencies and government

- Inadequate vision, leadership, co-ordination and ownership on reform issues by government.
- Lack of transparent and open communication by government toward development agencies.
- Lack of national counterparts, including government champions required for reform processes.
- High turnover of development staff (usually in three-year cycles).
- Changes in development priorities (development agencies should design projects that run for 5-10 years).
- Piece meal funding of reform interventions.
- Reliance on programmes designed and decisions taken at headquarters, thus, a limited capacity among multilateral development field offices to decide on resources and interventions without headquarter approval.
- Difference in cultures, values and reform objectives between development agencies and domestic stakeholders.
- Tied aid arrangements, whereby development support requires the sourcing of advice, equipment, etc. from specified sources (this is particularly an issue for bilateral development agencies).
- Time taken to approve projects and disburse funds.
- Limited trust between government, business associations and development agencies.

Source: Olomi & Nchimbi (2002)

Addressing the human factor in reform processes

144. While it is easy to focus on the technical issues of reform, it is important for development agencies to pay attention to the importance of changing the attitudes of government officials toward private investment and the relevance of reform. Attitudinal change is an important pre-condition for reform. Some development agencies describe this work as the "hearts and minds agenda" – changing the hearts and minds of government officials so that they are more aware of the impact their procedures have on the private sector and are more open to looking for ways to improve this situation. Interventions to bring this about include training programmes and study tours for government ministers, members of parliament and senior officials. The use of regulatory impact assessments is also a way of making government officials more aware of the influence they can have on private investment.

Programmes preferred over projects

145. Many development agencies have come to focus on reform programmes in preference to individual projects. The term "project" describes a discrete activity with specific outputs that stands alone from other activities, while a "programme" refers a collection of interventions (*i.e.*, a collection of projects or components) that are assembled to maximise the impact of development intervention at a number of levels. This approach bundles reform interventions and spreads reform efforts across different levels and development fields. Thus, investment-enhancing ODA requires effective management and co-ordination skills within development agencies and among programme partners.

The demand for longer timeframes

146. Investment-enhancing ODA often requires a longer programme timeframe compared with other ODA fields. While many development agencies typically operate on a two-to-three-year project life for most of their work in other sectors (*e.g.*, education, health), investment-enhancing ODA cannot achieve results in such a short period of time. Thus, development agencies need to find innovative ways to increase the timeframes for their interventions. This may include establishing short-term milestones within a longer-term programme.

Monitoring the progress of reform

147. A programme monitoring system should be set up in the early stages of implementing an investment-enhancing programme to ensure there is timely feedback on outcomes and impact from the start. In addition to helping with fine tuning aspects of the programme design and implementation, the data gathered from programme monitoring will contribute to the *ex post* evaluation of the programme.

Build on the demand for reform

148. After years of frustration and programme failures, development agencies have learnt that they cannot force developing countries to reform.[18] The motivation for reform must come from within. In most cases, it is governments that must come to see the need for change and to take measures themselves to improve their capacity to mobilise investment and stimulate economic growth. However, private sector organisations, civil society and even the local media also have a role to play in making demands on government for change. The World Bank (2004a, p.192) cautions development agencies against being too eager to support investment reforms, indicating that they can easily fall prey to supply-driven approaches: "the bookshelves of many ministries in developing countries are lined with reports presenting detailed proposals for the design and implementation of reforms never implemented". Development agencies should ensure there is a demand for reform they can support and build upon. In the absence of such demands, development agencies are faced with a choice. They can keep their distance and not take any reform initiative unless such a demand is manifest, or they can undertake efforts that stimulate the demand. Some development agencies undertake studies into the political economy of countries to determine the "drivers of change" as well as those areas where resistance to change can be found. These mostly confidential reports have been used to inform the design of programmes that build a demand for reform. However, it should be noted that developing country governments could interpret this as interference in domestic politics.

Ensure political commitment

149. Sustainable reforms only work when they are driven, owned and managed by domestic agents. The principal agent in most cases is government. Governments should exhibit a commitment to reform from the highest level. Development agencies and developing country governments should form mutually agreed reform agendas.

