

Appendixes

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Taking stock of ADB assistance for private sector development through public sector operations

Credit line operations

Traditionally, the Asian Development Bank's (ADB) assistance for private sector development has been through its public sector operations. Through Article 14 (i) of ADB's Charter,¹ ADB has been extending credit lines to selected state-owned and private financial intermediaries of its developing member countries (DMCs) through the government or with government guarantees specifically to support investments in productive private small- and medium-sized enterprises (SMEs). The credit lines were a quick and cost-effective mode for ADB assistance to these private enterprises, which otherwise may not have had any access to foreign exchange needed for investment. ADB has approved 110 credit lines totaling about \$4.4 billion for use by 65 intermediaries in 23 DMCs. These have benefited over 22,000 SMEs.

Experience with these operations was varied. Several ADB-assisted development finance institutions (DFIs) have developed into profitable, mature, strong, and diversified institutions that play important roles in their countries' economic progress. These include, for instance: China Development Corporation (Taipei,China); ICICI Ltd. (India); Korea Development Bank and Korea Long-Term Credit Bank (Republic of Korea); Development Bank of Singapore, and Industrial Finance Corporation of Thailand. At the same time, several other DFIs, particularly state-owned ones, have encountered major problems resulting from excessive state control and regulation of their lending policies and operations; directed lending to specified enterprises or target groups; major changes in official trade and investment policies affecting client performance; substantial depreciation of the local currencies resulting in large exchange losses that destabilize clients and, in turn, the intermediaries' own stability; inadequate capitalization that cannot withstand substantial portfolio losses; inefficiencies arising from lack of competitive motivation and institutional weaknesses; absence of effective prudential oversight; and failure to develop alternative

1 Asian Development Bank. 1995. Agreement Establishing the Asian Development Bank. Article 4, para.1.

sources of long-term funding. Many of these weak DFIs became virtually bankrupt. To keep ailing DFIs afloat, some governments have continued to sustain them with subsidized funding, straining limited budgetary resources. The credit line operations have clearly shown that ADB's focus on the intermediaries alone will not ensure viability. Success depends to a large extent on the policy, legal, and regulatory environment in which the intermediaries function. Even strong and mature institutions may fail if the policy and regulatory environment is not conducive to efficient performance. The focus in these operations is, therefore, increasingly on broader financial sector reforms and wider institutional policies as much as on the soundness and suitability of the intermediaries chosen to channel ADB funds.

Historically, the credit line operations relied largely on state-owned DFIs. Since the 1990s, a number of private financial intermediaries (including commercial banks and leasing companies) have been used to channel ADB funds under umbrella credit lines. This has led to expeditious and competitive use of ADB funds. Credit line operations have also (i) enhanced ADB's contributions to institutional enhancement, capacity building, and human resource development in the financial sector; and (ii) reinforced ADB's policy dialogue with DMC authorities on financial sector reforms and capital market development issues.

Enabling environment

A range of ADB interventions has focused on improving the policy, legal, institutional, and regulatory environment of the private sector in the DMCs. Through policy dialogue with DMC authorities, technical assistance (TA), and since 1987, program lending, ADB has encouraged and assisted DMCs in formulating and implementing reforms that promote private sector development by removing market distortions, strengthening domestic financial markets, and promoting good governance standards. Program loans, in particular, have been used to support policy and institutional reforms in the financial sector (India, Indonesia, Lao People's Democratic Republic [Lao PDR], Sri Lanka, Thailand, and Viet Nam), agriculture (Bangladesh, Lao PDR, Nepal, Pakistan, Papua New Guinea, Philippines, Samoa, and Sri Lanka); industry (Bangladesh, Mongolia, Nepal, and Pakistan), hydrocarbon (India), trade (Indonesia), and road transport (Philippines).

Cognizant of the DMC's stage of development, and the fact that most DMCs had weak markets overshadowed by public interference offering poor incentives to private investors, ADB has supported the creation of an enabling environment for private investment. ADB provided support aimed at stable macroeconomic management; investment, trade, and price decontrol; well-functioning financial and capital markets; flexible labor markets; good infrastructure; and a legal system protecting and enforcing contractual and property rights. Solid, but partial, progress has been achieved in most DMCs. With program lending playing a key role, investment deregulation has been the area of greatest success, as DMCs have opened up closed sectors to private investment, both local and foreign. ADB support has played a role in India, Lao PDR, Nepal, Pakistan, Philippines, and Viet Nam, where prices were partially decontrolled. Although ADB has not yet explicitly undertaken labor reforms, its efforts to reform public enterprises and deregulate investment have indirectly supported the introduction of flexibility in labor markets. ADB has also provided assistance for legal system reform.

