



ECONOMIC OPPORTUNITY SERIES



# The Role of the Extractive Sector in Expanding Economic Opportunity

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### **Acknowledgements**

The authors express their special thanks to Pamela Skaufel of ExxonMobil, Heather Kulp and Tam Nguyen of Chevron, and Liz Reicherts of BP who generously offered their experience and perspectives, as well provided background information on the initiatives profiled in this report. Special thanks also go to Alice Shay for providing research support to complete the report. They also gratefully acknowledge the substantive input and support of Jane Nelson, Beth Jenkins, and Jennifer Nash of the CSR Initiative.

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Wise, Holly and Sokol Shtylla. 2007. The Role of the Extractive Sector in Expanding Economic Opportunity. Corporate Social Responsibility Initiative Report No. 18. Cambridge, MA: Kennedy School of Government, Harvard University.

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# Preface

*Beth Jenkins, CSR Initiative, Kennedy School of Government, Harvard University*

The past fifty years have witnessed a “revolution” in global economic growth. Yet not everyone has participated in this revolution. More than 65% of the world’s population, over four billion people, still lives on the equivalent of less than \$4 per person per day. Even worse, the world’s poor are severely constrained – and often completely lacking – in opportunity to do better for themselves.

The business community has both the capabilities and the strategic, business reasons to play a major role in creating these opportunities. The CSR Initiative’s Economic Opportunity Series, a product of our Economic Opportunity Program, explores this role across a range of industries.

**“Economic opportunity enables people to manage their assets in ways that generate incomes and options.”**

For the poor, livelihood choices – in employment and entrepreneurship – are constrained by a wide range of interdependent obstacles, ranging from geographic isolation to market failures to political exclusion. This suggests that when we think about eradicating poverty, we should think broadly about creating economic opportunity. Economic opportunity is not, in itself, a solution; instead it is a context in which individuals can create their own solutions. It is a combination of factors that enables the poor to manage their assets in ways that generate incomes and options.

Creating or expanding economic opportunity could rightly be considered a responsibility of governments toward their citizens. But in today’s global market environment, various risks and opportunities provide reason for business to engage.

One key reason, across industries, is for business to leverage its own comparative advantage in society. As Milton Friedman might say, “the business of business is business” – and this is exactly what gives firms the capability and credibility to expand economic opportunity. Business activity creates jobs, cultivates inter-firm linkages, enables technology transfer, builds human capital and physical infrastructure, generates tax revenues for governments, and, of course offers a variety of products and services to consumers and other businesses. Each of these contributions has multiplier effects on development.

In developing countries, companies’ multipliers often fail to reach the scale or leverage of which they might be capable – often due to market failures and governance gaps. More deliberate management attention is required to unlock their full potential.

The Economic Opportunity Series explores four key strategies companies can use to expand economic opportunity:

<b>Creating Inclusive Business Models</b>	Involving the poor as employees, entrepreneurs, suppliers, distributors, retailers, customers, and sources of innovation in financially viable ways
<b>Developing Human Capital</b>	Improving the health, education, experience, and skills of employees, business partners, and members of the community
<b>Building Institutional Capacity</b>	Strengthening the industry associations, market intermediaries, universities, governments, civil society organizations, and grassroots groups who must all be able to play their roles effectively within the system
<b>Helping to Optimize the “Rules of the Game”</b>	Shaping the regulatory and policy frameworks and business norms that help determine how well the economic opportunity system works and the extent to which it is inclusive of the poor

There is enormous variation in the roles companies can play, depending on their industries, their particular business models and relationships, and the contexts in which they operate. The industry reports in the Economic Opportunity Series explore this variation, offering more specific and detailed examples for different industry sectors. The research suggests, in general, that inclusive business models can be the most effective and sustainable ways companies can contribute. Complementary strategies such as developing human capital, building institutional capacity, and helping to optimize the “rules of the game” can also have significant impacts. These strategies are often used in combination with inclusive business models, to enhance both their commercial viability and their development impact.

The research that has gone into this series also suggests that company efforts to expand economic opportunity can draw upon core business, philanthropic, and public donor funding, depending on the balance of business and social benefits expected, the likely timeframe for their realization, and the level of uncertainty or risk involved. Hybrid approaches are increasingly common.

So is collaboration. Complex, systemic challenges like expanding economic opportunity present frustratingly frequent bottlenecks to unilateral action, corporate or otherwise. Even the best-resourced efforts eventually run into limitations on scale somewhere. Collaboration allows parties to share knowledge and information, pool scarce or diverse assets and resources, access new sources of innovation, create economies of scale, and enhance the legitimacy of the parties’ own individual activities. In addition to assembling the necessary resources and capabilities, collaboration can generate new capabilities and change operating environments in ways that create new strategic opportunities.

The Economic Opportunity Series is part of a growing effort within the business and development communities to make the links between business activity and poverty alleviation. Experimentation and learning are happening fast. As a result, the series must be considered a work-in-progress, and readers are invited to share their experience and reflections with us. We look forward to being part of the dynamic growth and development occurring in this field.

# 1 ■ Introduction

Resource extraction fuels the global economy. It also contributes substantially to the national economies of countries from which the oil, gas, and minerals are derived. While the macroeconomic impact of extractive sector operations is significant and usually, if not uniformly, positive, the microeconomic impact of extraction enterprises is even more uneven, and in many cases could be greatly enhanced if companies adopted more explicit policies and practices to expand economic opportunity along their value chains.

In 2007, energy and mining companies made up six of the 10 largest companies in the world, and five of the 10 most profitable – with ExxonMobil topping the list as the world’s most profitable company.<sup>1</sup> However, the communities from which these companies extract commodities are among some of the poorest. Economic opportunity does not flow directly and evenly from multinational extractive companies to those closest to and most affected by their business activities. And given the fact that over the next 20 years, approximately 90% of new hydrocarbon production will come from developing countries, the gap between company profits and local economic benefits could widen.<sup>2</sup>

Expanding economic opportunity in the communities and countries where they operate is in extractive companies’ best interest. It can lessen their production costs, provide continuity of supply and distribution outlets for goods and services, enhance social license to operate, and mitigate risk and potential conflict. Yet approaches to economic opportunity enhancement are not widely adopted or consistent across the extractive sector. There is room for understanding what has worked and why, scaling up best practices, and strengthening mechanisms for collaborative action which would benefit extractive companies, host governments, communities, and individuals.

This report explores the dimensions of extractive sector firms’ role in expanding economic opportunity. It focuses on multinational extractive companies, touching on the activity of national joint venture partners. Given that national oil companies control 80% of remaining global oil reserves<sup>3</sup> and face different incentives and pressures related to economic opportunity expansion, they bear separate treatment outside the scope of this report. Through an overview of the issues and vignettes of industry-specific activity, coupled with a series of more in-depth case studies, we attempt to describe the business case for economic opportunity enhancement, specific strategies firms pursue in doing so, and recommendations for collaboration moving forward.

## 2 ■ The Role of the Extractive Sector in Expanding Economic Opportunity

Extractive companies are major players in the economic landscapes of many developing countries. While circumstances vary from country to country, the proceeds from mineral, oil, and gas extraction contribute substantially to many developing country public budgets. In Nigeria, for example, the extractive industry contributes 20% of the country's gross domestic product (GDP) and 65% of its budgetary revenues. In Azerbaijan, oil is the leading export. Revenues from offshore oil production will double the country's current GDP of \$60 billion over the next three years.<sup>4</sup> At the macro level, extractive companies generate substantial levels of revenue for host governments in the form of royalties, income taxes, or other profit-sharing arrangements. In 2005, for example, the Shell Group paid \$18 billion in government taxes in its countries of operation throughout the world.<sup>5</sup>

In September 2004, the World Bank Group's Extractive Industries Review process concluded that "extractive industries can contribute to sustainable development, when projects are implemented well and preserve the rights of affected people, and if the benefits they generate are well-used."<sup>6</sup> Furthermore, independent research commissioned by the International Council of Mining and Metals (ICMM) has concluded that mining can provide an important, and sometimes critical, contribution to economic development and poverty reduction in developing countries – provided the underlying conditions are right.<sup>7</sup>

When allocated effectively and equitably, revenue flows from the extraction of natural resources can finance public goods and services such as education and training, health care, and infrastructure – all of which ultimately contribute to expanded economic opportunity for host country citizens. However, this type of indirect contribution does not guarantee the expansion of economic opportunity in developing countries. The well-documented "resource curse" is often a problem, as the activities of the extractive sector fail to consistently and directly affect economic growth and expand economic opportunity, and in a number of cases have actually worsened conditions and qualities of life for certain population groups.

Frequently, the actual benefits of natural resource flows do not equal anticipated ones. There is often a mismatch between revenues generated and local benefits, which is due primarily to issues of governance, transparency, and accountability in funding allocation, as well as weak administrative capacity in many governments. The ICMM study found that three underlying conditions generally drive economic development in mineral-rich countries including: reformed legal frameworks and mineral legislation, significantly improved macroeconomic management, and some improvements in governance.<sup>8</sup> The absence of these and other reforms can reduce the positive impact that mining and other extractive industries can have on local economies. This is a significant issue for both extractive companies and host governments. While it receives some attention among these parties and within the development community, there is a relative paucity of experience in effective revenue management schemes and the human and institutional capacity requirements to implement them well. There is an opportunity to build effective public-private partnerships

beyond those that currently exist. These have the potential for channeling significantly more economic growth-enhancing benefits to local communities than are currently available.

In addition to their contributions to national coffers, extractive companies impact local economies through:

- procurement of goods and services
- product distribution and sales
- employment, and
- social and community investment.

## **2.1 Procurement of Goods and Services**

Extractive industries are inherently capital intensive and have traditionally relied heavily on imported equipment and production inputs. Fully assembled rigs, heavy machinery, and sophisticated monitoring equipment pass through customs and provide no opportunity for host country manufacturers, assemblers, suppliers, and laborers to add value. There are a growing number of contractual obligations under host country agreements to meet local content requirements and social investment targets. The Russian government, for example, has set a requirement of 70% Russian-sourced materials and services to be used in the Sakhalin II project in which Shell is a partner.<sup>9</sup> This, coupled with the cost-of-production pressure to source locally, provides an incentive for extractive companies to look to local suppliers of goods and services.

## **2.2 Product Distribution and Sales**

While there is generally imperfect alignment between sources and markets for extracted resources, there are nonetheless business drivers for sales in developing countries and emerging markets, particularly for downstream oil, gas, and lubricants, and for certain minerals. Extractive companies can and do engage local distributors and suppliers to meet host country needs for their products. Intermediary, wholesale, and retail operations related to the provision of extractive sector goods and services provide employment and economic opportunity for host country nationals and can have regional economic impacts as well. Total, a leader in downstream operations in Africa with a market share of 24.5%, operated seven refineries and 3,750 service stations there as of 2005, employing 8,500 mostly national staff.<sup>10</sup>

## **2.3 Employment**

Extractive industries are not labor intensive. Employment and other economic opportunities are somewhat more concentrated in the construction phases of capital projects, but less so during exploration, ongoing operation, and close-down phases. Although more limited than in other industries, extractive sector employment offers significantly higher income than employment in other sectors of local economies. For instance, during 2006-2007, Barrick Gold offered entry-level wages in South America between 130% and 215% higher than the minimum wages offered in those countries.<sup>11</sup> To prepare for direct and outsourced

human resource needs, extractive companies frequently invest in tertiary education facilities and secondary technical-vocational training, sometimes targeting shortage categories such as geologists, petroleum and mining engineers, and the like. These investments in human capital development benefit not only their own workforces, but more widely expand the skills and capacities of workers in developing countries.

