SigmaBleyzer

The Role of Private Capital in Accelerating Foreign Direct Investment Flows to Developing Countries

Michael Bleyzer

Where Opportunities Emerge

The New World Order

- Today, conflicts rarely stay within national boundaries
- Today, a tremor in one financial market is repeated in the markets of the world
- Today, confidence is global; it's presence or its absence
- Today, the threat is chaos, because for people with work to do and family life to balance and mortgages to pay and careers to further and pensions to provide, the yearning is for order and stability. And if it doesn't exist elsewhere, it's unlikely to exist here

I have long believed that this interdependence defines the new world we live in

Tony Blair, October 2, 2001

The Brave New World

- Scientific Breakthroughs
- Technological wonders
- Open Society
- Space travel
- Genetic engineering
- Accessibility of art
- Freedom of self-expression
- Democracy triumphs
- Market economy flourishes
- Worldwide prosperity is within reach..

- Polarization
- Envy
- Misery
- Poverty
- Hunger
- Illiteracy
- Terrorism
- Radicalism
- Hatred
- Corruption

GDP Per Capita

GDP per capita (constant 1995 USD), Average for Ten Richest and Ten Poorest Countries

	1960	1970	1980	1990	2001	Change 2001 vs. 1960
Ten richest countries *	$13,951	$21,629	$27,715	$31,965	$38,671	*177%*
Ten poorest countries *	$152	$174	$180	$180	$163	*7%*
Gap, times	92	124	154	178	237	*159%*

* by GDP per capita (constant 1995 USD)

Source: World Bank, World Development Indicators, 2003

The gap between the ten richest and ten poorest countries has widened by 159% since 1960.

Infant Mortality Rate By Income Group

(per 1,000 live births)	1960	1970	1980	1990	2001	Improved By
High income	35	22	12	8	5	76%
Middle income	118	79	54	40	31	61%
Low income	148	128	110	91	81	37%
Heavily indebted poor countries	165	139	113	105	99	29%
World	119	94	78	63	56	40%

Source: World Bank, World Development Indicators, 2003

Higher income countries have significantly improved infant mortality rates, whereas lower income countries have not

Life Expectancy at Birth By Income Group

Total (years)

Income groups	1960	1970	1980	1990	2001	Improved By
High income	69	71	74	76	78	13%
Middle income	46	61	66	68	70	52%
Low income	43	48	53	57	59	37%
Heavily indebted poor countries	41	45	49	52	51	25%
World	50	59	63	65	67	33%

Source: World Bank, World Development Indicators, 2003

Lower income group life expectancies remaining below 60 years even today

Illiteracy Rates By Income Group

Adult total (% of people ages 15 and above)	**1970**	**1980**	**1990**	**2001**	**Improved By**
High income (select OECD countries*)	13.4	8.7	5.7	3.4	75%
High income (select Non-OECD countries**)	21.4	14.6	10.5	7.3	66%
Middle income	34.5	25.6	18.5	13.1	62%
Low income	64.0	55.6	47.0	38.1	41%
World	44.1	36.1	28.9	22.9	48%

* Selected OECD countries include: Italy, Korea, Rep., Portugal, Spain, Greece

** Selected non-OECD countries include: Barbados, Brunei, Cyprus, Hong Kong, China, Israel, Macao, China, Malta, Netherlands Antilles, Puerto Rico, Qatar, Slovenia, United Arab Emirates

Source: World Bank, World Development Indicators, 2003

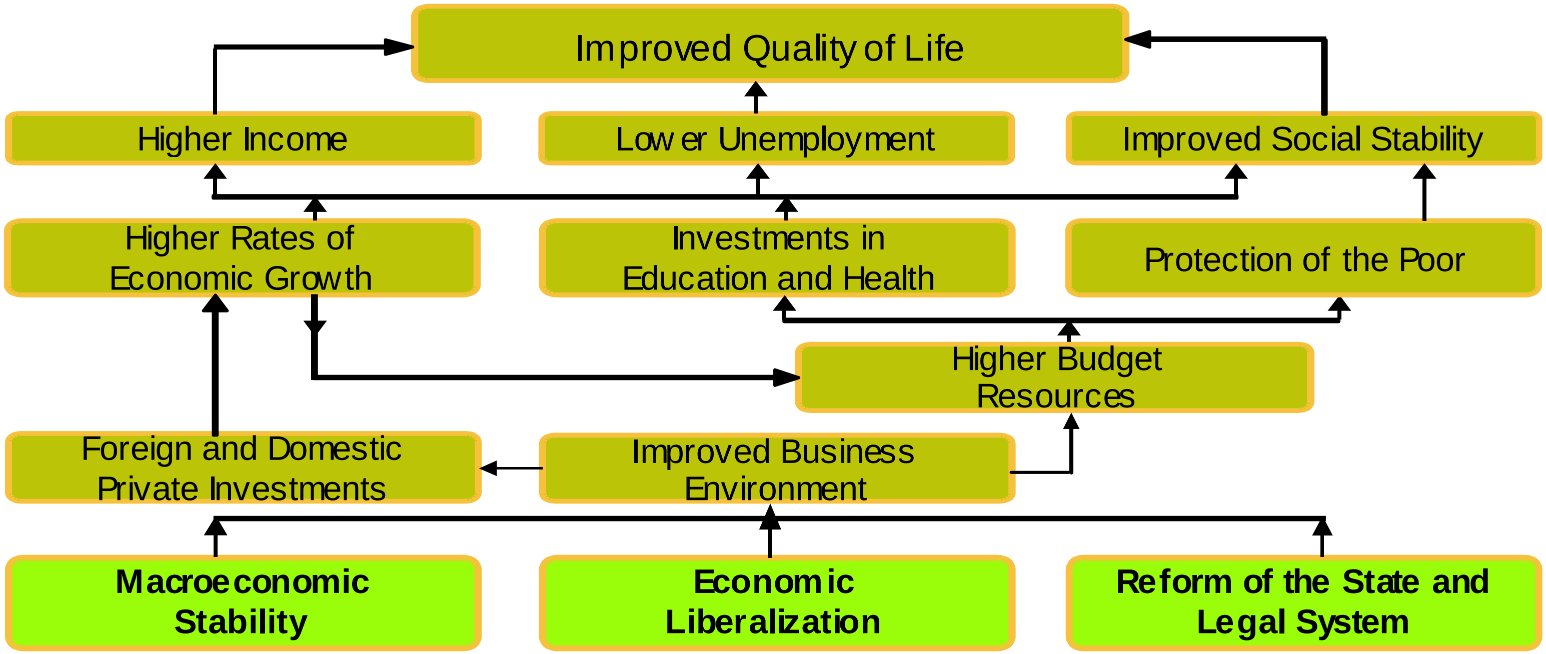
Higher income countries have had a significant improvement in literacy rates