Physical infrastructure

In the 1990s, ADB began to address the weaknesses of public agencies in key sectors. These weaknesses appeared to be rooted in the structural characteristics of public ownership, a persisting obstacle to improving sector management in the 1980s. Growing recognition was being given to the effectiveness of competition to achieve efficient management of sectors that had originally appeared to be natural monopolies, and to lower costs despite the economies of scale that appeared to support monopoly structures. Privatization of state-owned enterprises (SOEs) in the physical infrastructure sectors became a principal objective of ADB. In DMCs with underdeveloped markets or constraints derived from their political economies, SOE corporatization became the alternative means of improving the efficiency of sector management.

ADB efforts to support the Philippines install new power generating capacity through private sector participation have been hugely successful, ending the brownouts that were the main obstacle to the Philippines' efforts to improve its investment environment. The

thrust of ADB's efforts in privatization has been substantially to commercialize state-owned utilities, with notable success in People's Republic of China (PRC), Indonesia, Philippines, Sri Lanka, and Thailand, and with ongoing efforts with good potential for success in India, Lao PDR, and Viet Nam. An important lesson learned is that powerful vested interests frequently seek to subvert privatization to their own ends; transparency and competitive bidding are key elements of sound privatization, but are not easily secured.

ADB has also supported several DMCs' efforts to pursue an integrated approach to transport development, with a focus on the road subsector. ADB has helped DMCs privatize road subsector management through road construction and maintenance and through tollways, which are commercially viable only on a few road sections in several DMCs. ADB has made successful progress with road construction and maintenance in nearly all the DMCs in which it has been active in the sector. ADB has improved sector management by transferring it from government line ministries to autonomous road authorities. ADB continues to seek ways to improve the funding of road construction and maintenance—a key issue—as revenues generated through vehicle and fuel taxes are significant, but tend to accrue to the budget rather than to the sector.

ADB has also been utilizing TA to help DMC governments identify the scope of private sector participation in infrastructure development, and formulate appropriate policy and regulatory frameworks to facilitate private investment. In 1998, ADB approved a TA for the study of private sector participation in gas transmission in Bangladesh, and port development in the Maldives. ADB also funded a study, completed in 1998, in the PRC road subsector that concluded that, although construction risk is best left to the public sector, once traffic volume increases to a sufficient level, leasing or securitization is a feasible option for mobilizing private capital for the transport sector.

Financial sector

In parallel, recognition was also being given to the fact that if infrastructure services are properly priced, they can be self-financing in their capacity to generate capital and to service debt, and do not need to be financed by government. This strengthened the need to

develop strong markets to support the financing requirements of private sector-led growth. With this aim, ADB shifted its financial sector operations from a narrow focus on the resource needs of DFIs, to a broader effort of developing financial and capital markets in the DMCs. In support of this second objective to develop DMC financial markets, ADB undertook the following range of activities: recourse to market pricing of funds and introduction of competition among lenders to reduce funding costs; decontrol of lending to allow funds to move to activities offering the highest returns; introduction of market-based funding of public sector borrowings; widening the range of instruments mediating between savers and borrowers; strengthening public supervision of deregulated markets; and improving DMC access to global capital markets. Primarily through program lending, ADB has made good, but partial, progress in financial sector and capital market reform in India, Pakistan, Philippines, and Sri Lanka.

Agriculture sector

An important part of ADB's agenda in the 1990s was the commercialization of agricultural production, as most of the DMCs were subject to heavy public intervention in the sector during the 1970s and 1980s. These interventions consisted of support prices and input subsidies for producers, and price controls on items consumed by the poor. In most DMCs, the balance of subsidies provided adequate production incentives, which combined with technological innovation, led to Asia's green revolution. Poverty reduction provided the rationale to redistribute through subsidies. But, what resulted were distorted incentives, misallocated resources, escalating fiscal deficits, and the dead weight of public bureaucracies. ADB has attempted to undo this by providing assistance to dismantle complex state interventions to allow markets to determine input and output prices; open the market for agricultural produce and input supply to the private sector; and develop rural infrastructure with a substantial focus on farm-to-market roads, rather than input supply. ADB also promoted wider participation by beneficiaries, nongovernment organizations (NGOs), and the private sector in the design and implementation of ADB projects.

