

Public Disclosure Authorized



The IFC Review of Private Investment in Developing Countries

# Impact

Spring 1999

Vol. 3

23476

Public Disclosure Authorized



# Corruption

**IFC**

IFC is a member of the World Bank Group supporting private sector development in member countries through investment, advisory services, and technical assistance.

**International Finance Corporation**  
2121 Pennsylvania Avenue, NW  
Washington, DC 20433 USA  
www.ifc.org

**Editor**  
Rob Wright

**Design**  
Patricia Hord.Graphik Design



The IFC Review of Private Investment in Developing Countries

# Impact

Spring 1999 Vol. 3, No. 2

## In this issue

1 *Caspian Sea oil; trade finance in Korea.*

### Features

**2 The Hell of Corruption**  
*Those clever devils who said corruption wasn't all that bad for developing countries were wrong — really wrong. It is deadly for the private sector. Successfully fighting it, journalist Philip Segal writes, helped put Hong Kong and Singapore in business.*



**8 Just What the Doctor Ordered**  
*Private sector health care is making a big contribution around the developing world. IFC is there to help.*

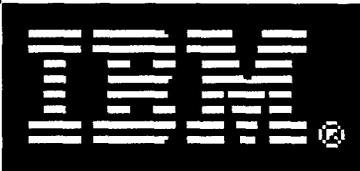


### Financial Markets

**14 Echoes of a Bank**  
*Bringing first-class financial services to West Africa.*

### Client Perspectives

**18 Louis V. Gerstner**  
*Chairman & CEO, IBM Corporation*



### BrainWaves

**22 Francis Fukuyama**  
*Think globally, write interestingly.*

Cover and pp. 3-5 illustrations: The Image Bank  
All references to dollars are U.S. dollars unless otherwise indicated.

**WRITE US!**

Fax: 202-974-4384

E-mail: [Impact@ifc.org](mailto:Impact@ifc.org)

## Oil

## Into the Caspian

The Caspian Sea's oil reserves are considered to be at least as large as those in the North Sea that currently supply about 8% of the world's oil. But they were barely touched during the Soviet era, and the surrounding countries remain some of the poorest in the region. To help them move forward, IFC and the European Bank for Reconstruction and Development are together lending \$400 million to companies developing the Chirag oil field in the Caspian Sea off Azerbaijan. It is the first stage of a planned \$10 billion, 4 billion-barrel mega-project that is expected to become one of the largest private investments in the former Soviet Union.

The loans to BP Amoco, Exxon, Unocal, Lukoil (Russia), and Petrolleri (Turkey) have multiple goals. They will be used not only to refurbish existing offshore platforms but also drill new wells and construct undersea pipelines in the Caspian, new terminals, and new storage facilities in both Azerbaijan and Georgia. The loans will also finance completion of two existing onshore oil pipelines running from Baku across Russia and Georgia for export from the Black Sea ports of Novorossiysk and Supsa. In Azerbaijan, the project is expected to start an oil boom whose tax revenues will increase the national budget by 40% over the next 11 years. The related pipeline development should also help Georgia attract more foreign investment than it has received since independence in 1991.

But why continue with the effort at a time of depressed oil prices, when many companies are pulling out of the Caspian? "We knew when we started this project that the short-term fall in oil prices would have an impact, but both IFC and EBRD still view it as a landmark for the region," said IFC's Dimitris Tsitsiragos. "The companies involved view this as a 30-40 year investment. We want this project to serve as a model for future financing in this region. Without the involvement of IFC and EBRD, I don't think any oil company would have been willing to commit funds there."

— Linda McCormick

## Asia

## Pieces of the Puzzle

IFC is back in the wholesale lending business in South Korea, teaming with top US, German, and Japanese commercial banks on new trade finance projects worth a combined \$250 million. The efforts supply one piece of a complicated, still fragile comeback puzzle in the world's eleventh largest economy. In each case, the model being used also has potential applications for re-igniting trade flows elsewhere in Asia.

The first move came in June 1998, when IFC agreed to establish a \$100 million trade enhancement facility in cooperation with Japan's Sumitomo Bank. Six months later IFC announced a similar agreement with Bank of America (BoA), with both deals aimed at reviving the export trade that has long been the main engine of Korean growth. In each case IFC is guaranteeing 40% of the foreign bank's exposure up to \$100 million, thus helping it provide selected Korean financial institutions with the letters of credit, confirmations, and bankers' acceptances local companies need to purchase the imported capital goods and raw materials demanded by Korean exporters. Such financing declined by 36% between 1997 and 1998, when many foreign lenders cut their ties to Korea's commercial banks, stifling the production of goods for export.

Almost bankrupt in December 1997, Korea is now showing signs of life, with economic growth expected to be positive this year. The stock market is way up, interest rates are way down, and Korean sovereign debt has regained investment grade status. But all is not rosy — unemployment is still growing and expected to get worse as the large conglomerates known as *chaebol* carry out the reforms that could mean the difference between long-term economic recovery and ruin.

President Kim Dae-jung has vowed to rein in the *chaebol*, putting in place laws and policies to try to force them to cut their debt loads sharply. Staying the course of reform will likely make the difference over the long haul. US Deputy Treasury Secretary Lawrence Summers has warned South Korean government and business leaders against complacency, saying, "There is an important difference between recovering from a heart attack and changing your lifestyle to be sure you never have another one."

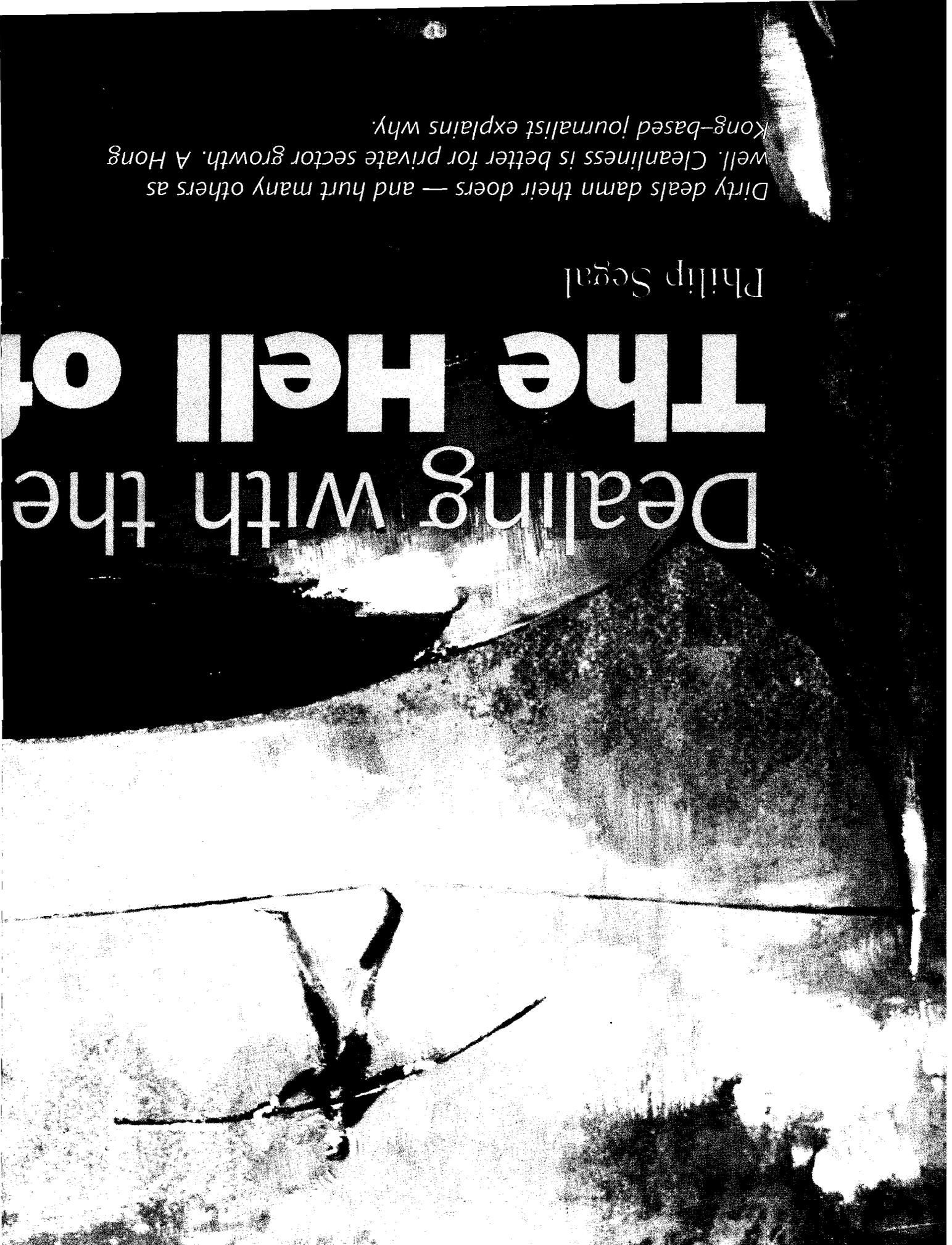
In another show of support, IFC will also be guaranteeing \$50 million of the 'forfeiting' transactions in Korea of Germany's West Merchant Bank. This form of trade finance allows firms exporting into Korea to receive payment at a discount without risk from Korean buyers. By its involvement IFC is encouraging West Merchant Bank to undertake a larger volume of transactions than it would on its own.

— Linda McCormick

*Dirty deals damn their doers — and hurt many others as well. Cleanliness is better for private sector growth. A Hong Kong-based journalist explains why.*

Philip Segal

# Dealing with the Hell of





Devil

**Corruption**

**T**hese are not good days for the old argument, widely popular even five years ago, that a little corruption in developing countries is probably good for greasing the wheels of commerce.

Of all the testing grounds for this theory, often associated with academic thinkers such as Nathaniel Leff and Francis Lui, Asia was supposed to be the most fertile. Advocates said it showed that "good corruption" could benefit a country, and that doing business with an emphasis on connections worked just as well as

or better than the openness, accountability, and competitive bidding practiced by leading Western companies.

Now, with parts of Asia beginning to recover from one of the fastest destructions of wealth seen anywhere in the world outside of wartime, many in the

region are reconsidering the merits of this argument, just as academics are concluding that corruption is not such a great economic lubricant after all.

