



A Consolidated U.S. Development Bank: Reorganizing Private Sector Policy Tools in Emerging Markets and Fragile States

Todd Moss & Benjamin Leo
April 6, 2011

"We need to think bigger... my administration will... merge, consolidate, and reorganize the federal government in a way that best serves the goal of a more competitive America."

-President Obama, SOTU, January 25, 2011

BACKGROUND: Promoting the private sector in low-income and fragile countries clearly supports U.S. national security. First, it creates commercial opportunities for American firms by building markets abroad. Second, it enables countries to meet their own needs and challenges without relying upon foreign assistance in the future. It is a win-win approach. The U.S. Government currently has a large number of existing tools, policy options, and institutions to encourage entrepreneurship and commercial activity abroad. To date, these tools – technical assistance, credit lines, seed capital, and other mechanisms – have not been deployed in an efficient or strategic manner. The fragmentation of effort and lack of cohesion across multiple agencies means that the sum of these parts is far less than optimal. These inefficiencies imply that the U.S. is: (1) losing out on potential commercial opportunities in the next wave of emerging markets; and (2) neglecting a key lever to support stability and prosperity abroad. While the Obama Administration currently is focused on consolidating the various export promotion agencies, an equally compelling case applies to the USG's various international agencies and programs focused on promoting private sector-based development abroad.

A cohesive USG effort to promote the private sector – deploying existing tools at no additional budget cost – could be especially useful in support of:

- (1) Non-Aid Tools in Emerging Economies. Growing middle-income markets (e.g., India, Thailand, Turkey, Nigeria, and Mexico) neither need nor desire major non-military U.S. aid. In these countries, promoting prosperity and stability is in large part expanding markets and economic opportunities for the rising middle and entrepreneurial classes. These are better achieved by using public sector tools to crowd-in private capital such as risk guarantees, seed debt capital, trade finance, or facilitating new private equity funds.
- (2) Fragile or Frontline States. In countries facing complex governance or security challenges (e.g., Afghanistan, South Sudan, Somalia, Yemen, and Zimbabwe), the U.S. and other donors typically concentrate activities on delivering basic services and humanitarian relief. Projects to promote investment and encourage entrepreneurial activity are a necessary component for rebuilding these traumatized societies by creating jobs, economic opportunities, and tax revenues. Indeed, private sector growth is the only long-term sustainable route for such countries to make the transition from dependency and poverty to self-sufficiency and middle-class status.
- (3) Special U.S. Initiatives: Food Security, Clean Energy, African Infrastructure. The White House has committed to promote food security (e.g., Feed the Future) and the development of clean energy for developing countries. Future commitments via the G-20, such as spurring investment in much-needed African regional infrastructure, also may soon be in the pipeline. Budget conditions make major public sector outlays unlikely, adding urgency to drawing in private investment. However, the existing facilities are each stand-alone and not packaged in a manner to help support these initiatives. Currently, many of these also are under increased congressional pressure, which is making them risk-averse and even less creative in supporting wider U.S. policy goals.

PROPOSAL: A CONSOLIDATED U.S. DEVELOPMENT BANK (USDB)

The U.S. should create a USDB, merging the full range of existing policy tools and mandates under its authority, including:

- *Overseas Private Investment Corporation (OPIC)* to provide political risk insurance, debt capital for projects, and its experience initiating and seeding new targeted private equity funds;
- *U.S. Trade and Development Agency (USTDA)* for feasibility studies and other technical assistance;
- *USAID's private sector units* that deal with business climate, land titling, and other business promotion-related issues;
- *USAID's Development Credit Authority (DCA)* which provides partial risk guarantees for financial institutions and bond offerings;
- International programs of the *Small Business Authority (SBA)*, *State (S/EEB)*, *Treasury Office of Technical Assistance (T/OTA)*, and possibly others; and
- Additional authorities to allow USDB to take equity positions and minimal constraints on tied assistance would be important enhancements.

By combining these authorities and programs, this new entity would provide a full range of financial and technical products to build an initiative-specific or country-specific private sector strategy in support of U.S. policy and interagency efforts. The *U.S. Export Import Bank* would remain outside of the proposed USDB given its domestically-focused mandate on promoting U.S. exports and job creation. The *Millennium Challenge Corporation (MCC)* would also be excluded given its broader focus outside of private sector-based development issues (health, education, etc.). However, additional consideration could be given to incorporating various MCC components.

GOVERNANCE: Similar to the existing OPIC structure, the USDB would be a separate government agency, led by a management team appointed by the White House, and overseen by a board that includes both government and private sector representatives.

GRANT-LOAN SPECTRUM: Like other development banks, the USDB could have tiered concessionality windows for different categories of countries (e.g., based on income level and creditworthiness). Offering a full range of products also would permit cross-subsidization. For instance, the cost of technical assistance grants in the poorest countries would be offset by commercial-rate project or trade financing.

NOTIONAL BUDGET: Even with no additional savings or new business lines, the USDB would be self-financing and require no annual budget appropriation. Indicative estimates, based on FY2011 request:

<u>Agency/Unit</u>	<u>USD Millions</u>	<u>Note</u>
OPIC	-189	
TDA	56	
DCA (USAID)	43	Incl. transfer funds
PSD (USAID)	36	Est. 10% of EGAT budget
SBA/OIT	5	
S/EEB	2	
T/OTA	38	
Total Cost	-9	

PROPOSAL BENEFITS: The USDB would:

- Provide a platform for coherence of U.S. policy tools in support of the private sector;
- Allow the U.S. to better compete in new markets;
- Reduce operating expenses;
- Minimize overlapping authorities and conflicting mandates of multiple agencies; and
- Limit the interagency fire drill in support of U.S. objectives.

LIKELY OBJECTIONS:

- Existing agencies will resist ceding authority to a new entity;
- Some may misinterpret a USDB as expanding government;
- Cost is likely to be raised, even if the proposed structure is, at worst, budget neutral; and
- New legislation would be required.

CONCLUSION: OPTIONS FOR STRUCTURE

- (1) An enhanced OPIC could provide the core for the USDB. Building out an existing agency might be easier politically and allow a quicker start, but might also induce greater interagency resistance. OPIC reauthorization legislation could provide a natural window for expanding its authorities and absorbing other USG programs.
- (2) The USDB could be created as a wholly new entity, consolidating the staff, authorities, and mandates of the agencies and programs listed above. This approach might be attractive for a clean start, but there would be additional hurdles and drawbacks in creating a new USG agency.