STRENGTHENING FINANCING FOR DEVELOPMENT: PROPOSALS FROM THE PRIVATE SECTOR

COMMENTS ON THE MONTERREY CONSENSUS AND PROPOSALS FOR THE INTERNATIONAL CONFERENCE ON FINANCING FOR DEVELOPMENT

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COMPILED BY THE UN-SANCTIONED BUSINESS INTERLOCUTORS
TO THE
INTERNATIONAL CONFERENCE ON FINANCING FOR DEVELOPMENT

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WITH A PROPOSAL BY GEORGE SOROS TO INCREASE SIGNIFICANTLY RESOURCES FOR DEVELOPMENT ASSISTANCE AND GLOBAL PUBLIC GOODS

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GENERAL COMMENTS

We welcome the overall practical and reasoned tone of the Monterrey Consensus, and above all, the call for new mechanisms, initiatives, and partnerships to advance the critical objectives of financing for development. The Consensus demonstrates a clear understanding of how to enhance and mobilize resources to finance development with its new, more productive results-based approach. We applaud the explicit commitment of UN member countries to the critical preconditions noted in the consensus.

We appreciate that the Consensus has taken into account a number of the suggestions submitted by the private sector in October 2001 and January 2002. Its support of new public-private sector financing and consultation mechanisms, strengthening of multilateral and regional development banks' support of private sector investments, and public-private sector initiatives that enhance the ease of access, accuracy, timeliness, and coverage of information on countries and financial markets has opened the way to important progress in these areas.

We particularly welcome the attention given to "Mobilizing domestic resources for development", since, as generally acknowledged, development must flow largely from national effort. It rightly recognizes that raising domestic resources to support necessary capital formation is a "critical challenge" in the pursuit of financing for development. Its stress on sound macro-economic policies, good governance as "essential for sustainable development" and the need to foster "a dynamic and well-functioning business sector" is most appropriate.

Beyond the useful framework provided by this section, what is critical to success is tangible official-sector commitment to the basic principles for business-enabling environments. This includes protecting creditor and investor rights and rule of law, a precondition to establishing a climate conducive to the optimal mobilization of both domestic and foreign investment for development, as noted below.

The attention given to mobilizing domestic and foreign private capital is well placed for another compelling reason. Since official development assistance (ODA) is almost certain to fall substantially short of meeting the daunting demands for development finance, financing of development will depend heavily on the private sector. However, it should be noted that the IMF has forecast significantly reduced net capital flows to developing countries, resulting in the likelihood of increased liquidity squeezes and refinancing risks.

Therefore, international organizations and national governments will need to be more innovative in dealing with these developments, proactively supporting specific, practical mechanisms to induce new private-sector investment.

MOVING FROM WORDS TO ACTION

As interlocutors for the private sector, we appreciate and generally endorse the tenor of the Monterrey Consensus. However, in our view, the general language concerning the private sector needs to be supplemented by concrete, actionable proposals to enhance the prospects that the objectives of the Conference will be achieved. To this end, we are putting forward specific proposals for discussion at Monterrey. These are summarized briefly below, with more detailed annexes attached. In general, they build on the following points and principles.

FOCUS

While policy problems are becoming more complex and multidisciplinary, entailing a considerable number of cross-linkages, we feel that a holistic approach should not become so broad as to impair operational and practical results. Ensuring pragmatic and operational links between the global plan of action and the country-level programmes would facilitate implementation. Programmes should be country-focused around actual measurable objectives, with clear performance benchmarks that ensure effective coordination, cost-effectiveness and policy coherence.

MICRO-POLICY

Most of the proposals made in the Monterrey Consensus with regard to mobilization of domestic capital are on the macro-economic level. However, the development objectives cannot be realized without attention to practical ways to improve the micro-policy preconditions for business-enabling environments – including issues such as: mortgage availability, the use of collateral to borrow from banks, the property ownership system, title deeds to assets, and the rule of law. We feel that not enough studies and analyses have been done on the hindrances to private entrepreneurship, investment, job creation and enterprise development, and subsequently, specific proposals on how to reduce these impediments are lacking.

PRIVATE-PUBLIC PARTNERSHIPS

The private sector supports private-public partnerships, and the critical role of the public sector in channelling private sector activities in ways that support development objectives. Increased innovative multilateral finance and official development assistance are critical to financing for development. Key examples include co-financing, guarantee insurance, and the linking of foreign direct investment (FDI) to official development assistance (ODA) in the financing of specific projects, particularly infrastructure. Such linkages can contribute to the achievement of good government and good governance, without which ODA and private investment cannot be effectively used. Further, without public support and guarantees, the private

sector is unlikely to assume the risk of major investment in basic development projects.

BASIC PRINCIPLES

If the international and domestic private sectors are to be more effective in financing for development, the following basic principles must be put into practice by national governments and their international financial and development institutions, and reflected in everyday policies and decision-making.

- ***Accountability***
  Explicit performance measurements systems must include mapping of the use of funds and evaluation of performance against original objectives.

- ***Respect for creditor and investor rights***
  Investors within and outside countries need to have independent assurances that their rights are acknowledged and respected by national governments.

- ***Country-centered, results-based focus***
  Governments should be encouraged to "own" and advance their development plans, creating explicit performance benchmarks and identifying needed supports from the private sector as well as the development agencies, non-governmental organizations, and other governments.

- ***Third-party audits and evaluations***
  Government credibility to investors would be enhanced with third-party audits of country disclosures, in line with corporate disclosure requirements.

- ***Ongoing, meaningful consultations with the private sector***
  Public policy-makers need to be proactive in exploring new ways to involve the private sector—both domestic and international—in planning and decision-making processes.

- ***Transparency of decisions***
  Governments should ensure transparency initiatives go beyond the current standards-setting process to those areas of critical importance to financing development, such as establishing more stable policies for the international financial system.

The adoption of these basic principles by governments is important to the building of confidence and credibility so critical to both domestic and international investors, and creating the basis for global prosperity and stability.

SUMMARIES OF PROPOSALS

As the designated business interlocutors for the UN, we are reaching out to the larger business community and to development experts in the official sector in both developed and developing countries, asking for specific proposals on how to increase the volume, sustainability, and cost-effectiveness of equity and debt financing for development.

The proposals will be further refined with the input of policy-makers in governments and multilateral and regional development institutions and the private sector before being presented during the International Conference on Financing for Development at The Business Forum on Monday 18 March. Subsequently, at the Conference from Tuesday 19 March to Friday 22 March there will be day-long Follow-Up Roundtable Dialogues with governments, multilateral institutions, and investors to develop these proposals further with the intent to launch them as private-public sector initiatives upon the conclusion of the Monterrey Conference.

The proposals now being developed by the private sector for the International Conference on Financing for Development are from various sources, and do not necessarily represent the views of all our organizations or our respective company members. They fall into the following four categories: strengthening communication, information, analytics, and capacity; enhancing equity finance; enhancing debt finance; and enhancing ODA, as outlined below.

SUMMARY I

MECHANISMS FOR STRENGTHENING COMMUNICATION, INFORMATION, ANALYTICS, AND CAPACITY IN THE GLOBAL FINANCIAL SYSTEM

The Monterrey Consensus explicitly acknowledges the importance of launching new private-public initiatives in information: “We encourage public/private initiatives that enhance the ease of access, accuracy, timeliness and coverage of information on countries and financial markets, which strengthen capacities for risk assessment” (paragraph 22). The essential precondition to effective finance is quality, timely communication, information, and analysis that deepen the capacity of both policy-makers and investors to be accountable to their respective objectives of development and investment performance. Quality communication, information, and analysis provide the underlying basis for domestic governance and capacity-building, national and international policy coherence, debt management, and sovereign risk assessment. None of these objectives can be realized without the proactive endorsement of new initiatives by national governments and international and regional organizations of specific concrete actions to further strengthen communication, information, analytics, and the capacity of all decision-makers to make better quality, timely decisions. Below are specific working proposals to advance these objectives.

A. ESTABLISHMENT OF AN INFORMATION CLEARINGHOUSE: CLOSING THE INEFFICIENCY, RELEVANCY, AND CREDIBILITY GAPS BETWEEN INFORMATION USERS AND PROVIDERS

Despite the huge investment in country “transparency” and codes and standards, the failures in information and analytics continue, as is well evidenced by the continued costly miscalculations of investors and policy-makers after the Asian crisis (e.g., the failures of country risk analysts and risk managers to identify and formulate preemptive risk-mitigating actions for major macro risks such as the Argentina crisis, Long-Term Capital collapse, and terrorist attacks of September 11th). The ongoing gap in information and analytics is also evidenced by the continuing market outreach efforts of the international financial institutions as well as the conclusion of the 21 August 2001 report of the Financial Stability Forum on the Implementation of standards stating that a “mechanism for information exchange” is needed to meet the challenge of technical assistance, facilitating the implementation of codes and

standards, and the integration of information on progress into market investment decision-making.

Leading information and internet technologies could be employed for the benefit of both investors and policy-makers, facilitating cost-effective "one-stop-shopping" for free and paid-for information, analysis, and risk management services provided by governments, international organizations, research organizations, independent experts, and private sector firms.

An information clearinghouse would strengthen the global financial system and the accountabilities of both investors and policy-makers by:

- ***increasing the cost-effectiveness of existing economic and political information***, closing the costly gap between users and providers with an efficient "market outreach" interface for information providers, making it easier for decision-makers to use quality relevant information to improve their decision-making;
- ***providing a much-needed distribution platform*** for a range of independent expert assessments, improving the quality of decision-making by both investors and policy-makers and reducing over-reliance on fixed-income country ratings and the associated risks of market herding, bias, and contagion; and
- ***enhancing "Market Transparency"*** and the capacity to manage market-related risks by tracking market decision-making criteria and behaviour.

Such an information clearinghouse could be activated with UN support, a modest amount of funding from the official sector, and the recruitment of international investors and leading edge technology companies. Maintaining independence of the clearinghouse from short-term political and business influences is critical to its success as a credible independent broker bridging information and decision needs between investors, analysts, and policy-makers. ***(See Annex A and Moody's Investors Service's Proposal to "Enhance Infrastructure Finance through Expanded Access of Issuers to Knowledge and Training")***

B. ESTABLISHMENT OF COUNTRY-BASED INVESTOR NETWORKS

The Monterrey Consensus explicitly acknowledges the importance of launching new mechanisms to facilitate public-private sector communication and cooperation: "…public/private initiatives could include the development of consultation mechanisms between international and regional financial organizations and national governments with the private sector in both source and recipient countries as a means to create business-enabling environments" (paragraph 21bis). The establishment of Country Investor Networks could serve to facilitate direct exchanges between governments and investors (domestic and international) on impediments to finance and possible remedies, focussing scarce resources and priorities for reforms, and the adoption of codes and standards. Employed in a systematic manner, these Country Investor Networks would also provide many widely-recognized benefits of Investor Relations Programs to national governments and their citizens.

Also, such Country-Investor Networks can be employed to aid in the sequencing of reforms as well as global codes and standards within the differing context of individual countries. As noted in the post-Asian crisis debate on capital account liberalization and the often-cited claim "One size does not fit all," there is a practical need to establish priorities within the specific context of the needs and capabilities of each individual country, and its potential investors (domestic and international). A country-centered focus that facilitates ownership and accountability, with immediate feedback loops reinforcing progress is critical to effectiveness.

Country Investor Networks could be established at low cost as part of the Information Clearinghouse (noted above), with international financial organizations or global technology companies contributing technology resources to construct an internet-based global template, supplemented with technical assistance to individual countries requesting such a service. ***(See Annex B)***

C. ESTABLISHMENT OF INDEPENDENT EXPERT ADVISORY GROUPS TO PROVIDE OPEN, TIMELY INPUTS AS AN INTEGRAL PART OF POLICY-MAKER DECISION-MAKING

As globalization confronts us with unprecedented issues, failures in policy-making at all levels exact escalating social, political, and economic costs to all stakeholders in the global financial system. Again, the examples abound: the late identification of debt problems in Asia, the insufficient response to Argentina's currency board dilemma, the ongoing quandary of sovereign bond restructurings, etc.

The global community of responsible leaders and institutions can significantly enhance our shared capacity to identify problems in a more timely manner and formulate possible remedies by using Independent Expert Advisory Groups

consisting of experts from across the private and public sectors, with different country, sector, and functional expertise. Serving as a systemic improvement to the front end of information and analytical processes, Expert Advisory Groups could provide countries and international organizations with a cost-effective means to harness expert capacity in building the national, regional, and global regulatory and institutional frameworks critical for investment, growth, and stability.

This would also advance public-private partnerships, by serving to systemically engage the private sector in proposing remedies to critical problems and defining collaborative solutions. This systemic strengthening to the information and analysis process would provide critical checks and balances against short-term pressures and vested interests, enhancing pre-emptive capacity and the decision-making processes for both policy-makers and investors. Such Independent Expert Advisory Groups could be established as part of the Information Clearinghouse (noted above), with the endorsement of the UN and collaboration from experts in the international and regional development institutions. One example is the AMBAC proposal to set an independent expert advisory group on Enhancing Access to Debt Markets described in the later section on debt-related initiatives. ***(See Annexes C and M)***

D. THIRD-PARTY AUDITS AND PERFORMANCE BENCHMARKS OF CRITICAL FUNCTIONS IN THE GLOBAL FINANCIAL SYSTEM

At no other time in our history have our international financial institutions and national governments themselves been the subject of such extreme controversy and criticism from a range of investors, policy makers, and civil society. The credibility of the global financial system, its members, and the process itself can be enhanced through a meaningful system of credible audits and evaluations that would underpin confidence in its integrity, and serve to authoritatively pinpoint progress and setbacks.

Such a system could also provide a critical platform for developing countries to set forth national development strategies, establishing these development objectives as the key criteria for evaluations of success and failure. Audits could be done against designated development objectives. In effect, these "country disclosure reports" could function like the annual and quarterly reports of private sector companies, serving to reinforce government accountability and build confidence in the investor community. The establishment of such a credible evaluation system would provide immediate and meaningful rewards for those countries showing progress, improving investor's ability to differentiate between countries, thereby reducing the costs of bias and financial contagion.