Build strong domestic institutions

150. Institutions have an important role to play in the sustainability of reforms that lead to greater levels of private investment. As a result, many development agencies are paying more attention to how

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[18] Collier and Dollar (1999) have found that the promise of development finance is not enough incentive for host governments to undertake reforms. They need to see the longer-term value in undertaking these initiatives. Thus, development agencies are more aware of the need to stimulate debate around reform issues in an effort to build a stronger and broader demand for reform.

they can build stronger domestic institutions. However, it is also acknowledged that this is not an easy task.[19]

Regularly bring key actors together

151. Development agencies should facilitate the building of "competitiveness partnerships" between the public and private sectors. They can facilitate and bring credibility to processes that structure dialogue between the public and private sectors.[20] However, success in this field depends on the public and private sector perceptions of the development agency, which varies according to country context and individual development agencies. Furthermore, local ownership of these processes is important. Development agencies should ensure that while they may help to facilitate these processes initially, ownership should be handed over to the participating parties as quickly as possible. This includes the setting of agendas for dialogue and the language in which dialogue occurs.

Focus on the local private sector

152. There is a danger that strategies for greater investment and growth will be entirely based on a search for outside solutions. Similar to the "smoke stack chasing" of the 1970s and 1980s, national governments will try to entice outside investors with the lure of attractive government subsidies. Recent development experiences in improving investment climates have shown that the competitiveness of the domestic private sector is an important ingredient promoting economic growth and attracting FDI.[21] Thus, creating a positive business environment for business operations in country should take priority over special incentives for foreign investors.

Include sub-national levels of reform

153. While many development efforts are directed to helping national government agencies manage reform processes, attention is also paid to the role of sub-national levels of government, in particular local government. While on the one hand this involves support for reforms that enhance the decentralisation of government services, it can also address the roles of local and provincial governments in improving sub-national investment climates. With the breaking down of national trade barriers, local and provincial economies are becoming more directly engaged in world markets. Indeed, it is at the local level that many private investors may have direct contact with government agencies. Thus, development support for investment-oriented reforms should include support for reforms at the local level.

Recognise the importance of perceptions

154. Reform is a political process, which is influenced by the choices people make. A number of studies have highlighted the negative perceptions investors have of developing countries and the impact this has on poor investment levels (Vickers, 2003). Some development agencies have specifically developed interventions to address this. However, reviews of past reform experiences have shown that helping local actors deal with change, building on success and helping local actors keep their eye on the big picture of reform is important.

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[19] A recent evaluation report on the World Bank Group's support for investment climate reforms found that not enough is known about good practice in institutional design, or about the dynamics of changing institutions (World Bank Group 2004, Para 2.8).

[20] See Herzberg and Wright (2005, pp. 23-25)

[21] This was an important finding of the DFID Investment Competition and Business Development Services Team and Bannock Consulting Ltd (2004).

CHAPTER 10

MEASURING THE OUTCOMES OF REFORMS AND EVALUATING PROGRESS

155. While there are many problems experienced by development agencies when measuring the impact of reforms on private investment, most agencies recognise this deserves careful attention. Measuring development impact requires the design of indicators and frameworks tailored specifically for each programme and country. There are specific issues within investment climate reform programmes that development agencies need to address in all their programmes.

156. This chapter presents advice on how to measure the results of investment-enhancing ODA in three important categories: how development agencies can monitor investment-enhancing ODA; how development agencies can measure the outcomes of investment-enhancing ODA projects; and how development agencies can identify the results and impacts of investment-enhancing ODA.

Monitoring investment-enhancing ODA

157. Most development agencies apply some type of monitoring procedure to their reform programmes. For example, most development agencies record programme inputs, activities and outputs. Many development agencies find they are required to apply different monitoring methods to their investment-enhancing programmes. Because investment-enhancing ODA uses new kinds of tools and processes – or applies well-known tools and processes in a different way or with different actors – there are specific challenges that need to be addressed.

158. One of the main challenges when monitoring investment-enhancing ODA is to ensure a long-term perspective on reform is maintained. It is easy for development agencies to focus on the specifics of programme activities and to monitor inputs, activities and outputs, but this should be done with a careful watch on the broader dynamics occurring in the investment climate. Because reform can take a long time, it is essential that reform programmes adjust where necessary to changing circumstances.

