Making Poverty Reduction Work:

OECD´S ROLE IN DEVELOPMENT PARTNERSHIP

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ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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Publié en français sous le titre :

Faire reculer la pauvreté

LE RÔLE DE L'OCDE DANS LE PARTENARIAT POUR LE DÉVELOPPEMENT

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Preface

No country should be excluded from reaping the economic advantages offered by our increasingly integrated global economy. The second half of the 20th century was, in economic terms, the most successful in human history. In this period, global incomes rose at an unprecedented speed. Yet, too many economies have not shared in the growing prosperity. The Millennium Declaration and the internationally agreed development goals – adopted originally in 1996 by Development Ministers and Heads of Aid Agencies in the OECD's Development Assistance Committee – together with the global partnership enshrined in the Monterrey Consensus, affirm all countries' mutual agreement and obligation to make globalisation work for the common good.

The UN Summit of 2005 provides a reality check halfway between the baseline year of 1990 and the 2015 deadline for achieving the Millennium Development Goals. Drawing from information provided by the UN system, the OECD, WTO and the Inter-Parliamentary Union, our global monitoring system informs us that the results of implementation to date are mixed. Overall, we observe reduced incidence of malnutrition among children, some improvement in access to maternal healthcare, and increased primary school enrolment (especially for girls). These represent notable achievements. However, the current rate of progress is too slow to achieve most of the goals set out in 1996 by the target year of 2015, and regional disparities are striking. The regions most in need of development and poverty reduction are lagging, namely most of Africa and large parts of South Asia. It is of primary concern that half the deaths of children under five are occurring in sub-Saharan Africa and that the numbers of poor and hungry people are rising in this region.

The mixed record of progress halfway to the 2015 target calls for decisive action by all countries and organisations. We need to intensify our efforts to achieve the millennium goals. My message to the Secretary-General of the United Nations, and through him to all UN members, sets out a framework of the responsibilities and role of the OECD and its membership in contributing to the global development partnership needed to achieve the goals. This framework for action to make poverty reduction work is our contribution to the Summit preparations and reflections.

As a grouping of the wealthiest nations, we need to redouble our efforts to secure the fundamentals for growth in our own countries to enable developing countries to prosper, building a peaceful and secure environment for long-term growth. Under politically stable conditions, each developing country can then adopt a reliable macroeconomic framework for growth in which poor people participate. Most OECD members have pledged to increase the volume of their aid up to 2015, as well as to improve the results that this aid achieves through pursuing the commitments expressed in the *Paris Declaration on Aid Effectiveness* signed by nearly 100 countries in March 2005. We also need to improve the coherence and synergies between development and other government policies, especially by enabling developing countries to access OECD markets and attract business investment. We also need to help mobilise a full range of financing sources – domestic and international – to help attain the MDGs everywhere.

The framework for action on a wide range of policy fronts presented in this booklet fits with the OECD's mandate as an intergovernmental institution working to improve economic policy making in all areas of government. But even if we succeed in improving our policies and in scaling up the resources available to achieve them, none of our efforts can bear fruit without strengthened institutional and human capacity in our developing country partners. Here is where OECD's special brand of development partnership, with its networks of policy practitioners, non-negotiating discussion fora, practical tools and "soft law" instruments, can be most effective as we intensify our efforts to achieve the MDGs in all countries.

Donald J. Johnston
Secretary-General

EXECUTIVE SUMMARY

The Millennium Declaration and the internationally agreed development goals, including those contained in the Declaration, derive their force from firm commitments by Heads of State. They were reaffirmed in the spirit of shared responsibility and global partnership enshrined in the Monterrey Consensus. The year 2005 focuses on mutual accountability for delivering on these international development commitments, commonly referred to as the Millennium Development Goals (MDGs), culminating in the UN summit in September.

Contributing to global development is a key objective of the OECD as an intergovernmental agency and through its collective membership. *What* does the OECD bring to the international effort to achieve the international goals?

- a full range of policy experience and its special brand of capacity building;
- over 90% of the world's official development assistance (ODA);
- 80% of the world's foreign direct investment (FDI) flows, of which over a third goes to developing countries;
- analysis and ways to join-up government policies to support development;
- policy dialogue with partners in a non-negotiating context;
- information to both shape and monitor public opinion.

How does the OECD contribute to the global development partnership?

I. By ensuring the fundamental conditions for economic growth. Fundamental conditions for economic growth begin with a peaceful and secure environment. Efforts to reduce poverty are most effective in countries with sound institutions and policies, which is why OECD members direct their assistance efforts increasingly towards the better performing developing countries. Yet one third of the world's poorest people – those surviving on less than one dollar a day – live in "fragile states", characterised by weak governance and often prone to conflict. The OECD recommends that development and other agencies stay engaged, even in countries where institutions and policies are weakest and partnership is difficult, to help build capable states and prevent or resolve conflicts. It is working to ensure that awareness of conflict-related issues and appropriate responses get integrated into policy areas such as development co-operation, foreign affairs, defence and trade. The OECD's policy and good practices in security systems and governance, as well as its package of integrity instruments, are useful tools for working in difficult environments.

To ensure high and sustainable rates of growth, a stable macroeconomic environment is necessary. For developing countries, robust and stable output growth in OECD member countries has considerable benefits, offering *inter alia* more stable markets for exports from developing countries. Sound medium-term public finances help to reduce pressures on global interest rates, providing more favourable financing conditions and low and stable rates of inflation, thus reducing uncertainty about returns from long-term investment and loans. These benefits will increase as national economies become ever more integrated with each other through globalisation.

