



**DEVELOPMENT CO-OPERATION DIRECTORATE
DEVELOPMENT ASSISTANCE COMMITTEE**

DCD/DAC/POVNET/A(2003)2/RD3
For Official Use

DAC Network on Poverty Reduction

PROJECT ON THE SYNERGIES BETWEEN ODA AND FDI

(Note by the Secretariat)

OECD - Paris, 13-14 November 2003

This paper is the Secretariat's first draft of an operational proposal requested by CIME's Working Party. The Working Party has not yet seen the paper or provided inputs into the drafting process. The paper is tabled for the INFORMATION and COMMENTS of the Poverty Network.

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**PROJECT ON THE SYNERGIES BETWEEN ODA AND FDI:
DRAFT NOTE BY THE SECRETARIAT¹**

1. The Monterrey Consensus, adopted in March 2002, strengthens support for policies within developing countries to mobilise domestic resources and attract private investment, and for utilising aid effectively. The developing countries committed in Monterrey to implementing sound economic policies, tackling corruption, putting in place good governance, investing in their people, and establishing a favourable investment climate to attract private capital. In turn, the international community committed to scale up and intensify their efforts to help developing countries meet the internationally-agreed development goals by, among others, improving synergies between official development assistance (ODA) and foreign direct investment (FDI).

2. The use of ODA to maximise the benefits of private investment is considered a key home country responsibility in terms of enhancing the development of infrastructure, human resources and institutional capacity in the developing host countries, whose FDI absorption capacity is weak. At the May 2003 OECD Ministerial there was broad support for a proposal from Japan for additional work on a strategy to promote investment in developing countries. One element of this proposal was strengthening coordination between ODA and FDI.

3. At its meeting in September 2003, CIME's Working Party on the Declaration endorsed a proposal to undertake a project along these lines [DAFFE/IME/WPD(2005)5]. The Working Party expressed its preferences regarding the general direction of the project. It also expressed a desire to cooperate closely with OECD's development policy community and other interested parties throughout the course of the project. The Working Party asked the Secretariat to prepare an operational proposal for approval at its meeting in December. The present paper was produced in response to this request.

I. Directions of the project

4. The Working Party's main directions to the Secretariat at its meeting in September – which were further supported by CIME's consultations with BIAC, TUAC and civil society – can be summarised as follows:

- The project is not merely about the impact of ODA on FDI. It will focus on *synergies*, by which is meant a two-way process that allows FDI to amplify the effects of ODA, and ODA to amplify the effects of FDI.
- The usefulness of FDI in the development context is not limited to attracting investors. Similar weight must be given to analysing policy approaches to *maximising the benefits* of investment. (This orientation is consistent with ongoing intra-OECD cooperation on MNE/SME linkages in the context of the Bologna process.)

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- FDI/ODA linkages must be analysed in the context of *sustainable development* (i.e. including economic, environmental and social effects).
- Developing *policy recommendations* is not the priority of the early phases of the project. The initial focus will be on pulling together already available information and engaging non-Members and other stakeholders in an inclusive dialogue. Policy lessons could emerge as the project matures.

5. The document discussed by the Working Party in September 2003 put forward a large number of topics that could be potentially covered by the ODA/FDI synergies project. The Working Party expressed its preference for the following two subject areas:

- *Employing ODA to enhance the enabling environment for investment.* The elements of a society or economy that are of importance to the enabling environment for investment are legion, so a certain amount of pruning is necessary. The ODA/FDI project will focus on the following three aspects:
 - *Governance.* Improving corporate and public governance in developing countries is becoming a key objective of (and, increasingly, a conditionality in) ODA policies. The quality of governance also ranks consistently as one of investors' top concerns about investing in developing nations. Hence, important synergies between ODA and FDI can be obtained when ODA-backed governance improvements take into account the needs of investors (whether domestic or foreign).
 - *Human capital and entrepreneurship.* A recurrent problem with attracting FDI to developing countries is the absence of manpower with the relevant skills, or, where this hurdle has been overcome, investors' fear that skills shortages will be an obstacle to future expansion. ODA can be employed to redress skill lacunae, and to foster longer-term co-operation between enterprises, social partners and local society aimed at identifying and meeting future human capital needs.
 - *Infrastructure and utilities.* Inadequate or absent infrastructure is one of the key impediments to FDI and sustainable development. ODA-backed schemes to provide transportation, water, energy and telecommunication are needed not only for their immediate effect on the health and quality of life of individuals, but to improve competitiveness and opportunities for economic growth. A special role for infrastructure investment relates to the regional dimension of economic development. In many small and poor countries, cross-border transportation networks are key to reaching a market size that is sufficient to attract investors.
- *ODA-backed public-private partnerships.* PPPs seek to create a framework in which public and private actors can bring their distinctive competences to a project while also ensuring a transparent and fair allocation of the project's risks and returns. In this context, investment projects that lack sufficient commercial viability can be carried out in the form of partnerships in which a subsidy is provided by the public purse – or by donors of development assistance. Recent examples include the provision of utilities services to poor neighbourhoods in developing countries through foreign-invested commercial entities, using ODA to subsidise the services to make them affordable to the local residents.