Global Inequities Exposed

- Greater awareness due to the global revolution in communications
  - Exchange of information has improved tremendously
  - Poor are now better able to recognize their growing income disparity
  - Many groups of poor have become more dissatisfied leading to resentment, frustration and desire to change the current world order
- Developed countries cannot isolate themselves from these inequalities
  - Rise of terrorism shows that they are not immune to tensions and resentment around the world
- There is a clear need to replicate the Wealth Creation Capacity in developing nations

How to Replicate Wealth Creation Capacity

Wealth Creation Chart



- Can be accomplished through carefully targeted assistance and active engagement
- Macro-level economic development and micro-level business development

FDI is the Key that Starts the Engine of Growth

- Countries able to attract large inflows of foreign capital are able to achieve above average levels of GDP growth
- FDI is the largest and most stable source of foreign financing for developing countries
- Emerging markets have been attracting $150B per year
  - In 2001, five developing countries (China, Mexico, Brazil, Poland and Chile) received over 60% of these inflows
  - Rest of the world does not offer attractive business environments and is therefore left out of the loop

Net Capital Flows to Emerging Markets

(USD, Billions)

	84-89	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Total Private	**12**	**151**	**193**	**227**	**133**	**78**	**87**	**47**	**43**	**80**	**113**	**94**
Foreign Direct Invest	13	81	101	116	144	156	175	166	181	143	144	145
Portfolio Flows	4	113	24	83	63	11	20	-4	-51	-53	-23	-17
Comm. Bank Loans	-5	-44	67	27	75	89	-108	-115	-87	-10	-8	-35
Net Official Loans	**26**	**4**	**50**	**-2**	**42**	**58**	**8**	**-13**	**21**	**7**	**10**	**-16**

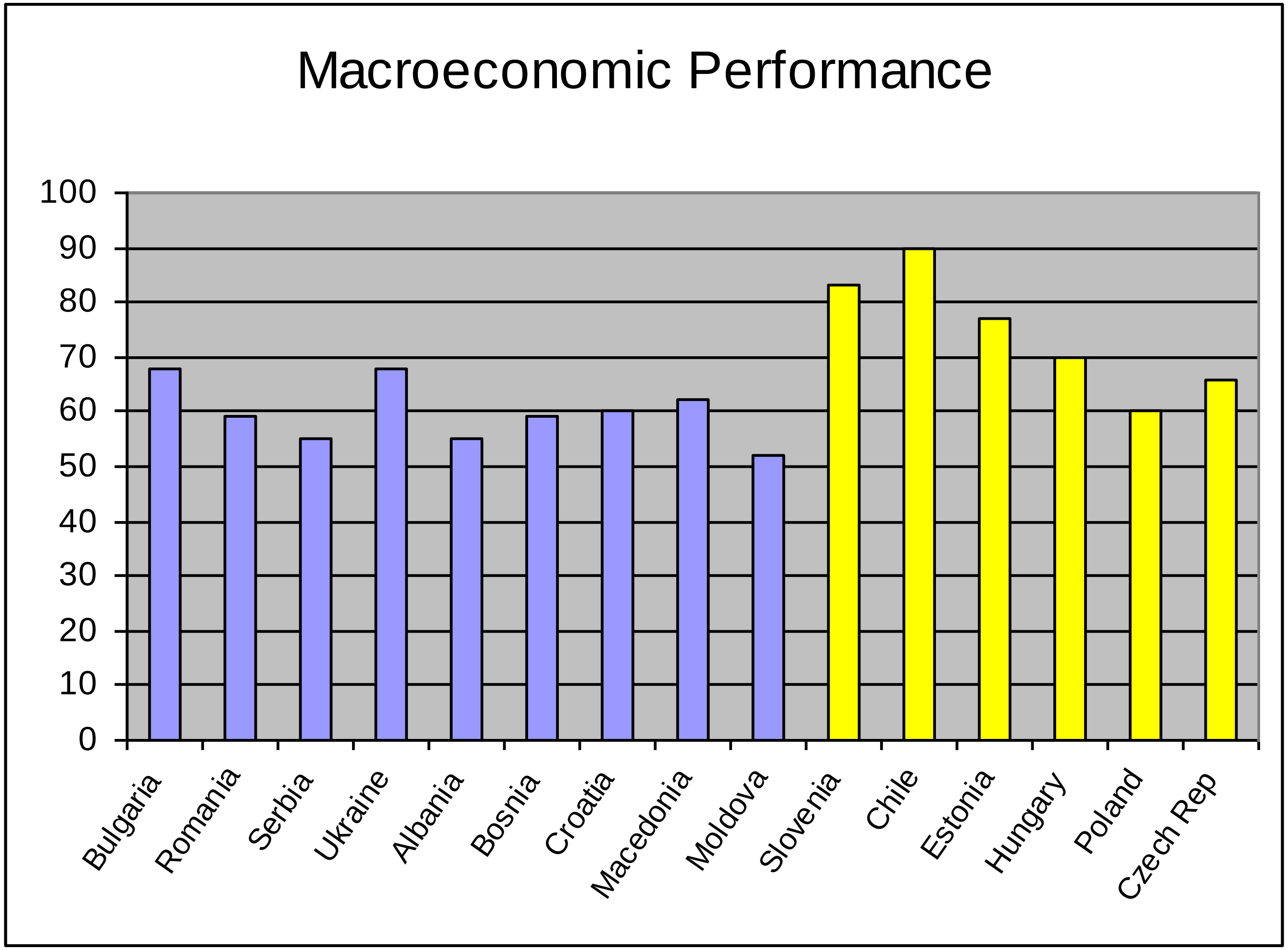
1. *Includes Developing and Transition countries, Israel, Korea, Singapore, Taiwan, and Israel*
2. *2001 prices*

