

CONFERENCE REPORT

CREATING PARTNERSHIPS FOR ECONOMIC EMPOWERMENT IN STRATEGIC REGIONS

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Foreward by Daniel Sullivan (under development)

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Executive Summary (to be completed last)

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Full Remarks and Summary Thoughts of Conference Speakers and Participants

I. Introduction

Daniel Sullivan, Assistant Secretary of State for Economic, Energy, and Business Affairs, noted Secretary Rice's commitment to engaging economic tools to confront current challenges in the Global War on Terror (GWOT) and underscored the importance of the private sector in creating economic opportunities in strategic regions. The purpose of the conference, he continued, was to identify critical challenges in strategic regions and consider ways to foster private sector-led development. Creating jobs and delivering hope to these regions, he concluded, was central to the fight against extremism.

Frances Townsend, Assistant to the President for Homeland Security and Counterterrorism, spoke about the importance of freedom and economic activity as the long-term antidote for the war on terror. The war on terror has two critical parts: the battle of arms and the battle of ideas. The latter depends significantly on our ability to quickly and effectively promote economic development and improve the US image abroad, through partnership between the USG and private sector. Economic concerns involving investments in unstable regions around the world have hindered our ability to improve economic conditions in regions that foster terrorism. The U.S. government and the private sector should exchange information in order to make informed judgments on investing in critical regions. She declared her firm belief that the way to win the battle of ideas is through the U.S. private sector. One way our foreign counterparts perceive Americans and judge the U.S. is based on interaction with our private sector. Thus our private sector is an important tool in winning the battle of ideas. Government partnership with the private sector is also important within the U.S. For example, the private sector was able to move relief supplies and equipment much more quickly than the USG after Hurricane Katrina. The private sector is an important aspect of our diplomatic agenda.

II. Defining the Challenge: Economic Empowerment as a Strategic Imperative

Topics in this discussion group focused on the nature of the global counter-terrorism/counter-insurgency challenge and why it matters to the United States; economic factors and the exploitation of poverty and underdevelopment by terrorist and insurgent elements; and corruption, tribalism and insularity as obstacles to global economic integration.

What is the challenge?

Discussion Leader: Juan Zarate, Deputy National Security Advisor for Combating Terrorism, said that understanding the nature of the enemy and the narrative they tell are the most important challenges we face, as terrorists will attempt to frame events and exploit them accordingly. For example, Al Qaeda claims that the West is at war with Islam and this is the reason for the chaos and misery Muslims experience in their daily lives. USG responsibility is to counter this narrative and to make our policies clear in the sense of what we want to achieve and the end state we hope to obtain. The U.S. is the most philanthropic nation on Earth; but its reputation does not reflect this fact. Delivering humanitarian aid directly affects people's lives and changes their perceptions. Everyday both the State Department and the U.S. private sector do great things around the world but we aren't drawing on these stocks of good will to create a new narrative. The private sector has the ability to directly affect the foreign perception of the U.S. through real-world actions such as foreign direct investment in education and women-run businesses. We must figure out how to leverage the private sector to meet both private sector needs and our security interests, as well as effectively counter our enemy's narrative.

Henry Crumpton, former State Department Counterterrorism Coordinator, spoke about the emergence of a new type of global warfare due to four main variables. First, enemy actors are adapting to our military preponderance by forming operational units that are smaller and thus harder to locate and penetrate. Second, these micro-actors increasingly have macro-impact because of growing sophistication of tradecraft, communications, and weapons. Third, the battle space is global: enemy forces can, for example, harness the instruments of cyberspace to communicate, recruit, train or raise funds. Micro-actors with macro-impact are operating with speed and agility in this global interchange. Fourth, although the state is still the primary means of organizing ourselves in the international arena, the relative importance of non-state actors is on the rise. Non-state actors include both our enemies and some of our most effective allies, such as tribal leaders, clerics, NGOs, multinational corporations, or educational institutions. The challenges of operating in this new era of conflict are substantial and most are not military; thinking in terms of counter insurgency strategy, hard power only accounts for 10-20%. One part of this challenge involves intelligence. We need to understand not just the physical terrain on which we engage our enemies or allies, but the economic, social, political and cultural terrain. We also need to engage the enemy, going beyond traditional instruments of statecraft, and focusing on the local level. We need to harness the economic power of the United States. Think of our economic might and compare that to the economic power of al-Qaeda or Hizbollah – there is no comparison. With the help of the U.S. private sector we can provide enduring solutions at the micro-level that benefit the U.S. as well as the lives of those vulnerable to recruitment into terrorist networks. To do this involves risks and opportunities, and will take real leadership on the part of both the U.S. government and the private sector.

What are we doing now to deal with these challenges?

John Herbst, the State Department Coordinator for Reconstruction and Stabilization, opened the discussion by saying his office (S/CRS) was created after operations had already commenced in Afghanistan and Iraq and it became clear that military engagement alone was not enough to maintain and promote post-conflict reconstruction and stabilization. The office was established to organize the civilian side of the U.S. government to work as a unified team with the military in unstable, post-conflict countries. As part of this mandate, S/CRS has also been charged with forming a Civilian Reserve Corps, a reserve of civilian professionals who could be deployed overseas within 48 hours. The CRC, modeled on military reserves, would assist and support the establishment of government functions in war-torn countries.

Lt. Gen. William M. Fraser III, Assistant to the Chairman of the Joint Chiefs of Staff, stated that military measures alone are not enough. Our nation's strategic objective is not attainable without a unified and comprehensive approach both at home and with our partners abroad. We must become more adept at integrating efforts to contribute directly to U.S. foreign policy and our objectives. Stability operations are at the core of the U.S. military mission, and seek to create an environment – characterized by the rule of law, civil society and democracy – where crucial “bottom up” economic development can take place. A new Department of Defense directive that gives stability operations priority comparable to military planning goals which represents a significant policy change and demonstrates the importance DoD has accorded to establishing partnerships in capacity building. Rebuilding the private sector and the construction of new infrastructure require a robust partnership among military, civilian government, and private sector actors to drive economic recovery. The role of the military, therefore, will be informed by civilian activities in post-conflict reconstruction, with the private sector playing a key role. For example, the top military commander in Iraq, General David Petraeus, said the solution to counter-insurgency in Iraq is only 20% military; the remaining 80% of the solution will require political and economic stabilization with assistance and support from the private sector. But these activities cannot always take place sequentially; they necessitate concurrent action by the military and civilian entities. In Iraq and Afghanistan, Provincial Reconstruction Teams (PRTs), blending military and civilian expertise, are essential to success and stability there and have already been useful in establishing important lessons learned.

Robert Mosbacher, Jr., President and CEO, Overseas Private Investment Corporation (OPIC). I want to thank Assistant Secretary Dan Sullivan and his staff for organizing this conference and Ambassador Hank Crumpton for helping inspire it. He is sorely missed in the counter-terrorism arena, but much appreciated for his service to our country.

I would like to just quickly give you what we call "OPIC 101," because it is important for you to know exactly what we do. We are an independent agency of the Federal Government. We were created 35 years ago to help facilitate and mobilize U. S. private capital investment in developing and emerging-market countries. We do so with a look toward not only if it is a good business deal, but also if we can have a positive developmental impact on the host country. We try to support and reinforce American foreign policy.

We have three product lines. We have political risk insurance that protects the buyer against expropriation, currency inconvertibility, and political violence. We have loan guarantees or investment guarantees, and then direct loans. And we have private equity funds where we identify a country or region where we want to stimulate investment, we put in between a third and a half of the fund in the form of senior secured debt. Then the fund manager goes out and raises the balance and makes the investments.

So, that is what OPIC does. We are a risk mitigator and a development agency, and we can help work with financial institutions to help share risk when they go into countries. If our friends at Ex-Im can't help you, give me a call.

