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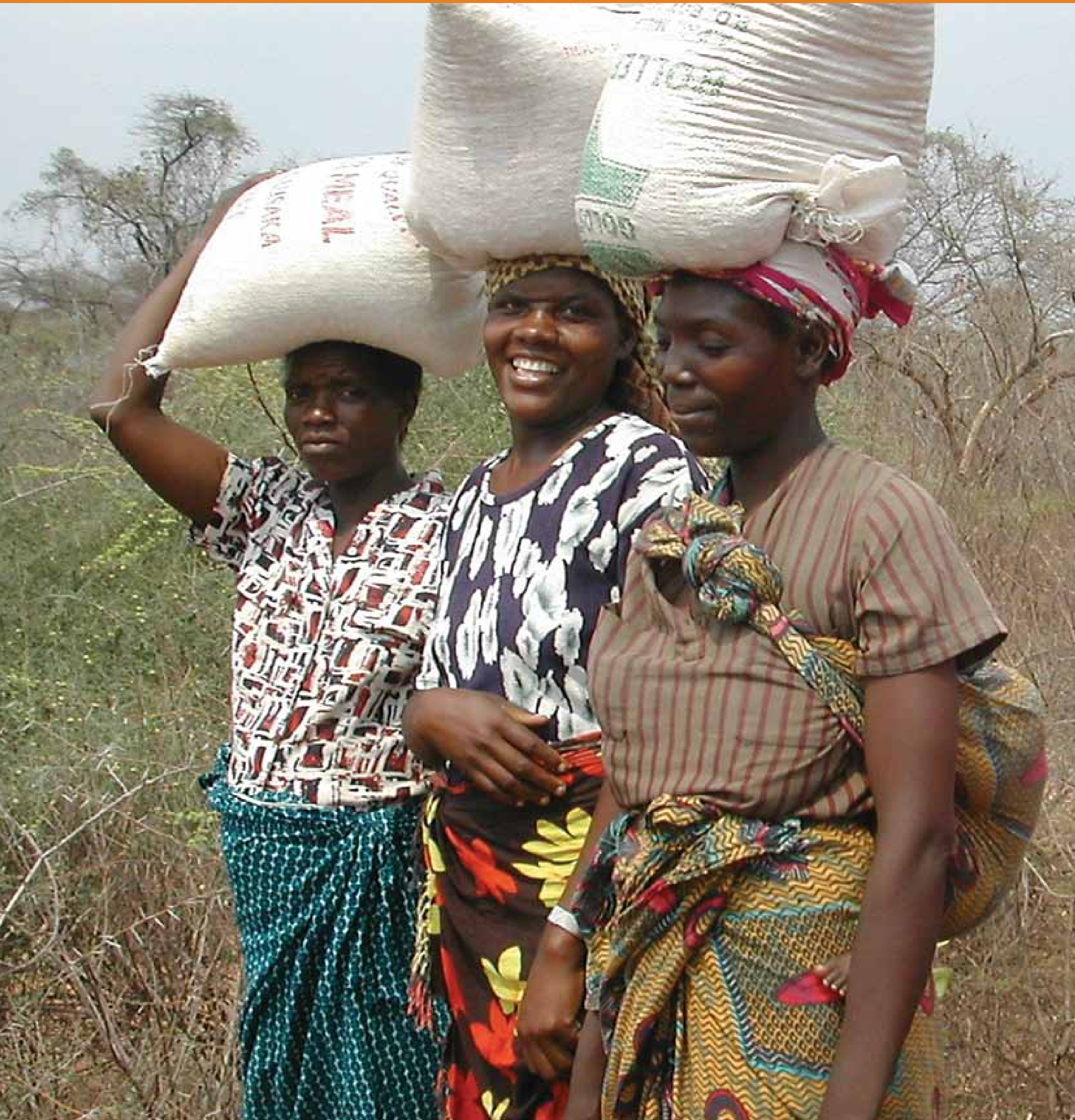
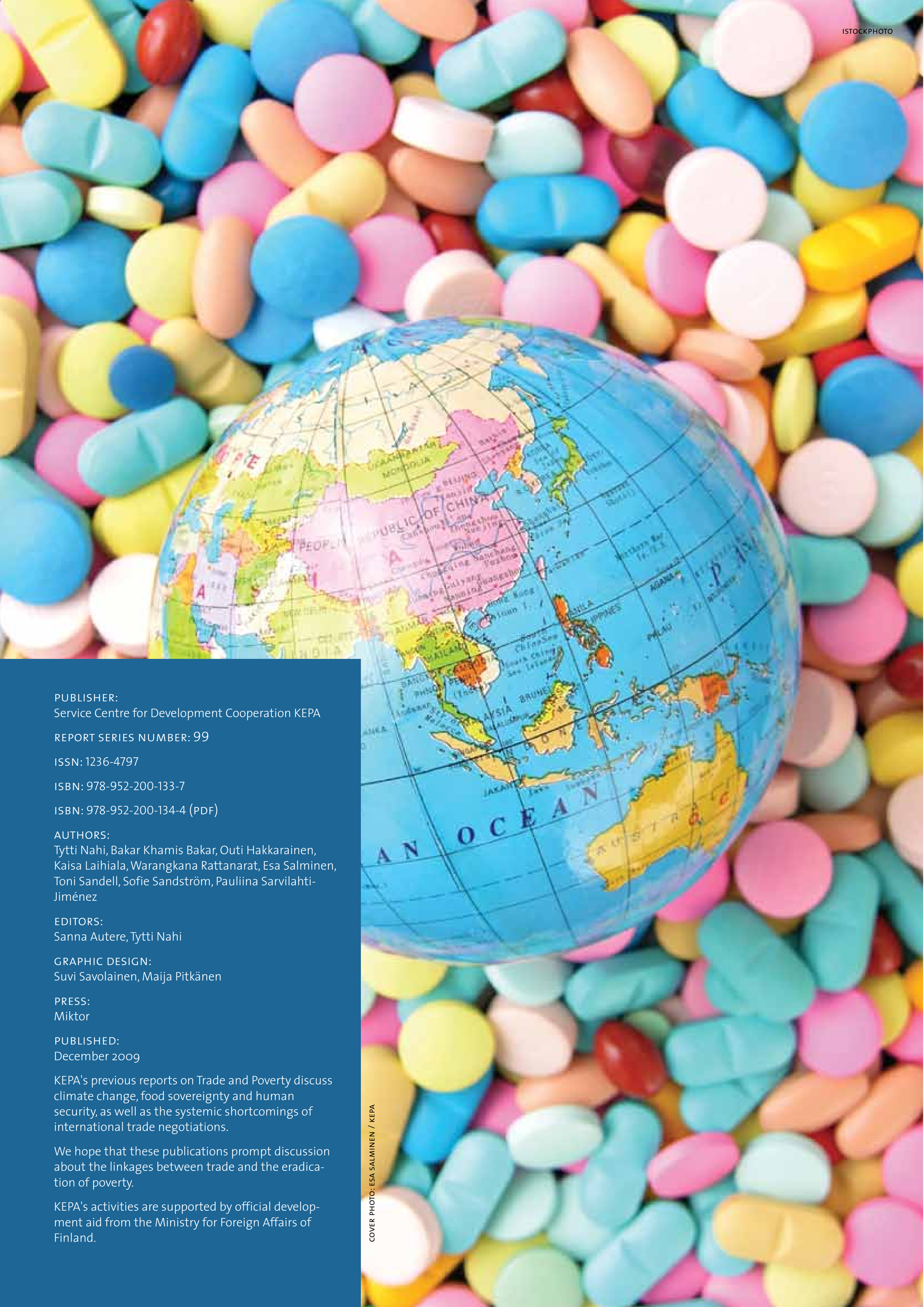
SERVICE CENTRE
FOR DEVELOPMENT
COOPERATION

POVERTY AND TRADE, PART IV

WELLBEING FOR SALE?
SERVICES AS KEY TO DEVELOPMENT





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KEPA's previous reports on Trade and Poverty discuss climate change, food sovereignty and human security, as well as the systemic shortcomings of international trade negotiations.

We hope that these publications prompt discussion about the linkages between trade and the eradication of poverty.

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COVER PHOTO: ESA SALMINEN / KEPA

WELLBEING FOR SALE?

Wellbeing and economic growth both call for more and better services. Clean water is still out of reach for every fifth person in the world. Over a quarter of children in Sub-Saharan Africa receive no education. Energy shortages and a constant credit crunch keeps hard-working entrepreneurs poor.

The responsibility for ensuring services to poor people and small enterprises lies with governments.

This report, however, focuses on the international context: reforms in international policies and agreements are needed, so that developing country governments have space to make fair and effective service policies.

Examples from Africa, Asia and Central America, presented on pages 10–22 of this report, provide rich insights in the required reforms.

What is needed is case-by-case analysis and attention to the needs of the poorest people.

Also needed, are earnest attempts to foster cooperation between the public and the private sector. The global financial crisis has shown that markets are not self-regulatory. Financial markets and other service sectors need dynamic public regulation.

The ideological call for privatisation, foreign investment and export promotion, on the other hand, needs to be left behind. For example, depending on local circumstances, foreign investment can bring capital, know-how and efficiency – or crowd out domestic entrepreneurs.

This publication proposes ways to apply these new lessons to trade policy.

KEY RECOMMENDATIONS

- Right to regulate must be strengthened in all trade agreements and developing countries must be able to slow down the liberalisation of services.
- Mechanisms for settling commercial disputes between corporations and states must be developed to render them fairer to developing countries.
- Legally binding international rules on corporate responsibility must be established under the United Nations.

