



Canadian International
Development Agency

Agence canadienne de
développement international

CATEGORY 505 ☐



ECONOMIC INTEGRATION STUDY

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Summary

CATEGORY 505 - ECONOMIC INTEGRATION STUDY

This document presents the findings and recommendations of the assessment phase of CIDA support for Private Sector Development (PSD), with particular reference to *Trade and Economic Integration*. The latter comprises one of five sub-categories of CIDA programming for private sector development, the other four being *Enabling Environment* (0501), *Capacity Skills and Productivity Enhancement* (0502), *Canadian and Developing Country Private Sector Linkages* (0503), and *Local Enterprise* (504).

As in the case of the other four areas, our own study was asked to assess the validity and utility of the current criteria used to determine whether CIDA activities fell within “Trade and Economic Integration” as currently described, viz.

“comprises the adjustment of the private sector in developing countries to the post-Uruguay Round trade regime to facilitate integration into the world economy – i.e. helping developing countries to build their private sector for trade and strengthen it in light of world-wide developments. Countries often abide by requirements of a legal nature arising from agreements with world organizations or multilateral frameworks, where increasingly failure to do so gives rise to trade disputes and sanctions which may cause significant disruption to emerging economies”.

In common with other studies undertaken in this phase, our own assessment lays the basis for the next one, namely an in-depth evaluation. To this end, we examine the utility of the above definition; consider practices for coding activities; develop and test a framework to guide the evaluation of projects; and raise key operational and strategic concerns through an in-depth examination of various types of projects falling within the 0505 category.

Briefly we set out below some strategic findings that should be considered in the design and implementation of the next phase.

Trade and Economic Integration

The current formulation focuses almost exclusively on trade – in goods. Consequently it ignores the broader effects of globalisation, on development assistance in general and the expanding range of goods and services potentially or actually being traded internationally. These comprise both opportunities and sources of competition for the private sector. Also overlooked is the role played by capital flows, far larger in magnitude and more immediate in impact than those in goods and services. Especially at the country level, CIDA activities will be affected by such movements, most notably in the context of the *Heavily Indebted Poor Countries Initiative (HIPC)* for relieving multilateral debt.

Types of Projects

Our typology of projects highlights opportunities and risks, and consequently implications for their design and management. Among the salient distinctions are the level of activity (national, regional and international), CIDA's posture in terms of programming (proactive or responsive), and form of integration (goods and services, capital movements, transfers (of development finance)). Each of these parameters inherently poses challenges with respect to the design of CIDA interventions and factors bearing on their outcome.

Among the operational concerns highlighted by our analysis are:

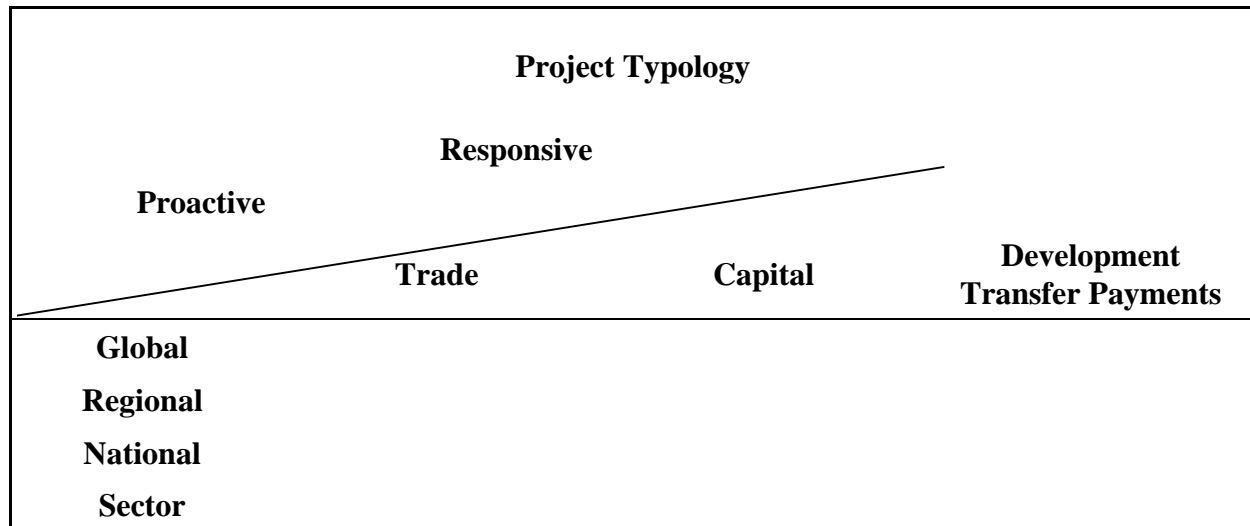
- Inconsistent use of the logical framework analysis;
- Absence in many instances of standardised procedures for tapping the corporate memory;
- Critical need for more creative and systematic use of in-house resources in reviewing projects;
- Insufficient respect for the complexities of regional projects and programs;
- Occasional overlook of important operational lessons to be obtained from well executed projects;
- Incomplete review of the advantages and drawbacks of responsive programming in particular circumstances; and
- Variations of risk according to the project parameters mentioned above.