A complementary objective in commercializing the agriculture sector was to reduce or reform the role of public agencies. ADB provided support to eliminate the public sector's role in the marketing of inputs and outputs in favor of the private sector, and assisted in transferring the management of on-field irrigation systems to farmer groups. Given the weak markets inhibiting the private supply of rural credit, extension, and research, ADB strengthened public capacity in the delivery of these support services and in the management of irrigation and natural resources.

The most notable impacts on the commercialization of the agriculture sector were made in the transition economies in Indochina,¹ the Central Asian republics (CARs), and Bangladesh. Through program lending, which has influenced policy changes, ADB has helped to induce impressive increases in output and productivity in Bangladesh since 1992. ADB program and project loans that have supplemented International Monetary Fund-supported interest rate, exchange rate, and pricing reforms; and have helped Lao PDR and Viet Nam implement sector policies that have reversed years of stagnating agricultural output and increased rural incomes. Program loans have also begun to facilitate the CARs in their transition from collective to private farming, and privatization of plantations has made good progress in Sri Lanka.

ADB's record in improving the delivery of support services has been mixed. Its support for agricultural research in international agencies and in DMCs has generated high returns in terms of developing new technologies and applying them on the ground. However, its record on improving rural credit has been poor, with the exception of microcredit, which is a relatively newer initiative that has shown good initial results and holds promising potential, particularly in its role in the development of women. This is due, in large part, to the weak performance of agencies ADB supports to manage irrigation, forestry, and fisheries. These problems are rooted in the structural characteristics of public management and negligible budget support.

1 Indochina includes Cambodia, Lao PDR, and Viet Nam.

Social infrastructure sector

ADB has been partly successful in improving the management capacity of public agencies entrusted with the delivery of health and education. Where feasible, management has been entrusted to beneficiaries and NGOs, or contracted out to the private sector (e.g., maintenance of vehicles, construction, or accounting and billing). However, as the actual delivery of health and education services remains in the public sector, ADB has provided significant amounts of capacity building, principally through training, to address weaknesses in delivery. ADB is increasingly providing support to DMCs through program and project loans to assist them in shifting budget funds from sectors that are self-financing, such as physical infrastructure, to those that are not, primarily health and education.

In urban development, ADB has shifted from discrete financing of urban water supply systems to a more integrated approach encompassing the financing and management of urban development. This has included (i) delineating boundaries between urban and provincial or national authorities to separate responsibilities and establish accountabilities; (ii) financing frameworks that facilitate revenue collection, revenue sharing, and cost recovery, and allow the development of borrowing capacity and self-financing municipal budgets; (iii) contracting out municipal services and privatization where possible (e.g., ADB-supported privatization of Manila and Colombo water supply); and (iv) capacity building of municipal bodies. These issues have recently become part of ADB's policy agenda.

Postcrisis assistance

Following the Asian financial crisis, ADB has taken significant measures to help its crisis-affected DMCs. In 1998, to help Indonesia strengthen its financial sector and assure a sustainable flow of resources to the private sector, ADB approved a \$1.5 billion loan to support reforms of governance in the financial sector to assist in sector restructuring, and to restore its ability to effectively mobilize and efficiently allocate resources for investment. With physical infrastructure bottlenecks constraining growth, ADB has been helping DMC governments encourage private sector participation in the

provision of physical infrastructure services. ADB approved a \$300 million loan to the Philippines for a power sector restructuring and privatization program, designed to transfer ownership of power generation to the private sector.

Catalyst for information

ADB has played a pivotal role as an intermediary and catalyst of information flows. ADB sponsored a regional workshop in Manila in December 1998 that brought together government officials, bankers, and private sector developers to discuss best practices for promoting private investment in power, ports, airports, expressways, and water supply development.

Regional and subregional cooperation

ADB has played a significant role in the emergence of several initiatives aimed at regional cooperation. It nurtured and sustained the effort, launched in 1992, of six countries in the Greater Mekong Subregion to develop norms of cooperation that have now reached the level of preparation of specific subregional projects in transport and energy, with the participation of the private sector. Two other subregional groupings (Indonesia-Malaysia-Thailand, and Brunei Darussalam-Indonesia-Malaysia-Philippines) have requested ADB assistance to prepare subregional growth centers. More recently, the South Asia Growth Quadrangle (Bangladesh, Bhutan, India, and Nepal) has asked for ADB assistance, and ADB has already undertaken a similar initiative in the CARs.