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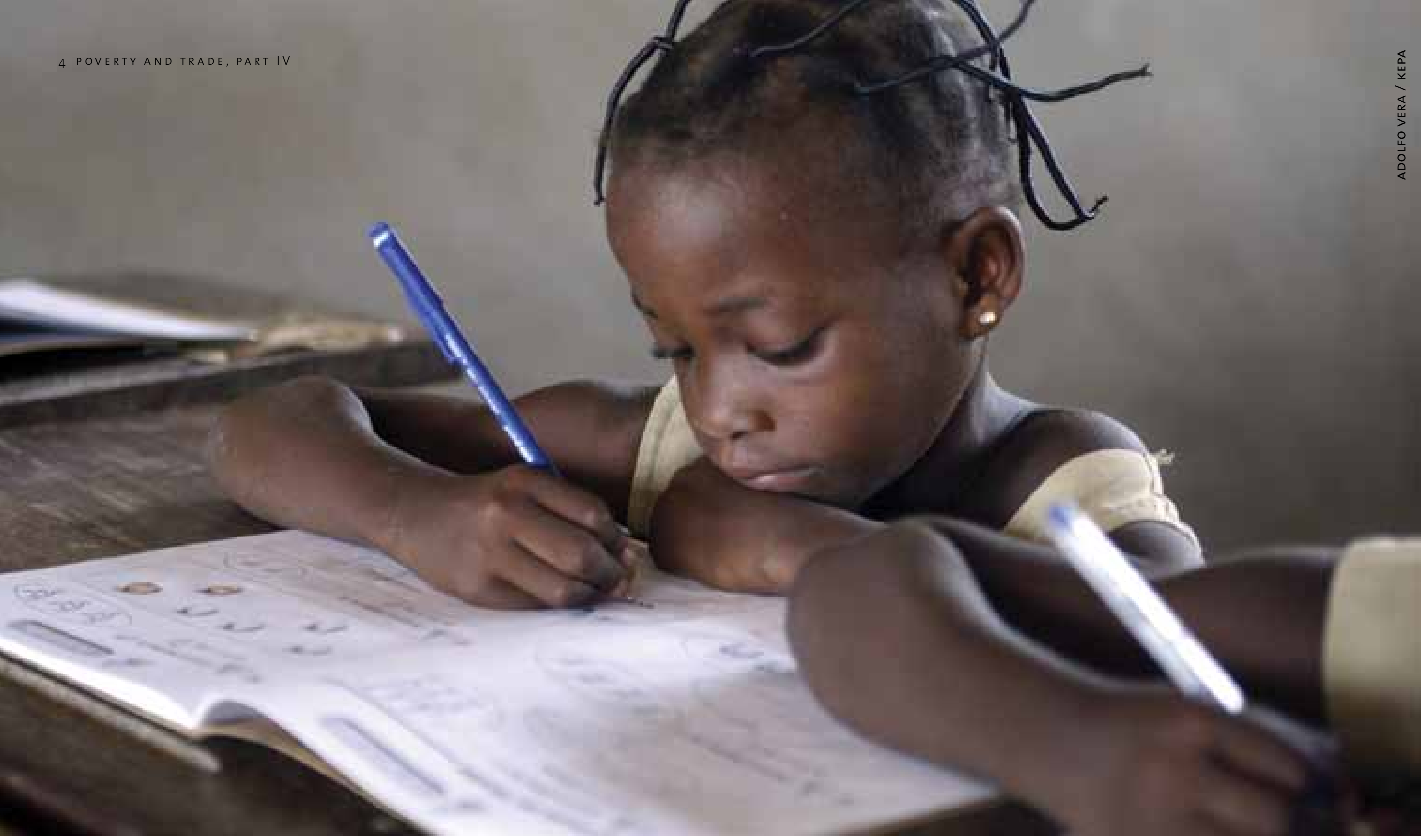


Progress towards the UN Millennium Development Goals will be reviewed again in autumn 2010, five years before the deadline. Already 88 percent of children in the world get primary education but the number of hungry people has risen by over 150 million in 2008–2009.

SERVICE TRADE ON POOR PEOPLE'S TERMS

WELFARE IS BASED ON A WIDE ARRAY OF SERVICES FROM HEALTH CARE TO INSURANCE. PEOPLE'S WELLBEING IS DIRECTLY LINKED TO BASIC SERVICES WHILE ENTERPRISES NEED FOR INSTANCE FINANCING AND ENERGY. IN THE RECENT DECADES, POLICIES ON SERVICE PROVISION HAVE CHANGED SIGNIFICANTLY.

► **THERE IS A GLOBAL CONSENSUS** that access to high-quality basic services is a strong engine for human development. At the beginning of this century, the UN member states translated this consensus into eight Millennium Development Goals (MDGs) and agreed that primary education and family planning services, for example, should be universally available by the year 2015.

Services are crucial for business and exports as well. Key inputs into agricultural and industrial production include financial services, telecommunications, insurance, energy supply and retail services. The main export services of developing countries include tourism, construction, transport and business services. Even gambling and entertainment count as services.

It's the duty of the states to guarantee access to essential services for the poor, the vulnerable and the marginalised.

EVOLUTION IN SERVICE PROVISION

The diversity of services brings challenges to policy-making: there are no one-size-fits-all solutions to developing services. This has not, however, always been recognised.

In the 1980s leading development thinkers recommended that developing countries reduce the role of the state and seek to attract foreign private investment. A sweeping wave of structural adjustment processes across Africa, Asia and Latin America was coordinated by the International Monetary Fund (IMF) and the World Bank.

The IMF and the World Bank encouraged the adjustment via advice, technical aid, reducing funding to public services, and conditioning their financial support to such reforms as privatisation of public utilities.

Economic thinking has, however, developed since then. The doctrine of structural adjustment was first shaken by

Privatisation is sometimes good and sometimes not. There are no one-size-fits-all solutions in poverty eradication.

the fact that it did not spur economies into fast growth. African economies grew slower in the 1980s than before.

LESSONS OF THE ASIAN CRISIS

In late 1990s the Asian financial crisis also had an impact on economic policy-making. Liberalisation of financial markets and high interest rates had attracted considerable foreign investments to South East Asia. In the summer of 1997 some investors suspected that abundant capital had propelled Thai real estate prices too high, and withdrew their money from Thailand.

Other investors followed as in a herd, and the value of the Thai baht collapsed. The panic spread and the same pattern repeated itself in the neighbouring countries.

The advice of the IMF deepened the crisis. Instead of a stimulation package, it recommended cuts in government spending, high interest rates and allowing insolvent banks to fail.

Insufficient regulation on financial markets is widely considered one of the root causes of the Asian crisis. The knock-on effects reached far. Lending to developing countries dropped, economic growth slowed, oil price fell and the Russian economy hit a crisis in 1998.

WORLD BANK CALLS FOR REGULATION

Further, structural adjustment did not persuade the private sector to channel their capital into African infrastructure. The World Bank has noted that even food security was badly influenced.

"Structural adjustment in the 1980s dismantled the elaborate system of public agencies that provided farmers with access to land, credit, insurance, inputs and cooperative organisations. The expectation was that removing the state would free the market for private actors to take over these functions. Too often, that didn't happen," reflected the World Bank in its World Development Report 2008: Agriculture for development.

"[T]he institutional reconstruction of agriculture is still incomplete. Moving forward requires more clarity on the roles of the state and the private sector – and more analysis of what works and how it could be improved," the bank added.

"Foreign direct investment (FDI) in services through privatisation poses a special challenge in terms of regulation and governance. The outcome of such FDI is affected by the way in which privatisations are undertaken, the nature of competition in privatised industries and the quality of the national regulatory framework and institutions", continued The UN Conference on Trade and Development (UNCTAD) in its World Investment Report 2004: The Shift Towards Services.

FINANCIAL CRISIS PROVED THE NEED FOR REGULATION

The financial crisis and economic depression of the last couple of years have again shaped economic thinking. The crisis burst in the summer of 2007. For the last fifteen years, banks in the United States had been granting mortgages to low income households.

To maintain their credit ratings, banks had packaged these mortgages and other loans together, issued debt obligations backed by these packages and deposited their own obligations in the secrecy of tax heavens.

When real estate prices fell in the US in 2007, households were no longer able to service their loans. Confidence in the financial markets started to fall, because nobody knew how many bad obligations each bank and corporation had. Stock markets plummeted and in the latter half of 2008 lending tapered off.

The underlying cause of the crisis was the deregulation of the financial markets since the 1980s. No regulations were placed on the solidity and risk taking by banks, as free markets were trusted to be efficient. Financial markets became increasingly separated from the real economy, indebtedness grew deeper and it became very difficult to estimate the risks of different assets.

In responding to the crisis, the financial centres of the world have not relied on free markets. The US lowered interest rates and invested a massive seven percent of its national income in a stimulation package. Europe also lowered interest rates and channeled considerable subsidies to banks.

The crises and the research of recent decades have rendered economic thinking more nuanced. Today, instead of privatisation, the leading economic thinkers call for cooperation between the public and the private sector as well as the development of appropriate regulations. ◄

FEW EXPORTS FROM POOREST COUNTRIES

The share of services in worldwide economic activity has expanded markedly in recent years.

Services employ about 35 percent of people and account for over half of the gross domestic product in developing countries. In developed countries the share of services in employment and total production are both over 70 percent.

International trade in services has grown even faster. Since 1990 it has nearly tripled. On average, exports from developed countries have grown by 6 percent and those from developing countries by 8 percent each year.

Yet the share of the poorest countries is small. Africa accounts for only 2 percent of world trade in services. The largest exporters are the EU, North America and Asia, who make up 90 percent of global trade.

WHERE ARE THE RULES OF SERVICE TRADE DETERMINED?

► **SEVERAL INTERNATIONAL** agreements and actors set boundaries on national policy-making. Service related policies are influenced for instance by the World Trade Organisation (WTO), regional trade agreements and the World Bank.

Companies providing and trading services are also influenced by guidelines on corporate responsibility.

WTO "DEVELOPMENT ROUND"

The first multilateral agreement that aimed to liberalise trade in services came into effect in 1995, when the World Trade Organisation (WTO) was established. The WTO has 153 member countries. Its decisions are prepared among member country officials in Geneva and ratified in ministerial meetings.

In negotiations about updating the General Agreement on Trade in Services (GATS) each country defines which service sectors it opens up to private and foreign competition. With over one thousand pages of text, the GATS is one of WTO's most complicated agreements.

The negotiation round that started in 2001 is called a "development round". The stated aim is to reform trade regulations in accordance with the needs and interests of developing countries.

Even so, disagreements have coloured the talks on services. Many developing countries have stressed the importance of clearer definitions on how states can regulate service provision. The industrialised countries, however, are more interested in liberalisation, and progress on regulation issues has been very limited (see pages 8–9).

REGIONAL TRADE AGREEMENTS PROLIFERATE

The industrialised countries and large corporations have recently considered the WTO talks too slow and have started promoting free trade through bilateral and regional trade negotiations. At the time of writing this report, a total of 195 regional trade agreements are operational, and 74 of these cover service trade.

The EU is currently negotiating regional service trade rules with more than 100 countries. These include developing countries from every continent.

In other words, trade deals form a growing jungle of agreements. Their number is increasing rapidly and their contents are diverging from each other more and more.

CORPORATE RESPONSIBILITY BECOMES BETTER DEFINED

There are several international and national guidelines on the ecological and social responsibilities of corporations. The most influential guidelines are the Labour Standards agreed at the International Labour Organisation in 1930–1999 and the guidelines to multinational corporations agreed at the Organisation for Economic Cooperation and Development (OECD) in 1976.

The OECD guidelines state, for example, that companies should not look for or accept special environmental, labour or tax exemptions, which are not in accordance with the legislation of the host country. The guidelines were last updated in 2000, and they apply to companies of all sizes and from all countries.