In its final report, the Mining, Minerals, and Sustainable Development (MMSD) Project concluded that mining companies should pay particular attention to employing local workforces in their operations. Besides offering training opportunities to enhance the technical capacities and skills, mining companies should also foster career advancement opportunities for local staff. Finally, the report concluded that “skills training should not be limited to workers but should be extended to the community as a whole” and that human capital development programs “should consider the need for alternative economic activities to support the community during and after the life of the mine.”<sup>12</sup>

## **2.4 Social and Community Investment**

Social and community investments are another avenue to empower the poor to manage assets to expand their incomes and options. Strategic philanthropy targeting agriculture, small and medium enterprise (SME) development, transport, finance, telecommunications, or the services sector can create local economic opportunity and generate medium-term benefit for extractive companies in growing their cohorts of suppliers and buyers. However, the majority of social and community investments currently focus on health, basic education, arts, culture, sports, and the environment rather than on local private sector development.

Extractive companies are not unique in leaning away from economic growth as the focus of their philanthropy,<sup>13</sup> though they have perhaps more to gain from such investments than other sectors. Chile’s mining industry illustrates the potential. The ICMM’s Resource Endowment Initiative research found that Chile, one of the better performing economies among those surveyed, “has developed stronger linkages between the mining industry and other sectors of the local economy than have many other mining countries. Suppliers to the industry have flourished, partly as a result of deliberate fostering on the part of the mining firms.”<sup>14</sup>

### 3 ■ The Business Case for Engagement

Extractive industries, by their very nature, have longer time horizons than many other industry sectors. They do not have wide choice in investment locales, nor are they very mobile. They follow the fixed placement of existing mineral and energy deposits. And while they may operate offshore, underground, behind barricades, and in failed states, they function most productively in stable economic and political environments with markets for both their inputs and products. Hence, expanding economic opportunity in host communities, countries, and regions can reduce risk, decrease costs of production, and increase profitability for extractive companies.

As major multinational energy and mining companies continue to expand their developing country footprints, they are finding challenges to the long-term sustainability of their operations in local communities. Michael Warner of the Overseas Development Institute describes these issues as part of a “benefits gap” between the anticipated and actual rewards to the local communities impacted by their operations.<sup>15</sup> Analyses by international financial institutions, advocacy groups, and local non-governmental organizations (NGOs) have pointed out the disconnects that often occur between industry profits, payments to host governments, on-allocation of resources to social organizations, and community benefits. Initiatives such as Publish What You Pay<sup>16</sup> and the Extractive Industry Transparency Initiative<sup>17</sup> focus on the need for greater transparency and accountability in tracking these resource flows. Extractive companies vary in their contractual freedom to disclose, and countries vary in their participation in these global initiatives, but the fact remains that extractive companies must deal with public opinion and activism based on perceived imbalances in the distribution of benefits from resource extraction.

Expanded economic opportunity can become an important risk mitigant for extractive companies. It can be seen as enlightened investment in risk insurance. Operating in a vibrant economy and a stable environment is cheaper. The real and reputational costs of protests, work stoppages, boycotts, and regulatory backlash can be forestalled if companies are and are seen to be investing in the poor and helping them build their assets. In vivid terms, for example, a group of angry women with nothing to lose can bring an oil company to its knees. In July 2002, several hundred Nigerian women shut down the Chevron-Texaco Escravos facility in the Niger Delta by occupying the control room and blocking all arrivals and departures for 10 days. The women, aged 25 to 90, asked for the employment of local residents and the construction of clinics and schools.<sup>18</sup> Investing in “preventative defense,” as the United States Government refers to some economic assistance programs, can yield high return on investment for extractive companies.

The Niger Delta also provides a stark example of the “pay now or pay later” scenario facing extractive companies. As of July 2007, Royal Dutch Shell PLC reported that 195,000 barrels of oil a day remain trapped in Nigeria,<sup>19</sup> with a daily price tag for the company of nearly \$16 million at the current price of over \$80 per barrel.<sup>20</sup> These costs far exceed the amount of money that oil companies spend on economic opportunity programs in Nigeria.<sup>21</sup> While many debate the variety and weighting of factors that contribute to violence and disruption of operations in the region, lack of economic opportunity, both real and perceived, is certainly among them.

Managing community expectations about wealth-sharing is critical to reputation and social license to operate. Helping to diversify the local economy also creates income and employment opportunities outside of the extractive industry and reduces dependence on the industry as the sole provider of livelihoods. Broad-based and sustainable economic growth in host communities can also reduce the need for companies to assume inherently governmental functions such as welfare and social protection.

A more vibrant local economy can also positively impact company bottom lines by reducing the cost of production inputs. A well-functioning host country market can provide access to a continuous supply of labor at prices well below expatriate packages, materials that need not be imported, and innovation in products and processes that are appropriate to local operating environments. However, in many locales, extractive companies struggle with capacity of local markets and entrepreneurs to deliver the quality and quantity of goods and services they require. They often have to invest both up and down the supply chain. These activities can range from investment in agriculture to supply the cafeteria to supplier training for small business operators to management training for service station personnel. While these programs have demonstrated good returns, their utility is not yet widely accepted and awareness of best practices remains low.

## 4 ■ Business Strategies for Expanding Economic Opportunity

There are compelling business drivers for extractive companies to engage in expanding economic opportunities. And these companies are well positioned to contribute materially to enhancing the assets of the poor. The most sustainable strategy involves nesting an economic opportunity expansion approach into the core business operations of procurement and sales. Extractive companies can also invest in growing the cohorts of entrepreneurs and skilled workers that will be their future employees, suppliers, distributors, regulators, and customers. Investments in the building blocks of civil society and the enabling environment are also productive.

### BOX 1 SIERRA LEONE PEACE DIAMONDS ALLIANCE

Sierra Leone's war in the late 1990s was largely funded by illegal and untracked diamond exports. Small-scale miners were hugely exploited during this period due to smuggling and unfair labor practices. Towards the end of the war, the government of Sierra Leone, large-scale diamond corporations such as DeBeers and Rapaport, and several international development organizations and NGOs came together to create the Peace Diamonds Alliance. The project advocates an integrated and transparent approach to diamond management: developing competitive buying schemes, training miners to recognize the value of their products, tracking diamonds from earth to export, providing credit to miners, and ensuring that communities benefit from the mining that takes place in their localities. The Rapaport Group with Kono's Hope has contributed \$75,000 to support five pilot cooperatives for one mining season. The Alliance has trained 209 individuals on valuation techniques. This project has increased economic opportunity for small-scale diamond producers as well as increased transparency in larger-scale production. The Alliance is an example of an inclusive business model that involves considerable human capital development.

United States Agency for International Development (USAID). 2006. "Sierra Leone Peace Diamonds Alliance: Rebuilding after war." *The Global Development Alliance: Public-Private Alliances for Transformational Development*. Washington, DC: USAID. Pages 67-70.

The Sierra Leone example demonstrates effective industry engagement with existing miners. In other cases, mining companies actually exclude small-scale and artisanal miners from economic activity as a result of their business operations. According to the Communities and Small-Scale Mining (CASM) initiative, at least 13 million people from over 30 developing countries engage in artisanal and small-scale mining, supporting a further 80 to 100 million people.<sup>22</sup> Local residents who may have traditionally worked certain geographies, and sometimes professionals such as teachers or health care workers who have been drawn to mine sites by increased activity are sometimes forced off the land and excluded from the economic opportunities mining might offer.

Few traditional miners can be employed within the formal industry. Extractive companies are faced with the challenge of relocating and retooling these individuals for productive employment elsewhere. Nonetheless, some mining companies are giving this matter an increased level of attention. AngloGold Ashanti, for example, conducted an external baseline study of artisanal and small-scale mining in Ghana in 2006 and is now working with other mining companies, the Chamber of Mines, and the National Minerals Commission to identify properties which are suitable for small-scale mining and to promote registration by miners to operate on these

properties.<sup>23</sup> In Tanzania, DeBeers has partnered with the government, local NGOs, communities, and development organizations to establish the Mwadui Community Diamond Partnership. The goal of this initiative is to produce a viable and potentially transferable model for improving qualities of life in mining-based rural populations, by enhancing existing artisanal and small-scale business model and exploring alternative livelihood projects.

In addition to artisanal miners, extractive companies face the challenge of developing their sites and infrastructure without harming other existing livelihoods. In the case of Shell's Malampaya deepwater gas-to-power project in Palawan, Philippines, for example, the challenge was to build and operate offshore platforms so as not to damage fishing livelihoods.<sup>24</sup>

## 4.1 Creating Inclusive Business Models

This report uses UNDP's definition of "inclusive business models" as mechanisms through which businesses include and benefit the poor, whether as employees, entrepreneurs, suppliers, distributors, retailers, customers, or sources of innovation, that are or have the potential to become financially viable.<sup>25</sup>

Extractive companies are limited in their ability to generate large-scale impact through employment. Nonetheless, many companies make local hiring a priority as is the case with Rio Tinto and its subsidiary, Diavik Diamond Mines Inc. (DDMI), which has made an explicit public commitment to have 66% of its workforce comprised of local residents from Canada's Northwest Territories and 40% of Aboriginal descent (see case profile on Diavik in this report).

Extractive companies can have greater impact when they develop inclusive business models that integrate local SMEs into their value chains, thus creating indirect employment and fostering the development of local entrepreneurs. Unfortunately, this type of inclusive business model is not as widespread across the industry as may be possible and desirable.

### BOX 2 GLAMIS GOLD'S INTEGRATED COMMUNITY DEVELOPMENT PROGRAM (ICDP)\*

**In July 2003, Glamis Gold partnered with the International Finance Corporation (IFC) and the Citizens Development Corps to create a collaborative public-private community development program in San Marcos in the western highlands of Guatemala. The integrated community development program, called Montana Exploradora Marlin Project, seeks to benefit communities impacted by the company's gold and silver mining project by providing health services, enterprise development, vocational training, agro-forestry, and environmental awareness. To date, Glamis Gold has contributed over \$1.3 million to programs in these communities. By training local residents in the mining process, Glamis Gold aims for an 80% local employment rate for mining operations. The project is a collaboration between the corporation, international NGOs, local organizations, and the municipality. Glamis Gold has incorporated the Montana Exploradora Marlin Project as part of a strategy to enhance the long-term social sustainability of its mines in Guatemala and to reduce local economic dependence on gold and silver mining.**

*\*In 2006, Glamis Gold was purchased by Goldcorp Inc.*

Gomez, Adriana and Corrie Shanahan. n.d. "Glamis Gold Ltd.'s Montana Exploradora Marlin Project in Guatemala." <http://go.worldbank.org/Q11EL8V5F0> (accessed November 26, 2007). Also see Citizens Development Corps. n.d. "Integrated Community Development Program: Guatemala." [http://www.cdc.org/desktopdefault.aspx?page\\_id=122](http://www.cdc.org/desktopdefault.aspx?page_id=122) (accessed November 26, 2007).