Good governance

Although ADB formally adopted good governance as a development objective only in 1995, sector level governance interventions have formed part of its operations since its inception. These have focused mainly on the governance dimensions of private sector development and public sector reform, but good governance comprises key elements that cut across sectors and require a macro framework approach: public administration, public finance management, subnational governance, and development of sound judicial and audit frameworks. In the past two years, ADB has initiated work in all these

areas in several DMCs, and will continue to do so, with the additional element of improving information technology.

Commercial cofinancing

Commercial cofinancing (i.e., private capital) has been mobilized for public sector institutions. In the Philippines, for example, ADB used its partial credit guarantee to enable the National Power Corporation to tap the Japanese capital market for 20-year yen financing. In addition to facilitating capital market development in the Philippines, this transaction helped the corporation increase its exposure to market-based sources of financing. Commercial cofinanciers typically require adherence to agreed financial ratios, generally accepted accounting principles, and other market-related requirements. The financial discipline associated with commercial cofinancing complements financial reforms in public sector institutions. In addition, the involvement of private capital through commercial cofinancing can help set the stage for successful restructuring and/or privatization efforts.

Lessons learned

A lesson learned for the use of credit lines, both in relation to the financial intermediaries and assisted private enterprises, is that the right policy, legal, and regulatory environment, and good governance are vital for effective functioning. While ADB has helped DMCs address the enabling environment, the Asian crisis showed that concerted efforts are required by DMCs and, in turn, by ADB. This underlies ADB's rationale in reducing its DFI lending in the 1990s, as most DFIs were inextricably linked to public interference in resource allocation. ADB support for employment-generating investment has shifted to creating an enabling environment for market-based financing, rather than directly providing investment funds, to promote more inclusive and sustainable growth toward the ultimate goal of poverty reduction.

The rise in economic growth rates in Asia, up to the financial crisis, was the most important event of the 1990s. The market-driven and private sector-oriented framework that enabled this transformation was mostly put in place by the DMCs themselves. However, many DMCs turned to ADB for assistance, notably in South Asia, the

transitional economies, and the Philippines. In these cases, ADB can claim credit for successful efforts in this area. ADB's efforts in the Pacific DMCs were less fruitful, as structural constraints remain difficult to overcome in these small states. In the Pacific DMCs, ADB assistance has shifted to improved aid coordination, rather than additional aid, with a focus on supporting policy frameworks and private investment.

ADB has used several approaches to reduce poverty. The first was to consider how to relate growth-oriented projects. Growth is the single most important contributor to poverty reduction; increasing employment and access of the poor to productive resources are recognized tools to this end. However, ADB has learned that growth in the DMCs must be labor intensive. One of the most crucial comparative advantages of ADB's DMCs lies in their inexpensive labor forces. Policies that have facilitated labor-intensive, rather than capital-intensive, production have been the key to generating real employment, typically in industrial and service SMEs and through foreign direct investment. ADB is keeping these lessons in mind and bringing them to bear in establishing links between its growth, led by the private sector, and poverty reduction objectives.

A third lesson learned is that ADB's public and private sector windows should have worked more closely together to increase benefits to the DMCs, and optimize development impacts. Public sector assistance pay systematic attention to private sector interests and concerns. ADB will draw on this experience in reviewing its approach to private sector development.

Private sector activities of other multilateral agencies

The World Bank Group

World Bank (WB)

Support by the World Bank Group—The World Bank (WB), International Finance Corporation (IFC), and Multilateral Guarantee Agency (MIGA)—for private sector development to promote growth and efficiency, and thereby to reduce poverty, has undergone substantial evolution. Early project lending focused on creating the infrastructure base to complement industrial and agricultural development. Adjustment lending in the 1980s expanded the focus by working to establish a macroeconomic framework for private sector development and appropriate relative prices. Since 1989, a strategy has been incorporated that focuses on improving the business environment, restructuring the public sector and supporting privatization, and reforming and developing the financial sector in developing countries. Together, the components of this strategy are helping to nurture a healthy private sector, a prerequisite for attracting private capital flows.