SOURCE: *IMF, September 2003 (2003: projection, 2004: estimate)*

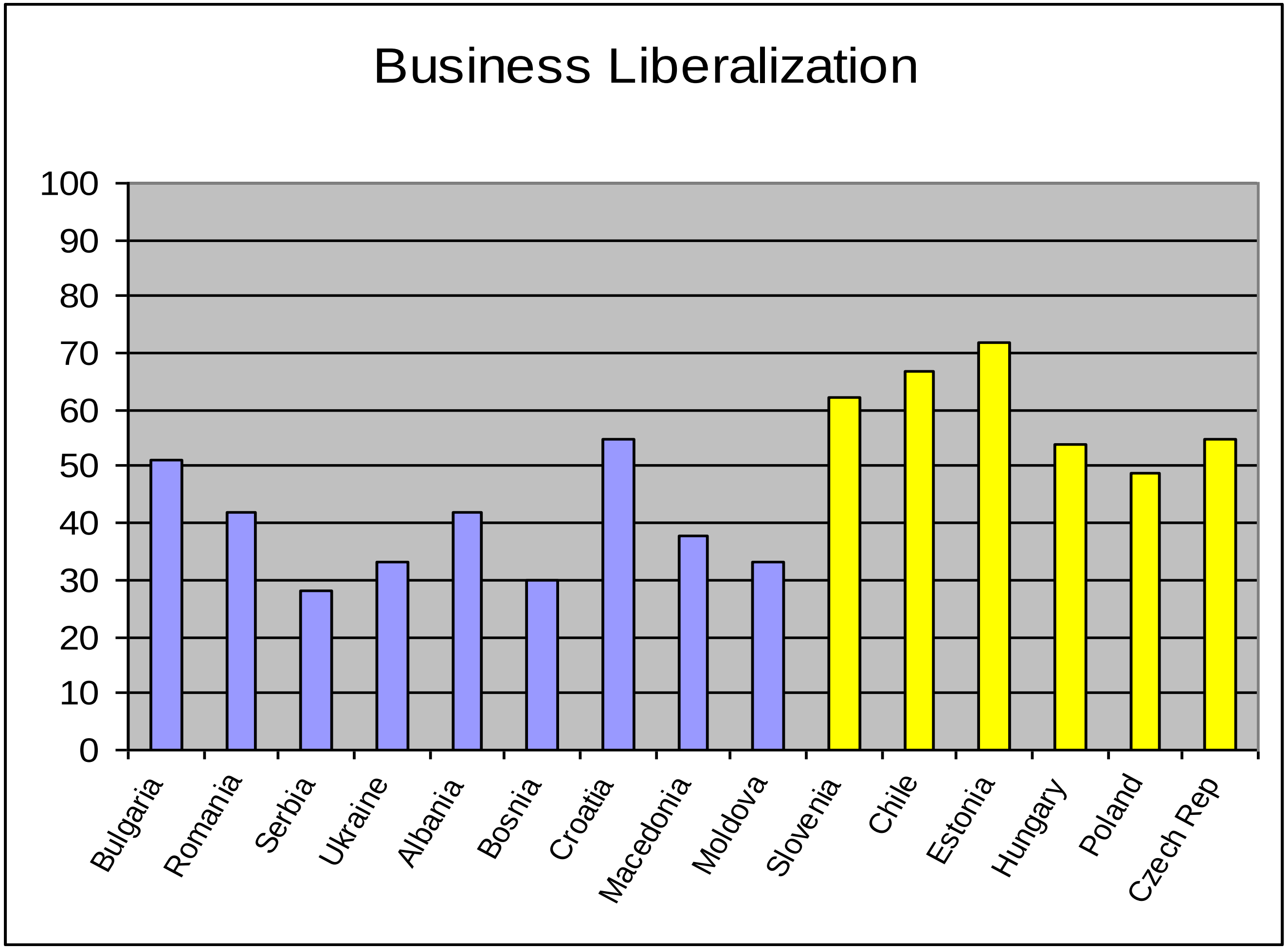
TBI Key Investment Drivers

1. Liberalization and Deregulation of Business Activities
2. Stable and Predictable Legal Environment (the Rule of Law)
3. Privatization, Public Administration reform and Corporate Governance
4. Removal of International Capital & Foreign Trade Restrictions
5. Facilitation of Business Financing by the Financial Sector
6. Reducing Corruption levels
7. Minimization of Political Risks
8. Improving Country Promotion and Image
9. Macroeconomic Performance

Country Ratings



Country Ratings



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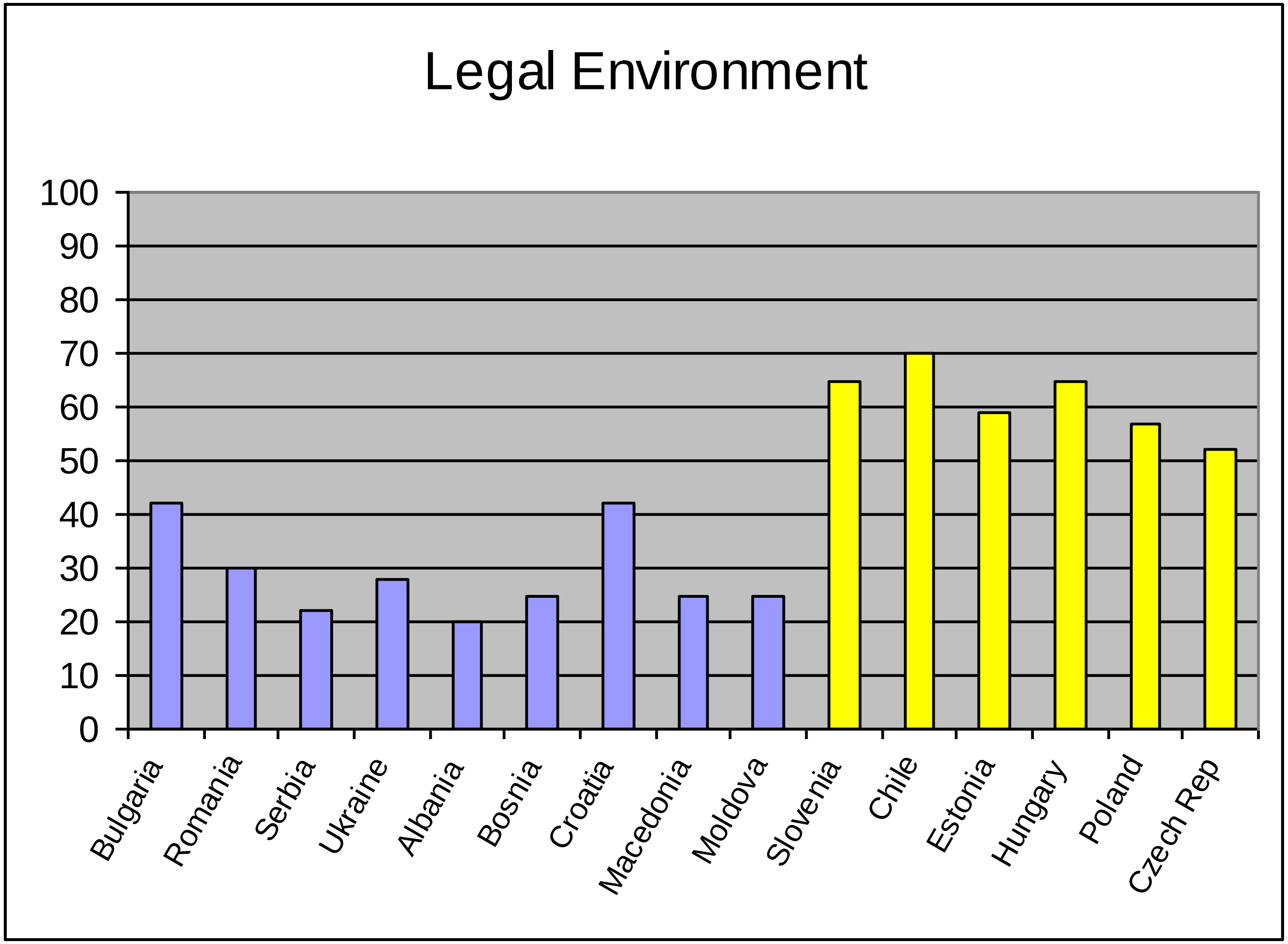