The threats and challenges facing our country are complex and numerous. As much as we try to understand and relate to different cultures and attempt to help them understand the true nature of the American people, there is a level of hostility which is difficult for many of us to understand. However, there are at least two basic aspirations which every society shares no matter where it is or what the dominant culture: to be secure from violence and to provide for one's family.

These two basic needs are fundamental, and they are inseparable. Sustainable economic development will not happen where widespread violence and conflict exist; and stable, secure societies cannot emerge where rampant, abject poverty exists.

Former Israeli Prime Minister Shimon Peres is fond of saying that unless tangible economic progress is experienced by average men and women in the heart of the Middle East, resulting in the financial fortunes of the Palestinian people being intertwined irrevocably with those of the Israelis, negotiated peace agreements will not endure. In other words, despite years of conflict and seemingly insurmountable hatred that divides Arabs from Israelis, one of the keys to peace in the Middle East is developing a dynamic, integrated regional economy where the opportunity for a better life is not just a hope, but is a reality.

Just as it has been said here that the best welfare program in America is helping someone get a job, it can also be said that the best way to fight terrorism and the support for terrorism around the world is to help others get jobs. Create more

economic hope and opportunity in Iraq, Afghanistan, the FATA area of Pakistan, and in the Philippines, just to name a few, and you will begin to drain the swamp that breeds terrorists.

But this is much easier to say than it is to do and we must face the fact that there are some things our Government does well and there are things we could do much better. For instance, normally, we are quite good at humanitarian assistance, and at providing foreign aid to support building institutions for governance and infrastructure. We are also good at advising and encouraging governments on the steps to take in order to create a more attractive environment for business, and at explaining the advantages of open markets and free trade.

However, there are some things our government does not do as well and one of them is stimulating quick and tangible economic growth in targeted countries, particularly when time is of the essence. Given the clear correlation between poverty and terrorism, and the "real time" pace at which the war on terrorism is being waged, we cannot afford to do less than our best when it comes to kick-starting economic activity in these countries.

We need to develop a new approach. We need an approach which enables us to bring to bear all the economic assets at our command and enables us to harness more effectively the extraordinary financial resources of both the public and private sectors. What might such a new approach look like? It would be based upon four fundamental suppositions.

First, while military assistance and foreign aid is an essential part of stabilizing weak nations and helping them transition from subsistence towards self-sufficiency, long term sustainable development can only be driven by private sector investment, both foreign and domestic. This may seem obvious to some and yet only recently have many development experts come to this realization.

Second, whatever public sector resources are brought to bear on a given country or region must be better planned, coordinated, and accounted for if these resources are to maximize the impact and benefit on the recipient country. That is precisely the goal of the current review of foreign assistance programs underway within the Administration. But beyond the State Department and USAID, there are DOD programs, USDA programs, USTR trade preferences, MCC Compacts, TDA feasibility studies, EXIM export finance, and OPIC support programs, all of which should leverage and complement each other better.

Third, the billions of dollars that the U.S. Government spends in foreign assistance around the world pales in comparison to the hundreds of billions of dollars invested and spent by American companies, philanthropists, non-profits, and NGO's. Without expecting anyone to subscribe to a particular administration's agenda, there must be a

more dynamic and inter-active dialogue among the various U.S. participants overseas, particularly as it relates to the developing world and the war on terrorism. The goal must be to identify and institutionalize acceptable forms of public/private collaboration.

When the Chinese target a country or region, whether it is to gain access to natural resources or to acquire market share, they speak with one voice. The United States speaks with a thousand voices and while that freedom is one of our great strengths, we must do a better job of finding and articulating our common interests.

Fourth, and finally, it is important to recognize that even in countries where recent developments would seem to make economic growth as opportune as at any time in recent history, it rarely happens quickly, and sometimes not at all. Whether it is the end of armed conflict, the democratic election of new leadership, or the adoption of new economic policies which are intended to open previously closed markets, there is often a very disconcerting delay between the change in circumstances and visible proof of economic progress.

The quality of the political leadership and their commitment to transparency and the rule of law can certainly accelerate the process. However, there is a tendency to think that unless the legal and regulatory framework for business investment is just right, investment will not happen. In other words, the assumption is that creating a favorable business climate, and the advent of private investment must happen sequentially. That is simply not true. These things can, and should happen simultaneously. One of the principal reasons why OPIC exists is to help mitigate those risks while countries are in transition.

For example, OPIC supports over \$1 billion of low and moderate income housing development around the world. We do so because we are a development agency and there are few, if any investments which are as broadly beneficial as housing development. And yet, if we waited until every country had adopted a comprehensive system of title registration, we would not be doing one-tenth as much. So, in answer to the question can economic progress take place despite significant legal, regulatory, or governmental obstacles, the answer is an emphatic yes.

What is needed is a highly coordinated combination of public and private sector initiatives based upon the priorities of the host government, the particular history and needs of the local economy, and the input of the private sector on the ground. These initiatives should be aimed at accomplishing several goals concurrently: facilitating investment that creates jobs; addressing critical infrastructure needs that impact the quality of life and inhibit economic growth; and identifying the most important legal and regulatory reforms that would lead to further investment and growth. This is not to diminish the importance of helping build institutions for governance or strengthening the delivery of critical social services. Rather, it is to suggest that we must pursue a

variety of initiatives at the same time with a greater sense of urgency, and a stronger sense of accountability.

Let me give you an example of the kind of investment that will create jobs quickly. No matter what the country or region, there is a private sector that is made up of traders, builders, farmers, or just plain entrepreneurs. And yet, most have no access to credit on terms they can afford. It is our experience that the best way to kick-start economic activity and create jobs is to provide affordable credit at a number of levels. Micro-credit is necessary for the bottom tier and can help many generate enough income to feed themselves and their family.

The level just above that, and where the greater job creation will come, is the small and medium sized business sector. That is where loans at reasonable interest rates and for longer tenors can be transformational. Along with the increased access to credit must go the technical assistance to both the lenders and the borrowers about how to qualify, service, and price such loans. Not every financial institution needs the help, but most do because they simply have no history of having made SME loans. This is the approach that we are taking in the West Bank and Gaza Strip where OPIC will be part of a \$160 million small business lending facility provided through Arab banks.

In terms of critical infrastructure needs, those are usually easy to identify. Again, in our experience, electricity repeatedly emerges as a need which would both improve the quality of life and facilitate economic growth. Addressing those needs quickly while the longer term solution is being developed, is something that we should emphasize more. If you want recent proof of how important an increase in the availability of electricity is to the local perception of progress, ask Liberian President Ellen Johnson-Sirleaf who committed to get some lights on in Monrovia by a date certain, and delivered.

It is concrete evidence of economic progress that is necessary to win the hearts and minds of those who we hope to influence in the war on terrorism. But in order to facilitate that progress, we must get much better organized at the Federal level, enlist the active involvement of the private sector early, be prepared to put business teams on the ground to identify and develop projects, and then finish the job no matter what the challenges. We cannot afford to fail.

III. Current Strategies and New Possibilities

What is the private sector doing?

David McCormick, Deputy National Security Advisor for International Economic Affairs, noted key points for discussion. These include:

- Learn what the private sector is doing to create jobs and economic empowerment;
- Unique role the private sector can play in conflict regions;
- Successes and failures of the private sector in operating in strategic regions.

E. Floyd Kvamme, Partner Emeritus, Kleiner Perkins Caufield & Byers, gave two examples of successful private sector job creation in Israel and Thailand.

- **Israel Research & Development:** In the late 1970s, engineers were few and hard to come by. A few Orthodox Jews in his company wanted to establish a base of operations in Israel. Today Israel is a significant exporter of technology and R&D because of these men.
- **Thailand:** In 1967, a team was sent into Bangkok to build a plant where labor costs would be much lower. Unemployment in Bangkok was 70% and new jobs were created. Direct investment in this area was a significant factor in stopping the “Thai” domino from falling in the wake of the Vietnam War. People value jobs and promotions.
- Both are examples of Foreign Direct Investment with strong government leadership.