Further this capacity for third-party audits needs to apply to both public and private participants, and cover all levels of participants in the global financial system, from global to regional, country and local. Such a system of audits could be administered

through the information clearinghouse (noted above), with support from third-party entities in the private sector (such as accounting firms) as well as the international/regional financial institutions and member countries. ***(See Annex D)***

E. DEVELOPMENT OF COUNTRY-BASED KNOWLEDGE TOOLS AND CAPACITY-BUILDING PROCESSES FOR LEAST DEVELOPED COUNTRIES

UNCTAD and ICC are engaged in a project on investment guides and capacity-building for selected least developed countries (LDCs). Its principal goals are to create a knowledge tool that enables LDCs to attract and maintain increased foreign direct investment (FDI) and forge a convergence of purpose between investors and LDC governments. The objective of this project, at the most general level, is to assist development and poverty reduction in LDCs, by helping LDCs attract foreign direct investment (FDI). At a more specific level, the objective is to help bring together countries that seek new investment and companies that seek new locations.

The project promotes capacity-building in LDCs from the ground up with all partners through a dialogue among local enterprises, foreign investors and government. Workshops focus on best investment promotion practices and policy options, and consider the microeconomic issues relevant to FDI. The workshops analyze the implementation of international support measures in the areas of official development assistance (ODA), debt, investment and trade. Since accurate information concerning investment conditions within a country is essential, business investment guides are produced to provide a broad overview of current investment opportunities and prevailing socio-economic and political conditions; and general guidance on the legal and other issues related to undertaking investment in each individual country. The project can easily be expanded to cover a wide range of LDCs at relatively low cost provided that governments are willing to find the necessary funding. ***(See Annex E)***

SUMMARY II

ENHANCING EQUITY FINANCE WITH GOVERNMENT SUPPORTED INITIATIVES

The Monterrey Consensus explicitly acknowledges the importance of new initiatives in finance supported by the official sector: "… we invite banks and other financial institutions, in developing countries as well as developed countries, to foster innovative developmental financing approaches" (paragraph 21); "We will support new public/private sector financing mechanisms, both debt and equity, for developing countries and countries with economies in transition, to benefit in particular small entrepreneurs and small and medium-size enterprises and infrastructure" (paragraph 21).

As recognized in the Report, enhanced equity finance is especially critical to achieving development objectives. The cornerstone of development is the mobilization of domestic resources, and the overwhelming problem of developing countries is an overreliance on debt finance. However, this objective of enhancing equity finance is not achievable without the launch of new initiatives proactively supported by national governments and critically, with the explicit support and funding of international and regional organizations. Below are summaries of proposals now in development to build targeted equity funds for developing countries that would mobilize both domestic and international private sector equity capital.

A. DEVELOPMENT OF COUNTRY RESTRUCTURING FUNDS

The proposal is to establish a global program for country restructuring funds that accelerate private sector finance for small and medium-sized companies in developing countries, with the support of the national governments and funding from multilateral and regional development banks. The global program would enlist international fund managers to partner with domestic private sector investment companies in the provision of finance and expertise to weak, but viable private sector companies under clear investment guidelines with regular reporting and incentive fee structures. This proposal would be implemented on a country basis, focusing on helping a large number of viable over-indebted domestic companies, in the process rejuvenating the local economy, providing jobs, and establishing a larger basis for the national economy. National governments would be asked to endorse the project, and development financial institutions can contribute by providing funding and exit

vehicles to bridge "equity liquidity gaps." The proposal is based on a successful corporate restructuring fund in South Korea. ***(See Annex F.)***

B. INCUBATING COUNTRY VENTURE CAPITAL FUNDS

The proposal is to establish country venture capital funds, with the support of the national governments and the regional and international financial organizations, to provide finance and expertise to individuals and companies with promising business concepts. The international development community would designate a significant component of its aid program to risk-ventures and work with local public entities, using similar programs as the Small Business Administration in the US, in developing countries.

Such funds can be engineered to attract limited foreign funds over time. To do so, an international fund can be set up and allocated on a regional basis among four or five regions, e.g., Latin America, South Asia, the Middle East, and Africa. The Fund can enter into a "master agreement" with a number of developed country private managers with proven skills. Each regional grouping can focus on a number of countries whose governments must be willing to support the activities of the Fund through allocation of supplementary local funds as well as providing the prerequisite regulatory framework and other facilities. The Fund would work with local entrepreneurs who may also become partners. ***(See Annex G)***

C. DEVELOPMENT OF COUNTRY-BASED MICRO-CREDIT AND CONNECTIVITY PROGRAMS

The proposals is to develop county programs around both micro-finance and telephone access, thereby enabling rural populations in developing countries to develop critical linkages to markets and finance. The project is based on the successful experiences of Grameen Bank and Grameen Phone in Bangladesh, two institutions which have empowered rural populations through micro-credit and telephone access, respectively.

The first proposed target country would be Afghanistan, with the establishment of Afghan Credit and Connectivity ("Afghan C&C") as a long-term project dedicated to meeting two fundamental development needs of Afghan citizens who are substantially impoverished during two decades of war and misrule. While in Bangladesh the connectivity program was piggybacked on an already existing micro-credit program, Afghan C&C envisions launching both programs at the same time with each supporting the other. Credit will enable citizens to start small enterprises, including retailing telephone services. Telephone services, for example, would help

administer a credit program in a country such as Afghanistan where clusters of villages are separated by great distances.

Afghan C&C will be put together primarily through a partnership between a micro-credit institution and an experienced telephone company. A detailed feasibility study and other initial groundwork can be started with $2 million and the company can be launched with $200 million, with half the funds dedicated to credit and the other half for a telephone network. ***(See Annex H)***

D. PROMOTING EQUITY IN DEVELOPING COUNTRIES

Efforts to strengthen development should focus on the role of equity markets in promoting capital formation and economic growth in developing countries. During the1990's the number of developing country equity markets expanded dramatically in Eastern Europe, Central Asia, Africa, and other regions. The markets developed in response to several factors. They included the end of communism and the privatization of state owned companies, the introduction of tax allowances to promote equity IPOs, and the rise of institutional savings flows targeted on non-bank financial assets through the establishment of pension funds.

As a result of these factors the developing countries now have an aggregate stock market capitalization of over 2 trillion dollars compared to only a few hundred billion dollars during the early 1980's. We should focus on a variety of proposals for promoting further growth of equity markets in developing countries. They would include: tax allowances for equity IPOs, further expansion of retirement savings programs focused on non-bank financial assets, creation of more securities with dual listings such as GDR's and ADR's, introduction of better standards for financial disclosure and corporate governments to promote public confidence in equities, establishment of effective regulatory institutions to ensure that security laws are obeyed, and establishment of an emerging market association of minority shareholders to protect the rights of non-management owners.

The industrial countries now have an aggregate stock market capitalization approaching 30 trillion dollars for a population of 900 million people. Developing countries should aim to have a market capitalization of at least 10 trillion dollars by 2010/2015 through the pursuit of policies aimed at producing broader equity ownership. The Financing for Development initiative should ensure that experts from both the private and public sector partner in exploring policy options for achieving this objective. ***(See annex I)***

E. ESTABLISHMENT OF WORLD DEVELOPMENT CORPORATION TO FUND REGIONALLY-BASED OPERATING COMPANIES THAT PROVIDE FUNDING, MANAGEMENT, TECHNOLOGY, AND MARKET ACCESS

The World Development Corporation, an idea developed by Professor George Cabot Lodge from Harvard Business School, is designed as a primary funding vehicle for massive job creation (a "Salk" vaccine to eradicate global poverty) in a very pragmatic way. The way is for the WDC to be the catalyst investor in developing six New York Stock Exchange listed operating companies, for the following emerging markets: Emerging Europe, Emerging Asia, North Africa and the Middle East, Sub-Saharan Africa, Emerging Latin America and Emerging North America. Each of these NYSE companies will be used to provide money, management, technology and access to global markets for its respective area. These resources will be used to acquire and develop (often in exchange for stock in the NYSE company to create true partnerships with local participants) control positions in economic opportunities in these areas.

GE is a good corporate role-model for operations, however ownership in each NYSE company will include a much larger participation by local and regional investors. Local partners will provide natural and human resources, and access to local markets and capital.

Each NYSE entity is expected to become a primary developer of local management and entrepreneurial talent because of its ability to provide resources, training, and superior compensation (both cash and stock in the NYSE company). The combination of financial incentives and the ability to make a major difference to one's country or region, is expected to act as a magnet for management talent, and over time WDC's "graduates" should spawn many new enterprises. ***(See Annex J)***

SUMMARY III

ENHANCING DEBT FINANCE WITH SPECIFIC OFFICIALLY SUPPORTED INITIATIVES

The Monterrey Consensus explicitly supports the creation of new public-private financing mechanisms, and further calls on the international financial and development institutions to increase their support for private foreign investment with provisions of risk guarantees, co-financing, and export credits:

> "We will support new public/private sector financing mechanisms, both debt and equity, for developing countries and countries with economies in transition, to benefit in particular small entrepreneurs and small and medium-size enterprises and infrastructure" (paragraph 21bis); "…the relevant international and regional institutions as well as appropriate institutions in source countries to increase their support for private foreign investment in infrastructure development and other priority areas"; the recognition of the importance of "… export credits, co-financing, venture capital and other lending instruments, risk guarantees, leveraging aid resources, information on investment opportunities, business development services, fora to facilitate business contacts and cooperation between enterprises of developed and developing countries, as well as funding for feasibility studies";"…strengthening of the multilateral and regional financial and development institutions is desirable" (paragraph 20); "… we invite banks and other financial institutions, in developing countries as well as developed countries, to foster innovative developmental financing approaches" (paragraph 21).

The Report recognizes that the provision of affordable, adequate debt finance is critical to achieving development objectives. Again, these objectives are not achievable without the launch of new concrete action plans that are proactively supported and funded by international and regional financial institutions. Below are summaries of specific proposals in development to advance these objectives.

A. A PROPOSAL TO CREATE A PUBLIC/PRIVATE BUSINESS ENTITY TO PROVIDE LONG-TERM DEBT FINANCING FOR INFRASTRUCTURE DEVELOPMENT IN DEVELOPING COUNTRIES

This proposal is aimed at providing large-scale (multi-billion dollar), recurring investment flows to infrastructure projects undertaken by both the public and private sectors in all countries, with no bias towards the larger economies. Since this investment would be in the form of ten to twenty-five year financing, the problems of volatility of capital and the lack of long-term financing for long-lived infrastructure investments would be addressed.

Infrastructure projects, such as power plants and water works, are both capital intensive and long-lived. In order for the rates paid by consumers to be affordable, the capital cost of the projects needs to be amortized over the economic lives of the projects, typically fifteen to thirty years. Long-term finance has not been available, however, on a regular basis to emerging economies, rendering the undertaking of such projects by the private sector uneconomic in such economies.

The proposal is to solve this problem by the creation of a funding mechanism by which senior secured debt, privately issued by both private and public sector sponsors, and of all levels of credit quality in infrastructure projects around the world, including OECD and non-OECD countries, are pooled to form the collateral for trusts that would issue investment grade publicly-traded debt instruments in the world capital markets. The organization sponsoring such trusts would be jointly-sponsored by public and private sector parties.

Specifically, the proposal involves creation of sector-specific Ginnie Mae-like investment pools, each aimed at a specific economic sector, which would purchase secured, non-tradable debt and fund themselves by issuing tradable fixed income securities in the global capital markets. In order to create diversified pools that would receive investment-grade ratings, the sponsors envision combining securities from both developed and developing markets - including both investment grade and below investment grade securities from the public and private sectors - which would enable even the poorest countries to have ongoing access to long-term international capital.

For infrastructure financing, which is currently done on a project basis in the private placement market where there are limited resources, this new financing vehicle would provide a liquid market for securities issued by the diversified investment pools that it would create, increasing the availability of finance while reducing the cost of capital. In addition to improving developing country access to long-term funding, this process could standardize project structures and instruments, reducing costs (administrative, legal, accounting, etc.) while improving transparency. For investors, the pools formed would be liquid (an active market would be established) and income producing.

The sponsors of this proposal are requesting that the public sector, multilateral organizations, and private sector investors participate in the initial capitalization of this entity, through the purchase of founders' shares, sufficient to establish the company and financing its first trust for infrastructure investment by the end of 2002. To function most efficiently, this entity would need to operate on a large scale so that a liquid public market for its securities is created; this means it needs to undertake financings of the multi-billion dollar magnitude annually. ***(See Annex K)***

B. AN INDEPENDENT EXPERT ADVISORY GROUP TO ENHANCE ACCESS TO DEBT MARKETS

This proposal is to create a platform (an independent expert advisory group) that enables the private and official sectors to work together to create the best package of credit enhancement for the international investors at the lowest cost to developing country issuers. Today, understanding and coordination critical to effectiveness is often hampered by the normal competitiveness among private sector parties and by the differences between public and private sector objectives, operating procedures and skill sets.

The first step is the formation of an on-going forum for discussions among the critical participants, including developing country borrowers (such as banks and finance companies, corporations, utility companies); official multilateral and regional financial organizations; official bilateral financial organizations; investment banks; financial advisory services specializing in developing country structured financing; credit rating agencies; private insurance companies offering partial credit or risk insurance or contingent liquidity facilities); monoline bond insurance companies; and institutional investors (insurance companies, pension funds, mutual funds, etc.).

Critical issues that need to be discussed and resolved include how specific political risks can best be mitigated and by whom (public or private sector); procedures to ensure timely processing of transactions when public and private sector entities are working together; ways to coordinate pricing when several insurance policies or contingent financing facilities are offered together in a transaction; standardization of coverages and contracts; roles for public and private sector participants in post issuance surveillance of transactions; how public and private sector parties might work together in remediation efforts to prevent adverse political events; and rights in recovery by public and private sector creditors and insurers following a default.