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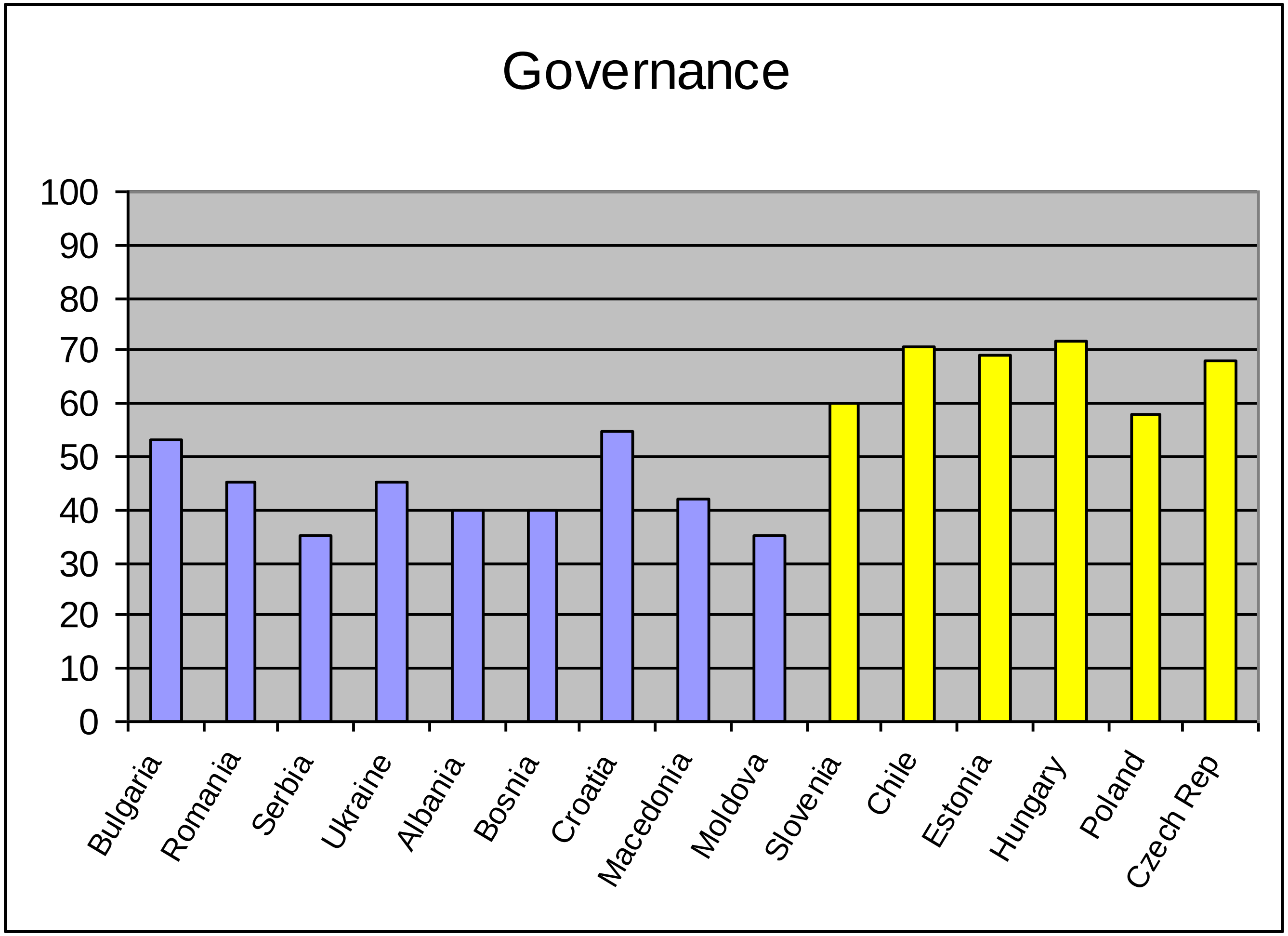

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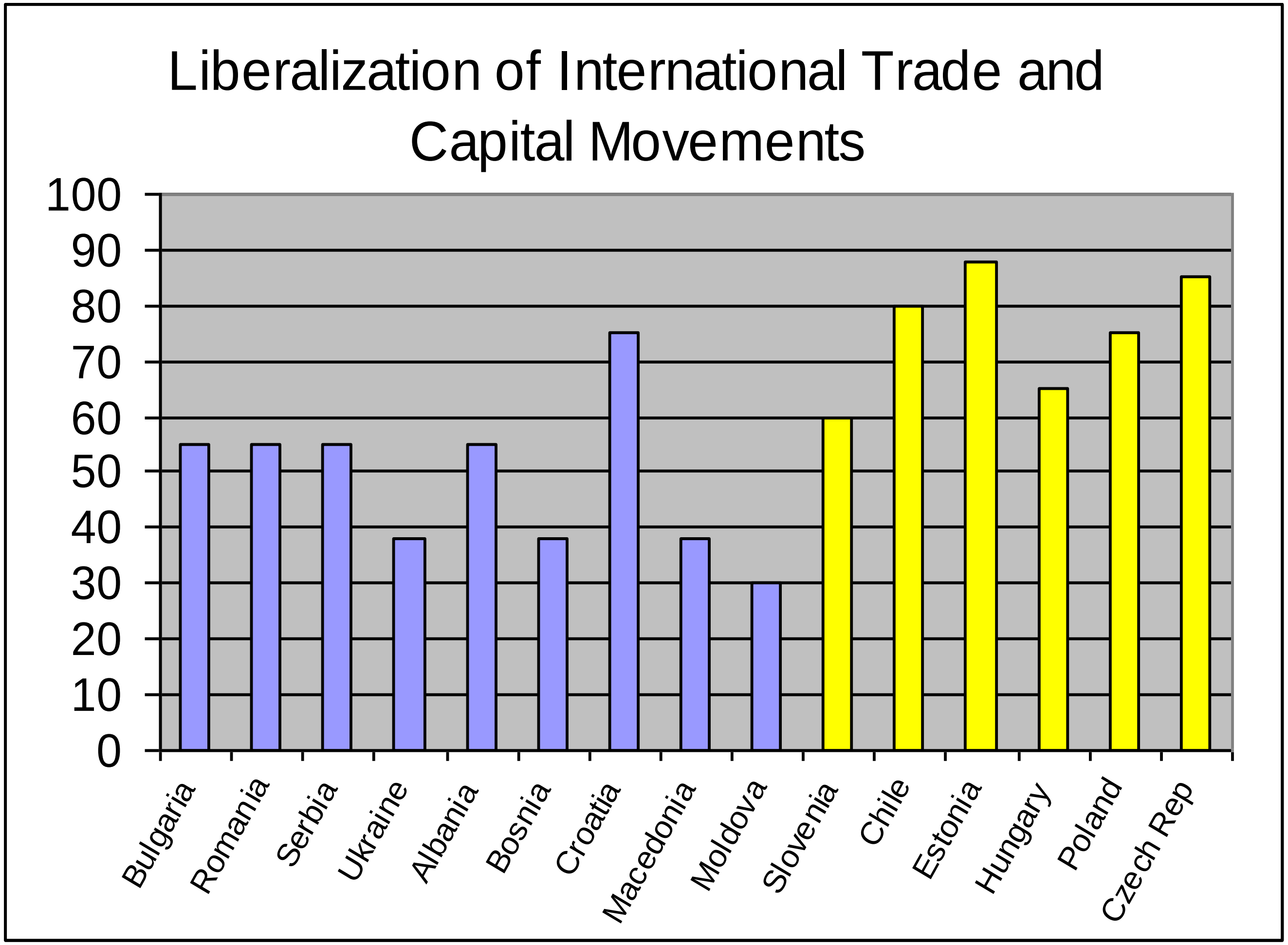