Following the OECD guidelines is voluntary but it is monitored by National Contact Points.

Further clarification of corporate responsibilities is underway by UN Special Representative for Business and Human Rights John Ruggie, whose proposals have been positively received by corporations as well.

Ruggie suggested in 2008 that corporations have a responsibility to respect human rights and refrain from contributing to any abuse of human rights. This requires continuous monitoring of their operations and often proactive action for instance to promote anti-discrimination at workplace.

Tax evasion and competition is addressed by UN tax committee and the so-called Leading Group on Innovative Financing for Development. Their work has sped up due to the financial crisis. ◄

WHY REGULATE?

Evidence from Africa, Asia and Central-America shows the need for regulation that favours poor people and small entrepreneurs.

BASIC SERVICES TO THE POOR

It is the duty of the states to ensure that even the poorest people and the smallest enterprises have access to essential services. If services that are crucial for wellbeing are provided by private companies, the state needs to clarify the expected quality and extent of provision. The funding can be ensured by the state as subsidies or by granting monopolistic rights to the company. This is discussed in cases on banking in Mozambique and health services in Thailand (pages 14–17).

Numerous privatisation processes around the world have gone sour because the obligations of the new private companies have been unclear or insufficient. There are two examples of problematic privatisation processes in this publication: the privatisation of Tanzanian water distribution and Nicaraguan energy services (pages 10–13).

DEVELOPING DOMESTIC PRODUCTION

Few developing countries have strong domestic service providers even in such sensitive sectors as banking, telecommunications or energy generation. It is not advisable to leave the development of such key services for international providers.

For example UN Conference on Trade and Development (UNCTAD) sees that it may require temporary regulation of foreign competition to spur the development of young local companies in strategic sectors.

STABILISING THE MARKETS

The financial crisis of 2008 showed that self-regulation by markets is a myth. In order that future crisis can be tempered or avoided financial markets need dynamic, clear and neutral regulations.

Stronger rules are needed for example on risk taking by the banks, reporting of risks and uncertainties and transparency especially in tax heavens. Similar regulatory needs exist on many service sectors.

BENEFIT FROM INVESTMENTS

Most developing countries have liberalised their economies for the last 15 years to attract foreign investment. Still, only 0.7 percent of private investments flow to the poorest countries.

The examples of tourism in Northern Mozambique and supermarkets in Thailand (pages 18–20) highlight that it is time to shift attention from attracting investment to reaping its benefits. At their worst, multinational companies can crowd out domestic entrepreneurs, exploit natural resources, evade taxes, ignore worker's rights or contribute to other human rights abuses.

International guidelines on corporate responsibility aim to strengthen the benefits. National investment laws can also oblige foreign investors to bring technology or engage in joint ventures with local entrepreneurs.

CONSERVING THE ENVIRONMENT

As suggested by the case of Nicaraguan energy services (pages 12–13), regulation is often required to make markets and companies operate ecologically. Markets cannot promote ecologically and socially optimal results as long as market prices bear no reflection of the value of natural resources, and protecting the environment brings no profits to people or companies.

As a result, it is necessary to have rules about emissions, waste, landscapes, consulting local people, and other issues.

FAIRER COMPETITION

Competition between multinational enterprises and smaller local companies is unequal. Examples of drug patenting in India and retail in Thailand (pages 16–19) and a look at the settlement of investor-state disputes (page 22) show that competition is also often unfair and against the spirit of free trade: large companies have a lot of power on markets and at courts.

Still, the concentration of market power is not automatic. It can be moderated by strengthening, competition rules and channeling support to small companies.

FOSTERING REGIONAL INTEGRATION

Many developing countries and regions are in the nascent stages of tightening economic cooperation with their neighbours. Cooperation on regulatory policies can temper the competition among developing countries, and help them adopt higher standards in labour, environment and tax laws. ◄

WHAT SHOULD BE DONE

SEVERAL REFORMS ARE NEEDED IN INTERNATIONAL RULES ON TRADE AND CORPORATE RESPONSIBILITY, IN ORDER THAT DEVELOPING COUNTRIES HAVE POLICY SPACE TO ADOPT AND MAINTAIN PRO-POOR SERVICE POLICIES.

IMPACT OF LIBERALISATION MUST BE ASSESSED CASE BY CASE

Every economic reform creates winners and losers. Considering how diverse the service activities are – from health care to telecommunications and gambling – a wholesale liberalisation of all services would create a vast and intricate web of winners and losers.

Instead of fast liberalisation, countries should therefore assess the impact of each sectoral reform at a time.

Regional trade negotiations do, however, encourage wholesale liberalisation. Developing countries are asked to freeze their policies, so no new regulations can be introduced later. They also need to welcome multinational companies to all sectors that they do not specifically exclude from the treaty.

RECOMMENDATIONS

- All trade negotiations must be based on empirical assessments of their impact on poverty and the environment.
- Developing countries need a right to refrain from or slow down the liberalisation of services.

SPECIAL TREATMENT FOR THE POOREST

That the rules are the same for everybody does not ensure fair play, if one player is much bigger than the other. To ensure fair play for poor producers working where education, technology, infrastructure and investment are the scarcest, WTO agreements promise special and differential treatment to the least developed countries (LDCs).

Accordingly, the WTO member countries agreed in 2004 to prioritise the opening up of service markets where LDCs feel they have export potential, especially the temporary migration of labour. LDCs duly made a request in May 2005 that the temporary movement of "semi-skilled professionals" and "service providers other than professionals" be opened.

This request is yet to be met. The EU and the US do frequently boast that they've given a good response to the proposal, but in reality their offers are below the existing levels of liberalisation.

RECOMMENDATIONS

- Special and differential treatment to the least developed countries needs to be deepened, especially in regional trade agreements.
- Industrial countries need to open their borders to temporary workers from developing countries.

> The fact is that it pays companies to behave in an ethical way and there is a lot the EU can do to encourage companies to move in this direction.
>
> DR EWA BJÖRLING, MINISTER FOR TRADE, SWEDEN

RIGHT TO REGULATE MUST BE SECURED

Developing countries have a right, according to WTO rules, to regulate service markets in order to strengthen domestic service capacity, to fulfil such policy objectives as universal access to education, and to maintain public order.

But it is extremely difficult to apply this right to regulate. Most regulations judged by WTO Dispute Settlement Panels have been found non-permissible.

A good example of this are Mexico's regulations in the telecommunications sector. Mexico regulated some telecommunications prices to improve infrastructure, widen poor people's access and limit predatory pricing.

The Dispute Settlement Panel ruled, however, that foreign telecom firms should not be obliged to fund infrastructural development, that Mexico cannot invoke

> Appropriate regulations need to be drafted and put in place before liberalisation. This takes time, resources, expertise and policy space.
>
> SOUTH CENTRE, THINK TANK

the rights which it did not explicitly ask for at the time of signing the WTO telecommunications rules, and that predatory pricing was not likely.

The right to regulate therefore needs to be clarified. No deal has been achieved, however, though negotiations to clarify the WTO rules have been ongoing since the 1980s. The agenda includes, for instance, subsidies, technical standards, licensing requirements and safeguards against import peaks. So, quixotically, there is no agreement on the legal parameters of liberalisation commitments, but countries must make binding commitments anyway.

Regional trade agreements allow for even less regulation than the WTO. This is revealed by a detailed analysis of a trade deal between the Caribbean and the European Union.

For example the rules on telecommunication outlaw several practices allowed by the WTO, such as cross-subsidisation of one activity (like local calls) with revenues from another (like international calls), which are commonly used to better serve the poorer sections of the clientele.

To strengthen the right to regulate, the mechanisms for settling commercial disputes between corporations and states also need to be reformed. Developing countries are currently disadvantaged in these disputes (see page 22).

RECOMMENDATIONS

- Right to regulate must be strengthened in all trade agreements.
- Dispute settlement mechanisms must be developed to render them fairer to developing countries.

BINDING RULES FOR CORPORATE RESPONSIBILITY

There will always be gaps in national regulations and monitoring. Developing country governments worry that proper environmental, labour and fiscal laws would limit the competitiveness of the national economy and deter foreign investment. Gaps in monitoring even tempt some companies to ignore the existing rules.

These gaps are problematic for responsible companies. They are left to choose whether to run higher costs than competitors or to act less responsibly.

Stronger global rules on corporate responsibility would thus help both poverty reduction and the most responsible companies.

Industrial country governments could also strengthen the existing rules by monitoring them better. OECD countries have set up so-called National Contact Points, whose duties include monitoring the OECD guidelines for multinational corporations. Yet most of these bodies have little resources to actually investigate companies' operations abroad.

RECOMMENDATIONS

- Legally binding international rules on corporate responsibility must be established under the United Nations.
- The implementation of existing guidelines on corporate responsibility must be better monitored.

CURBING TAX EVASION

Corporations have an indisputable duty to abide by tax and other laws of their host country. Even so, multinational enterprises regularly dodge taxes. Tax evasion by multinational corporations is estimated to cost developing countries at least 160 billion US dollar tax losses each year. This corresponds to one-and-a-half times the total aid budget.

Corporations often implement the evasion by underpricing sales to their daughter companies operating in tax heavens. This way the profits shown in each country can be adjusted and taxes minimised. Attempts to plug the evasion are complicated by the tendency of multinational corporations to report their revenues and costs regionally or at corporate level.

"The era of banking secrecy is over", declared the leaders of the biggest industrial and emerging economies in a G20 meeting in April 2009. Unfortunately the chosen tool are bilateral agreements on exchange of tax information. This does not help the poorest countries that have no capacity to negotiate or apply bilateral agreements.

RECOMMENDATIONS

- Tax heavens must be regulated by increasing automatic exchange of tax related information between countries.
- International accounting standards must be reformed so that multinational corporations need to report their revenues and costs on a country-by-country basis.

TANZANIAN WATER SERVICES: PRIVATISATION DID NOT SOLVE THE PROBLEMS

THE CITIZENS OF DAR ES SALAAM, THE MAIN CITY OF TANZANIA, HAVE SEVERAL TIMES HOPED THAT A CHANGE IN OWNERSHIP WOULD IMPROVE WATER DISTRIBUTION. THESE HOPES HAVE NOT COME TRUE. MOST PEOPLE STILL HAVE NO RUNNING WATER.

► **WATER IS A SHOCKINGLY SCARCE** resource in Dar es Salaam. Three out of every four citizens have no running water at home. Therefore epidemics like cholera are chronic in the population. Poor households have to use dirty water from streams and puddles, and illnesses spread easily.

People can buy water from street vendors, but each drop is expensive. A 20 liter bucket of water from a vendor commonly costs over 50 cents, while households with running water pay 0.8 cents for the same amount. The wealthiest fifth of households spends 1.6 percent of their income on water, while the poorest fifth spends 5.9 percent.

