STRENGTHENING THE PRIVATE BASIC EDUCATION SECTOR

A CASE FOR USAID SUPPORT AND FINANCING THROUGH THE DEVELOPMENT CREDIT AUTHORITY

DEVELOPMENT CREDIT AUTHORITY DAI SUPPORT CONTRACT

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ACRONYMS

ADB	Asian Development Bank
BSS	Bodh Shiksha Samiti
DCA	Development Credit Authority
DPS	Delhi Public Schools Society
EFA	Education for All
GDP	Gross domestic product
IDB	Inter-American Development Bank
IFC	International Finance Corporation
NGO	Nongovernmental organization
ODC	Office of Development Credit
OECD	Organization for Economic Cooperation and Development
PROBE	Public Report on Basic Education
UNESCO	United Nations Educational, Scientific and Cultural Organization
USAID	United States Agency for International Development
WEI	World Education Indicators

EXECUTIVE SUMMARY

This report develops a case for private sector involvement in the provision of basic education and explores the financing needs of schools and related service providers towards expanding the supply and quality of basic education. It offers guidelines for the United States Agency for International Development (USAID) to invest in the private basic education sector using the Development Credit Authority (DCA), a financial guarantee mechanism through the Office of Development Credit (ODC). This report provides an overview of historical trends in the provision of private education, describes the characteristics of this sector, and presents the main rationale for investing in it. Privately managed and financed schools are becoming more prominent globally in education, even at the level of basic education. Private schools increase efficiency, access, and quality of services, and have the potential to play a more significant role in relation to the public sector. Drawing from literature and past donor experiences in financing for social services, this paper offers recommendations for USAID to use its loan-guarantee mechanism to fill a financing gap and stimulate growth of the basic education sector.

The right to free basic education was included in the United Nations Declaration of Human Rights in the 1940s; since then it has been mandated by national laws and supported by international agreements. The Education for All movement in the 1990s reaffirmed the right to basic education, making it a priority in the development agenda. Many developing countries, however, are struggling to fulfill this commitment and experience shortfalls in providing basic education to the school-age population. Increasingly, many of these countries look toward the private sector to complement public provision and help them to supply education for all.

The concept of private education and privatization in relation to education is complicated, given the nature of education as a social service and public good. This idea typically encompasses both the ownership and management of schools as well as the financing of education, which is increasingly being borne by students and their families. Mixed ownership and financing characteristics are often the rule rather than exception and should be taken into account when considering strategies for working with and financing the private education sector. This report defines private schools as institutions that are not operated by a public authority, but are controlled and managed by a private agency, such as a nongovernmental organization, religious body, special interest group, foundation, or business enterprise. This report is concerned with formal schooling that officially recognized establishments provide.

In many countries the private education sector is growing to meet demand and address shortfalls in public supply. In some countries, such as Zimbabwe and Chile, it is meeting the basic education needs of a significant portion of the population. The questions for policymakers is whether this growth should be supported and, if so, how? In a climate of diminishing resources, donors must determine the most effective use of their scarce funds. Over the years a number of arguments have been put forward in favor of strengthening the private sector, including:

- reducing the burden on government expenditure
- improving the efficiency and effectiveness of schools
- increasing equity and access in education
- increasing diversity and choice in terms of educational provision
- making schools more accountable to their clients.

Based on the literature review, the private sector can have an important role in supporting the achievement of Education for All's goals. Governments are increasingly channeling public funds to the private sector through contracting with private providers to manage educational services, directly covering the cost of private education in the form of teacher salaries or infrastructure, or targeting subsidies directly to students who enroll in the private sector. As a supplier of education, the private sector has the potential to increase access and equity, efficiency and effectiveness, and accountability.

Access and equity: Educational gaps in developing countries are large and are most pronounced in rural areas, among girls, and for culturally diverse groups, including migrant populations. Moreover, the distribution of public subsidies favors urban areas and middle and upper-income groups in many countries and points to embedded inefficiencies in the allocation of public resources. The private sector in a number of countries—including Brazil, India, and much of sub-Saharan Africa—has played a critical role in meeting the needs of disadvantaged groups and has the potential to further increase access and equity.

Efficiency and effectiveness: Private provision of education is more effective in terms of student achievement on standardized tests and is an effective alternative to publicly provided education. The unit costs of private schools are also lower than their public counterparts. Most empirical studies in developing and some middle-income countries support these claims, yet they also note that the effectiveness varies across countries and can be influenced by clientele served, as well as strength of the private sector in terms of the school's management, teacher quality, pedagogic style, and responsiveness to clients.

Accountability and quality: Increased accountability in private schools has the potential to increase the overall quality of education. There is also recognition, however, of the need to institute stronger assessment and accountability systems that cross public and private sectors and address different dimensions of quality, such as teacher training and school management. Policymakers have recognized that increased spending alone does not directly affect the quality of education or student achievement.

Given the potential the private sector has in improving access and equity, efficiency and effectiveness, and accountability and quality, governments and donors should consider them as a partner in achieving Education for All. Working with the private sector to achieve development goals, however, requires a new type of programming. Potential strategies for engaging the private sector include strengthening the investment and regulatory climate to impact the scale, efficiency, and quality of services provided; instituting effective accreditation systems that are focused on providing incentives for quality education in the private sector rather than burdensome regulations; identifying innovative models for providing private services, such as networks; ensuring that resources are targeted to different population segments through public-private partnerships and targeted vouchers; and facilitating access to finance.

While it is beyond the scope of this paper to fully address all of these strategies, this report does explore how improving access to financing can be used to engage the private sector in the delivery of basic education. Access to finance is an important ingredient in private sector development. While the literature review did not reveal statistics on commercial bank lending to the education sector in developing countries, anecdotal evidence suggests that lending to it is limited because of perceptions of risk, concerns about collateral, lack of market information, and limited understanding of the private education sector business model.

Limited access to financing impedes new entrants to the education sector and negatively affects growth, access, and quality. Schools and related service providers are forced to rely on their savings as well as loans from family and friends to invest in and grow their businesses. These practices have serious implications on both the size of the private education sector and the quality of education. If the private education sector is to meet increasing demand and comply with public-sector regulations, it will need access to financing. In addition, the lack of student loans—with the potential to alleviate household financial pressures, particularly at the secondary level—may further constrict access to basic education.

Donors working to stimulate growth and financing of private education traditionally have targeted their support to higher education; however, in response to the growing need and potential for benefit at the basic education level, there is recent interest among donors to increase access to financing at all levels. Financing basic education is still a nascent market for donors and presents an important opportunity for USAID to have a leadership role in using proven strategies to expand access to financing for this sector. Financing interventions can be developed to contribute to USAID missions' strategic objectives in education by improving quality, efficiency, and access. On the supply side, financing can be targeted directly at private schools, networks of schools, or related service providers, such as institutes for accreditation, professional development, publishing, or school transport. On the demand side, commercial financing can be targeted to individuals and families to help them cover the costs of their education, particularly at the secondary level.

One important strategy in expanding access to financing for the private basic education sector is USAID's DCA guarantee. This guarantee stimulates lending to underserved markets. The DCA guarantees up to 50 percent of the loss on a loan or a portfolio of loans and can help banks overcome their concerns about a new market. By sharing risk the DCA can help banks in lending to underserved sectors, such as private primary schools; offer longer terms, which are essential for school construction; and reduce conservative collateral requirements, which have posed a major constraint to education sector loans. The DCA also mobilizes local capital to support the education sector, leveraging important new resources to complement USAID missions' education programming.

USAID's ODC offers four products under a shared-risk guarantee: the individual loan guarantee, loan portfolio guarantee, bond guarantee, and portable commitment guarantee. Loan guarantees and portable guarantees can be used to support specific institutions or projects, especially ones that call for larger-scale investments. Loan portfolio guarantees can be effective in reaching multiple small schools or related service providers in the education sector. Portfolio guarantees also can be used to administer student loans in partnership with local educational institutes. Bond guarantees have the most potential in municipal financing of education sector projects.

Selecting suitable countries to structure education sector DCAs will depend on a number of factors (assuming USAID already has a strong presence in the basic-education sector). These considerations include whether the country has high levels of private sector enrollments and private funding to education, a favorable regulatory regime and accreditation and licensing policies, an investment climate that attracts private sector participation (schools and other service providers), and demand for increased access or improved choice in obtaining basic education.

While the DCA is a key mechanism in expanding access to finance for the private education sector, it is a new market for most financial institutions and parallel strategies should be considered in addition to the DCA. Because of the constraints in lending to the education sector, including banks' perception of higher risk and limited knowledge about the sector, utilization of an education sector DCA would most likely benefit from technical assistance. Financial institutions can be supported with market research, training in education sector lending, support in developing targeted loan products, and providing market referrals of potential borrowers. Education sector borrowers will benefit from accessing business-development services so that they can prepare a bankable business plan and manage financing.

In sum, the private sector has an important role to play in achieving the goal of Education for All. The private sector is already contributing to the delivery of basic education in many countries. As donors and governments grapple with identifying the most effective strategies for partnering with the private education sector, it is important to consider the role that financing can have in improving access, efficiencies, and quality. USAID's DCA guarantee can be an effective tool in stimulating commercial lending to the basic education sector. The DCA can leverage local financial resources in support of USAID missions' education goals.

1. INTRODUCTION: OBJECTIVES AND BACKGROUND

1.1 PURPOSE AND SCOPE OF THE REPORT

This report develops a case to strengthen private sector involvement in basic education and explores the financing needs of players in the education market. It discusses the potential for the United States Agency for International Development (USAID) to invest in the private education sector using its Development Credit Authority (DCA) guarantee, a financial guarantee mechanism through the Office of Development Credit (ODC). The paper provides an overview of historical trends in the private education sector, describes characteristics of privately provided education, and presents the main rationale for the emergence and continued growth of private education. Ultimately the purpose of this report is to provide USAID with guidance to strategically invest its resources in the private education market to complement public sector provision and ensure access to quality basic education for all. The paper offers suggestions for the ODC to use the DCA guarantee for the private basic education sector, consisting of formal schools and related educational agencies, such as training institutes or digital technology companies. While the DCA has been used to a limited degree to stimulate growth in higher education, it has not been used for basic education.

This paper makes a case for investing in the private basic education sector and offers approaches for using the guarantee mechanism and other strategies to promote access to financing in different regions and education markets. Promising countries to invest in already will have a strong USAID presence in the basic education sector, high levels of private sector enrollment and private funding for education, a favorable regulatory regime and accreditation and licensing policies, an investment climate that attracts private sector participation (schools and other service providers), and demand for increased access or improved choice in obtaining basic education.

USAID defines basic education broadly to include all program efforts aimed at improving early childhood development, primary education, and secondary education (delivered through formal or informal settings), as well as training for teachers working at any of these levels. In its definition USAID also includes training in literacy, numeracy, and other basic skills for adults and out-of-school youth (USAID Education Strategy 2005).

This report provides a synthesis of the literature on private provision of education globally, it explains the trends towards privatization and analyzes the growing market coverage of private educational providers, and it sets forth the main rationale for investing in private education—including access and equity, efficiency and effectiveness, and increased accountability. The second component of the report is forward looking: it examines how improving access to finance is an important strategy in strengthening the private education sector and suggests potential intervention areas for USAID to use its DCA mechanism to increase the scale and quality of privately provided basic education.