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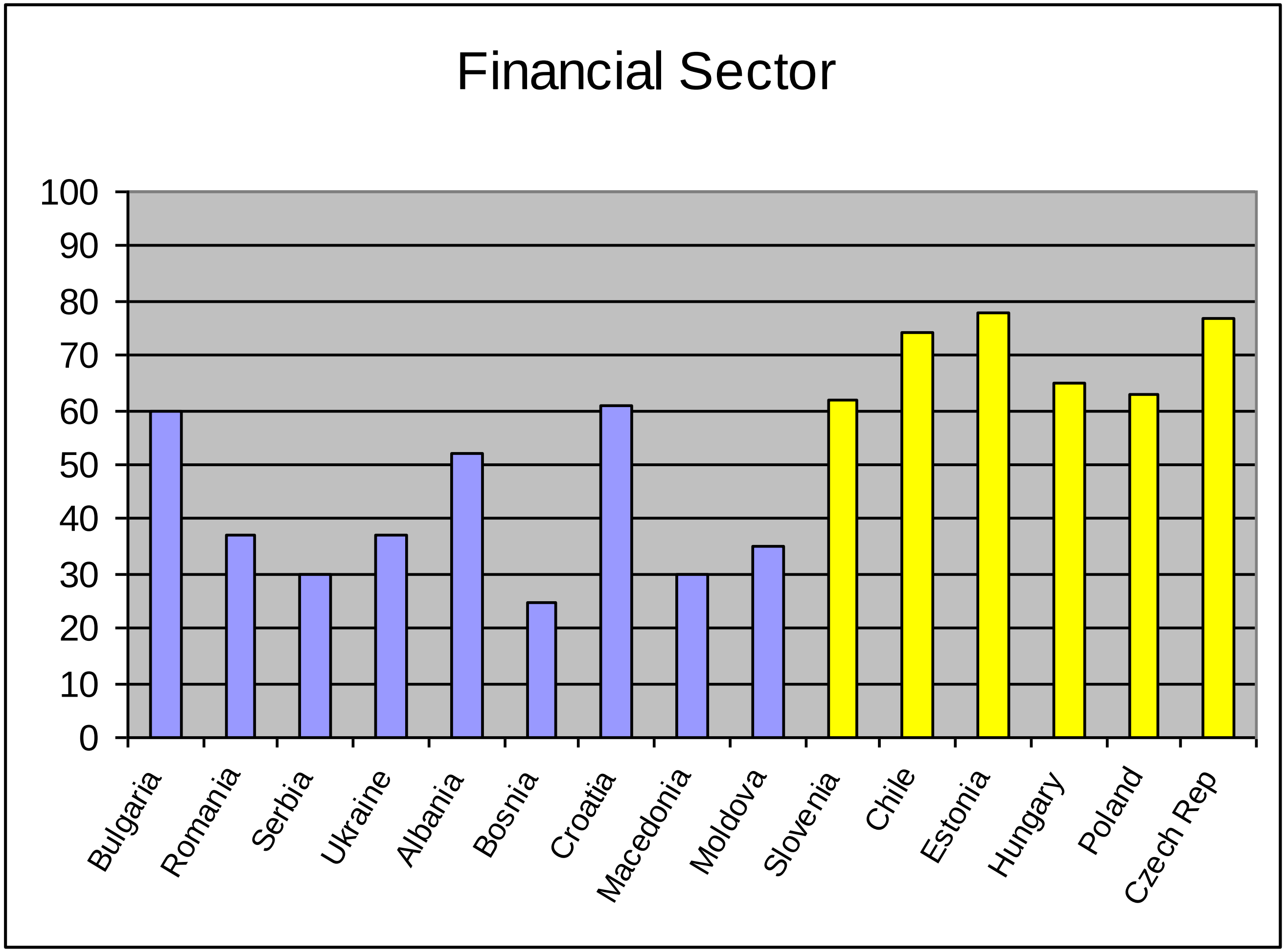

