

The Role of Public Policy in Private Sector Development
Leadership Academy for Development & Lee Kuan Yew School of Public Policy
25-29 January 2016

Introduction:

This module addresses the challenges faced by public sector leaders as they foster economic growth in politically charged environments. Offered in partnership with the Leadership Academy for Development (LAD) at Stanford University and Johns Hopkins University School of Advanced International Studies, it uses case studies (mostly drawn from Asia) on how public policy can help the private sector be a constructive force for economic growth and development. A driving principle of the LAD module is that policy reform is not like engineering or other technical fields that have discrete skills and clear, optimal solutions. Instead, successful reformers must be politically aware and weigh a broad range of factors that influence policy outcomes. They must have a solid grasp of country-specific economic, financial, political and cultural realities. Most importantly, they must have a sense of how to set priorities, sequence actions and build coalitions. LAD provides participants with an analytical framework to build these leadership abilities and operate effectively under adverse conditions. Major themes are 1) Providing Public Goods 2) Bypassing Bureaucratic Obstacles, 3) Facilitating Investment, and 4) the State as Economic Catalyst. This program is designed to reinforce and illustrate three critically important hypotheses about the role of public policy in private sector development:

1. Public policy matters! The performance of the private sector and its role as either a catalyst or an obstacle to economic growth is closely connected to how well or badly government policies are designed and implemented.
2. The public officials responsible for enhancing private sector participation must acquire a range of analytical skills to be effective. But policy reform is not like engineering or other technical fields where there is a clear optimal solution to a problem. Designing and implementing meaningful policy reform requires a broader, more interdisciplinary knowledge of economics, politics, local history and culture, combined with a sense of how to set priorities, sequence actions and build coalitions.
3. Successful policy outcomes that encourage and strengthen private sector participation are contingent upon the capacity of government officials and business leaders to understand and appreciate the interests, motivations and objectives of their counterparts.

Leadership Academy for Development (LAD)

The Leadership Academy for Development (LAD) trains government officials and business leaders from developing countries to help the private sector be a constructive force for economic growth and development. It teaches carefully selected participants how to be effective reform leaders, promoting sound public policies in complex and contentious settings. LAD is a project of the Center for Democracy, Development and the Rule of Law, part of Stanford University's Freeman Spogli Institute for International Studies, and is conducted in partnership with the Center for International Business and Public Policy at the School of Advanced International Studies, Johns Hopkins University.

The Case Method

The “case method” is a technique of teaching and learning through the analysis of actual events that have occurred, allowing you to gain a realistic understanding of the roles, responsibilities and analytical skills required of decision makers, as well as the tensions that may arise between various stakeholders with different objectives. The cases in this course highlight both the political challenges and analytical tasks encountered by government officials in different countries who are responsible for formulating policies and programs designed to encourage a larger, more constructive private sector role in the local economy, such as improving consumer credit information in China, eliminating corruption in the Indonesian customs service by contracting out critically important services to a private firm, or restructuring a public water and sewerage authority in India. Each case is presented from the point of view of a practitioner—usually a government official—who played a central role in the policy making process. As the reader of the case, you are required to assume the role of the principal analyst/decision maker who must thoroughly analyze the problem, identify and assess the issues, and make a defensible decision on whether to proceed, and if so, how.

The case method is an *active* approach to learning. Rather than listening to lectures by professors (i.e. passive learning), participants are expected to *actively* engage in a structured class discussion of the case led by the professor. It cannot be stressed too strongly, therefore, that success with the case method used in this course hinges on your willingness and ability to prepare meticulously in advance of each class, and then participate actively in the class discussion. Because this is a relatively realistic, “hands-on” method of learning, the case method approach should help you to develop the skills needed to analyze some of the complex issues you encounter in your work. In addition, it should strengthen your ability to make difficult decisions and communicate effectively.

Study Groups

You will be assigned to a study group consisting of about five members on the first morning of the course. Time will be set aside during the course for groups to meet to discuss the case assignments *after* you have completed a careful reading of the case. These group sessions provide an opportunity to exchange views and discuss some issues likely to arise during class discussion. Reaching a group consensus is *not* the objective. Ultimately, the goal of this process is to challenge all participants to be more effective class participants, which heightens the quality of class discussion for everyone.

Final Study Team Assignment

Each study team will prepare a 15-minute presentation that will be given before the entire class on the final day of the course. The presentation will outline a specific policy challenge regarding an aspect of private sector development and recommend a new government initiative to address this challenge, drawing on lessons learned during the course. For example, the presentation might focus on a policy initiative designed to combat corruption that has adversely affected private sector performance, or a new program to facilitate SME access to affordable financing, or a regulatory change that would attract higher levels of infrastructure investment via public-private partnerships (PPPs).