1.2 UNIVERSAL ACCESS TO EDUCATION AND THE NEED FOR PRIVATE PROVISION

Most developing countries experience serious shortfalls in providing basic education to the school-age population and increasingly have looked toward the private sector to complement public provision. The right to free basic education (for up to seven years) was included in the United Nations Declaration of Human Rights in the 1940s and since has been mandated by national laws and supported by international agreements. Thus expanding access to basic education for all children is a policy priority for most national governments that receive support from the international community. It is increasingly being recognized, however, that policies supporting universal basic education face serious implementation difficulties unless public sector efforts are complemented with private sector resources (for example, in the form of cost-sharing, management oversight, or infrastructure contributions) from local communities, religious organizations, and private institutions (Kitaev 1999).

Goals of universal access to education

The basis for compulsory mass schooling originated in the Reformation movement and became part of the legal framework in the nation-state building process in 19th century Europe and the Americas. Western governments set forth a legal basis for establishing state-administered schools and instituted this same foundation within their colonies. Sixty countries that had gained independence by 1945 had enacted compulsory attendance laws; by 2000, 85 percent of the 125 former colonies that became independent had passed compulsory school laws. The ideology of compulsory education was thus increasingly part of the nation-state model during the 20th century (Benavot and Resnik 2006). There was growing pressure on new states to pass compulsory school laws, but their limited capacity to implement or enforce these laws only became more pronounced after independence.

An education-for-development discourse prevailed during the 1950s and 1960s whereby international organizations embraced the notion of education as a key factor in economic growth. Member states to the United Nations were expected to increase their allocations for public education and use modern planning techniques to improve educational systems. These efforts resulted in remarkable growth of public educational systems and enrollment rates throughout the developing world. In the 1980s, however, the debt crisis and reduction in international aid towards education forced central governments in most developing countries to cut spending on education and other social sectors. They sought alternative ways to leverage resources and funding, including advocating for decentralization and privatization policies. In addition to ensuring adequate revenue was devoted to education, governments and policymakers also were recognizing the need to make schools more effective and responsive to the needs of disadvantaged segments of the population.

Responding to education goals in different regions

The ability of countries to achieve goals of universal access to education depended largely on their colonial history, political priorities, governing system, and level of tax revenue. Governments in Western countries were successful in building unified education systems during the 19th and early 20th centuries, offering only a small role for the private sector. Privatization experiences among Western countries were first inspired by the need to address religious diversity and provide communities with the opportunity to run their own publicly financed schools. Privatization in the West took place under the continued predominance of public funding, government-supported national standards, and multilevel accountability systems.

Centralized governments under socialist regimes in Eastern Europe, China, Vietnam, and Cuba also were successful in providing universal access to mandatory schooling in public schools, with little or no room for independent or private schools. In recent decades, however, all of those countries except for Cuba and Vietnam have engaged in the processes of decentralization of their school systems, ensuring a larger role for the private sector in school ownership and management. Privatization experiences among these countries have been tied to the need for devolving decision-making to local governments in order to attend to previously ignored social and cultural diversity and thus improve school quality within market economies. Private schooling, however, appears also as a response to unmet demands given the limitations in public financing for education. This case was particularly true in Russia and other Eastern European countries during the economic crises of the 1990s. In China privately managed community schools have been established to attend to the needs of migrant populations who cannot access education in public urban schools.

The incomplete nature of universal access under free and publicly provided schools is especially evident in most ex-colonial and newly independent countries of Latin America, Asia, and Africa—with some notable exceptions in East Asia (Taiwan and South Korea) and the Latin American Southern Cone (Argentina, Uruguay, southern Brazil, and Chile) –leading governments to increasingly recognize a much greater role for the private sector in achieving the goal of basic education for all. The educational contexts vary considerably within this large group of countries that includes most low and middle-income ones. Some countries have a strong presence of private religious schools, others have strong community-based movements and many have the presence of nongovernmental organizations (NGOs) or for-profit institutions. Nonetheless, from the perspective of the public sector, there is widespread recognition of the need to engage with the private sector to meet goals of universal access and increase the efficiency and quality of services provided.

Renewed commitment to basic education for all

In the 1990s the United Nations Educational, Scientific and Cultural Organization (UNESCO) and other international organizations launched the Education for All (EFA) movement and placed basic education as a top priority on the development agenda. Representatives from 160 governments in Dakar reaffirmed their commitment to EFA and produced a set of goals, actions, and monitoring mechanisms to guide national and international efforts in the next decades. Although enrollment rates in primary and secondary education increased throughout the developing world, new concerns emerged about issues related to quality as learning in primary and secondary schools was being assessed systematically through standardized testing of reading and mathematics in many nations (Baker and LeTendre 2005).

There is consensus today about the need to increase funding, public and private, for education to attend to the rising demands for skills in the new global economy. The 1990 EFA Conference stressed the importance of partnerships to meet the obligations of basic universal education. Its final summary report acknowledged that

> National, regional and local education authorities have a unique obligation to provide basic education for all, but they cannot be expected to supply every human, financial or organizational requirement for this task. New and revitalized partnerships at all levels will be necessary…(including) partnerships between government and non-government institutions, the private sector, local communities, religious groups and families.
> (Cited in Bray 2002).

Donor support to private basic education

Donors and governments, however, grapple with how to work with the private sector to achieve education goals. Donor involvement to support the provision of basic education through the private sector, as well as public subsidies to private schools, is controversial as it falls within the polemic battle between supporters of *either* private *or* public education. As governments have the fundamental responsibility to fulfill objectives of universal access to basic education, donors traditionally have channeled their support to the public sector to increase access and quality of education at the systemic level. Donor support has played a key role in many governments' attempts to reform public schools to improve their quality, efficiency, and responsiveness to students' needs. Reforms in the public sector in the last few decades have focused on providing information on success and failure rates; increasing school autonomy; and encouraging the empowerment of students, families, and communities. Although private schools have a quantitatively minor role in primary and secondary education, many governments seek to stimulate their growth to increase the total effort behind meeting the goal of universal access to basic education.

The following points summarize the primary controversial areas in working with the private sector for many donors:

- *User fees*: Most private schools require user fees, thus making them less accessible to lower-income groups. As will be discussed later, however, research has shown that user fees are just one of the many costs students and their families bear in both public and private schools. Many low-income families are willing to pay user fees, within limits, when doing so gives them a greater voice in school affairs and encourages school authorities to be more responsive to their needs.

- *Choice*: Private schools, unlike their public counterparts, can exercise choice in student admission. They may limit access to students who have difficulty in paying fees or are perceived as higher academic risks. Public schools thus face higher costs as a result of private school's skimming students who have more supportive family background. This claim is perhaps the most damaging one against public subsidies to private providers. Yet, public subsidies and donor support may stimulate greater access by targeting their funds to needy students as well as by working with private providers whose mission includes work with underrepresented or marginal groups (for example, rural and urban poor, ethnic minorities, and girls).

- *Quality*: Private providers are often poorly controlled by governments and enter into asymmetrical relations with students and their families who are unable to assess the quality of educational services. In fact, the quality of learning in both public and private schools has become the focus of concern with the widespread availability of testing in many countries that only recently have achieved universal access to basic education. While the evidence about public/private advantages is conflicting, recent studies have highlighted the enormous achievement gaps between different student groups and between schools within each of these sectors.

- *Segmentation*: Public schools traditionally have educated children in heterogeneous societies, supporting social integration and promoting pluralism, while private schools have been more responsive to interests and ideologies of particular groups, tending to cater to rich families or to those of particular religious or ethnic backgrounds. Critics thus see the growth of private schools as a further step in social segmentation. The landscape, however, is more complex. Centralized and bureaucratized public school systems currently are blamed for ignoring cultural, ethnic, and religious diversity in complex national societies. Minorities, often large, are poorly represented in the dominant school system, while private schools tend to be more responsive to the needs of local groups.

As a recent report from the Inter-American Development Bank (IDB) indicates, countries need both, public education with private efficiency goals and private education that supports social objectives (Castro 2001). The key question is not whether to support one or the other, but rather what kinds of public policies are more likely to promote a greater national effort devoted to education and the expansion of a school system more responsive to the needs of all students. The main rationale for supporting the private sector in basic education is to complement efforts in the public sector by:

- increasing private funding and thus reducing the burden on government expenditure
- improving the efficiency and effectiveness of all schools
- increasing equity and access in education
- increasing diversity and choice in terms of educational provision
- making schools more accountable to the public, in particular their clients.

This paper explores the literature behind each of these points to further inform the discussion and contribute to a better understanding of the potential of the private sector in achieving educational goals.

2. OVERVIEW AND FRAMEWORK

2.1 DEFINITIONS: PRIVATE SCHOOLS AND THE PRIVATIZATION PROCESS

The concept of private education and privatization in relation to education is complicated given the nature of education as a social service and public good. It is important to begin with definitions to provide a framework for understanding the private education sector. The definition of what constitutes a private school varies but it is generally a function of government regulation in a particular country. Governments worldwide play a major role in shaping national educational systems through the ownership and operation of schools, funding of education (including support to students and to private schools), and regulation of the educational sector as a whole. Although few, if any, regulate teaching or learning, all governments regulate schooling and its formal outcomes in terms of recognized credentials. Thus, government action always shapes the definition of private schools.

Private schools

This report uses the UNESCO definition of private schools as institutions that are not operated by a public authority but controlled and managed by a private agency, such as an NGO, religious body, special interest group, foundation, or business enterprise. It is concerned with formal schooling officially recognized establishments provide that may be under considerable influence of the state (in terms of financial subsidies, accreditation, or curriculum standards). Private schools take a variety of forms and typically are categorized according to who operates them, who uses them, and whether or not the state supports or regulates them. In broad terms they can be classified as religious or secular, for-profit or not-for-profit.

The privatization process

In recent years there has been increased privatization in the education sector. Privatization is usually defined as a process, that is, a trend in education provision and organization observed along parallel yet conceptually different dimensions, school ownership, or management and school financing. Unlike other sectors, mixed ownership and financing are often the rule rather than the exception in the privatization of education and this relationship should be taken into account when developing strategies to work with the private sector. The following graphic offers a visual depiction of the public-private continuum in the privatization process.

Privatization typically encompasses two dimensions:

- ⇒ The relative growth of private schools (some strictly privately owned and operated, others with government subsidies)
- ⇒ The growing share of total school costs students and their families bare in payment for services provided by either of these types of schools.

Figure 1. Privatization: Public-Private Mix in Financing and Control

Ownership/Management

		Public	Private
Financing	Public	**Traditional public schools fully subsidized by government**	**Government-supported private schools** • Contracting out • Targeted vouchers and scholarships • Transfer payments • Tax incentives
	Private	**Public schools with private cost sharing** • User fees • Private contributions • Student loans	**Independent private schools** • User fees • Private contributions from communities, foundations, and businesses • Student loans

Privatization →

Privatization ↓

Source: Adapted from IFC 2001.

School ownership and management: who operates the schools?

This dimension is usually based on a dichotomy (the government or a private organization, such as a church, a for-profit enterprise, or a community-based association, own and operate the schools). Different levels of government, however, may be involved in managing schools. In decentralized systems, when local governments are requested to provide mandatory schooling, school management tends to be mixed, with heavy involvement of families, local groups, and associations who participate in school governance and management and may even own the school.

School finance: who pays the costs of running a school?

School finance usually relies on a combination of private and public contributions. In most kinds of private schools, governments make financial contributions in different ways alongside private contributions (mostly made by students and their families, but also other parties). Thus, school finance usually is seen in terms of the proportion of funding governments provide through taxation, grants, or subsidies, and the proportion private individuals, associations, and donors contribute.

Privatization as a process usually is defined as the shift along these dimensions towards the nongovernmental side—measured as an increase in the proportion of students enrolled in schools owned, managed, or financed with greater participation of NGOs and private individuals. Privatization also is used normally to characterize government policies geared to foster this process.