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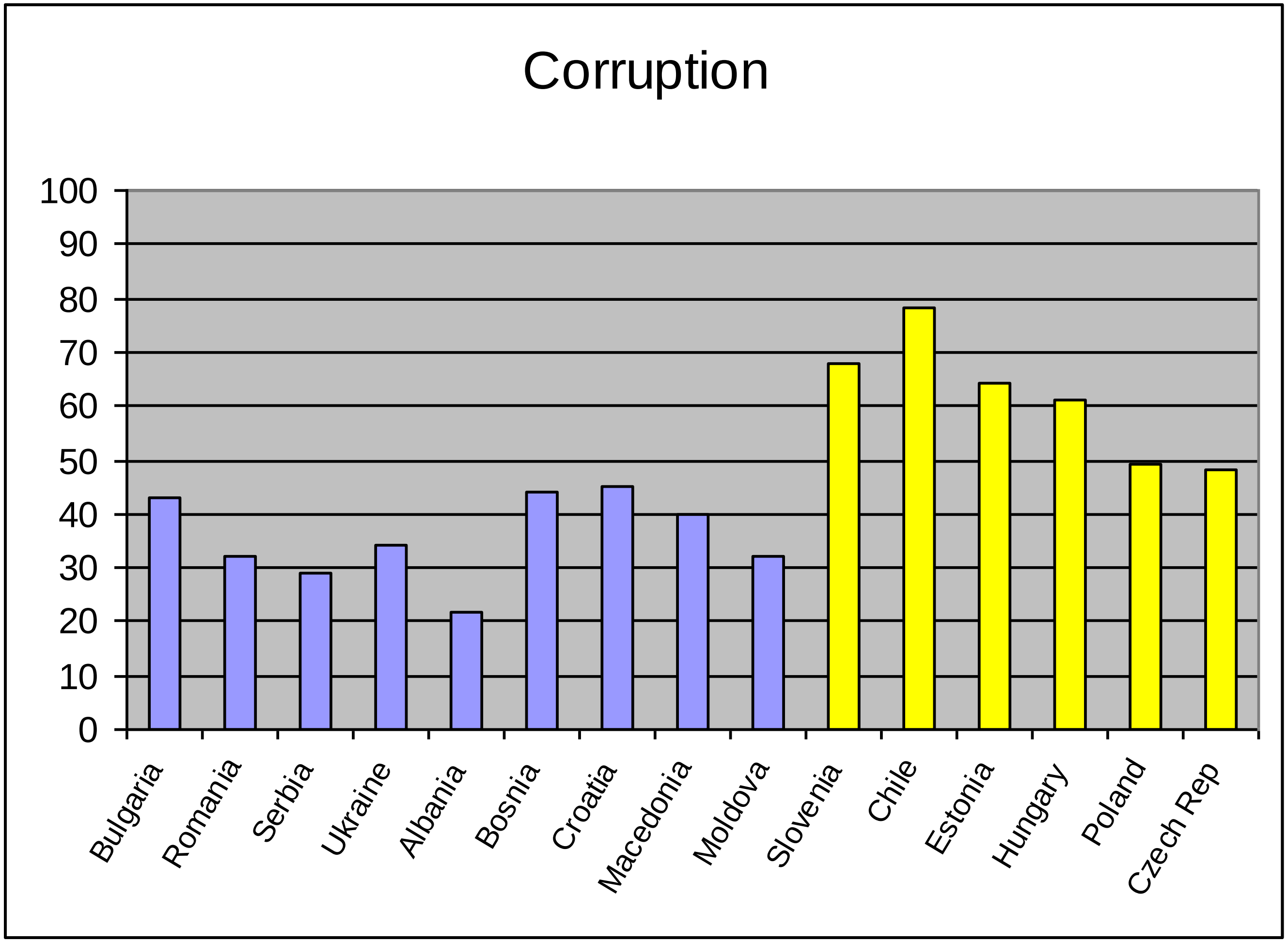

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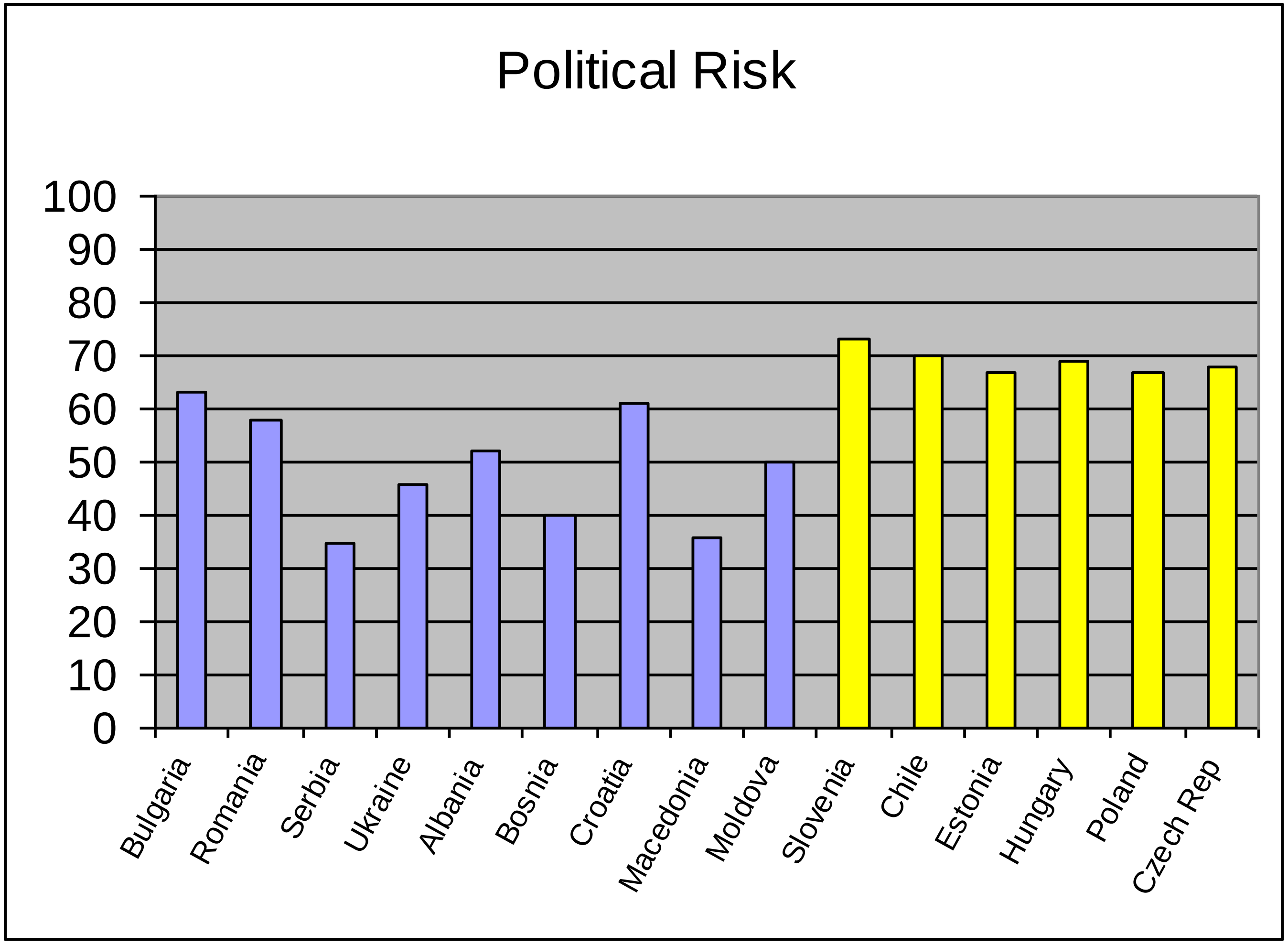