Large contracts, impenetrable procurement systems, and complex technology, quality, safety, labor, and reporting requirements often exclude local SMEs from the competition. Nonetheless, several companies in the industry have made concerted attempts to expand their pools of local suppliers. For example, extractive sector firms have explored business process improvements to expand access to procurement opportunities, as demonstrated by ExxonMobil's e-procurement innovation in the Chad-Cameroon pipeline project. In combination with other interventions, e-procurement has increased transparency and thus the responsiveness of local bidders to business opportunities with the company.

Equally significant are inclusive business models such as those adopted by BP in Trinidad and Tobago or by Anglo American in South Africa, which have moved beyond generating procurement opportunities for local SMEs and are building local supply chains and complex capabilities. In Trinidad and Tobago, BP's subsidiary decided to pay an initial premium to design and fabricate its offshore platform wholly in Trinidad and Tobago instead of shipping it in from Louisiana. The company estimated that the savings generated over time would significantly exceed the upfront premium. With the support of other industry actors, Trinidad and Tobago's upstream services industry is on its way to becoming competitive on the international market, while BP has already realized significant savings on the local production of its second and third platforms (see the case profile on BP in this report).

In South Africa, Anglo American's Zimele program aims to achieve large-scale impact by investing in and supporting black-owned and -managed enterprises. More than 70% of the enterprises in which Zimele has invested have survived eight years or more, according to a survey conducted in 2005. These vibrant businesses are growing by operating within and beyond Anglo American's value chain, thus generating sustainable benefits for owners, employees, and their families (see the case profile on Anglo Zimele in this report).

## **4.2 Developing Human Capital**

Most companies in the extractive industries are involved in efforts that improve the health, education, experience, and skills of their employees, business partners, and/or larger communities.

Initiatives range from adopt-a-hospital programs in local communities to subject-specific education initiatives in math, science and engineering to funding for stand-alone technical-vocational training centers. These community investment programs usually fall within the purview of a company's corporate citizenship team or foundation, at either the national or headquarters level.

A key complementary strategy for expanding economic opportunities in developing countries is to facilitate what the Shell Foundation calls the "transferring of business DNA"<sup>26</sup> to local entrepreneurs. As the Shell Foundation's research has shown, the viability and scalability of interventions, such as those aimed at expanding economic opportunity, depend on the ability of local actors to apply "business thinking and business principles to how they operate and to the interventions they propose." To this extent, extractive companies utilize a variety of programs to develop human capital in host countries. ExxonMobil, for example, has invested in capacity-building for local cohorts of suppliers and distributors in a variety of

locations, including supplier training initiatives that have communicated industry needs to small existing and potential contractors and sharpened their business acumen.

Mentoring programs are hosted by some business units of extractive companies. These employee volunteer programs engage staff with small-scale entrepreneurs who are able to grow their businesses through the counseling and support they receive – sometimes as part of the value chains of the sponsoring companies.

Human resources departments often make substantial investments in human capital development for local recruitment and retention. Often these are not harmonized with CSR investments in education and training that also target human capital development, and this is an area where increased coherence in company policies and practices could yield benefits for both companies and for the communities and regions in which they operate.

### **BOX 3 VOCATIONAL TRAINING ALLIANCE: CHEVRON CORPORATION**

**In May 2005, the Chevron Corporation created a public-private alliance to support immediate and long-term vocational training needs in Aceh, Indonesia, a region greatly affected by the 2004 tsunami. Members of the alliance have committed to contribute \$10 million to the project by 2007 to increase local involvement in the reconstruction process and redirect economic benefits from reconstruction to local communities. The program includes training for construction, teaching, and community development as well as the building of the Polytechnic Aceh, a vocational training center. Projects such as the Aceh alliance reflect Chevron's intentions to be considered a locally-engaged global energy company. Chevron's work in Aceh is an example of developing human capital and institutional capacity.**

CHF International. 2007. "New Partnership between CHF International and the Chevron Global Fund to Drive Economic Development in Post-Tsunami Indonesia." Press release dated July 24.

Investments by extractive sector firms in human capital development tend to focus on specific skill areas. In some cases they also target specific cohorts such as indigenous peoples, youth, and women. Broad-based approaches to capacity development and inclusion will not uniformly benefit all segments of the population. For instance, Chevron found in Indonesia that the first group of trainees in the polytechnic the company built contained few women. It was only by sending a signal to include more women in the training that its alliance partners there identified and included a sizable proportion of women in the program.

Extractive sector firms have the potential to enhance their impacts by creating economic opportunity with a focus on the most vulnerable segments of the productive population, such as women and youth. Women and youth have the highest rates of unemployment and underemployment, less access to credit, and are often not equally represented in public education and training programs. In addition, their voices are neither heard nor considered consistently in stakeholder discussions. Initiatives such as IFC's Gender Enterprise Markets Initiative and credit programs for female borrowers, which are supported by extractive companies through their community investment portfolios, are a start in targeting economic opportunity creation for these groups. ExxonMobil, most prominently among other extractive companies, has an explicit focus on women and girls' education in its community investment programs.

#### **BOX 4 EXTRACTIVE INDUSTRIES ALLIANCE, DEMOCRATIC REPUBLIC OF THE CONGO: PHELPS DODGE/TENKE FUNGURUME MINING (TFM)**

In the Democratic Republic of the Congo (DRC), Phelps Dodge/Tenke Fungurume Mining (PD/TFM) has collaborated with the Extractive Industries Alliance (EIA) and PACT, an NGO focused on community capacity-building, to implement social development projects that will help the communities surrounding PD/TFM become economically self-supporting. In 2006-2007, the collaboration created 24 micro-enterprise start-ups in brick and fence production and implemented 10 village water systems. PD/TFM has invested \$500,000 in local community development and seeks to expand activities to all 42 communities identified by EIA as impacted by the mining project. In addition to cultivating business linkages with smaller enterprises and improving local infrastructure, PD/TFM is working to improve economic opportunity in the area by advocating transparency, human rights, and artisanal mining alternatives in the DRC mining industry. These projects benefit PD/TFM by sustaining social support for the company from local up to international levels.

Robinson, Richard. 2007. "The Extractive Industries Global Development Alliance (EIA) for the Democratic Republic of the Congo." USAID memo dated March 16. Also see PACT. 2006. "Road Map for Social Development: Tenke Fungurume Concession for Phelps Dodge/Tenke Fungurume Mining, Katanga, Congo (DRC)." Document dated April 24.

In certain locales, the government sets social investment targets that the companies must meet either through lump-sum payments or pay-as-you-go levies. One such case is Angola. In 1982, the Government of Angola signed a decree requiring oil companies to allocate \$0.15 per barrel of oil produced to Training Levy Funds. Later, in 1997, a penny per barrel of this training levy was decreed to be allocated to higher education through the Agostinho Neto University and the new Catholic University. Estimates are that this could have yielded some \$3 million for each university.<sup>27</sup>

Finally, efforts to develop human capital are most effective when devised within a company's broader strategy to expand economic opportunities. In Rio Tinto's Diavik Diamond Mine in Canada's Northwest Territories, human capital development initiatives directly contribute to the company's overall strategy for increasing Aboriginal and local participation in its workforce. Through a host of programs both within and outside of the company, local residents receive targeted training to enhance their technical skills and participate in apprenticeships, mentoring, and leadership programs that help them advance their careers with Rio Tinto and its contractors. With their enhanced skill sets, these individuals can benefit from expanded career opportunities both within and outside the extractive industry.

### **4.3 Building Institutional Capacity**

Extractive companies are engaged in a variety of activities that build the external institutional capacity that is often necessary for expanding economic opportunities in developing countries. These efforts include supporting industry associations, both in extractives and in other fields, providing funding for universities, and strengthening the managerial and oversight capabilities of government agencies, civil society organizations, and grassroots groups – all of whom must be able to play their roles effectively within the system that determines the availability of economic opportunity for the poor.

#### **BOX 5 THE URBAN DEVELOPMENT ALLIANCE: SIBERIAN-URALS ALUMINUM COMPANY (SUAL)**

The Urban Development Alliance is a public-private alliance aimed at encouraging civic activism in small towns where the Siberian-Urals Aluminum Company (SUAL) is the main industry. In 2003, SUAL approached the United States Agency for International Development (USAID) with the idea to rebuild the local economy in a sustainable way by improving the environment for enterprise development, working with local banks and investors to fund a micro-credit facility, providing technical assistance and training to local government for business transparency, and establishing local capacity to sustain improvements. This collaborative project pools together the resources of USAID and SUAL which are contributing \$1 million and \$1.25 million respectively to meet the alliance's objectives. For SUAL, the alliance leverages additional expertise and cash resources for its own social investments in the communities where its workforce resides.

USAID. 2006. "The Urban Development Alliance: Improving Service Delivery through Partnership." *The Global Development Alliance: Public-Private Alliances for Transformational Development*. Pages 71-75.

There are numerous examples of programs that provide capacity-building services for SMEs, although these efforts remain mostly outside of the industry's own value chains – aiming instead to diversify national economies more generally and reduce host country dependence on the industry. Chevron's Angola Partnership Initiative, for example, has devoted considerable resources to develop the country's agricultural sector as a way to create income generation opportunities for the vast majority of the population, and at the same time help reduce dependence on the extractive industry. Chevron's programs have built the technical knowledge of farmers to help improve their yields while also helping them diversify and begin producing higher-value crops (see the case profile on Chevron's Angola Partnership Initiative in this report).

Another category of activity that falls under the umbrella of institutional capacity-building is the creation of support systems for local private sectors, including business associations, enterprise centers, and banks. These collective mechanisms serve the important function of facilitating knowledge transfer and sharing of best practices among local entrepreneurs. Perhaps most important is the role that these associations play as advocates for local business interests.

In Angola, Chevron helped create 32 associations of over 3,000 small agricultural producers. These associations serve as conduits for training and technical assistance as well as wholesale negotiators of collective sales contracts. In Peru, Newmont's Minera Yanacocha created and is funding the Asociación Los Andes de Cajamarca (ALAC) whose purpose is to support sustainable development in the region. ALAC is currently the beneficiary of IFC technical assistance aimed to strengthen its capacity to serve as a local business and community advocate and supporter for many years to come. In Azerbaijan, BP has created the Baku Enterprise Center to support the development of local companies as potential suppliers. The center provides technical assistance to help participating SMEs meet bidding and other procurement requirements within BP's local value chain.

#### **4.4 Helping to Optimize the "Rules of the Game"**

Extractive companies can create economic opportunity through inclusive business models that expand access to indigenous vendors and downstream agents as a result of new business processes, through community-level

investments and initiatives that build human capital and institutional capacity, and through influencing the policy and regulatory environments in which SMEs operate. This last opportunity is often the least utilized. Extractive companies often create firewalls between governmental interactions that are a part of their business operations and those they undertake – often in partnership with government, NGOs, and other stakeholders – to address broader social and economic goals. They are often reluctant to “play in the policy space” due to concerns about perceived self-interest or conflict of interest and the desire to maintain harmonious relationships with host governments.

Often as a result of “obsolescing bargaining power”<sup>28</sup> dynamics, extractive companies are generally slow to engage in large-scale efforts to change the “rules of the game,” especially on an individual, company-by-company basis, because they are seeking either to win or retain exploration and production concessions from host governments. Some companies also claim that binding concession agreements mean that their influence with host governments is more limited than some assume. While they are key players in the local and global economies, multinational extractive companies may feel more like guests than legitimate partners in national-level economic growth challenges.