Multiple dimensions of ownership, finance and accountability

This multidimensional concept of privatization, including the separation of historical processes from policies aiming to foster them, highlights the difficulties of defining what is a public or a private school in practice. Schools and school systems have different degrees of privateness. Kitaev (1999), for instance, finds that in different African countries schools are considered private due to funding, ownership, and management, but there are a number of factors creating confusion in the simplistic classifications by type of funding or ownership.

Box 1. ***Public Versus Private Financing****:* The distinction between public and private financing can be blurred. In Cambodia, for example, households provide 60 percent of the resources for public primary education (in the form of fees, transport, supplementary tutoring, and other items), while in Indonesia the government provides 69 percent of the resources for private primary schools (Bray 2002). Similarly, in Mauritius, the government pays for teachers' salaries as well as most direct expenses of private schools that provide services free of charge (Kitaev 1999).

Estelle James (1993) treats funding and ownership/management as two independent dimensions. Thus, she classifies schools and school systems in four roughly defined boxes: publicly owned and funded, publicly owned yet privately funded, privately owned with public funding, and privately owned and funded. In addition to ownership and funding, other authors, including Belfield and Levin (2002), add a third and important dimension, accountability to stakeholders (in particular students and their families), which many assume is characteristic of private schools (or privatized public schools). Given the nature of privatization and the previously described dimensions, opportunities to facilitate financing for schools can be conceptualized in two channels:

- to fund educational institutions (schools and related agencies) and expand the supply and quality of education
- to target financing for individuals or families who can exercise choice or simply access privately provided education.

2.2 STIMULUS FOR PRIVATIZATION: PUBLIC POLICY AND UNPLANNED CHANGE

Typically the privatization of education occurs as a result of deliberate policy or unplanned change (Bray 1998, 2002). A deliberate policy may emphasize and be based on one or more of the following tools and rationales:

- *Contracting for economic efficiency*: The operations of public schools may be transferred to private owners or managers through a contracting or sub-contracting mechanism to private providers, but more often it is used for select school functions, such as transportation, food, administration, or special educational services. Contracting is used to increase operational efficiencies, reduce public expenditure on education, and improve quality. In India, for example, a chain of private schools called the Delhi Public Schools Society (DPS) has been contracted to oversee the management of 32 public schools in 11 states using innovative technologies and curricula (Tooley 2001). In the United States, a niche of ancillary business suppliers emerged in the 1990s—educational management organizations—that enable public schools to contract out services such as student assessment, budgeting, or transportation (Levin 2002).

- *Competition and school choice*: Increased public funding may be channeled to private schools to increase competition through targeted school vouchers, transfer payments in the form of student scholarships, or direct transfers to schools through payment of teachers' salaries, extension of tax benefits, or reduced price of public services. For example**,** education reform in Chile included a universal voucher scheme that gave families the choice of attending public or private schools. Between 1981 and 2002 enrollments in the private sector increased from 15 to over 40 percent of all students and the market of private providers expanded to include a variety of religious and secular for-profit private schools (Levin 2002).

- *Increased private funding to public schools*: Individual and family contributions in the form of regular fees to public schools are intended to decrease differentiation between public and private schools and to increase community and family commitment towards schools.

Box 2. *Private Contributions Towards Basic Education:* Countries where private payments constitute a large proportion of total educational expenditures include Cambodia, China, Indonesia, South Korea, the Philippines, Thailand, and Vietnam. In South Korea private education spending on schooling and on additional tutoring amounts to approximately the same as that of government expenditures (Levin 2002). Cost sharing for education also can take the form of corporate donations to schools that are tied to government-sponsored tax relief incentives. In the Philippines, the government has instituted an adopt-a-school program for corporations. Three elementary and two secondary schools in Manila have benefited with inputs from an oil refinery, a detergent company, and a multinational hamburger outlet (Bray 2002).

Privatization also takes place as a result of unplanned change, which generally occurs in the case of failed public policy to provide universal access through publicly funded and managed schools. It is characterized in the literature as demand-driven, or spontaneous movements, addressing educational needs that are totally or partially unmet by governments—whether in terms of lack of supply, poor quality schools, or their inability to serve a particular segment of the population. Using public failure as a starting point, the emergence and growth of privately owned and managed schools can be classified under the following three conditions:

- *Inability to meet overall demand*: Limited public spending fails to satisfy growing demand from people who may prefer to use the public schools but are excluded or pushed to the private sector (James 1993). This case is largely true with secondary education that often is characterized by limited supply. When only primary schooling is available publicly, many motivated students are denied access to secondary education because of limited supply, which commonly results in an expanded private sector role at the secondary level. Moreover, it suggests that government subsidies potentially can be spread across primary, secondary, and higher education levels to ensure increased access across the board.

Box 3. ***Increased private sector enrollments at the secondary level:*** In Africa, where government efforts are focused at the primary-education level, secondary education is especially under-funded and demand typically far exceeds supply. Strong increases between 1985 and 1995 in private secondary-school enrollments are attributed to limited supply, as observed in Botswana (50 to 74 percent), Côte d'Ivoire (29 to 36 percent), Chad (5 to 13 percent), Djibouti (3 to 11 percent), and Zimbabwe (67 to 85 percent) (Kitaev 1999).

- *Differentiated demand of specific population segments*: Public schools typically cannot meet differentiated demand tied to cultural or religious identity and may more explicitly deny access to certain groups because of their legal status in a specific territory, such as undocumented migrants and refugees.

Box 4. ***Community schools in Brazil fill the gap to provide education for marginalized groups***. The mainstream public education system in Brazil does not cater to the cultural, linguistic, or economic needs of the black or Afro-Brazilian communities, particularly those living in informal neighborhoods or *favelas*. Community schools initiated by resident associations have responded to meet the demand for basic education in these neighborhoods and some have successfully demanded the transfer of public funds for teachers' salaries and school materials. For example, community schools in the state of Bahia legally can secure 3 percent of education funds allocated to municipal schools. (De Almeida 2003)

- *Entry of private, especially non-profit, providers to underserved markets:* Non-profit suppliers traditionally move into areas where the population is historically underserved, to create or strengthen demand for education, such as in rural areas or in urban slums. This segment traditionally includes schools with religious as well as educational goals, but is increasingly represented by a much greater variety of NGOs, often with international sponsorship.

Box 5. ***NGOs in India play an important function in increasing access to education for underserved communities***. The Bodh Shiksha Samiti (BSS) is one of six NGOs surveyed in a World Bank study that works in the slums of Jaipur Rajasthan where there is limited access to formal schooling. Based on a UNESCO baseline survey in 1998, 30 percent of the population lived in slums and only 74 of 279 slums had government schools. BSS started its work in the late 1980s to build new community-managed schools. It also developed an innovative model for teacher training in close collaboration with the municipal schools and with support from donors including CARE India and the Joint United Nations Agencies Initiative. Besides increasing access in the target areas, the municipal schools reported a reduction in dropout rates from 60 percent to less than 20 percent after incorporating the BSS approach of providing responsive, quality education (Jagannathan 2002).

Excess demand and limited supply pressures have been well described in the economic literature (Belfield and Levin, 2002). The most striking trend in recent years within the developing world is the overlap between changing public policy, moving towards a more favorable position regarding the private sector out of need (that is, declining public funding) or ideology (that is, market-friendly reforms), on the one hand, and unplanned or spontaneous changes in the form of excess demand, increased recognition of cultural diversity, and the strengthening of a nongovernmental sector in basic education on the other hand. Intergovernmental organizations, such as UNESCO, the Organization for Economic Cooperation and Development (OECD), international development banks, and global NGOs have been playing a key role in promoting a climate favorable to public policy change and the growth of a nongovernmental sector in education.

This growth of the private sector is not confined to schools or educational institutions alone, but comprises a variety of related service providers, including teacher training and professional development institutes, curriculum development specialists, standardized testing and private accreditation bodies, and digital or web-based technology firms. They also can include firms that usually are subcontracted to provide transportation, catering, uniforms, and other non-technical support services. Taken together, this market for education services is growing fast in response to the increasing and diversified demand posed by consumers, favorable government support to enter the market, and increasing recognition of the viability of the sector. While the private market for these services is likely more robust at the secondary and tertiary level, there is indeed overlap in the functions and services these specialized education firms offer that span all educational levels.

3. THE MARKET FOR PRIVATE BASIC EDUCATION: A GLOBAL OVERVIEW

3.1 STUDENT ENROLLMENT IN THE PRIVATE SECTOR

The private sector generally has experienced upward trends in enrollment at the primary, secondary, and tertiary levels, despite the lack of rigorous monitoring or consistent data available about this sector. Studies of the private or nongovernmental sector are based on official statistics and official classifications of schools. As has been shown in many cases, a major pitfall of the latter is that they ignore unrecognized schools operating without official authorization (Kitaev 1999, Kingdon n/d). The total enrollment of students in the private sector is thereby generally underestimated, as these informal schools constitute an important segment of education providers.

Statistics on enrollment in the private and public sectors are highly unreliable due to the varying and unstable definitions of public and private providers around the world. Authors have noticed that many private providers are unregistered (Tooley 2001, 2005), in particular schools or independent teachers serving the poor. They are, in fact, part of the informal economy. As such, they are defined by their exclusion from the formal sector that prescribes a set of standards unmet by these providers. As it often has been argued regarding the informal economy more broadly, deregulation in some dimensions may enable unregistered educational providers to play a more positive role in serving their current functions and to be counted in national statistics. Furthermore, registered private providers are often classified under legal categories (such as for profit and nonprofit) that do not necessarily reflect their true nature. As nonprofits usually benefit from special taxation and other benefits, and in many countries only nonprofits are legally entitled to issue degrees and diplomas at certain levels, it is common for profit providers to adopt the nonprofit umbrella, but not necessarily the nonprofit mission.

With these limitations in mind, a brief review of the recent literature on private enrollments around the world leads to some major conclusions.

- Private enrollments tend to be proportionally larger in secondary education, particularly upper secondary leading to higher education, than in primary education, given the governments' commitment worldwide to guarantee access to basic education.
- Private enrollments tend to be proportionally larger among the recently independent and ex-colonial countries, where the commitment to universal access is more recent and its implementation has been more difficult.
- Private enrollments have grown throughout the world in recent years, in particular as a response to public subsidy to private providers and the shift of international donors' educational aid to NGOs.

Based on UNESCO surveys conducted for a select number of developing countries under the World Education Indicators (WEI) study, of the 17 participating developing countries, eight have private schools at the primary and secondary levels that are government dependant, and all except Zimbabwe have some completely independent private schools.[1] In fact, in 10 out of 17 WEI countries, the share of private sector enrollment exceeds 10 percent and is higher than the average share in OECD countries (see Table 1). In Zimbabwe private community schools cater to as much as 87 percent of the primary school population and close to half in Chile. It is noteworthy that in both countries, private education is almost entirely reliant on government funding. (See Annex 1 for a table complete with figures, including public provision.)

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[1] Government-dependant schools receive over 50 percent of their funding from public sources; independent schools receive less than 50 percent of their funding from the public sector.

Table 1. WEI Countries in which over 10 Percent of Primary Education is Provided Through the Private Sector.

Primary Education			
	Government Dependent-Private (%)	Independent Private (%)	Total Private (%)
Argentina	16.3	3.5	19.8
Chile	41.4	7.0	48.4
India	6.0	10.7	16.7
Indonesia	-	16.1	16.1
Jordan	-	29.2	29.2
Paraguay	10.3	5.3	15.6
Peru	3.4	10.3	13.7
Thailand	15.0	-	15.0
Uruguay	-	12.9	12.9
Zimbabwe	86.9	-	86.9
OECD Mean	8.2	2.4	10.6

Source: OECD/UNESCO WEI 2005.