Tunku Abdul Aziz, a former Malaysian central bank official and now a board member of Transparency International, a global nongovernmental organization set up to expose and battle corruption, maintains that the old argument excusing graft "proved to be nothing more than an elaborate prop for what was basically a morally indefensible and decadent heritage." Attempts to explain corruption away on cultural terms were "grounded in complete and utter disdain for transparency and accountability in those matters that have public interest implications," Aziz said in a recent speech.

Even in countries closer in spirit to the West that appeared to be adopting free-market reforms, the evidence is that competitiveness and corruption do not mix. Take the unwary foreign investors who thought Western capital would forever avert its eyes from Russia's failings and thus help keep the country's nuclear arsenal safely at bay. They have learned a painful lesson. "The best and the brightest on Wall Street lost billions betting that Russia was too nuclear to fail," US House Banking Committee Chairman Jim Leach said at IFC in December. "What they didn't realize was that it was too corrupt to succeed."

## Good Examples

In the new global financial environment, the idea that corruption makes the business climate more attractive is fast losing favor with academics and businesses alike. There is much to learn in this regard from Asia's own two great success stories that have proved that theory wrong: Hong Kong and Singapore.

The message of their successful campaigns to eliminate corruption is clear: zero tolerance. Once corruption takes hold, these economies have found, it can rage out of control and threaten the entire fabric of a society, weakening development prospects in a disturbing, dangerous way. Working instead to cut out corruption at the roots brings great benefits: increased investment, more stability, and a greater basis for the high-value, service-oriented economies in which education and income levels rise dramatically.

Look at Hong Kong: During the 20 years that elapsed from the time that it got serious about fighting corruption until the onset of the Asian financial crisis, it changed from a poor developing economy to a sophisticated first-world financial center. Now home to Asia's largest stock market outside Japan, businesses perceive Hong Kong to be even less corrupt than the United States, according to Transparency International's 1998 Corruption Perceptions Index.

In his 1988 book, *Controlling Corruption*, one of the first to tackle the issue head-on, author Robert Klitgaard called Hong Kong's Independent Commission Against Corruption (ICAC) "probably the largest and most famous anticorruption agency in the developing world." That agency's former head, Peter Williams, well remembers Hong Kong's bad old days. He had first-hand experience of corruption entrenched at the highest levels of power. "The result is virtually the setting-up of an alternative, illicit form of government," Williams wrote. "The officials impose their own illegal rules of conduct on the public, and the lawful rules of the government for which they work are blatantly ignored. When corruption reaches this stage, the situation is certainly grave, and inevitably produces a crisis in which either drastic countermeasures are imposed or society lurches further downwards."

Who would want to invest under those conditions? Not many, according to figures assembled in a 1996 World Bank study. These found that countries with high but "predictable" levels of corruption had a gross investment-to-GDP ratio of 19.5%. For countries with low predictability but a still high level of corruption, the ratio was just 12.3%. Unsurprisingly, countries with the highest ratio were those with low corruption and high predictability (28.5%).

"In our research on emerging markets, corruption is the single most important factor contributing to political instability and economic decline," adds Marvin Zonis of the University of Chicago's Graduate School of Business. "Corruption is a misallocation of capital, where resources are directed for noneconomic purposes. Corruption inevitably leads to political decline."

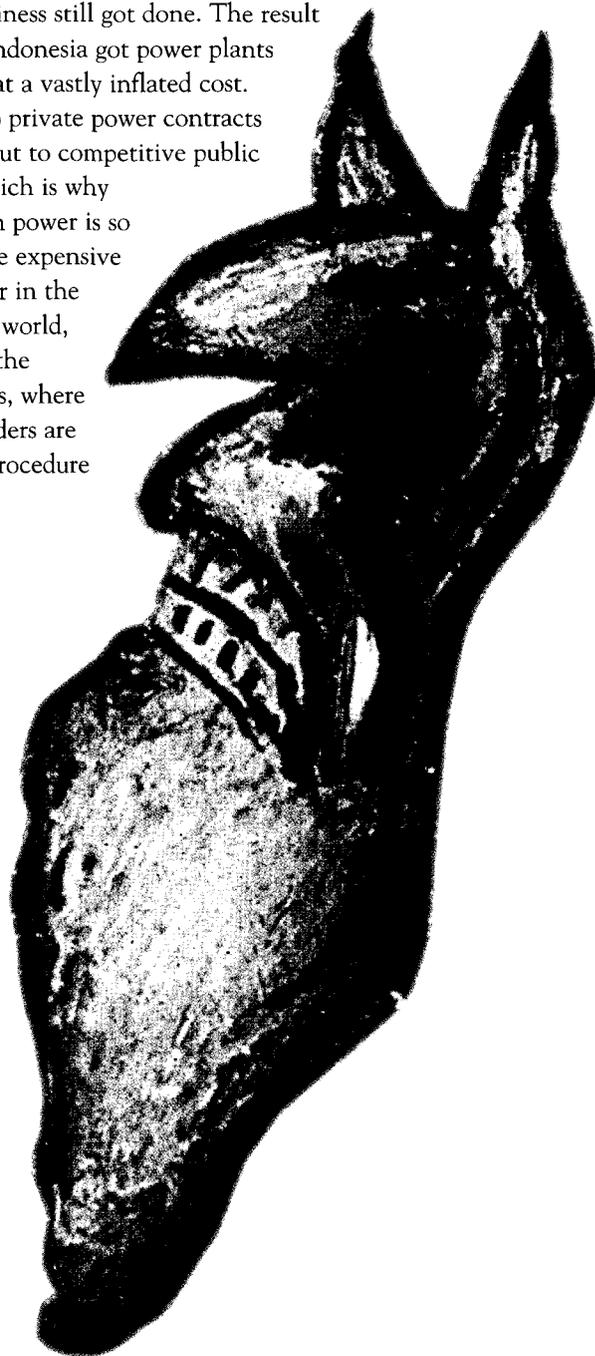
## A Poor Excuse

Corruption also eventually inspires people to take to the streets. Why? Not only because it can be bad for the long-term stability of political systems or companies. Those it hurts the most and the soonest are not the rich and powerful. They are the hapless consumers in the country in question — especially the poor, who suffer the most when prices of essential goods rise.

George Moody-Stuart, a long-time consultant in African agriculture and the author of the 1994 book *Grand Corruption*, argues that "once the possibility of personal gain becomes a factor, it rapidly becomes the only factor that matters, pushing aside cost, quality, delivery, and other legitimate considerations in the awarding of contracts. The result is that the wrong suppliers and/or contractors are selected. And the wrong goods are purchased." Why else, he asked, would it be the case that "half the roads in Africa break up after two years?"

Or look at the Indonesian power industry, which operated in what was supposed to be a model of the "good" kind of corrup-

tion: Companies cut in a member or friend of the Suharto family, but business still got done. The result was that Indonesia got power plants built, but at a vastly inflated cost. Almost no private power contracts were put out to competitive public tender, which is why Indonesian power is so much more expensive than power in the rest of the world, including the Philippines, where public tenders are standard procedure now.



Moreover, one Indonesian power joint venture between US sponsors Mission Energy and General Electric was obliged as part of its contract to buy its boilers from a foreign company for which one of President Suharto's sons was the local agent. The increased cost to the project, passed on to the consumer, was \$20 million, the *Wall Street Journal* reported.

Worse still for the companies involved, cronyism also blocked the growth of a healthy financial sector. In the words of Indonesia's former environment minister Emil Salim, "inadequate enforcement of the Central Bank regulations has created

an environment where rules covering intra-group lending, loan concentration, and creditworthiness criteria were violated with impunity.”

At times, however, corrupt and noncorrupt industries can exist side by side. In Taiwan, China, the big economic success story has been the electronics industry. In contrast, the more traditional industries such as chemicals or steel trundle on but do not thrive in the rest of the world the way electronics do. Why the difference?

Take Taiwanese technology companies such as Acer, Taiwan Semiconductor, and Quanta, giants of world electronics that actually make much of what Dell or Compaq repackage. They tend to prosper without having a chairman who is related to someone in the government, getting sweetheart credit deals from state banks, or padding their balance sheets with overvalued, empty office property in some half-finished industrial park. Without such advantages, they still make capital grow, reporting returns on equity of as much as 60%.

“These are strategic industries,” said Jeffrey Toder, head of research at investment bank Jardine Fleming in Taipei. But just as important, they are also industries in which fair competition is allowed to proceed without the distorting hand of the state or corrupt officials.

## Islands Apart

Any place where corruption thrives has much to learn from Hong Kong and Singapore. Once among the world’s most corrupt places, they have become two of its cleaner business centers. The main reasons these two have succeeded where so many others have failed are that their fight against corruption began at the top and, just as critical, was removed from the hands of the police. Both have rules that mandate transparency in tendering and other procedures and clean law enforcement to make sure they are followed.

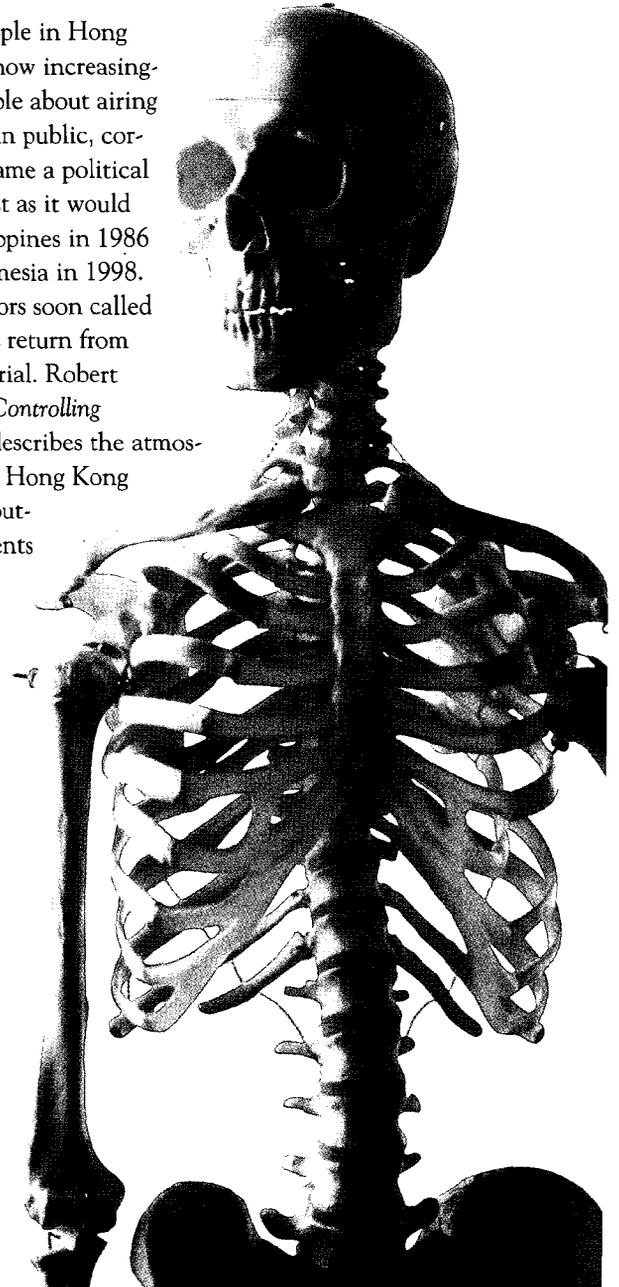
Despite overcrowding and an almost complete lack of natural resources (aside from its glorious harbor), Hong Kong has emerged as one of the world’s great economic development success stories, and not by coincidence: It is hard to name a major financial center in which courts are unduly slow or unreliable and where commercial crime goes unpunished. Hong Kong saw that to continue developing economically it needed to move from manufacturing to services, and that to do so, rooting out corruption would be essential. Today manufacturing accounts for just 7% of its GDP, which is dominated instead by services such as banking, insurance, and real estate.