With respect to more strategic concerns, our analysis cites the following issues:

- The increased intertwining of Canada's own interests and those of developing countries in various international arenas, notably the WTO.
- The growing need for CIDA and Canadian expertise in such areas as trade and international financial architecture since global developments have a direct bearing on its programming within specific countries and sectors.
- A need for a more sanguine and informed approach to programming within and for particular regions.
- The need for CIDA to invest in Canadian expertise in many of these fields, and
- The importance of continued strengthening of relevant institutional and professional capacities in developing countries.

Section 1 details the procedures, materials and terms of reference guiding the formulation of the work plan and the principal outputs from the inception phase of the study. It outlines the sections of the report and their respective contents.

Section 2 centres on the formulation of a typology that was subsequently used to assess the corporate data base and analyse a sample of projects. The utility of this typology was also tested during the assessment. The recommended typology comprises three elements as depicted below.



The three “elements” of the typology, as portrayed by the three axes of the diagram are as follows:

Forms of Economic Integration (Y axis)

- trade in goods
- trade in services
- flows of portfolio capital
- flows of direct investment
- development transfer payments, especially debt relief

Levels of Intervention (X axis)

- global
- regional
- national
- sector

Approach to Program Identification and Implementation (Z axis)

- proactive, viz. initiated by CIDA
- responsive, viz. initiated by the recipient(s) and/or implementor(s)

In principle all projects concerned with economic integration can be accommodated within this typology illustrated in the table below.

Project Typology Grid

Level of Activity	Form of Economic Integration					CIDA Approach	
	<i>Trade in Goods</i>	<i>Trade in Services</i>	<i>Portfolio Capital</i>	<i>Direct Investment</i>	<i>Development Transfer Payments</i>	<i>Proactive</i>	<i>Responsive</i>
<i>Global</i>							
<i>Regional</i>							
<i>National</i>							
<i>Sector</i>							

With respect to the performance review, we offer the following observations:

- A necessary if by no means sufficient condition for the reduction of poverty – in the absence of continuous and significant income transfers – is the need to raise total factor productivity. Given the very limited size of the domestic market in virtually all poor countries, factor productivity can only be improved significantly through expanded access to and exploitation of richer and larger international markets for their goods and services. Put somewhat differently, successful integration in the global economy comprises a necessary condition for the alleviation of poverty.
- The typology does cover all potential
 - “Development transfer payments” should cover balance of payments support and lines of credit for the purchase of Canadian goods and services as well as the pending major involvement in debt relief.
 - With respect to *level* of intervention, we found that the lowest, namely that involving individual firms, should not be included in our typology. In effect, such interventions are more accurately directed toward promoting direct economic linkages and should be coded as 0503.
- The typology can help explain differences among projects in terms of their results. In effect, projects involving “economic integration” in trade of goods and services differ significantly in their aims, time frame, design, and risk from those concerned with flows of capital and/or those focusing on various types of international transfer payment. Likewise conditions for success will differ among projects implemented at a global, regional, or national level.

Finally, we have detected significant differences, especially with respect to project design and likely sustainability, between those designed and implemented on a proactive basis, and those where CIDA has provided resources in response to a proposal originating outside the Agency.