It would be desirable for the discussions of the Independent Expert Advisory Group to be ongoing, with the proceedings recorded and widely disseminated. A clearinghouse of documents and data (preferably accessible via the internet) should also be established. The activities could be established as part of the proposed Information Clearinghouse and Independent Expert Groups (Annexes A and C), with

the support of the United Nations and collaboration from experts in the international and regional development institutions. ***(See Annex L and Standard and Poor's comment paper "Using Project Finance to Facilitate Private Sector Investment in Infrastructure and Export Projects")***

C. PROPOSALS TO INCREASE THE NUMBER OF VIABLE WATER PROJECTS IN DEVELOPING COUNTRIES

In the Millennium Declaration, the United Nations reconfirmed the goal of halving by 2015 the proportion of people who do not have adequate access to water and sanitation services. The estimates prepared for the second World Water Forum in the Hague (March 2000) show that implementing this goal would require a doubling of the annual water investment in developing countries (the current $80 billion figure should be raised to $180 billion). The second WWF concluded that private financing should be looked for since public budgets cannot cope with the enormous financing needs.

Although private finance is available for funding sound water projects in many industrialized countries on a project finance basis, very few projects are really implemented in this way in developing countries. Because of this lack of adapted financing tools, globally, water and sanitation services do not improve at a pace sufficient to meet the official Millennium target. This is detrimental to more than 1 billion people worldwide for water supply and more than 2 billion for sanitation services.

As water differs in many respects from other types of services, we make three proposals to facilitate the financing of water and sanitation projects in the developing countries. They should help to increase the number of viable water projects.

Water Projects Proposal 1: Facilitate the Mixing of Public Funds with Private Funds

When a city wants to fund significant investments for developing its water networks and simultaneously decides to take advantage of the management expertise of a reputable private operator it usually chooses one of the 3 following schemes:

1. Contracting out the operation and management of the water system to the operator while keeping the funding of the necessary new assets with public money. In this case the operator is not enabled to consistently optimize capital and operation expenditures, which can be detrimental in the long-term.

2. Privatizing the water and sanitation system: the city sells the water assets to an investor. This scheme is the most expensive for the water-users, since they must refund over time the purchase price of the existing assets.

3. Contracting out the management of the water system and the funding of the necessary new assets (via private finance) to the operator while keeping a public ownership of the existing assets. This scheme, also known as "concession", usually yields the best results. But it is not applicable everywhere since it requires an overall full-cost pricing policy in the related territory.

This proposal is to modify the constraints, which currently rule the use of International Financing Institutions-backed public money in order that such money could be used to partly fund the needs of a publicly owned water system even if it is temporarily operated by a private operator.

Obviously, this would not mean subsidizing the operator but subsidizing a project in order to make it economically viable. The public money would either fund publicly-owned new assets (to expand the water network, or to jump-start sanitation programs), could be targeted at improving service in low-income neighborhoods, or could partly subsidize the water rates in order to keep them affordable to low-income people.

The rapid improvement achieved in the quality of service thanks to the combination of public and private finance would start a virtuous circle and eventually make full cost pricing politically acceptable.

Water Projects Proposal 2:
Develop Long-term Loans Adapted to Long-term Contracts

One of the peculiarities of the water assets is that water networks are made of pipes that last several decades. To keep prices affordable the economical owner of the network, whether public or private, amortizes them over long periods. Unfortunately in many developing countries the maturity of the loans that can be obtained from financing institutions is far shorter. This adds unnecessarily to the burden of funding the initial period of a project.

International Financial Institutions should consider the specificity of water assets and offer very long loans to water operators as well as specific insurance framework at international level. In case of private operators, the length of these loans should be in accordance with the duration of their contracts.

Water Projects Proposal 3:
Develop New Insurance Tools for a Better Risk Allocation

When a local government wants to create a long-term public-private partnership with a private operator, it has to allocate the various risks of the project carefully. The natural owner of the technical and managerial risks is the private operator. However, other risks such as inflation, variation in currencies exchange rates, variations in public policies, are completely out of his control.

The more such external risks are transferred to the private operator, the higher the water rates must be, and the riskier and the less viable the project becomes. Attracting private funds becomes more and more costly and more and more difficult or even impossible. The International Financing Institutions must consider building an insurance framework at international level that temporarily helps private funded water projects when impacted by unexpected brutal changes. ***(See Annex L)***

SUMMARY IV

ENHANCING OFFICIAL DEVELOPMENT ASSISTANCE (ODA) WITH RESTRUCTURING OF OVERSIGHT AND ALLOCATION PROCESSES

The Facilitator's Draft calls for ODA to double, in order to meet the Millennium goal. It also calls for all countries – recipient and donor – as well as international institutions, to make ODA more effective. Again, words must be matched with action. Below are two proposals that aim at providing more financing and more effective use of ODA for development.

A. USING SDRS TO INCREASE INTERNATIONAL ASSISTANCE WITH IMPROVED MANAGEMENT

It is proposed to use issues of Special Drawing Rights (SDRs) to mobilize a substantial increase in international assistance. Less developed countries can add their SDRs to their monetary reserves; richer countries (as defined in the IMF "transaction plan") would donate their allocations to provide public goods on a global scale.

The proposal would be implemented in two stages. In the first stage, a special SDR 21.4 billion issue (approximately $27 billion) authorized by the IMF in 1997 currently awaiting ratification by the United States Congress would be approved by Congress with the proviso that the richer countries donate their allocations in accordance with a Plan.

SDR donations could be made only to pre-approved programs. Programs would include trust funds for the provision of public goods on a global scale as well as matching funds for public/private partnerships. In the first stage, the list of eligible programs would be confined to three or four specific priority areas such as public health, education, information (the "digital divide"), and reform of judicial systems. Government sponsored poverty reduction programs would be excluded; they would be left to the IFIs.

The Plan calls for the creation of an Advisory Board of eminent persons operating under the aegis of the IMF but independent of it. The Board would be appointed on the basis of publicly stated professional qualifications and would not be subject to instructions from the governments that appointed them. The Board would establish a list of programs eligible for SDR donations and it would also recommend priorities but it would have no authority over the spending of funds. The donors would retain

the right to select from the menu prepared by the Board. In this way, there would be a market-like supply and demand interaction between donors and programs. The Board would vouch for the quality of programs and donors would be responsive to public opinion in the quality of their selections.

There would be a separate Audit Commission to supervise and evaluate the programs.

If the Plan is successfully implemented in connection with the special issue of SDRs, the second step of the proposal is to have annual issues of SDRs along the same lines. The range of eligible programs would be expanded. Government sponsored poverty reduction programs could also qualify but only up to a certain limit in order to leave funds for non-governmental channels. ***(See Annex N)***

B. USING PUBLIC-PRIVATE PARTNERSHIPS TO MOBILIZE COST-EFFECTIVE ODA

Engaging the private sector in the production of public goods will require moving away from the model of philanthropy that still characterizes public-private partnerships to a model of joint management and oversight of funds, objectives, and performance. Here are the steps of our proposal:

Divide the production of public goods into major thematic areas, such as education, digital divide, Aids, etc. In some cases, a regional sub-division of these issues may be relevant or necessary.

Create thematic and/or regional funds for each issue-area and/or region, and organize corporate giving to these funds by targeting the Global 500 corporations. In some cases, micro-finance mechanisms and low-interest loans could also be used.

Each fund is to be headed by a board of corporate representatives from the donating corporations, NGO representatives, academia when relevant, and observers from the UN and other multilateral organizations. The funds should be incorporated as foundations, with a president and staff. The composition of the board and staff would reflect the issue-area or the region of activity of each particular fund, and UN observers would be matched to each fund on the basis of their mandate in the UN. A system of consultation with local authorities would be put in place in each region/country at the project approval stage as well as during implementation.

On a regular basis, these foundations would receive grant proposals for projects or other activities to be undertaken with their funds. The board would review and make decisions on proposals.

The actual implementation of projects and activities would be left to UN agencies, other parts of the multilateral system, and NGOs. However, the use of funds, the

monitoring of projects, and the achievement of objectives would be reviewed jointly by the board of each fund and representatives of the implementing partners. ***(See Annex O)***

ANNEXES

PROPOSALS FOR PRIVATE-PUBLIC INITIATIVES AND PARTNERSHIPS

ANNEX A

PROPOSAL FOR AN INDEPENDENT INTERNATIONAL INFORMATION CLEARINGHOUSE

Submitted by Samuels Associates

The establishment of an Independent Information Clearinghouse for cost-effective investor and policy maker access to information and analyses on countries and risk management services would provide a basis for enhancing the accountabilities of both investors and policy makers. It would leverage the massive investments in information, risk management, transparency, and codes and standards by providing a cost-effective bridge between users and providers of information in both the public and private sector. The clearinghouse would serve as a cost-effective, practical mechanism for advancing the objectives of improving country transparency, market transparency, public-private partnerships, and capacity-building.

Despite the abundance of information and analytics, the mistakes and miscalculations of both investors and policymakers are well-charted. Investors and policy makers, confronted with information overload – hundreds of country websites, daily and weekly investment bank publications, country risk reports from rating agencies and independent country risk services, media reports, risk management services and products, and most recently, country compliance with codes and standards – are simply unable to locate and process all the information and analyses on countries relevant to the quality of their decision making and risk management. Often political, competitive, and short-term pressures dominate, and the fundamental analysis is lost in the thick of other more pressing issues or the crisis mode of panicked decision-making. The costs of these information inefficiencies are high for both investors and countries, escalating the risks of misunderstandings, uninformed decision-making, and missed opportunities.

One central website, an efficient "one-stop-shopping" Information Clearinghouse, could act as a cost-effective "bridge" between information providers and decision-makers, closing the current costly gap between existing information and user needs, serving to highlight critical problems for more urgent attention. The Clearinghouse would leverage the massive existing resources already invested by the public and private sectors in information, analysis, and risk management providing the missing links in dissemination ("market outreach") and tools (research, analysis, data feeds, formats, etc.). Similar to other cost-effective organizing vehicles (such as the *Michelin Guide*), the Clearinghouse would provide an information guide that would be regularly updated, easily accessible to all parties, with leading edge technology for

retrieval and analysis. In addition, the Clearinghouse could provide decentralized country platforms for government-investor relations, thereby fulfilling the Financial Stability Forum's recommendation for an "information exchange" mechanism on codes and standards.

In addition, the Information Clearinghouse could serve as a cost-effective umbrella organization for administrating other related critical functions:

- ***Country Investor Networks:***
  facilitating direct exchanges between governments and investors on impediments to finance and possible remedies, focusing scarce resources and priorities for reforms ***(see recommendation two and Annex B);***

- ***Independent Expert Advisory Groups:***
  engaging private and public sector experts in proposing remedies to critical problems and defining collaborative solutions ***(see recommendation three and Annex C);***

- ***Provision of selective third-party audits and evaluations***:
  verifying information critical to investor confidence ***(see recommendation four and Annex D)***.

To be successful, the four above functions would need to be coordinated by a small expert staff, insulated from business and political vested interests, protected by strict rules of governance with undisputed credibility, and placed at arm's length from all existing governmental bodies and business interests. Key providers of relevant information and analysis in the official sector would need to make available their information, analyses, and experts to the above networks, as an integrated part of their respective market outreach, research, and country programs.

Therefore, the information clearinghouse would strengthen the global financial system and the accountabilities of both investors and policy makers by:

- Increasing the cost-effectiveness of existing information, closing the costly gap between users and providers with an efficient "market outreach" interface for information providers, making it easier for decision makers to use quality relevant information to improve their decision making;

- Providing a much needed distribution platform for a range of *independent expert assessments*, improving the quality of decision making by both investors and policy makers and reducing overreliance

on fixed-income country ratings and the associated risks of market herding, bias, and contagion; and

- Enhancing "Market Transparency" and the capacity to manage market-related risks by tracking market decision making criteria and behavior.

Such an information clearinghouse could be activated with UN support, a modest amount of funding from the official sector, and the recruitment of international investors and leading edge technology companies. As noted, maintaining independence of the clearinghouse from short-term political and business influences is critical to its success as a credible independent broker bridging information and decision needs between investors, analysts, and policy makers.

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This proposal is made possible by support from the
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EXAMPLE OF CLEARINGHOUSE FUNCTION:

Moody' s Proposal to Enhance Infrastructure Finance through Expanded Access of Issuers to Knowledge and Training

Submitted by Chee Mee Hu

The following concept paper attempts to contribute to the answer to the fundamental question: "What are the best methods for strengthening realism in the perception of risk by investors (particularly for foreign direct investment) and reducing the gap that may emerge between improvements in a country's investment climate and the response of foreign investors? How, for instance, can national and international policymakers promote private financing of critical infrastructure projects in the developing world?" posed in the Business Council for the United Nation's ***"Executive Summary of Key Issues Relevant to the Private Sector"*** (dated September 6, 2001).

The issues are complex, and ultimately require a melding of private sector and public sector goals and viewpoints. Before that can happen, we need to agree on the following:

- The "private sector" is not homogenous;
- Private sector and public sector goals are not necessarily adversarial;
- Innovation and flexibility is key to optimizing market access; and
- Transparency and structural stability are essential to long-term development.

Objective

An essential objective should be the development of a "common vocabulary" designed to facilitate the private-public sector dialogue. A comprehensive and consistent education program designed to level the playing field among developing countries would serve as the foundation for strategic planning, capital budgeting and financing implementation. The background material for such a training program could be freely available to developing countries on the proposed "Clearinghouse" Internet site and be supplemented by training programs administered in individual countries.

Proposal

Integrated and comprehensive training modules could be set up to establish a common vocabulary for infrastructure investment for developing countries. These

training programs would (1) lay the groundwork for meaningful dialogue based on a universal language, (2) point the way for subsequent research, analysis and training, and (3) stimulate critical thinking about national and regional needs, goals and resources. Without a standardized vocabulary it will be difficult to foster the development of an efficient global market capable of cutting through generalities and misconceptions.