Efforts to improve the business environment focus on necessary policy, regulatory, and legal reforms. These activities have an increasingly sharper focus through a program of private sector assessments, initiated in fiscal year 1992 and carried out in conjunction with IFC.

Promotion of public sector restructuring has tended to focus on trimming overextended public sectors and supporting privatization of state-owned enterprises (SOEs) and private sector delivery of public services. However, the focus has shifted to complement privatization with efforts to upgrade areas of public administration that have the potential to profoundly affect the growth and efficiency of the private sector: tax and customs administration, trade and investment promotion, enterprise-support services, court administration, and infrastructure planning and provision. WB is also involved with issues relating to the importance of transparency, dealing with the potential direct social costs of privatization, and establishing a postprivatization environment that stimulates competition, promotes equity, and inhibits avoidable concentrations of ownership and economic power.

WB provides support for the private provision of infrastructure, focusing on (i) privatization of public utilities; (ii) development of regulatory frameworks to provide appropriate mechanisms for pricing privately delivered infrastructure services, encouraging competition and, where appropriate, removing barriers to entry; and (iii) provision of WB financing or partial guarantees to attract additional private capital for infrastructure projects.

In the financial sector, WB focuses on creating the appropriate legal, regulatory, and supervisory structures to realize the full benefits of financial sector reform. WB emphasizes the need for policy reform in conjunction with macroeconomic reform, improvements in the financial infrastructure, and strengthening of specific financial institutions.

WB is improving its capacity to support governments design and implement private sector development reforms by understanding the dynamics of the environment affecting private sector development and devising ways to eliminate or work around obstacles to implementation; forging links between various local institutions critical to private sector development to build capacity so that local institutions can deepen and sustain progress initiated through WB; and learn from successful country experiences internationally, and tailor these to a specific country's needs.

In recent years, WB's efforts to support private sector development have accelerated rapidly. Typically, about two thirds of all WB operations include components that explicitly support private sector development. WB has a vice president under who a critical mass of highly competent professionals has been assembled to provide technical support for financial and private sector development, and the industry and energy sectors. WB has also initiated major efforts to promote small- and medium-sized enterprises (SMEs) and the entrepreneurial role of women, encouraging the private sector in the poorest of developing countries and supporting the necessary underpinnings of public sector reform.

Recently, WB started reaching out to, and conducting dialogue with, multinational corporations (MNCs) in an effort to promote private enterprise in developing countries. WB has noted that in many countries where it operates, the industry sector consists mainly of

export-oriented enterprises, such as textiles and electronics, over which the host country has little influence on market and production decisions: the MNCs are in control. Without this dialogue with MNCs, multilateral development banks run the risk of providing incorrect advice if they do not understand the decision-making processes of multinationals.

WB and IFC recently began working together to create synergies. They are undergoing an organizational change at the corporate level and a merger of offices is being orchestrated in the field. Colocation of offices has already been accomplished in a number of countries to better coordinate IFC and WB efforts in private sector development. There has been a recent merger of the positions of the WB country director with the IFC resident representative. In a recent move to increase its presence and operations in the Asian region, a joint WB-IFC regional office is being established in Singapore.

International Finance Corporation (IFC)

IFC was established in 1956 as a member of the World Bank Group. It is a legally and financially independent multilateral agency that fosters economic growth by promoting private sector investment in its developing member countries (DMCs). IFC combines aspects of a multilateral development bank with that of a private merchant bank. In its project financing, IFC provides loans without government guarantees, makes equity investments, and seeks to mobilize additional project funding from other investors and lenders through loan syndications, parallel financing, and guarantees. IFC prices its financing and other services in line with the market, and seeks profitable returns. In addition, IFC sponsors and funds selected financial intermediaries.

IFC offers a range of advisory services and technical assistance (TA) in such areas as capital market development, corporate restructuring, risk management, and project preparation and evaluation, and advises member governments on creating an environment that encourages the growth of private enterprise and foreign investment. IFC maintains an emerging markets database, functions as an adviser to several projects that it finances, and frequently joins large MNCs and leading DMC business groups in its operations.

