SigmaBleyzer

Brining Prosperity to The Developing World - The Role of Private Capital in Replicating Wealth Creating Capacity and Poverty Reduction

Michael Bleyzer

Where Opportunities Emerge

"Business Has Vital Role"

As we all know very well, the rapid globalization of international markets has brought prosperity and wealth to many. But a huge proportion of the world's population has not yet reaped its benefits. We have a shared duty to do all we can to shape globalization, so that it spreads prosperity far more broadly among the populations of less developed countries.

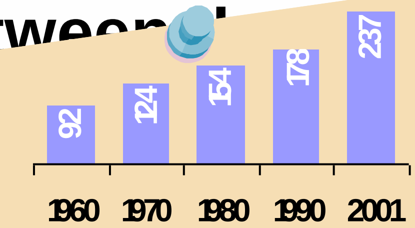
The business community has a direct stake in helping countries reach these goals and achieve broad-based, sustainable development. Reducing poverty helps create stable and inclusive markets, as well as the purchasing power that allows markets to grow. Supporting such progress makes good business sense, and it makes good development sense.

World Economic Performance – Recent Developments

Disparities in the world economic performance are impressive. Furthermore, despite faster average GDP growth in low income countries, the gap betwee richest and poorest countries has been wid

Selected Development indicators, 2005

	Gross National Income per capita (2005)	GDP per capita growth 04-05	GDP average annual growth rate 00-05
Ten richest countries*	43 788	2.0%	2.1%
Ten poorest countries*	200	2.4%	4.8%
High Income	35 131	2.1%	2.2%
Middle Income	2 640	5.4%	5.1%
Low Income	580	5.6%	6.0%



The ratio of income per capita in 10 richest countries to income per capita in 10 poorest countries

The income per capita in the richest countries is more than 200 times higher than the income per capita in the orest countries

Quality of Life and the Level of Income

Uneven economic achievements have shaped the differences in the progress of improvement in the quality of life. While higher income countries have notably decreased infant mortality rates, illiteracy rates and have high life expectancy, lower income countries have made much more modest progress in these areas. The disparity in performance is striking. For example, infant mortality rates in low income countries are 15 times higher than in OECD countries.

Infant Mortality Rate (per 1000 live births)

	1960	1980	1990	2000	2004	Improved by
High Income (OECD)	35	12	8	5.4	5.2	85%
Middle Income	118	54	40	35.4	30.9	74%
Low Income	148	110	91	83.9	79.5	46%

Since 1960 infant mortality rate in low income countries has been declining three times slower than in

Life Expectancy and Illiteracy by the Level of Income

SigmaBleyzer
Where Opportunities Emerge

Adult Illiteracy Rates (% of population aged 15 and above)

	1970	1980	1990	2001	2004	Improved by
High Income (OECD)	13.4	8.7	5.7	3.4	< 1	93%
Middle Income	34.5	25.6	18.5	13.1	10.2	70%
Low Income	64	55.6	47	38.1	38.5	40%
World	44.1	36.1	28.9	22.9	20	59%

Life Expectancy at Birth, total (years)

	1960	1980	1990	2000	2004	Improved by
High Income (OECD)	69	74	76	78.2	79	14%
Middle Income	46	66	68	69.1	70	52%
Low Income	43	53	57	58.1	58.8	37%

About 770 million adults in the world are illiterate; 75% of these people live in low income countries

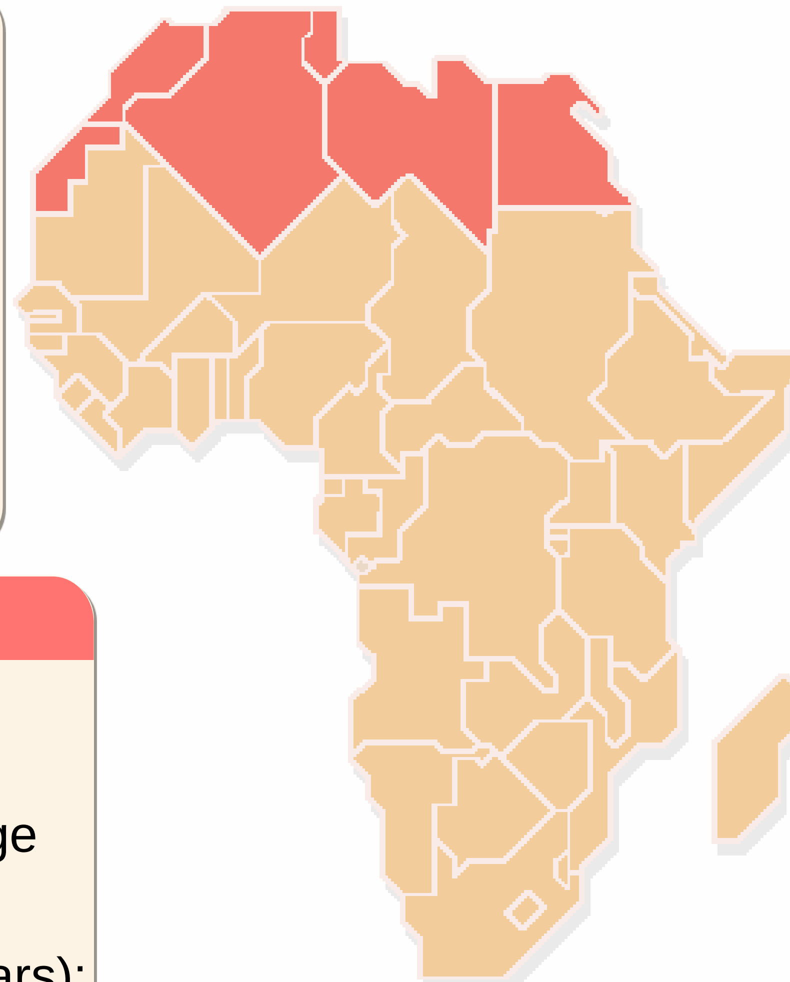
Life expectancy in low income countries is below 60 years and is less than 2/3 of the life expectancy in high income countries

Africa – Diverging Performance

SigmaBleyzer
Where Opportunities Emerge

African countries diverge in their economic performance as well.

	GDP per capita 2000	GDP per capita 2005	Average GDP growth 00-05
10 richest countries	3660.3	5556.6	13.1%
10 poorest countries	145.9	188.6	5.9%
Gap, times	25.09	29.5	-
Africa	718	1032	9.6%



Sub-Saharan Africa

Income per capita (2005): **745**

GDP growth (average 00-05): **4.2**

Life expectancy (years): **46.2**

Infant mortality rate: **100.5**

North Africa

Income per capita (2005): **2,826**

GDP growth (average 00-05): **7.1**

Life expectancy (years): **72.2**

Infant mortality rate: **27.8**

Source: *World Bank, World Development Report 2007, African Development Ba*

Global Inequalities Are Now More Exposed

Over more than 20 years poverty reduction has been the most debated and controversial issue in the international arena.

