Contributions of the private sector

Any national strategy to achieve the Millennium Development Goals needs to include a clear framework for private sector growth. Many of the public investment strategies outlined in the previous chapters are essential for an efficient and dynamic private sector. For their own part, private enterprises can contribute directly to the Goals through core pursuits such as increasing productivity and job creation or seeking opportunities for service delivery through public-private partnerships. In all these activities, companies need to adhere to high standards of responsible corporate governance and citizenship. However, companies and their leaders can also take action to support the Goals more broadly, by contributing to MDG-based policy design, by advocating publicly for the Goals, and by pursuing various models of corporate philanthropy. In these ways, businesses can "engage as reliable and consistent partners in the development process," as called for in the Monterrey Consensus (box 9.1). In this chapter we briefly describe each of the channels through which the private sector can critically support achievement of the Goals.

Increasing productivity and creating jobs

In a market-based economy, private firms contribute to poverty reduction through many channels. They reduce income poverty when productivity rises, job opportunities increase, and competition for workers drives up wages. By producing essential goods and services in large-scale production, they can also help to keep the price of essential goods and services down, increasing the real effective incomes of poor people, a point underscored by the Commission on the Private Sector and Development (UNDP 2004c). As firms grow, they provide a larger source of tax revenues to the government, which in turn supports increased public investments.

Box 9.1

The private sector's role in development: the Monterrey Consensus

Source: UN 2002a.

The 2002 Monterrey Consensus included specific reference to the private sector as partners in poverty reduction:

"23. While Governments provide the framework for their operation, businesses, for their part, are expected to engage as reliable and consistent partners in the development process. We urge businesses to take into account not only the economic and financial but also the developmental, social, gender and environmental implications of their undertakings. In that spirit, we invite banks and other financial institutions, in developing countries as well as developed countries, to foster innovative developmental financing approaches. We welcome all efforts to encourage good corporate citizenship and note the initiative undertaken in the United Nations to promote global partnerships.

"24. We will support new public/private sector financing mechanisms, both debt and equity, for developing countries and countries with economies in transition, to benefit in particular small entrepreneurs and small and medium-size enterprises and infrastructure. Those public/private initiatives could include the development of consultation mechanisms between international and regional financial organizations and national Governments with the private sector in both source and recipient countries as a means of creating business-enabling environments."

What can the private sector do more specifically to help reduce poverty and support the Goals? In the poorest countries, agriculture forms much of the private sector so the rural productivity investments described in chapter 5—particularly those to launch a Twenty-first Century African Green Revolution—will have a direct and sizable effect in kickstarting the private sector's contributions to economic growth and rural household incomes.

Both in agriculture and in other sectors, much private sector activity in developing countries lies outside the formal economy. Of all the nonagricultural private actors in Sub-Saharan Africa and Asia, an estimated 70–80 percent are in the informal sector (UNDP 2004c). Within the informal sector, women are estimated to be about two-thirds of self-employed entrepreneurs (ILO 2003). For these informal sector entrepreneurs, significant support is often needed to climb out of poverty—but success is possible. The Grameen Bank, for example, anchors the provision of credit to poor women not in collateral but in systems of accountability, supervision, participation, and peer management (see chapter 8). Grameen estimates that 51 percent of its borrowers have crossed the poverty line through the income-generating activities made possible in part through these loans (Grameen Trust 2004). Rabobank International has also worked in Uganda and Tanzania and developed financial instruments (risk management tools such as swaps and derivatives) to help small farmers protect themselves against price fluctuations (WBCSD 2004a).

In low-income and middle-income countries with higher levels of urbanization, urban sources of income become more important. In the good scenario, manufacturing firms grow to compete internationally, providing a source of sustained economic growth. Yet in many cases, such value-added production processes are less likely to take off on a path of sustained growth until the costs of entering regional or global markets are significantly reduced through improved infrastructure and a better educated and healthy labor force. When these conditions are not met, much of the urban economy is likely to remain informal and focused in basic commodity trade and the very low-skilled service sector. To enable the entrepreneurs of the informal sector to become the pioneers of the formal sector, basic public infrastructure is needed alongside low-cost credit and regulations (as discussed in chapter 7).[1]

When major multinational corporations decide to invest in developing countries, either to enter local markets or to build production platforms for global markets, they often foster local "business ecosystems" with vertical supply chains and horizontal industry clusters. Such networking is invaluable for diffusing technologies and skills, bringing local firms into the formal economy, and increasing market opportunities for local suppliers (UNDP 2004c). Some foreign investors, when provided appropriate incentives and adequate labor standards, can also place a special emphasis on labor-intensive production technologies that create dignified employment opportunities as an instrument to poverty reduction.