The discussion focused on how to stimulate venture capitalism:

1. Multilaterals move portfolio toward **Foreign Direct Investment**
2. Have an **Exit Strategy**
3. Hire **young people** who are willing to do what is thought impossible (i.e. internet/semi-conductor businesses led by people in their 20's)
4. Strong **leadership** to create a coalition of partners
5. **Intermediaries** at both the international and local levels to collaborate on the ground in order to build trust. Partner with women's groups and NGOs.
6. **Vision**

Stuart Hart, Professor of Management, Cornell University, described how terrorism can be defeated through the economic empowerment of “Tier 4” / “Bottom of the Pyramid” (BoP)—the 4-5 billion people (two-thirds of the world's population) whose annual income is less than \$1,500, and who have not received the benefits of globalization. Among the root causes of terrorism itself is a lack of economic opportunity caused in part by the failure of global capitalism to reach the BoP populations. Associated factors include corruption, inequity and frustration due to lack of options and opportunity. Multinational corporations (MNCs) can help solve this problem by focusing on the heretofore neglected Tier 4 market and creating adaptive solutions that treat the “aspiring poor” as business partners and not recipients of charity.

To successfully capitalize on the potential of Tier 4, MNCs will have to shed long-held assumptions regarding the poor: a) that they cannot be profitably targeted as consumers, b) that they have no use for current technologies, c) that they categorically lack entrepreneurial acumen, d) that they cannot afford, and have no use for products and services sold in developed markets. MNCs will also have to develop new business models and products with their Tier 4 partners (and perhaps NGO partners as well) that reflect local community needs, preferences, cultural norms and budgets. This formula has proven successful for numerous MNCs, most famously Hindustan Lever Ltd. of India.

In one example of successful public-private collaboration, SC Johnson organized youth groups in slums to clean up their neighborhood. This has turned into a joint business arrangement for cleaning services. Lesson is begin with engagement, not a pre-determined solution.

Jim Kimsey, from the Kimsey Foundation, mentioned a few life experiences. Military security and political stability are necessary but not sufficient. The real test of whether a state will achieve stability is the economic fabric we use, particularly among its middle class. Industry and job creation result when people are taught what to do and organized economically. When dealing with Iraq, our hope is that the employment of locals would create economic underpinnings for something that would bring hope to a dysfunctional country. Private industry is in a unique position because it is not constrained by bureaucratic rules like the government. Private industry will play a critical role in economic development in these regions because businesspersons have the unique ability to recognize human behavior patterns are the same around the globe and know how to organize people to their benefit.

The discussion focused on how to stimulate venture capitalism and the need for an exit strategy. Multilateral financial institutions are needed to move things forward on the ground in developing countries. One essential ingredient is leadership. Orchestrating multiple players to work together, creating a coalition of partners, takes great leadership. Intermediaries at both the international and local levels collaborating on the ground are the way to build trust. Trust will also be gained if the locals know our true motivations, and that way local populations won't be suspicious of our intentions. We must pursue innovative activities such the production of biofuels in tropical countries.

What public-private partnerships already exist? What is working?

Dina Powell, Deputy Under Secretary of State for Public Diplomacy, led discussion with the following questions:

- What models do we think work best and have already been successful?

- What are the preconditions for successful, high-impact economic empowerment projects?
- How can the government best support private sector efforts in strategic regions?
- How do we, the public and private sector, move forward together?
- What constitutes success and how do we measure it?

Patricia Sellers, Editor-at-Large, Fortune Magazine, described the recent success of the FORTUNE/U.S. State Department International Women Leaders Mentoring Partnership. The program paired 17 emerging women leaders from 14 countries (selected by US embassies) with mentors from the FORTUNE Most Powerful Women Summit for two weeks, during which mentees learned best practices, organization, and management skills. Part of the project's success was its lack of bureaucracy. An example of this success is that two of the mentees from Kenya started a mentoring program for women and several girls' schools.

Karen Holbrook, President, Ohio State University, emphasized the importance of education to American public diplomacy. Numerous educational programs, she noted—the Fulbright Fellowship, the Ford Foundation International Fellowships Program, and others—have opened the US to foreigners, and in doing so helped cultivate a positive image of this country abroad. Other important programs include the President's Summit. However, practical challenges continue to hamper these efforts: many foreign students are still unaware of the programs' existence, and remain unfamiliar with the quality and scope of American higher education. Cost is also a significant obstacle, though many universities are defraying some of the cost with alumni donations and fellowships; in addition, some countries, like China, offer scholarships and financial assistance for foreign study. Stringent visa requirements also prevent some qualified students from participating.

Lila Ibrahim, Chief of Staff, Intel Corporation, described how a public-private partnership between Intel and the Lebanese government helped the company meet the challenges it faced when it decided to expand its presence in the country. Cooperation with the government, Ibrahim pointed out, helped Intel bypass bureaucracy and coordinate the efforts of experts from both sides. Ibrahim also noted that the arrangement—which benefited from Intel's relationship with the State Department and USAID—proved mutually beneficial: jobs were created in Lebanon, and Intel increased its visibility in the country. In addition, Intel's relationship with the State Department and USAID was an incentive for more employees to engage in the project.

Technology infrastructure was also an important component in Intel's plans. Connected communities give the Lebanese people access to the world's technology but Intel's challenge was how to develop twenty-first century skills in higher education. Amid doubts about whether Intel should really be operating in Lebanon at all, Intel realized that it was already operating in several tense areas and that no outcome is ever guaranteed.

John Sullivan, Executive Director, Center for International Private Enterprise, described the importance of cross-border institutional and corporate partnerships to development. Strong partnerships, he argued, form the foundation for hiring qualified local talent and working within existing local legal, cultural and economic frameworks. The successful development of foreign informal sectors—where three-fourths of the world’s markets are “locked”—depends on the existence and quality of these partnerships.

Working in conflict/post conflict countries requires:

1. Finding and cultivating local talent to develop ideas and champion reform
2. Understanding the local economy and markets, and why people take certain actions.
3. Identifying key points of change.
4. Mobilizing local business associations voluntarily.
5. Engaging the private sector directly, and not relying solely or primarily on government-affiliated business chambers.
6. Providing technical assistance in legal reform (eg, Pakistan rewrote Chamber of Commerce law).
7. Managing expectations and conveying a message that lets people know they are going somewhere.
8. Investment by MNCs in local associations.

John D. Negroponte, Deputy Secretary of State, discussed the nature of terrorism and described the private sector’s role in the GWOT. In spite of the US’s successes in the GWOT—most of al-Qaeda, he noted, has been killed or captured—work remains because terror is a “globe-spanning phenomenon.” Terrorists, he argued, succeed by recruiting youth who have become alienated from the globalized world. The solution is the enfranchisement of these people by changing their condition; military solutions alone will not be sufficient to vanquish fundamentalist ideology. Deputy Secretary Negroponte cautioned that this was easier said than done, and pointed to programs like “Businesses Building Bridges,” which forges relationships with the Afghan private sector, as models to emulate.

IV. Breakout Sessions: Pakistan, Iraq and the Philippines

FATA/Pakistan-Afghanistan Region

Robert Mosbacher, Jr., President and CEO, Overseas Private Investment Corporation (OPIC), noted the topics to be discussed, including: Unique challenges for in-country private sector engagement; security and business

environment issues; economic development case studies; successes, failures and lessons learned; and hitherto-unsuspected ways in which the private sector help can advance economic development in strategic regions.

Lt. Gen. David Barno (Ret.), Director of Near East and South Asia Center, National Defense University, discussed “Challenges the military faces in the three wars of Afghanistan”:

- 1) War against senior leadership of terrorist organizations, including Mullah Omar, Osama bin Laden, and other Qaeda and Taliban leaders.
- 2) Conducting operations to defeat networks belonging to senior leaders. Military forces are working together to disrupt terrorist networks. The military is building intelligence in an effort to know leaders’ whereabouts.
- 3) The military needs to know how their objectives affect Afghans. Internal forces are always trying to pull Afghans apart. Any operations against terrorist forces take place within this context, therefore it is imperative that an effective government is implemented. The people of Afghanistan are the most important focus and winning the hearts and minds of the people remains a top priority.