OECD member country experience also offers useful lessons for the design of macroeconomic policy frameworks in partner countries, especially in ensuring attention to investment in both physical and human capital, the main determinants of economic growth everywhere. Stable, sustainable economic growth and all its determinants are central to the DAC (Development Assistance Committee) agenda, which emphasises the integration of growth into its poverty reduction objectives. Addressing persistent gender inequalities, together with promoting a dynamic private sector, agriculture and infrastructure, are the key strands of the pro-poor, growth agenda that the DAC Poverty Network (Povnet) is advancing, building on the DAC Guidelines on *Poverty Reduction*.

Analysis by the International Energy Agency – the energy forum for 26 industrialised countries, including most OECD members – demonstrates the strong link between income and access to modern energy services. Reaching the poverty reduction target of the Millennium Development Goals requires a significant reduction – by at least 600 million – in the number of people without access to electricity by 2015. Public-private partnerships (PPPs) that may include host-country governments, donors, multilateral development banks, NGOs and private companies represent an important option for mobilising the significant investment required.

II. By improving effective policy implementation and policy synergies in OECD member countries. The *Paris Declaration on Aid Effectiveness* of 2 March 2005 commits donors and partner countries to "take far-reaching and monitorable actions to reform the ways [they] deliver and manage aid." Developing country partners commit to producing operational development strategies linked to national budgets and making country systems reliable. Donors resolve to base their overall support on partner countries' national development strategies, institutions and procedures. Donors commit themselves to providing reliable indicative commitments of aid over a multi-year framework and to disbursing aid in a timely and predictable fashion according to agreed schedules. Developing country partners and donors will measure progress in aid effectiveness in terms of ownership, alignment, harmonisation, managing for results and mutual accountability against 12 specific indicators, with five preliminary targets to be reviewed and targets to be set against six of the remaining indicators before the UN General Assembly Summit in September 2005.

Tied aid undermines aid effectiveness. Untying aid generally increases its effectiveness by reducing transaction costs for partner countries and improving country ownership and alignment. By conservative estimates, tied aid reduced the value of bilateral aid by USD 5-7 billion in 2002. And it is incompatible with country owned procurement systems and their integrity, a basic component of the *Paris Declaration* package. Efforts to untie more aid continue as an integral part of the actions to improve aid effectiveness, and progress will be monitored.

Ensuring that aid and other policies are mutually supportive lies at the heart of the MDGs. The OECD seeks to improve joined-up policies in member countries through institutional and sectoral approaches. Analytical work reveals how successful coherent OECD member country policies are when they complement effective partner country policies. By engaging policy makers from all relevant parts of government, the OECD can help ensure that each member country pursues policies that support and do not undermine efforts to reach the MDGs. The DAC's peer review mechanism regularly monitors member country policy coherence in relation to development objectives. An innovative mechanism to promote mutual accountability between some African countries and their development partners is functioning through the *Mutual Review* of Development Effectiveness in the context of NEPAD.

The OECD continues to press for strong synergies between aid, trade and investment policies. Tariff reductions in manufactures and agricultural products and liberalisation in services trade will generate significant global welfare gains. Access to OECD country markets can positively influence domestic and foreign investment. Developing countries benefit from trade liberalisation in developed countries, and they also benefit when they cut their own tariffs. Studies have found that countries that do the most by eliminating or reducing distortions and discriminatory practices, register larger welfare gains relative to others. Greater efforts to liberalise trade could significantly enhance trade flows and welfare: these include further rationalising non-tariff policies and reducing transaction costs generated by inefficient import and export procedures. The OECD is promoting trade capacity building and documenting good practice.

Despite positive trends in the last decade, business investment and enterprise development in most countries outside the OECD area need to grow more strongly to meet development needs. The OECD is developing a Framework for Investment composed of a wide spectrum of policies that can serve as a checklist and reference point for creating a favourable investment climate. The OECD *Guidelines for Multinational Enterprises* provide voluntary principles and standards for appropriate business conduct. The *Guidelines* are part of the broader package of OECD integrity instruments designed to help those working in both the business and the public sectors.

III. By helping countries mobilise resources to achieve the MDGs. The Monterrey Consensus recognises that development is a shared responsibility starting with developing countries' own efforts to strengthen their economic and political governance and improve their economic performance. This will be all the more important if existing and new bilateral and multilateral initiatives lead to significant further increases in aid. Such increases, along with other resources, are critical, especially for the poorest countries. Although aid monitored and reported by the DAC reached its highest ever level at USD 78.6 billion in 2004 as a result of increases by most donors, at 0.25% of GNI, it is short of previous averages and far from the UN target. If donors meet their Monterrey and other commitments to increase aid, ODA will reach some USD 115 billion by 2010 – but it will still be well short of estimates of the amounts that may be required to help many more countries to attain the MDGs by 2015 than those currently expected to do so.

To advance the MDGs, donors and partners need to make aid delivery more efficient and use it more effectively. To be truly effective, aid must be much more predictable than in the past. Partner countries' medium-term budget and expenditure planning needs to be transparent and should be integrated into donor-supported Poverty Reduction Strategies. Without multi-year indicative commitments from donors, the credibility of medium-term budget planning is eroded. The OECD continues its research into successful models and best practices for strengthened and transparent public finance and more predictable levels of finance.

With respect to mobilising other resources to achieve the MDGs, OECD research has helped rationalise the debate on alternative forms of development finance. In line with the recognition embodied in the Monterrey Consensus that partner countries need to finance their own development, OECD member country experience can help them improve tax administration, reform tax design, and reduce tax avoidance and evasion.