## Looking for Mr. Godber

For years, though, this was a place where the great majority of the police took bribes while its British colonial governors appeared not to mind. By 1973, however, though still primarily a manufacturing center and not in any major way the kind of financial center it is today, Hong Kong was no longer simply an area where penniless immigrants from the Chinese mainland shoved up against a handful of wealthy, rapacious expatriate traders. The level of corruption its people would tolerate had been exceeded.

The turning point in the corruption fight came in June of that year, when an internal investigation revealed that a senior police officer, Peter Godber, had managed to skim off HK\$4.3 million (today US\$550,000), or about six times his total net salary during his 20 years of police service. Despite being on the exit watch list at the airport, Godber was able to board a plane to London, where he hoped to escape the arm of Hong Kong’s law.

Because people in Hong Kong were now increasingly comfortable about airing their views in public, corruption became a political problem, just as it would in the Philippines in 1986 and in Indonesia in 1998. Demonstrators soon called for Godber’s return from Britain for trial. Robert Klitgaard’s *Controlling Corruption* describes the atmosphere: “The Hong Kong public was outraged. Students rallied to



demand his return for trial. Radical elements accused the government of complicity in letting the 'big fish' go free." The implications were obvious. If Godber had been allowed to escape, the administration must be rotten right up to the top.

This was all that Murray MacLehose, the new, unusually activist governor appointed in 1972, needed to snap into action. Four months after Godber's disappearance, MacLehose formed the Independent Commission Against Corruption, took it out of the hands of the police, and had it report directly to him. The new organization had tremendous powers of search and seizure (some of which are now subject to court orders), and anyone disclosing that an investigation by the ICAC was under way was liable to prosecution under the anticorruption statutes of the day. In 1975 Godber was apprehended in Britain, returned to Hong Kong, and jailed. Eventually the ICAC would arrest 260 other Hong Kong policemen, and a long, sordid chapter in local history came to a much-deserved end. With its proximity to a fast-changing China and sound infrastructure supplemented by a cleaned-up business environment, Hong Kong soon saw its economy surge.

Hong Kong will need to maintain its reputation for taking on anyone suspected of corruption if its antibribery effort is to remain effective in the eyes of local residents. But its recent decision not to prosecute a controversial and politically well-connected media tycoon, Sally Aw, partly on the grounds that many people would have lost their jobs had she been convicted, has already prompted legal scholars and legislators to ask whether Hong Kong now has one law for the rich and one for everyone else.

## Something to Sing About

Singapore's story is similar, if less dramatic. Its anticorruption agency, the Corrupt Practices Investigation Board (CPIB), operates apart from the police and is based in the prime minister's office. Founded but dormant under British colonial rule, it only started gaining power as an effective anticorruption tool in the 1960s and 1970s. But it has a

critical difference from its

Hong Kong counterpart:

Singapore asks its citizens to

trust that its anticorruption agency is doing a good job and does not communicate with the public. The CPIB prefers secrecy, whereas Hong Kong's ICAC has a community relations department and depends heavily on public cooperation in the form of tips to pursue investi-

gations. Hong Kong's ICAC also has several oversight committees that can and do call for changes in the way the commission operates, although these all serve at the pleasure of one person — the chief executive of Hong Kong.

Like Hong Kong, though, Singapore has thrived as a haven for businesses looking for a place in which contracts can be enforced, and where the police do not have their hands out for bribes. Companies have flocked there to make electronics, to trade currency and equity futures, and to sell insurance, enabling Singapore to mount a serious challenge to Hong Kong for the title of Asia's premier financial center outside Japan. And, as anywhere that has successfully battled corruption, the fight continues. In 1996, Singapore imposed a five-year ban on five foreign companies, including Pirelli and Siemens, after they were alleged to have bribed a government telecommunications official.

But as successful as these two Asian examples have been, the great power that Hong Kong's and Singapore's anticorruption agencies have means they are not a model for everyone, according to Transparency International's Nihal Jayawickrama, in a paper presented at an anticorruption conference last year.

Although "Hong Kong did not have a democratically elected government," he wrote, "this apparent autocracy was balanced by an elected legislature, an independent judiciary, a vibrant press and an active and articulate civil society." In the case of Singapore, though, Jayawickrama saw even more risk in imitation: "Singapore is a city-state administered by a relatively authoritarian leadership, intolerant of dissent from any quarter. It is extremely vulnerable in that its strength lies in a single 'pillar' — the financial integrity and supreme professionalism of its leadership."

## Enter the OECD

As admirable as Hong Kong and Singapore have been in tackling bribery at home, like most of the world's countries they have been lax in limiting what their companies do abroad. Since 1977, with the exception of the US, the general rule was that acts of corruption that were illegal at home were permissible outside a country's borders. That has now changed with the February 1999 enactment of an international framework for outlawing the bribery of foreign officials signed by the 29 country members of the Organization for Economic Cooperation and Development. How active the signing countries will become in using it to prosecute their bribers is an open question. Many suspect they will be fairly slow to act.

A telling precedent may come from the US Foreign Corrupt Practices Act, which has been in place since 1977. Some US companies at first resented it, just as some in Europe resented

*Continued on page 25*



# Just What the Doctor Ordered

## Prescriptions for Private Health Care in Developing Countries

Sally Gelston, *IFC Corporate Relations Unit*

**K**enyan shopkeepers Aloysius and Josephine Mukami Maina Warui are glad they joined their managed health care organization when they did. A mere six months after the couple had enrolled in AAR Health Services, thieves brutally attacked them at home in a robbery attempt, leaving Aloysius unconscious and near death with a concussion and fractured skull.

His adult son ran to the nearest pay phone to summon help from AAR, 100 kilometers away in Nairobi. Within an hour an ambulance arrived with a doctor and two nurses inside. "They saved his life because they came immediately and started treatment," said his wife, who suffered less serious head wounds in the attack.

Residents of their village, Muranga, were impressed by the unexpectedly quick response of AAR's ambulance and subsequent complete payment of Aloysius' month-long hospital stay. "They kept waiting for the bill to come, because insurance companies here typically do not pay. When the bill never arrived, they decided to join AAR, too," Mrs. Maina Warui said.

Word spread quickly. Two years later, some 50 families in and around Muranga have joined AAR as a result of the Maina Waruis' experience. Their choice mirrors a shift occurring in much of the developing world, where people are opting for new private health care offerings that improve on the shortcomings of older systems, whether private or public. In many cases, cash-strapped governments are turning to the private sector to provide a higher standard of health care, thus easing the burden on overstretched public facilities, and the changes are often immediately apparent.

## The Challenge

Increasing access to quality medical care is one of the greatest challenges in development. In recognition of the potential private contribution to this sector, IFC has financed 16 health-related projects in the past two and a half years. Since mid-1996, it has approved transactions in Argentina, Brazil, Costa Rica, Kenya, Mexico, Slovakia, South Africa, Sri Lanka, Turkey, West Bank and Gaza, and Zimbabwe. The combined project costs total \$343 million, of which IFC agreed to provide \$135.3 million from its own resources and those of the financing partners it attracts.

Privately financed systems such as these can make a crucial contribution, sometimes even the difference between life and death, by increasing the range of products available in the local health care market. But to truly benefit a local economy, private care must be affordable to a large segment of the community.

Access can take widely different forms, depending on a country's level of development and the insurance systems it has in place, as shown by the three IFC-supported projects featured in this article. While private systems are usually more likely to reach the middle and working class than the poorest elements of a society, their repercussions often reach far and wide.

### Mexico: A Lifesaver

Jaime Creel is a business leader in the northern Mexican city of Chihuahua. When he joined 14 other local investors in backing construction of a new CIMA hospital there, he viewed it as a civic duty that would boost quality of life and help attract foreign investors to his hometown. Like the Maina Waruis in Kenya, he never imagined the benefits would hit so close to home so quickly.

Only one month after his hospital opened, a tragic auto accident outside of town killed Creel's sister and left his 26-year-old niece Myriam with a spinal fracture. Surgeons at the new hospital succeeded in stabilizing her after hours of surgery and 25 half-liters of blood. Her back injury was complicated by the



**Mexicare:** IFC-supported CIMA helps in Hermosillo and other Mexican cities.

presence of metal rods used to correct the scoliosis from which she had long suffered. The collision bent these rods, puncturing a lung and causing other serious injuries. She was airlifted to Houston, where her longtime doctors had high praise for the emergency care she had received in Mexico. Although the accident left her paralyzed below the waist, Creel is convinced his niece would not have survived without the higher caliber of care CIMA brought to Chihuahua.

CIMA — Centro Internacional de Medicina — is a private health care system developed by Dallas-based International Hospital

## Hospitals

**Name:** Centro Internacional de Medicina (CIMA)

**Description:** Chain of high-quality private hospitals in Mexico and Central America affiliated with Baylor University Medical Center of Dallas, Texas

**Sponsors:** International Hospital Corp. (US); IFC; local investors in each market

**Cost:** \$128 million

**IFC Role:** Provided \$20 million long-term loans, equity, and quasi-equity; advised sponsors on financial management issues

Corporation (IHC). IFC has recently supported CIMA with a \$20 million investment. In Mexico, it operates a private hospital in Hermosillo as well as one in Chihuahua. The company is also building others in Puebla, Mexico, and in San Jose, Costa Rica.