4. RATIONALE FOR INVESTING IN PRIVATE BASIC EDUCATION

Private contributions to the education sector play an important role in supporting the achievement of Education for All goals. Governments increasingly are channeling public funds to the private sector through contracting with private providers to manage educational services, directly covering the cost of private education in the form of teacher salaries or infrastructure, or targeting subsidies directly to students who enroll in the private sector. As a supplier of education, the private sector has the potential to increase access and equity, efficiency and effectiveness, and quality and accountability. These three related but distinct points or rationales for investing in the private sector will be elaborated on in this following section.

4.1 ACCESS AND EQUITY

Equal access to education is a basic human right and a component of social and economic well-being. Recent upward trends in enrollment rates and in educational achievement have improved the distribution of education in many countries. Educational gaps in developing countries are still staggering, however, and are most pronounced in rural areas, among girls, and for culturally diverse groups (including migrant populations). The distribution of public subsidies has been shown to favor urban areas and middle and high-income groups in many countries and points to embedded inefficiencies in the allocation of public resources. Meanwhile, the private sector in many countries has played a critical role in meeting the needs of disadvantaged groups and has the potential to further increase access and equity.

Considerable gaps in educational opportunities exist in all nations, but they tend to be large in developing countries, especially between urban and rural segments and in regions that exhibit a wide gap in wealth and income often aggravated by negative redistributive policies. Because of an inheritance of colonial domination and the economic growth in export enclaves, underdeveloped regions and rural areas remain poorly served by social and economic policies of many central governments. These differences, furthermore, are often associated with cultural cleavages rooted in race, ethnicity, national origin, and religious identity. National educational systems often have overlooked cultural diversity and neglected the needs of some groups. Furthermore, many of these educational gaps between groups defined by location, wealth and income, or cultural identity, overlap with gender gaps.

Many donors and governments are interested in improving access and equity in basic education. To be successful, these efforts must dramatically increase public and private funding to the least developed regions and to the poorest segments of the population, as well as to underprivileged ethnic and racial groups and girls and women. Access policies targeting these groups have been proposed and implemented with unequal success in most developing countries. The gender gap in basic education, for instance, has been greatly reduced in most Latin American countries, although it is still an issue in many rural areas and among the indigenous population. As the process of urbanization accelerates throughout the developing world, much of the wealth and income gap has been transferred to the urban sector. Differences between social strata are increasing as opportunities for publicly subsidized higher education, largely favoring the privileged upper half of the income groups, are not matched with an equal effort to expand public spending in basic education serving the lower-income groups. This point is underscored in the following table listing the distribution of public education subsidies across different expenditure quintile groups in seven countries (Guo, Steele, and Glewwe 1999 in IFC, 2001). The disproportionate allocation of subsidies to the rich—especially in Nicaragua, Vietnam, Côte d'Ivoire, and Pakistan—points to the highly inefficient use of public resources. In Nicaragua students in the highest quintile are receiving 46 percent of the subsidy, whereas students in the lowest quintile only receive 9.1 percent of the subsidy.

Table 2: Distribution of Public Education Subsidies Across Expenditure Quintiles (Percent of Total Subsidy).

	Expenditure Quintiles (lowest to highest)				
	1	**2**	**3**	**4**	**5**
Côte d'Ivoire	13.5	17.4	17.1	17.2	34.8
Guinea	8.5	13.1	21.1	30.4	26.9
Kenya	16.7	19.9	21.0	21.7	20.7
Nicaragua	9.1	11.8	14.0	17.6	46.0
Pakistan	14.3	16.7	19.4	20.5	29.1
Peru	17.1	25.5	23.4	18.5	15.5
Vietnam	12.2	16.1	17.1	19.2	35.4

Source: IFC 2001.

Expansion of the private sector is often considered as an indirect way of supporting access policies. To the extent that students and families in the middle and upper-income groups finance this expansion, it is expected to free public resources to focus on enhanced access to underserved groups. Furthermore, the competition with private providers is expected to improve management and accountability within the educational system, a topic discussed later. But perhaps most importantly it has been argued that the private sector often has played an important direct role in improving access to education, serving the educational needs of girls, the urban or rural poor, or particular ethnic groups, and might be expected to do a larger and better job with greater public subsidy or improved access to finance.

This point is demonstrated differently in the following examples from Colombia and Pakistan:

- *In Bogotá Colombia, the government explicitly included private providers within its access policy* (Uribe et al. 2006). Bogotá's Department of Education used a two-pronged strategy to meet the growing demand for primary schooling: first, it expanded the public sector through building schools, increasing class sizes, and re-assigning teachers from administrative posts, while also giving preference to low-income students; second, the department offered subsidies to private schools that enrolled low-income students. As a result, 53 percent of the students at the primary school level were enrolled in a private school, 90 percent of which were for-profit and 8 percent were religious schools working under government contract.

- *In Pakistan, the city of Quetta used private schools to extend access to low-income girls* (Kim, Alderman, and Orazen 1998). Public school constraints in serving girls were lifted through a fellowship program that was implemented through private providers. The absence of segregated girls' schools in poor neighborhoods often means that girls in poor communities do not enjoy any access to education unless alternative arrangements are made with private schools. As a result, the growth of private schools in Pakistan has risen steadily since 1979 (when a nationalization law was repealed) and private enrollment in rural areas accounts for as much as 45 percent of the total population. Moreover, private schools employ a substantially higher proportion of female teachers than public schools and have a female enrollment rate of 43 percent compared with 37 percent in public schools (Coulson 2003).

4.2 EFFECTIVENESS AND EFFICIENCY

Private provision of education is shown to be more effective in terms of student achievement on standardized tests and can be an effective alternative to publicly provided education. Most empirical studies in developing and some middle-income countries support this claim, yet also point to the fact that the effectiveness varies significantly across countries and is determined by factors including the strength of the private sector as well as the management capacity, teacher quality, pedagogic style, and responsiveness of a school to its clients. Socioeconomic status and family and peer characteristics have also shown to contribute to a large portion of the achievement difference.

The first empirical studies providing support to the hypothesis of the greater effectiveness of private as compared to public schools were conducted in the United States in the 1980s (Coleman, Hoffer, and Kilgore 1982; Murnane 1985; Murnane, Newstead, and Olsen 1985). These studies concluded that the average student did better in private than in public schools, after controlling for differences in family background. In the developing world, the first set of rigorous research projects comparing public and private schools as to their costs and educational outcomes was conducted under the sponsorship of the World Bank in the late 1980s, using a common methodology and with comparable results (Jimenez, Lockheed, and Pakeo 1991). The projects looked at secondary school students in five developing countries around the world.[2] They consistently showed that private school students outperformed public school students in standardized math and language tests.

In terms of efficiency, the same studies found that on average the unit costs of private schools are lower than those for public schools. For the same cost, private schools could provide as much as three times more learning as their public counterparts. The relatively higher efficiency is explained by more streamlined administrative and management practices in private schools. For example, in Thailand private schools make more efficient use of teachers by recruiting candidates with lower qualifications but providing them with rigorous in-service training and supporting them with better teaching protocols to manage their workload.

The authors, however, were careful in indicating the limitations of this set of studies in offering policy implications of their results: namely, that private schools are an efficient alternative to public schools and over-restrictive regulations (including outright prohibition) will deny an efficient alternative to public education. Moreover, the authors emphasize the need for governments to encourage private sector participation in

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[2] These countries include Colombia, Tanzania, Dominican Republic, the Philippines, and Thailand.

education, while keeping in mind that any efficiency gains are context-specific and dependent on the incentives and institutional environment in which it functions. They argue that the exact choice and design of government subsidies, of deciding to impose a tax exemption for certain schools or to negotiate a performance contract, for example, ultimately will affect the result of the intervention (James 1987).

In 1997 the UNESCO office in Latin America, in collaboration with 13 national ministries of education, assessed students' math and language achievement in the fourth year of primary schools using a common sampling methodology and survey instruments. A recent analysis of these data assessed the effectiveness of public and private schools in 10 countries (Somers, McEwan, and Williams 2004). Unlike previous studies, it controlled for the characteristics of student peer groups, a well-known advantage for private schools as, unlike public schools, they are able to enforce selective admissions. The study found that the achievement advantage of private versus public schools in fact disappeared when controlling for socioeconomic status and peer effects.

A more recent estimate of private school effectiveness uses data on math and language achievement across a sample of upper and middle-income countries (Vanderberghe and Robin, forthcoming). The study's substantive contribution is to show that private effectiveness varies significantly from country to country. In fact, a significant positive effect was found only in Dutch- and French-speaking Belgium and in Brazil, while there were no statistical differences in Mexico, Denmark, and Spain. In the remaining countries (Austria, France, and Ireland), the authors found divergent results according to the methods used.

Thus, the effectiveness and efficiency difference of private over public schools may depend finally on the predominant characteristics of the private sector in a given country, which differ widely in management styles, pedagogy, teacher quality, and ability to understand and respond to client needs. It also will depend on the relative strength of the public sector and segmentation of clientele in each sector.

4.3 ACCOUNTABILITY AND QUALITY OF EDUCATION

Policymakers have recognized that increased spending alone does not directly affect the quality of education or student achievement. There is recognition of the need to invest strategically to develop stronger assessment and accountability systems that cross public and private sectors and different dimensions of quality, such as teacher training and school management. Overall, higher accountability in private schools has the potential to increase the quality of education.

There has been a shift towards the achievement of quality schools in developing countries as policymakers are faced with the seemingly unavoidable choice between providing broad access to education and developing quality schools (Hanushek 1995, Hanushek and Raymond 2002). Research, however, shows that this is not an appropriate way to think about human-capital development. Grade repetition and high dropout rates lead to a waste of resources, in such a way that without quality there can be no real quantitative expansion (Lee and Barro 2000). Producing quality schools became, and still is, a major unachieved goal in many countries.

Differences in student achievement, as shown by the greater variance of testing results within developing countries, are calling the attention of education policy makers to the need to invest scarce resources more strategically and to understand better how quality of schooling (as determined by teacher and management quality, among other things) may be improved. Although the evidence on the efficiency advantage of private over public schools is mixed and context-specific, greater accountability—in part achieved through expanded participation of families, community organizations, and the private sector—has the potential to improve the quality of schooling.

Few studies have expressly surveyed parents on their satisfaction levels with private versus government schools. In 1999 the Public Report on Basic Education study was conducted in five northern states of India. Only 5 percent of the schools in these states are government-funded and the majority are unrecognized private schools. As one indicator of quality, the researchers examined the presence of teachers during regular school hours. They found only one in four teachers actually working in the public schools and one of every three headmasters absent. A higher level of teaching activity was found in private schools in which there was little regulation: teachers were present, more engaged, and actively doing their jobs in these schools (De et al. 1999).

National differences in student performance are not necessarily driven by the level of school spending, but by a host of other factors including the quality or availability of trained teachers. Systematic and standardized learning assessments are becoming a key tool for improving and sustaining quality at the school, district, provincial, and national levels. It is also opening the way for educational stakeholders to become more engaged with achieving higher school performance. Accountability systems are becoming more sophisticated in responding to the view that overall effectiveness and efficiency implies a better understanding of shared responsibilities, including the public and private sectors, different levels of leadership, and the teaching profession.