Section 3 focuses on our assessment of the corporate data base for projects. It outlines our methodology and sets out our findings. With respect to the performance review, we offer the following observations:

- Our principal recommendation is that there should be a single centralised process, if not locus, for the coding of all projects. Coding at the moment is either in the eye of the beholder and/or – understandably – driven by what seems to be “the flavour of the month” i.e. what is likely to get through the system at any given moment. The performance review must be able to draw broader inferences from a smaller sample of projects. But if the underlying data set is flawed from the beginning, the exercise is compromised. Rather than spend time and money in getting outsiders to rectify the set – an imperfect exercise at best – fewer resources could be much more effectively used in having the projects coded systematically and consistently across the agency in the first place. For this task, we would recommend three groups: the corporate memory group doing the data entry; policy branch, which has an overview of the agency’s strategies and activities; and not least, the program staff preparing the project in question. Where necessary, the results could be checked by some outsiders.
- In selecting a sample of projects for further analysis, it does appear helpful to group projects by scale and focus on those above a certain amount. In the case of the 0505 group, projects under \$100 thousand account for about half the projects in terms of number, but less than 1% of total allocation. Any spin-offs from these projects will likely have been reflected in further project development that can be picked up under larger scale activities. By observing the “grouping” of projects, our “cut-off points” were also consistent with different approval levels within the Agency.
- The CIDA Inc. coding clearly needs to be revisited.
- The larger number of projects within the 0505 data set comes from the CEE Program (prefixed with a “Z” in the project number). Initially this program focused on two objectives: transition to a market economy and partnerships at the enterprise level with Canadian firms. The 0505 category is compatible with the former. However, firm level linkages do not fit comfortably within the 0505 category. In a separate communication to the Performance Review Branch, we have identified those projects that, in our view, do not fit within the 0505 category for the purposes of the performance review of private sector development.
- Nonetheless, we do note that the larger number of smaller projects in the CEE program does highlight the potential importance of a “responsive” approach to the *initial* identification of a project, especially one involving the private sector. For firms, timing is often more important than the quantum of assistance. Being able to process a request more rapidly and with fewer transactions costs is mutually appealing to both CIDA staff and the project proponent. We suspect that the larger number of projects and their smaller scale – in duration and allocation

– within the CIDA Inc. and CEE program is important for activities involving individual private firms.

- The 0505 category does contain projects involving large income transfers, essentially to help cover shortfalls in a country's external balance. In the past, such "development transfer payments" have taken the form of a line of credit for the purchase of Canadian goods or, in one case, direct Canadian servicing of a country's external (IMF and World Bank) debt. In future, these income transfers will increasingly assume the form of direct debt relief. Since it will be closely tied to adherence to World Bank/IMF structural adjustment programs, such projects can be classified under the 0505 category. Yet to be determined is whether such transfers will be charged to CIDA's budget. If CIDA's overall "envelope" is not increased, these transfers could entail a high opportunity cost, in terms of cutbacks in other programs. These and related issues, e.g. the linkage to poverty reduction, have yet to be clarified. Indeed, at present there is no corporate policy on debt relief, albeit that Canada has been among its most strident advocates internationally. At this juncture, the easiest way to handle these types of payments is to treat them as "income transfers", whatever the modality in question. Our own view is that they comprise a separate category since they are directed toward changing the environment for development *per se* and not simply one specific to the private sector.

Part way through our study, we were requested to comment on a revised coding framework for the PSD category. In our view, the coding structure for the 0505 category should conform, as much as possible to the project typology, in part for consistency between classification and subsequent analysis, but principally because our work indicates that the typology does appear to capture the various interventions concerned with "economic integration". Our recommended structure, conforming to the level of disaggregation proposed for the 05 category, is set below.

Recommended Coding Structure

Title	Category	Sub-Category	Parameters
Economic Integration	505	Trade in Goods and Services	Interventions at the global, regional, national, and sector levels
		Financial Flows: Portfolio and Direct Investment	Interventions at the global, regional, and national levels
		International Transfer Payments including Debt Relief	Interventions at the global, regional, and national levels

Section 4 of the report presents our analysis of a sample of projects. One element of this analysis are the criteria for assessment. These are set out in a grid of factors bearing on development results and project success (Table 4.1). The second element is the sample of projects (Table 4.2). The processes and criteria used for their selection are also described in section 4.