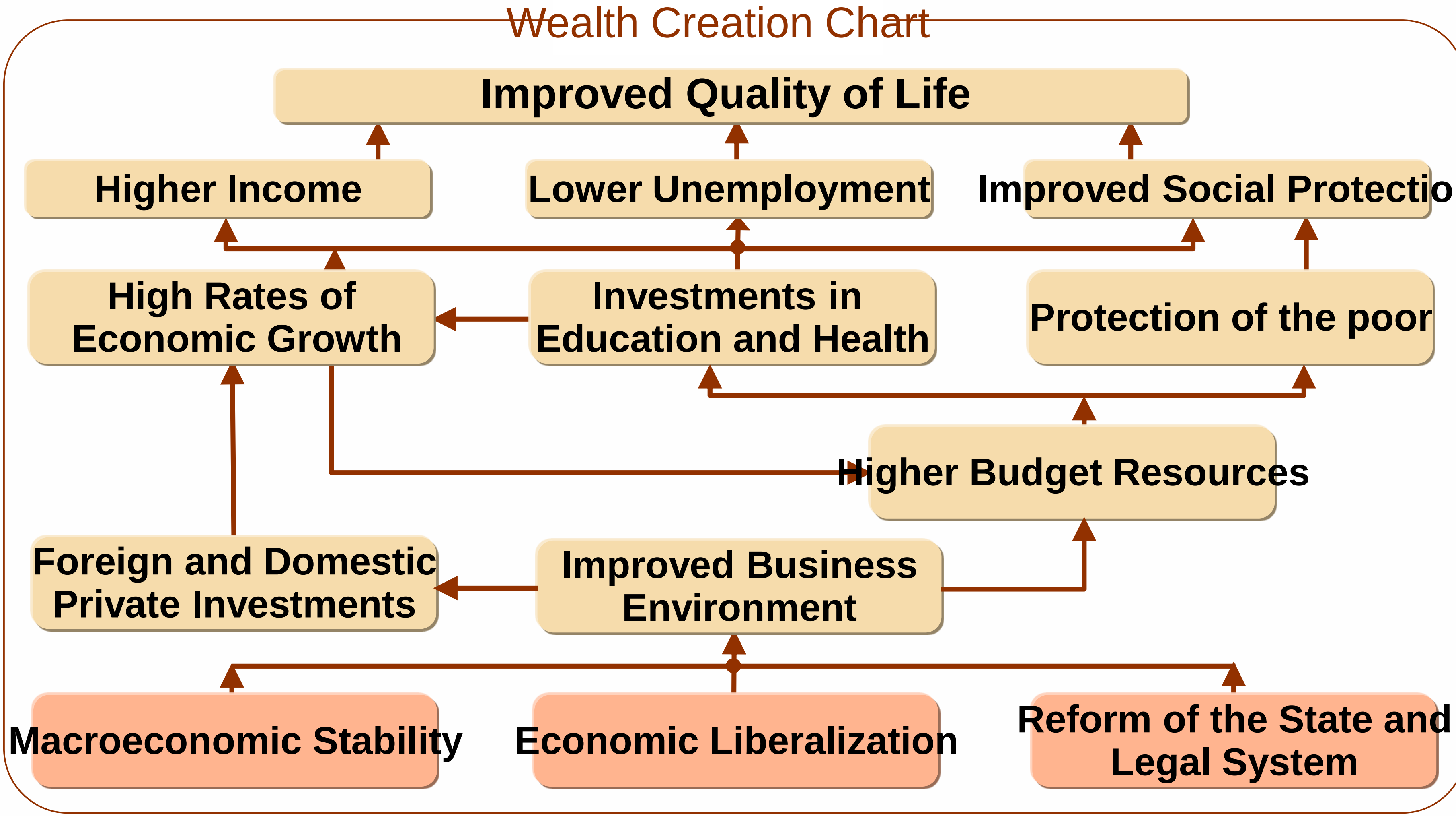
Greater awareness as a result of the global revolution in communications:

- improved exchange of information,
- poor nations are now better able to recognize their growing income disparity,
- many groups of poor have become more dissatisfied – resentment, frustration and desire to change the current world order have intensified.

Developed countries cannot isolate themselves from these inequalities:

There is a an urgent need to replicate Wealth Creation Capacity in developing economies.

Replicating Wealth Creation Capacity



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

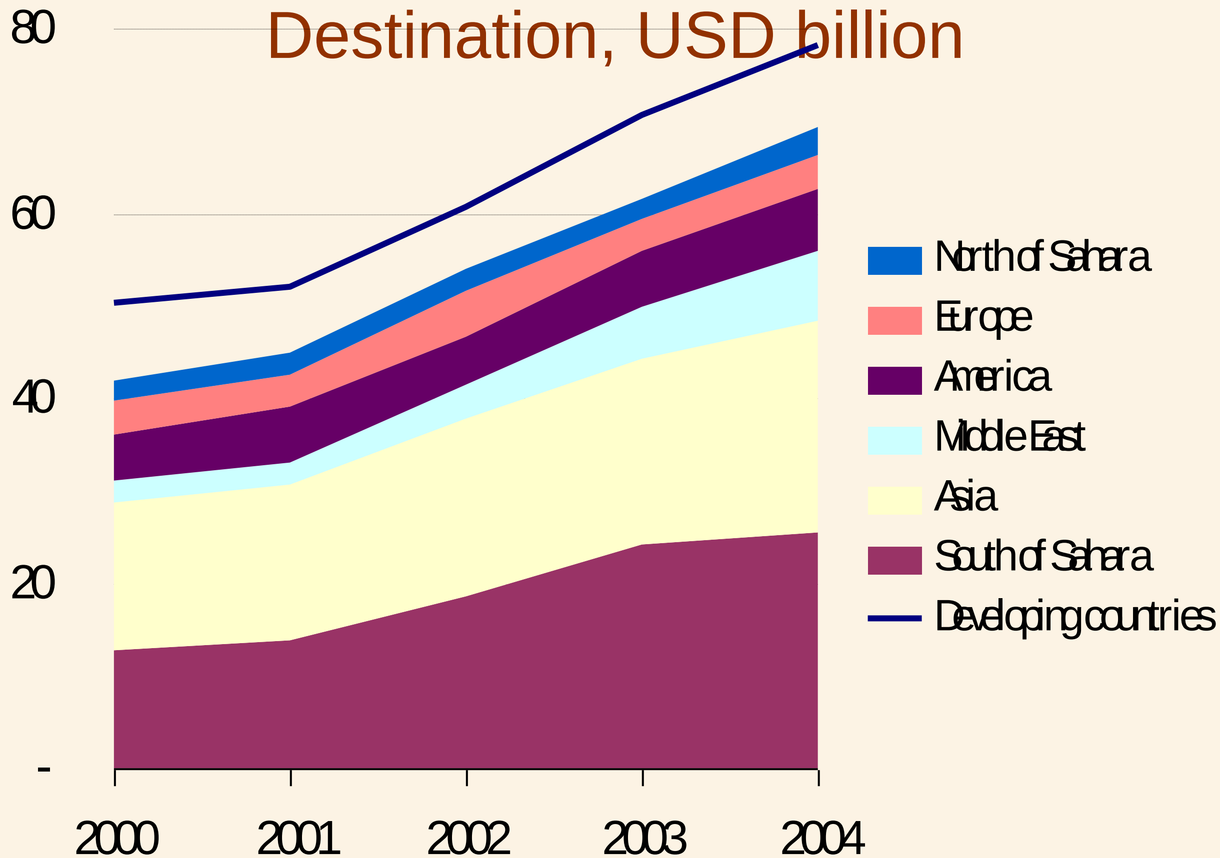
Main Functions of IFIs

The burden and responsibility to assist in building Wealth Creation Capacity in developing countries are almost exclusively put on the shoulders of the International Financial Institutions (IFIs):

- Help reduce poverty by making loans that support developmental projects to governments (World Bank and regional Development Banks).
- Provide loans to countries experiencing balance-of-payments problems so that they can restore conditions for sustainable economic growth (IMF).
- Provide project financing for banks, industries and businesses, both new ventures and investments in existing companies to help build market economy (EBRD).
- Provide technical assistance.
- Conduct extensive research on development

Recent Aid Developments

Net Total Official Aid by Country of Destination, USD billion



Source: OECD DAC International Development Statistics (IDS)

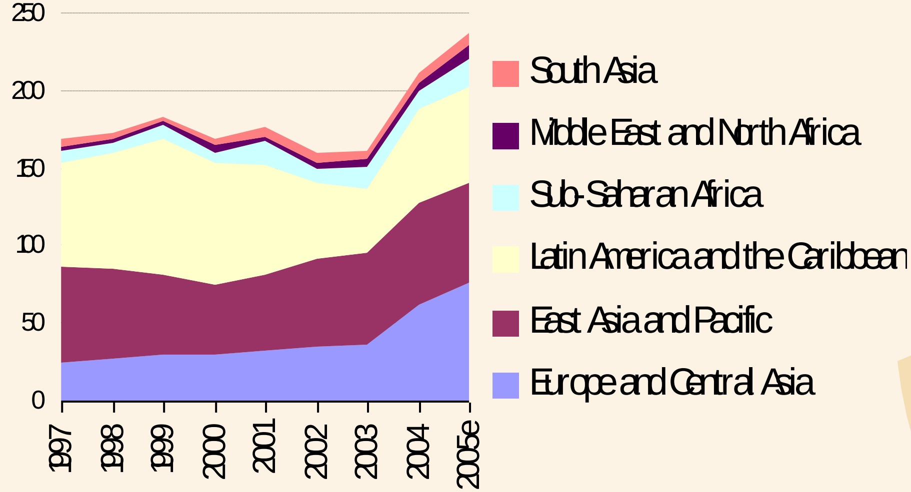
Debt relief grants increased more than 400% between 2004 and 2005, while other aid increased by 8.7%

Official development assistance to developing countries from member countries of the OECD's Development Assistance Committee rose by 31.4% to USD 106.5 billion in 2005.