5. REGULATIONS AND CONDITIONS FOR PRIVATE INVESTMENT

Typically, governments try to control quality in the private sector through regulation. The regulatory frameworks governments use depend considerably on bureaucratic traditions, the degree of centralization, and the openness to international expertise in the field of education. Government support to private schools through subsidies such as tax exemptions, payment per student enrolled, or salaries for teachers, normally require a certain level of regulation and control over what private schools teach, the quality of their facilities, the competencies of the teachers, and the performance of their students (Kitaev 1999).

As countries developed national curricula for mandatory schooling, often following international standards, they tended to enforce them upon private as well as public providers, in particular under centralized systems. Thus, much regulation had to do with processes and education contents, such as curricula, language of instruction, and time allocated to different topics. Furthermore, educational inputs became strictly regulated in many countries, in particular for teacher credentials and background, as well as building facilities. Increasingly, regulation has focused on outcomes and requires examinations (often under external examiners, sometimes taking place in public schools). New regulatory frameworks were developed in conjunction with decentralization efforts in the public sector and new subsidies and incentives for the private sector to expand. As part of their decentralization reforms to shift control to the private sector, for example, Argentina and Chile introduced national assessment systems to evaluate and accredit schools and ensure that quality standards in teaching and learning were upheld. Support to private schools, in the form of transfer payments, contracts and vouchers, was conditioned on their provision of quality education. (Benveniste 2002). Based on 1994 data from Argentina, over 65 percent of all private schools received a sizable subsidy from government to cover either all or a portion of their recurrent costs (such as teacher salary and payroll taxes), suggesting an important financial opportunity for private schools (Tooley 2001).

Investment Conditions

The existing investment climate for private schools is closely tied to the regulatory and legal framework of the particular country. In order to monitor the quality of education and ensure that standards are upheld, governments stipulate barriers and conditions for entry into the market and thus are able to affect the overall supply and quality of education. On the one hand, oversight and control measures are required to protect consumers and ensure that schools focus on providing a quality education and not simply graduating as many students as possible (Wolff and Castro 2001). On the other hand, excessive barriers to entry may not ensure that approved institutions maintain high standards, but instead restrict competition and impede growth of the overall sector.

Based on a study of the private sector in 12 countries, Tooley notes that regulations are substantial but mainly ignored, enforced in an ad-hoc manner, or petty and cause inefficiencies. For example, Argentina has a mandatory national curriculum for primary and secondary schools that restricts competition and innovation in teaching methodology; Turkey prohibits all for-profit private education—including at the higher level—that has had the unforeseen result of corruption and bribery and measures to disguise profits (Tooley 2001). Any donor initiative to work with the private education sector must take into account the regulatory framework that governs private provision. The DCA mechanism will be the most effective in countries with a pro-private sector policy environment or at least one that does not significantly restrict the private sector.

6. PROMISING AREAS OF INTERVENTION IN THE PRIVATE SECTOR

A key finding of this paper is that the private sector is playing an increasingly prominent role in meeting un-met demand for basic education in developing countries. It is an important complement to the public sector today and has the potential to provide services more efficiently and of higher quality than the public sector. It also has a role to play in improving access. There is no question that the private sector for education varies by region and historical processes around privatization, its relationship with the public sector, and the consumer market and ability to pay to fees. Collectively, these factors will shape the choice and design of any intervention in the sector.

In seeking to achieve the goal of Education for All it is important for donors and governments to understand the contribution of the private sector and its potential as a partner. This calls for new strategies to engage the private sector as a partner and improve its ability to contribute to education goals. Based on the literature review and findings from this paper, potential strategies for engaging the private sector are identified in this section.

Strengthen the investment climate

The regulatory and investment climate is a key determinant of the scale, efficiency, and quality of services that is provided through the private and public sectors. Effective regulation will govern the efficient use of public resources and ensure access to quality education for all population segments; it will also draw on the private sector to stimulate growth, increase coverage, and reach differentiated markets. Beyond the provision of direct education, a conducive investment climate also will encourage a market for related educational services (including technology firms, publishing houses, and teacher-training institutes) that collectively have a role in strengthening innovation and service quality in education, and attracting additional local and foreign capital. Strengthening the investment climate also will require better systems for tracking and disseminating information (such as standardized indicators, achievement tests and financial information) so as to attract and stimulate investments.

Strengthening the regulatory and investment climate is not the sole responsibility of government. Public-private dialogue between various stakeholders, including ministries of education, NGOs, and for-profit providers, can raise awareness on the role of the private sector, stimulate new partnership ideas, and offer a basis for initiating favorable policy change. For example, such dialogue could address regulatory bottlenecks or barriers to entry for new schools, or lead to an exchange of innovative practices by different education specialists and stimulate a private sector response from potential new businesses (in teacher-training approaches, the use of new technology or curriculum, etc).

Institute effective accreditation systems

In order to ensure a balance between maintaining quality standards and encouraging competition and growth, it is necessary to institute accreditation systems appropriate for the private sector. These should focus on offering incentives for quality education rather than on instituting burdensome regulations or controls that impede entry into the market. Incentives for high quality can include access to public contracts, subsidies, loan schemes or targeted vouchers. Accreditation can be conducted in a two-stage process whereby schools pass a minimum certification to open a facility with teacher qualifications and certificates, and subsequently pass a more rigorous performance evaluation to qualify for public subsidies or benefits (Wolff and Castro 2001). Voluntary associations can serve as a mechanism to conduct evaluations and provide accreditation in a cost-effective manner.

Identify cost-effective and innovative models of service provision

The literature has identified different models that can be used to provide quality education. Networks of private schools that work within or across national borders are able to develop a recognized brand and reputation among consumers, can institute cross-subsidies to reach mixed student groups, gain efficiencies through group professional development and technology transfer, and attract foreign or local investment as they are seen as less risky. In India, for example, the DPS school network is able to cross-subsidize its rural village schools (that are run at a loss) through its core network of urban schools; it is also able to transfer used equipment and technology from the center to the rural village schools (Tooley 2001). Also, the Fe y Alegre network of private schools in Latin America has cost-effective mechanisms for teacher training, mentoring, and ongoing information exchanges within the network (Navarro and Verdisco 2000).

Ensure resources are efficiently targeted to different population segments

The limited availability of resources for basic education underscores the need to effectively map overall education provision, understand gaps and constraints to access, and develop a plan to target services appropriately. Such efforts will require information sharing and partnerships between the public and private sectors and should result in the complementary provision of education. Public-private partnerships in the form of management contracts to private schools, transfer of funds, or targeting of demand-side subsidies (vouchers or scholarships) can be developed to increase overall access, choice, and segmentation of the education market. Designing and implementing such interventions will call for improved access to market information and education statistics on enrollment and coverage, student achievement, ability to pay, and educational access.

Facilitate access to finance

Access to financing for the basic education sector can improve quality, efficiency, scale, and ability to increase access for targeted groups. Finance can directly support schools to improve their physical infrastructure, access to equipment, and other learning technology, or to support service providers in the education market. It can also be used for targeted loans to students or teachers. Facilitating access to finance may entail working with financial institutions to increase their receptivity to lend to this sector, sharing risk through the DCA guarantee, providing financial institutions with market information (including benchmarks for assessing the quality and standards of a given school), and training in lending to the sector.

Donors and governments that are interested in partnering with the private sector to achieve education goals should consider the aforementioned strategies and determine how appropriate they are given the country context. While it is beyond the scope of this paper to fully address all of these strategies, the remainder of this report will explore how improving access to financing can be used to engage the private sector in the delivery of basic education. It is recommended that further research be conducted to develop the other strategies. Ideally, financing initiatives should complement and build on other USAID-funded education activities in the private or public sector.

7. ACCESS TO FINANCING FOR BASIC EDUCATION

Access to finance is an important ingredient in private sector development, as it helps both individuals as well as businesses leverage outside resources that can be used make productive improvements. Sectors that are not able to access financing typically are constrained and underdeveloped. This paper will explore how access to finance is a constraint to the development of the private education sector and explore strategies to improve access to finance, with a focus on USAID’s DCA guarantee.

7.1 ACCESS TO FINANCE AND THE DEVELOPMENT OF THE PRIVATE SECTOR

Limited access to finance for the private sector is a shared constraint in developing countries. Empirical evidence on the role of credit to stimulate economic growth has been demonstrated across sectors, with developed countries enjoying higher growth rates partly because they have more vigorous credit markets. According to the *World Bank Indicators 2004*, annual domestic credit provided by the banking sector in high-income countries averaged 168 percent of gross domestic product (GDP), 83 percent in middle-income countries, and 48 percent in low-income countries (Freedman 2004). Even where credit is available to businesses in less developed countries, the loans are often short-term, have high collateral requirements, and are restricted to certain sectors. The low volume of lending by banks is attributed less to the availability of funds than to the broader financial regulatory framework, including high central bank reserve requirements, limited legal authority to claim rights on borrower defaults, high interest rates, lack of reliable information about borrowers, and limited experience working with the private sector overall (Freedman 2004).

Financial institutions are especially reluctant to lend to sectors that are perceived to be risky and not profitable, including the education, health, and other social sectors. As legal and policy reforms are implemented, banks will be more inclined to increase their lending to the private sector; however, banks often perceive new sectors as inherently risky and are reluctant to invest resources in them even when favorable changes are made to the legal and regulatory framework (Freedman 2004). This is especially the case when potential borrowers are small- and medium-sized businesses, as are commonly found in the private education sector, which may not meet traditional commercial-sector collateral requirements. There is typically little incentive and inadequate market information available for lenders to reach new sectors and develop new and targeted financial products.

7.2 THE CURRENT STATUS OF EDUCATION SECTOR LENDING

The literature review did not reveal any formal, multi-country, research on the current status of education sector lending in developing countries. In the future if USAID or other donors are interested in expanding access to financing for the private education sector, a formal survey of financial institutions across priority countries would improve knowledge and refine recommendations on how to improve access to financing for the private education sector. This proposed study should identify the current size of education sector loan portfolios and obstacles and opportunities to lend to the sector.

Anecdotal conversations with bankers in developing countries as well as findings from work the International Finance Corporation (IFC) conducted point to a number of obstacles to lending to the sector. First, there is the perception of higher risk. As was described previously, traditionally education has been the purview of the public sector, and almost everywhere it is considered a public good and a basic human right. Accordingly, many bankers question how education can be a for-profit business capable of repaying a loan or they do not recognize the increasing pressure put on individuals or families to finance education. As a result, many financial institutions are unaware of the growing market opportunities in the private education sector. Second, most loan officers are not familiar with private school business models and cash-flow cycles or how to identify risks and opportunities in lending to the sector. This unfamiliarity is compounded by the fact that many private education providers are structured as not-for-profit organizations and many financial institutions are wary of lending to not-for-profits regardless of their ability to repay loan. Third, financial institutions often hesitate in taking school property as collateral on a loan because it could be difficult politically to seize and liquidate a school. Fourth, bankers are often reluctant to consider making student loans, which are typically made to individuals who are not employed. In many developing countries, future employment opportunities, even with a degree, may be limited and thus student loans are considered highly risky. Fifth, potential borrowers in the education sector are normally educators, not business people, and are as unfamiliar with developing bankable business plans and loan applications as the bankers are unfamiliar with the education sector. All of these factors constrain lending to the education sector.