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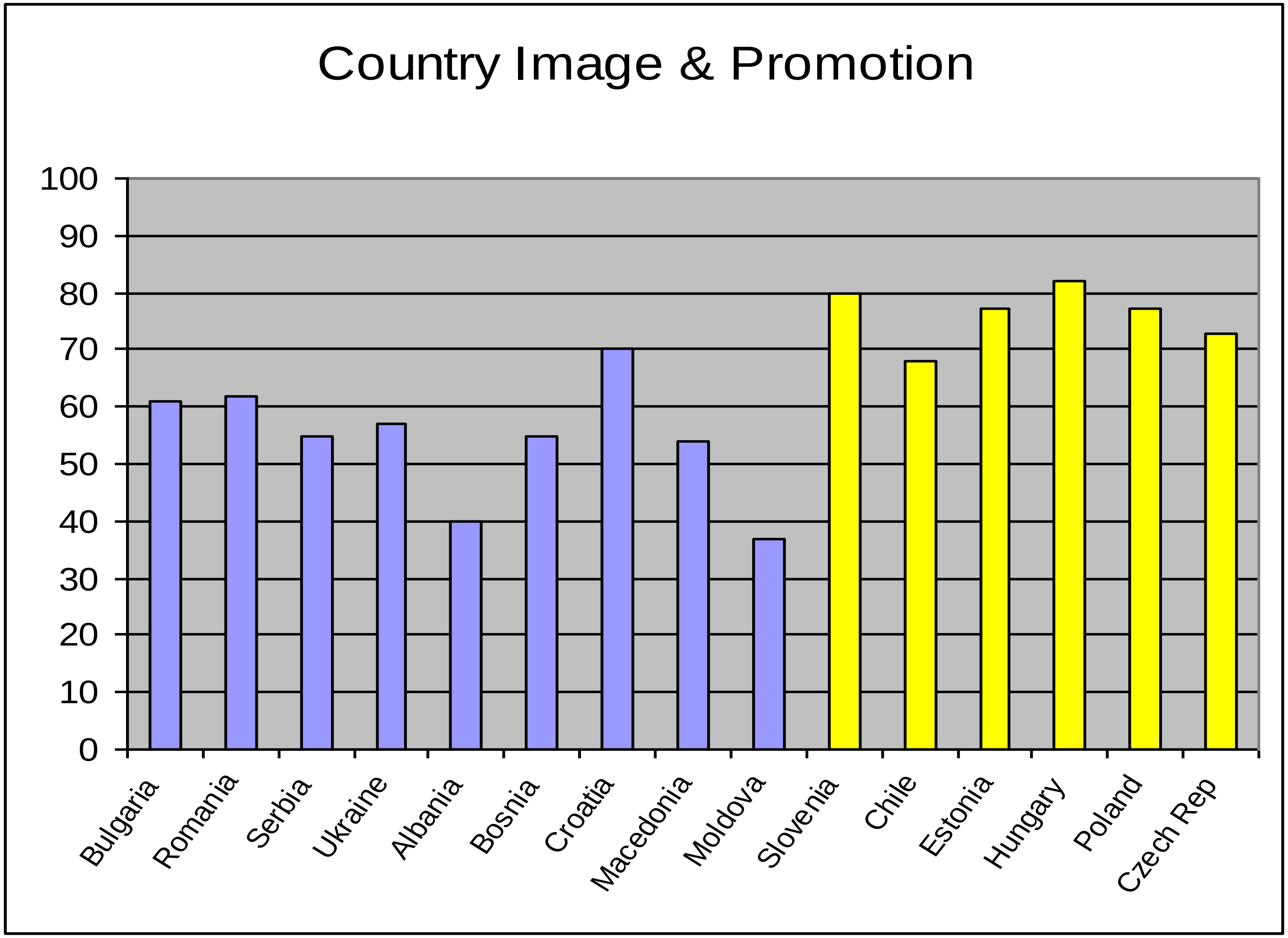
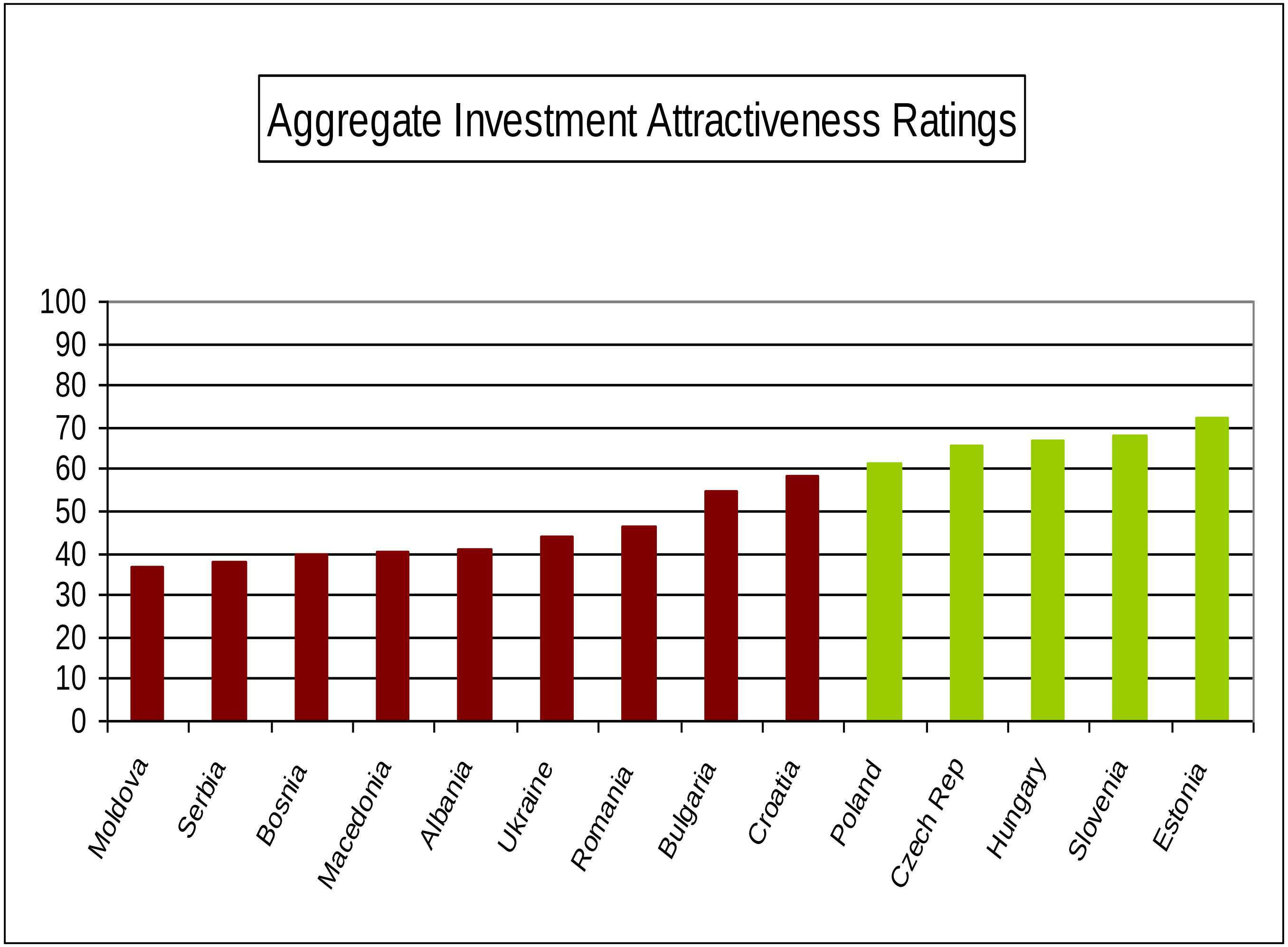
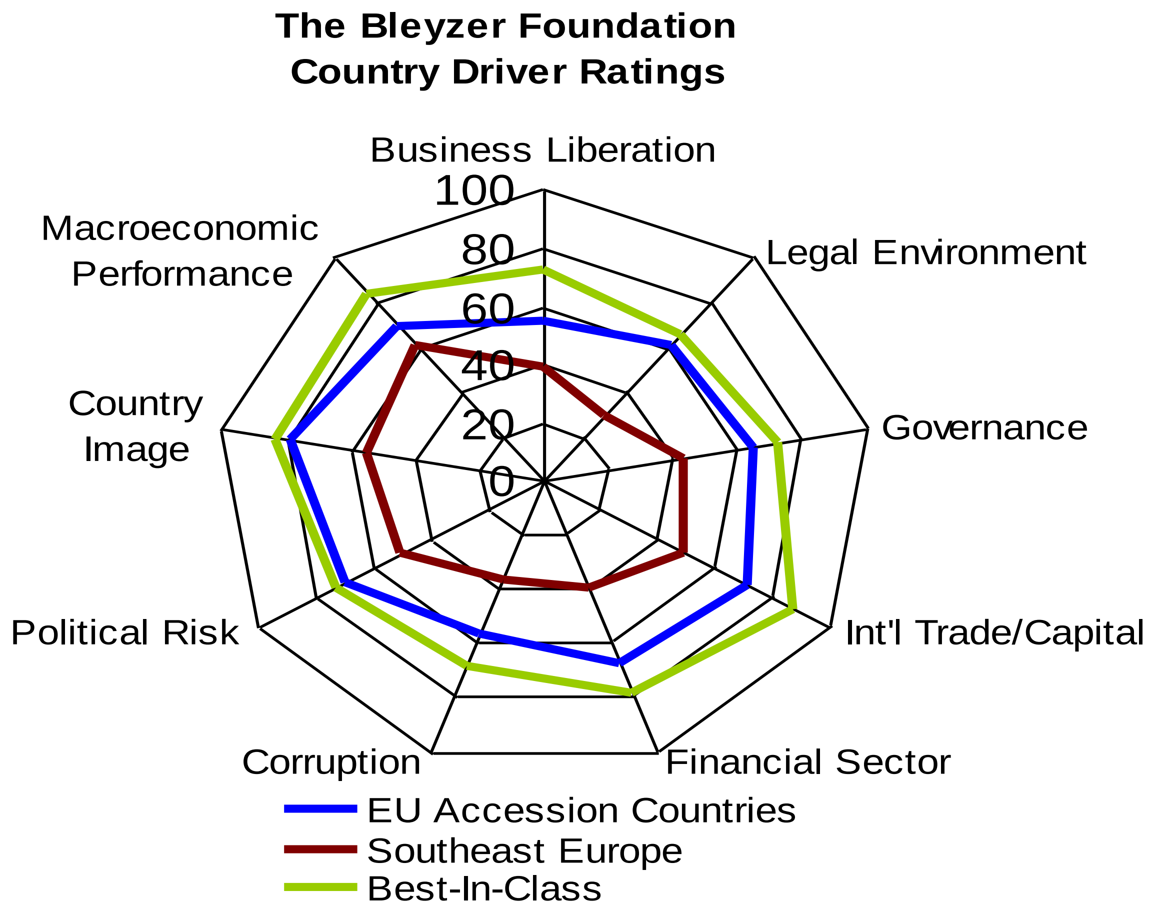