159. There is a range of tools and techniques that can be used to monitor investment-enhancing ODA (see Box 7). The choice of these will vary according to the programme.

Box 7: Techniques for programme monitoring

Focus groups: may be arranged on a regular basis with business association members and can include meetings with the general business community (*e.g.*, public meetings).
Impact panels: can be set up at the start of the programme; they should have the same membership throughout the period of the programme and meet regularly (six months is the norm). The membership should be representative of the sector or business type towards which the reform is targeted.
Point of delivery surveys and scorecards: can be simple tick-box cards placed at the exit of the point of delivery, *e.g.*, a one-stop shop for business registration, or a short form to be completed (usually anonymously) following an inspection.
Phone surveys: a quota of businesses can be phoned each week or month on a random basis to see how they have been affected by the programme or regulatory change, *e.g.*, a change in method of VAT collection, or inspection process.
Source: Pinder, *et al.* (2005)

160. When introducing a monitoring system for investment-oriented ODA, development agencies should:

- Ensure a monitoring system is designed as the programme is designed and implemented as soon as the programme begins.
- Ensure the logical framework of the programme is clear and the steps in this framework are measurable.
- Engage all relevant stakeholders (*e.g.*, government and the private sector, including domestic and foreign investors) in the process of monitoring progress and ensure the right kinds of tools are used for each stakeholder.
- Compare programme progress with changes in the investment climate (*i.e.*, monitor programme activities in light of broader events).

Measuring reform outcomes and change

161. Outcomes are an important link in the causal chain of events that lead from programme interventions (*i.e.*, development inputs and activities) to the achievement of specific reforms that contribute to increased private investment. Measuring these outcomes helps development agencies to see how their support has produced results that contribute to long-term improvements. The causal links between investment-oriented ODA outcomes and increasing levels of investment and growth need to be identified. This is usually done at the programme design stage. Following this, there is a need to better measure the nature and quality of these outcomes and the ways ODA can influence these outcomes.

162. The challenge for development agencies is to find ways where the outcomes of reforms lead to change in the investment climate. For example, the introduction of a development-supported deregulation unit may produce desired outcomes such as the reduction in the number of regulations that constrain private investment, but has this increased the amount of investment made by domestic and foreign investors?

163. There are different ways to measure the outcomes of investment-enhancing ODA. Some development agencies record outputs based specifically on development interventions (*e.g.*, drafting and adoption of a policy or law, removal of unnecessary regulations). This is useful, but it may not be enough to show that these outcomes have led to change in the investment climate.

164. Other development agencies undertake regular stakeholder perception surveys before, during and after development intervention. This can be useful because it produces a broader perspective on the conditions for investment and the contribution the programme has made to changes in these conditions. While anecdotal information is often considered a poor substitute for "hard" monitoring and evaluation data, good anecdotal information on the contribution of development efforts to reform and the benefits these reforms have wrought upon the target group can be very useful. In some cases, this kind of information meets the demands of taxpayers and other constituents very well.

165. When measuring reform outcomes and changes to the conditions for private investment, development agencies should:

- Look beyond the production of programme outputs to see how these may contribute to change (*e.g.*, a new law does not create change until it is enforced).

- Consider how programme outcomes address identified constraints to private investment (*e.g.*, constraints that may have been found when assessing the investment climate).

- Consider the contribution programme outcomes create at the macro, meso and micro levels.

Measuring results and impacts achieved

166. A concern to development agencies is the way they articulate and measure the relationship between supporting reforms that improve private investment in developing countries and the attainment of broader development objectives, such as the Millennium Development Goals. Development agencies are also often required to justify their expenditure. While the resources required for effective investment-enhancing ODA are not necessarily as great as other development fields (*e.g.*, famine relief, health and education services), many agencies are under greater scrutiny by their ministers and taxpayers to demonstrate that expenditure in this field yields results. Why, some may ask, should funds from urgent disaster relief or disease prevention programmes be reallocated to investment enhancing reform interventions? What is the real impact of these programmes on the poor in developing countries? Moreover, because investment-enhancing ODA brings development agencies into a number of unconventional domains (*e.g.*, direct engagement with the private sector), agency directors and programme administrators may need to be convinced of the value of such new fields of intervention.