Partner countries need to mobilise their own domestic resources to achieve the MDGs. Bringing enterprises into the formal economy has important fiscal implications, and countries can further broaden the tax base through such measures as a low, but consistently applied tax rate. OECD member countries' experience can provide useful input to the improvement of tax collection. The OECD Model Tax Treaty provides a framework within which countries can agree bilaterally about how to minimise and resolve cross-border tax issues and ensure taxation in the appropriate country. At the same time migrants and multinational companies can be certain of their tax liabilities and ensured of no double taxation.

The experience with non-tax revenue sources in OECD member countries is growing and can be tapped by partner countries. These sources include user charges and other economic instruments and finance strategies, which can be particularly effective in addressing environmental and sustainable development objectives closely related to meeting several MDGs.

Emigrant workers' remittances constitute a considerable source of hard currency for their home countries. The OECD with other international organisations is identifying ways to help migrants from partner countries transfer remittances more efficiently, and to assist receiving countries to take account of these significant flows in economic development plans. Such resources have played a major role in the development of several OECD member countries, experience that can be shared with partner countries for the channelling of remittances, for example through savings and investment schemes that could help reduce poverty and improve levels of education and healthcare.

Partner countries lose considerable resources through corruption, bribery and conflict of interest in the public and private sectors. Several OECD instruments, including the Convention on Combating Bribery of Foreign Public Officials, and other tools and guidelines, can help to curb illegal and dubious practices. Effective results depend on anti-corruption measures and on policies that address conflict-of-interest in both OECD and partner countries. The OECD is helping donors and partners in developing good practices for anti-corruption assistance.

IV. By strengthening capacity in partner countries. Strengthened capacity is essential for all other efforts to meet with success. Efforts to ensure the fundamentals of economic growth, to improve OECD policies and policy synergies, and to scale-up resources to meet the Millennium Development Goals require adequate capacity, which is seriously lacking in many partner countries. The final chapter of this report highlights a few of the policy domains – notably in statistics, investment, taxation, trade, entrepreneurship, environment, budget management, and science and technology – where the OECD is engaged in fortifying capacity in partner countries.

Through its unique networks of policy practitioners in most domains of government policy making, the OECD contributes its special brand of partnership to the capacity building needs. Partner countries are participating increasingly in a number of flexible and innovative consortia, fora, and other consultative, capacity building processes at the OECD. Examples include the PARIS21 consortium for statistical capacity building, the OECD Bologna Process for SME and entrepreneurship, the International Tax Dialogue, and global and regional fora in major policy domains ranging from agriculture, education and sustainable development policies, to competition, international investment and trade policies. Significantly more capacity is needed in partner countries, and long-term commitment to building it is essential to meeting the Millennium Development Goals.

Policy design, analysis and co-ordination and sharing the lessons of well-tested member country institutional and policy approaches are the OECD's *leitmotif*. Its unique approach to building capacity relies on networks of member country practitioners who make and implement policy in their own capitals everyday. The "how to" takes shape through a variety of "soft law" instruments, policy principles and guidelines, best practice, model provisions and treaties, checklists, tools, training materials and consultative mechanisms. By putting these human resources, knowledge, experience, and supporting tools at the service of partner countries – and by exploring with partners how best they can use and adapt them to their own needs – the OECD is contributing to the international development partnership.

The Millennium Development Goals: the role of the OECD

2005 focuses on mutual accountability for delivering on international development commitments.

The new millennium has focused co-operation between developing and developed countries on clear objectives. The Millennium Declaration and its goals derive their force from firm commitment by Heads of State but this commitment needs constant political reinforcement and concrete actions to deliver results. Governments acted quickly on their millennium promises by adopting the Monterrey Consensus in 2002.[1] It enshrined a global partnership based on mutual responsibility, including stronger partner governance and performance supported by additional aid by 2006 and beyond. Other World Summits and review processes further integrated these universal undertakings. Now, five years since the Millennium Declaration, we have a timely opportunity not only to renew the commitment, but also to confront the hard reality of what has – and has not – been accomplished.

In declaring their support, OECD Ministers recalled in 2002 that, "Contributing to global development is a key objective of the OECD. Its founding Convention calls upon the OECD to promote policies '*designed to contribute to sound economic expansion in member as well as non-member countries in the process of economic development*'." The Organisation provides supporting policy analysis and monitors OECD members' performance to help ensure that policies get adopted and implemented.

This report highlights the OECD's and its members' contributions to achieving the Millennium Development Goals.

This report looks at the OECD's special partnership with developing countries to help reduce poverty. It highlights the OECD's specific roles in the international effort as an intergovernmental agency and through its collective membership. In this context, it sets out (part I) the fundamental conditions for growth in both OECD and partner countries to support achievement of the Millennium Development Goals (MDGs). It examines improvements and synergies being exploited in key policy areas to achieve the goals (part II). It then discusses ways in which OECD countries can help partners mobilise additional financial resources at home and abroad and use them effectively (part III). Finally, part IV reviews the OECD's unique contribution to capacity building in partner countries through networks of member country policy practitioners.

As an inter-governmental agency, the OECD plays six critical roles in the partnership efforts to achieve the internationally agreed development goals.

- **Sharing policy experience and building capacity**. The OECD is a source of developed-country economic policy and institutional experience and best practices. Sharing the lessons of a range of well-tested institutional and policy approaches is an OECD *leitmotif* that increasing numbers of partner countries find useful. Access to analysis, knowledge and experience through OECD's networks of policy practitioners adds value and complements financial resources in the mutual efforts to attain the MDGs.

