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AND ECONOMIC CO-OPERATION

Policy Guidelines for Sida's Support to Private Sector Development

Private Sector Development



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Introduction

The purpose of these Guidelines is to briefly describe the purpose and key principles of Sida's support to Private Sector Development (PSD) and to provide guidance for the design and implementation of such support.

The Guidelines are a response to a series of evaluations of Sida's past approaches to PSD in which Sida was recommended to define a common Sida policy that would be applicable to all aspects of PSD support.

Poverty reduction is the overall goal of Swedish development cooperation. Sida's understanding of poverty and poverty reduction is expressed in "Perspectives on Poverty" published in 2002. It states that "sustainable poverty reduction requires high rates of economic growth as well as full and effective participation on equal terms of all countries in the global economy". These Guidelines form part of Sida's efforts to put "Perspectives on Poverty" into practice.

During the process of preparation of these Guidelines a separate document¹ was produced with the purpose of providing a source of information and an inspiration to debate on the PSD theme.

¹ Ref. "Making markets work for the poor: Challenges to Sida's Support to Private Sector Development" (Provisional Edition; October 2003).

Points of departure

Private Sector Development rests upon four fundamental elements:

- *competitive markets*, including clear and non-discriminatory rules of the game, ensuring a ‘level playing field’;
- *entrepreneurship* as the source of innovation and change;
- fair, non-discriminatory and effective *property rights*;
- *decent work conditions* and *sustainable use of the environment*.

PSD is not limited to a sector in the conventional sense, but encompasses agriculture, manufacturing and services, including trade, and increasingly also infrastructure and social services. It also includes all types of market players: the self-employed in the informal economy; small, medium and large enterprises; and transnational companies.

PSD is about the interplay between the state as a formulator of the ‘rules of the game’, the ‘players in the private sector’, and also of civil society. These interact in dynamic processes. Understanding the dynamics of such a system is critical to enable Sida to support development processes in partner countries.

Private sector development plays a crucial role in *poverty reduction*, not only in relation to the material dimension of poverty, but also to the political, social and environmental dimensions of poverty, as well as to peace and stability.

Support to PSD is primarily seen as an *instrument to achieve sustainable, poverty-reducing economic growth*. High rates of economic growth are a prerequisite to this end. At the same time the *quality of growth* is essential: its composition, distribution and sustainability are vital.

Increases in *employment and labour productivity* provide the main link between economic growth and poverty reduction. In order to reduce poverty, it is essential both to enhance the capacity of the economy to generate productive employment and to have decent working conditions. Strengthening the ability of the poor to gain access to and benefit from existing opportunities is also of key importance.

Purpose

The main purpose of Sida's support to PSD is to contribute to sustainable poverty-reducing growth based on three elements: (i) *direct inclusion of the poor* in economic activities, contributing to their employment, income and productivity, and to reducing their vulnerability, (ii) *economic growth* as the means of generating resources in society and enhancing productivity, employment and income, and (iii) *redistribution* so that the resources generated in society from growth are invested meaningfully for the poor, especially in human resource development.

Main policy guidelines

Making markets work for the poor

- The development of *efficient markets* working to benefit the poor is the key to pro-poor PSD. Sida's vision is to support the development of competitive and dynamic markets, where relevant measures are taken to correct market failures and where the poor participate on decent terms as producers, consumers and employees.
- A central element in support of this type is development of sound business environments and good governance – in particular the rule of law and fight against corruption – through support to *policy reforms*, *institutional development* and *capacity building*.
- Sida will give special attention to *markets in which the poor are directly involved*, primarily *agriculture*² (including fishery, livestock breeding and forestry) and the *informal economy*. In these sectors property rights are often informal, poorly enforced or non-existent. Under these circumstances, care needs to be taken to protect the ecosystem resources which are vital assets for the poor.
- Sida supports *market development*, primarily by addressing constraints in the business environment. Direct support to market players should be limited to purposes that justify subsidies, e.g. human resource development with clear positive externalities. The relevance of such support should be assessed in relation to “market failures” or redistribution policies. In this context Sida should make special efforts to *avoid creating market distortions*³.

An integrated approach

- Effective PSD depends upon and can contribute to peace and stability, human resource development, environmentally sustainable development, functional infrastructure, good governance, democratic development including respect for human rights and a vibrant civil society, i.e. Sida's mission in a broad sense. Consequently an *integrated and holistic approach* to PSD is required, involving Sida's organisation at large.

² Reference is made to Sida's guidelines for support to rural development (forthcoming).

³ Ref. Various ways of diminishing the risks for such distortions are described in Chapter 8.4 in the document referred in footnote 1.