This assignment is designed to encourage you and your study team colleagues to apply what you have learned during the course to a real world problem that is impacting private sector performance in your country. This assignment is a central component of the course. Study teams are expected to dedicate significant time during the week to this task, and produce a quality presentation that demonstrates original thinking. On the afternoon of the first day, instructors will assist each group to identify the policy challenge that they will address, and they will be available throughout the week to provide guidance on the presentations. One session at the end of each day is dedicated to working on the assignment.

COURSE PROGRAM

DAY 1: MONDAY 25 JANUARY

08:30— 09:00 REGISTRATION AND COURSE OVERVIEW (Roger Leeds)

09:00— 10:30 LECTURE by Donald Low: “The State and Private Sector Development”

10:30—11:00 TEA BREAK

11:00-12:30 LECTURE by Eduardo Araral: Public Private partnership for Infrastructure Development in Asia

12:30—13:30 GROUP PHOTO AND LUNCH

13:30—14:00 GROUP MEETINGS TO DISCUSS CASE 1

Case 1: The Hyderabad Metropolitan Water Supply and Sewerage Board (India):

This case discusses the efforts by the state of Andhra Pradesh and the Hyderabad Metropolitan Water Supply and Sewerage Board to provide water services to its poorest inhabitants. Pradesh must respond to the demands of politicians and private investors all the while ensuring the provision of a public good. Undermining this challenge is the reality that Hyderabad is located in a comparatively dry region of India, and the Water Board is only able to provide water for an average of two hours per day. To attract investment, the government decides to privatize the Water Board, but the World Bank conditions its support for this privatization on Andhra Pradesh's ability to develop a program that will provide water to the city's slums.

Study Questions

1. What are the goals of the HMWSSB? How should it prioritize among its various goals? (Which goals should it prioritize, and on what basis?)
2. To whom does Mr. Gopal answer? Whose interests does he have to be concerned with? Why? What resources does he have, and what constraints does he face, for managing this external environment?
3. What are the constraints on privatization facing the HMWSSB? How attractive would it be to international water companies?



4. Analyze the cost structure and user charges, using the data provided at the end of the case. Note in particular the gap between income and expenditure in Table 1. What are the implications of these figures for the ability of the HMWSSB to finance service improvements?
5. What strategies should HMWSSB pursue to achieve its priority goals? The case identifies three options related to the question of privatization. But there may be other alternative or additional strategies or actions to take. (For example, you might consider increases in user charges, improving collection efforts, adjusting the labor force size, etc.) What are the advantages and disadvantages of each strategy? Make sure to consider constraints that may limit feasibility.
6. Consider the policy options outlined in Question 5. How you would react to these options if you were:
 - Unions representing workers at the Hyderabad Metropolitan Water Supply and Sewerage Board and the Municipal Corporation of Hyderabad
 - The World Bank
 - An international water firm interested in entering the Indian market
 - A civil society organization that represents slum-dwellers who do not have water and sewerage connections
 - The Municipal Corporation of Hyderabad

Reading: Jennifer Davis & Sunil Tankha. “The Hyderabad Metropolitan Water Supply and Sewerage Board.” HKS Case #319.

14:00—15:30 CASE 1 DISCUSSION – Kent Weaver

15:30—16:00 TEA BREAK

16:00—17:30 STUDY TEAM MEETING TO DISCUSS POTENTIAL GROUP PROJECTS

DAY 2: TUESDAY 26 JANUARY

08:30— 10:00 LECTURE by Roger Leeds: Economic Growth, Poverty Alleviation and Financial Sector Development

This lecture will make the case that a critically important determinant of the pace of economic growth and poverty alleviation is the level of development of a



country's financial sector. Although foreign investment is important, most investment in developing countries comes from the efficient mobilization and allocation of domestic savings into productive investment through banks and other financial intermediaries. In many developing countries, however, large segments of the population do not participate in the formal financial sector because they lack confidence that their savings will be protected and used productively. This lecture will highlight a range of public policy challenges for governments seeking to encourage higher levels of participation in the financial sector, and how successful outcomes impact economic growth and reductions in poverty. Some of these challenges are technical, but many others are political, such as the government's ability to mobilize public support for reforms that may be resisted by stakeholders with a vested interest in maintaining the status quo.