#### **BOX 6 THE SOUTH AFRICAN MINING CHARTER**

**The South African mining industries have long been dominated by white capital. The South African Mining Charter seeks to achieve 26% ownership of mining companies by previously disadvantaged people within the next 10 years. A key component of the Charter is a scorecard that helps mining companies comply with the Mineral & Petroleum Resources Development Act, which encourages them to promote black economic empowerment when applying for new mineral rights or converting current rights. The scorecard focuses on direct empowerment through ownership and control of enterprises, human resource development, and indirect empowerment through preferential procurement and enterprise development.**

Department of Minerals and Energy, Republic of South Africa. 2002. “Broad-Based Socio-Economic Empowerment Charter for the South African Mining Industry.” [http://www.dme.gov.za/minerals/min\\_miningcharter.stm](http://www.dme.gov.za/minerals/min_miningcharter.stm) (accessed November 26, 2007).

While extractive companies may participate in dialogue on enabling environments for economic opportunity expansion, often their most direct methods for doing so are participation in and support for industry associations, local civil society organizations, and local business associations who, in turn, undertake public policy-shaping initiatives.

In Cajamarca, Peru, where Minera Yanacocha is located, Newmont and IFC worked together with local authorities to streamline their procedures for registering new businesses and reduce the associated fees. Local authorities undertook an administrative simplification process that created a “one-stop shop” for licensing and registration services, drastically reducing the number of days it took to register a small business from 100 to three. In addition, previous licensing fees averaged \$163, close to 8% of the annual per capita income in Peru, and were prohibitively expensive for micro and small business owners. As a result of the simplification project, the government was able to reduce these fees by 15% (see the case profile on Yanacocha in this report).

Increasingly, extractive companies also participate – individually and collectively – in multi-stakeholder governance and accountability mechanisms to help ensure that the economic benefits and opportunities associated with their work are shared more widely. The Extractive Industries Transparency Initiative (EITI) is a multi-stakeholder initiative including governments, extractive companies, and civil society representatives

who support improved governance in resource-rich countries through the publication and verification of company payments and government revenues from oil, gas, and mining. EITI was initially proposed by former British Prime Minister Tony Blair, who announced the initiative at the World Summit on Sustainable Development in Johannesburg in September 2002. Over 20 countries have committed to the EITI and they are currently at different stages of the implementation process.<sup>29</sup> The EITI's roll-out has been uneven and a bit slow as, among other challenges, it requires involvement from both public and private institutions and actors. Its premise is that transparency in resource allocation benefits not only the poor but also foreign investors and host governments. There is room for more public-private partnerships not only to improve the "rules of the game" but also to enhance the impact of corporate investments in human capital development, institution-building, and inclusive business operations.

## 5 ■ Opportunities for Industry-Wide Collaboration in the Extractive Sector

Companies in the extractive sector enter into joint venture and consortium arrangements frequently. They work together by necessity due to the magnitude of certain investments and the complexity of existing or newly earned concessions. Often the joint venture lead will determine the focus and level of community investment and local economic development efforts, and individual companies will use their own processes to fulfill their allocated responsibilities under the project. Less frequent is the blending of business processes across companies to enhance local content, or the harmonization of community investment across all aspects of large projects with multiple companies involved.

In addition, there are not enough mechanisms for consortia from different investments in a region or across the globe to coordinate their efforts and approaches. An example is the parallel work by Shell and Chevron in the Niger Delta, where each company is investing in governance structures for community development on its own separate track. It has been difficult for the companies themselves to forge a unified process; they might benefit from third-party involvement in the form of a public-private partnership focused on the common causes of local economic growth and stakeholder engagement. Such a partnership would also enable them to tap into the efficiencies of collaboration in terms of capacity-building and governance support costs.

### **BOX 7 INDUSTRY-WIDE COLLABORATION IN ANGOLA FOR SUPPLIER TRAINING**

**BP, Sonangol, ExxonMobil, Chevron, and Total have collaborated in a supplier training initiative to launch a business support center, Centro Apolo Empresarial (CAE), in Luanda, Angola. The center, launched in September 2005, has generated positive results in the two years it has been in operation by employing more than 65 local individuals, increasing the number of contracts for participating SMEs, training 547 SME participants, and providing in-kind consulting services valued at more than \$330,000.**

Glin, C. D. 2007. "Strengthening Local Content in Nigeria: Prepared for Chevron Nigeria Ltd." Citizens Development Corps. Presentation dated April 30.

The benefits of collaboration are obvious even though the methods for effectively achieving it are less so. When significant investments need to be made in building human or organizational capacity at the national or regional level, these costs can be shared rather than shouldered by a few, and the benefits can also accrue broadly to many extractive companies and many communities, beyond those immediately adjacent to a given site. In addressing enabling environment issues, extractive companies acting together – in bilateral partnerships, through nationally-hosted platforms such as chambers of commerce or industry or mining, trade associations, or issue-specific groupings – can be more powerful and less politically vulnerable because they provide a collective voice on systemic and sometimes sensitive issues.

Specific opportunities for collaboration can include co-investment in strengthening engineering, business, accounting, and planning departments in local universities, as is happening in Angola, Nigeria, Kazakhstan, China, Saudi Arabia, and the West Indies. Foundational investments in education and technical-vocational

training at the national and regional levels can be harmonized and shared not just among extractive industry investors, but also among offshore and national investors and large businesses in other industries. Another promising option for collaborative action is co-investment in girls' and women's education and managerial/leadership training – such as joint support for the Asian University for Women in Bangladesh – as a primary contribution to economic empowerment and the creation of a larger pool of potential female employees.

Extractive companies can also collaborate with partners to establish innovative financing mechanisms and joint technical assistance initiatives to support local economic development. In mid-2007, for example, a group of 20 mining, resource finance, and supporting companies joined with the Clinton Foundation to launch the Clinton Giustra Sustainable Growth Initiative. Launched with initial commitments of \$100 million each from Canadian mining leader Frank Giustra, Mexican businessman Carlos Slim, and the Lundin Group of Companies, this initiative aims to work with mining-related companies, governments and other development partners to build sustainable local economies in developing countries, with an initial focus on Latin America.

Closer to immediate business operations, there is potential to increase joint supplier training courses like those being conducted in Angola by BP, Chevron, ExxonMobil, and the national oil company Sonangol. A number of large first-tier suppliers such as Bechtel and Schlumberger are also involved. The BP case described later in this report involves some industry-wide collaboration in sourcing inputs in Trinidad and Tobago. In Azerbaijan, there has been joint support and cost-sharing among ExxonMobil, BP-Amoco, and the former UNOCAL (now part of Chevron) for similar supplier training programs.

To strengthen organizational capacity and enable extractive sector resource flows to reach the poor more directly, industry players can join forces to build multi-stakeholder governance and accountability mechanisms that will serve their own interests as well as the public good. Examples of such mechanisms include work under the South African Mining Charter and the EITI.

Another collaborative effort, less squarely focused on economic opportunities, is the Voluntary Principles for Human Rights and Security. This is a collaborative effort among bilateral donors, NGOs active in the human rights arena, and extractive companies that allows for sharing of operational best practices contributing to mitigating conflict, safeguarding workers and communities in and around industry sites, and allowing for sustainable livelihood activities.

While there are opportunities for industry-wide collaboration, the mechanisms for collective action are not well developed. Extractive sector first-movers need to provide leadership for joint action. Business-to-business coordination and sector-wide support of intermediary service and advocacy organizations are both useful approaches.

## 6 ■ Conclusions

Extractive industry portfolios are not portable. Companies invest in geographies endowed with resources whether they be swamps in the Niger Delta, tsunami-prone Asian countries, economies in transition or with weak governance structures, or remote locales without supporting local economies or sufficiently skilled entrepreneurs. They generally invest long-term despite mergers, acquisitions, and shifts in joint venture and local partners. Their costs of production and ease of operations are materially affected by local economic conditions. Extractive companies recognize that “a rising tide lifts all boats.” To the extent that local individuals, communities, and host nations are experiencing greater economic opportunity, companies’ production costs and local and regional sales may be positively affected. If companies are not only taking advantage of greater economic opportunity but also are seen as contributing in significant ways to it, their reputations and social licenses to operate will benefit.

Despite the business case and the potential to have meaningful impact, an explicit focus on expanding economic opportunity is not clear or integrated in most extractive companies. Some industry players have begun to make the business case for local economic opportunity expansion, leading to effective leadership in business practice and public policy engagement. Often, enlightened practices are not system-wide, even within a single company. Headquarters-level units on issues such as local content can be useful. However, these units most often have the authority to set standards and targets, share best practices, and provide assistance and encouragement to increase local sourcing, but do not undertake procurement themselves. Sourcing and decisions related to sourcing still rest largely with business units spread across the globe. Beyond sourcing, stove-piped investments in training, capacity-building, livelihood generation, and policy dialogue also run on parallel tracks within large, decentralized corporations. Procurement, marketing, sales, corporate citizenship, and recruitment units within companies all make contributions to enhancing economic growth and opportunity, but most often not in a purposefully harmonized manner.

In addition to the obstacle of integrating approaches within any given extractive company are the challenges of uniting different extractive companies in consistent approaches and joint programs. While they often partner in large joint ventures, competitors generally do not combine forces in functional areas to achieve consistency, economies of scale, or synergies.

There is great opportunity for the industry to scale up proven approaches to creating economic opportunity, such as those profiled in the case studies in this report. Specific suggestions for the way forward include a variety of intra- and inter-firm initiatives.

## 6.1 Intra-firm Opportunities

- Send strong signals that economic opportunity creation is in a company's best interests – for instance, through performance contracts, incentives, and CEO statements – and give examples of what this means.
- Share experiences and standardize, where possible, approaches to business inclusion of SMEs, local capacity development, and improving the “rules of the game” – upstream and downstream, from community investment to recruitment, and across geographic business units.
- Focus special attention on women and youth. Disproportionate benefit can come from effective extractive industry investment in creating economic opportunity for those that have the least access and greatest need. Broad-based community economic opportunity programs will not have the specificity and reach for these vulnerable groups. To target women and youth, make it a priority, hold people accountable, and measure the results.

## 6.2 Inter-firm Opportunities

Establishing stronger and more frequent inter-firm partnerships would allow extractive companies to benefit more fully from and contribute more substantially to expanding economic opportunity in developing countries and emerging markets.

- Collective action in support of multi-stakeholder governance and accountability mechanisms is critical. This can be implemented through industry-industry cooperation and through support for intermediaries.
- Cost-share in core investments in human capital development and communicate on programs and priorities at the regional, national, and global levels.
- Share best practices among extractive companies to increase the efficiency and scalable impact of economic opportunity investments.

## 7 ■ Extractive Industries Profiles

What follows is a series of snapshots highlighting extractive industry initiatives that promote economic opportunity. Among these vignettes, Chevron's alliance in Angola demonstrates the economic impact of putting community engagement resources to work strategically. The Anglo Zimele story in South Africa underscores the importance of having an exit strategy or transitioning options particularly when assuming non-traditional roles, such as in finance. The Rio Tinto example from Canada illustrates best practice in creating economic opportunity for targeted segments of the population, in this case the Aborigines. The Newmont case from Peru points to the utility of stakeholder engagement and partnership to leverage the assets and expertise of organizations like IFC. The BP story makes clear the challenge and benefits of investing in local capacity development. ExxonMobil shows adoption of company-wide local content approaches and their application in Russia. There are many additional examples; these few have been chosen to provide geographic and sectoral diversity of experience. These good practices could be the basis for wider cross-industry partnerships and scalable inclusive business models.