The principal findings of our analysis concern those factors central to the success of projects.

a) *The Logical Framework Analysis*

Our first observation is that the format and content of the “log frame” varied considerably among projects as did its application by CIDA staff. Furthermore, CIDA staff did not apply this analytical framework consistently. Consequently there were considerable differences among projects in the specification of outcomes.

A somewhat different issue pertains to the setting of indicators for measuring outcomes and impact. Inevitably, the margin of error in forecasting results must increase as the period in question is pushed forward. Attempting to impart a sense of rigour through quantification can therefore prove spurious and misleading. More useful would be projections of possible trends to measure progress in the desired direction.

Finally, we note a confusion, in some projects, between changes in a *specific policy* and in the *policy process* itself. Adopting a specific policy may not necessarily prove to be an accurate indicator of success, either in terms of advancing “economic integration” or even “better governance”. Much more important is a reform of the policy process itself in terms of providing accurate and timely information and analysis to decision makers; involving principal stakeholders in an effective manner, and providing workable solutions for implementation. This distinction was not always evident in terms of the indicators set for measuring both outcomes and impact.

b) *Corporate Amnesia*

Our own sample did not reveal a systematic attempt to record basic information that could, in conjunction with more formal reviews and assessments, comprise part of the corporate “learning curve”. The recording of such information in an electronic project file should not prove difficult and could yield considerable dividends. Such basic information could include:

- A listing of major documents used in preparing and assessing the project
- A listing of key people associated with the project in various capacities
- Major events over the lifetime of the project
- An ongoing “scratch pad” for recording lessons learned.

c) *Peer Review*

An absolutely necessary if by no means sufficient condition for success is an accurate definition of the issue or problem the project is purporting to address. If the problem prompting the intervention has been wrongfully diagnosed at the outset, the project will not achieve the desired results. Such errors, in our view, can be avoided through an independent review by individuals, with or outside CIDA, conversant with the topic and/or region in question. They can raise salient questions, thereby reducing the likelihood that the project is centring on the wrong issue or that the issue has been improperly understood.

d) *Regional Projects*

Our foregoing observations, centring on the need to “front load” the identification, design and appraisal stages of the project cycle are especially relevant to regional projects. The rationale or motivation behind a regional project will usually vary considerably from the formal statement of objectives. Formal statements of intent must be peeled away in order to arrive at the real motivation behind a project. The fact that this motivation may differ from CIDA’s does not necessarily mean that the activity should be cancelled. However, such knowledge can be used to focus on a more realistic set of activities and objectives that are mutually appealing to both partners. Consequently the project is more likely to achieve its desired results. Aside from “front loading” the project cycle, by investing considerable time and effort in analysing the motives behind an initial request, the complexities of regional efforts argue for an initially modest effort focusing on a small set of activities that can be implemented in a relatively short period. The experience and insights obtained from this pilot effort can then be put to good use in rolling out the project in successive phases.

e) *Sound Practices*

Among our projects, we did come across one that may warrant in-depth study by the performance review as a possible model for developing capacities – in Canada as well as recipient countries – in trade policy. We refer to the support provided by the Centre for Trade Policy and Law of the Carleton University and the University of Ottawa to assist Russia’s entry into the WTO. The program’s more attractive features include:

- The timely delivery of high quality technical support
- The deepening of linkages, beyond government, with non-government agencies/institutions
- Establishment of a viable Russian counterpart and the progressive transfer of functions to it
- Innovative use of information technologies
- Progressive adaptation of links to changing needs and interests on both sides
- Development of Canadian capacities

We hypothesise that a major factor contributing to the success of this project has been the *responsive approach* to project design and implementation. Others were the excellence of the

Canadian executing agency, namely its knowledge of the topic and area, as well as its network of resource persons internationally and in Canada.

f) *Proactive v. Responsive Approach to Programming*

Our project typology distinguishes among projects in the way they have been designed and implemented. Our principal observations should be treated as working hypotheses by the performance review.

Among the perceived advantages of “responsive” projects are:

- A greater likelihood of obtaining a qualified executing agency since the proponent of the project is usually well acquainted with the issue or country in question;
- A greater likelihood that the executing agency will choose the right local partners with mutually reinforcing interests;
- Stronger incentives to succeed since both the project proponent and recipient are contributing resources and are also more exposed in the event of failure; and
- A lower level of risk since a less cumbersome approval process allows CIDA to entertain smaller scale projects.