Khalid Tiwana, Director, Worldwide Government Affairs and Public Policy, Levi Strauss and Co., noted that Levi Strauss has had a presence in Pakistan for twenty years. Pakistan has a rising middle class, and the reason representatives from the company attended the conference is Levi Strauss’s interest in the Reconstruction Opportunity Zones (ROZ) in Pakistan and Afghanistan. Success is contingent on zones where business can be implemented and sustained. There needs to be a mixture of certain economic and global reforms. The Federally Administered Tribal Areas (FATA) are economically and educationally deprived, creating a breeding ground for Al-Qaeda. If the ROZs are placed in the FATA, it will be a non-starter. The areas are like the “OK Corral with an AK 47,” and the Pakistani Government doesn’t exist there. We also need to look at areas where the Pakistani Government exerts sovereignty and create opportunity in areas on the periphery of FATA. If we do not have a deeper understanding of what is happening on the ground we will not be able to move forward with development.

Muhammad Aslam Khan, Charge d’Affaires, Embassy of Pakistan, emphasized the importance of adopting a comprehensive approach in the fight against terrorism and articulated the Pakistani Government’s perspective. Economics has always been integral to President Musharraf’s “holistic” terrorism policy, which views security, governance and business as interrelated. The Pakistani plan to develop the FATA region includes improving security, building infrastructure, and investing in human resources. The US can assist with investment in human resource development

(education), building of infrastructure and by expanding US market access for Pakistani goods.

Lisa Chiles, Deputy Assistant Administrator for Asia and the Near East, USAID. These tribal areas have a unique status, but have gone through a process of economic development. In many ways this is very encouraging. These areas have problems but have several positive characteristics. Why have these areas lagged behind? We can partly blame tradition and way of life, but at the same time we must keep in mind that in the recent past these areas were the thriving gateway to South Asia. The people traveling from North to South Asia passed through this region. In the recent past there were problems due to the development process. Many of these people are hardworking and enterprising, and in many ways they are also open to free enterprise. They have been successful in the hotel industry and in investment. However, in many of these areas the local means of subsistence do not exist. These people were in the process of integrating in the country in a positive way but this process was interrupted. We cannot write these people off. This area can be developed in a positive way provided that the right conditions are created. And, it is entirely possible for these conditions to be created. The central message is optimistic as far as this area is concerned.

The private sector is compatible with the predominant cultures in these regions. In many ways the region's population have long engaged in free-market competition. The private sector can play an important role. The local population has experience in human resource development. This is why President Musharraf emphasized that the holistic approach.

Kevin Murphy, President and CEO, J.E. Austin Associates, provided an overview of Pakistan's economy:

- 2 million people per year have been pulled out of poverty in the past 5 years.
- 160 million people live in Pakistan, which represents a large market
- Almost 7% GDP growth in the past 5 years
- European competitors are already in Pakistan

J.E. Austin Associates is currently working on five projects in Pakistan. The company is also in China, India, Kazakhstan, and the Middle East and their economies are growing rapidly. Growth [in Pakistan] has averaged approximately 7% in the last two years. There are also opportunities for American companies to invest. In addition, Pakistani leaders make excellent partners. Once technology and markets are provided, one finds Pakistanis willing to invest.

- The industrial park in Peshawar near FATA is doing quite well and presents opportunities for expanded investment. However, many of the people who want to invest in these areas are unable to do so. This is one of the reasons the authorities should consider expanding industrial parks. Moreover, doing this could draw more investors and begin the process of investing in Peshawar. Natural resources like gems, cement and marble are coming from Pakistan and construction materials are booming. Demand for furniture, fruit juices and dairy products is on the rise. It has been said that Pakistan is one of the most dynamic countries in the world. Improvements in the microeconomic environment and major improvements in macroeconomics are a reflection of this phenomenon. Organizations like USAID have worked directly with investors giving them the opportunity for investment. If the 'Reconstruction Opportunity Zone' project is to be successful it must be accompanied by supporting infrastructure.
- As Prime Minister Aziz recently said, challenge the government to look towards markets, not government. If the U.S. allows duty free access to its market for Pakistani and Afghani goods, Pakistan may not immediately see a huge increase in investment, but it will be successful in the long run because Pakistani companies will invest – in fact, a few have already expressed interest. American jobs, meanwhile, will not vanish simply because of duty free access to goods from Pakistan. Long-term investment in these areas is on the rise: Nestle is willing to put a plant in Peshawar, for example. Dairy farms will be built in the earthquake-affected areas and a Pakistani firm owned by women is making wonderful products in Peshawar. However, there are still many impediments to long term investment in these areas, and the infrastructure environment still falls short of what is needed. The government must support reconstruction in these opportunity zones. Despite the challenges, these areas are a great place to invest and the time is now.
- **Robert Mosbacher, Jr.:** One of the greatest challenges facing these areas is the lack of basic necessities. Issues such as a shortage of electricity continue to be a major complaint of tribal leaders. Antiquated machinery is another problem. Although organizations such as OPIC have invested more than \$200 million, they have not addressed many of the root problems. According to marble manufacturers in the area, old machinery results in nearly 70% of harvested marble being wasted.

QUESTIONS AND ANSWERS:

Q: Our company was able to get a loan from OPIC and it is building dairies in Pakistan this year. We were able to attract large banks as there is zero shortage of investors in Pakistan and we also find the ROZ's to be very intriguing. Sweetwater is a long term player in Pakistan. The thing that I find fascinating is that if Levi Strauss is saying no to ROZs then why are other companies saying yes?

A: Levi Strauss representative said that his company supports the ROZ program, but wants to make sure it is done correctly. To have success we need to get in the trenches and make it work. These ROZs should be in the provinces near the FATA. If the environment improves, we will be able to attract laborers from FATA and show people that you can invest in it.

A: A Wal-Mart representative commented that, "The State Department needs to be serious about this and we need the administration to be clear about these types of operations." We would then have more opportunities if we could restructure what is currently in place and place greater emphasis on security. In the Wal-Mart operation the company is responsible for everything that is put on the boat: rules of origin, [intent], and security (Port Qasim). An important consideration for Wal-Mart is what kinds of products they will actually be able to "pull out" of Pakistan.

A: Black & Veatch has worked in Pakistan for many years and designed a number of power plants. If you do not have electricity, water and roads then you have a problem. Karachi has a water problem that is just waiting to explode and infrastructure is a major issue as well. Then there is corruption, which has led Black & Veatch to exit work on infrastructure. The notion of competition with U.S. firms needs to continue. Unfortunately, there are not many American engineering firms involved in Pakistan at this time. We can work together, but the U.S. government needs to work on client management in both ways.

Q: How does China's activity in Pakistan affect the U.S.?

A: The Chinese are the ones who are currently building Gwadar port in Baluchistan. We suffer competitively with China. We see this particularly in West Africa where resources matter. Many years ago we saw the China problem. A company would come out with a product, which would then be copied by China into hundreds of companies. As a result, checks and balances were created. Ultimately the U.S. simply cannot compete with China's products. The goal is to create opportunities for people in the FATA areas. Many people regularly travel outside these areas to make money. If ROZ's were created in areas where money was available then more stakeholders could be utilized. Diaspora linkages are also important. There are U.S. citizens who come from this general area. These Americans could be the go between, which would start the communication that people from FATA would like to see. Initiatives like this have the potential to create a lot of industry. The biggest business in Pakistan will be textiles. This is why it is imperative that textiles are included in the ROZ initiative. The Chinese are successful because they are consistent where the Americans are not. Americans need to create success in a manner which is sustainable.