PRIVATISATION AS AID CONDITIONALITY

Before privatisation, water services in Dar es Salaam were hardly a model of public sector efficiency.

First the objective was to provide water free of charge, save for the wealthiest areas. Then low prices were introduced in 1991 and a semiautonomous water authority DAWASA was established in 1997.

But funds were scarce. Pipes and other infrastructure fell in ever worse disrepair, and failed to keep up with population growth.

Donors had been recommending the privatisation of water services since the early 1990s, and in 2000 the World Bank and the International Monetary Fund (IMF) made it a condition of debt relief for the country.

The government of Tanzania complied with the pressure. Only 98,000 households in a city of 2.5 million people had a water connection and even they received water irregularly. As much as 73 percent of water was lost through leaks and unauthorised use.

FLAGSHIP CASE FOR PRIVATISATION

The privatisation process attracted a lot of attention: it was one of the most ambitious privatisation initiatives in Africa and was hoped to become a flagship case for structural adjustment.

The process started with a hiccup: no company offered to take on the water services as a whole.

One bid was received, however, when DAWASA offered to keep the job of rehabilitating and expanding the water network. In December 2002 the lone bidder, a British-German-Tanzanian joint venture called City Water, was contracted to operate, do routine maintenance, bill, collect tariffs and to share the profits with DAWASA.

EXPENSIVE WATER FOR FEW PEOPLE

Unfortunately, the hiccups did not end there. Citizens did not perceive improvements in the service. Those with running water were disgruntled because tariffs were raised, although many only received water for a few hours a week. This hurt even the poorest people as water vendors passed the price hike on to their customers.

No action was taken to improve water services for the 80 percent of the population, who lived in unplanned settlements with no water pipes.

The company brought in very little capital. City Water was supposed to bring in 8.5 million US dollars, DAWASA to provide 12.5 million dollars, while the Tanzanian government took a 143.5 million dollar loan from the World Bank, the African Development Bank and the European Investment Bank. The government also granted City Water a six year tax holiday.

Regulatory structures intended to facilitate dialogue between consumers, officials and the company were not set up in time. The structures were meant to include consumer councils and an Electricity and Water Utility Regulatory Authority (EWURA), but in the end the sole responsibility for regulation laid with an over-stretched Ministry of Water and Livestock Development.

INTERNATIONAL DISPUTE

In May 2005 the Tanzanian government reneged on the deal. It blamed City Water for failing to expand the services or collect revenues as planned, for excessive tariff raises, and for investing less than half of the promised 8.5 million dollars.

The chief executive of British Biwater, one of the founding fathers of City Water, conceded that the project had fallen behind schedule, but claimed that information provided by the Tanzanian government to Biwater was ”not only incomplete but also inaccurate”.

City Water sued Tanzania at ICSID, the International Center for the Settlement of Investment Disputes, but received no support. ICSID found that while technical breaches of Biwater's investors' rights did occur, Biwater was not entitled to compensation because the breaches were worth nothing and the termination of the contract was inevitable.

In a separate arbitration the Tanzanian government was even awarded damages for the breaches of contract that City Water had done.

NO MAGIC SOLUTIONS

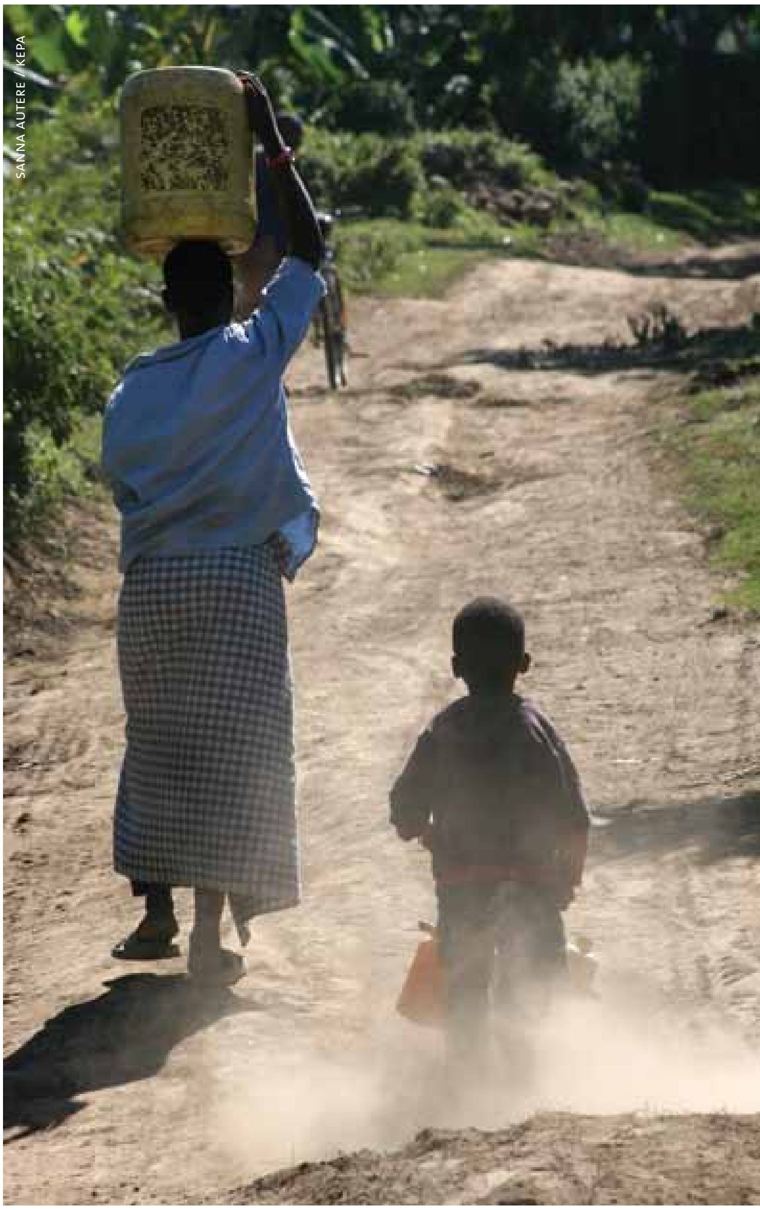
City Water's responsibilities were transferred to a newly-founded public company, Dar es Salaam Water Supply Company (DAWASCO). Hopes were high, and several observers in and outside Tanzania noticed improvements in the services, management, billing and tariff collection. The new management was considered dynamic.

No magic solutions are in sight, however. Within the first five years of its operation, DAWASCO has not managed to make any major capital investments. The water network still dates from 1974, leakages and unauthorised use means that up to half of the water is lost, and tariffs have been raised even further.

DAWASCO has sought to improve poor people's access to water by establishing kiosks in unplanned settlements. DAWASCO supplies water to kiosks where people can fill their buckets and pay per liter. The operation of the kiosks is contracted to water user groups or individuals. There continues to be challenges in the running of these kiosks, however.

The shifting of responsibilities from public to private and back to public management has not solved the problems of Dar es Salaam's water services. More than two-fifths of households in the city still need to travel for over half an hour to access clean water. ◂

BAKAR KHAMIS BAKAR AND TYTTI NAHI, KEPA TANZANIA



SANNA AUTERE / KEPA

Commodifying a basic need has not brought clean water for all in Tanzania. In the picture, a woman and a child are fetching water in Arusha, one of the largest cities of Tanzania.

Power cuts cause problems to companies and income losses to Nicaraguans. In the picture, women are cleaning sesame seeds in a factory in Chinandega, North-Eastern Nicaragua.

LARISSA BRUUN / KEPA

ENERGY FOR NICARAGUANS: ELECTRICITY IS EXPENSIVE AND FAR FROM GREEN

THE HISTORY OF NICARAGUAN ELECTRICITY SERVICES GIVES A LOT TO LEARN TO THOSE EAGER TO PRIVATIZE BASIC SERVICES. NICARAGUA HAS SEARCHED FOR PRIVATE ENERGY INVESTMENTS FOR THE LAST 15 YEARS BUT INSTEAD OF EFFICIENCY, THE RESULT IS HIGH ELECTRICITY COSTS, POWER CUTS AND OIL DEPENDENCY.

► **THE NICARAGUAN CONSUMER** pays the highest electricity bill in Central America. Electricity services have reached merely 50 percent of the population and electricity is produced with the least sustainable manner possible – oil.

UNDER THE YOKE OF INTERNATIONAL BANKS

In Nicaragua, 60 percent of energy production and all distribution is today in private hands.

The Nicaraguan civil war in the 1980s led to tens of thousands of casualties, greater impoverishment and astronomical public debt.

The resulting aid dependence gave international financial institutions such as the International Monetary Fund (IMF), the World Bank and the Inter-American Development Bank (IDB) vast powers over Nicaraguan policies. They initiated a structural adjustment programme, which promoted privatisation both directly via advice, lending and loan conditionalities, and indirectly by restricting public investment in infrastructure.

The privatisation of energy services was carried out according to the design and advice of the IDB. The Nicaraguan Electricity Enterprise (ENEL) was born in 1994 and divided into seven different companies in 1999.

International investors were then invited to take over the generation, transmission and distribution of energy. Only some regulatory activities were left for the state.

In December 2000 the pressure towards privatisation intensified further. Nicaragua was seeking debt relief from financial institutions and, under the so-called HIPC Initiative, the institutions decided to grant it. The relief was, however, conditional on several economic reforms, including the privatisation of all energy production.

DAILY POWER CUTS

The privatisation is expected to resolve the problem of energy shortages. Private companies are assumed to be more efficient than the public company was.

The government has also agreed to pay bonuses to companies that increase their energy generation potential. This was agreed in Power Purchasing Agreements signed by the companies and ENEL in the 1990s. The bonuses are paid to companies whether the generating potential is used or not.

The strategy has not been a great success. Energy production is still grossly inadequate. Power cuts were particularly common in 2006–2007, when Nicaragua had to rationalise its energy consumption. Most of the country suffered daily 8-hour power cuts.

The capacity has increased by only 351 megawatts between 1995 and 2004. At the same time in neighbouring Costa Rica, energy services have been kept in public hands and generating capacity has increased by 790 megawatts.

These cuts cause great income loss for the Nicaraguans. For example, thousands of small corner shops, known as pulperias, regularly lose their groceries as they can't afford to buy generators that would keep refrigerators running during power cuts.

OIL DEPENDENCE HARMS THE ENVIRONMENT

Nicaraguan energy is also far from green. Nicaragua has stuck to oil, while for example in Costa Rica renewable energy is growing fast. The generating capacity of renewable energy grew by 670 megawatts in Costa Rica and 7 megawatts in Nicaragua in 1995–2004.