167. Measuring the impact of reform programmes on the investment climate is difficult for two main reasons. The first is that it is extremely difficult to isolate the impact of specific reforms from other changes and programmes that occur. This is especially so when development agencies embed their reform initiatives within programmes that contain other elements (*e.g.*, a private sector development programme may contain a reform component along with other components dealing with promotion of the private sector). Thus, attributing change in investment or growth to a single reform intervention creates difficulties when measuring impact. Would this change not have occurred without the intervention? Or did the intervention improve or lessen the amount of change?

168. The second problem in measuring the impact of development-support reforms is the time over which reforms occur. Investment-oriented ODA reforms take a long time. While individual interventions can create short-term outcomes, the impact of these outcomes takes a longer period of time to eventuate, making it more difficult to measure.

169. The challenge for development agencies trying to measure the impact of their interventions is to find appropriate indicators to measure and draw causal links with their specific programmes. In many cases, development agencies and evaluators look for expedient means of dealing with this challenge. Many development agencies find is easier, and in some cases more relevant (in terms of their own accountability requirements), to measure the performance of ODA programmes (*i.e.*, programme outputs and outcomes), rather than the final impact these may lead to in terms of increases in investment and economic growth. The World Bank has found that the outcomes of its investment climate reform programmes "are positively correlated with indicators of macroeconomic and financial sector performance – although there is no evidence to indicate causality from operations to economic performance" (World Bank Group, 2004, para.2.14).[22]

170. A critical challenge for development agencies is to consider the link between increasing levels of domestic and foreign private investment and pro-poor growth. Greater levels of investment do not automatically lead to pro-poor growth. Thus, measuring the impact of investment-enhancing ODA will

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[22] In contrast, the World Bank (2004b, p. 3) suggests that a "hypothetical improvement to the top quartile of countries on the ease of doing business is associated with up to two percentage points more annual economic growth".

involve a measurement of investment levels as well as the extent to which progress is being made toward agreed upon poverty reduction targets such as the MDGs.

171. Effective impact assessment of investment-enhancing ODA should allow for the assessment of strategic development interventions in terms of their outcomes and final impacts of the intervention. This involves measuring the effect of development-supported reforms on private investment (*i.e.*, outcomes) as well as on the overall impact of reform efforts. There are four stages involved in doing this.

Stage 1: Initial screening

- Screening the conditions for private investment and the country context. This is a scan across the range of policies, regulations and institutions affecting private investment to identify constraints to domestic and foreign investment and identify areas of focus for reform.

Stage 2: Ex ante *appraisal*

- Review key conditions for investment and assess the ways the proposed programme will affect the conditions for investment and the achievement of broader ODA objectives (*e.g.*, pro-poor growth).

Stage 3: On-going monitoring and evaluation

- This should be built into programme design and implementation to ensure there is timely feedback on outcomes and impact from the start.

Stage 4: Ex post *evaluation*

- Conducted to assess the actual impacts of the intervention against the baseline scenarios developed at *ex ante* stage.

172. The process of measuring the impact of investment-enhancing ODA should involve a partnership between the development agency, the government and the private sector. Together, these parties can explore the constraints on private investment and its impact on pro-poor growth. ODA can be seen as adding value to reform processes that have been mutually agreed on. The performance of ODA programmes can be measured in this light. This kind of approach encourages increased transparency and accountability among all parties.

173. Development agencies have come to see the value in building good relations between development agencies and government, especially through the use of a well established and strategically focussed institutional frameworks for managing aid. Strong institutional mechanisms for accountability build mutual trust between development agencies and host governments. Such mechanisms allow both parties to monitor progress in reform efforts. This also discourages development agencies from micro-managing projects by introducing parallel management units with expatriate staff.[23]

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[23] See Tsikata (2001, pp. 15-16).

CHAPTER 11

CONCLUSIONS

174. Investment-enhancing ODA holds a great deal of promise to development agencies and developing country governments wishing to increase the impact of their efforts on achieving social and economic development goals. However, while private investment is a critical source of finance required to boost economic growth and contribute to poverty reduction, its mobilisation often requires new methods and approaches by public agencies.