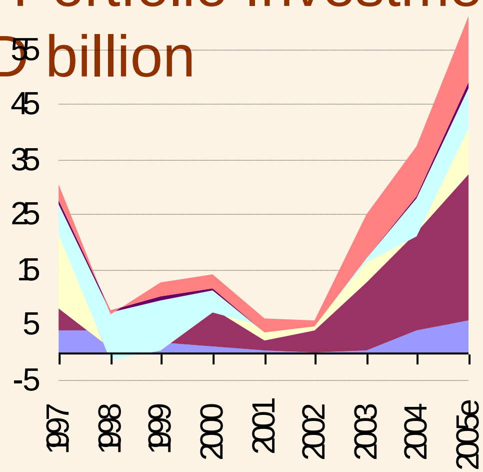
SigmaBleyzer
Where Opportunities Emerge

Net Capital Flows into Developing Countries

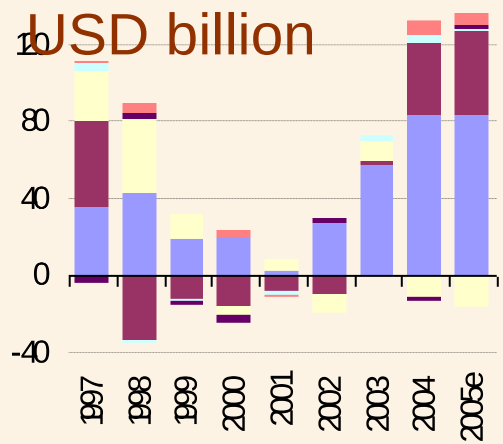
Net Foreign Direct Investments, USD billion



Net Portfolio Investments, USD billion



Net Debt Flows, USD billion



In 2005 only 10 countries (China, Mexico, Brazil, Russia, Czech Republic, Ukraine, Poland, Chile, Turkey and South Africa) absorbed over 67 % of total net FD or about USD 1 6 billion

2005 – World Bank estimates

Source: World Bank, Global Development Finance 2006

Inefficiencies of IFIs and Official Aid Programs

Aid flows have failed to ensure sustainable economic growth, significantly alleviate poverty and improve standards of living in recipient countries. Why aid programs did not succeed in developing reliable Wealth Creation Capacity?

- Strong political motives dominated aid allocation, preventing the efficient distribution of funds to developmental projects.
- Recipients lack ownership of assistance programs and projects – most of the efforts are channeled into the fulfillment of the targets set by donors.
- Inefficient coordination among donors in their aid activities.
- The practice of aid tying by donors – imposes excessive bureaucratic restriction on aid projects.
- Weak administrative capacity to absorb large aid flows in developing countries – costs of technical support and monitoring of aid programs are frequently too high.
- Inefficient utilization of aid funds – limited aid resources are channeled into developmental projects that advance wealth creation capacity in recipient countries.
- Aid fungiblity – increased dependency of recipient governments on aid flows in the provision of public goods and services.

IFIs Are Extremely Slow to Change

IFIs are at heart political, "official" institutions, owned by Governments and operating under political rather that economic incentives.

- IFIs' developmental targets are based on general concepts of poverty reduction which may frequently contain populist, unclear, diffused, or even conflicting goals.
- The implicit objective of any IFI is to promote the interests of share-holding countries.
- As a political institution, IFI must insure fairness and nondiscrimination of funds distribution among countries under the strict internal budget limitations.
- The decision to grant or withdraw aid is mostly considered as a political action grounded on the loyalty of the recipient countries to donor governments.
- For the same reason, restricting aid flows to a particular country is a very sensitive issue as it is perceived as a political sanction against the recipient country.
- IFIs are reluctant to admit the inefficiency of their aid projects due to the necessity to report sound performance to share-holding governments. Furthermore, aid efficiency is unlikely to have the highest priority in evaluating IFIs' activities.

IFIs Had Limited Impact on Wealth Creation Capacity

SigmaBleyzer
Where Opportunities Emerge

The principle objective of IFIs is to develop the economies of recipient countries through various assistance programs to the governments of these countries. However, inefficient implementation of aid projects has yielded results that fell short of expectations.

- Unsatisfactory progress was achieved in developing the key pillar of strong Wealth Creation Capacity – business-friendly environment:

  Most of the aid funds are channeled into the social development projects to compensate for the shortage of funds available to the local governments. While these projects significantly contribute to the enhanced provision of vital public services they considerably increase the dependence of governments’ budgets on unstable aid flows.

- Too much focus on debt capital – loans that often cannot be repaid while they are absorbed by programs that do not generate their own self-financing:

  - Aid is frequently biased toward government budget deficit financing, poverty alleviation, environmental programs, infrastructure building, democracy building.

  - Increased loan repayment burden on governments’ budgets.

IFIs Had Limited Impact on Wealth Creation Capacity

The pressure to allocate aid into the projects with an immediate impact on poverty led to the sizable investments into in the social sectors such as education, health, infrastructure and environment, while financing of the programs that develop efficiently functioning private sector was insufficient.

- Aid was an effective measure to address short-term shortages at the supply of basic public goods, however it failed to create a sustainable basis for the stable provision of these goods in the long-run.
- Aid had a small impact on building a solid and expanding base for budget fiscal revenues. In contrast, it increased the dependence of governments of recipient countries on aid flows and made them bid for more funds.
- Private sector development was inadequately covered by aid programs which significantly constrained the speed of business liberalization in developing countries.

A shift toward accelerated liberalization of business regulations and effective development of countries' investment potential is a necessary condition to ensure prosperity of developing nations.

More active engagement of private sector in shaping the agenda of economic reforms in developing countries is a must.

Why Private Sector Involvement is Scarce?

Improving business environment is a kind of "public good". Its advocacy has the cost incurred by the "champion", but the benefits will accrue to all investors. Once it is achieved, everybody will reap the benefits.

An individual investor will rarely engage in this activity as the cost is high and the improvements will also benefit its competitors, which would just be "free-riders", without bearing any of the costs.

International Institutions are less exposed to default and country risks and have effective political levers to influence local governments. The costs to manage these risks for an individual investor are too high.

As a result, the role of assisting developing countries was almost exclusively delegated to IFIs.

However, deficiencies of IFIs aid programs call for more active involvement of private sector in developmental

Improving business environment as a risky and "public good" project demands collective action among a group of investors.