Q: Let's be practical and look at options we have not looked at before. Would it be possible to train a number of people coming from tribal areas in Karachi, encouraging them to bring their skills back to the tribal areas?

A: The training can be arranged outside the target areas. And, these people have never been shy to settle in Karachi, Lahore or even abroad. When looking at infrastructure development areas, a few things must be taken into consideration. What is of utmost importance in the Government's priorities and where can the ROZs be located? And what are the Pakistani Government's actual priorities for the ROZ's ?.

In order to empower the population in these areas we have to move in a systematic and sensible way. We cannot set these facilities up at this time, but we could set up close by. It is important to note that the entire region is not in a state of conflict as the troubled regions are few. Therefore, we should set up in the tribal areas where there are fewer problems. Once people develop confidence that things will change in a significant manner it is likely that the entire environment will eventually change.

Although people are encouraged by Musharraf's remarks, they are worried about his strength and his ability to carry out his plans. Meanwhile, a bridge needs to be built between Asian countries and the U.S. We're going to have another meeting with Malaysia and we are trying to get people to sign up for action steps. This may ultimately cause a surge of modern elements in the country. We need to include the U.S. in this process as well. The United States could also work on its customs procedures as it usually takes Pakistanis approximately three hours to get through Customs. OPIC and the U.S. Trade and Development Agency have been helped by tripartite planning. They have addressed issues in Pakistan such as energy, health, and communications.

If we connect the diaspora communities abroad with Pakistan then we will be able to put in electricity and will get farther. Although it is important to talk about Pakistan from a strategic level we need to think about supporting Pakistan's economy at a local level. We also need to think creatively about how to address travel advisories. We need to think in terms of new entrance of exporters to the US. Another concern is competition from countries in the region benefiting from FTAs.

What if you were to find talented Pakistani American graduates in economics and put together a really good team who could go to the tribal areas? These graduates could combine basic business plans and link up young people with good business experience who could then take these plans to the next level. Their job would be to find leads for OPIC and it is possible that such people could create opportunities for early investment. The important thing is that we do it as we are trying to develop economic capacity. These things are not going

to happen soon enough if people on the ground are not developing business plans, a concept with which we have found they are frequently unfamiliar.

Why not take the younger generation of tribal areas in FATA and launch a program where their children could get a taste of an American education? The British took the children out of tribal areas, educated them and then gave them land.

Philippines/Mindanao

Eric John, Deputy Assistant Secretary of State, Bureau of East Asian and Pacific Affairs

- The active presence of Jemaah Islamiya (JI) and Abu Sayyaf Group (ASG) create the need for a continued and comprehensive counterterrorism approach in South East Asia;
- In Mindanao, including the Sulu Archipelago, longstanding separatist conflicts have contributed to giving this region, where a quarter of the country's population of 90 million live, the highest levels of poverty in the country;
- The ensuing lawlessness provides physical sanctuary for domestic and international terrorists, leaves many susceptible to terrorist ideologies, and makes the Sulu Archipelago the key transit route for terrorists and criminals traveling between the Philippines, Indonesia, and Malaysia;
- Since 2002, U.S. Special Forces have been working with the Armed Forces of the Philippines (AFP) through training and intelligence support to build a long-term self-sustaining capability to provide security;
- This partnership achieved remarkable success, driving the ASG out of the island of Basilan after only two years. Recently, the AFP has conducted a campaign since August 2006 that resulted in the deaths of ASG terrorist leaders Khadafy Janjalani and Abu Solaiman;
- Sustaining this military success is dependent on winning the local population's support. For this reason, USAID is working closely with the local population in Mindanao to improve schools and hospitals, construct roads, and provide electricity and clean water to many remote villages for the first time. Sixty percent of U.S. development assistance to the Philippines goes to Mindanao, particularly areas impacted by terrorism and violence.
- The long term prospects for stability depend on economic growth, which will require substantial private investment. We're here today to discuss what needs to happen to foster that investment.

Willy C. Gaa, Ambassador, Republic of the Philippines

I wish to thank the Department of State for inviting me to this important conference. I am privileged to be in the company of such distinguished guests, given such an important topic on **Creating Partnerships for Economic Empowerment in Strategic Regions** or what I simply call the "Business of Peace."

At a *Freedom House* Conference on Democracy and Development last January, USAID commended the Philippines, together with Egypt and Indonesia, for maximizing the positive synergy between both dimensions, within the context of the Community of Democracies.

As the oldest democracy in Asia, the Philippines is considered as one of the working models of "development democracy"—a development model anchored on enlightened government policy activism. Public-Private Partnerships are key to this brand of Philippine democracy. The Philippine brand follows a very challenging and dynamic process of pursuing democratic and economic reforms.

"Public-Private Partnerships," What's In a Name?

Public-Private sector partnerships (PPP) demand that states and governments should improve their national capacities to design and deliver policies as well as achieve results. These partnerships call for greater accountability of governments to their citizens and sound policies that will have positive impact on people's lives. Each Public-Private Partnership is a government's pledge to its people, mobilizing the strategic resources of the private sector and the social capital provided by civil society.

The Philippines pursues a Public-Private Partnership framework which aims to enhance the country's global competitiveness (RP is now considered as one of the Centers of Excellence in Business Process Outsourcing or BPO). A National Competitiveness Summit held in Manila in October last year was anchored on a PPP framework. During the Summit, President Macapagal Arroyo exhorted both the government and business leaders to "pursue targets that are tough but achievable."

Pursuing the peace agenda in the Philippines is tough but achievable, daunting yet doable, complex yet never cumbersome.

Partnerships for Peace: Some Innovative Cases

How can Public-Private Partnerships work to pursue the agenda for peace in Mindanao? Mindanao is blessed with an expansive territory, beautiful natural resources and a vast potential for human capital, yet Mindanaoans have yet to reap the island's bounty.

Let me cite several innovative cases and initiatives in Mindanao employing the Public-Private Partnership framework.

One outstanding example is **Paglas Corporation/La Frutera, Inc.** based in Maguindanao, Mindanao, a “no man’s land” more than 20 years ago. Paglas was a town that has been torn by violence from Islamic and communist insurgencies, personal vendettas and local political rivalries. Datu Ibrahim “Toto” Pendatun Paglas III was then the mayor of the town. In 1996, realizing that the culture of violence could not go on, Datu Paglas started negotiating with investors, with assistance from the Philippine Board of Investors (BOI), to establish a banana plantation in Paglas. His top priority then was to earn the trust of and prove to the investors that investment in Paglas could work.

Today, Paglas is a bustling banana plantation with more than 2,000 workers. It is a highly unusual business venture that brings together Italian and Saudi traders, Israeli farming experts, Cincinnati-based Chiquita Brands International Inc. and top Moro Islamic Liberation Front (MILF) commanders. More than a successful business venture, the company has given the local community a stake in peace. Former guerillas or military combatants now speak with a sense of pride about being able to send their children to school. As cited by the International Herald Tribune in its article dated 11 September 2006, the Paglas story has become “a shining example of the potential for jobs and a little economic prosperity to change the dynamics of the conflict.” Paglas is the only Muslim town in the Philippines where Jews and Muslim rebels are working together for bananas.

The Philippines is at the forefront of promoting Corporate Social Responsibility (CSR) or Corporate Citizenship, a business strategy and practice which incorporates the triple bottomline concept: financial viability, social accountability, and environmental sustainability. Simply put, CSR means “doing well while doing good.” The **Philippine Business for Social Progress (PBSP)**, a private and non-profit foundation of 214 international and national Member Companies dedicated to promoting business sector commitment to social development, pursues the Mindanao Peace and Development Program (MPDP) which mobilizes the business sector, civil society, and local governments to be involved in programs (e.g., functional and simple literacy; delivering basic health care services; productivity and income improvement projects such as vegetable/organic farming, buying and selling of marine products; community-building/community development) that contribute directly to the long-term peace and development in Mindanao.