Nicaragua has no strategy whatsoever to reduce its oil dependency. The international financial institutions have not required investments in renewable energy either.

THE HIGHEST BILLS IN CENTRAL AMERICA

During 2000–2005 the residential consumers' electricity bills increased by 15 percent.

High bills are partially due to oil dependency and world market oil prices. But fixed payments are also very high, exceeding 20 dollars per installed kilowatt, while the international medium price is nine dollars per kilowatt.

Energy distribution costs are high as well, due to challenges faced with privatisation. The state owned distribution company was divided into two and privatised in the 1980s. Competition between the two companies ended, however, in 2000 when the Spanish company Unión Fenosa acquired a monopoly in the sector for the next 30 years with 115 million dollars.

Unión Fenosa is collecting considerable profits, because during the privatisation the government accepted high margins recommended by the IDB. According to IDB, international investors would otherwise have evaded the small market and the energy sector that suffers from high losses.

This means, in practice, that Unión Fenosa makes its customers pay for the energy losses. The losses constitute around a third of all produced energy. About half of these losses are caused by illegal connections made by poor households. The rest are technical losses, which Unión Fenosa should fix by investing in the infrastructure.

As a result, Nicaraguans are constantly protesting against Unión Fenosa.

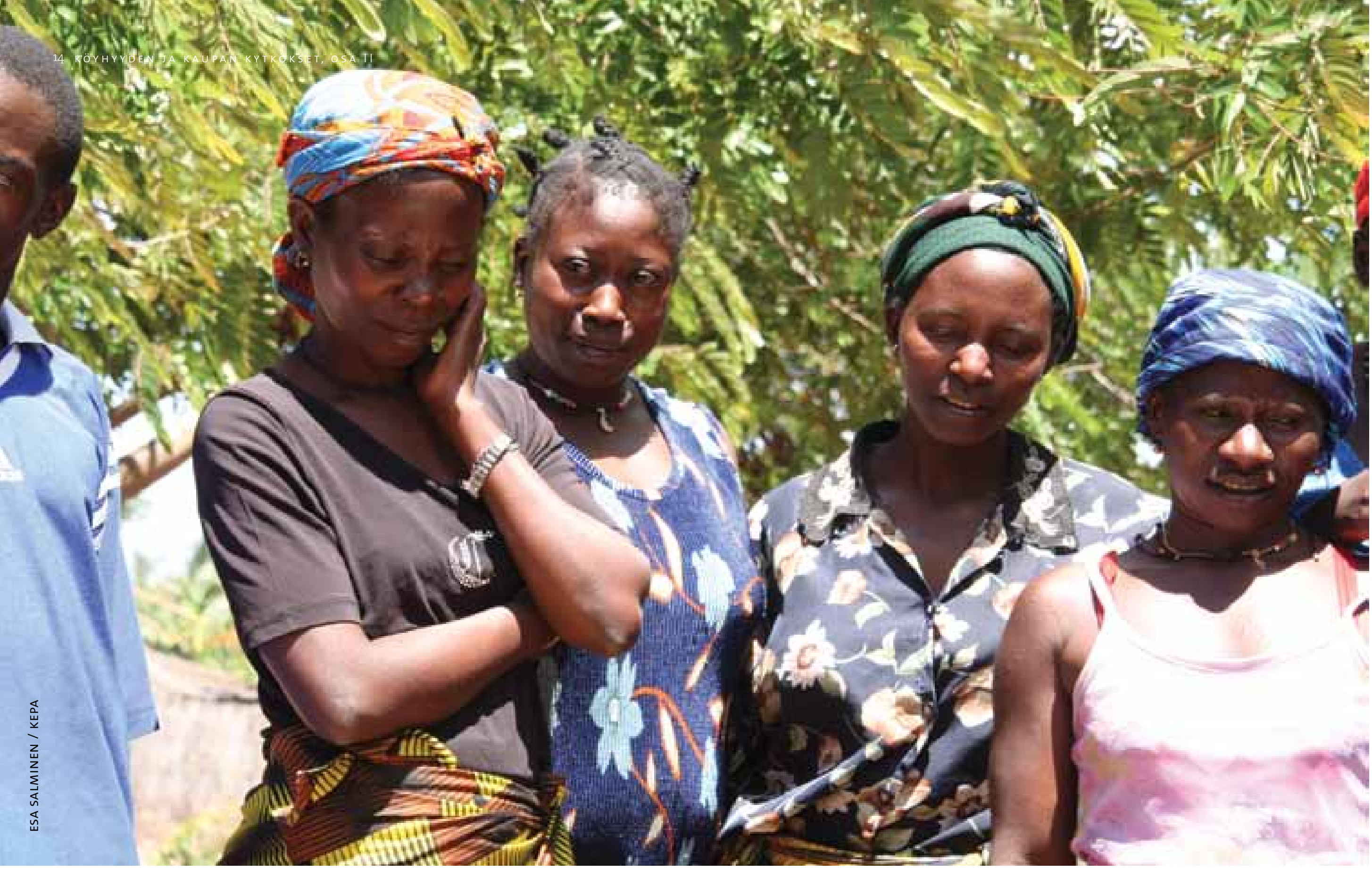
HALF THE PEOPLE WITHOUT ELECTRICITY

Half the Nicaraguans still cannot use an electric lamp or a refrigerator. Most of these people live in isolated rural areas where Unión Fenosa has little interest to invest. Large distances and small energy consumption by poor people mean high distribution costs and low revenues for the company.

State regulations do not oblige the private companies to offer services to isolated and vulnerable areas.

The only change brought by electricity privatisation in Nicaragua was the privatisation itself: the sector moved from the state into private hands. ◄

TONI SANDELL,
KEPA NICARAGUA



ESA SALMINEN / KEPA

It is hard to develop agriculture and entrepreneurship without access to credit. However, the members of UDACOMO, a North Mozambiquan union of farmers' associations, have noticed that private banks are not interested in poor customers in rural areas.

BANKING IN MOZAMBIQUE: MAJORITY ARE NOT GOOD CLIENTS

THE OPENING OF FINANCIAL AND TELECOMMUNICATIONS SECTORS TO PRIVATE AND FOREIGN CORPORATIONS IS AMONG INDUSTRIAL COUNTRIES' KEY OBJECTIVES IN TRADE NEGOTIATIONS. THE EXAMPLE OF MOZAMBIQUE SHOWS, HOWEVER, THAT FINANCIAL LIBERALISATION DOES NOT AUTOMATICALLY BRING HAPPINESS TO ALL.

► **POOR RURAL PEOPLE** seldom seem like good customers to banks. That is why 67 percent of Mozambican districts are yet to have a single bank.

The opportunity to access credit is, however, a key factor in developing agriculture and small enterprises. Isolated initiatives and the slow spread of commercial banks are helping the situation a little, but bank services are still far from reaching the majority of Mozambicans.

PRIVATISATION IN 1990S

Five of the six commercial banks operating in Mozambique were nationalised in the newly independent country in the late 1970s. The sector was re-liberalised in the 1990s during a structural adjustment programme of the World Bank and the International Monetary Fund. Between 1992 and 1997 all but the central bank were privatised, and the market was also opened for international banks.

Currently, all the country's commercial banks are private, since the central bank, Bank of Mozambique, has ended its commercial functions.

The liberalisation has had some good effects: the banking sector's net profitability grows 136 percent annually, and brings in annual profits of around 70 million euros, according to accounting company KPMG.

But the growth only reaches a selected few and is heavily urban-based. When the People's Development Bank (PDB) – tasked to grant loans at the countryside – was privatised in 1997, its rural branches were closed and agricultural lending was stopped. After privatisation, PDB became Banco Austral, the most famous case of mismanagement in the history of banking in Mozambique (see box).

MAJORITY OF PEOPLE WITHOUT ACCOUNTS

UDACOMO, the union of farmers' associations in the Montepuez district in Northern Mozambique, is located in a lucky area: there is a bank just 10 kilometres from the union headquarters. But UDACOMO could not get an account, though its papers were in order, and its Finnish partner organisation KEPA assured that money was forthcoming.

The reason was that poor farmers are not viewed as good customers. Agricultural lending is risky, because farming is affected by pests and unpredictable weather, and the low profits on offer in the rural areas do not interest private banks.

UDACOMO eventually opened the account in the provincial capital Pemba, some 150 kilometres away, where they were better received.

Most of Mozambique still has no banks, and the commercial banks remain largely concentrated in the cities. Yet 75 percent of Mozambicans earn their living from agriculture, and 82 percent live in rural areas.

In 2005, there were banks in just 28 of Mozambique's 128 districts. Three years later, that figure has risen to 42. This still leaves 86 districts without banks.

CREDIT IS KEY TO DEVELOPMENT

Poor access to credit slows down the growth of the economy, as it hinders the entrepreneurship of the working age population.

Along with the right to land and the state of infrastructure, access to credit is one of the cornerstones of agricultural and small enterprise development. The attitudes, regulations and requirements of the banks make it almost impossible for community groups such as UDACOMO to open and manage accounts. And when they do get credit, the interest rates are very high.

At present, most rural farmers have to rely on credit from agribusiness and trading companies when they need to buy seeds, fertilizer and pesticides, or to transport their products to markets. Usually agribusiness credit is based on contracts where the farmer agrees to sell his or her produce at a pre-arranged price.

CHARITY CREDIT IS NOT ENOUGH

Some poor farmers have access to microcredit offered by foreign organisations, charities, cooperatives, and even the government. These provide more tailored services to the rural poor but do not cover the majority of the country.

The government-sponsored microcredit programme, Fund for Investing in Local Initiatives, covers every district in the country. However reports from around the country reveal that access to credit is often restricted to a minority of people with the sufficient skills and political contacts to write suitable proposals.

It should also be remembered that microcredit is not banking: you cannot have savings, interest rates, cheque books or credit cards with microcredit NGOs.

Ernesto Gove, the Governor of the Bank of Mozambique, deplored to the news agency AIM in 2008, that there is plenty of money in the districts, but no banks where it can be deposited. Since rural savings are outside the financial system, they do not efficiently propel national growth. ◂

ESA SALMINEN,
KEPA MOZAMBIQUE

MURDER IN AUSTRAL: WORST CASE SCENARIO IN BANK PRIVATISATION

Mozambique's banking sector was quickly liberalised in the 1990s as part of the structural adjustment process.

The drafting of appropriate regulations for private banks can be demanding, however. When insufficient attention is given to questions of good governance, it is rather easy for those in power to exploit the privatised banks, draw large loans, neglect repayments and wait for the state to rescue the bank.

The saddest part of the privatisation of Mozambican banks is the murder of António Siba Siba Macuacua in 2001. The young economist was sent from the Central Bank of Mozambique to manage the second privatisation of the bad debt ridden Austral in 1997.