IFC's general policy guidelines are quite similar to and, in some respects, identical with those of ADB for direct private sector financing. IFC views development, not profits, as its primary goal. But, it sees the aim of profitability as consistent with the development objective and not in conflict with it. IFC seeks to strike a proper balance between its profitability and risk-taking in its investment activities. It makes a major contribution to development when its involvement makes a critical difference to investors intending to proceed with large investments that have an important impact on a country's economy. IFC tries to ensure that its participation makes a special contribution that supplements or complements the role of market operators.

IFC has been quite active in private sector financing in Asia, aided by its representative offices in Bangkok, Beijing, Islamabad, Jakarta, Manila, and New Delhi, and now by the newly opened joint IFC-WB office in Singapore. IFC's assistance to projects in Asia covers a wide range of industry and infrastructure sectors. It has financed projects in the oil refining, petrochemical, cement, textile, automobile, electronics, and agro-processing industries, as well as in energy, transport, telecommunications, tourism, and health. Some of these projects have been jointly financed by ADB. IFC has also supported several financial intermediaries in commercial banking, leasing, and housing finance. As part of its Foreign Investment Advisory Services program, IFC has provided advice on investment policy and procedural aspects to several Asian countries, including Bangladesh, People's Republic of China (PRC), India, Lao People's Democratic Republic (Lao PDR), Malaysia, Mongolia, Nepal, Philippines, Sri Lanka, Thailand, and Viet Nam. In addition, IFC has been providing advice on corporate financial restructuring and on privatization. To help entrepreneurs in the region's smaller economies establish new businesses or expand and diversify existing ones, IFC has established a South Pacific Project Facility based in Australia.

In the past, IFC focused mainly on sectors rather than on countries. This is, however, beginning to change as the planning exercise is now being driven by country considerations. However, when a project is cleared for processing, the concerned sector department takes the lead and drives the process. IFC's strategy currently focuses on three areas: (i) key sectors that were originally in the public sector but are

now moving to the private sector, i.e., infrastructure, oil and gas, transport, utilities, and education; (ii) financial sector, with emphasis on domestic financial market development; and (iii) SMEs. In its work to support SMEs, IFC has established a business advisory unit that provides capacity building and advice on producing viable business plans as well as accounting, financial, and credit analyses, and risk assessment skills to help SMEs and start-ups in their operations.

IFC used to prepare country assistance strategies (CAS) separately from WB. Currently, the IFC works closely with WB to prepare joint country strategies, particularly for activities in capital market development, foreign direct investment (FDI) promotion, and SME development. This has been institutionalized in the sense that the Board is aware of the process. For countries classified as high priority due to IFC's large investment program or where significant opportunities have been identified, IFC prepares a detailed private sector strategy as an annex to the CAS to supplement what is included in the text. There are 20 such countries. For lower-priority countries, the private sector strategy will only be included in the text. For countries classified as hostile to the private sector, IFC does not participate in the CAS. IFC signs off on the CAS and the Board presentation is done jointly.

To facilitate a division of labor and to prevent a conflict of interest on the advisory side, IFC will normally provide advisory services on issues such as FDI or regulatory frameworks, whereas WB advises on policy issues. IFC discloses its investments in projects so host governments are fully aware of the dual role played by IFC. In case of jeopardy, if IFC is a lender and/or investor, it acts as representative of other investors and lenders, whereas WB would advise on policy issues. This is where the "firewall" must be put up between the two entities to prevent a serious conflict of interest.

For the guarantee instrument, WB's guarantee program has not been used extensively, but IFC has issued \$100 million as guarantees. To mitigate risks, IFC shares guarantees with the local banks, and the local banks price the loan based on the percentage IFC is guaranteeing.

Multilateral Investment Guarantee Agency (MIGA)

MIGA was established in 1988 to reduce poverty through FDI to and among DMCs, by offering political risk investment insurance coverage

to private investors, and providing promotional and advisory services to help its DMCs attract and retain FDI. MIGA estimates that 55 out of 1,400 projects are submitted to their Board, and of the 1,400 projects received annually worldwide, 400 are from Asia. Twenty percent of MIGA's portfolio comes from Asia. Projects have been guaranteed in Bangladesh, PRC, and Pakistan. A constraint faced by MIGA in doing more work in Asia is the fact that some of their host countries are not MIGA members, e.g., Cambodia and Thailand.