Current plans envision a total of 10 CIMA health centers in Latin America with a combined 900 beds. Each will be built with support from local investors, usually prominent doctors and business people enlisted to ensure community support. Before opening, the hospitals enroll their doctors and lead administrators in a program with Baylor University Medical Center of Dallas, where the training focuses on strengthening health care and administration practices.

"We need to improve our medical organization," Creel acknowledged. "To do so, we hope to increase our interaction with Baylor. Our goal is to become an international-standard hospital, not just the best hospital in Chihuahua."

"We're changing the paradigm of how medicine is practiced in Mexico," added Lawrence Meagher, IHC's president and CEO. In his view, "the presence of IFC has been critical" to the project, which he calls an example of "what IFC is all about: supporting sectors that are important not just from an economic perspective but also from a social perspective."

Meagher said IFC's financial projections revealed weaknesses in his own initial assumptions and models, and helped CIMA rescale its growth strategy and reconsider its implementation time frame. An IFC architect, Geoffrey Willing, also visited the construction site in Costa Rica and provided valuable advice. "We have forged a very positive working relationship and partnership with IFC," Meagher said.

Hermosillo, Chihuahua, and Puebla are all experiencing rapid economic growth based mainly on labor-intensive manufacturing and "maquiladora" light assembly industries. The CIMA hospitals will strengthen the economic position of these cities by helping them attract and retain investors and skilled workers who demand quality health care services before relocating. The hospital in Hermosillo, for example, has the only cardiac catheterization laboratory in northwestern Mexico. Few Mexicans, however, have private health insurance, so choosing a private hospital usually means paying the bill in full. For the time being, CIMA is working with the public health system so that some of its advanced equipment can be offered to low-income patients at a discount. So far, two-thirds of the users of the cardiac catheterization lab have been covered by state assistance. The net result: more Mexicans of modest incomes are getting quality health care at home, rather than seeking it on costly trips to the United States or forgoing it altogether.

## South Africa: **Not for Whites Only**

The advent of majority rule in South Africa has meant increased demand for health care services, particularly from the public sector, with all races now gaining access to previously whites-only hospitals. But "the state of chaos in our public sector and the tremendous lack of funding" meant the government could not afford to build any hospitals or clinics, says Ameen Mohamed, chairman of the new IFC-financed Eerste River Medical Centre. The only such clinic in an area of Cape Town with a population of 400,000, it opened in February, four years after the government asked Mohamed's group to build it in this underserved location. The investors include doctors, lawyers, an accountant, and businessmen, all members of nonwhite ethnic groups that had suffered from discrimination under apartheid.

The \$5 million clinic serves a mostly lower- to middle-class mixed-race population, some of whom live in a formerly segregated township and a shanty town. People there work as teachers, as blue-collar workers in light industry, and at a nearby defense force training base. The highly populated area has grown quickly in recent years, despite the fact that it had no medical facilities within a 25-kilometer radius. To help finance the project, Mohamed's group sold a quarter of the medical center's shares to some 3,000 nearby residents, promising them an eventual 12% return. "What's really been rewarding for us was the excitement we saw when people from the neighborhood realized they could own shares in the hospital," Mohamed said.

The center opened with 80 beds and three operating theaters. Plans call for eventual expansion to 123 beds and four theaters, and the group owns adjacent land to accommodate further growth, if warranted. IFC provided \$1 million for a 20% equity stake in the project, helping the sponsors raise their equity to levels needed at that time to obtain financing from other

### Local Clinic

**Name:** Eerste River Medical Centre, Ltd.

**Description:** \$5 million facility in middle- and working-class section of Cape Town, South Africa; offers general medicine and surgery, obstetrics and gynecology, and pediatrics at levels of quality formerly available only to white population

**Sponsors:** Local investors from "previously disadvantaged" community

**IFC Role:** A founding shareholder with approximately \$1 million investment; attracted other investors

**To the Rescue:** AAR ambulance on the scene in area affected by last year's US Embassy bombing in Nairobi.



sources in South Africa. "Today we can get any amount of funding," Mohamed said.

Before investing, IFC required a feasibility study by an independent doctor from the United Kingdom, whose due diligence confirmed the local sponsors' projections. "That gave us confidence. I have to view the project as an investor," Mohamed said. "The feasibility study cost us \$10,000, but I was glad to have it."

## Kenya: **Better Coverage**

The Maina Waruis' health care provider, AAR, was established in 1984 as an emergency air evacuation service. But as public health care in Kenya has declined, AAR has stepped in to meet the growing demand for primary care services. In a private AAR clinic, Josephine Maina Warui says, "you feel you are wanted and you feel recognized. In the public hospital you are neglected unless you know somebody."

The company has four clinics in Nairobi and its suburbs, one in Mombassa, and a sixth in Kampala, Uganda. It has 65,000 members in Kenya, 70% of whom are covered through their employee benefits programs. The rest are individuals and small business owners such as the Maina Waruis, who pay \$89 to \$361 a year per person out of pocket, depending on the level of care they select. Most AAR clients choose levels that cost \$205 to \$262 a year, a sign of how much they value health care in a country where per capita income is about \$340.

AAR also has 5,000 members in Uganda and aspires to become a regional health care provider throughout East Africa. It has

recently begun expanding into Tanzania, Rwanda, and Ethiopia, and is also looking for opportunities in Mali and Mozambique. "The secret of our long-term success will be going into other places. We will grow from our start as a high-margin, low-volume business to a lower-margin, high-volume business," said Lord Enniskillen, the company's chairman and chief operating officer.

Within Kenya, AAR is seeking to enroll new members in rural areas. AAR also covers the spouses and children of its members who work in Nairobi and have left families behind in their villages. These outlying patients can travel to an AAR clinic by bus, or, in emergencies, in an AAR ambulance. The organization plans to significantly extend its reach to the underserved

## Managed Care

**Name:** AAR Health Services

**Description:** Largest managed health care organization in Kenya, with 65,000 members; also owns five medical clinics in Kenya and one in Uganda

**Sponsors:** Kenya residents who are expatriate Europeans; Acacia Fund; IFC; and AAR senior management

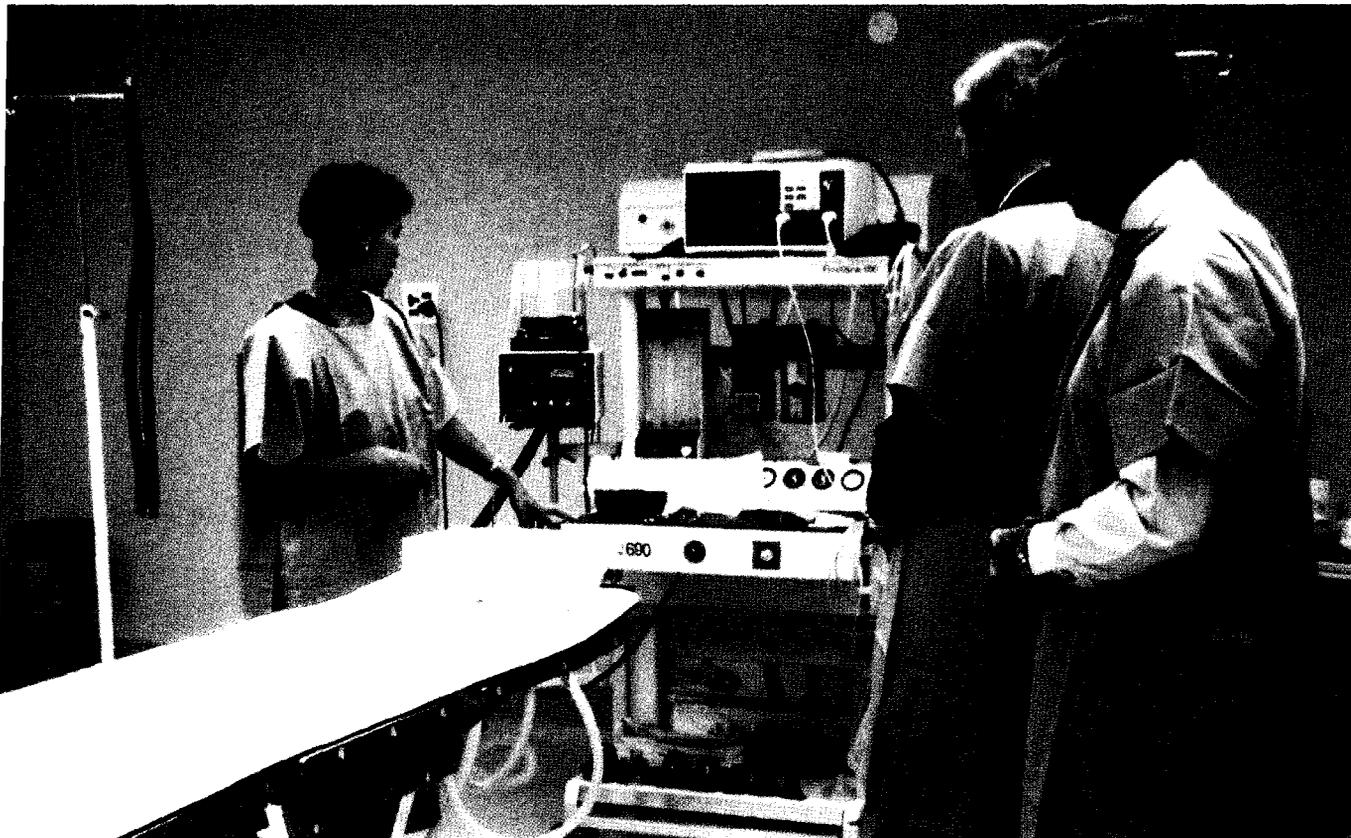
**IFC Role:** Invested \$500,000 equity to support AAR's expansion in Kenya and into other East African countries

rural populations by opening nurse-run outreach clinics, Enniskillen said.

IFC has taken a \$500,000 equity stake in AAR, thus becoming a 5% shareholder. The funding helped AAR expand and obtain rescue vehicles and communications equipment. An added benefit, Enniskillen said, is that surviving IFC's rigorous due diligence process helped his firm gain credibility in the eyes of other potential investors. AAR plans to launch a financing scheme that, with IFC's help, would allow corporate members to spread the current up-front annual fee for membership over 12 monthly payments. Thus more companies could offer the benefit to their employees, he said.