Responsive projects also have drawbacks:

- At the firm level, they may not be forthcoming in very difficult but needy circumstances, e.g. in Sub-Saharan Africa or in economically uncertain situations, e.g. Russia; and
- They are not appropriate for dealing with major, longer term processes of institutional and policy reform.

To this list can undoubtedly be added others identified by the parallel assessments of private sector development.

g) *Treatment of Risk*

Our assessment of the way risk is treated in the design and monitoring of projects has been informed by the Framework of Results and Key Success Factors and the draft discussion paper on risk management issued very recently by the Performance Review Branch. Our own analysis reveals that risk is often confused with “assumptions”. Indeed this confusion is understandable since the log frame lumps risks and assumptions together in the same column. In practice, the two are quite different.

Not yet considered in project appraisal is a *weighting* of risks. It will be a function of two factors. The first is the probability of occurrence of the risk in question. The second is the likely impact of the risk on project outcomes.

An important finding of our analysis is that the most effective risk mitigating measures are those taken prior to the start of the project. Such *ex ante*, before the fact, measures would include a focused attempt to comprehend the issues prompting the project along with their attendant risks; a systematic weighting of different categories of risk, and a gradual approach to CIDA involvement, typically through a pilot project, where there is a risk with potentially far reaching consequence for the project.

Drawing on our project sample, we have attempted to gauge how our project typology might be used to anticipate the degree of risk in initiatives concerned with economic integration.

- Our analysis suggests that regional projects will tend to be the riskiest since they often feature disparate partners with differing aims and agenda. Conversely global projects entail the least risk since CIDA will typically work through an international agency along with other partners. Our analysis points to high risk among sector projects since their success is usually contingent on other developments e.g. in world markets or complementary investments.
- In terms of type of integration, projects focusing on trade, especially in goods, will tend to be less risky since the key parameters can usually be identified. Direct investment is often perceived as riskiest, since the investor subsequently is vulnerable to changes in local conditions. Operationally lines of credit and debt relief are not especially risky, although achievement of their stated aims can depend on other longer term factors.
- In our view responsive projects will be less risky because of their generally smaller scale and time horizon, the limit placed on CIDA's own commitment, and the likely prior knowledge of the Canadian partner of local conditions as well as direct commitment to a successful outcome.

These considerations are reflected in the following representation of risk according to our project typology.

Typology	Degree of Risk					
	Low				High	
Level of intervention	Global		National		Sector	
Type of intervention	Trade in Services	Trade in Goods	Lines of Credit	Debt relief	Portfolio Investment	Direct Investment
Programming and Design	Responsive			Proactive		

Section 5 sets out our findings with respect to major issues that we were requested to address in our terms of reference.

The International Agenda

The global agenda comprises issues that will exercise a far reaching influence over international development and, within it, the specific role of AID. At present, however, CIDA's involvement in such issues is defined, or perhaps – more accurately put – confined to those relating to development of the private sector. Likewise, it has focused principally on trade even though economic integration encompasses issues possibly of far greater importance, in future, to the welfare of developing countries. We have also concluded that improved knowledge of the issues confronting developing and transitional economies are central to advancing Canada's own interests in the WTO. Among the salient factors will be an erosion in Canada's current status in the WTO due to the entry of many new members from this group; an inevitable expansion of the negotiating agenda to accommodate their interests; a cross linking of these issues with those of more immediate interest to Canada; and the likely need to accommodate, in the short term, some of the costs of liberalisation, especially in the poorest countries. All of these issues should be examined during the Performance Review in order to consider whether CIDA should continue to qualify its support for economic integration purely in terms of private sector development.

The CIDA Agenda

The following observations are pertinent to CIDA's Policy on Private Sector Development, which was still in draft form at the time of our assessment.

Poverty Reduction: There is no single unambiguous relationship between the various technological, economic, and political trends lumped under the sobriquet of “globalisation” and their likely impact on inequities, in income and well being, among and within regions. Some of them, in particular electronic commerce, should comprise a major opportunity for improving incomes and increasing employment, and therefore warrant much closer attention than has been the case to date.

Capital Flows: At present, CIDA plays a minor role in determining Canada's position toward restructuring international financial architecture. Whether and how this architecture is redesigned will necessarily shape international development in future, both globally and in specific countries and regions. What role CIDA might play in articulating Canadian policy, e.g. in providing a different perspective on the needs and interests of different “players” in the developing world, should be considered by the performance review.