A sample training program might include the following modules:

- A General Introduction to the Capital Markets: Local Currency and Cross Border
- How Do the Capital Markets Work?
- Primary vs. Secondary Markets
- Who Are the Key Capital Markets Participants?
- What Are Their Respective Roles?
- What Do Investors Want?
- Capital Budgeting and Strategic Planning
- Why All Projects Are Not Created Equal
- The Importance of Debt Management
- Financing Alternatives: The Cost/Benefit Analysis
- The Debt Issuance Process
- The Role of the Credit Rating Agencies
- Market Dynamics: The Cost of Borrowing
- Legal and Political Frameworks
- Piercing the Sovereign Ceiling
- Accounting Standards
- The Importance of Transparency and Informational Flows
- What Are the Financing Alternatives?
    - Debt Instruments
    - Short Terms vs. Long Term
    - Public Issue vs. Private Placement
    - Capital Markets vs. Bank Debt
- Components of Well Structured Capital Markets
- Credit Enhancement Alternatives
    - Private Insurance

  - Multi-lateral Agency Support
  - Structural Support
  - Government Support
  - Company Guarantees
  - Others
- Components of Risk Analysis and Their Potential Mitigants
  - Political Risk
  - Currency Risk
  - Construction Risk
  - Ramp Up Risk
  - Operating Risk
  - Management Risk
- Liquidity Analysis of Key Legal Documents
- The Importance of Surveillance and Transparency Over the Life of the Financing
- Case Studies and Typology of Projects
- Other topics

This is a rudimentary outline of the modules that would be included in the training program. There are many issues that would have to be ironed out in the development of modular training programs. For example, who would fund the development and implementation of these training programs? Who would be the lead agencies? How could we ensure that adequate attention is paid to the notion of equal access and adequate follow-up? How would the programs be staffed?

Final Thoughts

In Moody's experience, there are many programs available that provide similar training but there are noticeable differences in format, depth, and availability. The key to this proposal is the emphasis on comprehensive scope, standardization, and the goal of equal and open access. While such a program will be costly to fund and difficult to set up properly, it should be relatively efficient to administer over the long run.

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ANNEX B

COUNTRY-BASED INVESTOR NETWORKS

Submitted by Samuels Associates

The benefits of Investor Relations Programs (IRPs) have been widely recognized by the official community in extensive assessments as well as the private sector in industry forums and taskforces. The experience of several governments in using IRPs to date provides a strong basis for institutionalizing their use across all countries as a means of systemically enhancing governmental capacity in managing capital flows. The identified benefits to sovereigns of IRPs include providing a governmental forum for conveying macroeconomic objectives and explanations of policy measures, enhancing the decision making processes of investors through the provision of key information and streamlining its dissemination, helping policy makers interpret market behavior, and providing the impetus to promote the development of capital domestic markets.

By adopting two way interactive communication platforms, governments can in a cost-effective manner significantly enhance their ability to detect issues affecting access to capital markets, respond to issues, and preempt financial crisis. For example, Internet networks can be used to poll investor sentiment locally and internationally, preemptively addressing concerns, providing proactive explanations of policies and country developments, and reducing the volatility of capital inflows. These government-investor networks can serve as functions within the Information Clearinghouse, with information clusters organized around individual countries.

Country Investor Networks could be established at low cost as part of the Information Clearinghouse (noted above), with international financial organisations or global technology companies contributing technology resources to construct a global template, supplemented with technical assistance to individual countries requesting such a service

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ANNEX C

ENHANCING PREEMPTIVE ANALYSIS AND RESPONSE WITH INDEPENDENT EXPERT ADVISORY GROUPS

Submitted by Samuels Associates

Facing unprecedented global developments unfolding at supersonic speed, both policy makers and investors suffer unprecedented complexity and pressure in decision making. Further, both parties lack sufficient internal analytical resources and the decision making processes of both are pressurized by vested interests with short-term horizons and inherent biases. Governmental organizations at all levels, from the IMF to individual countries, are engaged in "private sector outreach programs" trying to engage private sector experts in the formulation of policies to insure their effectiveness. The establishment of Independent Advisory Expert Groups would extend this process and provide an overall systemic improvement to the analytic process itself.

By engaging the best available expertise in openly identifying problems, options, and possible remedies before crisis, these independent advisory groups would serve to improve the quality and timeliness of decision making, providing a wide array of expert inputs from across the private and public sectors. This systemic strengthening of the information and analysis process would provide checks and balances against short-term pressures and vested interests, enhancing preemptive capacity and the decision making processes for both policy makers and investors.

To be effective, these independent Expert Advisory Groups would need to be placed at specific junctures feeding directly into decision making processes to insure open, timely assessments: Country (Ministries, States, and Municipalities as needed); Regional and Subregional; and Global. The Expert Advisory Groups would provide quality decision making support for individual countries, as well as independent quality guidance to international and regional finance organizations (IMF, World Bank, Financial Stability Forum, regional development banks, G-8, etc.).

Providing a systemic improvement to the front end of information and analytical processes, the Expert Advisory Groups would provide countries and international organizations with enhanced expert capacity to build the national, regional, and global regulatory and institutional frameworks critical for investment, growth, and stability.

Such Independent Expert Advisory Groups could be established as part of the Information Clearinghouse (noted above), with the endorsement of the UN and collaboration from experts in the international and regional development institutions.

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ANNEX D

ENHANCING CREDIBILITY WITH THIRD-PARTY AUDITS AND EVALUATIONS

Submitted by Samuels Associates

The credibility of the global financial system, its members, and the process itself must be established through a meaningful system of credible audits and evaluations that underpin confidence in its integrity and process. As established within national settings, these audits need to apply to both public and private participants, covering all levels of participants in the global financial system, from global to regional, country, and local.

Third-party expert evaluations of Government functions of critical importance to local and international investor confidence:
The establishment of standards and codes is critical, but they have no meaning or import without evaluations of compliance, resulting in direct rewards and penalties. In addition, current codes and standards should be enhanced and customized to fit the specific country, including evaluations in critical areas such as the functioning of legal courts, regulation of financial system, and quality of government governance.

Audits of capital market activities:
International and national regulatory authorities lack sufficient capacity today to monitor systemic developments in capital markets that create underlying systemic vulnerabilities to the system itself, as well evidenced by the recent crises (Asian crisis, Long Term Capital, etc.). A roving team of global financial market auditors would enhance the capacity of identifying in a timely manner systemic risks related to concentrations (country, industry, maturity); instrument structure (such as derivatives); and mismatches in maturity and currency.

Establish universal audits of disclosed information produced by international financial institutions and country governments, with open disclosure of audit results to public and investors:
Audited institutions would include all institutional groupings with responsibility for governance of the global financial system, such as the IMF, World Bank (including IFC and MIGA), regional development banks, etc. Information would be audited by accredited third-party experts for accuracy, timeliness, and completeness. In addition, independent evaluations should be made of the actual performance of the governmental entity against established performance targets.

Establishing a Credible Platform for Government Reporting: Country Disclosure Reports

Critical to investor confidence, domestic and foreign, are transparent legal, regulatory, and institutional frameworks, with increasing certainty, consistency, and effectiveness. In today's global financial system, many "judges" such as the global rating agencies, investment bank analysts, media, and other risk services appraise countries with open disclosed reports. With the exception of external investor relations programs, governments themselves have no established standardized venue for communicating their long-term development objectives, financing plans, institution-building strategies or risk management strategies. Just as companies use annual and quarterly reports to communicate with their shareholders, governments could use regular disclosure reports to communicate directly with their domestic and foreign investors as well as country citizens in a professional, credible, and standardized manner. Similar to company financial disclosures, these reports would be comprehensive, covering long term growth strategies as well as the full range of factors and issues affecting the well-being and sustainability of the entity and its stakeholders: economic, financial, regulatory, institutional, social, political, and management.

By taking a proactive leadership role with these Country Disclosure Reports (CDRs), country governments would systematically enhance the quality and effectiveness of their communications with investors and internal constituencies, in the process improving technical capability, transparency, accountability, and credibility. CDRs would provide a useful vehicle to operationalize ongoing global efforts to strengthen the global financial system within a specific country context, providing a transparent, cost-effective baseline useful to investors, analysts, policy makers (international, regional, national, state, municipal), and civil society.

The following issues could be routinely covered in the CDRs:

- ***Identification of country long term development strategy, ongoing implementation plans, and performance targets***, including strategies for economic growth (assessment of global competitiveness for export markets and internal market potential); development of legal, regulatory, and institutional frameworks; development of local capital markets and small and medium-sized enterprises; provision of basic services to citizens, including education, housing, health services, and infrastructure; etc.;

- ***Formulation of debt and equity financing strategy for country and accompanying risk management (including private sector and state/municipalities),*** given assessments of the local banking system; liquidity needs of the public and private sector (including small and medium-sized enterprises); the strength of regulatory, institutional, and

legal frameworks; the balance of payments profile and outlook; and availability of debt and equity capital;

- ***Compliance with the Financial Stability Forum's compendium of codes and standards****,* along with the government's priorities for completion, implementation plans, and issues;
- ***Description of government management structure***, technical support programs, and action plans to build further capacity in priority areas (including donor activities);
- ***Definition of an Investor Relations Program for both domestic and foreign investors***, providing investors (domestic and foreign) with information on business-government forums, and contacts in the governments to facilitate business development; and
- ***Periodic updates of government performance against targets,*** with timely explanations of issues and action plans (quarterly reports, press releases, etc.).

As with company financial disclosures, these Country Disclosure Reports would provide the primary consolidating mechanism for information and analysis by investors (domestic and foreign) as well as other stakeholders.

As a result of this process, investors would have better information and analyses to inform their own decision making. By providing a specific disciplined venue for direct and relevant assessments of critical country developments and government performance, Country Disclosure Reports (CDRs) would provide a systemic improvement to the analytic process by providing a routine process reinforcing the analytic and communication accountabilities of both government policy makers and investors.

Such a system of audits and Country Disclosure Reports could be administered through the Information Clearinghouse (noted above), with support from the international financial institutions and member countries.

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ANNEX E

INVESTMENT GUIDES FOR LEAST DEVELOPED COUNTRIES (LDCS)

Submitted by the International Chamber of Commerce

We would like to call the attention of the Conference to an important project undertaken by UNCTAD and ICC on investment guides and capacity-building for selected least developed countries (LDCs). Its principal goals are to create a knowledge tool that enables LDCs to attract and maintain increased foreign direct investment (FDI) and forge a convergence of purpose between investors and LDC governments.

The objective of this project, at the most general level, is to assist development and poverty reduction in LDCs, by helping LDCs attract foreign direct investment (FDI). At a more specific level, the objective is to help bring together countries that seek new investment and companies that seek new locations.

The project promotes capacity-building in LDCs through a dialogue among local enterprises, foreign investors and government. The business community's role is to mobilize domestic capital and FDI to complement each country's own efforts. "Business champions" participate in and contribute to policy dialogue and benchmarking exercises. This process, on a country-by-country basis, is driven from the ground up with all partners: the local business community, international investors and governmental representatives.

In each individual case in the pilot phase, workshops were established to focus on best investment promotion practices and policy options, and to consider the microeconomic issues relevant to FDI. The workshops analyze the implementation of international support measures in the areas of official development assistance (ODA), debt, investment and trade. Since accurate information concerning investment conditions within a country is essential, UNCTAD and ICC have produced business investment guides to fill this gap.

These guides are country specific and their objective is to raise international awareness about investment conditions. They provide a broad overview of current investment opportunities and prevailing socio-economic and political conditions; and general guidance on the legal and other issues related to undertaking investment in each individual country.

The project can easily be expanded to cover a wide range of LDCs at relatively low cost provided that governments are willing to provide the necessary funding.

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ANNEX F

CORPORATE RESTRUCTURING FUNDS TO ACCELERATE PRIVATE SECTOR FINANCE FOR SMALL AND MEDIUM-SIZED ENTERPRISES

Submitted by Business Council of the United Nations and State Street

BACKGROUND

Well developed economies enjoy the benefits of deep capital markets. Most notable among these benefits is the ready availability of low cost equity financing for private enterprises across the spectrum from small and medium sized enterprises (SME's) financed through venture capital and private equity to larger enterprises financed through public listed securities markets. This equity financing is typically lower in cost and more market driven in availability than bank financing through debt.

Some of the crises affecting developing economies in recent years can be traced in part to the over abundance of cheap debt, particularly to large enterprises. This debt contained hidden costs (currency mismatch) and was often extended without the rigors of market discipline. The result was asset growth without profit growth and a debt burden that could not be serviced once currency relationships normalized.

At the same time, smaller companies suffered generally from a lack of both debt and equity financing - this, despite the fact that most economies rely heavily on smaller companies to create jobs and drive commercial innovation.

In response to the Asian economic crisis of the late '90's a number of programs were undertaken to help speed recovery. One of these initiatives, the Korean Corporate Restructuring Funds (CRFs) can serve as a model for improving private sector equity investing in SME's. This paper describes the salient characteristics of that program, its applicability in other economies, and outlines a proposal that highlights the potential beneficial role multi-lateral and regional development banks might play in accelerating SME equity financing in developing economies.

THE KOREAN EXAMPLE

In the wake of the financial crisis in Korea in 1997-1998, the government instituted a number of measures to effect financial and corporate restructuring in order to establish the base for a more stable and globally competitive economy. Of particular note is the innovative program of Corporate Restructuring Funds (CRF's) designed to

provide equity and longer-term debt restructuring for SME's. This program, funded with approximately US$2 billion from domestic institutions under the coordination of the Korean Development Bank, had the following key objectives:

- To provide finance for SME's to improve their balance sheet structure and reduce dependence on short term debt;
- To provide growth capital for SME's, particularly those with export potential and technological competitiveness;
- To establish an investment process which would meet international best practice standards and, ultimately, attract future private capital investors; and
- To facilitate the transfer of investment skills from international practitioners to domestic investment professionals.

The program achieved these objectives by following these important steps:

- Selecting international fund managers based on an open and competitive selection process;
- Establishing clear investment guidelines for each fund and delegating complete investment decision making to the professional investment manager;
- Requiring each investment manager to "partner" with a domestic investment organization; and
- Providing clear regular reporting of fund investments and an incentive fee structure for the managers.

The results of this program have been positive. A large number of investments have been made in SME's based solely on the investment merits of the investee companies. Many of these companies have subsequently been able to list on an exchange and gain access to the public equity markets for future financing. The investment returns for the funds have been positive and significant improvements in corporate governance have been achieved. The local investment teams have significantly enhanced their investment knowledge and foreign, private sector investors have begun to fund "follow-on" investment programs.