## The Future

IFC plans to broaden its contributions to the health care field. Building on recent experience with projects that raise medical standards, IFC is starting to work with companies whose sole purpose is to boost cost-effectiveness in a country's health system. An example is a Brazilian firm that offers an array of cost-saving services, such as home care to shorten hospital stays. Related areas on the horizon are telemedicine and privatization of public health insurance. Whatever is chosen, the goal will be to help the entrepreneurial energies of the private sector deliver quality health care to more people at an affordable price, thus complementing the role of government in this all-important sector. ■

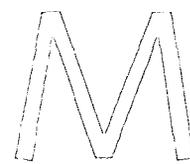


*In the Operating Room: IFC Executive Vice President Peter Woicke and South Africa representative John Pott visit Cape Town's Eerste River Medical Centre.*

# Echoes of a Bank

## *Raising a Region's Standards*

Rob Wright, IFC Corporate Relations Unit

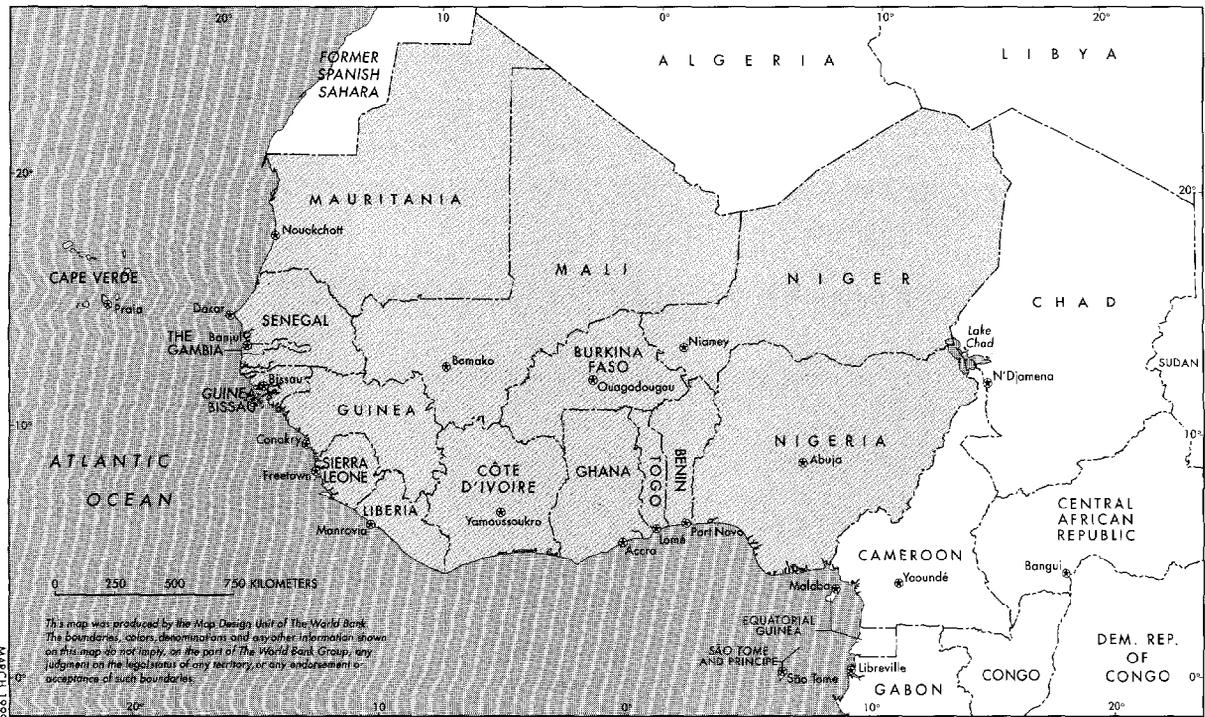


More than 2 million migrant workers from Burkina Faso have moved to Côte d'Ivoire,

seeking jobs that their far poorer country cannot offer. Much of what they earn they send home, where it makes a big difference in family members' daily lives. But even though the two countries share a border, a language, and a currency, until last year it was often impossible to wire money from Abidjan in anything less than two weeks. A sleepy local banking system wouldn't move any faster, making the workers reluctantly settle for bringing the money to relatives by hand whenever they went home.

It was not a great situation. Fortunately, though, things are changing.





**Underbanked:**  
The 16-country Economic Community of West African States region, Ecobank's target market.

Last year saw the opening of the Burkina Faso subsidiary of Ecobank, an African-owned holding company determined to provide better banking than what the region has come to accept. From the outset it has distinguished itself from competitors in Ouagadougou by not closing at lunchtime or on Saturdays and by offering same-day wire transfers from Abidjan. Customers responded well, making the bank profitable in its first year and forcing rivals to match the higher standards once they saw the government give it an award for innovation.

IFC is a founding shareholder in the Burkina Faso bank, having invested about \$300,000 for a 10% stake in 1997. Now it has gone a step further, investing another \$7.5 million in parent Ecobank Transnational Inc. (ETI) to help it bring similar banking improvements throughout the 16-country Economic Community of West African States (ECOWAS) region. The African-owned company wins high marks from both local and foreign banking specialists.

"Ecobank today, with its geographical coverage and integrated structure, truly is the West Africa bank," said Frank Kennedy, CEO of HSBC Equator Bank, a merchant and investment bank focused solely on Sub-Saharan Africa. "It is well positioned to play a leading role in the economic development of West Africa, and demonstrates that regional integration there is driven by the private sector and not necessarily by government."

No matter where in the developing world IFC works with private sector clients, one thing is clear: competition transforms markets. It's a golden rule, in Africa or anywhere else, and one Echo knows well.

## Reaction

"This is not rocket science," says Arnold Ekpe, who left a career with Citibank in 1996 to become Ecobank's CEO. "Once you introduce these kinds of service improvements, the local market tends to react well and you can't go back."

But while profitable today, as recently as 1994 the Ecobank network was in consid-

erable financial difficulty. Founded in Togo with initial shareholder capital of \$33.5 million in 1988, Ecobank lost half that money within six years. A bad loan portfolio, a failed commodity trading joint venture with N.M. Rothschilds, and a disastrous acquisition of the former Chase affiliate in Côte d'Ivoire had all threatened its goal of becoming the only regional bank active in both the French- and the English-speaking countries of ECOWAS. In a last effort to salvage the mission, the board was reconstituted and its profile raised by appointing cofounder and former Togo Chamber of Commerce head Gervais Koffi Djondo as chairman and by attracting other heavyweight directors such as Sam Jonah, head of Ghanaian mining powerhouse Ashanti Goldfields, and Abdoulaye Kone, who served as Côte d'Ivoire's minister of finance for 15 years.

The new board then moved to recruit a new CEO with the vision to turn things around. It chose the Nigerian-born Ekpe, who had just overseen Citibank's entry into the South African corporate finance

# Afromoney

**Name:** Ecobank Transnational Inc.

**Business:** Africa's first locally owned regional bank holding company

**Based in:** Lomé, Togo

**Subsidiaries in:** Benin, Burkina Faso, Côte d'Ivoire, Ghana, Nigeria, Mali, Togo; plans to open in several other West African countries soon

**Founded:** 1988

**Equity:** \$61 million

**Ownership:** Local shareholders and employees (79.4%), ECOWAS Fund (13%), Kingdom Holdings Africa (7.6%); IFC will become a 3.2% shareholder in the bank's holding company upon conversion of a recent \$7.5 million quasi-equity investment, and is also a shareholder in its Burkina Faso subsidiary

**Ethics:** Requires all employees to read and sign an eight-page corporate ethics statement detailing stances on conflicts of interest, fraud, reporting violations, and policy against "knowingly doing business with drug traffickers, money launderers, and other criminals;" also has directors sign a code of conduct prohibiting secret gains from Ecobank transactions and other acts that do not give priority to the interests of "shareholders, employees, and creditors"

**Development Impact:** Introduces top-quality management practices, technology, and customer service into West Africa's locally owned banking sector

and capital markets. His plan of attack: strengthening central management of the country subsidiaries and adopting a viable business plan that could attract new capital from local shareholders and bring in prestigious international investors for the first time. He soon approached IFC, which supported his goals but was a hard sell. It took two years of negotiations, but he finally reached a deal that will bring

integration, dependence on commodities with low prices, civil war in some member countries). Meeting that goal is quite a challenge, and the reason IFC has provided the bank with managerial assistance as well as financing (*see box, p.17*).

## Les Echos

On the wholesale side, Ecobank is targeting letters of credit, cash management,



IFC in as a 3.2% shareholder in the holding company.

"IFC's degree of thoroughness in considering a potential investment was similar to what I was used to at Citibank, but with one key difference," he added. "At big banks like that the process is a little more brutal. They can just decide to withdraw from a country or a transaction all of a sudden because it no longer makes sense for them. I can't see IFC doing that. They are tough, but also very sympathetic to the developing world — willing to walk with us, so to speak."

His bank's mandate is to help meet the demand for first-class corporate and consumer finance in the ECOWAS region, an area that has both its pluses (an "underbanked" population of 206 million and a combined GDP of \$70 billion) and minuses (little tradition of economic

**Cash Call:** Speedy service at Ecobank branch in Benin.

and treasury operations for the large middle market of local and foreign companies untouched by the big French, US, and UK banks interested only in the bluest of blue chips in Africa. In retail, the business involves savings accounts, credit cards, and traveler's checks — not high finance, but something for which there is a great need locally. While it is not the largest player in any of its target markets, the new focus on "basic banking done well," as Ekpe puts it, has led to steady earnings and dividends to shareholders since 1996, with the bank in Ghana the most profitable link in the chain.

More important from a development perspective, though, may be the innovations

# The Human Resource Challenge

Running a first-class multicountry financial services network in Africa requires a strong team with both excellent banking skills and a solid understanding of the business climate in each country of operations. But the local talent pool in finance is thin, and as an African-owned institution, Ecobank is well aware that human resources could be one of its toughest obstacles. Since management and training are in short supply in the ECOWAS region, IFC has introduced Ecobank to the African Management Services Company (AMSCO), which is helping provide both.