Environment: The case for major CIDA involvement in various facets of sustainable development, ranging from the establishment of guidelines for industrial projects to investment in knowledge, skills and training seems fairly straightforward. Less apparent, and yet warranting further study during the performance review is the application of country and sector specific

insights and practices to Canada's position in the WTO and other fora. We return to this question in our discussion of Canadian capacities.

Gender: There is no unambiguous causal linkage between the well being of women and closer integration of national economies in global movements of goods, services, knowledge and capital. In developing Canadian positions in various fora, CIDA could conceivably contribute a valuable perspective by sponsoring rigorous, in-depth analyses of the linkages, direct and indirect, between liberalisation of trade, services and capital movements, and their potential impact on women's incomes and opportunities.

Competition Policy: CIDA should anticipate the need to contribute to the formulation of Canada's position, with particular reference to the likely consequences to developing country economies.

Development Transfer Payments: Debt relief has very far reaching implications for CIDA, both with respect to the disposition of its resources on an Agency wide basis, as well as the programming of projects within specific sectors and countries. Our own review, which has drawn on documentation, interviews, and our sample of projects, found that inter-departmental exchanges are still largely informal. Among the still to be resolved issues are the assignment of primary responsibility for debt relief policy *and* its financing; and its implications for CIDA programming in specific sectors and countries. These concerns warrant further scrutiny during the performance review.

Programming at the Regional Level

The Underlying Rationale: Based on our own analysis, we conclude that insufficient attention has been paid, at the project formulation stage, to the principal justification for a regional approach. In effect, what is often put forward as the principal rationale for a particular project is belied by the underlying motives and assumptions. Closer scrutiny of these will yield a more realistic view of the project's likely output, principal risks, and likelihood of success.

Scope for CIDA Programming: A key issue for CIDA – and by inference for those concerned with regional programming – is whether the Agency has the capacity, either in house or through ready access to external expertise, needed to fulfil this broader mandate *in those regional groupings where Canadian membership or active Canadian participation is highly unlikely.*

Investing in Canadian Capacities

The Rationale: The rationale for nurturing Canadian capacities is a powerful one. However, the performance review should address the broader question of burden sharing among government departments since there exists an asymmetry between mandate and resources. CIDA's role in trade and economic integration is currently narrowly defined, insofar as it has been subordinated to the promotion of private sector development. Other departments exercise a much broader mandate with potentially major consequences for CIDA priorities and programming. However, CIDA possesses considerable more resources than these other departments for direct investment in Canadian capacities. A key issue, for the Performance Review, is how best to resolve these asymmetries, with particular reference to trade and economic integration.

Forms of Support: One very important issue is the appropriate balance between core support and the various types of program grants. Providing guidelines on how best to achieve a judicious balance between the two would be a useful issue for the Performance Review to pursue. Co-ordinating direct CIDA support for academic institutions and the need for investment in Canadian capacities to analyse policies and programs should also be considered by the Performance Review. Finally, it should examine what topics warrant longer term support through networks of excellence, the various forms such support might take, and how best to select network managers.

Strengthening Capacities in Developing Countries

The Performance Review should focus on the following issues in determining ways of raising the returns to CIDA investment in local capacities: cost recovery; the efficacy of a gradualist approach; an appropriate use of information technology to consolidate initial efforts; and the importance of professional motivations in ensuring that the investment is sustained and used. This combination of conditions is most likely to occur with responsive programming.

Attachment 3 contains a selective survey of Canadian resources expert in economic integration. These are grouped and discussed under three principal headings: government bodies; private associations; and think tanks. Especially useful are their web sites for obtaining additional information about or from them.

Attachment 4 contains similar information concerning international networks (of which the Canadian entities are members). These centres of expertise are grouped under two headings: official agencies and think tanks. Also supplied are their electronic (web site) addresses.

The principal audiences for both attachments are those conducting the performance review and CIDA staff involved in policy development or program management relating to trade and economic integration.

As stipulated in our terms of reference our “References” cite key documents on specific issues raised in the report. However, such documents date quickly. Hence we also list some of the principal websites from which readers can obtain further information concerning international trends and negotiations, as well as policy analysis and in-depth research.