While this CRF program serves as an excellent model for using development capital to spur private sector financing for SME's, Korea has several advantages that are

difficult to find in other developing economies. First, Korea had both the financial means and the political will to provide a significant level of funding for this program. Second, Korea has a relatively well developed capital market structure which makes exits onto listed exchanges (IPO's) a viable medium term exit for private equity investors. It is the lack of these two features, availability of funding resource and medium term exit into public securities markets, which limits the application of this model to other countries seeking to stimulate equity financing of SME's and encourage private sector investors. Multi-lateral development groups and regional development banks have the opportunity to help bridge these gaps.

A PROPOSED ROLE FOR DEVELOPMENT BANKS

The challenge of replicating the Korean CRF model is encumbered by two difficult problems. First, for a program to have economic impact it must be undertaken on a meaningful scale. This would generally mean funding such programs with at least several hundred million US dollar equivalents. Most developing countries lack the means and political will to allocate such a level of resource and to delegate the investment of the fund to "foreign" professional investment managers. Here the role of the multi-lateral development banks is clear as a source of funds to provide sufficient investment capital to have impact. While some development banks have made efforts to work with professional investment managers in targeted equity programs, these efforts have been small and scattered. This could be overcome with a substantial and concerted effort to more materially address equity investment in SME's. Thus, the issue is primarily a problem of scale.

However, the second problem, the lack of a well-developed public securities market into which the SME fund equity investment can "exit", is a trickier and more structural problem. In general, the private placement nature of the CRF program cannot take place in advance of the development of a reasonable IPO market. At a minimum, the program must anticipate the development of such an environment with a few years of undertaking investment. Most countries, however, have underdeveloped public securities markets particularly for smaller companies. There is also something of a "chicken and egg" problem. The development of a good IPO market relies on the availability of good new companies seeking listing. The supply of good growing companies depends on the availability of equity financing which, in turn, is often dependent on the existence of a good IPO market for exit. While market forces can eventually resolve this problem it is a process which can take decades. In the meantime, good growing SME's will lack equity financing resource.

Here, then, is another potential role for multi-lateral development groups. Such institutions could bridge the "equity liquidity" gap by building portfolios of exited investments and holding them until IPO markets develop. Or, such institutions could repackage them into diversified trusts whose units could be purchased by both foreign and domestic investors. While such approaches have not been undertaken before, there are some instructive parallels. For example, when the government of Hong

Kong engaged in market intervention of the Hong Kong equity market to stabilize price levels, it ended up with a large portfolio of highly diversified equity holdings. Disposing of these holdings was problematic. It hit upon the innovative scheme of packaging these holdings into an index fund and selling units to the public with an incentive program for longer term holders. If the equity liquidity gap could be foreshortened, equity investment in SME's could be accelerated by years, if not more. This should result in stronger and more balanced growth of this vital but generally neglected sector of developing economies.

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ANNEX G

INCUBATING VENTURE CAPITAL FUNDS IN DEVELOPING COUNTRIES

Submitted by Money Matters Institute and Potomac Associates

The international development community should designate a significant component of its aid program to risk-ventures and work with local public entities, using similar programs as the SBA in the US, in the emerging economies to implement such programs. Such funds can be engineered to attract some limited foreign funds over time. To do so, an international fund can be set up and allocated on a regional basis among four or five regions, e.g., Latin America, South Asia, the Middle East, and Africa.

The Fund can enter a "master agreement" with one or more US private managers with proven skills. Each regional grouping can focus on a number of countries whose governments must be willing to support the activities of the Fund through allocation of supplementary local funds as well as regulatory and other facilities. The Fund will work with local entrepreneurs who may also become partners.

The success of such a program will depend in large part on the availability of long term capital that is not only made available at the inception of the business, but also later to support expansion and/or deal with problems. This workout option is critical to startup businesses, the majority of which fail because of lack of follow up capital and managerial skills that venture capitalists often help provide.

To be successful, the international community should benefit from the experience of VC and other capitalists by attracting such managers to help install managerial skills into such companies.

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This proposal is made possible through a grant from the Better World Fund of the United Nations Foundation.

ANNEX H

DEVELOPMENT OF COUNTRY-BASED MICRO-CREDIT AND CONNECTIVITY PROGRAMS

Submitted by Money Matters Institute and Iqbal Quadir

The proposal is to develop country programs around both micro-finance and telephone access, thereby enabling rural populations in developing countries to develop critical linkages to markets and finance. The project is based on the successful experiences of Grameen Bank and Grameen Phone in Bangladesh, two institutions which have empowered rural populations through micro-credit and telephone access, respectively.

The first proposed target country would be Afghanistan, with the establishment of Afghan Credit and Connectivity ("Afghan C & C") as a long-term project dedicated to meeting two fundamental development needs of Afghan citizens who are substantially impoverished during two decades of war and misrule. While in Bangladesh the connectivity program was piggybacked on an already existing micro-credit program, Afghan C&C envisions launching both programs at the same time with each supporting the other. Credit will enable citizens to start small enterprises, including retailing telephone services. Telephone services, on the other hand, would help administer a credit program in a country such as Afghanistan where clusters of villages are separated by great distances.

Afghan C& C will be put together primarily through a partnership between a micro-credit institution and an experienced telephone company. A detailed feasibility study and other initial groundwork can be started with $US 2 million and the company can be launched with $US 200 million, with half the funds dedicated to credit and the other half for a telephone network.

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ANNEX I

PROMOTING EQUITY IN DEVELOPING COUNTRIES

Submitted by Business Council for the United Nations and David Hale

Efforts to strengthen development should focus on the role of equity markets in promoting capital formation and economic growth in developing countries. During the1990s the number of developing country equity markets expanded dramatically in Eastern Europe, Central Asia, Africa, and other regions. The markets developed in response to several factors. They included the end of communism and the privatization of state owned companies, the introduction of tax allowances to promote equity IPOs, and the rise of institutional savings flows targeted on non-bank financial assets through the establishment of pension funds.

As a result of these factors the developing countries now have an aggregate stock market capitalization of over 2 trillion dollars compared to only a few hundred billion dollars during the early 1980s. We should focus on a variety of proposals for promoting further growth of equity markets in developing countries. They would include:

- Tax allowances for equity IPOs
- Further expansion of retirement savings programs focused on non-bank financial assets
- Creation of more securities with dual listings such as GDRs and ADRs
- Introduction of better standards for financial disclosure and corporate governments to promote public confidence in equities
- Establishment of effective regulatory institutions to ensure that security laws are obeyed
- Establishment of an emerging market association of minority shareholders to protect the rights of non-management owners

The industrial countries now have an aggregate stock market capitalization approaching 30 trillion dollars for a population of 900 million people. Developing countries should aim to have a market capitalization of at least 10 trillion dollars by

2010/2015 through the pursuit of policies aimed at producing broader equity ownership. The Financing for Development initiative should ensure that experts from both the private and public sector work in partnership to explore policy options for achieving this objective.

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ANNEX J

ESTABLISHMENT OF WORLD DEVELOPMENT CORPORATION TO FUND REGIONALLY-BASED OPERATING COMPANIES THAT PROVIDE FUNDING, MANAGEMENT, TECHNOLOGY, AND MARKET ACCESS

Submitted by Business Council for the United Nations and John Allen

The World Development Corporation, an idea developed by Professor George Cabot Lodge from Harvard Business School, is designed as a primary funding vehicle for massive job creation (a "Salk" vaccine to eradicate global poverty) in a very pragmatic way. The way is for the WDC to be the catalyst investor in developing six New York Stock Exchange listed operating companies for the following emerging markets: Emerging Europe, Emerging Asia, North Africa and the Middle East, Sub-Saharan Africa, Emerging Latin America and Emerging North America.

Each of these NYSE companies will be used to provide money, management, technology and access to global markets for its respective area. These resources will be used to acquire and develop (often in exchange for stock in the NYSE company to create true partnerships with local participants) control positions in economic opportunities in these areas.

GE is a good corporate role model for operations, however ownership in each NYSE company will include much larger participation by local and regional investors. Local partners will provide natural and human resources, and access to local markets and capital.

Each NYSE entity is expected to become a primary developer of local management and entrepreneurial talent because of its ability to provide resources, training, and superior compensation (both cash and stock in the NYSE company). The combination of financial incentives and the ability to make a major difference to one's country or region is expected to act as a magnet for management talent, and over time WDC's "graduates" should spawn many new enterprises.

There are several important reasons why these NYSE development vehicles will work better than existing investment structures (both public and private) in creating massive and sustainable job creation. Alternative vehicles are mostly short-term, non-diversified and illiquid. They often foster rather than prevent flight capital, corruption and non-compliance with global standards of transparency and disclosure. However, the WDC—NYSE vehicles, once they achieve the necessary market

capitalization and critical mass of operations, should overcome these shortcomings in the following ways:

- ***Liquidity:*** Large-cap NYSE listed companies provide $US dollar denominated securities (debt and equity), and sufficient liquidity to attract major institutional participants.

- ***Transparency and Anti-Corruption Measures:*** These NYSE entities, because of their compliance with international GAAP accounting and SEC reporting standards, as well as through partnership with major international funding organizations, provide very effective tools to combat local corruption through full disclosure and transparency of operations.

- ***Local Buy-In to Prevent Flight Capital:*** By exchanging stock in local businesses for shares of these NYSE companies, local investors (private, management, government) immediately have global, $dollar denominated liquidity, which is the prime reason for flight capital. Then, by retaining and reinvesting local earnings instead of taking these profits out of the country, the enhanced local results can have a multiplier effect on the value of the NYSE securities that they now hold.

- ***Long-Term Development:*** These NYSE companies are diversified by geography, industry and time for realization. The latter is the most important, since realization of natural resource development and other long-term projects, such as transportation, telecommunications and financial infrastructure, can be reflected in the value of the NYSE stock (which has liquidity) as opposed to requiring a quick cash return.

- ***Partnership with Global Development Institutions:*** These NYSE companies can work effectively with development agencies (IFC, EBRD, ADB, IADB, OPIC, etc.) to deploy resources and process and manage deal flow in a mutually beneficial manner. In addition to financial leverage and management assistance, these agencies also serve as an implied insurance force to counteract local corruption.

- ***Critical Mass:*** With a critical mass of money, management, technology and access to markets, these NYSE companies can be very effective private means of starting and developing extremely profitable controlled operations in the short, medium and long-term. They will engage in trading and bartering, local manufacturing for export and for the local market, services, and long-term development of natural resources, financial and technical infrastructure.

The bottom line is that these NYSE vehicles must first meet their profit and financial objectives and then must also meet their social objectives. The definition and interdependence of these economic and social objectives is one of the primary functions of WDC's Board of Directors and Board of Advisors. Only by meeting both objectives can these NYSE companies attract the large global institutional investors and partner with the major international development institutions. As they achieve success they should become very effective instruments for constructive global change by helping to eliminate poverty and by stimulating positive economic, social and political development.

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ANNEX K

ESTABLISHMENT OF NEW VEHICLE TO PROVIDE LONG-TERM DEBT FINANCING FOR INFRASTRUCTURE IN DEVELOPING COUNTRIES

Submitted by Business Council for the United Nations and Dr Lincoln Rathnam

This proposal is aimed at fulfilling certain explicit objectives of the draft "Monterrey Consensus," specifically paragraphs 21bis[1] and 22[2]. The purpose of this proposal is to provide large-scale (multi-billion dollar), recurring investment flows to infrastructure projects undertaken by both the public and private sectors in all countries, with no bias towards the larger economies. Since this investment would be in the form of ten to twenty-five year financing, the problems of volatility of capital and the lack of long-term financing for long-lived infrastructure investments would be addressed.

Infrastructure projects, such as power plants and water works, are both capital intensive and long-lived. In order for the rates paid by consumers to be affordable, the capital cost of the projects needs to be amortized over the economic lives of the projects, typically fifteen to thirty years. Long-term finance has not been available, however, on a regular basis to emerging economies, rendering the undertaking of such projects by the private sector uneconomic in such economies.

The proposal is to solve this problem by the creation of a funding mechanism by which senior secured debt, privately-issued by both private and public sector sponsors, and of all levels of credit quality, in infrastructure projects around the world, including OECD and non-OECD countries, are pooled to form the collateral for trusts that would issue investment grade publicly-traded debt instruments in the world capital markets. The organization sponsoring such trusts would be jointly-

[1] "21bis. We will support new public/private sector financing mechanisms, both debt and equity, for developing countries and countries with economies in transition, to benefit in particular small entrepreneurs and small and medium-size enterprises and infrastructure. . ."

[2] "22. We underscore the need to sustain sufficient and stable private financial flows to developing countries and countries with economies in transition. It is important to promote measures in source and destination countries to improve transparency and the information about financial flows. Measures that mitigate the impact of excessive volatility of short-term capital flows, are important and must be considered. . . We encourage public/private initiatives that enhance the ease of access, accuracy, timeliness and coverage of information on countries and financial markets, which strengthen capacities for risk assessment. Multilateral financial institutions could provide further assistance for all these purposes."

sponsored by public and private sector parties and would be called the Infrastructure Bond and Share Company ("IBASCO"). It would be closely modeled on the Electric Bond and Share Company ("EBASCO") created by the General Electric Company (US) in 1905, which proved extremely successful in providing such financing to the electric sector both in the United States, Latin America, and Asia in the first quarter of the twentieth century. The sponsors of this proposal believe that conditions for infrastructure finance are remarkably similar to those that prevailed when EBASCO was created and that this model can prove effective today.

The sponsors of this proposal are requesting that the public sector, multilateral organizations, and private sector investors participate in the initial capitalization of IBASCO, through the purchase of founders' shares, sufficient to establish the company and financing its first trust for infrastructure investment by the end of 2002.

To function most efficiently, IBASCO needs to operate on a large scale so that a liquid public market for its securities is created; this means it needs to undertake financings of the multi-billion dollar magnitude annually. To reach such a goal in the medium term, additional support would be desirable. Such additional public sector support could include, as suggested in the Monterrey Consensus draft[3]:

- Subordinated or first loss positions by guarantors, such as OPIC, the development banks, and the private sector arms of development banks
- Co-investment by governmental and/or multilateral organizations
- Political risk insurance
- Net worth support of IBASCO

[3] "20. To complement national efforts, there is the need for the relevant international and regional institutions as well as appropriate institutions in source countries to increase their support for private foreign investment in infrastructure development and other priority areas, including projects to bridge the digital divide, in developing countries and countries with economies in transition. To this end, it is important to provide export credits, co-financing, venture capital and other lending instruments, risk guarantees, leveraging aid resources, information on investment opportunities, business development services, to facilitate business contacts and cooperation between enterprises of developed and developing countries, as well as funding for feasibility studies. Inter-enterprise partnership is a powerful means for transfer and dissemination of technology. In this regard, strengthening of the multilateral and regional financial and development institutions is desirable. Additional source country measures should also be devised to encourage and facilitate investment flows to developing countries."