Headquartered in Amsterdam, AMSCO was established as a fee-based enterprise in 1989 by IFC, the African Development Bank, the United Nations Development Program, seven European bilateral financial institutions, and 53 private shareholders to provide the management personnel and training

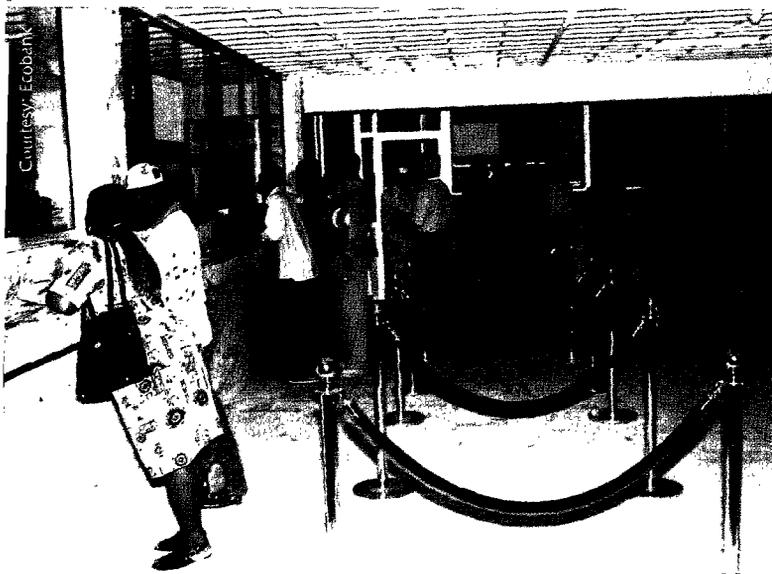
that African companies need to become and remain internationally competitive. It helps improve financial performance by delivering practical training and development customized to the needs of the local senior management team at each client company.

AMSCO has sent several senior managers from European and US banks on contract. They serve at the level of managing director or below in the subsidiaries in Benin, Burkina Faso, Cote d'Ivoire, Nigeria, and Togo, helping raise banking practices to international standards in each case. AMSCO is also facilitating staff training in credit analysis, treasury operations, and other fields through a \$250,000 donor grant that Ecobank matches on a three-to-one basis. The training is done through seminars, workshops, and on-the-job instruction given by specialists from Citibank and other institutions. A limited amount of foreign training is also

offered, either at the INSEAD business school outside Paris or at Harvard University.

Sending staffers overseas, however, is about two-thirds more expensive than what the comparable level of training would cost locally. So Ecobank plans to build the first regional school of banking in West Africa, seeking to upgrade the professional skills and competence of its 1,000 employees and those of other banks in the subregion and beyond. Both IFC and AMSCO have pledged to support the banking school project, with AMSCO already planning to provide a management team to help run it. The school is expected to be launched within 24 months and run on a cost-recovery basis.

— Ken Best



**Lobbying:** Financial services consumers at Ecobank in Togo.

that the group is introducing. It finances more trade between the three largest ECOWAS economies (Ghana, Nigeria, and Côte d'Ivoire) than any other institution, and is the settlement bank of the regional stock exchange in Abidjan that

has slowly emerged in the past two years. The Accra subsidiary introduced money market operations to Ghana and has become the launching pad for a new regional investment bank. The Togo-

based holding company's role is to apply international financial management standards to the whole operation — essential in a part of the world whose indigenously owned banks have often operated without them and allowed highly questionable practices to occur.

"We're not just doing this to make money," Ekpe said. "We're trying to make a difference. For example we have a strict anti-money-laundering policy, and all our employees have to sign onto our code of ethics. We also have very strict internal controls, with each subsidiary undergoing various audits four times a year. If something isn't caught the first time, it will show up later."

Ecobank is present in seven ECOWAS countries now, and ultimately wants to be in all 16 of them. Branches in Senegal

*Continued on page 25*

# Champion of Change

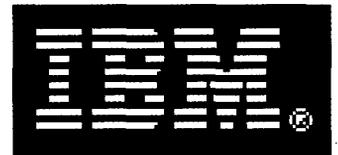
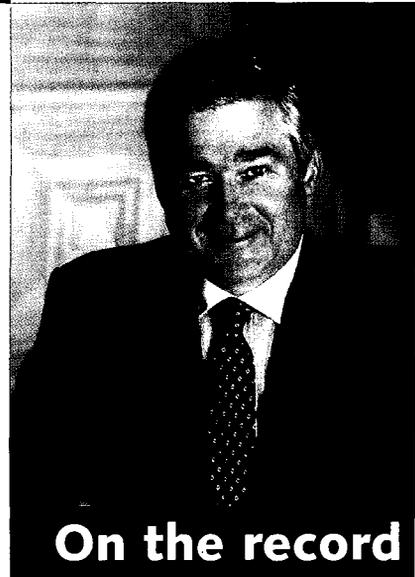
**Y**ou can look. You can look hard. You can look as hard as you want. But you won't find many corporate turnarounds more dramatic than the one Lou Gerstner has overseen at IBM.

When he arrived in 1993, taking a job no one else seemed to want, the venerable computer giant looked, by Gerstner's own admission, "like it was going into a death spiral." Through the '60s, '70s, and most of the '80s, IBM had defined information processing and its role in the world's leading enterprises. Ironically, it was IBM's own innovation — the introduction of the personal computer — that began a fundamental shift away from mainframes and the computing model that it created, ultimately calling the company's very relevance into question. By the time Gerstner took over, these questions of relevance had degenerated into questions about IBM's very survival.

At the time, many inside and outside IBM were calling for the company to splinter and allow product-specific divisions to compete on their own merits within individual niches. But as a long-time customer of the information technology industry, Gerstner had another idea. Instead of more component suppliers, he believed the marketplace needed someone who could tie the pieces together into integrated solutions. Rather than disaggregating IBM, Gerstner held it together and made integration the cornerstone in his rebuilding plan.

It worked. Today IBM is the world's largest diversified information technology company, an \$80 billion global solutions provider with strengths in hardware (from supercomputers to laptops), software (including products from the strategic acquisitions of Lotus Development, Tivoli, and others), services (consulting and systems outsourcing), components (microchips, hard disk drives), and research (more annual patents than any company worldwide for six straight years). In all this work, Gerstner says IBM does just two things: "create the industry's most advanced information technologies, and help customers apply those technologies to improve what they do and how they do it." IFC can attest: IBM's AS/400 servers and Lotus Notes software are critical parts of our own information architecture.

For the last few years Gerstner has been coming to Washington to brainstorm about corporate strategy with World Bank and IFC President James D. Wolfensohn and other CEOs, offering insights about managing for change and other topics. In this interview he again shares some of those thoughts, which will ring true to any business, no matter what the size. And from his vantage point at the vortex of the global communications revolution, he talks about what must be done so that all countries, rich and poor, can share in the unparalleled benefits the Internet brings.



**Name:** Louis V. Gerstner

**Age:** 58

**Title:** Chairman and CEO, IBM Corp. (since 1993)

**Background:** BS in Engineering, Dartmouth College, 1963; MBA, Harvard University, 1965; management consultant, McKinsey & Co., 1965–1978; top executive at American Express Co. 1978–1989; CEO, RJR Nabisco, 1989–1993

**Reputation:** "Intense, ambitious, driven ... precisely the CEO IBM needed." (Fortune magazine)

**He Says:** "Every day it becomes more clear that the Net is taking its place alongside the other great transformational technologies that first challenged, and then fundamentally changed, the way things are done in the world."

**IFC:** Since you joined IBM six years ago, the company's market value is up nearly \$150 billion. Clearly, you've turned around the company. How have you done it?

**Gerstner:** There are a number of ways to measure progress, and market value is one of them. But to deliver those results, we had to first win back the confidence of our customers — many of whom had staked a lot of their success to our technologies. So from day one, we made sure every corner of the company reconnected with our customers. Every change we've made has been driven by identifying who our customers are, what they want, and how we can best provide it.

So we started by eliminating the internal focus that had become part of the IBM culture. We'd been so successful for so long that we started competing with ourselves, rather than our competition in the marketplace. That inward-looking orientation generated two problems. First, it was disconnected from what was happening with customers in the marketplace.

Second, it made us slow in an industry where being first is almost as important as being right. No company in this industry has the luxury of waiting on perfect decisions or products. The industry moves too fast, and the pace of change is only accelerating. To succeed in this industry, you have to get into the market, learn, adapt, and continuously improve.

The other thing we did — the most important thing, actually — was re-energize an incredibly talented group of people who were very eager to bring this company back to a position of leadership. What they've done is the most extraordinary thing I've seen in 30 years in business. They're what made IBM's turnaround possible.

**IFC:** What can other organizations learn from IBM's success at reengineering and managing change?

**Gerstner:** I've got to be careful with this, because I don't want to leave the impression that we did everything right, or that we're done. That's a problem a lot of organizations box themselves into — setting a set of objectives, reaching them, and concluding that the work is done. It's never done. And as soon as you start thinking it is, you're headed back where you started in the first place. You're never done.

**IFC:** Does this kind of restructuring have to start with a commitment from the top?

**Gerstner:** Sure. I mean, there are a core set of decisions that have to be made at the top. They'll be executed by line management across the enterprise, but the strategic decisions will be made by a small group of people. Beyond that, I don't believe you can embark on any meaning-

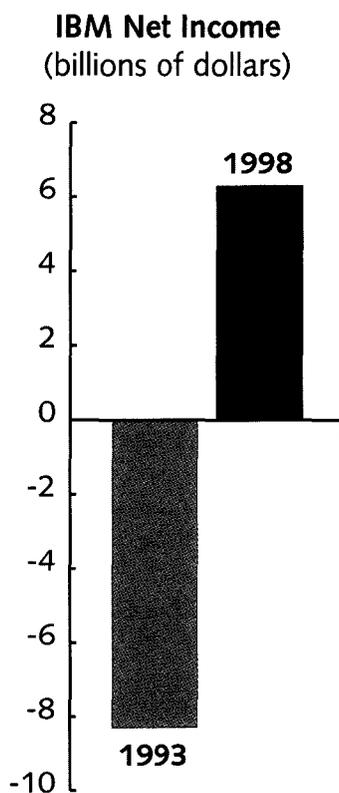
ful institutional restructuring without a commitment to lead an effort that will take five years — minimum. And you have to understand up front that the hard part isn't getting started. Responding to a crisis is relatively easy. The hard work is in sticking with your program over multiple years — seeing the changes through, reaching whatever objectives you set, but never being satisfied with that.