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## 7.1 LOCAL SUPPLY CHAIN DEVELOPMENT: BP IN TRINIDAD AND TOBAGO<sup>30</sup>

**Background** BP has operated in Trinidad and Tobago since 1961 and bpTT, its local subsidiary, today produces 70% of the country's petroleum. The company's business strategy highlights bpTT's aim to be "a distinctly Trinidad and Tobago business with sustained returns." At the turn of the century, bpTT sought to align its business strategy with the country's goal of transitioning from a developing to a developed economy by 2020. As a major player in Trinidad and Tobago's upstream sector, bpTT committed to supporting local capacity development to meet its own upstream services needs with the long-term objective of building the country's upstream services sector more broadly.<sup>31</sup>

**Drivers** bpTT's decision to support the creation of a sustainable local upstream services sector carried a sizeable upfront investment. According to company estimates, the first platform designed and fabricated locally had a premium cost of nearly \$10 million over the cost of production in Louisiana, where the company's previous platforms were developed.<sup>32</sup> However, the company estimated that local design, fabrication, and installation of its platforms had the potential to generate substantial savings over overseas production in the long run. Coupled with bpTT's commitment to contribute to the sustainable development of Trinidad and Tobago, these expected long-term business benefits served as a key driver for bpTT's decision.

It was also important for bpTT to strengthen its identity as a truly local company in Trinidad and Tobago by helping to support a growing local services sector and integrating it fully into its supply chain. Given the company's position as a leader in the national oil and gas industry, identity was an especially important driver.

**Activities** bpTT's efforts to develop a sustainable local supply chain in Trinidad and Tobago commenced with the planning and implementation processes for a new offshore gas extraction platform, the Cannonball. bpTT strongly believed that successful implementation of the \$54 million project utilizing a local supply chain would generate long-term benefits not only for the company, but also for the country's economy. The following key activities were implemented:

- *Joint venture creation:* bpTT encouraged the creation of two primary joint ventures to be engaged during the principal stages of the Cannonball project. The joint venture structure was important in order to facilitate the transfer of technology, knowledge, and skills between foreign and local partners, provide the necessary technical capacity, and facilitate seamless implementation of the project using the local partner's knowledge of conditions in Trinidad and Tobago. The first joint venture, Fluor/Summit, was formed between the US-based Fluor Corporation and the local company Summit to provide engineering and construction management services. The second joint venture, Trinidad Offshore Fabricators Unlimited (TOFCO), was formed between US-based Chet Morrison Contractors Inc. and the locally-owned Weldfab Limited to fabricate the Cannonball platform at the La Brea industrial park in southern Trinidad.
- *Human capital development:* To meet the highly-specialized needs of the design, fabrication, and installation processes, technical training programs were implemented by Summit and TOFCO. Foreign experts conducted formal training sessions, but also provided individual mentoring to augment the professional skills of local staff. In addition, bpTT also trained its staff in project and supply chain management skills, contributing to their increased capacity.
- *Sector-wide alliance:* The long-term sustainability of Trinidad and Tobago's upstream services sector depends not only on the development of appropriate technical capacity, but also on the support of major industry players willing to include local companies in their own supply chains. To bolster the impact of its efforts, bpTT helped form an alliance of businesses, professional, and educational institutions in the oil and gas sector whose primary objective is to help increase local participation in the sector through the creation of backward and forward linkages with local companies.<sup>33</sup>

## Results

Construction on the Cannonball project started in 2002 under the slogan “Do it local, define the future.” By 2006, the platform produced its first commercial gas. In 2005, bpTT engaged the same local firms to design and fabricate two new platforms, Mango and Cashima. bpTT expects new production by these platforms in late 2007.

- *Local competitive advantage:* Since the successful completion of the Cannonball project, TOFCO was contracted to build additional platforms for BHP Billiton and EOG Resources as well as the newest bpTT Mango and Cashima platforms. Through these engagements, the company now has a broad client base among the major players in Trinidad and Tobago’s oil and gas industry. Furthermore, bpTT awarded the Mango and Cashima contracts to TOFCO and Fluor/Summit over a number of foreign competitors who also participated in the bidding process. That award decision further emphasized the competitive advantage of the local companies.
- *Process improvements:* In building Mango and Cashima, bpTT adopted BP’s international strategy of standardization which allows for the design and construction of the same model with adjustments made when necessary. As a result of the supplier’s previous experience, process improvements resulted in a production time reduction, productivity increases, and cost reductions for bpTT in comparison to Cannonball. Mango and Cashima generated \$11 million in design cost savings alone, compared to Cannonball. In addition, process improvements reduced fabrication time from 16 months for Cannonball to 12 months for Mango and Cashima and reduced total engineering and procurement hours by 38% and 61% respectively, when compared with Cannonball.<sup>34</sup> The development of an efficient local supply chain will allow bpTT to generate further substantial savings over the next 20 years as it expands its production in Trinidad and Tobago.
- *Capacity-building and employment opportunities:* For the first time in bpTT’s history, a project of Cannonball’s size was led by a Trinidadian general manager. The same professional was also responsible for the construction of the subsequent Mango and Cashima platforms. In addition, a majority of bpTT staff who worked on the Cannonball project were also engaged in the Mango and Cashima projects. In all three projects, 65% of management hours were contributed by local bpTT staff.

Project suppliers also worked to increase the capacity of their local staff. During the design and fabrication stages of the Cannonball platform, 40 design and 185 fabrication professionals received specialized training from Fluor/Summit and TOFCO. In addition, local employees were responsible for over 80% of Cannonball’s fabrication hours and 45% of the engineering, including detailed design. Through training and direct experience, local employees have now developed stronger technical skills in design, welding, fabrication, procurement, construction, and project management, thus enhancing their ability to collect higher returns for their work.

The continuous flow of major contracts for TOFCO has created additional employment opportunities for members of the immediate local community. An estimated 40% of TOFCO’s workforce is comprised of inhabitants of La Brea and the surrounding region.<sup>35</sup> In addition, growing activity at the fabrication yard has spurred the development of new small and medium businesses that provide additional services to TOFCO and its employees, thus resulting in higher levels of employment for the region, which was previously underdeveloped.

A primary expectation is that enhanced local capacity will foster the development of adjoining industries, such as a ship-building, which can leverage the complementary skills of the local workforce and the infrastructure developed for the production and installation of oil and gas platforms.

## Lessons

*Overcoming the obstacles of upfront costs:* BP made a strategic decision to indigenize sourcing. This was important to provide the resources and support to source platform equipment from a local supplier. Had this vision and commitment not been embedded in procurement decision-making, investment in local suppliers and the resulting longer-term savings would not have occurred. As a one-off decision, offshore procurement would have been more cost-effective. A corporate commitment to local sourcing and a framework to measure savings over time are essential to making the business case for such a change in practice.

*Industry collaboration:* Trinidad and Tobago's upstream services sector is developing as a result of industry-wide support. For instance, coordination among key industry players has generated a staggering of fabrication orders for TOFCO, thus creating a continuous flow of contracts for the company and contributing to its sustainability and steady growth.<sup>36</sup> Sharing the costs and benefits of sector-wide capacity-building investments not only benefits the majors but also provides a steadier pipeline of market opportunities for local suppliers.

*Replication opportunities:* bpTT's success has led BP to consider the possibility of replicating its local supply chain development model in other countries, such as Angola. Efficient local supply chains have the potential to generate significant savings while also strengthening the company's social profile in the countries where it operates.<sup>37</sup>

*Can upstream lessons flow downstream?* Similarly, BP believes successful strategies designed and implemented in upstream operations may be replicated in the downstream business by applying lessons learned to blending, post-refinery, transportation, and retail operations. While the manufacturing content of exploration procurement is generally greater, techniques such as signaling to local industry, capacity-building investments, and procurement criteria other than price could apply to downstream operations as well. The challenge remains framing and communicating the benefits generated by the local supplier approach throughout a widely dispersed energy company and among other competitors in the industry.

## 7.2 ANGLO ZIMELE: ANGLO AMERICAN IN SOUTH AFRICA<sup>38</sup>

**Background** Launched in 1989 as the Small Business Initiative, Anglo Zimele (meaning “to be independent” or “to stand on one’s own feet”) is the enterprise development and empowerment effort of mining company Anglo American in South Africa. Anglo Zimele’s key objectives are to provide access to mainstream business opportunities for historically disadvantaged South Africans; create sustainable, commercially viable enterprises driven by people with passion and entrepreneurial spirit; and contribute to the sustainable development of mining communities. Anglo American supports additional community development programs that generate livelihoods and provide micro-financing at the local level; however, Anglo Zimele’s goal is to effect larger-scale change by strengthening a diverse and vibrant private sector in South Africa.

**Drivers** Anglo American was founded in South Africa in 1917 and has since been a major contributor to the country’s economy. The company saw the Small Business Initiative and subsequently Anglo Zimele as an opportunity to create local capacity that could efficiently support Anglo American’s non-core product and service needs. The ability to outsource to external firms allowed Anglo American to concentrate its efforts on its core business. As a result, the company could generate substantial long-term business gains. Also important, Anglo Zimele would play a key role in increasing employment and entrepreneurial opportunities for historically disadvantaged South Africans. Its Small Business Initiative would help the company meet its obligations to engage black economic empowerment (BEE) enterprises in its business activities and realize its requirements under the South African Mining Charter in the areas of procurement, human resources, mine community, and rural development.

**Activities** Anglo Zimele’s activities have focused on three primary areas: providing business development services aimed at strengthening the capacity of local businesses, creating procurement opportunities to facilitate the inclusion of these firms in Anglo American’s value chain, and finally, supporting local participation in South Africa’s mining industry through start-up funding.

*Capacity-building:* Like other small and medium enterprises, black-owned firms in South Africa face the significant challenge of securing financing for their start-up and growth efforts. Anglo Zimele helps mitigate this challenge by providing both equity and loan financing to the enterprises it supports. Its minority stakes of about 20-30% guarantee it board representation, thus allowing Anglo Zimele to exert a positive influence on the strategic and managerial direction of the companies it supports. In addition to the equity investing, Anglo Zimele facilitates the provision of loans to meet companies’ additional financing needs; however, these loans carry commercial terms and require careful management by the recipients.<sup>39</sup>

Anglo Zimele uses a rigorous due diligence process when selecting its portfolio companies. Key requirements include commercial viability and growth potential, as well as ownership by a BEE entrepreneur or significant partnership with a BEE. Existing commercial viability is important because it allows Anglo Zimele to focus on further bolstering the companies’ existing expertise to generate significant future growth. Anglo Zimele provides a range of business support services, such as skills transfer and strategic guidance on business principles, marketing, legal issues, corporate governance, and health, safety, and environmental management. It uses an incubator approach to nurture investments and entrepreneurs, matching up partners and businesses, and complementing technical skills. Matched with the commitment of the entrepreneurs, Anglo Zimele’s hands-on support generates significant results that allow it to exit its investments within a pre-determined timeframe of approximately three years. Specific timeframes are stipulated in each shareholding agreement entered by Anglo Zimele.