At a broader level of poverty reduction, private enterprises are vital to supporting overall technological advance, the long-term driver of economic growth. Technological learning for production occurs at the level of enterprises, both public and private. This becomes more important as countries reach middle-income status and need to develop their technological base to compete internationally. Technological advances in manufacturing industries tend, by raising the productivity of workers, to increase firm growth and then increase the demand for jobs. Manufacturing enterprises also spread innovation outward to the agricultural and service sectors (UN Millennium Project 2005g).

In some important development success stories, small and medium enterprises have developed much of the local technology that laid the foundation for rapid export growth. In Taiwan (China) for example, small and medium enterprises were the engines of the economy's postwar industrial upgrading, supplying multinational corporations and foreign buyers.

As outlined in Monterrey, financial enterprises also have a special role to play in enterprise creation. Although financial markets are extremely limited in the poorest countries, they have expanded in recent years to support business development in middle-income countries, the "emerging markets." External sources of private capital, including venture capital, can promote developing country firms and entrepreneurs. In more advanced developing economies with more sophisticated financial markets, these markets often provide some capital to new and growing firms. The cost of providing such capital should be minimized by governments—not only to support physical investments but also because venture capitalists and other specialists in business development often provide important knowledge to indigenous firms. Bringing venture capital markets into developing countries can help sustain the growth of new companies, contributing to local technology diffusion, economic growth, job creation, and poverty reduction (Chocce 2003).

Service delivery through public-private partnerships

Of the many goods and services recommended for MDG scale-up programs in chapter 5, most will need to be publicly financed and managed, including, for example, those for education, research, and basic healthcare (chapter 3). But in many cases the private sector can partner with the government for service delivery. To achieve the Goals, governments need to pursue universal access to electricity, roads, and water and sanitation services. In many instances, private firms have the expertise in delivery and logistics to provide these goods and services efficiently at scale (box 9.2).

In considering public-private partnerships, it is important to separate issues of delivery from issues of finance. Even if a private firm is best placed to provide a service on efficiency grounds, that service will often need to be publicly

Box 9.2

Scaling up public services through the private sector: rural electrification in Chile

Source: Jadresic 2000.

Two billion people in developing countries do not have access to modern energy services, and most of them live in rural areas. Rural electrification is expensive, can be technically difficult, and usually fails to attract investment from the private sector. Large-scale rural electrification has been successful in many countries, using a range of public, private, or public-private partnerships. A consensus is growing that electricity and other core infrastructure services can be provided efficiently using a broad range of delivery mechanisms, with a clear regulatory framework and adequate financing.

Where governments have retained a stake in electric utilities, setting access targets is a matter of public policy. Evidence from South Africa demonstrates that such a policy can be implemented efficiently at large scale by state-owned enterprises. But where power sector reform has privatized electric utilities, rural electrification may require special approaches to involve the private sector in scaling up access.

Experience in Chile suggests that the key to expanding rural access is significant public financing targeted at encouraging private companies to develop rural infrastructure. Using domestic resources and external aid, the government of Chile in 1994 set up a special fund for rural electrification, competitively awarding subsidies to private electricity distribution companies that undertake projects. To properly target the subsidies, only projects with a positive social return but a negative economic return are considered. Participating companies design and present rural electrification projects to the government. The projects that score best on a set of objective criteria (cost-benefit analysis, lowest subsidy required, social impact) receive subsidies to cover part of their investment costs. End users pay for less than 10 percent of connection costs, and repayment can be spread out over time.

Even in a competitive environment dominated by private companies, the program increased the coverage of electricity systems in rural areas from 53 percent in 1992 to 76 percent at the end of 1999. Key success factors were well designed incentive structures combined with public financing of up to 90 percent of the capital cost. The example shows how efficient private sector delivery can be successfully combined with public financing of core infrastructure services.

financed. Enormous numbers of poor people simply cannot afford to pay even the lowest market price for the necessary inputs to a healthy and productive life. This is particularly so in rural areas dominated by subsistence agriculture, where very little output is traded and little if any cash is in circulation.

The fact that the private sector does not serve the poorest of the poor is not by itself a market failure, since markets are meant to orient their activity around high-return activities rather than around people with no money. Markets alone will not solve the short-term needs of the most impoverished communities. Instead, for the poorest and most isolated communities, public finance and subsidies will have to create the conditions for market-based economic activity to thrive.