**IFC:** How did you start the restructuring at IBM?

**Gerstner:** You have to do a very honest and rigorous self-examination. What are we good at? What's our core competitive advantage? Is that advantage sustainable? Every organization has to do this — a very tough self-assessment of the strategic direction, the structure you want to achieve, the basic value proposition to customers, and a dispassionate assessment of strengths and weaknesses. This exercise led us directly to the central questions of where to concentrate resources, where to invest, where to disinvest, and it led to the most important business decision we made — the decision to hold the company together and serve our customers as the premier integrator of information technology solutions.

There are a couple of other things we believed, and believe, were important to our restructuring, and could be relevant to any company going through this kind of change. One is the importance of competitive benchmarking.

After you've determined what you want to accomplish — to be the best global competitor, or the best within your industry, or the best in one product segment, or whatever it is — then you have to quantify what it will take to reach that goal. To answer that question, you have to be able to measure your current position and where you stand relative to your competition — and you have to be able to track that position over time.



**Difference in IBM's bottom line from years one and five of the Gerstner era: more than \$14 billion.**

IBM now has major new research labs in Delhi and Beijing, part of a \$18.3 billion investment in research and development since 1995. Here are some ways it sees the Internet making its presence known in the developing world:

■ **E-commerce:** Peru's first online supermarket, *Tiendas E. Wong*, offers 15,000 items for sale. Operating costs are half those of traditional stores, and profit margins from online sales are 35% higher.

■ **Distance Learning:** Korean National Open University has more than 200,000 students at 13 regional and 31 remote education centers, plus a Web site that will soon hold 10,000 hours of broadcast lectures and learning materials. In Mexico, the Monterrey Institute of Technology puts digitally delivered education within the reach of some 43,000 students.

*But there's still a long way to go. Many developing countries' high access charges keep potential users logged off. Take Argentina: the local calls needed to get into the Net typically cost more than twice what they would in the US. Until local telecom markets open up to greater competition, bringing connection prices down, the information gateway will be thin indeed.*

Source: 1998 IBM Annual Report;  
*Alexis de Tocqueville Institution (USA)*



**Man and Computer:**  
*Would we have either without IBM?*

**IFC:** IBM has been out front pushing the concept of e-business. What do you mean by the term?

**Gerstner:** Three years ago, there was a lot of confusion about what the Net was all about. People were fixated on entertainment, online magazines, news, or a lot of applications targeted at the home. We said then, and have maintained continuously until now, that the Internet was not just about browsing for information, or some kind of planetary chat room. We said the Net was a vocational medium — a place where real work would be done, where real wealth would be generated, and real competitive advantage would be found. This was a novel idea at the time — so novel we had to create a new vocabulary to define it. “e-business” is the term we coined to describe all the ways people and organizations will derive value from the Net — all the physical transactions and interactions that will become digital and conducted using global networks: retailer to consumer; employee to employee; government to citizen; physician to patient; teacher to student.

The Net won't replace these physical transactions, but it's going to augment them in an enormous way. It's happening all around us.

**IFC:** Where is the Net having its greatest impact?

**Gerstner:** Right now most of the attention centers on e-commerce. And it's easy to see why — we're watching the creation of nothing less than a new digital economy. Within the next couple of years, Internet commerce will be a trillion-dollar marketplace. And the incentives driving organizations to enable wholly new ways of relating to customers or their trading partners are enormous. One example is the way networks alter the basic economics in the costs of transactions. Airlines estimate that it costs an average of \$8 to process a ticket order. The same transaction on the Net costs \$1. Banks estimate that a face-to-face transaction with a teller in a branch office costs a dollar or more. On the Net, the same transaction can be completed for about one cent.

And this isn't simply a powerful tool available exclusively to the world's entrenched franchises. One of the most dramatic effects of the Net is the way it levels the playing field for small businesses, or emerging economies. Small businesses can establish a global presence at nominal cost, and attack the household name brands with unprecedented levels of service and convenience. Developing nations can bypass whole generations of

technical investment. That creates an interesting set of opportunities for world leaders who now have the chance to nurture high concentrations of Internet usage as a way to leapfrog other regions in terms of production, productivity, and profitable growth.

**IFC:** Isn't all this largely a US phenomenon?

**Gerstner:** Right now it is, but that's changing fast. Seven countries other than the United States have around 10 percent of their populations using the Net, and very soon, there will be equal numbers of people accessing the Web in English and other languages. Two years ago, 85 percent of all Internet commerce was generated inside the US. Within three years, most forecasts say at least 35 percent of e-commerce will take place outside the US, and that percentage will grow as access to the computing infrastructure becomes more universal.

One of the really interesting implications of this emerging networked world, is that just as it dissolves barriers to market access and opportunity, it will redefine our notions of national and regional borders.

The Net is a great catalyst for economic expansion around the world. Look at what's happening with software development in India as just one example. India is already doing \$2 billion a year in software exports. And all the major players, including IBM, have established operations there. We employ more than 2,000 people in two joint venture companies, and last year we opened our newest IBM Research lab in Delhi.

**IFC:** Many analysts see the Internet as having unprecedented power to increase or decrease the gap between rich and poor worldwide in the 21st century. Which do you think will occur?

**Gerstner:** That's a very important question that policy makers and business lead-

ers around the world are just starting to address. The central question here is whether we're going to allow this technology to divide the world into two camps — one with access to the technology and one without. I think that's one possible outcome, but it's not inevitable. We have the chance to close the gulf between the so-called information "haves" and "have nots" if we can give the world's people fair, affordable access to information technology and the Net.

**IFC:** What has to happen to make access more universal?

**Gerstner:** A couple of things. First, governments have to end telecommunications monopolies and encourage competition. Markets around the world have to be open to new network operators and Internet service providers. There's no way the Net would have grown the way it has in the United States if users faced the leased line rates that prevail in Europe, if the market for Internet services was closed, or people had to deal exclusively with government or monopolistic providers. The World Trade Organization took an important step toward more open access with a general agreement on basic telecommunications. Now it's up to individual countries to step up and implement their commitments and to conceive even more ambitious ways to liberalize their telecommunications infrastructures. Beyond bringing down telecommunications rates, equal access will require a change in the current model of personal computing. On this front, there's a lot more to feel good about. Up until now, getting to the Net meant having — or having access to — a full-blown personal computer. But today, we can say with confidence that this is going to change, and change forever. The PC's reign as the center of innovation and investment in our industry is over. Within a few years, most of the devices that people use to access the Net will be non-PC devices — wireless hand-held computers, screen phones, Web-enabled TVs, public access kiosks, others that haven't even been

invented yet. All these devices will bring hundreds of millions of people to the Net quickly, and more cost-effectively than ever before. So I believe the Net has the potential to reduce the gap between the "haves" and the "have-nots," not widen it. We have a great opportunity to take unprecedented levels of information and learning to the entire world regardless of an individual's income or where they live.

**IFC:** Last year, you announced your decision to remain at IBM for another five years. What's the biggest challenge facing you?

**Gerstner:** I would say it's execution. We have our vision. It's e-business. The job at hand for us now — this year and for the next several years — is executing our strategy in the marketplace. And that's a big challenge — not just for me, but for my whole management team. It's the issue we spend most of our time on. I think we're up to it, but I don't ever want my leadership team to think we can relax.

**IFC:** Where's your greatest opportunity?

**Gerstner:** Leading our customers into this world of e-business. Showing them the benefits of the networked world and helping them to use the technology to improve what they do. The Internet is the epicenter of technological change today, but more important, it is the catalyst for business change — the redefinition of supply chains, business models, economic assumptions, the ways we build products and how we distribute them. The Internet has returned information technology to the agenda of the CEO. The Net is fundamental to every element in the CEO's strategic agenda: growth, competitive advantage, customer service, global expansion. We feel very fortunate to be in a position to help bring the benefits of this technology to our customers and the people they serve all over the world. ■

# MAN OF CULTURE



If you like the interplay of business, politics, and development, and wonder why some countries seem to be better at it than others, there may be nothing better you can do than sit down with a book by **Francis Fukuyama**. Rare are those who can interpret the age. Rarer still are those who can define it. He does both.

Born into a family that came to the United States from Japan three generations ago, he was almost unknown before the publication of his 1989 essay, "The End of History," which quickly framed the debate in the new post-Cold War era. With the conclusion of the century's great ideological struggle, it said with force, there was now only one option left for any country that wanted to succeed: "democratic capitalism." The primary question for the future was the identity of the winners within this single remaining context. Expanded into book form three years later, it was soon translated into 20 languages and became an international

best seller, prompting endless arguments and counter-arguments and emerging as one of the decade's most influential works.

In 1995 Fukuyama returned with an even more provocative work, *Trust*. A deep and challenging look into the cultural roots of economic success and failure around the world, it was named "Business Book of the Year" by the *European* and one of the top 10 in that same category by *Business Week*. It saw no accident in the climb of the US, Japan, and Germany to the summit of industrial power — they were "high trust" societies with a natural tendency to solve problems by working together. And they made full use of the single most valuable natural resource in the new global economy: the knowledge and skills of their people. At the same time, it warned, "low trust" societies with no impulse to build communities based on shared assumptions, such as China and France, would have serious trouble developing the flexible business organizations needed to compete in an increasingly open global economy. Why? Because cap-

italism was taking as its basis a new factor of production, *social capital*.

A former US State Department official, Fukuyama is now a professor of public policy at George Mason University in suburban Washington, DC. This summer he will publish his newest book, *The Great Disruption: Human Nature and the Reconstitution of Social Order*. Like his others, it is sure to excite some readers and confound others, yet make all think in new ways about the big global issues, including some they probably had not considered before. In February IFC's Economic Department arranged for him to speak at IFC in preparation for participation in a Seoul conference on democracy and development in Asia organized by Korean President Kim Dae-jung and the World Bank. His contribution there: a speech on "Asian Values in the Wake of the Asian Crisis" that asked whether East Asia's unique cultural traits were more responsible for the economic successes it enjoyed until recently, or the failure it has experienced since. Afterwards he took a few minutes to talk to *Impact*.

**IFC:** The roots of the financial crisis in East Asia are clear enough: over-valued exchange rates, excessive borrowing in hard currencies, weak regulation and corporate governance, and so on. But would you say it goes deeper than that? Were there larger cultural issues at work that made it all happen?

**Fukuyama:** The larger cause is a crisis of overproduction, and there you can find roots in culturally based institutions. Industrial policy in Japan, Korea, and to some extent in China really has encouraged investment decisions based on wanting to grab export markets that really did not promise a market rate of return. These would not have been made if those economies had been following market signals.