*Value chain involvement:* Directly related to Anglo American’s value chain, Anglo Zimele works closely with the company’s various divisional supply chain personnel to identify procurement opportunities for BEE suppliers, including black-owned and/or black-managed SMEs. Procurement contracts are awarded purely on commercial merits to companies that satisfy quality, price, service, and delivery requirements and generate cost savings for Anglo American. While Anglo Zimele provides hands-on support and coaching to facilitate SME participation in

bidding procedures, it also strongly encourages the diversification of the SME's client base to include other major companies operating in South Africa.

*Industry expansion:* Launched in 2003, the Anglo Khula Mining Fund is a 40 million rand joint initiative between Anglo American and Khula Enterprise Finance, run out of the government Department of Trade and Industry. The Fund's objective is to facilitate the entry of junior, but potentially commercially viable, mining enterprises into the mainstream mining sector. The Fund provides a maximum of 7.5 million rand in seed financing to assist new mining ventures during the pre-feasibility stages of their operations,<sup>40</sup> such as exploratory drilling, preparation of environmental reports, or application for permits and licenses. Once these initial prerequisites are met, the ventures are positioned to find commercial sources of financing in the marketplace.

## Results

Since 1989, Anglo Zimele has invested in some 150 enterprises through equity and loan financing. During 2006, Anglo Zimele invested in 14 new and existing BEE enterprises in a variety of sectors including education and training, mining supplies, pallet manufacturing, drilling consumables, tire maintenance, corporate advisory services, and various engineering disciplines. That same year, the Anglo Khula Mining Fund approved three new mining ventures. As a result of these engagements, Anglo American's BEE spending increased by 37% from the previous year reaching 12.6 billion rand, including over 11 billion rand in direct procurement contracts with BEE enterprises.<sup>41</sup>

An additional important outcome from Anglo Zimele's business development activities is the creation of employment opportunities for South Africans hired by the new or growing enterprises in which it invests. As of 2006, these companies employed over 2,200 people.

Attesting to the success of Anglo Zimele's capacity-building efforts, firms supported by the program have a 72% survival rate over an eight-year period, according to a survey conducted in 2005.<sup>42</sup>

## Lessons

*Strict criteria for investments:* Enterprises must be commercially viable prior to investment; realistic business plans are essential and reducing dependence on a single large buyer should be an ongoing goal. In addition, the impact of investments of this scale and scope will be substantially reduced if participant talent, motivation, and commitment are missing at any point in the engagement process.

*Importance of debt-equity-technical assistance:* The combination of equity and debt financing not only meets the funding needs of participating enterprises but, coupled with technical assistance, it also allows entrepreneurs to develop complex management and finance skills, thus allowing them to pursue diverse funding streams following their engagement with Anglo Zimele.

*Explicit exit strategy:* Investments and the entrepreneurs behind them require intensive support in the early stages, but dependence must gradually be reduced, and the investor must have a clear exit strategy. A clear timeframe for exiting investments can lead to clear strategy formulation and implementation, including the development of measurable targets, time-specific goals, and systematic performance monitoring and evaluation.

*Potential for replication:* The Anglo Zimele model may be replicable to other locations. Anglo American has initiated a similar program in conjunction with its operations in Chile, and is considering the possibility elsewhere in South America, China, and Eastern Europe.

## 7.3 EXXONMOBIL'S NATIONAL CONTENT STRATEGY: WORLDWIDE AND SAKHALIN, RUSSIA<sup>43</sup>

### Background

ExxonMobil has been engaged in developing local economies for decades, especially through its affiliates operating in developing countries. Based on the successes and learnings of these individual efforts, ExxonMobil formulated a company-wide initiative known as the “National Content Strategy” with a central goal “to ensure that [its] presence in a host nation helps develop human, social and economic capacity – content that benefits its people, communities and businesses over the long-term.”<sup>44</sup> Supported at the highest levels of leadership in the company, the national content strategy is considered a key business enabler at ExxonMobil and is a visible strategy in places like Chad, Malaysia, Russia, and others. According to Jean A. Baderschneider, Vice President of Global Procurement and Co-Chair of the National Content Team, ExxonMobil understands that “one of the most important contributions we make to the countries where we operate is supporting economic growth and improving the quality of life.”<sup>45</sup> Baderschneider views the company's national content strategy as an important factor in increasing the company's contributions to local economies.

### Drivers

ExxonMobil's national content strategy came about because the company recognized the need to replicate successful experiences instead of developing ad hoc programs from project to project. A comprehensive, company-wide initiative allows ExxonMobil to identify best practices and design interventions that can be executed – with the necessary modifications – in different contexts.

Most importantly, ExxonMobil's national content strategy is incorporated as an important component of the company's business processes. The expansion of national content is considered a strategic objective for ExxonMobil and its affiliates around the world and is pursued through tangible and definable interventions. ExxonMobil measures the impact of this strategy rigorously.

This level of priority is possible because the company recognizes national content as a strategic imperative that enhances long-term economic efficiency, as it “fosters the continuous development of a reliable and sustainable local supply chain” and allows “projects and affiliates [to] benefit from the experience of suppliers that understand the local business and operating environment.”<sup>46</sup> In addition, the strategy creates shared value for ExxonMobil, which benefits from strong, local supply chains, and for local economies, which lay the foundations for long-term growth.

### Activities

ExxonMobil has implemented its national content strategy through direct investments, knowledge and skills transfers, local goods and services procurement, local job creation, and education and training for employees, contractors, and suppliers.

These individual contributions are organized in three key areas: workforce development, supplier development, and strategic community investments.

*Workforce development:* Interventions focus on training employees in technical and professional skills that are needed for existing and future projects and operations. For the past 25 years, the company has offered a technician training program for local employees in Malaysia. Over 1,000 skilled technicians have participated in these trainings, making an important contribution to the development of the local workforce.<sup>47</sup>

*Supplier development:* Activities aim to expand capabilities and assist suppliers in meeting ExxonMobil's global standards in order to qualify for contracts with the company and its affiliates, as well as other players. For example, as part of its supplier development efforts in Chad, ExxonMobil in collaboration with IFC trained 200 suppliers to pursue business contracts through the company's electronic bidding system. As a result, a local company won a \$600,000 bid for a services contract with the company's local affiliate.

*Community investment:* Programs support infrastructure growth and improvements, but also contribute to important health and educational programs benefiting local communities. An example of this type of contribution is the Africa Health Initiative, whose goal is to assist countries in sub-Saharan Africa, particularly those hosting major ExxonMobil operations, in meeting their target of reducing malaria-related mortalities by 50% by 2010. Aside from financial contributions, which reached \$9 million in grants in 2006, ExxonMobil is also helping develop

the capacity of local entities to meet the challenges posed by malaria outbreaks. The company is sharing with local health service providers the knowledge and competencies it has developed over years of operations in Africa, especially in distribution logistics, to increase their capacity to manage the pandemic over the long term.

## Results

As a result of its concerted effort, ExxonMobil has contributed to economic welfare and created income-generating opportunities in local communities not only through direct employment, but most significantly through the development of local supply chains. For example, 98% of ExxonMobil's workforce in Malaysia in 2006 was comprised of local employees. In addition, during the same year, the company spent \$371 million on procurement from local suppliers. Similarly, the company's contributions to the improvement of the health and educational systems of various countries have also contributed to the quality of life and long-term prospects of local communities.

ExxonMobil has committed to continue rolling out its national content strategy in the company's developing and operating areas throughout 2007. To support this effort, the national content team has developed an internal handbook with models, tools, and best practices that will help local managers replicate and adopt best practices in new projects. Similarly, the company's internal website now includes a dedicated section focusing on workforce development, community investment, and supplier development efforts. In addition, the website features several detailed case studies of successful implementations of the national content strategy highlighting both challenges and lessons learned. Whereas earlier national content efforts relied heavily on the knowledge of individual ExxonMobil professionals with previous experience in such projects, this new knowledge-sharing system institutionalizes the expertise, allowing ExxonMobil to better implement its company-wide strategy. The improved flow of information has allowed ExxonMobil managers to replicate and adopt best practices and also make improvements, thus accelerating the growth of the company's local suppliers and increasing its contribution to strengthening local economies.

## BUILDING ON EXPERIENCE: THE CASE OF SAKHALIN-1

### Background

With initial exploration efforts starting in the early 1990s, Sakhalin-1 is one of the largest foreign direct investments in Russia and is expected to generate over \$50 billion in revenues for the Russian government. The ExxonMobil-led consortium is also contributing to significant improvement in the region's infrastructure, facilitating important technology transfers to local companies, and is engaging numerous Russian suppliers to meet contract and procurement needs for the project.

### Activities<sup>48</sup>

In order to meet its Russian content objectives, ExxonMobil is implementing a national content strategy for Sakhalin-1 that draws from the company's past experiences in different countries and builds on its best practices. Key activities in Sakhalin include the launch of a project website to serve as an information and communication gateway for local contractors and suppliers; a series of training seminars on project requirements to increase local supplier capacity; encouraging active Russian participation in the project design process; creating and maintaining a comprehensive database of local contractors; and developing key contract packages to encourage Russian participation.

*Supplier development:* ExxonMobil organized training and development seminars for Russian suppliers and contractors in Khabarovsk, Yuzhno-Sakhalinsk, and Moscow to strengthen their qualifications. The trainings aimed to inform suppliers and contractors about the Sakhalin-1 project and its design codes and standards, qualification and bidding procedures, and project objectives. Based on previous experience, these trainings are crucial in expanding the capacity of local companies and enhancing their ability to participate in complex procurement processes employed by large multinational companies such as ExxonMobil.

*Access to information:* A comprehensive website in both Russian and English was also developed to better disseminate information about the Sakhalin-1 project among local suppliers and contractors. The website

includes special sections outlining the project's procurement process, primary selection criteria, and key project contacts, as well as providing easy access to the vendor registration and employment registration forms.

*Supplier and vendor engagement:* In order to facilitate the utilization of Russian suppliers and vendors, ExxonMobil conducted an identification and qualification process for local companies. In conjunction with the Petroleum Advisory Forum-chartered Russian Sourcing Industry Work Group, ExxonMobil surveyed over 100 Russian suppliers. As a result of this analysis, ExxonMobil was able to identify qualified local companies that could be contracted to provide goods and services for the Sakhalin-1 project. The survey also identified companies that required additional training to meet ExxonMobil's technical requirements.

In addition, ExxonMobil has developed and maintains a comprehensive vendor database that currently includes information on approximately 3,500 local companies. With data collected through different sources, including a self-registration process facilitated through the project's website, the database is used by the project and its main contractors to identify possible suppliers and subcontractors.

*Design process:* In order to increase its compliance with local codes and standards, ExxonMobil engaged with the Russian Design Institutes (RDIs) at the early stages of designing Sakhalin-1. The process has been valuable to both parties as it has allowed for a sharing of experiences and knowledge to guarantee compliance with both Russian and international codes and standards.

*Contract design:* ExxonMobil and its partners have taken deliberate steps to tailor major Sakhalin-1 contracts in a way that encourages the participation of Russian companies. Local businesses can participate as principal suppliers and contractors, as subcontractors, or through joint-venture arrangements with international companies. Evaluation teams, which include all consortium representatives, assess Russian content plans as key components of all bids and proposals, along with other important commercial and technical factors.