Private Initiative Can Remedy IFIs' Inefficiencies

SigmaBleyzer
Where Opportunities Emerge

Private Investors

- More focused on private sector.
- Invest into projects that generate high returns and self-financing.
- More demanding and straightforward in measuring results.
- Clear business goals and, therefore, more understandable for recipient governments.
- Not operating in hopeless environments.
- More capable to walk away when promises are

IFIs

- Principle focus on social sector.
- Investment projects frequently rely on long-term aid financing.
- Clear criteria to monitor and control the utilization of funds are absent.
- Lacking concrete and politics-free objectives.
- Tend to extend financing to recipients with high stock of non-performing loans.
- A decision to cease aid is a politically controversial

The Benefits to Private Investors

- Experience over the last two decades show that countries that were able to secure larger inflows of foreign private capital achieved above average GDP growth.
- Developing countries have been significantly outperforming developed economies in terms of the rates of return on private equity investments.
- As most of the FDI were absorbed by the narrow set of countries, gradual saturation of these destinations for private equity investment in developing regions significantly limits the opportunities to secure above average returns in traditional markets.
- The value of assets in developing countries tends to boost as economic reforms and business liberalization advance, therefore, earlier entry guarantees superior capital gains on investments.
- Multinational corporations and global industrial

Why Should Governments Support This Initiative?

SigmaBleyzer
Where Opportunities Emerge

The growth of successful private sector in developing countries serves as a barometer of good economic reforms and improves country’s advantage in competing for foreign capital at the global financial markets. The benefits to local governments are ample:

- Inflows of external funds without increasing debt burden on the governments.
- High expertise at engineering investment-friendly environment brought by the international businesses with an extensive experience in developing countries.
- Large private sector investments significantly improve fiscal revenues as well as built a solid foundation for sustainable budget revenues in the long-run creating a stable source of funds to finance social programs and fight poverty.
- Foreign direct investments create new jobs and bring advanced technologies.
- Strong incentives to adhere to sound business regulations and economic policies to support foreign investors.
- The possibility to channel higher budget revenues into the social

Philosophy of The Privatized Financial Aid

Private Capital to support funding of the improvements in business environment in order to achieve accelerated economic development and superior returns.

Implementation of the concept is performed through the HYBRID INVESTMENT FUND – a combination of traditional NGO, non-p s with profit-oriented investments in the sa

Private World Bank

Private Capital

Hybrid Investment Vehicle

Principle Activities:

- **Financial aid programs**
- **Economic development:** advance investment environment at the macro and business environment level
- **Private equity**

- **Higher standards of living and reduced poverty**
- **Improved investment climate and business environment**
- **Superior returns for participating private investors**

A Concept of The Hybrid Investment Vehicle

A combination of non-profit economic development and research unit with a profit-seeking investment fund:

- Select an optimal organizational structure of this hybrid investment vehicle with a priority to cover a wide range of potential investors and insure effective cooperation between non-profit and private equity departments of the fund.
- Develop adequate marketing strategy that targets investors who are willing to invest into economic developments and investors who are interested in private equity investments.
- Outline the concept of economic development initiative that can be tailored to country specific problems. The sets of urgent policy improvements and relevant policy recommendations have to be defined and justified on the basis of a comprehensive economic research.
- Candidate countries and sectors for private equity investment should be selected.
- Employ a functioning management team equipped with

Private World Bank – Pilot Implementation Steps

I. Develop the strategy of the fundraising campaign:

- **Target: raise fund $100M - $500M.**
- **Approach potential Investors:**
  - Multinational Corporations and Global Industrial Companies
  - High net-worth individuals
  - Foundations
  - Government backed multilaterals and bilaterals
- **Form an advisory board with key investors.**
- **Ensure effective coverage in global and local Media.**
- **Gain support from International and regional developmental organizations.**
- **Attract attention of the potential recipient governments.**

Private World Bank – Pilot Implementation Steps

SigmaBleyzer
Where Opportunities Emerge

II. Select potential recipient countries (regions) and draft economic development strategy:

- **Identify candidate countries or regions.**
- **Utilize The Bleyzer Initiative criteria to predict potential FDI flows. Outline policy areas with the highest impact on business environment and institutional development and propose clear public policy recommendations.**
- **Present and explain approach to secure commitment:**
  - Long-term commitment
  - Definition of benefits and success
  - Philosophy and implementation of economic development approach
  - Progress measurement to retain funding
- **Gain commitment and support from recipient governments.**
- **Negotiate terms for investment with the recipient**

Private World Bank – Pilot Implementation Steps

III. Form investment portfolio

IV. Identify clear procedures to measure performance and report progress.

V. Develop infrastructure and tools to ensure successful launch of the pilot

- Project Management:
  - **Advisory Board**
  - **Executive Team** – negotiate the deal and raise funds
  - **Investment Team** – manage profit-oriented portfolio of the fund
  - **Development Assistance Team** – closely cooperate with the government, develop and implement Action Plan for the recipient country, manage financial aid projects of the fund
  - **Monitoring Team** – monitor and report fund progress, research and update Action Plan models.

Initial Challenges of the Pilot Fund

SigmaBleyzer
Where Opportunities Emerge

- **Identify and approach potential investors:**

  Set clear, non-conflicting targets so that the fund will be of interest to investors willing to support economic development as well as to investors willing to participate in the private equity investments.

- **Focus on a group of countries or a region to ensure long-run advantages in country selection and fundraising.**
- **Establishing the legal and tax structure of the organization:**

  The structure must guarantee the optimal combination of private equity investment and developmental unit,

  Formalize the procedures of allocating a portion of the fund to developmental activities and procedures to utilize these funds,

  Ensure effective communication between the two units of the organization.