Banco Austral, the fourth largest bank in Mozambique, had spewed out reckless loans, particularly to some prominent political figures. An audit by KPMG found 45 million dollar embezzlements. By April 2001, the bank was running a deficit of 150 million dollars, and the Central Bank hurried to its rescue.

Macuacua was appointed to run the bank. He embarked on a vigorous debt recovery programme and cancelled contracts that he considered harmful for the bank.

In June 2001, he published a list of more than 1200 debtors in Mozambique's main daily newspaper. Among the names published were former ministers and senior figures of the ruling party.

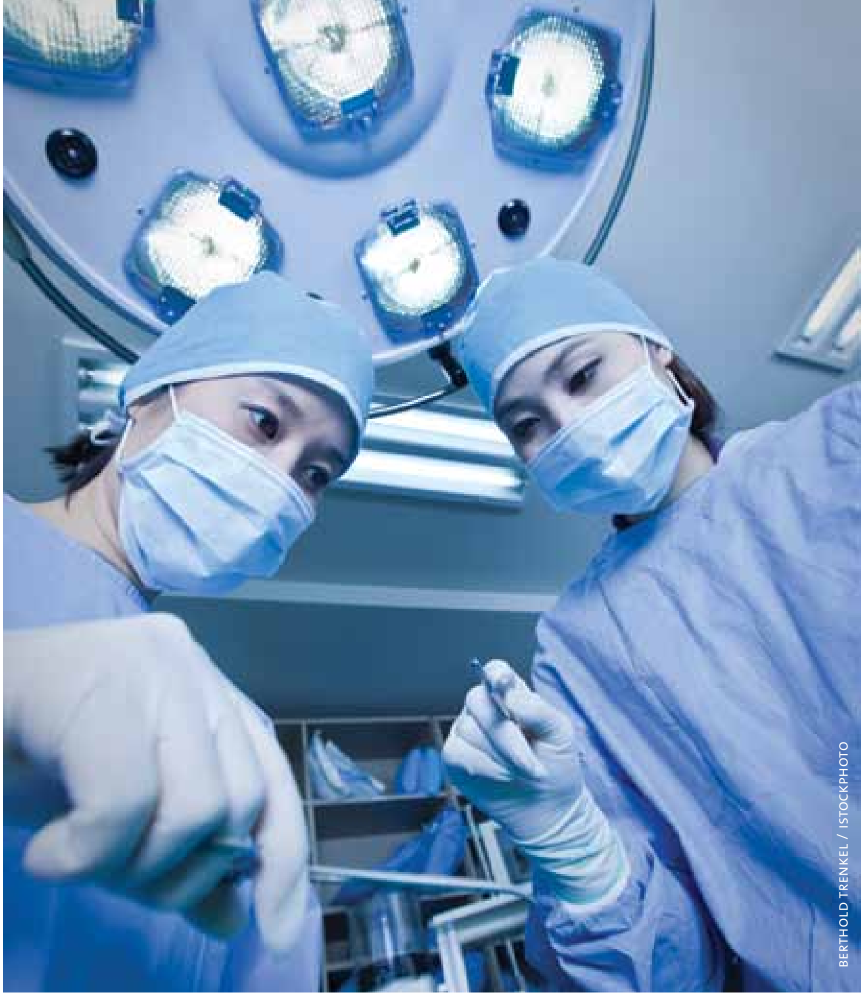
The cancelled contractors included Nyimpine Chissano, the son of the then president, who was a major suspect in the murder of the investigative journalist Carlos Cardoso in 2000. Cardoso's last piece of work was a semi-written article about corruption in Mozambican banks.

Macuacua's work as a bank manager only lasted for four months, because in the middle of the day on 11 August 2001 he was thrown down to his death from a ten-floor staircase at the bank's headquarters.

The murder is still unresolved. In 2008 one former board member and two security guards were arrested and charged with the murder.

However in May 2009 the court decided that there was insufficient evidence for the case to go to trial, and the suspects were freed.

No charges have ever been brought against the Banco Austral management for their ruinous management of the bank. Today, Banco Austral has been re-privatised and is run under Barclays Bank.



Top class hospitals and patented medicines are too expensive for poor people. Almost 500 Thai doctors shift from public hospitals to private clinics every year.

DRUG PATENTS IN INDIA: HEALTH FOR ALL OR PROFITS FOR SOME?

INDUSTRIAL COUNTRIES USE TRADE NEGOTIATIONS TO PROMOTE STRONGER INTELLECTUAL PROPERTY RIGHTS. THE CASE OF MEDICINE PATENTS IN INDIA HIGHLIGHTS THE CHALLENGES THIS CAUSES FOR POVERTY REDUCTION IN DEVELOPING COUNTRIES.

► **OFTEN DESCRIBED AS** "the pharmacy of the developing world", India is one of the leading suppliers of generic drugs. Indian drugs are often identical with patented medicines but many times cheaper.

GENERIC DRUGS AS SOURCE OF LIFE

The clearest example of the importance of generic medicines and Indian medicine production is the development of HIV/AIDS medication. Antiretroviral or ARV-medicines came to market in 1996, and the mortality of people living with HIV/AIDS in industrial countries fell by 84 percent in four years.

In developing countries the use of ARV-medicines started only once generic production in India drew the price of one person's annual dosage down from 10,400 dollars to 295 dollars in 2000–2001. Today the dosage costs 88 dollars a year.

The price drop revolutionised HIV/AIDS treatment in poor countries. Indian companies have also simplified the dosage and improved the heat-resistance of ARV-drugs, which are notable improvements in poor and tropical conditions.

Without generic medicines HIV/AIDS would kill even more people than today. It is the most common cause of death for adults in Africa. In nine African countries over tenth of the population carries the hi-virus. ARV-medicines are still only available for 42 percent of the people who would need them.

MEDICAL CORPORATIONS LOBBY GLOBALLY

Pharmaceutical corporations are, however, trying to curtail generic medicine production. The attempts of Swiss Novartis, the world's third-largest pharmaceuticals company, have been in the public eye particularly often.

Novartis is applying for an Indian patent for the second version of its leukemia drug Glivec. The price tag on the drug is 1,765 euros a month per patient. The drug also needs to be taken throughout the patient's life, which makes it unattainable even for well-off patients if they need to pay for the medicine themselves.

As the drug has already received patents in 40 other countries, the company argues it should be accepted for patent in India too.

In 1993 Novartis was granted an Indian patent for Glivec's active ingredient, but not for the whole drug. India has only granted patents for whole drugs since 2005, when membership in the World Trade Organisation has obliged it to follow the WTO agreement on Trade Related Intellectual Property Rights (TRIPS).

However, the Chennai Patent Office refused to grant a patent for the second version of Glivec in January 2006. It decided that the drug did not "differ significantly in properties with regard to efficacy" compared to the earlier patented ingredient.

The patenting of very similar substances is denied to prevent companies from 'ever-greening' expiring patents and prohibiting competition.

HEALTH CARE IS A CONSTITUTIONAL OBLIGATION

Novartis appealed against the decision, arguing that the new drug has much better bioavailability – and that the requirement of "significant difference" is "unconstitutional and in breach of India's obligation under TRIPS" in the first place.

The appeal has so far been refuted. India has a "constitutional obligation of providing good health care to its citizens", ruled the Madras High Court in October 2007.

Further, the Indian Intellectual Property Appellate Board (IPAB) ruled in June 2009 that the drug "lacks innovation". The IPAB also considered it against the "public order" to legitimise such a high monopoly price with a patent.

But the case is not closed yet: Novartis has taken the case to the Indian High Court. Switzerland could also still lodge a complaint against India in the WTO's Dispute Settlement Body.

TRADE AGREEMENTS AND PUBLIC HEALTH SERVICES

The members of the WTO agreed in 2001 that "the TRIPS Agreement can and should be interpreted and implemented in a manner supportive of WTO's members' right to protect public health and in particular to promote access to medicines for all."

The example of Novartis in India shows, however, that this important principle is interpreted in several ways. Doctors Without Borders, a highly respected non-governmental organisation, together with tens of other NGOs, have campaigned against tighter patents for years.

Any tightening of patent laws would dramatically decrease the availability and affordability of drugs around the world. The implications would be gravest in developing countries where patients pay for 50–95 percent of drugs themselves. Development cooperation would also become more expensive, because generic medicines are widely used by aid agencies such as UNICEF. ◄

KAISA LAIHIALA AND OUTI HAKKARAINEN,
KEPA HELSINKI

HEALTH TOURISM DRAINS DOCTORS FROM PUBLIC THAI HOSPITALS

The challenges facing Thailand's health services are an awakening example of the risks that export promotion policies can pose to poverty reduction. The influx of foreign health tourists drains doctors away from public hospitals in poor areas.

"All for health and health for all" is the motto of the Universal Health Care Coverage scheme of Thailand launched in 2001. The scheme seeks to guarantee equitable and free access to public health services for all Thais.

Health for all -scheme is, however, shadowed by simultaneous attempts to expand medical services for high-paying foreign patients. In 2004 private Thai hospitals gained over 600 million euros by treating 1.1 million foreign patients, according to Thailand's Export Promotion Department. The biggest group were the 240,000 Japanese, followed by patients from the USA, England, Asia and Middle East.

The growing number of foreign patients pulls doctors away from public hospitals. Each year 450–500 doctors resign and move to private hospitals.

This is a grave concern for understaffed public hospitals. In the country's poorest region in the Northeast, there is just one doctor for 7,542 patients. Finland has one doctor for each 299 citizens.

Thai Public Health Ministry has estimated that 15,000 new doctors would be needed each year in 2003-2013, but only 8,000–10,000 doctors graduate annually.

The exodus of doctors from public hospitals also carries a cost to the government, which funds 98 percent of doctors' training. The losses for every 100,000 foreign patients are estimated to amount to 8.4 – 25.2 million euros.

The profits generated by private hospitals are not trickling down to the common people. Profits accrue to the owners of the 33 private A-class hospitals that receive foreign patients and charge fees far above the means of the common people.

Trade negotiations have been used as a way to open up the Thai health sector. For example the Japan-Thailand Economic Partnership Agreement (JTEPA) stipulates, that Japanese patients can get reimbursements for 70 percent of the medical fees paid in Thailand from the State Medical Service Fund of Japan.

WARANGKANA RATTANARAT
KEPA MEKONG

THAI RETAILING: HYPERMARKETS SIDELINE SMALL ENTREPRENEURS

ENSURING EQUAL TREATMENT FOR FOREIGN AND DOMESTIC INVESTORS IS AMONG THE KEY OBJECTIVES IN INTERNATIONAL TRADE AGREEMENTS. THE EXAMPLE OF THE THAI RETAIL SECTOR SHOWS, HOWEVER, THAT THE ENTRANCE OF LARGE MULTINATIONAL CORPORATIONS CAN THREATEN FAIR COMPETITION.