Reading:

1. World Bank, "Rethinking The Role of The State in Finance," (Global Financial Development Report, 2013), pp 1-14 ("Overview") and Chapter 5, "The Role of The State in Financial Infrastructure," pp. 129-160. [The entire Report, available online: www.worldbank.org].
2. Paulson, Henry, "Let China's Markets Speak Truth to Power," Financial Times, July 22, 2015 (op ed). (Available online: www.ft.com).
3. Quintyn, Marc, & Verdier Genevieve, "Trusting the Government," Finance and Development, Dec. 2010, pp. 41-43, <http://www.imf.org/external/pubs/ft/fandd/2010/12/quintyn.htm>

10:00—10:30 TEA BREAK

10:30—11:00 GROUP MEETINGS TO DISCUSS CASE 2

Case 3: Increasing financing opportunities for local companies by reforming the domestic stock market (Brazil): This case focuses on the importance of creating a local stock market that serves as an attractive source of financing for growth-oriented small and medium size enterprises (SMEs) as well as established large companies. Brazilian officials recognized that in order for the private sector to become a larger, more constructive contributor to the country's economic growth and development there must be major reforms in the regulations and infrastructure of the stock exchange. The case examines the constraints to stock market development and various policy and regulatory options considered by Brazilian officials as they worked to strengthen the domestic stock market and expand private company access to equity capital.

Study Questions:

1. What specific factors would you cite to support the proposition that a well-functioning stock exchange is vitally important to economic development in Latin America, and therefore should be a high priority for the government?
2. Are there similarities between the Brazilian and situations in Southeast Asia that demonstrate the challenges of creating a stock exchange that will provide access to capital for growth-oriented companies?
3. How do you define “corporate governance”? Why are internationally acceptable corporate governance standards a fundamental prerequisite for companies, regardless of the country in which they operate, to issue public securities successfully? Why do many company owners resist adopting acceptable corporate governance practices?
4. The Brazil case identifies a diverse range of stakeholders in both government and the private sector who will be affected by stock market reforms—some will benefit, but others may not. What are the similarities and differences between these Brazilian stakeholders and those in Southeast Asia today?
5. Based on what is described in the Brazil case, would you be in favor a creating a stock exchange in your country that is geared specifically to addressing the financing needs of SMEs?
6. Which option should Maria Helena Santana and Gilberto Mifano recommend for implementation? What arguments would you emphasize to gain support for your recommendation with the major stakeholders? What are the risks that must be addressed and how can they be mitigated?
7. What are the broader lessons learned from Brazil’s experience that are relevant to developing countries today?

Reading: Aaron Mihaly, “Access to Financial Resources for Local Companies: Revitalizing Brazil’s Stock Exchange,” Case Study, Leadership Academy for Development.

11:00—12:30 CASE 2 DISCUSSION – Roger Leeds

12:30—13:30 LUNCH

13:30—14:00 GROUP MEETINGS TO DISCUSS CASE 3



Case 3: Creating a Consumer Credit Information System (China): This case examines (i) why governments must play a leadership role to ensure the creation of a credit information system (CIS) that is designed to encourage banks and other domestic financial institutions to increase their lending to local consumers; (ii) alternative strategies/models for implementing a new CIS that have been used by different countries; and (iii) the complex issues encountered by the government officials who are responsible for assessing the strengths and weaknesses of the alternative approaches to creating a new credit information system. The case focuses particular attention on the critical role of officials in the central bank of China's (PBOC) who were in charge, and their interactions with their technical advisors from the International Finance Corporation (World Bank affiliate) who were recommending a CIS model that differed from what the Central Bank believed was appropriate for conditions in China.

Study Questions

1. What is the main explanation for why fewer than 25% of households in many developing countries deposit their savings in a bank?
2. What specific reasons explain why banks and other financial institutions resist lending to consumers and SMEs in many developing countries, including Peru?
3. How does a well-functioning credit registry system (CRS) mitigate the risks and strengthen the incentives for banks to increase lending to ordinary citizens and SMEs? (For background please read Chapters 1 & 2 of IFC's "Credit Bureau Knowledge Guide" in the reading packet.)
4. As the case explains, China had no previous experience with a CRS and created a system from scratch. What are the similarities and differences between China's experience creating a CRS under the direction of Mr. Dai and the circumstances in Peru today?
5. Did Mr. Dai and his Chinese colleagues encounter specific political and policy challenges that are similar to what Peru would likely experience in creating a CRS? For example, are the stakeholders who have a vested interest in the final CRS structure similar?
6. Why did the International Finance Corporation (IFC) advocate a private rather than a public model for the Chinese CRS, and why did Mr. Dai decide not to take the IFC advice? Based on your perception of the realities in China, which model would be most appropriate, and why?

Reading: Sai Ma and Justina Wong, “Establishing the Individual Credit Registry System in China,” Case Study, Leadership Academy for Development.