7.3 THE IMPACT OF LACK OF ACCESS TO FINANCE ON THE PRIVATE EDUCATION SECTOR

Lack of access to financing for school construction and equipment is one of the main impediments to entry into the private education sector (Wolff and Castro 2001). This translates into a necessity for schools and related service providers to rely on their savings and loans from family and friends, which has serious implications on the size of the private education sector and ultimately the quality of education. If the private education sector is going to be able both to meet increasing demand and comply with public-sector regulations, it will need better access to financing. In addition, offering the possibility of student loans can help alleviate financial pressures, particularly those associated with secondary school. Families are likely to contribute an increased portion of their income to education at the secondary level where there is relatively less public subsidy, or where parents chose to send their children to a more expensive private school because of quality, reputation or convenience. In general, while many families have the ability to pay school fees over time, the lump sum annual or semi-annual payments that private schools (and some public schools) charge can be difficult and create unnecessary family cash-flow shortages and hardship. Access to finance is an important strategy to strengthen the overall scale and quality of education supplied by private education institutions and related service providers and to facilitate targeted demand-side interventions, such as school loans.

7.4 PAST USAID AND OTHER DONOR SUPPORT TO FINANCE PRIVATE EDUCATION

Recognizing the important role of the private education sector and the potential that access to finance can play in the development of the sector, some donors, including USAID and some of the development banks, have begun to channel their support to develop the private education market. Most of these efforts have focused on higher education.

USAID's DCA Guarantees

Since 1999 USAID has used its partial credit guarantees to increase access to finance for a variety of private sector businesses, including small and medium enterprises, agriculture cooperatives, and municipalities—an effective way to draw capital from local financial institutions into sectors traditionally underserved by financial markets. As of 2006, the total DCA portfolio was worth over $1 billion, representing growth of over 19 percent from its portfolio of $845 million in 2005 The DCA has a total of 160 guarantees in 46 countries. Partner banks have disbursed $452 million of DCA-supported credit to date or 45 percent of the total portfolio. By sector, the largest share of the portfolio is targeted to small and medium enterprises (28 percent), followed by lending in agriculture and micro-enterprise sectors (19 percent each). The education and health sectors comprise the smallest share of the portfolio at approximately 1 percent or $10 million each.

The DCA guarantees in the education sector have been made for higher and tertiary education. Two DCA guarantees have been made in the education sector, one in Panama and another in Vietnam. These represent around 3 percent of the guarantee portfolio in Latin America and 1 percent of the portfolio in Asia and the Near East.

Initiatives by other donors

The World Bank, the IFC, the IDB, and the Asian Development Bank have played important roles supporting and lending to the education sector in developing countries. What follows is a summary of investment trends by the World Bank and IFC.

World Bank lending for primary education comprises a significant share of its portfolio but is reserved for public-sector loans for policy-level reforms including student financing or capacity building, or loans that are on-lent to the private sector for specific projects. Between 1995 and 2000, the World Bank projects have included building public-sector capacity to develop public-private partnerships at the primary level (Djibouti), improving quality improvement in teacher training and curriculum programs for private schools (El Salvador), and instituting competitive principles for public-private partnerships at the higher level (Indonesia).

The IFC’s activities in education have grown steadily in the last decade. Recent 2006 data indicates its total portfolio in education is $165 million, of which approximately $16 million is targeted to elementary and secondary schools. Unlike the World Bank, the IFC lends directly to the private sector by investing in educational institutions and supporting student-loan schemes. Its lending has traditionally focused on higher education sectors that experience higher growth, but the IFC is increasingly channeling support to the basic education sector. It currently has over six projects targeted to primary and secondary education, including loans for school construction and expansion in Lebanon, Mexico, and Indonesia and partial guarantees to financing facilities in Ghana and Kenya. (See Annex 4 for a description of the deals in Kenya and Ghana). Other recent projects in the IFC portfolio include establishing a financing facility for higher education student loans in Indonesia, supporting a technology firm to roll out information and communication technology to universities in Nigeria, providing low-cost primary and secondary education for disadvantaged townships in South Africa, and supporting the expansion of private international schools in Lebanon and Kenya.

Key lessons from IFC financing of the private education sector

The Health and Education Department at the IFC has drawn a number of important lessons from its experience in investing in the private education sector, which should be considered in developing future education sector DCAs and in promoting lending to the sector (IFC 2001).

- The management capacity of private education providers is limited. For-profit institutions tend to have stronger managerial capacity and their for-profit status has not been shown to negatively influence the quality of the education.
- Local loans and guarantees are necessary in most investments to protect against foreign-exchange currency risk and stimulate lending by local banks.
- Alternatives to traditional loan collateral, such as using escrow accounts, are needed because of the political risk associated with a foreclosure on schools.
- Changing regulatory environments in many countries have had a significant favorable impact on IFC investments.

Going forward, the IFC recognizes that it needs to develop financial instruments to deal with smaller projects that require less than $5 million (its typical project investment) and often less than $1 million. In addition to processing smaller deals, the IFC will look at networks of education providers, which would act as the financial intermediary. The Health and Education Department also plans on collaborating with the Small and

Medium Enterprise Department of the IFC to transfer learning between sectors and link up with its capacity-building facility (IFC 2001).

7.5 LOOKING FORWARD: ADDRESSING THE FINANCING GAP

While there is increasing donor involvement in financing the private education sector, to date these efforts have been largely focused on higher education. Several factors explain this focus. Higher education providers often require larger financing amounts, which make them more attractive borrowers and investees. In many countries the private sector plays a more significant role in the higher education sector, which is therefore seen as a better market opportunity. As the literature review has shown, however, the private sector is also an important actor in basic education. Increasing access to financing for the basic education sector is an important strategy to strengthen the supply and quality of education. Given the relatively nascent nature of financing to this sector, there is a significant opportunity for USAID to take a leadership role in expanding access to financing for basic education. Decisions on the type and structure of financing will be based on a thorough assessment of the specific context: the legal/regulatory environment governing public and private schooling, the commercial financial market, and financial and capacity needs of schools will all influence decisions on whether and how to facilitate access to financing. In broad terms, however, this lending can be distinguished by supply and demand.

Expanding supply and quality of basic education

Expanding the overall supply of private sector education will improve access to underserved communities; it will also stimulate competition and improve the quality of education. Financing for the basic-education sector can be targeted directly at private schools, networks of schools, or to related service providers in the education market, such as institutes for accreditation, professional development centers, research and curriculum development agencies, or school transport providers. Such institutions will generally call for smaller scale investments that can be appropriately channeled through local financial institutions. Schools and related service providers have a number of financing needs, including:

- physical infrastructure—renovations, construction, or purchase of property
- equipment and technology—computers, science labs, sporting equipment, or musical instruments
- educational materials for student learning—digital or web-based learning software, audio-visual learning aids, and textbooks
- professional development opportunities—instituting ongoing in-service teacher training or peer-to-peer mentoring, launching on-line discussion forums and chat groups, and creating loan funds for teachers to access training at external institutes
- general operations—teacher salaries or ongoing expenses covered through working capital loans

Improving access and equity through demand-side financing

Commercial financing can be targeted to individuals in the form of student loans to ensure access to educational services—a mechanism for students to finance their education through borrowing. Loan funds can be targeted to needy students to help them cover the difference between the enrollment fee and their capacity to pay. Student loans encourage individual responsibility and are based on the expectation of increased earnings after completion of education. For this reason financing of loan funds for students is most appropriate at the higher or tertiary level where they are closer to entering the labor market and can expect a return on their education in the form of wages.

At the basic education level, loans still might be offered to families to allow their child to attend a particular school, especially at the secondary level where the practice of charging user fees is more common and of a higher amount. A loan also can enhance a family's range of choices and enable it to overcome an existing (perhaps temporary) financial barrier to attending a school of their preference. Given the predominance of the public sector in the provision of basic education, the demand for credit by parents to finance their child's education at this level may be more limited.

Evidence on the effectiveness of student loans suggests that these are best administered by a company (school or financial institution) rather than by government. The rates of default on government loans are traditionally high because of moral hazard. In the early 1990s it was found that loan recovery rates on government loans were typically less than 50 percent in developing countries (Albrecht and Ziderman 1992, UNESCO 2002). Loan schemes are found to be more effective when administered directly by a school. Arguably, there is an inherent honor system where students feel indebted to the school and realize that any delayed payments will only affect the ability of students in the future to continue attendance (Tooley 2001). Thus, servicing education loans by private financial institutions in partnership with a local school will ensure that qualifying students access the loans and that these loans are closely monitored.

8. THE DCA GUARANTEE AND THE PRIVATE EDUCATION SECTOR

This section discuss the contributions that the DCA can make with regard to private sector providers of education, which has an important role to play in partnering with the public sector to achieve education goals. Access, quality and scale in the private sector, however, are constrained by lack of access to financing. The constraints to increased education sector lending have been described previously: perceptions by financial institutions of higher risk, concerns about collateral, lack of information about the sector, and lack of understanding within the education community of a bankable business model. Despite these constraints, in many countries the private education sector is growing and profitable and could be an interesting new market for financial institutions that are looking to grow, remain competitive, and increase market share. As a result there are opportunities to work with financial institutions to promote education sector lending, thereby contributing to USAID's education goals.

One important strategy in promoting education sector lending is USAID's DCA guarantee, a proven tool to stimulate lending to underserved markets. The DCA guarantees up to 50 percent of the loss on a loan or a portfolio of loans. By providing a risk-sharing guarantee, the DCA can help banks overcome their concerns about a new and possibly risky market, such as the education sector. By sharing risk the DCA can help banks in lending to underserved sectors, such as private primary or secondary schools; offer longer terms, which are essential for school construction loans; and reduce conservative collateral requirements, which have posed a major constraint to education sector loans. The DCA also can mobilize local capital to support the education sector, leveraging important new resources to complement USAID's education programming.

These guarantees can also support the long-term capacity of local financial institutions to serve the education sector overall. In the process of conducting due diligence, assessing risk or monitoring loans, financial institutions will develop their understanding of the sector. The DCA guarantee can help demonstrate the profitability of lending to the education sector and serve as a catalyst for future development of the sector.

USAID's ODC offers four products under a shared-risk guarantee: the individual loan guarantee, loan portfolio guarantee, bond guarantee, and portable commitment guarantee. Loan guarantees and portable guarantees can be used to support specific projects. Loan portfolio guarantees can be effective in reaching multiple small schools or related service providers in the education sector. Bond guarantees have the most potential in municipal financing of education sector projects. Each of these guarantees will be discussed in relation to potential for application to the education sector.

8.1 TYPE OF DCA GUARANTEES AND THEIR POTENTIAL USE

Loan Guarantees

The ODC offers individual loan guarantees that cover 50 percent of the risk of an individual loan to a pre-determined borrower. These can be effective to support specific investment projects, including infrastructure to build a new school, or to support a related service provider to develop advanced technology or a specialized curriculum. If USAID is working with a specific partner in the education sector, it may want to consider a loan guarantee to complement additional programming with this partner.

Portable Guarantee

The portable guarantee is a commitment letter between USAID and a prospective borrower that helps to open the door for the individual business or entity to access financing. Portable guarantees are appropriate for specific purposes when the borrower is known, but the lender is not yet known. USAID enters into an agreement with the lender once the prospective borrower is approved. Like the individual guarantee described previously, these can be used for a specific project or activity in the education sector. Portable guarantees can enable schools or other related service providers to shop around and obtain the best possible terms with a financial institution with which they want to build a relationship. As with loan guarantees, the portable guarantee allows USAID to support a specific private education sector partner and activity.

Loan Portfolio Guarantees

Loan portfolio guarantees cover 50 percent of the loss to a lender from a portfolio of loans that is targeted for a certain group of borrowers. Loan portfolio guarantees have the most potential for maximum impact on the basic-education sector and can be structured with financial institutions to support multiple loans to schools and other education companies. Loan portfolio guarantees can assist financial institutions enter the education market in a significant way, while mitigating some of the risk. Loan portfolio guarantees can be used to support a variety of financing needs, such as working capital, construction and school renovation, purchasing equipment, and technology upgrades. Loan portfolio guarantees can also be used to service individual loans to students or to teachers. These can be administered in collaboration with specific accredited educational institutions, based on their target market or educational orientation, with defined criteria for offering loans to students or teachers based on need and merit.