A creative program of the **Prince of Wales Business Leaders Forum (IBLF)** and the **British Embassy Manila**, in partnership with PBSP, is the **Young Muslim Professionals for Business and Peace (YUPPEACE)** which aims to enhance the knowledge and skills of young Filipino Muslim professionals through internship and technology transfer from British firms into the Philippines. Host companies are also

encouraged to adopt internal management policies that promote cultural unity and diversity in the workplace.

At the multilateral level, examples of Public-Private Partnerships are the initiatives of the **World Bank, USAID** and the **Asian Development Bank (ADB)** in Mindanao. The World Bank is supporting the GRP-MILF (Moro Islamic Liberation Front) Peace Talks by way of leading a **Multi-Donor Trust Fund for Mindanao**, intended in post-peace agreement humanitarian, rehabilitation, and development of conflict-affected areas in Mindanao.

USAID has supported not only Mindanao development but also post-conflict activities such as the reintegration of rebel returnees. To date, USAID assistance to Mindanao has assisted 28,000 former combatants who took up farming seaweed, hybrid corn, rice, or high value crops; generated US\$441 million in investments; and created 77,000 jobs. Around 60 percent of total USAID assistance to the Philippines for the last three (3) years is focused on Mindanao. Complementing USAID's assistance is the **US Institute of Peace's** (USIP) public diplomacy and awareness projects in Mindanao to sustain broad popular support for the peace process.

ADB has provided grants for training and capacity building to enhance private sector activity in Mindanao through public-private sector partnerships for the small and medium enterprise (SME) sector in the southern region. Currently, ADB implements programs to assist local governments on poverty mapping as well as on the devolution of basic social and urban services.

All these initiatives and more are being pursued in partnerships with the local government unites (LGUs), the local business sector, the community and religious leaders, the media and other stakeholders. Public-private Partnerships in these instances help promote a better understanding of the key issues in broadening the constituency for peace.

From Instability and Insecurity, to Hope and Opportunity

I believe in the viability of the conference proposition which states that *"by creating new economic activity and connecting these areas to the global economy, we create jobs and deliver hope and opportunity to people who might otherwise be exploited by extremists."* The Paglas story is one powerful paradigm for the "Business of Peace."

The Philippine experience in Mindanao shows the importance of having visionary leaders and institutions, of setting the stage for economic development in conflict-ridden areas, which then translates into investing in peace. There is growing evidence that the private sector has a role in contributing—both directly and indirectly—to the prevention and resolution of conflicts.

Building stronger Public-Private Partnerships will lead to greater investor confidence, which, in turn, will generate peace dividends. These partnerships empower our people—moving them from a state of instability and insecurity, to one of hope and opportunity.

Matthew Daley, President, U.S.-ASEAN Business Council

- The first part of this decade was marred by political instability that deterred investment. But the last major business mission to the Philippines was struck by the improved situation. The VAT reform has reduced the deficit to under 2% of GDP, the Peso is the strongest growing currency in South East Asia, and inflows of foreign direct investment are up. This improvement in the macro-economic situation is important because you need to go to Manila to get to Mindanao, both literally and figuratively.
- We need to recognize that State Department travel advisories are meant for tourists, not seasoned business travelers. It might be better to do separate reports for business travelers. The current advisory deters small and medium sized businesses from investing in the Philippines.
- In the business community, the Ex-Im Bank is seen as being risk averse, while OPIC is viewed as more creative. It might be good to have Congress waive some requirements for both when dealing with strategic areas.
- The USG needs to match the rhetoric at the EESR Conference with action. If the private sector sees a decline in engagement, particularly assistance, this sends a message about the stability of that place.
- The USG has made good improvements in visa processing. But negative impressions of the process being overly difficult with extensive delays remains.
- Hope the USG can find some way of continuing to fund the U.S. Institute for Peace program in the Philippines.
- There are small ideas not requiring a big budget that would improve businesses' willingness to invest. For example, it would be good to have Ex-Im Bank officials participate in the next business delegation trip to Mindanao with the Ambassador.

Walter Lohman, Senior Research Fellow for Southeast Asia, Heritage Foundation

- The morning session lacked a discussion of the actual business climate. This is likely because Iraq and Pakistan are dominating the discussions. But the Philippines is not in nearly as desperate a situation. There are already investors active in Mindanao.

- Conversely, more is expected of the Philippines than Iraq. But the Philippines is last in Asia for corruption according to the Heritage Foundation, and in the low 10 in Transparency International's report.
- The mining sector has big potential for growth and was recently liberalized. We need to review this industry as a potential development engine. But corruption remains the key impediment to this at present.
- The EESR Conference has acknowledged that private investment is the key to development. One U.S. investor can hire hundreds of vendors and build infrastructure. Companies focus their corporate activism and social responsibility programs where they are invested.

Brig. Gen. John A. Toolan, Jr., Principal Director, Asian and Pacific Affairs, Office of the Secretary of Defense

- Charles Krulac said, " Our hearts are in Europe but our health is in Asia."
- Lee Kuan Yew met with former Secretary Rumsfeld three months ago and urged the U.S. not to leave Iraq. He cited U.S. persistence in Vietnam as being crucial to give the South East Asian nations time to develop their economies.
- There are two missions: 1) isolate insurgents, 2) create jobs. But 80% of serious job creation is by the private sector. Governments can only contribute 20%, and the U.S. is limited to aiding the situation until it can reach a tipping point.
- Physical risk is obviously the biggest deterrent to investors in these areas. The use of private security contractors, common in Iraq, to solve this has proved problematic.

Jon Lindborg, USAID Mission Director, The Philippines

The Jollibee Index and Basilan Model

Last Nov, my staff organized a lunch for the U.S. Ambassador Kristie Kenney -- along with the Ambassadors from Japan, Australia, Canada, U.K. New Zealand -- at a popular Filipino fast-food restaurant known as Jollibee -- which is as a ubiquitous fixture around the Philippines, with nearly 600 outlets, as McDonalds is here in the U.S. While this may seem strange, even more remarkable is the fact that this luncheon took place in Basilan, the northern-most island in the Sulu Archipelago in Mindanao.

This trip would not have been possible 5 years ago, because there was no Jollibee in Basilan back then. Why? At that point, Basilan was a "no go" zone with serious security challenges, and a strong-hold of the terrorist Abu Sayyaf Group (ASG), famous for kidnappings for ransom and be-headings.

So what changed to make Basilan safe enough for the visit of six Ambassadors, last November? *A concerted combination of applied military force and development assistance – in effect, an iron fist and the hand of friendship* – succeeded in largely driving the ASG from the island and restoring a reasonable level of peace and hope to the island. In 2002, there were 14 Armed Forces of the Philippines (AFP) battalions on the island. Today there is only one.

But back to the lunch. The six Ambassadors did more than sit down for a lunch of Jollibee's signature dish, "Chicken Joy." They met with members of the *Basilan Chamber of Commerce who talked about business prospects for the island*, which were generally quite positive, from increased opportunities for rubber, coffee and spice production, to even plans for small-scale tourism. They were particularly grateful for the substantial U.S. assistance, in partnership with local governments and communities, to improve basic infrastructure such as roads and two ports. They remarked at the fact that the Basilan Governor, a former member of the ASG, has renounced violence and is now more concerned about improving social services and promoting business.

So quite a turnaround. From a place that was a no-go zone to one where business is beginning to thrive. And which is also emblematic, I believe, of how we at Embassy Manila look at the future of Mindanao, and particularly conflict-affected areas of Mindanao – through the lens of *how we can use our "3D" resources of defense, diplomacy and development to ultimately promote economic empowerment and private sector-led growth*, the theme of today's conference. And one of the reasons that a number of colleagues and I have sometimes half-seriously thought about using a *"Jollibee Indicator"* to measure the level of peace and security for communities in Mindanao. In that regard, there are many communities in conflict-affected communities in Mindanao where there is still no Jollibee outlet, so work remains in building a more peaceful and prosperous Mindanao. And a reason why the phrase *"Basilan Model"* is frequently heard when describing the ongoing partnership between the Gov. of the Philippines and the U.S. in fighting terrorism on the conflict-affected island on Jolo.