14:00—15:30 CASE 3 DISCUSSION – Roger Leeds

15:30—16:00 BREAK

16:00—17:30 STUDY TEAM MEETING

DAY 3: WEDNESDAY 27 JANUARY

08:30— 10:00 LECTURE by Kent Weaver: Promoting Behavior Change Among Businesses and Individuals

10:00—10:30 TEA BREAK

10:30—11:00 GROUP MEETINGS TO DISCUSS CASE 4



Case 4: Diminishing the size of the informal sector in Medellin (Colombia): The new mayor of Medellin, Sergio Fajardo, arrived to office in 2004 pledging to remake the social contract between society and the state. He campaigned to introduce innovative social programs designed to lessen the high levels of poverty and violence in the city. But the mayor needed money to finance these programs. The Minister of Planning, Federico Restrepo Posada, was charged with engaging the private sector, increasing tax revenue and promoting job creation. To do this, Restrepo needed to address the high levels of informal economic activity hindering economic dynamism and depressing the tax base. The state could not provide the necessary services because it did not collect enough taxes, but businesses refused to pay taxes because they did not believe the state capable of delivering the services that they required. The case looks at how Restrepo addressed this dilemma.

Study Questions:

1. From the perspective of a person starting or operating a business, list the benefits and costs associated with operating in an informal context and in a formal context.
2. What are the causes of having a large informal economy? What are the consequences (positive and negative) for a country or a city of having a large informal economy?
3. Why does Restrepo want to decrease informality in Medellin?
4. What are the major challenges in getting Medellin businesses to formalize? How does Restrepo go about thinking about this problem?
5. What constraints does Restrepo face in reducing the informal sector? What tools does he have at his disposal?
6. There are several policy options implicit in the text. These include:
 - a. Increase penalties for informal businesses
 - b. Create business service centers in marginalized areas that serve as a one stop shop
 - c. Work to increase the access to markets for small businesses via trade fairs and other government assistance programs
 - d. Reduce the number of procedures for opening a business or locate all of the registration process in one central location
 - e. Provide a tax holiday for registering businesses

Identify the advantages and disadvantage of each option. Which stakeholders would you have to collaborate with in order to execute each option? Which policy option would you choose?

7. Consider the policy options outlined in Question 7. How you would react to these options if you were:
- a small bakery with one outlet and five employees
 - a small manufacturer of apparel with ten employees
 - a small construction company that employs ten employees on an irregular basis, depending on demand for services
 - Front-line workers in tax and labor inspectorates
 - Local drug gangs

Reading: Seth Colby, “Serious Business: Diminishing the Size of the Informal Sector in Medellin, Colombia,” Case Study, Leadership Academy for Development.

11:00—12:30 CASE 4 DISCUSSION – Kent Weaver

12:30—13:30 LUNCH

13:30—14:00 GROUP MEETINGS TO DISCUSS CASE 5

Case 5: Anti-Corruption Commission in Indonesia: The prevalence of widespread corruption in Indonesia has, among other consequences, distorted markets, increased business uncertainty, and undermined the development of a dynamic and efficient private sector. Believing that serious anti-corruption reform was an imperative in order to unleash Indonesia’s significant economic potential and strengthen private sector capacity, in 2003 the government created the Indonesian Corruption Eradication Commission (KPK). Despite high public expectations, many were skeptical that the government was sincere about cracking down on corruption and would provide the KPK with the political support necessary to be successful. In July 2004 the KPK commissioners faced the first major challenges to its credibility: bringing the powerful and well-connected governor of Aceh to justice for corruption.

Study Questions:

1. What is the nature of corruption in Indonesia? Who is involved? Why have previous anti-corruption Initiatives failed?

2. Do you expect the KPK to be successful where other anti- corruption initiatives in Indonesia and elsewhere have failed? If so, why? If not, why not?
3. What are the pros and cons of ordering Megawati to suspend Puteh?