Bond Guarantees

The DCA's bond guarantees support the issuance of bonds by financial institutions, private sector corporations, and sub-sovereign entities by covering 50 percent of the risk to bondholders. Bond guarantees can be structured to assist financial institutions to reduce the risk of their education portfolio by raising bond financing. This option is only possible in countries with sophisticated financial systems that include a broad range of investors. Furthermore, as most financial institutions in developing countries do not currently have large education portfolios, the demand for bond financing as a risk management strategy will most likely be nominal in the short run.

The most likely education sector bond guarantees would either involve bonds issued by large education companies, not-for-profit organizations, or municipal bonds supporting education projects. As has been seen in the health sector, in many developing countries the financing requirements of most education organizations will be too small to attract institutional investors. This makes bond financing unlikely for the vast majority of schools or other education companies, particularly those operating in basic education. In some countries, bond financing may be appropriate for larger organizations operating in higher education, such as universities, which may have substantial financing requirements.

For these reasons, bond guarantees—a type of long-term borrowing that sub-sovereign governments can use to raise money—may have the greatest potential to support municipal financing of basic education projects. Municipal governments use bonds to finance major capital investments, such as educational facilities, that support services that are delivered over time. While sub-sovereign financing is fairly undeveloped in many parts of the world, some countries, in particular Mexico, are making important strides in this area. Municipal education sector bond financing could potentially be an interesting public-private partnership to support basic education in some parts of the world. By leveraging private, local financing, municipalities may be able to invest in long-term capital projects that improve quality and access to basic education.

8.2 IDENTIFYING APPROPRIATE COUNTRIES FOR THE DCA GUARANTEE

Suggested regions for the DCA

Preliminary suggestions of regions and countries where donors might invest are offered based on the literature review. Decisions on whether to utilize the DCA to strengthen the basic private education sector in a given country will be based on a number of factors, including the potential of the private education sector, its ability to meet USAID missions' education objectives, and the strength of the financial sector. It should be considered first in countries where USAID has a strong presence and commitment to growing the basic-education sector. (Annex 2 contains a complete list of 55 countries where USAID has basic education programs.) Beyond this criteria, this report recommends additional factors that should be examined to determine the strength and investment potential of the private education sector in a given country, summarized in the table below. (A more complete guide to assessing the private education sector is provided in Annex 3.) A decision to introduce the DCA guarantee will also be based on an in-depth financial-sector assessment, including a mapping of existing lending by commercial banks and microfinance institutions that is not fully addressed in this report.

Table 3. Key Factors Affecting the Strength of the Private Education Sector

Private funding to education	Relatively high levels of private funding to education (through user fees and other private contributions from NGOs, communities and corporations) signal opportunities to increase private supply of education.
Enrollment in the private sector	Existing private sector enrollment will provide a good indication of the different sources of supply available to families and the overall demand for privately provided education.
Government policy towards basic education	The concrete policies of the government in meeting EFA objectives, and its commitment to public-private partnerships, will indicate whether the broader policy climate is favorable to private sector participation in basic education.
Licensing and regulation of private education	When regulations that seek to accredit providers and ensure quality standards are over-restrictive and burdensome, they may inhibit competition and innovation by private providers.
Investment climate	A key determinant of the potential strength of the private sector is whether the existing investment climate, shaped in part by government policy towards it, offers incentives for new providers.
Potential market for private basic education	The potential market for private basic education can be estimated by unmet consumer demand as well as by the existence of private schools at other levels or the existence of suppliers providing related services.

Given the scarcity of standardized national data on all these suggested indicators, additional research and country assessments on the current education and financial sectors will need to be conducted in order to fully understand the risks and opportunities in a given country. However, a few key indicators for assessing the market of private education, and for which data is more readily available, is provided in the following table for countries where USAID is funding basic education programs. This includes enrollment in the private sector, public sector expenditures in education and an index ranking from the World Bank on the ease of doing business in a particular country.

The data on private sector enrollment at the basic education level shows a mixed picture: high enrollments in much of sub-Saharan Africa, a number of Asian countries and Latin America and the Caribbean, and a nominal share in Europe and Eurasia. While this data does not offer a breakdown distribution by region or socioeconomic status, it is nonetheless an important starting point to recognize the significant role of the private sector in meeting existing demand.

As indicated in the table, in most sub-Saharan African countries, private sector enrollments exceed 20 percent of total enrollment in at least primary or secondary education in a number of countries, including Benin, Djibouti, Ghana, Guinea, Liberia, Mali, Rwanda, Senegal, and Uganda. The share of enrollments at the secondary levels in Rwanda and Uganda, in fact, exceed 40 percent of the total. In Asia, countries with high private sector enrollments include Bangladesh (comprising 96 percent at secondary levels), India, Indonesia, Jordan, Nepal, Pakistan, and the Philippines. While most countries have higher private sector enrollments at the secondary level, at least 30 percent of the students at the primary level in Pakistan, Jordan and Bangladesh attend schools in the private sector. In Latin America and the Caribbean the relative proportion of private enrollments is markedly higher at the secondary level, with over 20 percent in Bolivia, Dominican Republic, El Salvador, Guatemala, Nicaragua, and Peru. In fact, in Guatemala, the private sector enrollment at the secondary level is as high as 74 percent. As noted previously, all countries in Europe and Eurasia where USAID has programs (and for which data is available) have less than 1 percent share of private sector enrollment in either primary or secondary levels.

The composite business climate indicator from the World Bank Doing Business database provides an objective measure of business regulations and their enforcement, and is comparable across 175 countries, ranked in descending order from 1 to 175. The indicator provided in the following table is an average of country percentile rankings from a set of 10 indicators, including starting a business, dealing with licenses, hiring and firing, registering property, getting credit, protecting investors, paying taxes, trading, enforcing contracts, and closing a business.[3] Together they indicate the regulatory costs of business and can be used to analyze specific regulations that enhance or constrain investment, productivity, and growth in a particular country. For example, in Asia and the Near East, Jordan (ranked at 78) and Bangladesh (ranked at 88) have relatively conducive business environments as well as high private sector enrollments. In sub-Saharan Africa,

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[3] A ranking on of each of these components can be accessed on the Doing Business website: http://www.doingbusiness.org/CustomQuery/.

Namibia and South Africa stand out in their strong business climate rankings, at 42 and 29 respectively, but both countries also have a predominant share of their basic education enrollment in the public sector. Thus, while each indicator sheds light on a particular factor affecting the private education sector, it should be taken together with other variables and conditions in a particular country.

Table 4. Select Enrollment, Expenditure and Business Climate Data for Countries with Basic USAID Programs.

		Private Enrollment Share (%)			Public Education Expenditure		Ease of Doing Business[4]
Region	**USAID Country**	**Year**	**Primary**	**Secondary**	**Year**	**% GDP**	**Rank 1-177**
Africa	Angola	-	-	-	2001	2.61	156
	Benin	2004	10.81	19.75	2002	3.26	137
	Congo, Dem. Rep.	2002	11.11	13.38	-	-	175
	Djibouti	2004	15.46	21.03	2004	6.07	161
	Eritrea	2004	7.77	6.17	2004	3.78	170
	Ethiopia	2005	4.63	5.94	2002	4.59	97
	Ghana	2005	20.52	14.39	1999	4.11	94
	Guinea	2004	20.58	9.78	2000	1.85	157
	Kenya	1991	-	10.9	2004	7.05	83
	Liberia	1999	38.44	37.15	-	-	-
	Madagascar	2004	19.34	-	2004	3.29	-
	Malawi	1992	9.5	-	2003	6.03	110
	Mali	2004	34.77	22.38	1999	2.99	155
	Namibia	2002	4.3	4.43	2003	7.22	42
	Nigeria	2000	4.76	-	1995	0.65	108
	Rwanda	2003	0.84	44.05	2000	2.75	158
	Senegal	2004	11.17	26.25	2004	4.04	146
	Somalia	-	-	-	-	-	-
	South Africa	2003	2.04	2.57	2004	5.37	29
	Sudan	2004	4.41	10.44	1996	7.63	154
	Tanzania	2004	0.58	-	1999	2.17	-
	Uganda	2004	9.07	44.58	2000	2.48	107
	Zambia	2004	2.44	3.76	2004	2.84	102
Asia and Near East	Afghanistan	-	-	-	-	-	162
	Bangladesh	2003	38.86	95.92	2004	2.25	88
	Burma	-	-	-	-	-	-
	Cambodia	2003	0.89	6.43	2004	2.01	143
	Egypt	2004	7.97	5.49	1995	4.67	165
	India	2003	17.04	41.89	2003	3.26	134
	Indonesia	2004	16.32	42.94	2003	0.94	135
	Iraq	-	-	-	-	-	145
	Jordan	2004	29.89	16.57	1999	4.95	78
	Morocco	2004	5.48	4.59	2004	6.31	115
	Nepal	2005	15.22	26.73	2003	3.39	100
	Pakistan	2004	35.96	22.86	2004	1.97	74
	Philippines	2004	7.26	19.72	2003	3.22	126
	Yemen	2004	1.8	1.68	2001	9.64	98

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[4] These rankings are based on 2006 data.

		Private Enrollment Share (%)			Public Education Expenditure		Ease of Doing Business
Region	**USAID Country**	**Year**	**Primary**	**Secondary**	**Year**	**% GDP**	**Rank 1-177**
Europe and Eurasia	Armenia	2004	0.82	0.55	2002	3.17	34
	Kazakhstan	2004	0.68	0.84	2004	2.39	63
	Kyrgyz Republic	2004	0.26	0.46	2003	4.45	90
	Macedonia, FYR	2004	-	0.5	2003	3.37	92
	Russian Federation	2004	0.46	0.48	2003	3.68	96
	Tajikistan	-	-	-	2004	2.78	133
	Turkmenistan	-	-	-	1991	3.94	-
	Uzbekistan	-	-	-	1996	7.67	147
Latin America and the Caribbean	Bolivia	2002	19.59	28.03	2004	6.37	131
	Dominican Republic	2004	14.8	24.91	2004	1.14	117
	El Salvador	2003	9.68	20.15	2004	2.77	71
	Guatemala	2004	11.5	73.94	1996	1.63	118
	Haiti	-	-	-	1990	1.51	139
	Honduras	1993	5.5	-	1995	3.61	111
	Jamaica	2004	8	5.79	2004	4.88	50
	Mexico	2004	8.07	15.46	2003	5.79	43
	Nicaragua	2004	15.27	28.27	2003	3.12	67
	Peru	2004	15.31	21.58	2002	2.99	65

Sources: World Bank EdStats and Doing Business databases.

9. ADDITIONAL STRATEGIES TO EXPAND ACCESS TO FINANCE FOR THE EDUCATION SECTOR

While the DCA is a key mechanism in expanding access to finance for the private education sector, additional strategies should be considered. Due to the significant constraints that have been identified, utilization of an education sector DCA would most likely benefit from additional technical assistance, including:

- *Market research*: In addition to perceived risk, one of the biggest impediments to education sector lending is lack of market information. Financial institutions will be more interested in lending and marketing to the private education sector if they have a good understanding of the market size, geographic location, and trends.

- *Training in education sector lending*: A key obstacle to lending to the education sector is sufficient familiarity with the usual business model of education institutions as well as cash flow and collateral issues. Training loan officers and bank managers in lending to the education sector and how to structure loans to the sector will improve the utilization of an education sector DCA.