175. Developing country governments may need to recognise and become more response to the dynamics of private investors. This may entail liaising more closely and regularly with domestic and foreign investors and redefining their roles as regulators, promoters and developers of the private sector. Similarly, development agencies may need to apply a more systemic approach to their work in this field and broaden their range of programme partners.

176. The guidance provided in this document has highlighted the challenges faced by development agencies and identified the principles and practices that agencies have applied to meet these. Development agencies can add value to domestic reform processes. They can share international experiences and information on what reforms developing countries can make and offer advice and support on how to make these. They can build the capacity and competencies of key public and private agencies and they can help their programme partners to see how reforms can lead to improvements in private investment, economic growth and the sustained reduction of poverty.

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ANNEX 1

DEVELOPMENT FIELDS THAT ENHANCE THE VOLUME OF PRIVATE INVESTMENT

Different organisations have identified a range of development fields that contribute to the mobilisation of private investment. Some of these are briefly outlined below.

The Development Assistance Committee has stressed the role development agencies can play in creating a favourable legal environment for private sector development by reducing administrative and regulatory barriers to investment, strengthening the financial sector and fostering the privatisation of state-owned enterprises under competitive conditions (OECD, 2001b, p.75).

The World Bank's *World Development Report 2005* (p.189), suggests there are three main ways development agencies can improve the investment climate in developing countries: *i)* by removing policy distortions in developed countries that harm the investment climates in developing countries; *ii)* by providing more, and more effective, assistance to the design and implementation of investment climate improvements, and better leveraging support provided directly to firms and transactions; and *iii)* by tackling the substantial knowledge agenda to help policymakers broaden and accelerate investment climate improvements.

The World Bank's Operations Evaluation Department (2004, p.7) has categorised areas of investment climate reform into "core" and "non-core" themes.[24] Core investment climate themes include regulation and competition policy, corporate governance, legal institutions for a market economy, judicial and other dispute resolution mechanisms and personal and property rights. Non-core themes include tax policy and administration, infrastructure services for private sector development, export development and competitiveness, trade facilitation and market access and other financial and private sector development.

Sweden's Global Development Policy (2004, p.32) says that if "a climate that is conducive to investment and growth is to be established in developing countries, many of them will need to build stronger public institutions, in particular an effective judicial system. By providing support for capacity-building (institution development and management expertise) development cooperation can increase the developing countries' prospects for benefiting from economic globalization".

The UN Millennium Project (2005, pp.45-46) says that the key variables of interest to private investors include: adequate infrastructure (roads, ports, electricity, water); physical safety, including peace and security; reliable sites for operations, such as industrial zones close to seaports and airports; the rule of law for predictable contracts and relations between business and government; a healthy and skilled labour force; safe and accommodating location for expatriate managers and their families; and favourable tax treatment. It recommends (pp.121-124) that each government collaborate with the local private sector to design a private sector development strategy that helps create a favourable business environment. This would include measures in seven key areas: *i)* a supportive macroeconomic framework; *ii)* a favourable legal and regulatory environment; *iii)* adequate infrastructure, human capital and research and development; *iv)* actively promote business activities in science, technology, and innovation; *v)* specific actions to promote foreign direct investment; *vi)* functioning, competitive markets for both inputs and

24. It has been proposed that the categories "core" and "non-core" be replaced with "narrow" and "broad", to avoid the implication that one category of activities is more important than the other.

products; and vii) enable easier access to financial capital by simplifying rules for collateral, increasing flexibility for informal entrepreneurs, and providing credit at subsidised rates.

The OECD (2003a, p.14) report entitled *From red tape to smart tape* suggests that there is a risk that administrative regulations can impede or create unnecessary barriers to investment and even threaten the legitimacy of regulation itself. "The cumulative effect of many administrative regulations and formalities from multiple institutions and layers of government is to slow down business responsiveness, divert resources away from productive investments, reduce transparency and accountability, hamper entry to markets, reduce innovation and job creation, and discourage entrepreneurship."