A public-private partnership can combine the respective strengths of the private and public sectors. The private sector can leverage its advantages of greater efficiency, lower costs of distribution, and more complex delivery systems to reach new markets. The public sector can ensure universal access by providing financial support to subsidize impoverished households, thereby enabling private firms to enter large markets with guaranteed consumers. Public funding for the private provision of essential goods and services needs to cover both capital and recurrent costs to “close the revenue cycle.” This is necessary to ensure that subsidized infrastructure investments do not naively project that household outlays will cover the long-term operating expenses, since in many extremely poor communities and countries, households will not be able to afford even to pay the marginal cost of basic water and energy services.

There are many instances where private firms have offered creative solutions to challenging delivery needs. In Namibia, for example, a public-private partnership between the Ministry of Health and Social Services and the United Africa Group, a private company, has allowed for efficient, timely, and regular delivery of state pensions, disability allowances, and child maintenance grants to almost all beneficiaries in rural areas. The company teams are equipped with portable automatic teller machines to disburse payments, smart cards to identify payment recipients, and small teams traveling by truck to manage the monthly delivery systems (ILO 2003).

For such arrangements to support the achievement of the Goals, it is crucial that all contracts be negotiated fairly with full transparency—to ensure that politically well connected firms do not profit unjustly (chapter 7). In cases of large infrastructure projects where economies of scale make it efficient to have a single large private contractor, the government needs to ensure that essential goods and services are universally available based on need rather than ability to pay. This may require price regulation, government subsidies, and perhaps other innovative financing mechanisms.

A promising innovation in ensuring quality service provision of basic social services by private providers is performance-based contracting—where the government contracts with private companies or NGOs to provide agreed-on services to a defined population. Payment is then based on service targets achieved and the quality of services (as confirmed through consumer feedback and inspection). This has improved the access to and quality of essential healthcare in parts of Cambodia, among other places.

Public-private partnerships can also take advantage of creative mechanisms to provide poor people with access to technologies that would otherwise be priced out of reach. Marginal cost pricing, for example, entails private firms agreeing to produce and make available a specified number of products and then to sell them to a public body for the cost of production rather than for any margin of profit. The decision of several major pharmaceutical companies to offer their antiretroviral drugs at cost rather than at patent-protected prices was an important step in this direction. So was the global recognition that low-cost generic drug manufacturers have an important role in alleviating suffering from disease in the poorest countries. In the future, tiered-pricing strategies could expand the reach of many new information technologies, biotechnologies, and other emerging breakthroughs from high-technology companies.

Responsible corporate governance and citizenship

In all their activities, private firms and their executive leadership have a unique obligation to adhere to high norms of corporate governance and citizenship. Private production processes and delivery mechanisms often have broad economic, social, and ecological consequences, which enterprises should address in a socially responsible manner (CSR Platform 2003). International treaties and instruments such as the Universal Declaration of Human Rights, the International Labour Organization (ILO) labor conventions, the 1992 United Nations Conference on Environment and Development in Rio de Janeiro, and the Copenhagen Declaration on Social Development provide guidelines for responsible business practices that help ensure private sector growth benefits society and protects the environment.

More recently, the UN Global Compact was enacted in 2000 as a UN-sponsored initiative to enable global businesses to sign up to a code of conduct that respects human rights, labor standards, and environment standards and fights corruption. The Global Compact lays out 10 basic principles for conducting business and provides useful guidelines for global corporations, in the spirit of the UN Millennium Declaration (UN 2004e). The Compact is a valuable undertaking that should promote operational guidelines and measurement tools, including targets where possible, for companies that want to contribute actively to the Goals. We endorse the UN Global Compact as a voluntary initiative and recommend that all corporations with operations in the developing world sign up for it.

For corporations with global operations, a first major priority needs to be vigilant support for human rights in their business processes, even in countries where gross violations of human rights occur. All personnel, especially security personnel, need to respect international principles of human rights (as outlined in the Universal Declaration of Human Rights) as part of the company's code of conduct. Before doing business in a country, corporations should be sure to understand how human rights may be affected by their operations.

Relevant to human rights, a healthy and decent work environment is essential for any company's work force. The International Labour Organization has promoted minimum norms for work standards, as defined in the Decent Work Initiative, that focus on steps to ensure international labor standards, provide decent and nondiscriminatory employment, offer social protection, and foster social dialogue among workers, governments, and businesses. The UN Global Compact focuses on many of these elements, such as upholding freedom of association and collective bargaining, eliminating forced and child labor, and eliminating discrimination in employment. Corporations also have an obligation to minimize work-related accidents and illness for their work force, and create safe and hygienic working conditions. We recommend that all companies adhere to these basic principles.