**IFC:** For whatever reason, the successful economies that do follow those signals seem to be either Western or based on a Western model. Why would you say that is?

**Fukuyama:** Well, there is always a question of what is really Western and what is just a feature of economic modernity that can be adopted by a lot of other cultures, such as advanced in science and technology, but innovation and entrepreneurship probably are more Western kinds of phenomena. The individualism that is encouraged in the Western tradition, especially in American culture, and the Western values of questioning authority and thinking outside the box are a very helpful source of innovation. That's especially true at time like the 1990s, when what's happening is a real change in the basic paradigm of economic activity, making production processes far more information technology-based than in the past.

**IFC:** But why not Japan's tradition that instead favors groups over individuals? It seemed so good for so long.

**Fukuyama:** Japan is known for a norm-based factory management system.

In a way that is very good when you have an established technology, such as automobiles in the '50s and '60s, where the productivity gains lie not in a dramatic change or innovation in the underlying technologies, but a tweaking of the social system that uses an existing, fairly mature technology to produce a final product. The Japanese were really excellent at that.



1 9 9 2

**IFC:** Give us an example.

**Fukuyama:** The clearest example was "Just in Time" manufacturing in the auto industry. The Japanese were able to double or triple labor productivity in the space of five or six years by applying techniques based on an understanding that firms behaved like social organizations, and that workers and managers were bound to each other. Managers tend to devolve more responsibility to workers in a trust-based system like that and get more rapid information feedback that leaves them closer to the production process. This happened first in Toyota, and when those techniques were import-

ed to Detroit, the American auto industry also saw that kind of increase in labor productivity.

I think there's something in social connectedness that is important as a technique for managing a production process, and that there's an argument to be made that this kind of consensual, norm-based management is going to become more prevalent as the technological sophistication of an economy rises. Partly as a result of these examples from Japan, the emphasis all over the industrialized world now is more on letting people set their own rules instead of on the classic Western factory model that had a very legalistic, rule-based, hierarchical system of management and did not require any social trust. But where I think the reason the Japanese have fallen down since is in the fact there's been a large change in the whole technological paradigm: the shift towards knowledge and away from manufacturing.

**IFC:** Why can't its culture do a better job of responding to that?

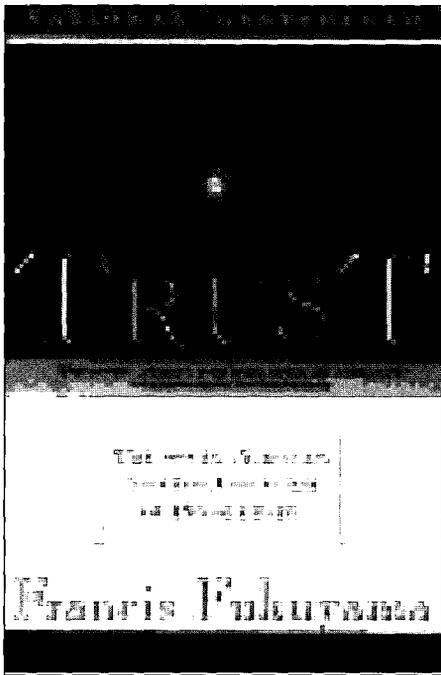
**Fukuyama:** Because there the group-oriented, consensus-based system has not been very helpful to them. It hinders things. Changes in technology require changes in labor markets, and one thing the Japanese have is sticky labor markets. They've got all these groups, obligations, and norms of reciprocity that demand that you don't fire people or move them around. But right now, on balance, doing that is what's called for.

**IFC:** You're just back from Korea. How does it rate on these same issues?

**Fukuyama:** Korea's a really different place. To my mind it is a much more recognizably European-style society than Japan is. It has these traditional class cleavages that are much more out in the open: There are workers and managers in Korea that don't like each other; the workers go on strike; the managers don't like them. Its labor history is much more

like that of Britain, Sweden, any other European country. What I think is really very weird is the Japanese system, which tries to smother these social conflicts in a big web of mutual obligations. The Koreans are out in the streets contesting who's going to get a bigger share of a pie. It's a much more conflict-ridden society, and in a sense its democracy may evolve in a more recognizable Western pattern than Japanese democracy.

**IFC:** Why?



1995

**Fukuyama:** In Japan, there's one all-embracing political party that somehow smothers all the social cleavages that exist. It brings together rice farmers, industrialists, and others under the big Liberal Democratic Party (LDP) banner. Whatever social tensions exist are all hidden from view — they're discussed in the back rooms of the LDP, but there's no open contestation of these different social actors. In most European countries, the contestation is much more overt: The workers have a Social Democrat Party, the managers have a Christian Democrat

or a Liberal party, and then you fight it out in a democratic arena. I think Korea is probably more likely to develop along those Western models than Japan is, which I think is healthier.

**IFC:** So as the 21st Century wears on, will you be more bullish on Korea's economic future than on Japan's?

**Fukuyama:** Possibly.

**IFC:** Speaking a little more broadly, some of your critics contend that recent events have shot down your basic argument from *The End of History*, the one that says the only way left to become an "advanced country" is to be a free market democracy. What do you think?

**Fukuyama:** Assuming that the current crisis does not turn into a global depression, in which case all bets would be off, I think the argument essentially still stands. There is a path to development, and there's really no alternative other than integration of the world economy.

**IFC:** What's the path?

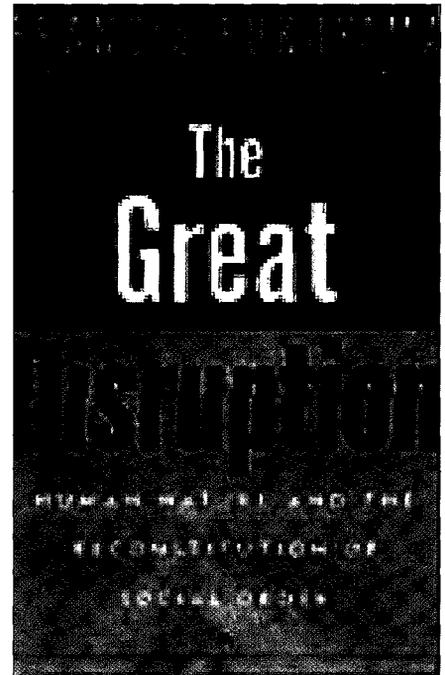
**Fukuyama:** There are three parts to it: (1) Democracies don't fight and therefore you have a democratic "zone of peace" that has developed in the world; (2) the way to get democracy is through economic development (these two have a strong correlation); and (3) the way to get development is to integrate as completely as possible into the global economy.

Now that three-part syllogism is threatened if, in fact, integration into the global economy turns out to be destabilizing. I think you can at least make a plausible argument that the kind of financial instability you've seen in the 1990s — a European currency crisis, a Mexican peso crisis, an Asian financial crisis, Russia and Brazil — is evidence that there's something not working right in the global financial system. Therefore the link

between integration into the global economy and development looks more problematic than it would have looked seven or eight years ago. But no one has really come up with a lasting alternative, and it's not clear to me that you couldn't fix those problems.

**IFC:** But think about Russia's recent experience. What does it show you about all this?

**Fukuyama:** What it shows is that



Forthcoming

there are real political and cultural preconditions for the establishment of either a market economy or a working democracy. What's been happening in Russia in the last year really forces a certain kind of thinking. It's possible that they're now in an equilibrium situation that is neither capitalist nor democratic, but is also not obviously going to evolve into something that we would call a working capitalist democracy. They could be stuck there for a very long period of time. ■

*Continued from page 7*

the new OECD convention on the supposed grounds that business in most of the world cannot be conducted without bribes. Today, though, US companies tend to say they approve of the FCPA, although that could be because of what it does not do as much as for what it does. Since 1977, there have been fewer than 50 convictions under the act, although supporters insist it has nevertheless been a powerful deterrent.

One good reason to be hopeful about the OECD convention is that it now brings most of the world's major exporters and foreign direct investors under roughly the same rules about bribery. As in most cases, competition may prompt companies to police one another. Before, all a US company could do if it was beaten to a contract by a bribe-wielding European firm was to complain to Washington.

Wesley Cragg, a business professor at Toronto's York University and head of Transparency International's Canada chapter, recalled that it was Boeing that raised the possibility of corruption (as yet unproven) in the purchase of Airbus aircraft by the Canadian government. Intense competition will do that for a place. If the OECD convention is enforced, Cragg predicted, increasingly "companies who lose contracts because of what they see as corruption will come forward." The truest sign, perhaps, that competitiveness and corruption do not mix. ■

*Philip Segal is the Hong Kong correspondent of the International Herald Tribune. He has lived and worked in Asia for seven years and has also been a correspondent of the Economist in Mexico City and Ottawa.*



*Continued from page 17*

and Niger are due to open later this year, perhaps followed even by Liberia. The expansion requires new capital and must be managed carefully, as the record of others who have tried and failed, such as Meridien-BIAO, shows.

After Ecobank proved itself by attracting \$13.5 million in new capital from its African shareholders, IFC made an initial show of support by introducing it to Saudi Arabia's Prince Alwaleed Bin Talal Bin AbdulAziz Al Saud, a master of the markets whom *Money* magazine unabashedly calls "one of the world's greatest investors." The single largest shareholder in Citigroup, Apple Computer, and Four Seasons Hotels, he is one not easily impressed. But his Kingdom Holdings Africa investment vehicle is committed to investing \$1 billion in the continent's most attractive companies, and after doing thorough due diligence on the Ecobank story, it agreed to inject \$7.05 million into the holding company and take a seat on its board.

In January IFC followed with its \$7.5 million equity and quasi-equity investment, which helped raise total capital from \$33 million to \$61 million and complemented the earlier IFC stake in the Burkina Faso subsidiary. While still small compared with the capital of the large South African, Nigerian, and foreign institutions that dominate African banking, this is money that can go a long way in improving standards from Mauritania to Cameroon and helping channel savings into investment — the key to development everywhere. In a few more years, the world will know how far Ecobank's echoes resound. ■

*IFC's work with Ecobank has been carried out by its Sub-Saharan Africa Financial Markets Division (Bahadurali Jetha, manager). Papa Madiaw Ndiaye is the investment officer on the project.*

**IFC**

**International Finance Corporation**

2121 Pennsylvania Avenue, NW

Washington, DC 20433 USA

[www.ifc.org](http://www.ifc.org)

*IFC is a member of the World Bank Group  
supporting private sector development in member  
countries through investment, advisory services,  
and technical assistance.*