- **Raise seed capital for the initial organization.**

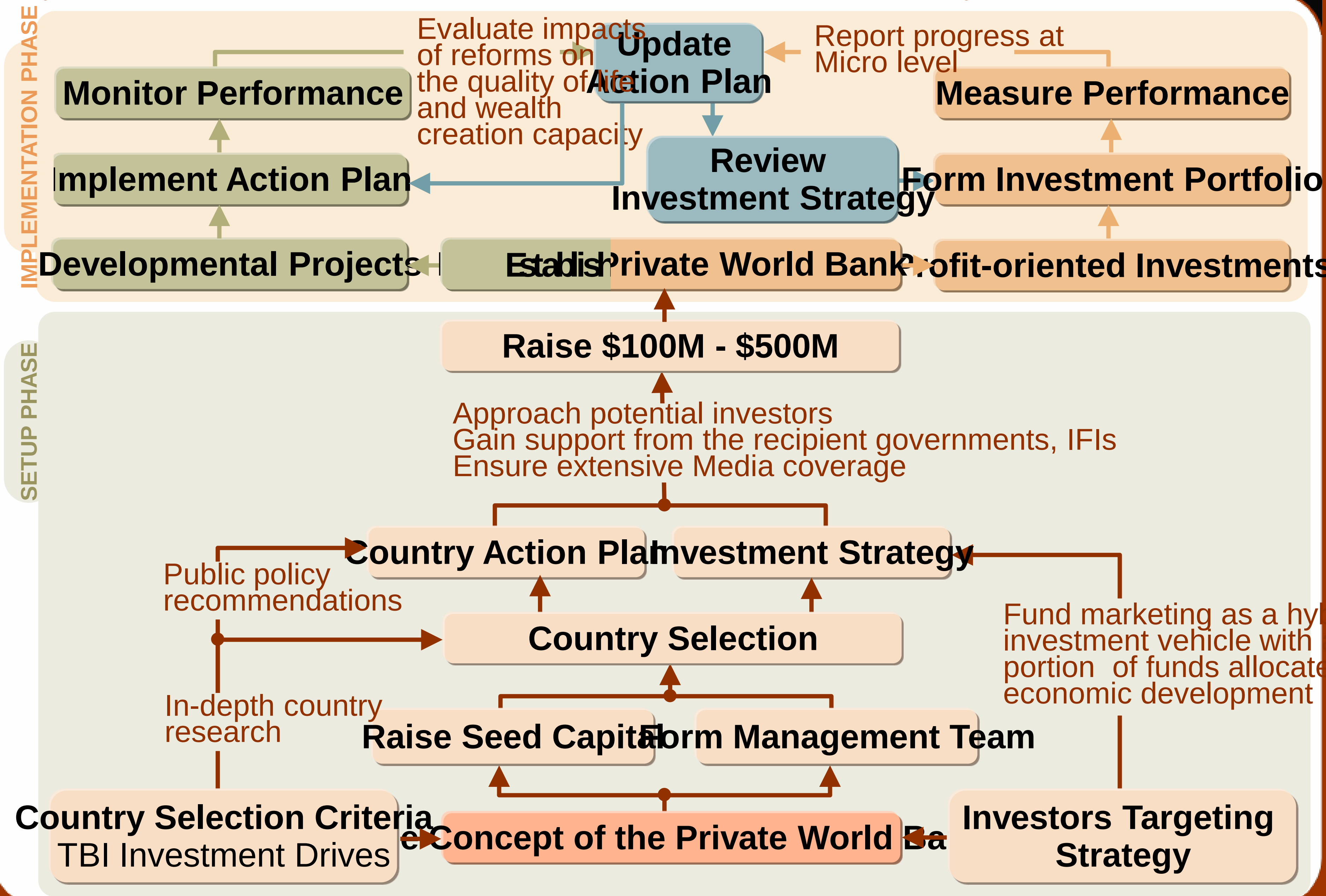
Prerequisites of Success

- The existence of a clear authority to execute economic development Action Plan within the recipient government.
- The country is willing to accept and support economic development initiative.
- The country should have sufficient capacity to implement Action Plan.
- The government should be committed to market-oriented reforms and willing to cooperate with the fund.
- There is an urgent need to reform.
- The country itself is willing to invest.
- The pilot should be done in more than one country to test the different scenarios.
- Low barriers to institutional changes should exist.
- The private sector should show interest in the project.
- The capacity to prove the approach should be high:

The fund should be the leading developmental

Private World Bank Pilot

SigmaBleyzer
Where Opportunities Emerge



Example: SigmaBleyzer and The Bleyzer Foundation

- **SigmaBleyzer is a private equity firm that for over ten years has been successfully investing into transition countries. SigmaBleyzer currently manages funds with total committed capital of over $500 million.**
- **In 2001 The Bleyzer Foundation was founded as an international non-government organization supporting the successful development of transition economies into healthy, democratic market economies. To achieve this goal, the Foundation's activities include:**
  - Engaging governments in dialogue to influence economic policy in areas related to improving the business climate,
  - Monitoring and reporting on the evolution of key economic reforms and policies that affect the investment climate,
  - Promoting associations and alliances of businesses and non-government organizations that share the Foundation's goals,
  - Promoting education and implementation of best practices in government policies,
  - Promoting the necessity of legal, administrative, economic, and other reforms in order to ensure sustainable economic growth,
  - Advocating and promoting campaigns to create positive images of developing countries and strengthen their international

The Bleyzer Initiative (TBI)

SigmaBleyzer
Where Opportunities Emerge

Based on the extensive research of FDI determinants in developing countries nine investments drives with the highest impact on FDI flows were selected.

TBI key Investment Drives:

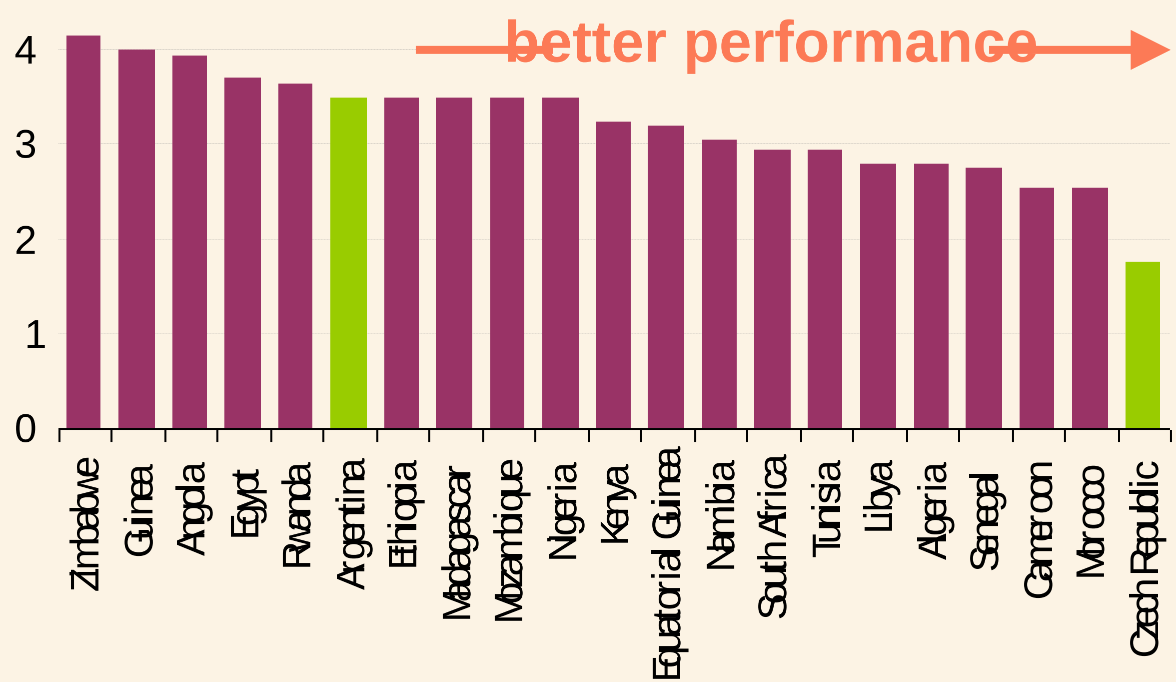
- Macroeconomic Performance
- Liberalization and Deregulation of Business Activities
- Stable and Predictable Legal Environment (the Rule of Law)
- Privatization, Public Administration reform and Corporate Governance
- Removal of International Capital & Foreign Trade Restrictions
- Facilitation of Business Financing by the Financial Sector
- Reducing Corruption levels

Objective: engineer a set of policy measures that have a direct positive impact on each of the nine investment drives in recipient countries.

Institutional Environment in Africa is Weak

SigmaBleyzer
Where Opportunities Emerge

Macroeconomic performance



Source: Index of Economic Freedom 2006

This Index is based on the average of monetary policy and fiscal burden scores. The lower the index – the better is the country's performance

The countries of North Africa have better macroeconomic performance than the countries of Sub-Saharan region

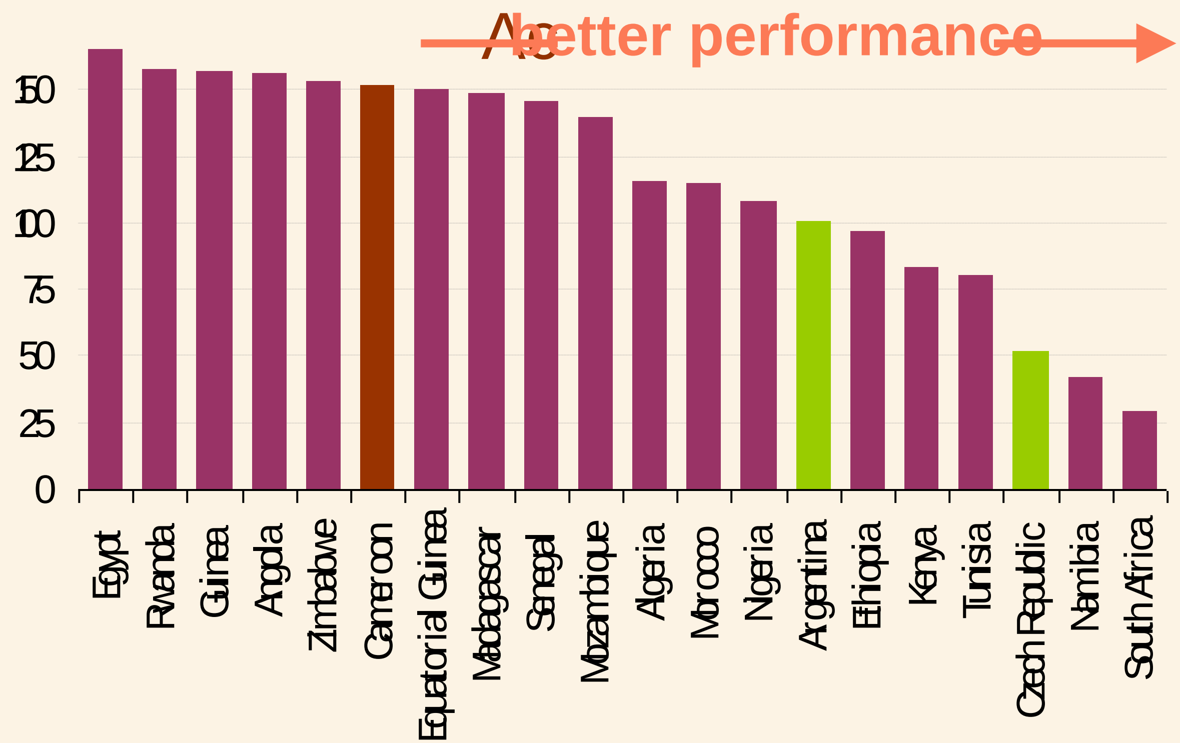
Key policy recommendations:

- Strengthen fiscal discipline and control over budget expenditures
- Improve revenue side of the budget and built strong tax administration capacity
- Enhance monetary policy through better management of

Institutional Environment in Africa is Weak

Liberalization and Deregulation of Business

As



Source: World Bank, Doing Business 2007

“Ease of doing business” countries’ ranks – the higher the rank (1 is the highest) – the easier is to do

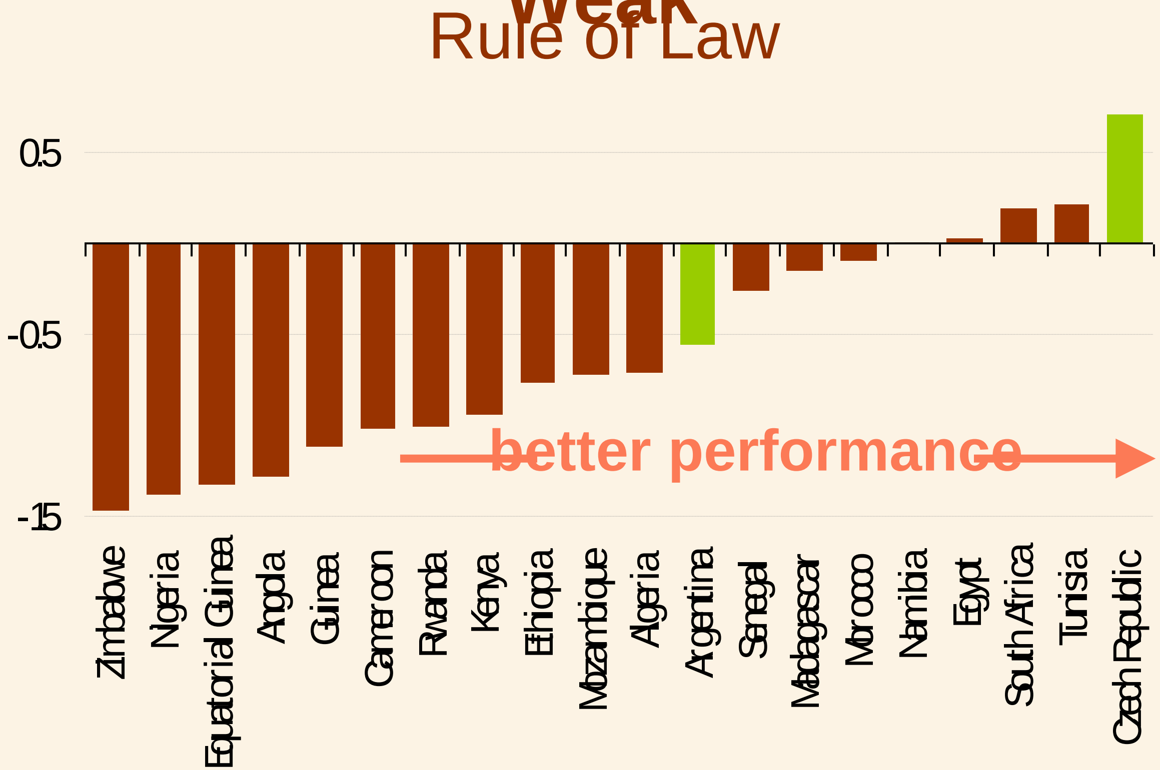
In North Africa it takes on average 21 days and 10 procedures to start a business, while in Sub-Saharan Africa – 62 days and 11 procedures

Key policy recommendations:

- Simplify business registration and taxation procedu
- Advance exit procedures and modernize bankruptcy codes
- Enforce competition laws and sanction anticompetitive behavior

Institutional Environment in Africa is Weak

SigmaBleyzer
Where Opportunities Emerge



Source: World Bank, Governance Indicators (2006)

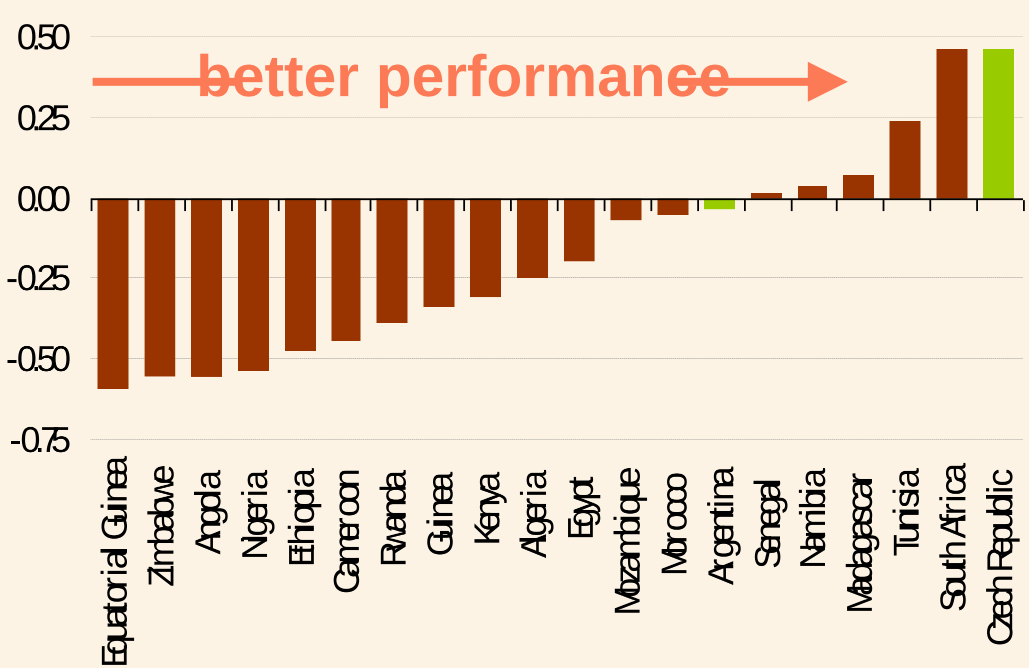
"Rule of Law" index is measured on a scale from -2.5 to 2.5, with higher value representing better performance

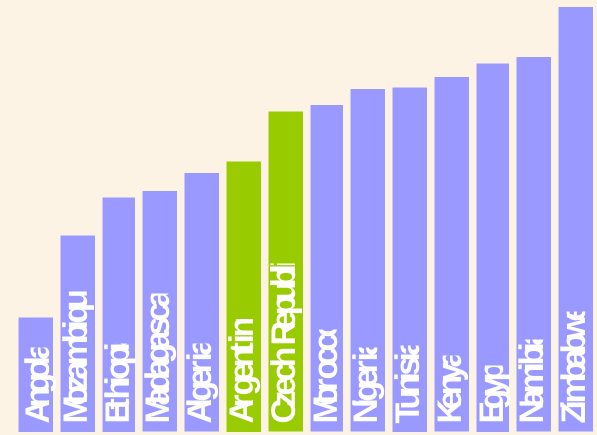
Key policy recommendations:

- Define the "rules of the game" for all business, without discrimination or preferential treatments
- Create an independent Judiciary, with its independent budget
- Enhance effective enforcement of legislation

Institutional Environment in Africa is Weak

Public Governance





World Bank's Corporate Governance Indicator

Source: World Bank, Governance Indicators (2006), Index of Economic Freedom 2006

Public Governance: weighted average of government effectiveness index and government intervention

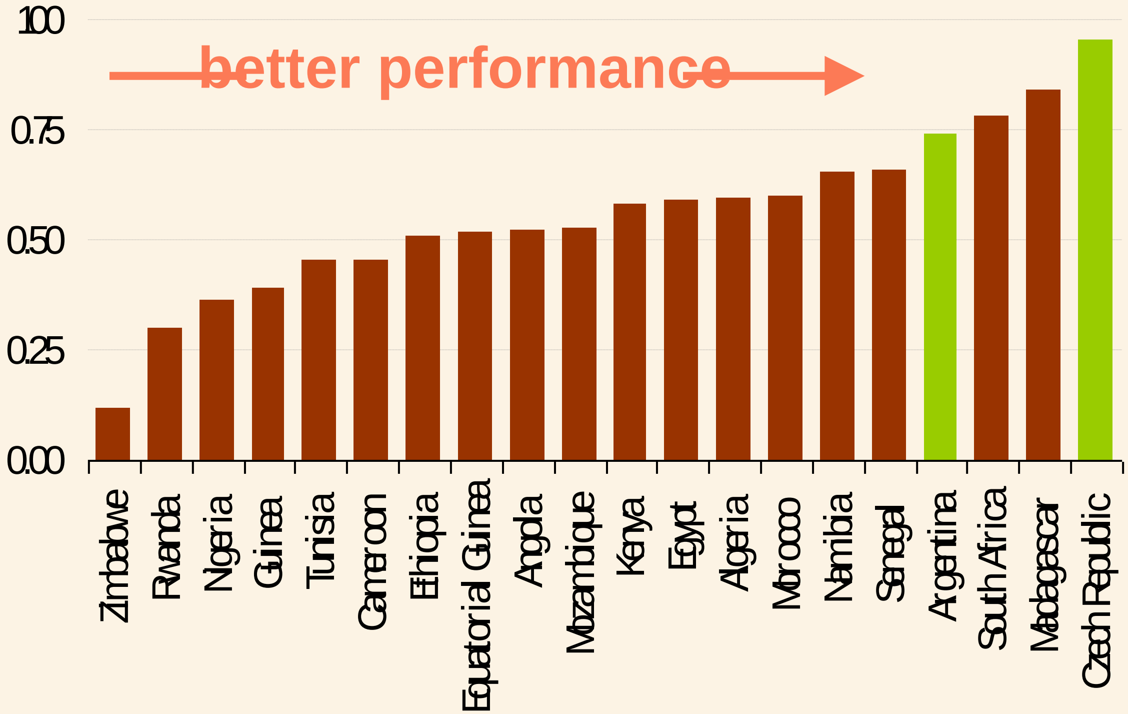
Key policy recommendations:

- Accelerate public administration reform
- Reduce and restructure the participation of the state in the economy
- Enact appropriate corporate governance legislation and enforce

Institutional Environment in Africa is Weak

SigmaBleyzer
Where Opportunities Emerge

Foreign Trade and Capital Flows



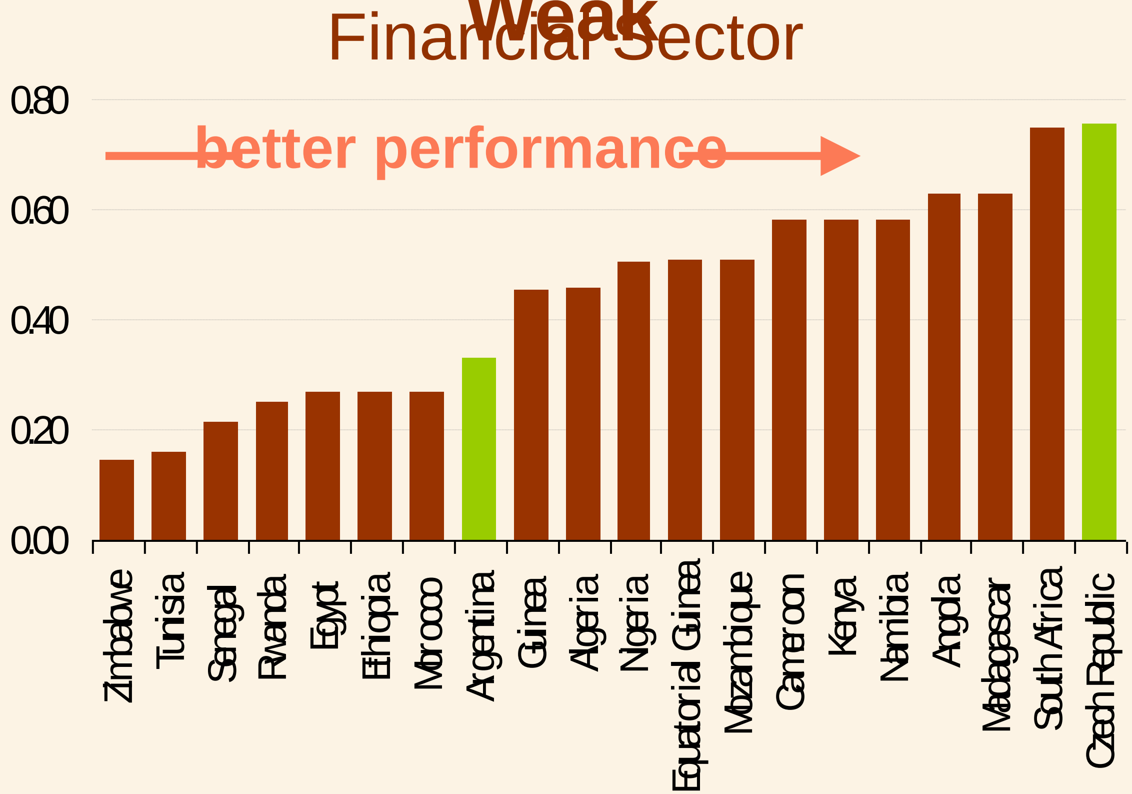
Source: World Bank, Doing Business 2007, Index of Economic Freedom 2006

Weighted average of trade policy index, capital flows restrictions index and "ease of trading across boarders" indicators

Key policy recommendations:

- Remove restrictions to exports and imports
- Simplify custom procedures and improve certification requirements and standards of products
- Liberalize foreign exchange markets cross-border capital flows