ANNEX 2

DEVELOPMENT FIELDS THAT ENHANCE THE CONTRIBUTION PRIVATE INVESTMENT MAKES TO SUSTAINED POVERTY REDUCTION

There are a number of development fields that affect the contribution private investment makes to sustained poverty reduction. For many development agencies, this means finding a link between better conditions for investment and the achievement of the Millennium Development Goals.

Sida (2003, pp.20-21) has identified four clear linkages between private sector development and the MDGs. First, the attainment of the goal of halving income poverty by 2015 requires robust economic growth and a dramatic change from the current growth pattern in many countries and regions of the world. Second, achieving the Millennium Development Goals depends on major investments in the social sectors such as primary education, child and maternal health, HIV/AIDS and safe water. Third, public sector investments into social and infrastructure programmes can be enhanced by private investments. Fourth, the last Millennium Development Goal includes several dimensions of private sector development such as global trade and finance systems, work standards and transfer of technologies in certain key sectors.

According to the **United Kingdom Department for International Development** (2001) there are three fundamental requirements for halving world poverty by 2015: economic growth, equity and security. While private sector activity is the primary driver of economic growth, this implies the need for well functioning markets and a strong foundation of effective governance and institutions. Public policy needs to work to ensure that public expenditure and taxation have a significant impact on poverty reduction and the poor are able to participate in market-led growth. Thus, while private investors provide the resources for economic development, sustained poverty reduction requires proper government policies, good governance and effective institutions.

"If growth is to lead to poverty reduction," says **Sweden's Global Development Policy**, "an effective income distribution policy and institutional structures that focus on the needs of the poor are essential" (Government of Sweden 2004, p.32). Klassen (2003) found that pro-poor growth requires a combination of reforms that include good macroeconomic policies; good governance; human resource development; a focus on the economic activities in which the poor are directly engaged (*e.g.*, agriculture, rural and non-farm employment); and equity in distribution of income and assets, such as land, and gender equality.

Improving the conditions for private investment and facilitating the contribution of these investments towards sustained poverty reduction requires that public institutions, often in collaboration with private sector actors and private sector representative organisations, undertake reforms that reduce the costs of doing business (*i.e.*, the transaction costs of private investment) and enhance the capacity of private actors to act entrepreneurially (*i.e.*, taking a calculated risk when mobilising resources in pursuit of market opportunities). The **UN Millennium Project** suggests that the goal is to "combine the critical public investments in infrastructure and human capital with market-oriented economic policies to ensure the dynamism of private sector growth" (United Nations Millennium Project 2005, p.8).

ANNEX 3

INVESTMENT CLIMATE ASSESSMENT TOOLS

Development agencies use a variety of diagnostic tools and techniques to assess the investment climate. Several of these tools are outlined in this annex.

Business Environment and Enterprise Performance Survey (BBEPS) Eastern Europe and Central Asia: The Business Environment and Enterprise Performance Survey's Interactive Dataset provides downloadable results from surveys of over 4 000 firms in 22 transition countries in Eastern and Central Asia conducted in 1999-2000. It examines a wide range of interactions between firms and the state, including such areas as corruption, state capture, lobbying and the quality of the business environment.

Foreign Investment Assessments – Administrative Barriers: The Foreign Investment Advisory Service (FIAS) of the World Bank Group has undertaken assessments on administrative barriers in some 120 countries. In addition to a survey of firms and stakeholder consultations, FIAS takes a 'self-assessment' approach to reviewing administrative barriers to investment in client countries. Under this approach, a counterpart team in the Government will use FIAS templates to collect the basic "institutional" information on administrative procedures for business establishment and operation in the country, following the existing norms and regulations. Assessment also relies on the expert opinions of the consultants.

Global Entrepreneurship Monitor: Developed by the Ewing Marion Kauffman Foundation in 1998. 2003 saw the fifth annual GEM assessment of entrepreneurship. The programme has expanded from ten countries in 1999 to over 30 in 2002 and 2003—a total of 41 countries have been involved for one or more years. National teams have been in operation in 39 of these countries; their host institutions, membership, and sponsors are listed below. The annual GEM assessment involves four major types of data collection:

1. Surveys of the adult population are completed in each country. This involves locating a representative sample of the adult population to determine which are active in entrepreneurship, either by starting a new firm or as the owners of an existing firm pursuing an entrepreneurial strategy.