- **Contributing over 90% of ODA, co-ordinating aid policies, monitoring performance**. The OECD's Development Assistance Committee (DAC) groups the major donor countries that provide over 90 per cent of the world's official development assistance (ODA). Donors work together through the DAC to foster co-ordinated, effective and adequately financed support to help partner countries meet the MDGs. The DAC developed the MDGs' precursor, the "International Development Goals" adopted in 1996. DAC members share best practices and examine each other in peer reviews that monitor and analyse their performance, including scrutiny of field operations.
- **Providing 80% of the world's FDI**. Investors from OECD countries provide 90 per cent of the world's private capital flows. This includes 80 per cent of foreign direct investment (FDI), over a third of which goes to developing and transition countries. The Monterrey Consensus identified FDI and other private international capital flows as vital complements to national and international development efforts. OECD countries' investment and related policies have important ramifications for poverty reduction, and developing countries compete to attract FDI. The OECD investment policy community can address obstacles to these flows and help build capacity to attract more and better FDI, while encouraging local enterprise and investment.
- **Analysing and seeking joined-up government policy support for development**. The OECD provides a framework for its member countries in all economic, social and related policy areas touching on development. While ODA furnishes resources and expertise, members increasingly recognise that other policies can have potentially far more powerful impacts. The OECD's strong analytical capacity and its unique committee structure, which engages policy makers from all relevant parts of government, can encourage member countries to pursue policies that support and do not undermine efforts to help partners reach the MDGs.
- **Engaging partners in policy dialogue.** The OECD offers a forum for policy dialogue between members and non-OECD countries in a non-negotiating context. Partner countries and groups of them can and do participate in such analysis-based dialogues and consultations, as do representatives of civil society. These exchanges of insights and perspectives contribute importantly to the joint effort to attain the MDGs – to take stock of progress, to analyse, correct and improve on current approaches and to seek resolution of thorny issues.

- **Informing and tracking public opinion.** The OECD monitors public support in OECD countries for the MDGs and facilitates the exchange of best practices for communication about them. It facilitates the work of an Informal Network of Heads of Information from DAC member countries' development co-operation agencies, which shares lessons learned and expertise in building public awareness about the goals (See Box 1).

Box 1. **Public awareness of and support for the MDGs in OECD countries**

Greater awareness and support for the MDGs by OECD citizens is key for sustaining the political will of OECD governments to meet their Millennium Summit commitments. Although ministries of foreign affairs, development agencies and non-governmental organisations (NGOs) try to build public constituencies for the goals, OECD research shows that consensus on the strategic importance of achieving the MDGs remains largely confined to a bureaucratic elite and has failed to enter national public debates. According to recent public opinion surveys in OECD countries, only six to ten per cent of citizens on average have even heard of the MDGs, with higher awareness in countries where concerted MDG communications have taken place in the past two years. Survey findings also suggest that citizens are more optimistic about the achievement of some goals than about others. For example, fewer people think that the overall goal of halving global poverty is achievable, while more are optimistic about achieving Education For All and Reductions in Maternal and Child Mortality, even though at a global level the inverse is the case.

Current steps by OECD countries to engage critical public support in the fight against global poverty include:

- creating better and more internationally comparable data on public opinion and international development co-operation, including through closer co-ordination among DAC members' information units;
- research and analysis to improve knowledge on how public engagement influences the development policy process;
- more focus, investment and evaluation of global development education;
- as part of a general move towards more consultative and participatory governance, provision of more transparent information on development co-operation policies.

Note

1. Formally, the Monterrey Consensus on Financing for Development.

I. Ensuring the fundamentals of growth

Five years after the Millennium Summit – and with ten years remaining towards the goals set for 2015 – it is essential to take stock and to adjust course where needed. This includes ensuring that the following fundamental conditions for economic growth to achieve the MDGs are in place in both OECD and partner countries:

- A peaceful and secure environment.
- A reliable macroeconomic framework.
- Sustainable approaches to meeting growing energy needs.

Fostering a peaceful and secure environment

"Fragile states" represent 13% of the developing world but account for one-third of the poorest population.

Security and political stability are fundamental to long-term growth, development and poverty reduction in developing countries. Poverty reduction and the promotion of human rights are mutually reinforcing approaches and of immediate relevance for a peaceful and secure environment. Efforts to reduce poverty and promote human rights are more effective in countries with sound institutions and policies. Fragile states,[1] on the contrary, are characterised by weak governance and are often conflict-prone or conflict-affected. These countries represent 13 per cent of the developing world but account for an estimated one-third of people living on under a dollar a day. They have a major impact on regional and global security and present an enormous challenge for the MDGs.

Conflict has devastating human and economic costs and a profound impact on the political, social and economic development of a country – and often its surrounding region. All too often the outbreak of violent conflict reverses the benefits of development. Much remains to be done to ensure that awareness of conflict-related issues gets integrated into policy areas such as development co-operation, foreign affairs, defence and trade. The international community must work better together to prevent violent conflict, react effectively to the outbreak of violence, and help make these fragile states more capable.

DAC policy and good practices in security systems and governance offer a tool for working in fragile states.