► **THE RETAIL SECTOR** in Thailand has changed rapidly in the last 15 years. Hypermarkets and transnational retail chains have come to occupy 70 percent of the market, while tens of thousands of small Thai-owned shops close their doors every year.

The retail sector forms an important part of the national economy. It accounts for as much as 15 percent of the gross domestic product.

HYPERMARKETISATION

Hypermarketisation gained momentum when Thailand became a member of the World Trade Organisation (WTO) in 1995. Under the WTO agreement on trade in services, Thailand has to welcome foreign enterprises in the retail sector.

The Asian financial crisis further accelerated the change. To attract foreign investment, the Thai government abolished the need for foreign investors to engage in joint ventures with Thais. Since then, large investors with capital of over 100 million Thai baht (approximately 2 million euros) have been allowed to operate alone.

As a result, the number of hypermarket branches has increased from 56 to 706 in the period 1998–2008. Transnational retailers present in Thailand include Tesco (UK), Carrefour and Casino (France), Ahold and Makro (Netherlands).

Small retail shops, on the other hand, are becoming fewer. Today, about 2,500 small retail shops are shut down every month, according to the Small and Medium Enterprise Promotion Office of Thailand.

SMALL-SCALE PRODUCERS ARE MARGINALISED

Hypermarketisation reduces employment in the retail sector, because small shops used to employ more people than hypermarkets do (see the box).

Hypermarketisation also brings difficulties for small-scale farmers and other producers. Negotiations between large hypermarkets and small-scale suppliers are unequal. As more and more people shop at hypermarkets, producers become more and more dependent on the hypermarkets as an outlet for their goods.

Hypermarkets tend to utilise this power to demand high quality, large volumes and punctual deliveries from their suppliers. This is causing a concentration of production into fewer and larger corporations, because few small Thai producers are able to meet the requirements.

Hypermarkets also offer low producer prices. In Thailand the offered producer prices have at times even been below production costs. Despite this, Thai hypermarkets expect producers to pay various fees for shelf space, adverts, special promotions, the opening of new hypermarket branches and so on.

HOUSE BRANDS CAPTURE MARKETS

What completes the marginalisation of small-scale producers is the expansion of so-called house brands. For example Tesco has its own Tesco brand, which includes over 8,000 household and food items. No fees are charged for these items, so they are up to 50 percent cheaper than other brands.

House brand items need to be produced in large, homogeneous quantities, so hypermarkets tend to contract their production to large corporate producers. As the house brand series are becoming wider they eat shelf space and market share away from other products.

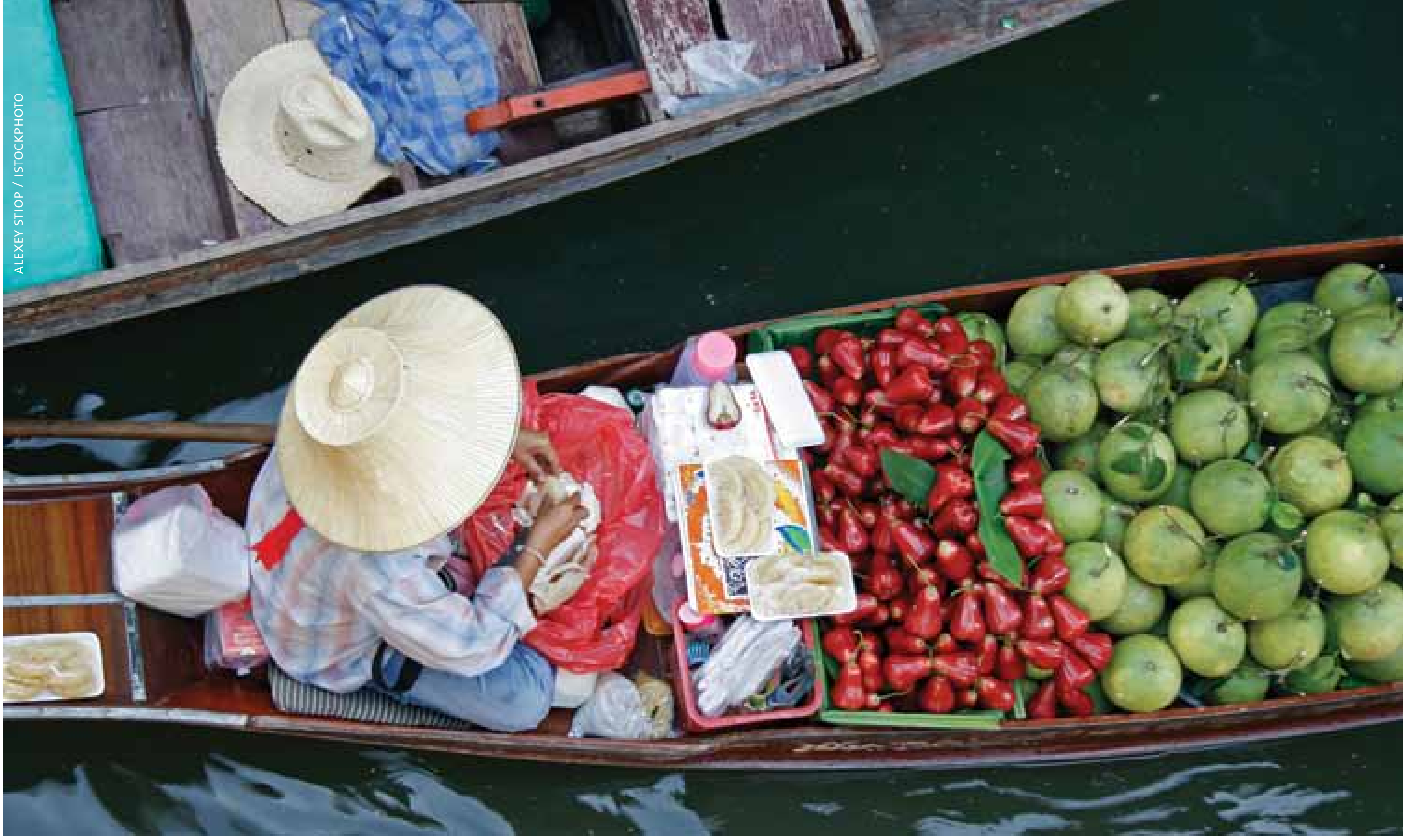
Foreign producers are also gaining space. Chinese vegetables and fruit have become particularly common since tariff cuts were agreed in a free trade agreement between Thailand and China in 2003.

SOCIAL SPACES CHANGE

The concentration of the retail sector also has social implications. When small local shops are closed down, the consumers' choice becomes more limited.

The trip to a hypermarket can be arduous and expensive for the most vulnerable consumers, such as elderly people, single mothers, the disabled and sick people.

In rural areas, markets are not only places for shop-



Ensuring fair competition in retailing requires competition rules and support to small entrepreneurs. In the picture a fruit vendor at a wet market near Bangkok.

ping, but also for social exchange. It is inevitable that changes in traditional market areas also change the social space and the culture of local communities.

FAIRER PLAY WITH SHARED RULES

Concentration seems to be an inevitable end of the current economic system.

In Thai retailing, however, the competitiveness of large shops is not only based on efficiency, but also the harsh use of market power (see the box). So it is not a result of free but of non-free markets.

It is even reasonable to ask whether hypermarkets have actually reduced or increased poverty in Thailand. They do provide cheap goods for consumers. But they also cut incomes among small producers, suppliers, vendors and shopkeepers.

These adverse effects need to be tempered through stronger competition rules and support to small entrepreneurs. Public policies to moderate the power of large corporations must not be a tabu. Extreme concentration is not inevitable. It is just the result of inadequate public ground rules for the big players with the big money. ◂

WARANGKANA RATTANARAT,
KEPA MEKONG

SMALL RETAILERS LOSE OUT

Jiraporn Suksani, a grocery shop owner, has lived through the changes of the Thai retail sector. Her shop, first owned by her mother, has been the main source of income for her family for over 20 years. The shop is located at Muang Pol wet market in Khon Khen province, 500 kilometers Northeast of Bangkok.

The market used to be crowded with customers, but the change came suddenly in 2007 when the first hypermarket branch opened its doors close-by. Jiraporn's incomes dropped to half their previous level. She used to sell her goods within a week, but now it can take over a month.

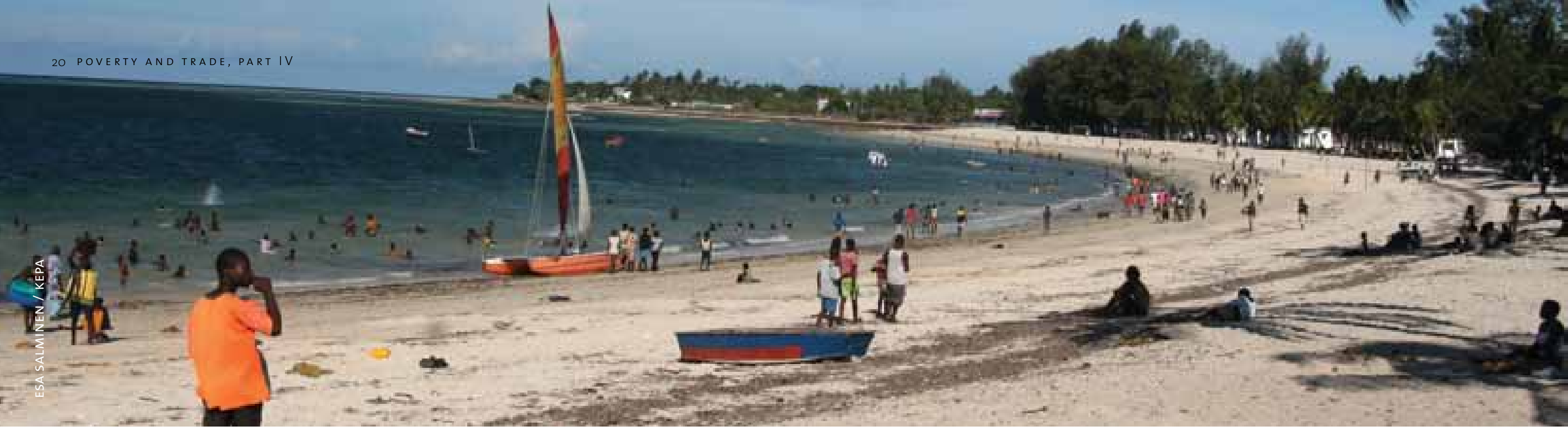
Next door, pork butcher Sunee is facing similar problems. Instead of selling at least four pigs a day, her sales have plummeted to two pigs.