*Collaboration:* ExxonMobil has also engaged both local and national authorities to bolster its efforts to increase national content in the Sakhalin-1 project. In collaboration with the local Sakhalin government administration and the Ministry of Economic Development and Trade of the Russian Federation, the company has established a Joint Committee on Russian Content whose primary objective is to assist in maximizing the involvement of Russian subcontractors and suppliers. Some of the committee's contributions include assisting the company develop criteria for assessing Russian ownership of contractors and suppliers, determining the selection process for certain types of contracts, and proactively monitoring the inclusion of Russian businesses. Perhaps most significantly, the committee serves as a conduit for information-sharing between ExxonMobil and Russian stakeholders, which has been particularly helpful in managing expectations and effectively communicating ExxonMobil's national content strategy.

## Results

*Workforce development:* During the peak of construction activities in the summer of 2005, Sakhalin-1 employed approximately 8,000 local workers, including direct employees and contractors. ExxonMobil's affiliate in Sakhalin employs approximately 350 local employees, many of whom have participated in professional development and training programs in Russia, the US, and Canada. As the skills and knowledge of the local workforce increase, ExxonMobil expects the number of Russians working in the Sakhalin-1 project to approach 90% of the workforce in the next 10 years.

*Benefits for Russian companies:* Through ExxonMobil's national content strategy, the Sakhalin-1 project has already resulted in \$3.8 billion in project contracts for Russian firms, including \$412 million in 2006 alone, accounting for two thirds of total contract value awarded by the project.<sup>49</sup>

*Enterprise growth:* In collaboration with USAID, ExxonMobil launched a small business development program focusing on promoting regional economic growth in North Sakhalin. The project has a total budget of over \$1 million and has contributed to launching and supporting 180 small businesses, creating more than 500 local jobs.

*Support for local education and health care:* Since 1994, ExxonMobil has contributed over \$2 million in the form

of small grants to various organizations working in local communities. Focusing primarily on education and health care, these grants have supported improvements to local hospitals and health clinics and have increased funding for science education and teacher professional development, among other benefits.

**Lessons Learned** *Knowledge-sharing is key:* The implementation of a company-wide initiative like ExxonMobil's national content strategy relies heavily on documenting and disseminating best practices tested on the ground. The company's effort to streamline information flows from field projects and identify best practices has allowed project managers to replicate successful interventions and achieve faster results.

At the operational level, it is important to be clear and consistent from the very beginning of the project when communicating with local firms, particularly regarding requirements for goods and services. Project websites and other mass communications tools play important roles in informing local audiences about the work of the company, advertising procurement needs, and explicitly highlighting company requirements, policies, and procedures. Besides building the appropriate level of understanding among suppliers, these tools help establish the company as transparent and build goodwill in the local community.

*Utility of joint ventures:* ExxonMobil has found that local companies that take advantage of joint venture opportunities with established foreign partners increase their capacity and grow faster. As a result of greater knowledge and technology transfers, and access to higher levels of capital, local joint venture partners are better able to meet supplier and vendor requirements. In the long run, these local entities can grow to become trusted partners for ExxonMobil and other large companies, entering long-term contractual agreements that contribute to sustainable growth and becoming important players in the local economy.

*Local staff capacity:* To the extent possible, local personnel should be responsible for identifying and managing local supply chains. Local staff members have an inherent understanding of local norms and culture that gives them an important advantage. Furthermore, this level of engagement contributes to their capacity as effective managers.

## 7.4 MINERA YANACOCHA SME LINKAGES PROGRAM: NEWMONT AND IFC IN PERU<sup>50</sup>

**Background** Minera Yanacocha in the northern Peruvian region of Cajamarca is Latin America's largest gold mine. Newmont is the mine's majority shareholder with a 51.35% ownership interest, while the Peruvian mining firm, Compañía de Minas Buenaventura S.A.A owns 43.65% and IFC holds the remaining 5%. Since 1993, the population of Cajamarca has swelled from 30,000 to 240,000 in 2004. Minera Yanacocha currently employs more than 8,000 workers, both directly and through contract engagements. In addition to being the primary employer in Cajamarca, Yanacocha is one of Peru's largest taxpayers. According to the current mining royalty tax law, 50% of the mine's tax payments are designated to remain in Cajamarca.

**Drivers** At the end of 2001, Minera Yanacocha had invested over \$15 million in community development programs focusing on health care, education, agribusiness, and micro-credit as part of its social engagement efforts. External donors had contributed an additional \$7.3 million to these efforts. Launched in 2002, the SME Linkages Program focuses on increasing the long-term sustainability of the region's economy by both incorporating local businesses in Yanacocha's value chain and expanding economic activity beyond the mining industry.

**Activities** The goal of the Minera Yanacocha SME Linkages Program is to build a diversified and sustainable economic base that takes full advantage of opportunities related to, but also extending beyond, Yanacocha's mining operations.

*Supply chain development:* For SMEs within Yanacocha's value chain, primarily in the transportation and construction sectors, supplier development efforts center around a total quality management program to improve productivity and optimize company management abilities. Through the delivery of professional training models, the program focuses on raising safety, environmental, and business standards.

Marketing, another main focus for cash-strapped SMEs, has been addressed through group marketing events such as "Business Encounters" which spread costs and facilitate contracts between local SMEs and large private and public firms.

Finally, based on what local businesses identified as a critical need, an advisory services program was implemented to improve financial management and business processes. SMEs received training in areas such as bookkeeping, cash flow management, and business plan development. This has helped participating SMEs become more creditworthy, opening up a wider range of financing options from local banks and microfinance institutions and allowing them to expand operations and increase sales.

*Diversified local economy:* The Minera Yanacocha Program extends to SMEs outside the company's value chain as well, particularly in the handicrafts (ceramics and textiles) and agribusiness sectors. For example, in the ceramics and textiles sectors, local artisans have received technical and managerial training to upgrade their product design skills and production capacities.

*Enabling environment:* In parallel to SME development efforts, the program has worked to strengthen the enabling environment and remove obstacles to SME growth. In conjunction with municipal authorities, IFC funded an administrative simplification project which resulted in the establishment of a "one-stop shop" business registration process helping eliminate multiple visits to different agencies, while also reducing paperwork. Municipal authorities also developed an electronic government portal to facilitate information-sharing on registration procedures. As a result of these efforts, the number of days it took to register a small business was drastically reduced from 100 to three. Another obstacle to SME growth involved the cost of licenses. Previous licensing fees, averaging \$163, were close to 8% of the annual per capita income in Peru, prohibitively expensive for micro and small business owners. As part of the simplification process, the local government reduced these fees by 15%. These reforms have resulted in a sharp increase in small business registrations, bringing them into the formal sector for the first time. These SMEs are now legally able to compete for Minera Yanacocha and other firms' contracts, as well as to access financial services from banks.

*Institutional capacity:* The Asociación Los Andes de Cajamarca (ALAC) was created by Minera Yanacocha in 2004 to support sustainable development in the region. Since then, ALAC has funded projects and activities that contribute to building business and institutional capacity in both rural and urban areas. Newmont and IFC have made a commitment to enhance ALAC's own capacity to serve as a long-term supporter of regional sustainable development.<sup>51</sup> While Newmont expects to fund both ALAC's endowment and operating expenses for the duration of its mining activities at Yanacocha, IFC is providing technical assistance to build the long-term capacity of this local institution to support regional economic growth and development.

In addition, changes in the Peruvian mining royalty tax law stipulate that 50% of Minera Yanacocha's tax payments remain in Cajamarca. In response to this change, Newmont asked IFC to help build the capacity of the local municipality to optimize its revenue management systems and ensure that Newmont's tax payments and other contributions to the local budget effectively contribute to improvements in basic social and economic infrastructure.

## Results

SMEs bidding for contracts with the mine and with other enterprises had increased their cumulative sales to \$10.5 million by 2005, comprising a \$4 million gain in new sales over the previous 18-month period. 150 entrepreneurs from the emerging construction sector received extensive training, and 25 SMEs became more competitive by acquiring modern technology and know-how. A capacity-building program for small agribusiness enterprises generated 54 new jobs and tripled aggregate sales to more than \$2 million over the previous 15-month period. Finally, the number of participants in "Business Encounters" marketing events grew from 64 in 2003 to 193 in 2005, while turnover among participants increased seven-fold from over \$373,000 in 2003 to over \$2.2 million in 2005.

## Lessons

*Stakeholder engagement:* Conduct extensive stakeholder consultations at the beginning of program design to obtain buy-in from all parties involved. This ensures alignment of program objectives with company and community objectives.

*Importance of partnerships:* Linking company initiatives to the programs of IFC and other partners leverages resources and expertise and enhances relationships with local governments, NGOs, and other important stakeholders, ultimately increasing the impact of economic opportunity programs. Coordination among key actors, such as extractive companies and IFC, also reduces the duplication of efforts.

## 7.5 EXPANDING ECONOMIC OPPORTUNITY THROUGH COLLABORATION: CHEVRON'S ANGOLA PARTNERSHIP INITIATIVE<sup>52</sup>

### Background

Chevron's presence in Angola commenced 50 years ago and the company's capital investments in the country are expected to surpass \$10 billion by 2010. The largest employer in the industry with approximately 3,000 direct employees and an additional 12,000 contract workers, 88% of Chevron's workforce is comprised of Angolans. While Angola is today the fastest-growing economy in Africa, Chevron is contributing to the long-term development of the country through its Angola Partnership Initiative (API). API's primary goal is to build the local capacity required to sustain the country's economic growth and improve the living standards of Angolans in the long run.<sup>53</sup> As emphasized by Chevron's Vice Chairman, Peter J. Robertson, the API's "efforts are helping the Angolan people to develop the skills and create the opportunities to develop a well-functioning, sustainable economy."<sup>54</sup> Since the API's launch in 2002, Chevron has contributed \$23.5 million and has leveraged additional resources from its key partners, USAID and UNDP, to reach total funding of over \$55 million.

### Drivers

At the end of a 27-year civil war, Chevron was approached by Angola's president to help rebuild the country's economy. Due to its long history in Angola, the company was compelled to seek new opportunities to support economic growth and sustainability in order to respond to this request. The API was designed to complement and add to Chevron's existing contributions to Angola's economy through local employment and supplier linkages.

### Activities and Results

A set of strategic objectives were developed to meet the API's goal of improving living standards and enhancing local capacity. These included the promotion of peace and stability through food security and reintegration of refugees, ex-combatants, and displaced people; improvement of health and education standards; capacity-building for Angolan NGOs and government entities; and poverty reduction through agribusiness and the development of micro, small, and medium enterprises.

Chevron and its partners designed and implemented several activities to accomplish these objectives, including the following efforts that created and expanded economic opportunities for Angolans:

*Consortium for Development Relief:* In the aftermath of the civil war, immediate attention was given to meeting the basic needs of those affected by the fighting through the Consortium for Development Relief. During the three years that the effort was implemented, an estimated 2 million Angolans benefited from its services. Over 200,000 families (approximately 1 million people) received food, as well as seeds, tools, and technical support to allow them to cultivate their land and start crop production to sustain their food needs and earn additional income. Additional "food for work" programs created immediate employment opportunities that resulted in substantial renovations to Angola's local infrastructure, including the rebuilding of roads and bridges. Among those benefiting from these programs were between 40,000 to 50,000 refugees and ex-combatants returning to their homes after the war.