2. Firm surveys.

3. Interviews with national experts, including the completion of a 10-page questionnaire by experts to provide a standard measure.

4. Existing data on national features assembled by a variety of international research organisations (*e.g.*, World Bank, International Monetary Fund, UN, International Labour Organization).

Investment Policy Reviews: UNCTAD has undertaken IPRs in 14 countries. These reviews help countries improve policies and institutions that deal with FDI and increase their capacity to attract and benefit from it. The IPR team comprises UNCTAD staff and international and local experts. The IPR team conducts the review over a period of six months. It culminates in the presentation of the findings and recommendations to the UNCTAD intergovernmental Commission on Investment, Technology and Related Financial Issues and in other appropriate forums, as well as in follow-up technical assistance.

Investment Compass: This is a new web-based benchmarking tool developed by UNCTAD, which reveals the competitiveness of each country's taxations system for FDI. Investment promotion agencies complete two questionnaires, one on the investment regulatory framework the other on taxation. Once the questionnaires have been validated by national authorities, UNCTAD completes the data collection and compiles an Investment Compass. Investment Compass is an interactive tool for analysing the main economic and policy determinants that affect the investment environment. The Investment Compass permits comparisons between countries, between a country and a region and between a country and a best performer. The tool comprises 60 indicators based on international statistics and on special national surveys conducted by UNCTAD. The Investment Compass is organised around six major areas*: i)* resource assets; *ii)* infrastructure; *iii)* operating costs; *iv)* economic performance and governance; *v)* taxation and incentives; and *vi)* the regulatory framework.

Regional Program on Enterprise Development Sub-Saharan Africa: The World Bank's Africa Regional Program on Enterprise Development is an ongoing research project that generates business knowledge and policy advice useful to private sector manufacturing development in Sub-Saharan Africa. The programme implements Investment Climate Assessments in sub-Saharan Africa and undertakes additional research, including regional assessments.

World Business Environment Survey: The World Business Environment Survey, a joint firm-survey project of the World Bank's Investment Climate and Institute units, covers over 10 000 firms in 80 countries in 1999-2000. It covers the quality of the investment climate as shaped by domestic economic policy; governance; regulatory, infrastructure and financial impediments, as well as assessments of public service quality.

World Bank Institute Governance Data: Governance Research Indicators is a dataset of aggregate governance research indicators for almost 200 countries for 1996-2002, for six dimensions of governance: *i)* voice and accountability; *ii)* political stability and absence of violence; *iii)* government effectiveness; *iv)* regulatory quality; *v)* rule of law; and *vi)* control of corruption. This dataset draws in part on the results of both Business Environment and Enterprise Performance Surveys and Investment Climate Surveys.

World Bank Investment Climate Surveys and Assessments: Investment Climate Assessments (ICAs) were officially begun in July 2002, although this was preceded by eight pilot studies. Since this time, 45 surveys have been conducted and ICA reports have been prepared. Investment Climate Surveys (ICSs) uses large samples of firms (*i.e.*, 1 500 firms), while the ICAs supplement this with information from key informants. ICAs are designed to systematically analyse conditions for private investment and enterprise growth. Underpinning all ICAs is a standard core investment climate survey instrument, which allows the comparison of existing conditions and the benchmarking of conditions to monitor changes over time. The survey is administered to managers of firms and consists of a core set of questions as well as several modules that can be used to explore in greater depth specific aspects of the country's investment climate and links to firm-level productivity.

World Bank Doing Business Survey: The data set covers 140 economies. The sample includes 22 high-income OECD economies as benchmarks, 25 economies from Europe and Central Asia, 33 from Africa, five from South Asia, 21 from Latin America, 14 from the Middle East and North Africa and 13 from the East Asia and the Pacific region. The survey reviews laws and regulations in each economy and conducts targeted interviews with regulators or private sector professionals in each topic. It relies on co-operative arrangements with other departments of the World Bank, other development agencies, private consulting firms and business and law associations. Main topics covered include: starting a business; firing workers; enforcing contracts; getting credit; and closing a business. Standard templates/questionnaires have been developed for all topics.