DETAILS OF THE PROPOSAL

The proposal involves creation of sector-specific Ginnie Mae-like investment pools, each aimed at a specific economic sector, which pools would purchase secured, non-tradable debt and fund themselves by issuing tradable fixed income securities in the global capital markets. The idea, conceived to fund infrastructure projects – which are capital intensive as well as critical for emerging economies, and which as a rule generate high levels of free cash flow when completed – could be carried out in a wide range of industries. Other sectors where the idea could be applied include any that have collateral backing in developed markets, such as real estate, automobiles, etc.

In order to create diversified pools that would receive investment-grade ratings, the sponsors envision combining securities from both developed and developing markets – including both investment grade and below investment grade securities from the public and private sectors – which would enable even the poorest countries to have ongoing access to long-term international capital. For infrastructure financing, which is currently done on a project basis in the private placement market where there are limited resources, this new financing vehicle would provide a liquid market for securities issued by the diversified investment pools that it would create, increasing the availability of finance while reducing the cost of capital. In addition to improving developing country access to long-term funding, this process could standardize project structures and instruments, reducing costs (administrative, legal, accounting, etc.) while improving transparency. For investors, the pools formed would be liquid (an active market would be established) and income producing.

PURPOSE OF THE PROPOSAL

The proposal seeks to enlist public and private sector support for the formation of a financing structure aimed at facilitating infrastructure investment internationally, with a particular focus on providing long-term capital to projects in emerging market countries. The Infrastructure Bond and Share Company, Inc. ("IBASCO" or the "Company") will provide efficient access to debt capital for infrastructure projects in emerging market and industrialized countries by applying the "insurance principle" of diversified pools of collateral. These diversified pools would be of credit quality superior to that of individual assets in the pools due to diversification, and because IBASCO will issue collateralised securities on a large-scale basis, a liquid market will be created, further reducing the cost of capital.

HISTORICAL PRECEDENT

IBASCO is not without precedent. In 1905, General Electric formed the Electric Bond and Share Company ("EBASCO") to serve as a financing vehicle for the young, risky and fragmented U.S. electricity industry. EBASCO purchased preferred stock, bonds and other securities of numerous local electrical companies in the U.S. in exchange for cash or equipment. Portfolios of these securities were packaged and

sold as debt instruments in the New York market. The basic concept was to apply the principle of portfolio diversification to a developing, fast-growth industry. EBASCO was extraordinarily successful. It financed the establishment of over one-half of the U.S. electricity industry while providing investors with security of payment. The concept was extended by EBASCO to the emerging countries through its subsidiary, American & Foreign Power, which financed electrical companies in Mexico, Brazil, Venezuela, China and elsewhere. General Electric spun off EBASCO in 1924 due to anti-trust concerns, and EBASCO divested itself of its utility holdings as a result of the Public Utility Holding Company Act in the 1930s. The success of EBASCO's financing efforts resulted from two factors:

- The "Ginnie Mae" type diversification of the collateral pool
- The pro-active and remedial actions of EBASCO as problems emerged in the portfolios

CONCLUSION

Given the interest of the United Nations, member governments, and multilateral organizations such as the World Bank in increasing the efficiency of investment in, and access to, capital of infrastructure projects in emerging market countries, we propose to join with these and other sponsors, including the private sector, to create and finance EBASCO-like collateral pools that will facilitate the financing of infrastructure projects in emerging market countries.

Globalization and communications are now coming together to afford an opportunity for standardization and efficiency in the provision of financing for infrastructure projects in emerging countries, based on sound investment principles.

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ANNEX L

INCREASING THE NUMBER OF VIABLE WATER PROJECTS IN DEVELOPING COUNTRIES

Submitted by SUEZ (Ondeo)

SUMMARY

The number of viable water management projects in developing countries should be increased by moving the existing institutional tools in three directions, to:

- allow to more easily mix public funds and private funds
- adapt the maturity of International Financing Institutions' loans according to the specific long life of water assets; and
- build a specific insurance framework at the international level

BACKGROUND AND CONTEXT

In the Millennium declaration, the United Nations reconfirmed the goal of halving by 2015 the proportion of people who do not have adequate access to water and sanitation services. The estimates prepared for the second World Water Forum in the Hague (March 2000) show that implementing this goal would require a doubling of the annual water investment in the developing countries (the current $ 80 billion figure should be raised to $ 180 billion). The second World Water Forum concluded that private financing should be looked for since public budgets cannot cope with the enormous financing needs.

Although private finance is available for funding sound water projects in many industrialized countries on a project finance basis, very few projects are really implemented in this way in the developing world. Therefore, globally, water and sanitation services do not improve at a pace sufficient to meet the official Millennium target. This is detrimental to more than 1 billion people for water supply and more than 2 billion for sanitation services.

Many local governments would like to improve and develop their water and sanitation services. Some of them try to organize partnerships with private companies in order to take advantage of their managerial and financial capabilities.

However, many projects are stopped at a very early stage. Others have their goals reduced to very modest levels. This results from constraints that are too high for attracting private finance or from the fact that the project's structure is such that water-users cannot afford to pay the water rates.

In order to increase the number of projects in the area of water and sanitation services in the developing countries, the international community should consider and promote innovative ways of organizing projects and then take actions that benefit to more people.

Out of the many initiatives that could favor the success of new projects, we would take the opportunity of this Conference to suggest three main ones. These proposals derive from the specific characteristics of the water management area. Indeed, water differ from other types of services in many respects such as:

- ***The extreme psychological and political sensitivity to water rates****:* For historical or cultural reasons, in many cities water is charged at a rate which is inferior to the real cost of the water supply. And although all the recent international water conferences (Paris 1998, The Hague 2000, Bonn 2001) recommended to drive the rates towards the full cost, according to our experience the necessary increases cannot be implemented without simultaneous service improvements.

- ***The long life of piped water networks:*** They last several decades and therefore may be amortized over very long periods, far longer than the usual amortization periods of industrial assets.

- ***The dedication of water assets to a specific supply area:*** For economical reasons, water is usually not conveyed over long distances and the water physical assets cannot be transported to other areas. Therefore, when an external brutal and unexpected change affects the economics of a project a water regulated company has no other solution than to renegotiate the partnership contract. Even if the parties agree on the necessary adaptations of the contract, they may not be immediately enforceable.

PROPOSAL 1
MIXING PUBLIC AND PRIVATE CAPABILITIES

When a city wants to fund significant investments for developing its water networks and simultaneously decides to take advantage of the management expertise of a *reputable private operator* it usually chooses one of the 3 following schemes:

a) It contracts out the operation and management of the water system (Opex) to the operator but keeps the funding of the necessary new assets (Capex program) with public money.

b) It *privatizes* the system. This means that it sells the water assets to an investor.

c) It contracts out the management of the water system and the funding of the necessary new assets (via private finance) to the operator while keeping a public ownership of the existing assets.

However in many cases none of these schemes would deliver optimum results and it would be useful to invent more appropriate models combining the capabilities of both public and private sectors.

The price to the water-user is key for taking a decision and selecting the most appropriate scenario.

Scheme a) is used in many cities where it has brought significant improvements. However, very often, such a scheme does not deliver an optimized management and therefore does not allow the lowest price to the water users. It is an hybrid scheme which puts side by side two different bodies with two different sets of constraints without efficient common management. The public body uses public funds for implementing an investment program and the private company, which is specialized in managing existing systems in a competitive way, is not enabled to consistently optimize capital and operation expenditures. If a full-cost pricing policy is not immediately affordable by the water-users, it means that the investments are funded by the city budget and it is very difficult to schedule them in a timely manner.

Scheme b) is more expensive than scheme c) since the water-users must refund over time the purchase price of the existing assets. In addition getting the public opinion support of such scheme b) is often very difficult.

Scheme c) is very efficient and has delivered impressive results in cities such as La Paz, Buenos Aires, Casablanca, etc. Usually this type of operation is not subsidized with public money and thus requires an overall full-cost pricing policy in the related territory (such a policy does not prevent the government from implementing a social policy with tariffs brackets). When for any reason such a full-cost policy is not

immediately possible, this scheme c), often named concession project, is impeded. It is the case in all cities where the current water prices are heavily subsidized and therefore are far below the full economic cost.

Proposal 1: the international community should modify the constraints which currently rule the use of International Financing Institutions-backed public money in order that such money could be used to partly fund the needs of a public-owned water system even if it is temporarily operated by a private operator.

Obviously, this would not mean subsidizing the operator but subsidizing a project in order to make it economically viable. The public money would either fund publicly-owned new assets (to expand the water network, or to jump-start sanitation programs), could be targeted at improving service in low-income neighborhoods, or could partly subsidize the water rates in order to keep them affordable to low-income people.

The rapid improvement achieved in the quality of service thanks to the combination of public and private finance would start a vertuous circle and eventually make full cost pricing politically acceptable.

PROPOSAL 2: DEVELOP LONG-TERM LOANS ADAPTED TO LONG-TERM CONTRACTS

One of the peculiarities of the water assets is that water networks are made of pipes which last several decades. To keep prices affordable the economical owner of the network, whatever public or private, amortizes them over long periods.

Unfortunately in many developing countries the maturity of the loans which can be obtained from financing institutions is far shorter. This adds unnecessarily to the burden of funding the initial period of a project.

Proposal 2 : the International Financing Institutions should consider the specificity of water assets and offer very long loans to water operators. In case of private operators, the length of these loans should be in accordance with the duration of their contracts.

PROPOSAL 3:
DEVELOP NEW INSURANCE TOOLS FOR BETTER RISK ALLOCATION

When a local government wants to create a long-term public-private partnership with a private operator, it has to allocate the various risks of the project carefully.

The natural owner of the technical and managerial risks is the private operator. However, other risks such as inflation, variation in currencies exchange rates, variations in public policies are completely out of his control.

The more such external risks are transferred to the private operator, the riskier and the less viable the project becomes. Attracting private funds becomes more and more costly and more and more difficult or even impossible.

Therefore, ***in order to build sound projects and simultaneously keep the water prices as low as possible*** it is wise to delegate to the private operator all the risks that it can mitigate and to keep external risks within the public partner's scope.

Most of the current PPP contracts are built in this way and are able to survive macro economical changes. This is why lenders are able to lend their money to the project.

However, there are exceptional situations when both partners may be unable to implement the contract provisions in a timely manner. Although the probability of such situations occurring is low, their possibility may frighten potential lenders.

These exceptional situations are unforeseeable brutal changes. For example a sudden significant devaluation of the local currency versus the currency with which the project is funded. Early termination of the contract also has to be considered since the public authorities may require to adapt their water policy over time. In poor countries such exceptional situations may be very difficult to manage and therefore prevent sound projects to be built.

Proposal 3: the international community should consider building an insurance framework which temporarily helps private funded water projects when impacted by brutal unexpected changes.

The implementation of these three proposals would significantly increase the number of sustainable water management projects in developing countries.

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ANNEX M

AN INDEPENDENT EXPERT ADVISORY GROUP TO ENHANCE ACCESS TO DEBT MARKETS

Submitted by Business Council of the United Nations and Dan Bond, AMBAC

"Political risk" is a major impediment for borrowers residing in developing countries that want to access international capital markets. Until recently banks provided the bulk of international financing for developing countries. However, the longer-term/larger-volume/lower-cost financing normally provided by capital markets in North America and Europe is rapidly spreading throughout the world. This process should continue as long as the problems of economic instability, interfering governments, inadequate legal frameworks, etc. are slowly being overcome in the developing countries.

THE CHALLENGE

The shift to capital market financing means that developing country borrowers must accept much greater public disclosure about their operations, obtain credit ratings, forget about "relationships" with creditors, and adhere to the rigors of timely payment of debts. Even so, under the best of circumstances, "political risk" will remain a key impediment for most developing countries for years to come.

As private sector borrowers in the developing countries come to the international capital markets they must satisfy creditor concerns about a myriad of political risks--in addition to normal credit risks. Some of the key political risks are:

- Inability to convert domestic currency into foreign currency and to transfer these funds out of the country (T&C risk)
- Major devaluations of the domestic currency that damage obligors' ability to make payments on their foreign currency debts
- Breach of contracts by government entities
- Adverse changes in the regulatory environment
- Government expropriation of assets, funds or rights

- War, domestic violence
- Embargoes

The main purchases of bonds are institutional investors (pension funds and insurance companies). These organizations are rather risk adverse and normally not prepared (or allowed by their regulators) to assume the level of risk present in most developing country transactions.

However, various forms of credit enhancement—achieved through financial structuring and/or via insurance, guarantees and contingent financing—can provide protection against political risks and enhance developing country bonds to the point where institutional investors can purchase them.

Some forms of credit enhancement are as appropriate for developing countries as there are for developed countries. (Securitization using overcollateralization is one example.) However, the political risks in developing countries are not as easily overcome. While protection from some political risks might be provided by the private sector, this is not likely to develop quickly in the volume and at the prices that would be most helpful to the developing countries.

Institutional investors have favored so-called "future-flow" transactions where future dollar-denominated export or financial receivables from the largest corporations or banks are sold to a special purpose vehicle and payments are captured in off-shore accounts. Such structures can reduce T&C, devaluation, corporate bankruptcy and government interference risks.

There is considerable potential for the continued growth of such "future flow" transactions. A recent World Bank study suggested a six-fold increase in the current $10 billion of financing is possible.

With the recent appearance of third party insurance for transfer and convertibility risks, liquidity facilities to protect against major devaluations, and partial credit guarantees to reduce other country risks, institutional investors are now looking at structures other than future-flow transactions. With such enhancements, we are seeing increased financing for projects and utilities, as well as asset-backed transactions (using leases or mortgages as security).