...WHEN HYPERMARKETS USE THEIR POWER

Pork butcher Sunee feels that the close-by Tesco branch uses underpricing intentionally to force competitors out of business. For example red meat, normally sold at 125 Thai baht per kilogram at Muang Pol market, is periodically sold at Tesco for as little as 90–110 Baht per kilo, according to Sunee.

Tesco-Lotus is the leading foreign retailer. In September 2008 it had 465 branches in 50 of the 76 provinces in Thailand. To penetrate small cities, Tesco-Lotus has downsized its branches into small discount stores.

Having more branches means not only more customers, but also more negotiating power vis-a-vis suppliers. With this aggressive expansion strategy, Tesco has captured 39 percent of the Thai retail market.



ESA SALMINEN / KEPA

In Northern Mozambique, tourism brings revenues to luxury hotels but local people have access to an ever narrower stretch of beach.

TOURISM IN NORTH MOZAMBIQUE: WEAK LINKS TO LOCAL ECONOMY

WITH 2,700 KILOMETERS OF INDIAN OCEAN COASTLINE, A RICH CULTURAL HERITAGE AND GREAT BIODIVERSITY, MOZAMBIQUE HAS ENORMOUS POTENTIAL TO BENEFIT FROM TOURISM. THE FOREIGN INVESTMENTS FLOWING TO THE TOURISM SECTOR HAVE NOT, HOWEVER, BENEFITED THE LOCAL POPULATION AS HOPED.

► **IN MOZAMBIQUE,** one of the poorest countries in the world, tourism is expected to bring foreign investment, boost employment and increase demand for local production.

Tourism is indeed attracting foreign investment. Industry currently gets 33 percent, energy and natural resources 18 percent and tourism 16 percent of all foreign investment. Nevertheless, the tourism sector only yields 1.5 percent of the country's gross domestic product.

There are high hopes for tourism, but the actual benefits have been small.

SUPPORT GOES TO LUXURY RESORTS

Support from the government of Mozambique has mainly been allocated to large-scale lodges and resorts, says Chabane Agostino Combo, president of the Tourism and Hotel Association of Cabo Delgado in Northern Mozambique.

According to Combo, community tourism could create local jobs and increase the appreciation of the local culture and gastronomy, but the only available support has been the micro-credit programmes of some NGOs.

Medium-sized hotels and restaurants are also suffering from the lack of support. One problem for many aspiring entrepreneurs is the lack of capital: they need start-up capital for getting a bank loan.

The luxury lodges and resorts, supported by the government via cheap loans and land, tax breaks and other incentives, are all in the hands of foreigners, mainly South Africans, Europeans and Arabs.

PRODUCTS AND EMPLOYEES FROM ABROAD

The resorts make few purchases from local producers. Local vegetable, fruit and seafood sellers are losing the competition to foreign commercial cultivators operating in the region. Some resorts fly in all their supplies from South Africa or Maputo, the capital of Mozambique.

Tourism employs some 1,600 local people, but mainly informally, with low salaries and harsh working conditions. Luxury hotels bring their employees from South Africa, Europe or other countries.

In the Quirimbas National Park, somewhat higher expectations are placed on foreign investors. The land rent is higher than outside the park, and one entrepreneur can only rent a maximum of 200 hectares on the mainland and 5 hectares on the islands. Tourism enterprises have to give a fifth of their income to community development programmes. This money has already financed some water and agriculture projects.

Dicrepancies are common, however. According to José Dias dos Santos, Chief Park Warden of the Quirimbas National Park, a considerable part of the revenues is simply not reported.

LOCAL PEOPLE LOSE THEIR LANDS

What is most concerning, however, is that foreign investment has even curtailed local people's wellbeing in some ways.

Luxury resorts have leased large land areas. Lacking documents and clear information about their rights, hundreds of people have been pushed away from these lands. Land laws state that local communities should be consulted before a long-term land lease is signed, but the laws have been squarely ignored.

Some lodges have even denied access to the beach from the local people, although in principle all beaches in Mozambique are public. ◄

PAULIINA SARVILAHTI-JIMÉNEZ
KEPA MOZAMBIQUE

TEMPORARY MIGRATION TO THE NORTH: ONLY THE SKILLED AND THE BEAUTIFUL ARE WELCOME

INDUSTRIAL COUNTRIES NEED FOREIGN EMPLOYEES WHILE DEVELOPING COUNTRIES NEED REMITTANCES AND THE RETURNEES' KNOW-HOW. EVEN SO, TEMPORARY MIGRATION IS AMONG THE HARDEST DISPUTES IN TRADE NEGOTIATIONS.

► **IN SEVERAL INDUSTRIAL** countries, the work force will soon start shrinking. This is already the case in two aging countries – Japan and Finland – and Europe is following suit. So industrial countries need immigrants.

Developing countries also need migration. In Kenya, for example, remittances from the 200,000 migrants living in industrial countries account for 2.7 percent of the national economy. The contribution is larger than that of aid, which has recently hovered around 2 percent of the national economy.

Remittances flow directly to migrants' families so they cannot fix weaknesses in economic structures or public services. Even so, the impact can be lasting: the World Bank estimates that remittances reduce poverty in Kenya with 8.5 percent.

In addition to employment opportunities and better wages, migrants may also seek distance from societal instability or environmental catastrophes. Approximately two million people from all over the world arrive in Europe each year.

EUROPE BUILDS FENCES

The international demand and supply of labour still do not meet. About a quarter of all migrants to Europe arrive through illegal channels. Human trafficking has grown to a large scale industry in the Southern and Eastern outskirts of Europe.

Considerable resources are also used to control illegal immigration. The newest "friendship treaty", where the key objective is curbing illegal immigration, was signed by Italy and Libya in March 2009.

It's not free trade when only goods and capital travel.

The agreement includes joint naval patrols on Libyan and international waters, in order that boats carrying migrants can be interdicted and returned to Libya.

MIGRATION AS A TRADE ISSUE

In trade negotiations temporary migration is considered a service issue: sometimes service providers need to travel abroad to sell their services to foreign employers. This is common on several service sectors from research to construction engineering.

Moving temporarily from one continent to another is much more difficult for less educated than highly educated people. Developing countries have demanded corrections to this imbalance in several trade negotiations.

In the World Trade Organisation, the least developed countries made an official request in May 2005, that boundaries be opened for employees with no university level education. Industrial countries have not responded.

DOORS OPEN FOR MODELS – NOT FOR CLEANERS

The attitude of the European Union member countries towards migration is revealed by a regional trade deal with the Caribbean countries, which is likely to be ratified in 2010. The Economic Partnership Agreement (EPA) increases employees' access from the Caribbean islands and small countries to European job markets.

Caribbean employees working on 29 service sectors are allowed to enter the EU once they have secured a contract, and on 11 sectors temporary entry is even allowed to self employed people. Without a university degree or a similar professional qualification immigrants are, however, only accepted if they work as entertainment workers, fashion models or chefs.

A random check in the Finnish Job Centre vacancy database in December 2009 showed over 1,500 vacancies for workers in catering, cleaning and hair-dressing. There was one vacancy for a fashion model. ◄

SOFIE SANDSTRÖM

DISPUTE SETTLEMENT: DEVELOPING COUNTRIES AT DISADVANTAGE

COMMERCIAL DISPUTES BETWEEN CORPORATIONS AND STATES ARE BECOMING MORE AND MORE COMMON. THE DISPUTES ARE EXPENSIVE AND OFTEN TAKE YEARS TO SETTLE. LACK OF FUNDS, SHORTAGE OF COMMERCIAL LAW EXPERTS AND FEAR OF RETALIATION PUT DEVELOPING COUNTRIES AT A DISADVANTAGE IN THE ARBITRATION PROCESS.

► **WHEN A FOREIGN COMPANY** finds that the laws of its host nation conflict with international trade agreements and constrain its business, it can lodge a complaint with the national courts or international arbitration bodies. Disputes are becoming more common, as the number and coverage of trade agreements grows.

Going international is also increasingly common. Free trade treaties usually establish a right for foreign investors to bypass host country courts and go directly to international arbitration bodies.

ARBITRATION TAKES YEARS

Dispute settlement is problematic on several accounts. The arbitration processes take years, which is challenging for corporations and states alike.

For example at the WTO, countries or companies are only asked to change their policies after the dispute is solved. This often first involves consultations, then analysis by a sectoral board, the Dispute Settlement Body, and a tailor-made panel, and finally again the Dispute Settlement Body.

The disputes are also very diverse, which creates its own challenges. The arbitrators, who are usually lawyers and economists, have to decide whether free competition is more or less important than for instance restricting gambling, recycling old tyres or reducing in-country digital divides.

There are cases where the panel has simply not been up to the task.

THE POOR AND THE POWER-PLAY

Formally, all countries get equal treatment in the international dispute settlement bodies. In practice the developing countries face greater pressure to settle cases, and have smaller chances of winning them.

The commercial law expertise at the disposal of developing country governments is usually smaller than the fleets of lawyers commanded by the large corporations and governments of the industrialised countries. This limits the capacity of the developing countries to claim their rights in the jungle of complicated trade and investment agreements that prevails today.

Small economies cannot afford to face big fines or retaliatory measures. Many developing countries are small indeed: there are 79 countries whose national product is smaller than the annual turnover of the hundredth largest company in the world.

Retaliation by a major trading partner can really disrupt a poor economy. The WTO allows the claimant for example to raise tariffs. This can be a big problem for a poor country which only exports a few goods to a few countries.

Even high litigation costs are a bigger concern for a smaller purse. At ICSID, all arbitration costs and legal fees must be paid by the losing party.

The settlement processes also involve a lot of power-play. The Swedish International Development Agency (SIDA) has noted that strong economies are more likely to win disputes already in the consultation phase, as developing countries bow under pressure and the fear of retaliation. ◄

OUTI HAKKARAINEN AND KAISA LAIHIALA, KEPA HELSINKI

ARBITRATORS OF THE WORLD ECONOMY

Among the most popular international arbitration bodies is the International Center for Settlement of Investment Disputes (ICSID). It facilitates the arbitration of investment disputes between companies and its 144 member countries.

The number of disputes is clearly growing. There were 121 cases in process in November 2009, while only 180 cases have been solved since 1972. The favourite culprit, with 29 pending cases, is Argentina.

Service-related cases make up more than a fifth of all the cases at ICSID. The defendant is usually a developing country and the claimant an industrialised country or an investor from Europe or United States.

Another popular arbitration forum is the dispute settlement mechanism of the World Trade Organisation (WTO). As an intergovernmental organisation, the WTO only accepts complaints from states, so arbitration processes often start with a company lobbying its government to lodge a complaint.

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