II. How to proceed?

6. Under the assumption that sufficient voluntary contributions will be made available, the intention is to apply a broadly based strategy, bringing together the knowledge of outside experts, OECD committees, Member and non-Member policy makers, other international organisations and representatives of OECD's social partners and civil society. The approach will be three-pronged: first, experts will be asked to provide an in-depth analysis that will act as the starting point for discussions; thereafter, the enhanced outreach mechanism established as part of the Strategy on Investment for Development will be used to engage non-Member countries in a dialogue about the developing country perspective on the issues; and at the same time CIME and OECD's development policy community (e.g. DAC/DCD and the Development Centre) and other interested parties will be invited to take the analysis forward, contributing their perspective, discussing the feedback from the non-Member consultations and, as appropriate, contribute supplementary material.

7. The project could involve the following main elements and deadlines:

- Early 2004 an informal workshop will be organised, involving experts from all the relevant policy communities (investment and development policy, environment and other interested parties) to discuss how to shape the project and conduct it with a view to maximising its benefits throughout the organisation.
- Four consultants are commissioned to write substantive analytic papers covering the main building blocks of the project (ODA-based upgrading of governance, human capital and infrastructure; ODA-backed public-private partnerships). Their reports will provide a body of evidence summarising the experiences of donor agencies, multilateral development institutions and host countries. This work will take place in the first half of 2004.
- The consultant reports will be made subject to a peer review within a group comprising the authors and experts drawn from OECD's investment and development communities, other international organisations, non-Member representatives, the social partners and civil society. The probable venue will be an event organised back-to-back with CIME's meeting in September 2004.
- In parallel with the consultants' work, a series of consultations with non-Member countries will be undertaken throughout 2004 and in early 2005. The main venues will be meetings organised in the broader context of the Strategy on Investment for Development, including the nascent regional investment forums. As the work progresses, one or two events could also, financial resources permitting, be dedicated to discuss the outcome of the project with developing countries.
- From mid-2004 onward extensive consultations with OECD's development community and other international organisations are foreseen. These will be invited to bring to the attention of CIME any information on ODA/FDI linkages that they feel is insufficiently represented in the consultants' reports, and as appropriate undertake supplementary or complementary analysis of the main topics of the ODA/FDI project and beyond. Joint meetings between CIME and relevant other bodies could be organised to discuss the final shape of the project's tangible output.
- At its meeting in December 2004, CIME will consider a draft background report, summarising the findings of the consultants' work, the consultations with non-Member countries and the joint work with other bodies. The document will attempt to synthesise recent experiences with ODA/FDI linkages within the areas selected by the Working Party.

- At its meeting in April 2005, CIME will be invited to consider a set of draft policy conclusions based on the background report, and on the discussions at the December 2004 meeting. As appropriate, the conclusions could take the form of a policy guidance for optimising ODA/FDI synergies.
- The final policy conclusions will be presented to the 2005 OECD Ministerial meeting.

III. Intra-OECD cooperation

8. Extensive co-operation will be sought with the Development Assistance Committee and full use would be made of work that has already been done under the aegis of this Committee. In this context, relevant parts of the OECD Secretariat (e.g. Development Cooperation Directorate, Development Centre) will be invited to comment and contribute throughout the duration of the process. In the early phases of the project, these bodies' inputs will for instance be sought in choosing consultants and determining their remit, and they will be invited to play a prominent role in the peer review process. [Text will be added here to inform CIME/WPD of the views of the Poverty Network.]

9. Another OECD body has expressed an interest in participating in the process. The Environment Policy Committee's Working Party on Global and Structural Policy, at its meeting on 6 November 2003, expressed its appreciation of the WPD's decision to address sustainable development issues in the context of the ODA/FDI project. It decided to assign a more prominent role to a project on the environmental impact of ODA and investment that has figured on its work programme for some time, and to explore the possibility of contributing to CIME's project.

10. As the project evolves an even broader range of OECD and OECD Secretariat bodies can be invited to cooperate. Possible candidates include the OECD Roundtable on Sustainable Development and the Directorate for Science, Technology and Industry.