ANNEX 4

MECHANISMS FOR INVESTMENT-ENHANCING ODA

There are a variety of mechanisms development agencies use to provide investment-enhancing ODA. The term "mechanism" is used here to describe the way in which ODA-supported activities are designed, implemented and monitored. This usually involves organisational structures – either formal or informal – and the use of processes that bring programme partners together and build support and commitment for reforms that are supported by investment-enhancing ODA.

Direct programme interventions: This refers to a typical development-supported activity in which a single development agency provides direct support to one or more development partners. Because policy and institutional reform can take a long time, in many cases development agencies work with development partners over quite a few years. There are a number of advantages to this approach:

- Programmes can be relatively easier to plan and implement since there are fewer partners to consult with.
- Lines of accountability and programme management procedures can be clearer and more direct.
- Programme flexibility can be enhanced – with fewer partners to consult with and agree on, programmes can more easily and quickly respond to changing external conditions.

One of the greatest disadvantages of this model of intervention is that it can lead to a situation in which there are many development-funded programmes that are poorly co-ordinated and giving different messages to the government and other stakeholders.

Collaborative programmes: In some cases, development agencies collaborate together on specific programmes. Increasing evidence can be found of bilateral and multilateral development agencies working together to mobilise investment in developing countries. Such collaborations enable development agencies to share risks and provide access to a larger pool of expertise. Collaborative programmes can also help many development agencies to "speak with one voice", which is critical when development agencies are supporting reform efforts.

There are a number of recent development frameworks that have been adopted by development agencies and development organisations that encourage better co-ordination and collaboration. These include Poverty Reduction Strategy Papers, the Monterey Consensus and the Millennium Development Goals.

Care should be taken when applying generic programme planning frameworks. Many of these are based on broad poverty reduction perspectives, which can be limited in terms of the role of the private sector and the importance of the investment climate. While most full Poverty Reduction Strategy Papers, for example, acknowledge that macroeconomic instability, inadequate policies and weak governance may limit the extent to which the poor benefit from economic growth, most underlying issues such as the regulatory framework, lack of transparency and corruption are only dealt with in a very limited way. Moreover, the actual involvement of the private sector in the process of preparing Poverty Reduction

Strategy Papers has tended to be limited, with greater attention being paid to the involvement of civil society organisations (see Bannock, 2002).

Participation in formal multi-development facilities: There are an increasing number of formal facilities being established to facilitate the involvement of different development agencies in the support of investment-oriented reform programmes. An example of the multi-development facility model is the Public Private Infrastructure Advisory Facility. Another example is the Integrated Framework, a multi-development structure supporting trade capacity building, as well as the Financial Sector Reform and Strengthening Initiative which is a large technical assistance facility, located within the World Bank and funded by a number of multilateral and bilateral development agencies.

Establishment of specialised funding and programme facilities: Within certain fields, investment-enhancing ODA can benefit from the use of dedicated facilities that focus and co-ordinate interventions more effectively. In some cases a single development agency will establish these facilities (*e.g.*, the World Bank Group Project Development Facilities, DFID Challenge Funds); in other cases a group of development agencies will do this (*e.g.*, Public Private Infrastructure Advisory Facility). One of the greatest advantages to these programme facilities is that they can draw in the commitment and resources of agencies other than development agencies. One of the most important contributors in this context is the private sector. Multi-development facilities for technical assistance, says the World Bank, "leverage resources and expertise and facilitate learning by participating development agencies". This is especially important where the frontiers of knowledge are moving quickly, as is the case with investment-enhancing ODA. Such facilities can bring specialist expertise to bear on the design and implementation of projects and can reduce sensitivities associated with technical advice coming from developed countries (World Bank 2004a, p.193).

Supporting regional institutions: Improving private investment often requires support for reforms that go beyond national boundaries. There is a growing range of examples that demonstrate the value of regional co-ordination and information sharing that can be used to enhance national reform efforts and, to this end, development agencies have recognised the importance of supporting regional institutions. Development support for reform efforts in Africa through the New Partnership for Africa's Development (NEPAD) is an example of this, as is the Global Coalition for Africa.