*Business capacity and human capital development:* Moving beyond programs that provided immediate relief, API designed interventions that supported the transition of farmers beyond subsistence agriculture into sustainable agribusinesses. To facilitate the provision of assistance, API helped create 32 associations of over 3,000 small agricultural producers. Through these associations, Angolan farmers received support services including seed production and multiplication, harvest protection, and crop diversification. As a result of these services, farmers now produce and commercialize higher-value crops and are developing new market linkages for their products.

In conjunction with building capacity among existing farmers, API is also focusing on the development of human capital by supporting technical training and education through Angola's Faculty of Agrarian Science. Since 2003, the number of agronomy students has increased from 200 to 700, greatly improving the technical skills and capacity of Angolan agronomists. In addition, API has funded research efforts to further improve innovation and foster the adoption of advanced agricultural practices among Angolan farmers.

*Access to finance:* The long-term sustainability and growth of Angola's economy depends to a great extent on financing opportunities for farmers and other local businesses. In 2004, API helped establish NovoBanco, a private microfinance bank whose primary objective is to support the creation and expansion of micro, small, and medium enterprises. In just three years, NovoBanco has made over \$27 million in loans to more than 5,000 micro and small enterprises, and in 2006 it became a profitable enterprise. The bank's contribution to Angola's development is even greater, however, because it has served as a model for the expansion of the micro-lending sector in Angola. For example, the government has recently launched a \$10 million micro-credit program through two commercial banks to continue to meet the demand for financing among Angolan small and medium enterprises.

## Second Phase

Following an evaluation process, Chevron has committed to supporting the API for a second five-year period from 2008-2013. During this phase, the API will focus its efforts on projects that have direct impact on improving livelihoods and generating incomes for their beneficiaries. Two activities are already underway, focusing on strengthening the capacity of municipal governments and community organizations and continuing technical assistance and capacity-building for the agricultural sector.

*Municipal Development Program:* This project was designed to increase the capacity of municipal governments and community-based organizations to plan, budget, and implement projects that benefit local communities. Its key objective is to foster collaboration between government agencies and community organizations and promote participatory decision-making processes. As a result of these collaborative efforts, community members have input in the selection of infrastructure and construction projects that are implemented in their regions, thus helping prioritize developments that most directly impact their welfare.

*ProAgro:* A continuation of previous efforts, the principal objective of ProAgro Angola is to diversify the country's economy by strengthening and expanding the agricultural sector. The project continues to provide technical assistance to farmers and farmers associations to increase yields and productivity, improve processing practices, and develop and implement marketing strategies for their products. In addition, the project is helping to establish and strengthen business linkages between farmers and their suppliers and buyers, further contributing to the long-term sustainability of the sector.

## Lessons

*Importance of leadership:* One of the key lessons learned from this effort is that high-level executive support, within Chevron and from its partners, is crucial to success. Besides providing the necessary material means to implement the initiative, internal "champions" are indispensable<sup>65</sup> – particularly at the early stages of the effort – to guarantee the necessary levels of autonomy and flexibility to experiment with new approaches and make adjustments as needed to increase impact. In addition, at all stages of the process, the appropriate individuals were assigned responsibilities that matched their skills and experience, thus providing operational-level leadership and enhancing the project's chances of success.

*Value of experimentation:* API is a unique experience for Chevron in that it was a sizeable, long-term commitment to a proactive versus passive collaboration with development partners in Angola. Flexibility was key. It allowed Chevron to experiment with different types of activities in order to identify the interventions with highest impact.

*Leveraging partnerships:* Chevron's commitment to the API helped double the resources available for the project by attracting commitments by additional partners. Collaboration with partners not only increased resources, but most importantly expanded the collective knowledge and expertise of the initiative, as well as fostered innovation and creative solutions to problems faced.

*Proactive engagement:* API demonstrated that Chevron was able to create greater value by being a proactive participant in the development and implementation of its social investment efforts. Active participation in all stages of the program helped expand the company's relationship base among government officials and, perhaps more importantly, among the communities in which it operates. As a result of this engagement, Chevron was

also able to increase its visibility in local communities throughout Angola and demonstrate its commitment to the long-term development of the country.

*Highest impact:* Projects that contributed to income generation and helped improve livelihoods had the largest impact and enjoyed the highest levels of support in local communities. Projects such as NovoBanco, ProAgro, and the Municipal Development Program enjoyed the highest visibility and support because they most directly impacted the daily lives of Angolans. Most importantly, these projects contributed to the long-term sustainability and growth of the country's economy because they also helped strengthen local capacity.

## 7.6 DIAVIK DIAMOND MINES INC.: RIO TINTO IN CANADA'S NORTHWEST TERRITORIES<sup>56</sup>

### Background

The Diavik Diamond Mine is located on a 20 square kilometer island in Lac de Gras, approximately 300 kilometers northeast of Yellowknife, the capital city of the Northwest Territories in northern Canada. The region has fewer than 50,000 residents and 40% of them are of indigenous descent. Diavik Diamond Mines Inc. (DDMI), a wholly-owned subsidiary of Rio Tinto plc, owns 60% of the mine and manages its operations, while Aber Diamond Limited Partnership owns the remaining 40% of the joint venture. Construction began in 2001 and mining operations formally commenced in 2003. Over its 16 to 22 year lifetime, Diavik is expected to produce over 100 million carats of diamonds.<sup>57</sup>

### Drivers

There are two significant drivers behind DDMI's efforts to expand economic opportunities in the Northwest Territories. First, the company was driven by its own corporate commitment to sustainable development. Second, a significant development in the regulatory regime provided for meaningful participation of indigenous communities in the regulatory bodies and processes governing resource development in the Northwest Territories.

### Activities

In collaboration with a host of local partners, including government authorities and representatives of indigenous groups, DDMI has made a commitment to the sustainable development of the Northwest Territories by providing significant training, employment, and business opportunities to benefit local residents. DDMI and its partners have entered into a number of formal agreements that serve as a framework to help facilitate the implementation of commitments to expand economic opportunities, as well as monitor progress.

*Socio-Economic Monitoring Agreement (SEMA):* DDMI entered into a Socio-Economic Monitoring Agreement with the government of the Northwest Territories and five neighboring Aboriginal groups in 1999. The agreement articulates DDMI's commitment to training, employment, and business opportunities. It also establishes a Communities Advisory Board comprising representatives from all parties, with majority representation of indigenous groups, to facilitate the active involvement of local communities and government in the broader socio-economic aspects of the mine. As a monitoring and advisory body, the board makes recommendations to mitigate potential negative effects and to enhance positive opportunities for local communities created by the mine's activities. During 2006, the board provided its ongoing advice with respect to business opportunities, recruitment strategies, cross-cultural awareness, employee-specific support programs, and several other areas of interest.<sup>58</sup>

*Participation Agreements:* DDMI signed five Participation Agreements (PAs) directly with its neighboring indigenous communities. These agreements were negotiated prior to the mine's construction to provide communities and DDMI with a foundation upon which to build their relationship as the project progressed from construction into operations. The PAs formalize commitments for both DDMI and the Aboriginal signatories to work together to maximize community benefits by identifying business opportunities for Aboriginal service providers,<sup>59</sup> employment and training opportunities for community residents, and support for community educational initiatives. In addition, four of the PAs create formal implementation committees that externally verify the mine's performance on socio-cultural and economic aspects, provide recommendations for improvement, and generally create an environment for ongoing transparency and collaboration.

*Northern Business Participation Policy:* Within the company itself, DDMI developed a publicly available policy that lays out a clear set of principles and commitments to providing business opportunities and creating long-lasting business relationships with neighboring communities. To pursue these activities, DDMI hired a venture development manager to work closely with existing and potential local business partners, created a Northern Vendors and Contractors Capacity Database, adjusted contracting requirements to fit local business capabilities, and facilitated and monitored joint venture partnerships.<sup>60</sup>

In an application of its Northern Business Participation Policy, DDMI has outsourced approximately half of its workforce requirements to northern businesses. Through outsourcing contracts, northern firms will become better positioned to grow their business beyond total reliance on the mine. Some of these long-term operations labor contracts with Aboriginal and northern businesses provide a range of goods and services including light vehicle

maintenance, mining equipment operation, site services, security, and air passenger and cargo transportation. In terms of employment opportunities, this approach has the potential to create additional new career opportunities for Northerners. In addition, DDMI has worked with its contractors to ensure that their policies, procedures, and benefits are aligned with its own.

## Results

As of January 2006, after six years of construction and operation activities, DDMI's spending with Aboriginal businesses had surpassed \$1 billion. DDMI is one of only three Canadian businesses to have reached this level of spending with Aboriginal businesses. Total spending with regional businesses was at \$1.9 billion, over 70% of the \$2.6 billion that DDMI has spent since 2000. Since 2004, the mine has either met or greatly exceeded its commitment of 70% regional spending.

The mine employs approximately 800 people and in 2006 it surpassed its target by having 68% of its workforce comprised of Northern residents. Despite its efforts, the mine did not meet its commitment in terms of Aboriginal employment, reaching 33% in 2006 instead of its targeted 40%. Nonetheless, this level of Aboriginal employment was significantly higher than previously expected and the mine is committed to reaching its target by focusing on pre-employment initiatives, recruiting, employee retention, and employee development programs. While most Aboriginal employees are first engaged in entry-level or semi-skilled positions, DDMI seeks to expand their skills through its own apprenticeship and professional development programs, as well as collaboration with a community and government partnership that administers a series of workforce development programs. DDMI has also designed a leadership development program targeting Aboriginal employees and contractors. Besides completing a customized curriculum based on Rio Tinto leadership competencies, participants are also matched with a DDMI manager as a mentor.<sup>61</sup>

## Lessons

Regular, consistent, and systematic consultation from the outset: Community consultation processes began when the area was first explored in the mid-1990s, and the company made a commitment to ensure repeat visits by the same people throughout this period. During the feasibility stage of the project, over 300 meetings were held with affected communities, regulators, and the general public.

*Specific employment and procurement targets:* DDMI committed to targets through both the construction and operation of the mine. Monitoring its collaborative objectives is an integral part of Diavik's community consultation process.

*Advisory role for communities:* In addition to consultation, communities were given a formal advisory role in the project, providing a new level of transparency and a platform for planning, monitoring, and ongoing development.

*An integrated approach to training, employment, and procurement:* Company- and partnership-based training on technical, operational, and leadership skills has been linked with hands-on business advice, venturing, and contracting activities.

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### **About the Corporate Social Responsibility (CSR) Initiative**

Under the direction of John Ruggie (Faculty Chair) and Jane Nelson (Director), the CSR Initiative at Harvard's Kennedy School of Government is a multi-disciplinary and multi-stakeholder program that seeks to study and enhance the public contributions of private enterprise. It explores the intersection of corporate responsibility, corporate governance, and public policy, with a focus on the role of business in addressing global development issues. The Initiative undertakes research, education, and outreach activities that aim to bridge theory and practice, build leadership skills, and support constructive dialogue and collaboration among different sectors. It was founded in 2004 with the support of Walter H. Shorenstein, Chevron Corporation, The Coca-Cola Company, and General Motors and is now also supported by Abbott Laboratories, Cisco Systems, Inc., InBev, InterContinental Hotels Group, Microsoft Corporation, Pfizer, Shell Exploration and Production, and the United Nations Industrial Development Organization (UNIDO). Visit the Initiative's homepage at <http://www.ksg.harvard.edu/m-rcbg/CSRI>

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