T&C insurance has been available for bank loans for many years—as has insurance for some of the other political risks listed above. The innovation necessary to make T&C insurance work for bonds was a clearly defined claims resolution process with a finite timeline that insures timely payment on the bonds.

Starting about two years the U.S. Overseas Private Investment Corporation (OPIC) and a few private sector insurance companies began offering protection against T&C risk for capital market transactions. This product is now well accepted and a significant volume of developing country bond issues has utilized this insurance. Within the last year devaluation liquidity facilities have also appeared in the market. The most recent development in this area has been the appearance of insurance against "government non-honoring of obligations" by a private sector insurance company. However, insurance policies for most regulatory risks, expropriation, war risks or embargoes have still not been developed for capital market transactions.

Today the nascent market for private T&C protection is being tested by events in Argentina. It is a highly risky undertaking for private insurers to offer protection against most political risks, since claims are likely to be very large and "lumpy", driven by events such as the collapse of the Argentine Convertibility Law. It takes time for an insurer to build a sufficiently diversified portfolio to absorb the impact of such claims.

The official agencies are in a better position to provide investors with protection against political and country risks. Some public sector programs are already addressing this need. A/B-bond programs (provided by the IFC and IADB) and partial risk and credit guarantees (provided by the IBRD and other multilaterals) have already been successfully used for to enhance the creditworthiness of developing country bonds--and thus increase the level of private sector financing. With their strong financial backing and protection from bankruptcy, official agencies can better assume the risks involved as they build a diversified portfolio. And as advisors to developing country governments, they have some ability to prevent events that might cause claims on their policies.

On the other hand, official agencies need not assume all the risks. Private sector lenders and insurers should be willing to provide protection against most corporate credit and market risks. The private sector also has special expertise in financial structuring and the accompanying legal and contract risks. In fact they are more likely than the public sector to have the skills to properly evaluate and price these risks.

To be most effective, official and private sectors need to work together to create the best package of credit enhancement for the international investors at the lowest cost to developing country issuers.

Unfortunately understanding and coordination is often hampered by the normal competitiveness among private sector parties and by the differences between public and private sector objectives, operating procedures and skill sets.

THE PROPOSAL

Multilateral organizations could help to overcome these impediments to better coordination. Given that they recognize their responsibility to assist developing countries access private finance for development, they can justify making a significant expenditure toward this end. In addition, they can use their potential participation in transactions as a catalyst to overcome private sector inhibitions about sharing information.

The first step might be the formation of an on-going forum for discussions among the following organizations:

- Developing country borrowers (such as banks and finance companies, corporations, utility companies)
- Official multilateral financial organizations (IBRD, IFC, MIGA, IADB, EBRD, ADB, CAF, etc.)
- Official bilateral financial organizations (export credit and insurance agencies such as U.S. Eximbank, U.S. OPIC, Japan Eximbank, Coface, ECGD, EDC, Hermes, SACE, EKN, etc.)
- Investment banks (Merrill Lynch, Lehman Brothers, JP Morgan Chase, Salomon Smith Barney, CSFB, Deutsche Bank, Bank of America Securities, Goldman Sachs, Morgan Stanley, UBS Warburg, Barclays Capital, ABN Amro, and others)
- Financial advisory services specializing in developing country structured financing (such as Kleiman International Consultants, Samuels Associates, Protego Investment Banking Financial Advisors, Malecka Capital Formations, Societas, etc.)
- Credit rating agencies (Moody's, Standard & Poor's, Fitch)
- Private insurance companies offering partial credit or risk insurance or contingent liquidity facilities (AIG's Risk Finance Group, ACE Ltd., Centre Group, Zurich Emerging Market Solutions, Sovereign Risk Insurance Ltd., Swiss Re New Markets and others)
- Monoline bond insurance companies (Ambac, MBIA, XL Capital Assurance)
- Institutional investors (insurance companies, pension funds, mutual funds, etc.)

Some of the issues that need to be discussed:

- How specific political risks can best be mitigated and by whom (public or private sector)
- Procedures to ensure timely processing of transactions when public and private sector entities are working together. (In my view, one of the major problem with current official credit enhancement organizations is their extremely slow speed of execution. Private sector participants often give up trying to utilize their programs because of the costs of the delays involved.)
- Ways to coordinate pricing when several insurance policies or contingent financing facilities are offered together in a transaction
- Standardization of coverages and contracts
- Roles for public and private sector participants in post issuance surveillance of transactions
- How public and private sector parties might work together in remediation efforts to prevent adverse political events
- Rights in recovery by public and private sector creditors and insurers following a default.

It would be desirable for the discussions to be on going, with the proceedings recorded and widely disseminated. A clearinghouse of documents and data (preferably accessible via the internet) should also be established. The activities could be undertaken by an Independent Export Advisory Group established as part of the proposed Information Clearinghouse, with the support of the United Nations and collaboration from experts in the international and regional development institutions.

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COMMENT PAPER FROM STANDARD & POOR'S:

USING PROJECT FINANCE TO FACILITATE PRIVATE SECTOR INVESTMENT IN EMERGING MARKET INFRASTRUCTURE AND EXPORT PROJECTS

Submitted by Peter N. Rigby

SUMMARY

Standard & Poor's, a division of the McGraw-Hill Companies, has observed how project finance techniques have mobilized billions of dollars of private sector funds to build economically sustainable infrastructure and export projects in the emerging markets. Many projects have not only mitigated the risks imposed by host country business and legal institutional problems, but have survived financial and political crises when equity capital has retreated to safe havens. Opportunities exist for multilateral agencies and governments to provide more innovative credit enhancement programs that build upon the current offerings of inconvertibility, expropriation, and war risk, which would increase these agencies' and governments' effectiveness and eligibility for private sector investments, including capital markets transactions.

PROBLEM

The gulf between the developed, industrialized countries and the developing countries continues to grow, despite the past decade's growth in private sector investment in developing countries. Nonetheless, regional and global financial shocks during the past decade, combined with the challenges of corruption, lack of defined property rights, ineffective regulatory and policy frameworks, nascent rule of law, among other troubles, have maintained immense barriers to private sector capital flows into emerging markets. Few will argue that private sector finance is a desirable public policy objective to help alleviate poor economic, social, and political conditions in emerging markets. Nonetheless, the perception of serious risk will continue to discourage private sector capital flows into the developing countries unless effective means of risk mitigation can be brought to bear on investment.

OBJECTIVE OF THE BUSINESS COUNCIL FOR THE UNITED NATIONS

In response to a resolution by the UN General Assembly calling for private sector input and participation in the Monterrey conference in March 2002, the Business Council for the United Nations and the United Nations Association of the United States of America are developing a proposal to mobilize private sector capital and resources and to facilitate international financial cooperation and global trade.

STATEMENT ON PROJECT FINANCE AS A MEANS OF MOBILIZING PRIVATE SECTOR CAPITAL

Since Standard & Poor's began rating capital markets debt for project finance transactions in 1991, we have observed that project finance has been an effective tool for raising and deploying capital in developing countries. Projects in the Philippines, Pakistan, India, Venezuela, as well as parts of Africa and the Middle East, have withstood financial shocks caused by financial and currency crises when many investors and their equity fled these distressed countries. Many corporations failed, yet single-asset, single lines of businesses, which were financed by project finance, continued as ongoing, sustainable businesses.

Project finance, which is a highly structured form of asset-based financing, identifies and allocates risks to those best able and willing to absorb the risks. Lenders to these highly leveraged transactions agree only to look to the entity's cash flow potential as a source of repayment. Project sponsors, in turn, agree to bind themselves to many covenants that, among other restrictions, limit the scope of business, prevent the incurrence of additional debt beyond the initial investment, preserve the project's liquidity and credit profile, and generally limit management discretion concerning the operation of the project. In addition, well-structured project-financed transactions provide incentives for all parties, including the host country government, to honor their obligations, explicit or implicit, to the project.

Successful projects have raised debt from capital markets and commercial banks. Equity has come from direct sponsor equity, private institutional equity funds, and pooled equity, among other sources. Projects in politically risky countries have used political risk insurance and currency convertibility insurance to protect equity and debt investments.

Standard & Poor's has found that project-financed transactions can help achieve many goals consistent with development financing, including:

- Technology transfer to the host country;
- The mobilization of domestic labor, resources, and capital;
- The funding of sustainable projects that do not need additional debt;
- Surveillance and monitoring of project construction and operations by independent, third parties, such as Standard & Poor's, to help ensure that the interests of lenders, equity sponsors, insurers, and the host country remain aligned;
- The provision of essential services, such as electricity, water, transport, and communications infrastructure;

- The creation of hard-currency-earning export projects in the oil and gas, petrochemical, and mining industries;

- Amortizing debt structures that reduce host country debt burdens over time and eliminate refinancing risk;

- The elimination of the need for venture capital returns often required to attract private investment, but which can either make a project uneconomic or create incentives for government interference;

- The elimination of the host country government guarantees;

- The lessening of corporate governance and transparency problems that can dissuade private investment; and

- The prevention of capital flight during a financial or political crisis.

Standard & Poor's has also observed that project-financed transactions in emerging markets have distinguished themselves from other development efforts in one key area. Project finance can proceed within the current constraints and challenges of the host countries. Little effort is spent requiring countries to improve legal systems, transparency, corruption, cronyism, and other woes when the prospects for such near-term change will not likely come until economic conditions truly improve. Instead, most projects attempt to set examples of good practices and try not to add to the problem.

OPPORTUNITIES FOR GOVERNMENT AND MULTILATERAL PARTICIPATION IN PROJECT FINANCE

Many projects that sought a Standard & Poor's project finance rating have failed to go forward because certain credit risk enhancements were unavailable or ineffective, commercially uneconomic, too time-consuming to pursue, or any combination of these impediments. As well as project finance techniques mitigate many credit risks, some structures cannot address certain host country risks, namely political risk and foreign exchange convertibility risk. To the extent that government and multilateral agencies can develop and provide credit enhancement products that can help prevent project defaults at reasonable commercial rates, project finance may be able to mobilize greater capital flows for emerging market investments. While political risk insurance has been available for many years, and has provided incentives for projects to proceed, there is an ongoing need for political risk insurers to innovate more quickly, broaden the availability and effectiveness of their products, and thus provide better risk mitigation for the many political risks that remain serious stumbling blocks to moving projects forward.

ANNEX N

SPECIAL DRAWING RIGHTS (SDRS)

Submitted by George Soros of Soros Fund Management

It is proposed to use issues of Special Drawing Rights (SDRs) to mobilize a substantial increase in international assistance. Less developed countries can add their SDRs to their monetary reserves; richer countries (as defined in the IMF "transaction plan") would donate their allocations to provide public goods on a global scale.

The proposal would be implemented in two stages. In the first stage, a special SDR 21.4 billion issue (approximately $27 billion) authorized by the IMF in 1997 currently awaiting ratification by the United States Congress would be approved by Congress with the proviso that the richer countries donate their allocations in accordance with a Plan.

SDR donations could be made only to pre-approved programs. Programs would include trust funds for the provision of public goods on a global scale as well as matching funds for public/private partnerships. In the first stage, the list of eligible programs would be confined to three or four specific priority areas such as public health, education, information (the "digital divide") and reform of judicial systems. Government sponsored poverty reduction programs would be excluded; they would be left to the IFIs.

The Plan calls for the creation of an Advisory Board of eminent persons operating under the aegis of the IMF but independent of it. The Board would be appointed on the basis of publicly stated professional qualifications and would not be subject to instructions from the governments that appointed them. The Board would establish a list of programs eligible for SDR donations and it would also recommend priorities but it would have no authority over the spending of funds. The donors would retain the right to select from the menu prepared by the Board. In this way, there would be a market-like interaction between donors and programs, supply and demand. The Board would vouch for the quality of programs and donors would be responsive to public opinion in the quality of their selections.

There would be a separate Audit Commission to supervise and evaluate the programs.

If the Plan is successfully implemented in connection with the special issue of SDRs, the second step of the proposal is to have annual issues of SDRs along the same lines.

The range of eligible programs would be expanded. Government sponsored poverty reduction programs could also qualify but only up to a certain limit in order to leave funds for non-governmental channels.

The proposal would:

- Increase the amount available for international assistance;

- Ensure a more equitable distribution of the burden;

- Remove some of the deficiencies of international assistance as currently administered:
    - an independent board would ensure that the needs of the recipients take precedence over the interests of the donors;
    - the stranglehold of intergovernmental dealings would be broken; recipient governments could no longer act as gatekeepers;
    - donor coordination would be enhanced;
    - recipients would have a greater sense of ownership and involvement;
    - there would be a feedback mechanism that reinforce successes and eliminate failures.

SDRs bring tangible benefits to less developed countries quite independently of the donation plan, but the donation plan would significantly enhance the merits of SDRs as a monetary instrument.

- International trade is growing roughly double the rate of global GDP. Countries need to maintain a prudent ratio between currency reserves and imports. Less developed countries have to set aside part of their export earnings as reserves. SDR allocations would ease that burden. Alternatively, SDR allocations would reduce their cost of borrowing. Richer countries have no need for SDRs because they have ample reserves and/or easy access to international financial markets. By donating their SDRs, richer countries would have found a good use for them.

- The needs of the poorer countries have become more acute since 1997 because emerging markets have been facing a capital drain since then.

- New issues expand global liquidity and could be considered inflationary, but inflationary pressures have abated and there is a real

possibility of global deflation. Since nominal interest rates cannot be lowered below zero, traditional monetary tools lose part of their effectiveness in a deflationary environment (e.g.: Japan). SDRs would be useful as a counter-cyclical tool especially if the richer countries are obliged to spend their allotments through donations.

Whether SDR donations should be treated as a budget item or not is a vexing question. A case can be made for both alternatives. In principle, the allocation of SDRs is a bookkeeping item but when the SDRs are donated that is a real expenditure. That is the case for including it in the budget. But the allocation of SDRs goes to strengthen the monetary reserves – in the case of the United States, the Exchange Stabilization Fund. If an equivalent amount is then withdrawn and spent, the monetary reserves remain unaffected except for the interest obligations vis-à-vis the Fund. Central banks or in the United States case, the Treasury, do not normally seek appropriations to cover changes in their foreign exchange reserves including interest earned or lost, - that is the case for making the donations outside the budget. If SDRs are treated as a counter-cyclical tool a case can be made that the donations should pass through budgets not when SDRs are issued but when they are recalled. In the end every country would have to make its own determination.