Our Approach

Unique Benefits derived from U.S.-Philippine historical relationship: Long-standing military to military cooperation, development assistance (focused on Mindanao since 1996, 60% of annual funding; nearly \$300 million during this period) trade ties, goodwill between our nations, Filipino-Americans. Tradition of Philippines corporate social responsibility (CSR). Our ability to work with U.S. military on civil-military projects.

Being A Mile Deep, Not a Mile Wide: Focusing our programs both thematically and geographically so that we can demonstrate a measurable impact. Not doing everything. Bulk of what we have done is to focus on accelerating equitable economic growth. But

we also focus on basic education, health, environment, energy, governance and conflict mitigation.

Local Ownership and Cost Sharing: Not doing anything for free, but requiring community, local gov planning and cost sharing for all programs. For infrastructure projects, at least 30%.

Governance and Policy as Important: Our work with local governments units (LGUs) has paid dividends in improving governance, as good governance promotes investment. Similarly, policy work on such issues as opening up transport sector to competition. e.g., roll-on, roll-off ports and shipping; business climate.

Infrastructure as critical business enabler, but also contributes to improved security. General Santos story with impact of port, airport and road infrastructure. More recently, we have focused on small- and mid-scale infrastructure, which has real impact on more remote communities/locations. Jobs.

By, With and Through the Private Sector: Similar to the mantra of U.S. military forces in Mindanao and how they operate with the AFP. We have sought to maximize opportunities to work with the private sector with our development programs. Two types efforts in this area:

First, pure *corporate social responsibility* type partnerships:

- U.S. energy firm, Mirant, which has provided \$4.5 million for a solar power program that has provided light in nearly 7,000 households.
- U.S. IT companies (Intel, Microsoft, IBM) that have helped provide internet connections and computers in nearly 500 schools.
- Multiple partnerships in education sector.
- Using American Chambers as a springboard for engagement; English language training program.

Second and more commonly, catalytic *business development*, where our assistance programs have played a more of a "*development venture capital*" role:

- Helping promote broad cellular coverage through assistance with site surveys (from 10% to 70% coverage today).
- Working at the *sectoral level* to help expand an entire industry such as seaweed, fisheries (tuna and finfish), vegetables, bananas, exports, cold chain, etc.
- Business chamber development; coaxing local private companies to expand beyond "safe" regional centers such as Davao and Cagayan de Oro.
- 300 privately-owned rural banks, profitably providing loans to more than 300,000 clients
- Even in health sector, promoting privately-owned mid-wife clinics.

Lessons Learned

Patience, Persistence and Changing Perceptions: Overnight solutions unrealistic. In some respects, we are working on generational issues. USAID has been focused on Mindanao for a decade, and U.S. military has been there for past 5 years. There still remains much work to be done in ensuring sustainable peace and development.

Real projects that improve the quality of life for average citizens: Need “ribbons to cut” and show that local governments are serious about development and can deliver improved local services.

Pro-Active Partnerships that build markets and institutions: With the Government of the Republic of the Philippines (GRP), the Armed Forces of the Philippines (AFP), NGOs, religious leaders, private sector, other donors and international community. Being proactive in looking for new opportunities to leverage our respective strengths. Role of youth and “new generation,” our Congressional internship program in Manila for Muslim youth from Mindanao.

3D Approach Works: A force-multiplier for our programs. Using all instruments of our national power. Planning, working together. Country Team approach, now including Foreign Commercial Service and USDA. It's more than eliminating all the bad guys. It's vital to combat the conditions that give rise to terrorism and decreasing the space for bad guys and terrorists.

A Filipino Face and Local Ownership: Maximizing use of local staff. We have nearly 600 project-funded partner staff in Mindanao, but only 6 Americans. During a recent ceremony on Jolo Island, the Sulu Provincial Administrator Don Loong noted the importance of local people in the battle against insurgents: *“It must be the people who are empowered to demand peace for themselves. The bad guys are neighbors, friends, relatives – and the people must demand that they stop the insurgency. The military will never be able to keep a watch over everybody at all times – but the people can keep a close eye on what's happening,”* he said. In essence, it takes a community to ensure peace, so working in an integrated fashion at the community level works, which is also what the 3D approach is all about in the Philippines.

Similarly, Local Private Sector Development as Key: But role for multinationals, too, particularly agribusiness, fisheries, extractive industries in Mindanao. But great opportunities for Corporate Social Responsibility.

Development is Necessary but Not Sufficient: Need a baseline of security and order to carry out good development. Commitment of GRP to a peaceful solution, which we certainly have in the case of Mindanao peace process. Still, ultimately, a political solution is necessary to bring lasting economic growth and peace.

On the Plus-Side

Peace & security remain top GRP priority.

GRP-MILF truce has held; role of International Monitoring Team

Strong international support and goodwill.

Improving AFP understanding & capabilities.

Increasing private sector investment.

Dynamic regional markets for exports.

Emergence of regional "growth poles" in Davao, General Santos, Zamboanga and Cagayan de Oro. Springboards to expand zones of economic growth.

Real opportunity to "get it right" in Mindanao

QUESTIONS AND ANSWERS:

- International Business Forum: Agree that progress is being made. Their original focus was on capacity building, but are now concentrating on attracting foreign direct investment. Concerning corruption, the Voluntary Principles for Extractive Industries is a useful framework. The Makati Business Club published a guide to current regulations. The Mintex factory is a dark cloud, and needs help to survive as a major employer.
- Ambassador Gaa: the GRP qualified for a \$20 million program as a Millennium Challenge Account Threshold Country for anti-corruption in the revenue and customs bureaus, and to create the office of ombudsman.
- Lindborg: On perceptions, public diplomacy is a key component. Getting positive press of Mindanao itself is important. The Philippines' investment rate is 15%, but this needs to rise to 20%.
- U.S. Institute for Peace: Recently prepared a paper "Mindanao Perils and Promise." When there is a peace agreement, the area will need investment for the transition/implementation phase. The U.S. needs to look at preferred market access for Mindanao as a strategically important area.
- Global Land: The issue in Mindanao is not about religion, but land. The roots of the conflict stem from Christian land grabs during the colonial era. The Abu Sayyaf group is just using the resentments from this issue. The U.S. has been in the Philippines for 100 years, how will this effort be any different? We are not

addressing the land issue or the need for property rights. Don't think we can achieve sustainable growth in Mindanao without such a change in the legal system, and this is, so far, not happening.

- Lindborg: The MILF demobilization was generally successful and land was a crucial aspect of this effort. Land is seen as critical to any MILF agreement's implementation. Trends during the last three years give cause to be optimistic. Though we need to acknowledge threats, on balance the situation is currently more positive.
- Ambassador Gaa: I'd like to thank Jon Lindborg for his support and optimism. Reiterate that the GRP has a program to combat corruption. Given that institutions already exist, the perception is worse than the reality.

Iraq

Mark Kimmit, Deputy Assistant Secretary of Defense for the Middle East, opened by saying this breakout session would focus primarily on discussing ways to attract private capital in Iraq. There is a significant amount of government money going into Iraq and now we need to take the necessary steps to foster private sector involvement.

Samir Shakir Mahmood Sumaida'ie, the Ambassador of the Republic of Iraq, said the challenges Iraq faces everyday are primarily on the security front. Iraq is now fundamentally different in terms of attitude and ideology. For decades, Iraqis had the mentality of central government control. Anything that wasn't controlled by the government was viewed with suspicion. An open market, free enterprise, a private sector and international engagement now all exist. In 2003, observers were hopeful that the economy of Iraq would start quickly; however, terrorists and enemies of Iraq have been successful at undermining these plans. A thriving black economy exists and is linked to insurgency, arms dealing, kidnapping, and criminal activity. The challenge ahead of us is to transform this black economy into a productive economy with policies and vision to back this up. Despite these difficulties in Iraq, areas that are relatively safe and secure do exist in both the north and south of Iraq. These are regions where outside investors can open businesses and expand from there.