The OECD's recent report, *Security System Reform and Governance: Policy and Good Practice,* concludes that accountable and efficient security systems operating under civilian control in a democratic context can create an enabling environment for development. This comprehensive approach to security system reform reinforces the idea of human security, which prioritises the basic safety and security needs of ordinary people. OECD countries can effectively contribute to security-system reform through joined-up government approaches that respond to the needs of partner countries and their populations. Support for regional and sub-regional efforts will complement support at the country level.

The DAC recommends that development and other agencies remain engaged, even in countries where institutions and policies are weakest and partnership is difficult. The OECD is building consensus on the special requirements for engaging effectively with fragile states in terms of aid allocations; alternate practices for harmonisation and alignment; service delivery; and coherence of aid with diplomacy, trade and other policies.

The UN Security Council has called for assistance from countries adhering to the *OECD Guidelines for Multinational Enterprises* for a specific fragile state, the Democratic Republic of Congo (DRC), because of the illegal exploitation of its resources. The OECD has responded with its broad package of integrity instruments – not only the *Guidelines*, but also its *Convention on Combating Bribery of Foreign Public Officials*, *Corporate Governance Principles*, and *Guidelines for Managing Conflict of Interest in the Public Sector*. These instruments can serve as useful tools for companies considering investments in DRC and other fragile states, where achieving the MDGs and strengthening state capabilities represent particularly pressing challenges. While complementing broader efforts to enhance multinational enterprises' contributions to these difficult investment environments, this work also recognises that the primary responsibility for policy reform lies with the host country itself and that multinational enterprises cannot substitute for governments that are unable or unwilling to assume their responsibilities.

Securing a reliable macroeconomic framework for shared growth

High and sustainable rates of growth are essential for poverty reduction. Studies at the OECD and elsewhere stress the importance of a stability-oriented macroeconomic framework for ensuring sustainable long-run growth in per capita incomes. Economic stability allows consumers, firms and governments to plan more effectively for the long term, improving the quality and quantity of investment in physical and human capital – two key long-run determinants of economic growth in all economies.

Transparent policy decisions reduce uncertainty and improve financial market conditions.

Clear and sound macroeconomic policies of OECD countries provide considerable benefits for developing economies. Sound medium-term public finances help to reduce pressures on global interest rates, providing more favourable financing conditions and low and stable rates of inflation, thus reducing uncertainty about the returns from long-term investments and loans. More generally, robust and stable output growth in OECD economies offers more stable markets for exports from developing countries. Clear medium-term policy objectives also help to enhance policy transparency and lower market uncertainty about future policy actions. Reduced uncertainty should be favourable for global financial market conditions, lowering risk premiums in interest and exchange rates and output and inflation volatility in all economies. OECD analyses and peer reviews are geared to ensuring macroeconomic stability in member countries.

Macroeconomic policy frameworks in developing countries can draw upon experience of OECD countries. Integration of economic growth with locally owned poverty reduction strategies is essential.

The experience of OECD countries also offers useful lessons for the design of macroeconomic policy frameworks in developing countries. Well-designed policy rules can support medium-term goals while leaving sufficient flexibility for macroeconomic policies to react to unexpected short-term economic fluctuations. If allowed to operate, automatic fiscal stabilisers such as transfer payments and reduced tax yields can help to smooth the path of the economy through the business cycle. Equally, a focus on medium-term price stability permits monetary policymakers to respond to deflationary as well as inflationary shocks.

The benefits from adopting clear and transparent macroeconomic frameworks will likely rise as national economies become ever more integrated with each other. Stable frameworks also provide a favourable setting in which microeconomic and regulatory reforms can be introduced to help improve productive potential and in which barriers to international trade and investment can be lowered. Yet, enhanced cross-border production and trade linkages and increasing financial market integration raise the speed and extent to which financial and economic instability in one region or country can quickly spread to others. A macroeconomic framework designed to maintain long-term stability should help policy makers in all economies to minimise the adverse impact of such external events on long-term growth prospects.

Growth episodes in some developing countries have been weak and unsustainable, and the patterns of growth often have not significantly reduced poverty. Efforts to increase growth have focused on the social sectors, given the critical importance of factors such as health and education in long-term growth prospects. Stable economic growth and its other determinants have been somewhat neglected, a perspective now being addressed in the DAC and Povnet agenda to promote sustainable growth and poverty reduction.

Developing country experiences with pro-poor growth vary considerably. In some developing countries growth and distributional objectives have not been well integrated (*e.g.* Bangladesh, where the incomes of the poor rose less than those of the better off). In other countries, growth and poverty reduction have gone hand in hand (*e.g.* Ghana, where the income of the poor grew faster than average income). Studies reveal that programmes and policies need to target poverty reduction, to involve the poor in the process by making markets work for them, and to be integrated with a locally owned poverty reduction strategy. Gender equality is fundamental to achieving shared growth and attaining the MDGs (See Box 2).

A dynamic private sector, agriculture and infrastructure are key strands of the pro-poor growth agenda.

A dynamic private sector, agriculture and infrastructure are key strands of the pro-poor growth agenda. Jobs and self employment constitute the main pathway out of poverty. Most poor people live in rural areas, and agriculture is a major contributor to developing countries' GDP. More and better infrastructure is essential for broad-based growth, increasing international economic linkages and mobilising investment. DAC will produce, in 2006, guidance to donors on how best to promote pro-poor growth.

Box 2. **MDG3, gender equality and empowerment of women: key to growth and achieving MDGs**

Addressing persistent gender inequalities is crucial to growth, reducing poverty, achieving the MDGs, and increasing the effectiveness of aid. The international community is not on track to meet the target to eliminate gender disparity in primary and secondary education preferably by 2005 and at all levels no later than 2015. Although there has been significant progress over the last decade, without additional effort the 2015 target will not be met in many countries.