Another major element of sound corporate citizenship is to fight corruption. Corporations should refuse to pay bribes, especially in low-income countries where governments often struggle to strengthen the rule of law. Firms in extractive industries that operate in natural resource–rich developing countries have a special responsibility in this. The international oil companies have a particular responsibility to be transparent in their transactions with the government and local authorities, so that citizens can keep track of where the revenues are flowing. The recent "Publish What You Pay" initiative is an example of efforts by citizens in developing countries to track resource revenues and hold oil, gas, and mining companies accountable by demanding transparency in tax payments, license fees, and royalties (chapter 12).

Contributing to policy design

Many developing countries have legacies of political tension between the private sector and the public sector, often reflecting past ideological battles. As a central element of our recommended strategy for open national processes to develop MDG-based poverty reduction strategies, we recommend that the local private sector contribute to the development of these programs, alongside civil society, development partners, and the multilateral agencies. We also recommend that governments prepare a long-term private sector development strategy within the context of their MDG-based framework, consulting with the local private sector in the development of that strategy (chapter 4).

The local private sector represents a key constituency whose responsible voice should be represented alongside others in major policymaking processes. National chambers of commerce can often lead in representing the voices of private firms. Often, they are supported by the valuable work of international business organizations, such as the International Chambers of Commerce, the African Business Roundtable, the World Business Council for Sustainable Development, and the International Business Leaders Forum.

Of course, the private sector has to be balanced with civil society and other communities. Since the private sector is capable of wielding tremendous influence in decisionmaking through its financial strength, national governments have an added responsibility of ensuring transparency and balancing interests in all public discussions relating to private sector development processes.

Advocacy for the Goals

Since members of the private sector often have access to important channels of public debate, they can advocate the public investments needed to spur private economic activity, particularly in low-income countries. Domestically, private companies can have a big influence if they lobby publicly for improved infrastructure, better health services for their workers, and better education for the work force. They can help map out the sequence and scaling up of large-scale basic infrastructure over a medium-term time frame. They can also inform their home governments of the scale and type of investments needed to sustain economic growth. Major multinational firms can also lead in global advocacy efforts for the Goals, either by lobbying their local politicians that global development is a worthy undertaking, or by identifying specific practical initiatives where they might provide support to raise awareness of the Millennium Development Goals in their home countries.

Corporate philanthropy

The discussion above highlights that there are many ways in which the private sector can contribute to poverty reduction and the Goals, quite separate from direct philanthropy. Nonetheless, many companies are well positioned to make important contributions through direct giving or other philanthropic models. In aggregate, these flows can be sizable. In 2003, for example, 232 of the largest U.S. corporations alone donated $1.1 billion for international philanthropy (Muirhead 2004). Although this amount was not oriented solely to developing countries and is vastly less than what is needed to achieve the Goals, it represents considerable resources from one country and indicates an important volume of assistance that could support poverty reduction in many places. For companies seeking to increase or streamline their philanthropy, the Goals provide a framework to undertake specific activities aligned to countries' actual investment needs. Corporate philanthropic efforts can only supplement, not replace, government-led efforts. But they can often provide the trigger or "seed" funds that pave the way for increased investments.

In pursuing philanthropy, multinational corporations that operate across several countries have the ability to leverage their tremendous voice and resources to advocate and support specific development objectives. They can adopt specific Goals and base their philanthropic endeavors on these Goals in each country of operation. They can become ambassadors for those Goals and mobilize partners. The Merck Mectizan Donation Program is an example of a large-scale and long-term commitment. Since 1987 Merck has partnered with the World Bank, the World Health Organization, and other agencies to reach more than 40 million people suffering from onchocerciasis (African river blindness) in more than 30 countries, providing Mectizan free of charge and combining treatment with prevention.

Philanthropy can also be in-kind—for example, through community partnerships and education and training. Private firms can invest heavily in the development needs of their local host communities through such partnerships, signaling a long-term commitment to the welfare of the host community. Examples of such partnerships include Bayer's Integrated Crop Management Program for farmers in Guatemala and especially in Brazil, where the company trained more than 25,000 farm families in improved farming techniques. Corporations can also donate employee and management time to help public sector enterprises and governments design and implement projects. And they can contribute to developing local capacity by undertaking extensive training programs and contributing to the development of the local private sector. For example, Alcoa Aluminio in Brazil has developed an extensive training program in close collaboration with local universities that has helped build the skills of the local work force.

These are only a few examples of innovative approaches to corporate philanthropy. To systematize corporate support for the Goals, and to provide a set of benchmarks for companies to measure themselves, we encourage all Fortune 500 companies to voluntarily include a Millennium Development Goals scorecard in their annual reports. This would outline how their philanthropic and corporate governance activities have contributed to achieving the Goals, taking advantage of the quantified and time-bound nature of the Goals to measure results, plan future activities, and coordinate with other philanthropic partners.