Reading: Michael Goldfien, “Indonesia’s Corruption Eradication Commission,” Leadership Academy for Development Case Study

14:30—15:30 CASE 5 DISCUSSION – Roger Leeds

15:30—16:00 BREAK

16:00—17:30 GROUP PROJECT MEETING

DAY 4: THURSDAY 28 JANUARY

08:30— 10:00 LECTURE by Kent Weaver: The Challenge of Policy Implementation

10:00—10:30 BREAK

10:30—11:00 GROUP MEETINGS TO DISCUSS CASE 6

CASE 6: Defending the Environment at the Local Level: Dom Eliseu, Brazil, 2008-2014. A former center of the timber industry in the Brazilian Amazon, the municipality of Dom Eliseu had built its economy around deforestation—much of it illegal. In 2008, as part of a strategy to enforce the country’s environmental policies, the federal Ministry of the Environment included Dom Eliseu on a list of the worst violators of deforestation laws. The blacklist cut off residents’ access to markets and credit and made the municipality the target of intensive law enforcement. To get off the blacklist, the community had to overcome a collective-action problem. The local government had to persuade the owners of 80% of private land—more than 1,000 properties—to map their property boundaries, declare the extent of deforestation, enter their properties in the state environmental registration system, and adopt more-sustainable methods of production. The municipality also had to build the capacity to take on new responsibilities for environmental protection—most important, environmental licensing, which would enable the local government to regulate land use.

Study Questions:

1. List the different actors/stakeholders in the case. What are the interests or concerns of each with regard to the policies being implemented in Dom Eliseu? Are interests shared or divergent? Are relationships between different actors cooperative or conflictual?
2. Was the municipal government well placed to take on the challenges of removing Dom Eliseu from the blacklist and taking on the deforestation problem? What made it difficult? What did Neto and Poggi need to do to be successful?

Reading: Maya Gainer, “Defending the Environment at the Local Level: Dom Eliseu, Brazil, 2008-2014,” Case Study, Leadership Academy for Development.

11:00—12:30 CASE 6 DISCUSSION – Kent Weaver

12:30—13:30 LUNCH

13:30—14:00 GROUP MEETINGS TO DISCUSS CASE 7

Case 7: From water scarcity to a global hydro-hub: Developing the local water industry (Singapore): The Singapore government placed a very high priority on making the transition from water scarcity to water self-sufficiency. Ultimately, they developed an internationally competitive water industry by harnessing the resources, initiative, and creativity of the private sector. The case traces the challenges encountered by government officials as they assessed alternative strategies for achieving this ambitious objective, and the specific actions they took to strengthen the capacity of local water companies to compete internationally. The case highlights the strong and effective public-private cooperation that was designed to increase the export of Singapore’s technological know-how and water management expertise.

Study Questions

1. Many developing countries have state-owned utility companies that both lose money, fail to provide adequate services, and are tremendous sources of corruption. Why didn’t that happen in the case of the PUB?
2. What considerations went into the setting up of the Research, Innovation and Enterprise Council (RIEC) in the manner chosen? What advantages did this have over other governance structures?
3. What are the main pitfalls facing the RIEC at present? In particular, how should it treat SMEs in the water business?

4. Could your country have done what Singapore has done with its state-owned utilities? What are the specific obstacles standing in the way?

Reading: Selina Ho, “Growing Singapore’s Water Industry: From Water Scarcity to Global Hydro-Hub,” Case Study, Leadership Academy for Development.

14:00—15:30 CASE 7 DISCUSSION – Selina Ho

15:30—16:00 TEA BREAK

16:00—17:30 STUDY TEAM MEETINGS AND FINAL REHEARSAL FOR GROUP PRESENTATIONS

DAY 5: FRIDAY 29 JANUARY

08:30-9:00 GROUP MEETINGS TO DISCUSS CASE 8

Case 8: Singapore’s Productivity Challenges

This case examines how Singapore’s policy decisions for economic development in the past, while appropriate in their particular historical contexts, produced unintended consequences and knock-on effects that now limit the country’s on-going efforts to increase labour productivity in Singapore.

Study Questions:

1. How would you describe Singapore’s growth model since Independence?
2. What was the role of the state in fostering rapid economic development? What were the key institutions and policies that were essential to economic growth?
3. What are the limitations and constraints of the growth model that Singapore is faced with today?
4. How do you think the Singapore government should respond to the country’s productivity challenge? What reforms or changes do you think Singapore needs to sustain economic growth?

9--10:00 CASE 8 DISCUSSION—Donald Low

10:00—10:30 BREAK

10:30—11:00 GROUP MEETINGS TO DISCUSS CASE 9

Case 9: Nam Theun Hydropower Project

Study Questions:

1. What are the risks faced by the Nam Theun Hydropower project?
2. How were these risks allocated among private investors, donors, financiers and the Government of Laos?
3. What have we learned about principles of risk allocation from this case study?
4. Can these principles and practice of risk allocation be applied to other public-private partnership projects?

11:00—12:30 CASE 9 DISCUSSION – Eduardo Araral

12:30— 13:30 LUNCH

13:30—15:30 GROUP PRESENTATIONS

15:30—16:00 TEA BREAK

16:00—17:00 GROUP PRESENTATIONS

17:00—17:30 GRADUATION