The education assistance policies of a number of DAC members focus specifically on girls' education, in line with the World Bank's finding that educating girls is the single most effective way of tackling poverty. Educating girls reduces not only poverty but also the rate of childhood diseases and death and the spread of HIV/AIDS. Secondary education also has the greatest payoff for women's empowerment. Yet the degree to which gender gets addressed comprehensively in education projects and programmes remains unclear.

Parity in primary and secondary education is only a starting point. In most developing countries women do not enjoy the same opportunities as men. The OECD's analysis of aid in support of gender equality, 1999-2003, shows that it is concentrated in the social sectors, especially basic education and basic health, including activities in the area of reproductive health. Approximately half of the aid to these sectors targeted gender considerations, with 10% of the assistance having promotion of gender equality as its main purpose. While several DAC members appear to be implementing a gender mainstreaming approach, others address gender inequalities through a relatively small number of activities targeted to women and girls. To complement this analysis of DAC members' financial assistance, a survey will be developed on the structural and staffing arrangements within member agencies to support and advise on the achievement of gender equality objectives.

Further DAC priorities include: strengthening the integration of gender equality dimensions into poverty reduction strategies and other national planning processes; and refining and developing methodologies, such as the DAC gender policy marker, so that agencies can more accurately measure and assess sectoral and programmatic approaches to ensure that they specifically target and benefit women and girls.

Promoting sustainable approaches to meeting growing energy needs

Economic growth and energy consumption are tightly linked. Investment demand in electric power alone in developing countries will amount to over USD 185 billion annually until 2030.

Economic growth and energy consumption are fundamentally linked. Access to energy is an essential requirement for economic development and a key contributor to social development. Energy services enable basic human needs to be met and contribute to social development by improving education, sanitation and public health. In many poor countries, under-investment in public utilities, inefficient management, under-pricing and a generally unattractive climate for private investment can cause energy shortages and hold back economic growth and development. The International Energy Agency (IEA) – the energy forum for 26 industrialised countries including most OECD members – estimates that the investment requirements for electricity generation, transmission and distribution in developing countries will amount to over USD 185 billion per year from now until 2030. Domestic capital, FDI and development aid will all be necessary, especially in the poorest countries. Public-private partnerships (PPPs) that may include host-country governments, donors, multilateral development banks, NGOs and private companies represent an important option for mobilising the needed investment.

The IEA's *World Energy Outlook 2004* (*WEO-2004*) analyses the energy implications of meeting MDG1: Eradicating extreme poverty and hunger. One yardstick for this is halving the proportion of people living on less than USD1 a day by 2015. Modelling work by the IEA demonstrates a strong link between income and access to modern energy services. Based on that link, reaching the poverty-reduction income target of the MDGs requires reducing the number of people without access to electricity in 2015 by a further 600 million from the 1.6 billion in 2002, which calls for additional investment of around USD 16 billion per year or a total of USD 201 billion.

Meeting the target also implies extending the use of modern cooking and heating fuels to over 700 million more people from 2002 to 2015. The use of traditional biomass and waste for energy, usually a characteristic as well as a cause of persistent poverty, is both inefficient and the source of the indoor smoke pollution responsible for the deaths of more than 1.6 million women and children in developing countries every year.

The Clean Development Mechanism (CDM), defined under the Kyoto Protocol to the UN Framework Convention on Climate Change, promotes investments in developing countries that help to reduce global greenhouse gas emissions. Many of these investments will flow toward energy projects that are more sustainable. The OECD and IEA have been active in recent years in helping to define the criteria under which abatement credits for CDM activities will be provided to developed countries. They have provided technical assistance in developing standardised baselines for use in approving CDM projects, thereby contributing to speeding up low-cost energy-improving investments that will ultimately help to alleviate poverty in many developing countries.

Projections of the new Energy Development Index to 2030 indicate that only a few countries will reach the level of energy development of the OECD area three decades ago.

The IEA has introduced an Energy Development Index (EDI), a composite measure of energy use in developing countries. The EDI seeks to capture the quality as well as the quantity of energy services provided and is calculated to mirror the UNDP's Human Development Index (HDI). The EDI and the HDI are strongly correlated, but the correlation is non-linear; the indices appear to decouple at higher levels of wealth and human development. The EDI can be used to assess the need for policies to promote the use of modern fuels and to stimulate investment in energy infrastructure. EDI projections to 2030 indicate that although EDI scores should continue to rise in all developing regions, only a few countries in the Middle East and Latin America will have reached by 2030 the stage of energy development already attained by OECD countries three decades ago.

Note

1. There is no agreed global list of fragile states, but a proxy for state fragility using those countries in the two lowest categories of the World Bank's Country Policy and Institutional Assessments (CPIA) five categories and including a separate group of unranked countries also deemed fragile provides a list of 46 fragile states. Middle-income countries are not included in this list, which contains 870 million people or 14 per cent of the world's population but nearly a third of the world's poor people and 41 per cent of all child deaths.

II. Improving policy implementation and policy synergies in support of the MDGs

The OECD and its members are striving to improve aid policies and to leverage their effectiveness through synergies with other policy areas. A major international effort is underway to focus the whole aid process more sharply on results and to reduce unnecessary donor-generated demands on countries with over-stretched capacities. Efforts to untie more aid continue. OECD countries are devoting greater attention to interactions between policies and their impact on development. Of highest priority is strengthening the aid-trade-investment-migration nexus in support of shared growth and poverty reduction. These issues are taken up under four headings:

- aid effectiveness: harmonisation, untying and complementarity with partner strategies and programmes;
- improved coherence and synergies between OECD member country policies that impact on development;
- enabling partners to benefit from open markets;
- policies that help attract business investment.