- *Loan product development*: In some cases existing financial products will not fully meet the financing needs of the private education sector. Technical assistance to financial institutions in developing appropriate loan products will increase the likelihood of appropriate and timely financing to private education organizations.

- *Market referrals*: Market referrals are another strategy to promote the utilization of an education sector DCA and education sector lending. Referring bankable, education sector borrowers to financial institutions can achieve two goals. It can jump-start a financial institution's marketing effort to the sector. It can also feed directly into the USAID mission's education goals, by ensuring that private education companies that are contributing to increased access and improved quality are being referred to financial institutions that are willing to lend to them.

- *Borrower training and access to business-development services*: Another obstacle to access to finance is the limited business skills of many education companies, which are often founded by teachers without formal business training. Training private education companies in business planning, financial management, and access to financing can improve their ability to prepare a bankable loan application and obtain financing.

10. CONCLUSION

In the context of inadequate public expenditures towards education, various models of private education have filled the gap to complement public provision. Some entail explicit public subsidies in the form of transfer payments, tax incentives, or vouchers to private schools; in other cases, private schools operate autonomously under government oversight and regulation. There is evidence across the board of private household contributions towards basic education, both in private and public schools. Meeting the goals of universal access to basic education will require that government and donor subsidies are reserved for the neediest populations, while private contributions are recognized and leveraged at primary, secondary, and tertiary levels. Ensuring an efficient and equitable allocation of total education resources will call for partnerships between the government, donor, and business sectors. The role of government is especially critical to set and enforce standards regarding the quality of teaching and learning, and to determine the best mix of subsidies and incentives to encourage the growth of private schools that serve public objectives. While there is no single best public-private approach to addressing the objectives of Education for All, there is little question that the private sector will continue to play a complementary role in charting the way forward.

Access to financing is an important component to strengthen the private sector's ability to provide quality services and increase the overall supply of this public good. Financing alone will not ensure these outcomes, but access can be offered as an incentive to stimulate growth of new schools, especially those that serve disadvantaged groups, or to enable existing schools to invest in new technology and improve their efficiency and competitiveness. Increased access to financing can also spur growth in the overall education marketplace and allow teacher training firms or curriculum specialists to test digital innovations or to model new approaches for increasing access to rural areas. Dialogue and partnerships between public and private stakeholders to identify major financing gaps and opportunities in a given country can be a first step towards increasing the role of the private sector in basic education.

ANNEX 1: DISTRIBUTION OF PUBLIC AND PRIVATE ENROLLMENT IN SELECT COUNTRIES

		Primary Education			Lower Secondary Education		
		Type of Institution			Type of Institution		
WEI Participant	**Year**	**Public**	**Government-dependent private[5]**	**Independent private**	**Public**	**Government-dependent private**	**Independent private**
Argentina	2002	80.2	16.3	3.5	78.0	18.8	3.2
Brazil	2002	91.8	a	8.2	90.6	a	9.4
Chile	2003	51.6	41.4	7.0	55.2	37.9	6.9
Egypt	2002/03	…	…	…	94.6	1.0	4.4
India	2002/03	80.8	6.0	10.7	67.0	14.4	18.6
Indonesia	2002/03	83.9	a	16.1	63.8	a	36.2
Jamaica	2002/03	95.2	a	4.8	99.0	a	1.0
Jordan	2002/03	70.8	a	29.2	80.8	a	19.2
Malaysia	2002	99.1	a	0.9	97.0	a	3.0
Paraguay	2002	84.4	10.3	5.3	79.4	12.2	8.4
Peru	2002	86.3	3.4	10.3	83.1	4.8	12.1
Philippines	2002/03	92.9	a	7.1	80.3	a	19.7
Russian Federation	2002/03	99.6	a	0.4	99.7	a	0.3
Thailand	2003/04	85.0	15.0	x(2)	93.7	6.3	x(5)
Tunisia	2002/03	99.1	a	0.9	98.6	a	1.4
Uruguay	2002	87.1	a	12.9	88.3	a	11.7
Zimbabwe	2003	13.1	86.9	a	…	…	a
WEI mean	2003	81.4	11.1	7.9	81.0	9.8	9.8
OECD mean	2003	89.5	8.2	2.4	85.9	11.4	2.7

Symbols for missing data	
a	Data not applicable because the category does not apply.
…	Data not available
x (y)	Data included in another category/column of the table

Source: World Education Indicators Survey, UNESCO 2005.

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[5] Government-dependent schools receive more than half their funding from government institutions; independent private institutions receive less than half from public sources.

ANNEX 2. COUNTRIES IN WHICH USAID CURRENTLY HAS BASIC EDUCATION PROGRAMS

Africa

1. Angola
2. Benin
3. Djibouti
4. DR Congo
5. Eritrea
6. Ethiopia
7. Ghana
8. Guinea
9. Kenya
10. Liberia
11. Madagascar
12. Malawi
13. Mali
14. Namibia
15. Nigeria
16. Rwanda
17. Senegal
18. Somalia
19. South Africa
20. Sudan
21. Tanzania
22. Uganda
23. Zambia

Asia and Near East

1. Afghanistan
2. Bangladesh
3. Burma
4. Cambodia
5. Egypt
6. India
7. Indonesia
8. Iraq
9. Jordan
10. Morocco
11. Nepal
12. Pakistan
13. Philippines
14. Yemen

Europe and Eurasia

1. Armenia
2. Kazakhstan
3. Kyrgyzstan
4. Macedonia
5. Russia
6. Tajikistan
7. Turkmenistan
8. Uzbekistan

Latin America and Caribbean Region

1. Bolivia
2. Dominican Republic
3. El Salvador
4. Guatemala
5. Haiti
6. Honduras
7. Jamaica
8. Mexico
9. Nicaragua
10. Peru

ANNEX 3: SUGGESTED GUIDELINES TO ASSESS THE STRENGTH OF THE PRIVATE BASIC EDUCATION SECTOR

1. Funding for Education

Relatively high levels of private funding to education (through user fees and other private contributions from NGOs, communities and corporations) signal opportunities to increase private supply of education.

- What is the total national expenditure on basic education? (Note that donor funding may be channeled through government or be off-budget).

- What percentage of total expenditures are private expenditures?

- How are public and private expenditures allocated between primary and secondary levels of education?

- What percentage of household income is spent on education?

- Do families pay fees to attend schools in the public sector? How comparable are the fees between public and private sectors?

- In addition to tuition fees are there other expenses that families incur (textbooks, uniforms, dues to the PTA, etc.) in the public and private sector?

2. Enrollment in the Private Sector

Existing private sector enrollment will provide a good indication of the different sources of supply available to families and the overall demand for privately provided education.

- What percentage of enrolled students in primary and secondary school are enrolled in the formal private sector? (Supplementary data may be available from the national or municipal Ministries of Education)

- Who are the main providers of private education (NGOs, community groups, for-profit companies)?

- What market niches do each of the different private providers serve? (Urban middle/upper class, urban poor, underserved rural or slum communities, etc).

- Are the statistics not representing certain private providers, including those considered informal?

3. Government Policy Towards Basic Education

The concrete policies of the government in meeting EFA objectives, and its commitment to public-private partnerships, will indicate whether the broader policy climate is favorable to private sector participation in basic education.

- What role does the government play in mitigating or exacerbating differences in educational opportunities?

- Has the government established financial incentives to increase demand for education? (For example, through vouchers, scholarships or loan schemes)

- What is the government policy on private provision of basic education?

- Does the government subsidize private schools? What are the rules governing these subsidies?

- Does the government contract with other service providers in the education market? (For example, in student testing, curriculum development, transportation)

4. Licensing and Regulation of Private Education

When regulations that seek to accredit providers and ensure quality standards are over-restrictive and burdensome, they may inhibit competition and innovation by private providers.

- Are the procedures for licensing and accreditation of private providers burdensome or easy?

- Are there restrictions on for-profit schools to operate in the basic education sector?

- Are there mechanisms for the government to ensure quality education among all providers? (For example, through standardized assessment systems).

- Can and do students easily transition between the private and public sectors?

5. Investment Climate

A key determinant of the potential strength of the private sector is whether the existing investment climate, shaped in part by government policy towards it, offers incentives for new providers to enter.

- Are there incentives for private providers to benefit from government subsidies, tax breaks or state-sponsored programs?

- Are commercial banks lending to the education sector?

- How acceptable is foreign investment to the education sector?

- What is the overall “Ease of Doing Business” ranking of the respective country? (This is an aggregate benchmark created by the World Bank that includes indicators such as the ease of starting a business, dealing with licenses, registering property, getting credit, etc). See http://www.doingbusiness.org for further information.

6. Potential Market for Private Basic Education

The potential market for private basic education can be estimated by unmet consumer demand as well as by the existence of private schools at other levels or the existence of suppliers providing related services.

- What is estimated un-met demand for basic education? (This can be estimated by the number of students currently not enrolled in school by education level, socio-economic status or geographic area; market surveys on consumer preferences regarding education can also be very useful to assess demand).

- What are the main gaps to providing quality education to communities or sectors expressing highest unmet demand?

- Are there opportunities for the private sector to play a role in filling this gap?

- What role does the private sector play in other education sectors, including pre-primary, higher, university or vocational education?

- What role do other private education service providers play in the current education sector? (For example, companies involved in student testing, curriculum development, or school transportation)

ANNEX 4. TWO IFC PARTNERSHIPS TO SUPPORT THE FINANCING OF PRIVATE EDUCATION[6]

The IFC has recently supported two banks in sub-Saharan Africa through its risk-sharing facility to lend to the private education sector. These projects in Ghana (2005) and in Kenya (2006) will support lending to the private education sector, including at the primary and secondary levels. The project in Ghana served as a pilot and basis for structuring the initiative in Kenya. The IFC expects to scale these efforts nationally and replicate in other African countries.

Both initiatives are based on the premise that education sector loans are generally short-term and not appropriate to building facilities and acquiring equipment. The short tenor of the loans available in these countries also puts a strain on the cash flows of schools and limits their ability to operate effectively.

In **Ghana**, the IFC has signed a structured risk sharing agreement with The Trust Bank Limited (TTB) to support its lending to private schools. The project is the first such initiative in Ghana's education sector. A strong demand for private education in Ghana has resulted in tremendous growth in the number of private schools. IFC's support through this structured risk sharing facility with TTB will support efforts by the private sector to invest in and ensure delivery of high-quality education.

IFC's risk sharing facility is aimed at encouraging TTB to provide longer-term loans to schools. TTB's risk would also be reduced by the technical assistance provided directly to individual schools before and after receiving loans. IFC is providing TTB with a partial guarantee of up to 9.5 billion Ghanaian cedis (about $1.1 million equivalent) on loans extended to eligible private schools to finance construction, purchase of educational materials, and other capital expenditures.

In **Kenya**, the IFC has signed a partnership with Kenya's K-Rep Bank to support its lending to private primary and secondary schools.

As in Ghana, strong demand for private education in Kenya has led to tremendous growth in the number of private schools. However, loans available to the sector are not appropriate to meet longer term financing needs. IFC is providing K-Rep Bank with a partial guarantee of up to 120 million Kenya shillings (about $1.7 million equivalent) on loans extended to eligible private schools to finance construction, purchase of educational materials, and other capital expenditures.

In parallel with the risk-sharing facility in both countries, comprehensive technical assistance will be provided to eligible schools to strengthen their financial, management, and educational capacities. In addition, technical assistance will be provided to the

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[6] This information is drawn from IFC press-releases that can be downloaded at: http://www.ifc.org/ifcext/che.nsf/Content/PressReleases

financial institutions to build their capacity to conduct due diligence of educational institutions and monitor their portfolio.

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