MIGA recently raised its capital to \$2 billion, its project limits to \$200 million (project size of up to \$1 billion) and country limits to \$620 million. In 1998, it provided 73 guarantees worth \$1.3 billion, mainly to power projects, charging 50 to 150 basis points. MIGA has issued 60 guarantees related to infrastructure projects. High investor confidence in the past made obtaining political risk insurance for war or insurgency a low priority. The trend, however, has reversed. Most of the policies underwritten by MIGA provide coverage to investors in the event of war in the host country.

MIGA would like to collaborate with ADB in the following areas: (i) providing guarantees to projects where ADB is an investor; (ii) coinsuring in ADB projects with ADB; and (iii) relying on ADB's due diligence on projects that MIGA insures, as similar standards (e.g., environmental and labor) set by ADB are also required by MIGA.

Inter-American Development Bank

The Inter-American Development Bank (IDB) has traditionally followed policies similar to those of WB for private sector development. In recent years, private sector development has begun to occupy a more prominent position in its activities. IDB has set up the Inter-American Investment Corporation (IIC) to support SMEs in Latin America and the Caribbean with loans, guarantees, and equity investments. IDB also administers the Multilateral Investment Fund (MIF), which was established in January 1993 to finance programs for policy change, training, and improved access to credit to help member countries strengthen their private sectors. The MIF consists of a technical cooperation facility that helps identify and implement policy changes to promote the private sector, a human resources facility that helps retrain displaced workers and strengthen worker productivity, and a

small enterprise development facility that helps broaden economic participation by the poor, women, and minorities.

Over several years, IDB has made a conscious effort to promote institutional change in mindset and work processes. This has resulted in much closer collaboration between its public and private sector departments to successfully develop private sector projects in its DMCs. IDB established a management review process whereby justification must be made systematically as to why the private sector is not participating in a public sector project. This review process is proving to be an incentive for the public sector departments to coordinate with the private sector departments to identify projects that have the potential of being undertaken and/or funded by the private sector.

To facilitate the coordination of activities for private sector development, the president of IDB created a private sector coordination committee. The committee is comprised of the vice president and individuals from MIF, IIC, the Private Sector Department, and the Legal Department. The key to the committee's success relies on agreements in internal processes.

To promote the development of the private sector, during its eighth replenishment in 1994, IDB raised its private lending limit from 5 percent of annual lending commitment to 10 percent. Project limits were also increased to \$75 million or 25 percent of total project cost, except for smaller countries where a limit of up to 40 percent of project cost applies.

Inter-American Investment Corporation

The Inter-American Investment Corporation (IIC) is a multilateral investment corporation that promotes the economic development of its regional member countries by stimulating the establishment, expansion, and modernization of private SMEs in the Latin American and Caribbean region. IIC began operations in 1989 with subscribed capital of \$200 million; this was recently increased to \$700 million. IIC provides long-term loans and guarantees to, and makes equity investments in, private enterprises that have difficulty raising finance from other sources on reasonable terms. It provides lines of credit to financial intermediaries. By Charter, IIC can only provide corporate

lending or project financing; it is prohibited from accepting sovereign guarantees. IIC mobilizes additional capital for assisted projects through syndication and underwriting operations, by identifying joint venture partners and facilitating transfer of technology. IIC also provides fee-based advisory services to private firms and advisory services to member governments on their investment policies, and assists them in privatizing SOEs, particularly those of medium size.

IIC supports projects that, in addition to providing potentially profitable investment opportunities, have a development impact on the host countries. Particular attention is paid to mitigating adverse environmental impacts. IIC is currently developing a new product—an agency line of credit—that will enable them to lend directly to a project sponsor with a financial institution counterpart. The risk will be borne by IIC and the financial institution to the extent of their respective exposures.

European Bank for Reconstruction and Development

The European Bank for Reconstruction and Development (EBRD) was established in 1991 with a unique mandate to foster the transition to open market economies and to promote private and entrepreneurial initiatives in the Central and Eastern European countries committed to, and applying, the principles of multiparty democracy, pluralism, and market economics, thereby assisting their economies to integrate into the international economy. EBRD seeks to help the countries where it operates to establish the framework of a market economy, implement restructuring and privatization, create modern infrastructure, strengthen financial institutions and legal systems, and develop the local private sector. EBRD has 55 members, and like ADB enjoys a strong triple-A credit rating that reflects its strong capital level and membership, and conservative fiscal policies.