Institutional Environment in Africa is Weak



Source: World Bank, Doing Business 2007, Index of Economic Freedom 2006

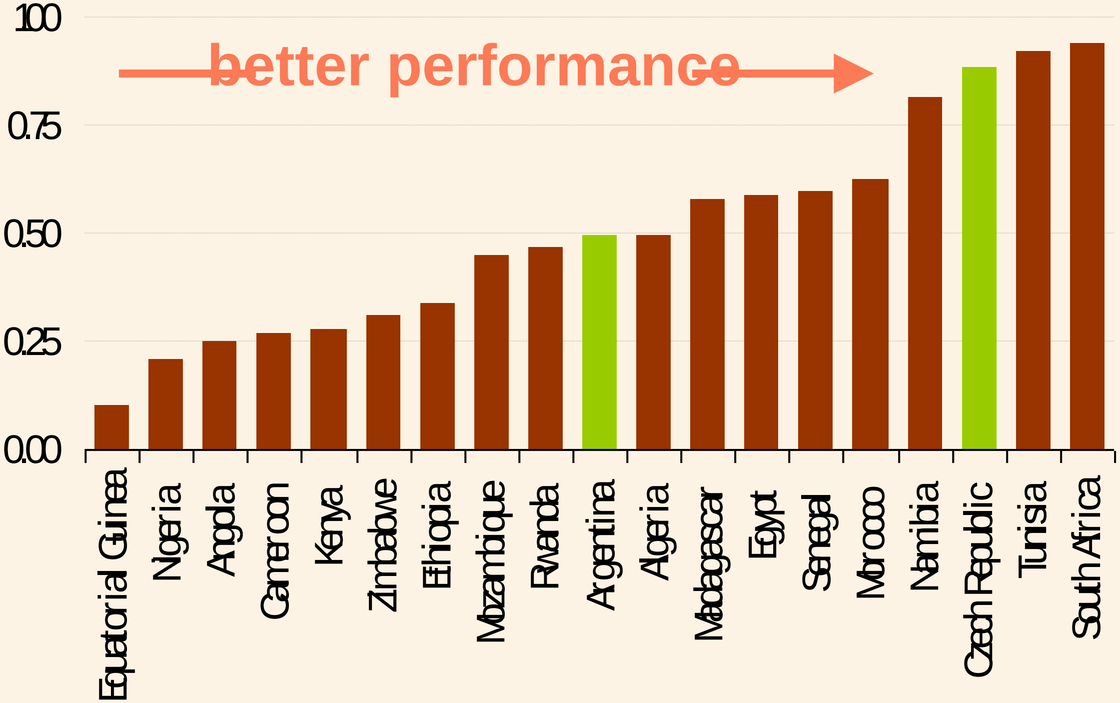
Weighted average of banking and finance index and "ease of getting credit" rank

Key policy recommendations:

- Increase the independence and autonomy of the Central Bank
- Improve bank supervision and enforce prudential regulations
- Encourage competition and efficiency in the financial sector by facilitating the expansion of foreign banks and non-bank financial institutions

Institutional Environment in Africa is Weak

Corruption Levels



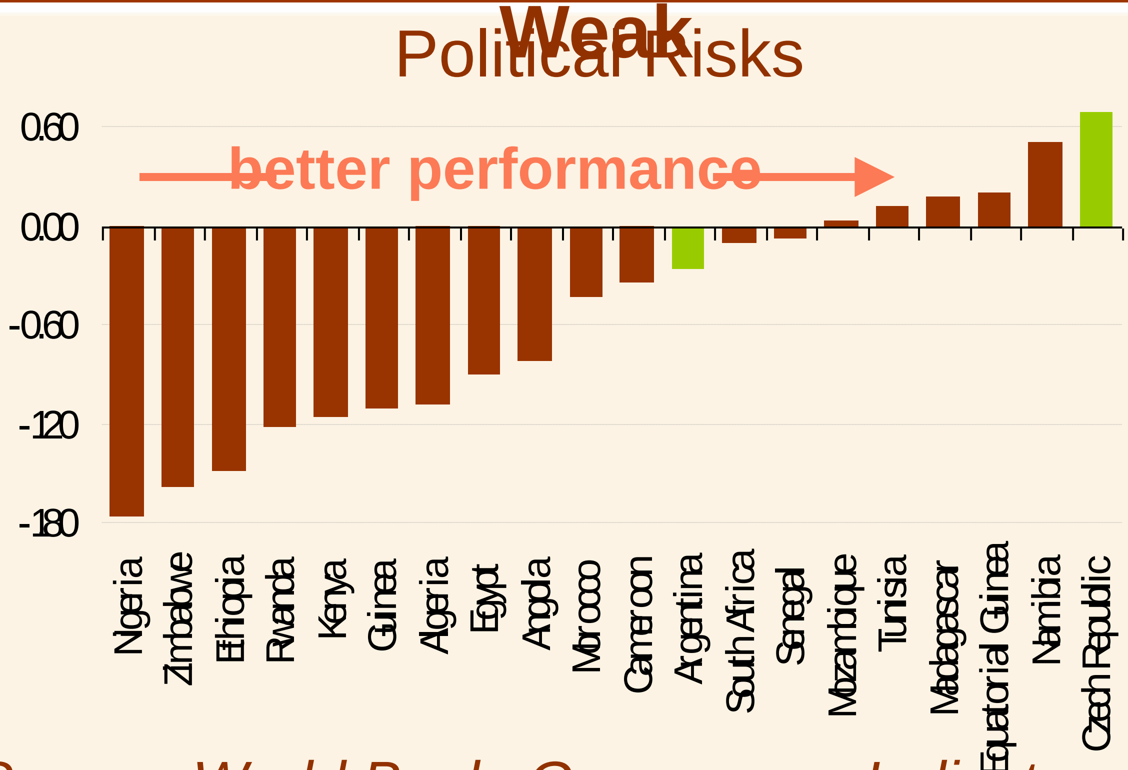
Source: World Bank, Governance Indicators (2006), Transparency International – Corruption Perception Index 2006

Weighted average of corruption perception index and control over corruption index

Key policy recommendations:

- Undertake measures to “prevent” corruption
- Develop the legal framework to ensure better enforcement of anticorruption measures
- Gain public support for anti-corruption programs

Institutional Environment in Africa is Weak



World bank: Political Stability Index

Source: World Bank, Governance Indicators (2006)

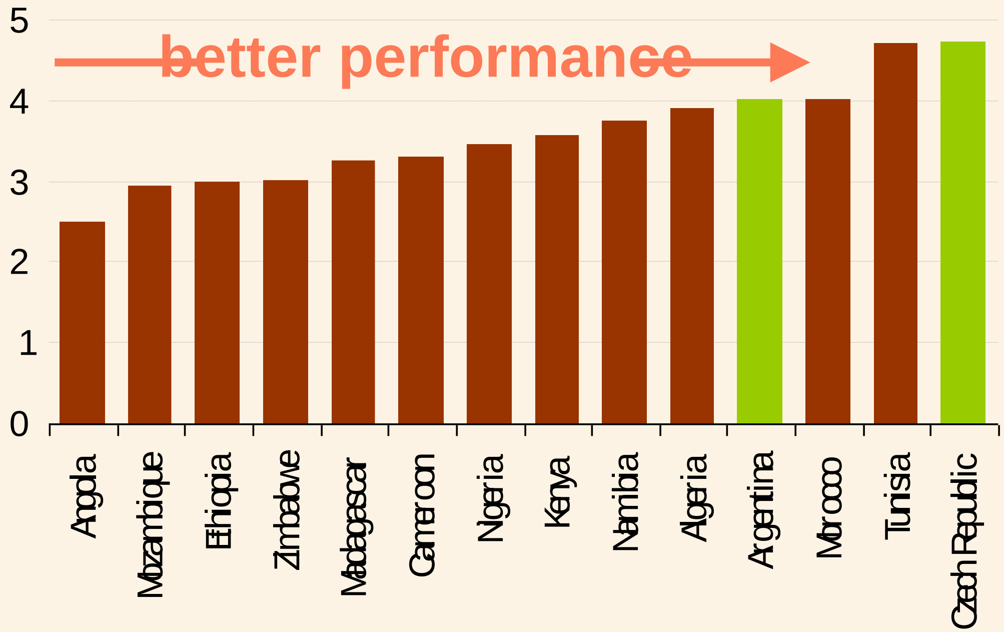
Key policy recommendations:

- Pass appropriate legislation to reassure investors that arbitrary expropriation of private property, including "creeping expropriation", will not be permitted in the country
- Provide Governmental stability
- Introduce strong measures to eliminate power abuses by the Government authorities

Institutional Environment in Africa is Weak

SigmaBleyzer
Where Opportunities Emerge

Country Promotion and Image



Source: World Economic Forum, Global Competitiveness Report 2006

Global Competitiveness Score

Key policy recommendations:

- Develop a comprehensive country promotion strategy
- Announce and disseminate widely the Government's policy and commitment to implement strong market oriented policies and show implementation progress
- Support foreign investment by changing the attitude of officialdom at central and local levels