Overall Investment Drivers – Country Ratings



TBF Investment Drivers Nonagon



Ineffectiveness of IFIs and Official Aid Programs

- Aid flows have failed to bring about sustained economic growth and higher standards of living to recipient countries for multiple reasons:
  - Political rather than developmental objectives of foreign aid allocation by donors
  - Lack of ownership of assistance projects and programs by recipients
  - Lack of coordination among donors in their aid activities
  - The practice of aid tying by donors
  - Lack of administrative capacity to absorb large aid flows in developing countries
  - Inefficient terms of aid use
  - Aid fungibility
  - Trade barriers imposed by developed countries

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International Private Sector As A Solution

Where Opportunities Emerge

What do we propose?

- A private sector initiative – Private World Fund Pilot
  - Focused on the private sector development
  - Demanding business environment improvement as a condition for success and providing financing to make this happen
  - Capable of walking away when promises are not fulfilled
  - Attention of the world media to an experiment in private sector funded economic development
- Why has the private sector not stood up in the past?
  - Economic advice is a "public good"
  - There is a cost incurred by advice provider, but benefits available to all investors
- This "public good" demands "collective" action

A Hybrid Investment Approach

- Total pool of capital split to accomplish two objectives
- Hybrid = Private Capital Investments + Development Assistance
  - First portion structured as a private equity fund
    - Invests in enterprises and helps to modernize economy
    - Looks for superior returns
  - Second portion will finance economic assistance to advance legal frameworks, implement economic reforms and develop institutions
- Suggested methodology – TBI Economic Policy Framework

Conclusions

- *The private sector is best placed to help developing countries transition to free market economy based societies*
- *History has shown that IFIs have not done the job*
- *OSCE should consider supporting such an approach as a practical way to improve security and cooperation in Europe and the rest of the world*
- *We would like to discuss this proposal in depth at the 12th OSCE Economic Forum*