EBRD has merged its merchant banking with its development banking. Not less than 60 percent of its funding is to be directed to private enterprises and/or SOEs that are implementing programs to achieve private ownership and control. Not more than 40 percent of EBRD's funding is to go into public infrastructure and other projects. In reality, 85 percent of EBRD's operations benefit the private sector directly or indirectly, but 50 percent of these deals involve government

risk. In all its projects, EBRD must follow three principles: transition impact, sound banking and investment, and additionality.

EBRD's Banking Unit is organized into six business groups, three of which are country groups and the other three sector groups. The country groups include (i) the Russia Federation and the Central Asian republics (CARs), (ii) Central Europe, and (iii) South and Southeast Europe, and the Caucasus. The sector groups include financial institutions, infrastructure, and industry and commerce. The sector groups normally take the lead and, currently, are lending 80 percent of the business, but there is an effort to push more business to the country groups. The country groups take care of sectors not covered by the sector groups, but overall, a country team approach is used. EBRD does not do programming work with governments as ADB does, and they also do not do advisory work.

Currently, their strategy is to focus on the following: (i) supporting banks and other financial institutions that have an institutional commitment to SMEs; (ii) providing a full range of financing structures in infrastructure operations including private, sovereign, subsovereign, and public-private partnerships; (iii) supporting the restructuring of potentially viable large enterprises, by carefully selecting a few projects that have a strong demonstration effect; (iv) continuing equity investments; and (v) promoting a sound investment climate and strengthening institutions that are important for the functioning of markets, by working closely with its foreign investment advisory councils.

EBRD's Risk Management Unit is located outside of the Banking Unit. The Risk Management Unit is responsible for reviewing every transaction, and signs off on all private sector projects. The Operations Committee helps coordinate the country and sector groups. In its project work, both the concerned country and sector groups get full credit regardless of which group originates or leads the deal. This provides an incentive for the country and sector teams to work together. The Operations Committee is cochaired by the vice president and deputy vice president of the Banking Unit, and is comprised of the head of finance, the chief economist (who ensures the transition impact), the general counsel, and the head of risk management.

EBRD is doing work with municipalities, given the trend toward decentralization of governments. They treat the municipality as a nonsovereign entity, i.e., a private sector entity, as a municipality does have its own sources of funding and does not depend solely on government transfers. An important criteria adhered to by EBRD is that all of its projects must be self-sustaining and, over time, the project revenues must be able to service the debt.

Scorecards Concepts

Private Sector Operations: A Scorecard for Greater Development Impact

A scorecard can “score” all prospective private sector projects against a set of development impacts desired in the developing member countries (DMCs). These development objectives will be defined in terms of the Asian Development Bank's (ADB's) strategic development and private sector development objectives. ADB-assisted private sector projects should have development impacts as defined by these objectives. Table A3.1 presents a conceptual illustration of the scorecard concept, using ADB's existing private sector projects as examples. Further refinement and elaboration will be needed to implement such an approach.

The scorecard will enable ADB to strengthen the development focus of its private sector operations because it will have defined upfront what the objectives of these operations are.

Table A3.1: Scorecard for Development Impact of Private Sector Projects (An Illustration)

Country	Project	Development Impact Areas									
		Poverty Reduction through Growth	Environment Protection	Subregional Cooperation	Infrastructure Improvement	Capital Market Development	Better Banking	More Competitive Sector	Opening to Foreign Direct Investment	Good Governance	Forex Saving/Earning Initiative
BAN	La Farge Surma Cement	■	■	■	■				■	■	■
PRC	Everbright Bank	■					■	■	■	■	
PHI	Maynilad Water Services	■	■		■			■	■		
THA	Eastern Power	■	■		■	■		■	■	■	

Public Sector Operations: A Scorecard for Greater Private Sector Development Effect

A scorecard can also be developed to track the contributions of ADB's public sector projects to private sector development, where public sector loans help to create enabling conditions or generate investment opportunities for the private sector (*Table A3.2*).

Table A3.2: Scorecard for Private Sector Development Effects of Public Sector Projects (An Illustration)

Country	Project	Private Sector Development Effects							
		Create Enabling Environment	Build Regulatory Capacity	Promote Effective Governance	Facilitate Financing	Develop Capital Markets	Provide Support Infrastructure	Generate Investment Opportunities	Commercial Cofinancing
IND	Private Sector Infrastructure Facility			█	█	█	█		
PHI	Power Sector Restructuring	█	█	█			█	█	
THA	Export Financing Facility	█		█	█				█