Making aid more effective: harmonised, untied, complementary

A focus on aid harmonisation, alignment and managing for results has emerged.

The international development community committed in Rome (February 2003) to align development assistance with partner-country strategies, to harmonise donor policies and procedures and to implement principles of good practice in development co-operation. A year later in Marrakech the Heads of the multilateral development banks and the DAC Chair affirmed their commitment to align co-operation programmes with desired development results, and to track progress and assess outcomes by relying on partner countries' monitoring and evaluation systems.

On *harmonisation:* Donors have made a start in using simplified procedures and practices, joint analytical work, a focus on delivery of development results, delegated co-operation, common procurement and financial management procedures, and common arrangements for programme-based approaches.

On alignment: By October 2004 some 43 countries had prepared poverty reduction strategies, and many other low- and middle-income countries had nationally owned development strategies. Information from DAC and other sources suggests a promising trend toward increased donor alignment behind country strategies and more joint support of these strategies. More donors use programmatic approaches including budget financing to support country strategies and programmes. Interest has surged in sector-wide approaches (SWAps) to align all aid modes around sectoral priorities, and a growing number of SWAps include use of countries' existing frameworks for allocating and accounting for funds.

Several factors hamper further progress. Some partner country policy and investment priorities are still poorly defined. The links between medium-term plans and annual budget decisions are often missing. It is difficult to agree upon indicators that can trigger disbursement of donor funding. More use of strengthened country systems along with arrangements that allow one donor to manage aid on behalf of another (delegated co-operation) and joint financing would increase harmonisation and alignment. Two other areas require attention: the special needs of fragile states, where harmonisation and alignment have proved even more critical than elsewhere; and the integration of global programmes and partnerships with partner country strategies and programmes.

High-impact operational goals agreed in March 2005 need to be monitored and met.

Building on growing momentum for change, on 2 March 2005 Ministers of OECD and partner countries and Heads of multilateral and bilateral development institutions adopted the *Paris Declaration on Aid Effectiveness.* It commits donors and partner countries to "take far-reaching and monitorable actions to reform the ways [they] deliver and manage aid as [they] look ahead to the UN five-year review…" Donors resolve to base their overall support on partner countries' national development strategies, institutions and procedures. Donors commit themselves to providing reliable indicative commitments of aid over a multi-year framework and to disbursing aid in a timely and predictable fashion according to agreed schedules. They will measure progress in aid effectiveness in terms of ownership, alignment, harmonisation, managing for results and mutual accountability against 12 specific indicators, with five preliminary targets to be reviewed and targets to be adopted against six of the remaining indicators before the UN General Assembly Summit in September 2005.

Tied aid undermines aid effectiveness.

The tying status of aid has long been considered a key test of donors' commitment to coherent policies and effective aid delivery. In the context of improving aid effectiveness, partners challenge a system in which a significant part of ODA goes back to donor countries and recommend that aid should become untied. Tying raises the cost of many goods, services and projects by 15 to 30 per cent on average. This implies that tied aid reduced the value of total bilateral aid by USD5 billion to USD 7 billion in 2002, a conservative estimate that ignores the indirect costs. Tied aid often results in higher transaction costs for recipients and is a serious barrier to harmonising donor procedures. It is incompatible with country owned procurement systems and their integrity, a basic component of the *Paris Declaration* process.

A DAC Recommendation to untie ODA to the Least Developed Countries entered into force on 1 January 2002. In 2003 total bilateral ODA in the categories covered by the recommendation more than doubled and amounted to USD 9.4 billion. Of that amount members reported 91% as untied. Many donors have further increased the share of untied aid in their bilateral programmes. A few have untied all or large parts of their programmes. Based on incomplete coverage, about half of total bilateral aid is reported as untied. The Recommendation's contribution to aid effectiveness remains limited, however, by its present coverage (only covering the LDCs and excluding food aid and technical co-operation, for example). The Recommendation invites members to study the possibilities of extending untied aid to the areas beyond its coverage. The need for and the value of increasing the Recommendation's impact on broader aid effectiveness objectives are receiving growing acknowledgement: developing countries ask for more untied aid as part of the implementation of the aid-effectiveness agenda. DAC members are actively pursuing implementation of the Recommendation. They are also exchanging preliminary views on possibilities for extending the benefits of untying to areas beyond the current coverage.

Improving coherence and synergies between development and other policies

Policy coherence for development means ensuring that the objectives and results of an OECD member government's development policies are not undermined by other policies of the same government that impact on developing countries. Policy coherence increasingly features as a key item on the international agenda. The experience of OECD countries suggests that governments and institutions can seek greater policy coherence at the national, regional and international levels, including the consistency of policies adopted by donor and recipient countries to achieve shared development objectives.

OECD focuses mainly on intra-country, joined-up coherence in member countries' policies.

To complement the traditional focus on internal consistency of development policy, OECD countries began in the early 1990s to stress the other dimensions of policy coherence for development, particularly intra-country coherence. The DAC strategy *Shaping the 21st Century*, adopted in 1996, brought this to the fore by emphasising the importance of ensuring that the entire range of relevant policies is consistent with and does not undermine development objectives. The 2001 DAC *Guidelines on Poverty Reduction* introduced overall coherence between the different policies of OECD governments as a key factor influencing the effectiveness of development co-operation policies on poverty reduction. DAC peer reviews currently incorporate a dedicated chapter on policy coherence issues based on the *Guidelines*, which include a checklist of priority policy areas for policy coherence.