- There are strong links between *social development* – not least human resource development – on the one hand, and economic growth and private sector development on the other. It is a major challenge for Sida to identify and promote opportunities for partnerships between organisations in the public sector, the private sector and civil society, in ways that reduce poverty; for example in the education, health, culture and media sectors.
- *Gender* is an essential dimension of PSD. The respective roles of men and women in economic activities tend to vary as a consequence of cultural, religious and other traditional institutions and power structures. As a result, development, economic growth and private sector development have different outcomes for men and women in basically all societies. Therefore, a gender perspective is necessary in all Sida's support for private sector development. As an example, Sida should work to enhance the inclusion and productivity of women in economic activity and to counteract discriminatory legislation and practices based on sex.
- The struggle against the *HIV/AIDS epidemic* is a matter of great concern to the private sector in many of Sida's partner countries. Sida strives to integrate HIV/AIDS aspects in all its support to PSD⁴.
- Sida supports partner countries in the development of *local research capacity* in areas strategic to PSD. Such capacity is an essential component in the ability of partner countries to analyse PSD-related policy issues. It is also a prerequisite of the emergence of *innovation systems* that benefit PSD and economic growth. Research cooperation in science and technology contributes to improved competitiveness of the private sector in partner countries.

Interventions at different levels of the economy

- Sida's PSD support includes interventions at *different system levels*: the international system level, the macro and meso levels, as well as the micro level of the formal and informal economy in partner countries. Sida's role will vary between the different system levels. Sida should be prepared to *analyse constraints and opportunities in respect of PSD and to make appropriate interventions* at each system level. Political and cultural factors may have a strong potential impact on PSD, and should be fully integrated in this kind of analysis. Whenever relevant, Sida should make linkages and appropriate sequencing between interventions at different system levels.
- Recognising the importance of *trade* as an essential means of economic development, Sida assists partner countries in their efforts to integrate into the world economy. Elements in such assistance include strengthening trade policy expertise and analytical capacity, as well as trade-related institutional infrastructure, e.g. standards and quality⁵.

⁴ Ref. Sida's guidelines "The private sector and HIV/AIDS", November 2002

⁵ Ref. Sida's guidelines for its work on trade and development (forthcoming).

- Unstable and weak *financial systems* are often a cause of delayed or interrupted domestic economic growth with serious negative effects on poor groups. Sida contributes to the construction of stable, robust and shock-resilient financial systems in partner countries. Innovations aimed at increasing savings and deepening local capital markets are a major ingredient in these efforts. A priority area in the financial sector is *microfinance services*⁶, including savings, credit, remittances and insurance services for poor households and micro-enterprises.
- Sida gives close attention to the *reform of public enterprises* including *infrastructure reforms*. Important elements are support to strengthen regulatory capacity and the development of financial instruments which facilitate private participation in infrastructure. Sida is prepared to support *public-private partnerships* including “*output-based aid*” *schemes*, which provide poor target groups with access to public services.
- Sida’s support to PSD attaches special importance to the *social responsibilities* of the corporate sector. All PSD activities shall promote the nine principles embedded in the joint UN Global Compact initiative regarding human rights, core labour standards and the environment as well as the General Policy in the OECD’s Guidelines for Multilateral Corporations.

PSD in the development cooperation setting

- Sida will highlight economic growth and PSD dimensions in its analysis, monitoring and dialogue relating to the *Poverty Reduction Strategy Papers (PRSPs)*. PSD and trade aspects should be fully integrated in the *country strategies* for Swedish development cooperation.
- *Participatory approaches* are applied by Sida in PSD interventions, aiming at ownership by concerned stakeholders in the public and private sectors and, as far as possible, representatives of the ultimate beneficiaries, i.e. poor men and women. Sida will make use of opportunities to conduct a dialogue with stakeholders on constraints to PSD.
- Sida endeavours to provide PSD support in consortia with other donors. Elements of *sector-wide (SWAp) methodology* may be fruitfully applied in such contexts. *Institutional capacity building*, for example in the form of professional twinning with Swedish organisations, may be an important component in such programmes.
- Sida participates in a number of *international networks* through which multilateral and bilateral donor organisations promote policy coherence and exchange knowledge related to PSD.
- Sida works with *key organisations in Sweden*, including the *private sector in Sweden*, which provide valuable resource bases for Sida’s PSD support and act as providers of knowledge on what constitutes an “enabling environment” for business development. It is noted that Sweden and Sida have *comparative advantages* in certain knowledge domains within the field of PSD⁷.

⁶ This is further elaborated in Sida’s policy guidelines on microfinance (forthcoming).

⁷ Examples of a number of such knowledge domains are given in the document referred to in footnote 1.

Implementation

In order to make PSD a truly cross-sector effort at Sida, a separate *action plan* will be drawn up for the implementation of these Guidelines. Examples of actions of this type are the creation of a *Sida PSD Network*, *internal human resource development* and the strengthening of Sida's *analytical toolbox* both to support of the country strategy process and for analysis of programmes and projects in a PSD perspective. Given the central role that *Sida's field organisation* must play in PSD work, special efforts will be made to involve and support field staff.

Halving poverty by 2015 is one of the greatest challenges of our time, requiring cooperation and sustainability. The partner countries are responsible for their own development. Sida provides resources and develops knowledge and expertise, making the world a richer place.



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