Joseph Saba, Country Director for the Middle East Department in the World Bank, described the current state of Iraq's economy and offered strategies for future investment, which he asserted should be guided by three questions: a) What physical, institutional, financial, and human resources are available for investment? b) In what proportion should private and public sector be involved? c) What are the immediate priorities for allocation of public investment to maximize sustainability?

a) Resources

Iraq's mobilization of financial and capital resources, he noted, has been impressive; although a substantial part of its gross capital formation has been ensured by three years of aid inflows, the country is theoretically capable of maintaining similar levels of investment resources without aid. With improved security and institutional capacity, Iraq could become an attractive destination for both domestic and foreign investment.

Reliance on capital resources alone requires a tradeoff between quantity and quality of investment. Oil reserves are a double-edged sword: while they may bring revenue for public investment, they can also tempt governments to invest at unsustainable levels that strain domestic capacity and compromise the quality of investment both in terms of efficiency and effectiveness. There exists an upper limit to absorptive capacity—after a certain point, more investment doesn't mean more growth.

At present, the efficiency of Iraq's investment drive is low. Security risks are partially to blame, but so too are institutional bottlenecks, scarcity of human capital, governance problems, and rampant corruption. Iraq's institutional capacity to absorb investment has reached its limit. To deliver growth or employment, future investment must be carefully focused. While Iraq has financial resources, it lacks the other two: human and institutional capacity.

b) The Role of the State and the Private Sector

The state has traditionally loomed large in the Iraqi economy, and still does today. The government appropriates oil revenue and provides a broad range of services to the population. The public sector (including SOEs) accounts for over half of all jobs and over two-thirds of GDP. Over the short-term, the state will play a crucial role in moving the country toward a more dynamic, socially cohesive development model—and it will need to spend considerable resources to do so.

Over the medium term, the role of private enterprise will need to progressively grow, since the state cannot realistically employ every Iraqi and provide every service demanded by society.

c) Immediate Priorities

To maximize the growth and welfare impact of public investment, Iraq needs to move rapidly in building strong institutions for public finance management, strengthening the banking system and focusing sharply on key investment environment issues: economic legality and risk mitigation.

- i. Public Finance Management (PFM): There remains a critical need to build ownership of the reform content and process by the Iraqi government. The potential components of a public sector management reform and capacity development program might be linked to the Compact's Joint Monitoring Matrix (JMM).
- ii. Bank restructuring: A key priority in the financial sector is to reform the two large state-owned banks, Rashid and Rafidain, which account for 85% of commercial banking assets and 75% of the bank branch network. Both are antiquated (individual banks lack connections to headquarters), overstaffed and under-skilled. Immediate assistance is needed for the institutional and operational restructuring of the state-owned banks, including strategy, business plan, organization, credit risk management, human resource development, and information management system.
- iii. Risk Mitigation. International organizations and private firms should create new systems of risk mitigation to attract the private sector to key areas of the economy such as the petroleum sector, agriculture, and the construction materials industry. Using both political and partial risk guarantees, insurance pools, and novel contract and dispute resolution regimes, firms can be attracted to areas where security is acceptable and opportunities substantial.

Jim Bever, Deputy Assistant Administrator for Asia and Near East, USAID, said that the U.S. spends half its international development assistance on infrastructure. This money is spent on maintaining the Baghdad airport, water plants, schools, and clinics, all of which help to stimulate activities at the local level. Recently, we have moved away from this and are now more focused on governance and strengthening Iraqi institutions for budget purposes. Agricultural trade is a very important part of Iraq's non-oil economy. One out of every five Iraqis is employed in the agricultural area, yet this only contributes 7% of GDP. We believe this number can be tripled. The budget within Iraq must flow to stimulate economic job creation. On the micro side, there have been a number of community stabilization programs in key cities. More work is needed in their banking system.

Joseph Samora, Senior VP for Government Affairs, Case New Holland, spoke about the USAID joint private-public partnership. A lack of operational equipment is preventing agricultural productivity in Iraq. The Agricultural Reconstruction Development Program for Iraq (ARDI) program works with distributors in Iraq to refurbish agricultural and construction equipment. Based on experience and the real needs of the people, Case has developed a customer base for its merchandise. This strategy requires involvement from both sides. First, it is necessary

to break down what the private sector can do to grow business, then we must figure out the needs the government must handle. Workshops have already been underway in Turkey and Syria to train Iraqi mechanics. We must collaborate with the U.S. government to host Iraqi technicians and businessmen in the U.S. to train at and tour our facilities, and to see our equipment. Other U.S. businesses are encouraged to participate.

The discussion then focused on integrating efforts among all organizations to increase employment in Iraq, including the following:

- Contrary to common misconceptions, there are a number of factories and industries that are still in a pristine state.
- The Ambassador of Iraq said it is important not to disband all state-owned enterprises because this can create social instability. SOEs provide employment and peoples' livelihood. The authorities must gradually convert these SOEs into private enterprises.
- If privatization is going to work we must look at the governance of these enterprises and identify areas of corruption.
- There are two crucial laws needed to protect investment: the first is an investment law needed to get regulations out so that the law works. Next, is writing the law on paper in Iraq.
- Risk mitigation is needed to create conditions where we can get some fast results. One area may be fertilizer. We must also focus on recruiting investors.
- Issuing legislation is not sufficient. The mentality of those who apply the legislation must be changed. Once the perception of law by officials and the public changes, we will then be able to deal more effectively with corruption.
- Money spent must benefit the end user. Projects should be prioritized in terms of how much of their value cycles and recycles into Iraq's economy.
- Our responsibility is to get the money out onto the streets for Iraqis to rebuild their society. Trust needs to be built and we must be willing to give them a chance.
- Significant opportunity exists throughout the majority of Iraq, contrary to what is shown in the news media.
- It is now incumbent on investors to find ways to network and make projects thrive.

V. Closing Remarks

Daniel Sullivan, Assistant Secretary of State for Economic, Energy and Business Affairs, discussed lessons learned and next steps.

Themes:

- The importance of networking was one of the topics continuously highlighted during the conference. The State Department, for its part, is creating a civilian reserve core comprised of engineers, doctors, nurses, judges, police officers, etc., who are willing to go to trouble spots within 48 hours notice.
- Another important theme is the exchange of information between the private sector, government institutions and NGOs. The Economic Engagement Matrix has over ninety economic indicators for every country in the world. This kind of information is important.
- Local engagement plays an important role in local investment. Poland is an example of successful local engagement, as the country was not successful when it first emerged from communism but has since thrived.
- There is a connection between sustainable economic enterprises and one's ability to make a profit.
- From the government perspective there is a lot of "churn" from the ideas discussed today. Early in the fall there was a conference on counter-insurgency, which focused not only on combat operations but also on reconstruction operations. The U.S. military is ahead of its sister agencies in government because they are on the ground. We want this conference to be one more element of this broader discussion. It is imperative that we focus on the total economic engagement strategy. What are OPIC and USAID doing? Though the process can be difficult we must continue to improve the relationship between these organizations. In addition, we need to learn from the private sector what does and does not work. To be successful we must continue dialogues such as the one we had today, build our networks, and expand our knowledge of these regions of the world.
- The notion of hope and vision is still very much alive. The private sector will play a major role in the future. Moreover, the private sector is as powerful as the government. An example of the private sector's power is the Dell Computer call center established in El Salvador. It was a huge success and reinforced the notion that American private companies can bring investment. We must focus on the economic picture in places like Iraq and Afghanistan. Many of the people in these countries are open and don't want their children to be terrorists. They want their children to go to school and from the government side we need to continue supporting initiatives to make this possible.