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ANNEX O

MAKING PUBLIC-PRIVATE PARTNERSHIP WORK WITH BUSINESS MANAGEMENT AND OVERSIGHT

Submitted by Renaissance Strategy

This proposal addresses paragraphs 21 and 21bis of the Monterrey Consensus, which state, respectively:

> *"...We welcome all efforts to encourage good corporate citizenship and note the initiative taken in the United Nations to promote global partnerships."*
>
> *"We will support new public-private sector financing mechanisms..."*

The theme of public-private partnerships has emerged as a consistent focus of UN reports and conferences in recent years. Even if it were increased substantially, which we do not believe to be likely, ODA would not suffice to meet the challenge of spreading and sustaining globalization in the next decades. In addition to financial resources, meeting this challenge requires assets which government alone cannot provide without strong private sector participation. Key among these assets are technology, scientific knowledge, and fast and efficient operations.

Multinational corporations are, more than ever, interested in partnerships with UN member states and organizations. Witness the flurry of partnership activities and units or divisions that have surfaced in UN agencies recently, the success of the Global Compact, UN-business conferences, UN business advisory boards, and the Secretary-General's report on these activities (A/56/323). Multinational corporations therefore are not questioning the principle of partnership. What they are desperately seeking, however, is a cost and time effective mechanism that produces measurable results, is efficiently managed, and can report back to them on the use of their funds.

To engage the private sector in a consistent and sustainable manner, proponents of public-private partnerships must be ready to give the business community the transparency, accountability, and participation in decision-making and management that it requires—namely, a true partnership.

We propose to organize a multipartite arrangement that would give participating corporations the oversight they require, while respecting the sovereignty of governmental bodies and the mandates of the UN system. It would also associate NGOs and civil society at large.

PROPOSED STEPS:

1. Limit the organization of public-private partnerships to a few major thematic areas, so as not to lose focus and waste insufficient resources in the pursuit of too many goals. These areas could include: bridging the digital divide, the fight against Aids, the reconstruction of post-conflict zones, specific objectives of sustainable development, and SME development.

2. Create separate funds for each thematic area, each fund being additionally sub-divided into regions and/or countries as appropriate. The funds would be incorporated as tax-free NGOs or foundations to encourage philanthropic giving.

3. Tap the Global 250 corporations for grants. Commercial banks which are engaged in micro-finance activities could also be tapped for low-interest loans to supplement corporate grants.

4. To ensure the sustainability of each fund, participating corporations would make a five-year commitment before becoming engaged, therefore distributing their grant over five years.

5. Each fund is to be headed by a Board of Directors made of representatives from the donating corporations and financial services organizations. Representatives from NGOs, academia, and governmental bodies would also sit on the boards of the funds, at the global, regional, or local level. Representatives of the UN system (i.e. UN staff members) would be invited as observers.

6. On a regular basis (perhaps quarterly), governments, local authorities, or UN organizations in collaboration with governmental authorities would present proposals for projects to these funds in their respective thematic areas. NGOs or SMEs could also submit proposals for grants, provided that they had received the support of local, regional, or national bodies, as appropriate.

7. After reviewing the submissions, each board would make its own grant decisions based on the quality of the proposals, the capacity of the proposed projects to meet the objectives of the fund, multipartite support for the proposals, and financial soundness. Ideally, most of the proposed projects would ultimately become self-supporting.

8. The actual implementation of projects would be left to UN agencies, other parts of the multilateral system, and NGOs, which would be accountable to each board. The boards would monitor the implementation of projects on a regular basis, receive progress reports, and extend or withdraw their support to projects based on good management and implementation.

ADVANTAGES AND NOVELTY OF THE PROPOSAL

- This proposal would answer the requirements of the private sector regarding financial oversight, participation in decision-making, and association to project implementation and management.

- It would not imply an additional commitment of private sector resources to corporate responsibility and public-private partnerships. In fact, by providing an effective, clearly delineated, and participatory mechanism for private sector engagement, this proposal may allow large corporations to rationalize, and even trim, the amount of staff and dollars which they currently devote to CSR activities.

- A much called-for training in financial management and sound administration methods would be transferred to the recipients of grants at the local and regional level through the Boards of Directors, which would in effect "teach" business administration through the delivery of their functions.

- This proposal would also allow UN member states to experiment with a multipartite, participatory, and diverse system of administration, which would engage stakeholders, the business community, and UN bodies, and therefore be more likely to devise solutions that would be fully supported by local communities, be more sustainable, and have a better chance of becoming self-sustaining.

Because it will gather UN member states, the UN family and the Bretton Woods institutions, the private sector, and civil society, we believe that Monterrey provides an ideal opportunity to discuss this proposal further. In the context of the Business Forum, we will organize a follow-up dialogue on public-private partnerships. We stand ready to receive comments and expressions of interest from all parties as of now.

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ANNEX P

CAPITAL CONTROLS AND HOT MONEY

International Chamber of Commerce, Statement, 23 March 1999

ICC has long advocated the liberalization of international capital flows in the interests of promoting world trade, cross-border direct investment, and an allocation of global capital to its most productive uses. Much progress has been made in that direction in the past decade as a result of technological progress and policy reform at both national and international levels – developments which have spurred the advance of globalization.

It would be a grave mistake to use the current financial crisis affecting many emerging markets as an argument against the liberalization of international capital movements and in favor of controls on capital inflows. Nor does the crisis undermine the case for globalization.

It is true that, in an open and interdependent world economy, financial shocks can spread rapidly across and between different regions of the world. That does not, however, mean that globalization is the cause of the shocks. The lesson of the emerging market crisis is that, in a globalized economy, more efficient rules and supervisory mechanisms are required – at both national and international levels – to avert the conditions that give rise to sudden and contagious collapses in investor confidence.

Despite differences in the situations of the emerging economies affected by the current crisis, the underlying cause in most of them has been an excess of imprudent borrowing, lending and investment – for which the private sector accepts its share of the blame. Moreover, in several of the countries the crisis has been exacerbated – at least initially – by inappropriate policy responses on the part of governments and intergovernmental financial institutions. Globalization creates new risks as well as new wealth; and the international community has to develop new methods to manage the risks. Globalization requires strong governments that coordinate and cooperate well together.

The emerging market crisis has triggered an intense public debate about the role played by cross-border capital movements. ICC would like to contribute the following viewpoints to that debate with the aim of putting it into proper perspective.

An important distinction must be drawn between short-term financial inflows and foreign direct investment. Foreign direct investment is a long-term commitment and usually has the important additional advantage of bringing with it new technology, organizational and managerial skills, and an already established access to foreign markets. It has made a major contribution to raising world living standards over the past decade. In the current crisis, foreign direct investors have clearly indicated where their longer-term priorities lie and have helped stabilize the situation. A major conclusion must be drawn from this: it is in the clear interest of emerging markets to avoid measures that deter the expansion of foreign direct investment and that risk jeopardizing a mutually beneficial long-term partnership.

In the current financial crisis, the emerging markets most directly affected also need the restoration of inflows of shorter-term private finance for funding sound and profitable commercial ventures, and for financing trade transactions which will be an essential element in their economic recovery.

There is a world of difference between the concepts of control and regulation. The principal lesson of the emerging markets crisis is that their weak financial systems, coupled with inadequacies in national regulation of financial institutions in both borrowing and lending countries, permitted huge amounts of short-term international capital inflows that were invested in commercially unsound projects and that sought to take advantage of rising asset prices financed by high local savings rates and fuelled by distortions in local financial markets. The 'first best' response to the crisis is to improve regulatory and supervisory rules and procedures within national financial systems – particularly, but by no means only, in emerging market economies.

At the macro-economic level, the International Monetary Fund, World Bank, and other intergovernmental financial institutions have a key role to play in this process through the provision of technical assistance, the compilation of more focussed and relevant data, and a more cooperative sharing of information with national regulators and private lenders. Greater transparency and more comprehensive reporting are essential for better risk assessment and more effective supervision. To these ends, ICC welcomes the recent initiative of the G7 countries in establishing a Financial Stability Forum to include finance ministries, central banks and financial regulators, together with the IMF, World Bank and Bank for International Settlements. We urge the G7 to encourage emerging market countries to become active in this Forum at an early stage.

Reforms are also needed at the micro-economic level by financial institutions -such as improvements in risk assessment, the implementation of prudent capital adequacy ratios, adherence to more internationally acceptable accounting standards, and the adoption of rules for good corporate governance.

While it should be a vital priority of emerging markets to strengthen their financial systems and establish sound regulation of their domestic financial institutions as a precondition for benefiting from global capital flows, this clearly cannot be achieved overnight. It thus has to be recognized that, in countries with weak financial systems, carefully designed, flexible and temporary measures to discourage excessive inflows of so-called 'hot money' – that is, short-term bank credit and portfolio investment – may be a useful if very 'second-best' response. However, measures to discourage 'hot-money' inflows are of potential benefit only when foreigners are willing to lend. At a time when private international credit to emerging markets has all but dried up, such measures run the risk of reinforcing negative perceptions in the eyes of foreign investors.

ANNEX Q

THE "TOBIN TAX" – A BUSINESS VIEWPOINT

International Chamber of Commerce, Statement, 14 December 2001

INTRODUCTION

Since originally raised in 1974 by Professor James Tobin, Nobel Memorial Prize winner in economics, the question of taxing international transactions in different currencies has over the years been proposed in various versions and for a number of different reasons. While ICC considers that greater stability of financial markets is desirable, it also believes that a "Tobin tax" would be harmful to international trade, economic growth and welfare, and businesses throughout the world. The smallest nations would be most hurt. The tax would not prove feasible in practice since it would require uniform implementation throughout the world, and would need to encompass not only spot transactions but also substitutes and supplements such as currency swaps, forwards and futures in order to limit evasion.

TOBIN'S ORIGINAL IDEA

Tobin's original idea was to introduce an internationally uniform tax on all spot conversions of one currency into another, proportional to the size of the transaction. The impact of such a tax would obviously punish short-term trading more seriously than longer-term trading. A major concern was to make currency exchange rates reflect to a larger degree long-run fundamentals relative to short-range expectations and risks, and thus reduce volatility. A second objective was to preserve and promote the autonomy of national macroeconomic and monetary policies. To raise revenues for international purposes was never a main motivation of Professor Tobin, but is a major purpose of many of the present supporters of such a tax.

TRANSACTIONS ARE NECESSARY TO COVER CURRENCY RISKS

An estimated 1,500 billion US dollars are traded each day on the world's foreign exchange markets. Most transactions are for less than one week – most within a day – and the interbank share is approximately 70-80 per cent of the total. To a large extent, the high volume of the transactions reflects genuine needs to cover currency risks and spread the risks among different participants in the exchange market, in much the same ways that insurance risks are distributed on the international reinsurance market. Certainly, a single trade transaction may easily result in ten currency transactions because the currency risk is passed around among currency dealers like a hot potato.

In most countries there are strict regulations regarding how much uncovered currency exposure banks may accept.

HARMFUL EFFECTS

A consequence of a Tobin tax would be to reduce short-term trading. But there would be no guarantee that exchange rate volatility would diminish because liquidity would also diminish. Indeed, minor currencies might become more volatile and vulnerable to manipulative speculative attacks. Reduced liquidity would also make stabilizing long-term arbitrage more risky. Thus, customers' transaction costs would increase more than the tax levied. As with stock and security markets, some degree of short term trading – or speculation – is desirable on most currency markets to increase liquidity.

Transactions between minor currencies would be particularly hurt because there are no cross rates between many of them. Hence, it is necessary to use a major currency – for instance the US dollar (which is part of 80 to 90 per cent of all currency transactions) – as an intermediary currency. This implies two transactions or more (if an additional intermediary currency is required). Consequently, the tax might be doubled or tripled for conversions between many minor currencies. Because of the costs involved, pension funds and other portfolio managers would increase their home bias. Less capital would be available for international capital markets in general, and for investments in minor currencies in particular.

At a reasonable rate, say 0.05 per cent, the increased domestic autonomy the tax would provide in setting interest rates would be negligible. And to the extent it did work, there might be a loss of discipline on economic policy stemming from abroad.

A Tobin tax would not prevent speculative attacks on a currency where the expected gain might be high -- not unusually 10 per cent or more over a week. Furthermore, a tax could neither rectify nor repair unsustainable economic policy, which more often than not is the main reason why a currency comes under attack.

AN IMPRACTICABLE TAX

A Tobin tax would prove impracticable since it would require worldwide coverage, or at least coverage encompassing the G 10 countries, supplemented by a penalty on transactions to tax havens. Unilateral implementation would move currency trading offshore. Not only spot transactions, but also derivatives like currency swaps, forwards and futures would need to be taxed, since they are substitutes for and supplements to spot transactions.

ICC notes that Professor Tobin today is no longer a proponent of the tax that bears his name -- inter alia, because the currency regime is now very different from the time

when he originally proposed the tax and because he supports free trade as an instrument for raising welfare throughout the world.

CONCLUSION

In conclusion, ICC is firmly of the view that it would not be feasible to implement a Tobin tax. And even if it were feasible, such a tax would neither significantly prevent speculative attacks on currencies nor increase national economic autonomy. The tax would throw sand in the wheels of international trade and investment and would harm the prospects for raising global economic growth and the welfare of all peoples.

" UNLESS WE SUCCEED IN MOBILIZING FAR GREATER AMOUNTS OF RESOURCES – BOTH PUBLIC AND MARKET-LED INVESTMENT – OUR PLANS TO ERADICATE POVERTY AND TO ACCELERATE DEVELOPMENT WILL BE THWARTED"

-- KOFI ANNAN, UN SECRETARY GENERAL, MAY 2001

SAMUELS ASSOCIATES

Renaissance Strategy, Inc.

UNITED NATIONS ASSOCIATION
of the United States of America
AND THE BUSINESS COUNCIL FOR THE UNITED NATIONS

International Chamber of Commerce

The world business organization