Many OECD governments have promoted joined-up government approaches to avoid the wasted resources, missed objectives and lost credibility associated with inconsistent policies in different fields. OECD experience suggests that the success of such approaches depends on the acceptance by development people that coherence requires a "two-way street", *i.e.* development policy makers must also take on board the policies, lessons and experience of other policy communities.

An OECD project, begun in 2002, has been examining ways of mainstreaming climate change policy objectives into the development assistance efforts of OECD donors, as well as into the national planning activities of developing countries. National level case studies in six developing countries (Bangladesh, Egypt, Fiji, Nepal, Tanzania and Uruguay) have been completed. The main emphasis is on delivering cost-effective adaptation to climate change in developing countries, using sectoral and aid policies as vectors for doing so. Policy guidance to aid agencies is currently in preparation; the work is also examining ways of mainstreaming climate policy objectives into specific development instruments, such as the Poverty Reduction Strategy Papers (PRSPs). The work contributed significantly to the World Bank-led Multi-agency Report on Poverty and Climate Change (2003), endorsed by the heads of participating development agencies, including the OECD.

Coherence can be improved through both institutional and sectoral approaches.

Challenges to achieve policy coherence for development call for a combination of institutional and sectoral policy actions. Given the numerous forms of assistance to partner countries, the diverse government ministries responsible for various aspects of development assistance and for other policy areas that impact on developing countries, the sheer number of actors at the supra-national level and the multiplicity of decision-making forums, the need for co-ordination and coherence in policy making is easily recognised but still difficult to implement.

Based on good practice, the OECD has developed an analytical framework for institutional approaches to policy coherence for development that helps assess the progress of DAC members, as well as recommendations for improvement. Some OECD member countries have already embraced strategic actions for institutional change by adopting this analytical framework for assessing political will and institutional capacity; by drawing lessons from recent analytical work and experiences with institutional reform; by tackling issues in specific action areas according to a firm schedule; and by monitoring results on a regular basis. OECD's systematic application of this framework with subsequent monitoring is recommended as part of the peer reviews.

Sectoral work on coherence helps mainstream development dimensions into OECD's unique committee structure.

Sectoral approaches to policy coherence complement the institutional efforts. OECD frameworks are being developed for better understanding the impacts on partner countries of macroeconomic, agricultural and fisheries policies. Discussion of the conclusions and follow-up continues in relevant OECD committees. In agriculture, an analytical framework has been designed to help OECD countries assess the effects of their policies on partner countries in relation to the MDGs. Action on agricultural trade policy issues can be taken only in the WTO, but dialogue on policy coherence in agriculture with partner countries can help inform the negotiations and suggest development co-operation policy actions that could improve synergies. In the fisheries sector, a meeting planned between development and fisheries experts in 2006 will take up issues such as access agreements, trade, income effects and development co-operation policies.

The MDGs explicitly include providing access to affordable essential drugs and making available the benefits of new technologies, especially information and communication technologies (ICT). Rapid advances in science and technology open new opportunities for fighting poverty. Greater synergies between development policies and science and technology for sustainable development, access to medicines, and eradication of "neglected diseases" should receive greater attention in efforts to reduce poverty.

The OECD will seek to address in a more concerted fashion how member countries might encourage innovation that meets the health needs of developing countries. This will include incentives for the development of new drugs, availability, affordability and access to medicines as well as the need to address more explicitly the threat posed by emerging and neglected diseases. The latter is a serious economic issue. Several developing countries have seen decades of slow, painstaking improvement in standards of living wiped out in just a few years by the ravages of disease.

Coherent policies in OECD countries bear fruit when partners have the capacity to respond.

A regional case study of East Asia's development recently examined a range of OECD country policy vectors – trade, investment, migration, aid and others – and their impacts on Asian economies. The central findings of this study show that policy coherence in OECD countries can bear fruit only when partner economies have the capacity to respond: coherent policies are necessary, but not sufficient.

Interactions among OECD countries' policies in Asia, as well as Africa, Latin America and Eastern Europe, are being further examined through eighteen country case studies. When do such policies complement each other *(e.g.,* when aid increases trade capacity), and when do they work at cross-purposes *(e.g.,* when restrictions on trade increase pressure on clandestine out-migration)? How do OECD member countries' policies interact with those of developing and transition economies to overcome or reinforce development bottlenecks? The comparative analysis of the case studies will provide a rich source of policy-oriented insights in support of economic reform in OECD countries and developing countries alike.

As part of the OECD's evolving partnership with Africa (Box 3), the *Mutual Review of Development Effectiveness* takes up a range of themes of mutual accountability between African and OECD countries, including policy coherence. The issues taken up in the *Mutual Review*, together with the African country cases and other studies, will inform the OECD's next regional case study, which will focus on the impacts of OECD member country policies on Sub-Saharan Africa.

This regional case study work aims to solidify the case and quicken the momentum for development coherence, as well as to provide better understanding of policy impacts, through empirically based analysis of concrete regional and country experience. This could strengthen political resolve and public opinion in favour of development objectives where difficult policy trade-offs arise, such as between trade, aid, migration and investment policies. More positively, it could suggest best practices and more channels through which policy synergies can be created to strengthen developmental impacts in support of the MDGs.

Box 3. **The OECD's evolving partnership with Africa**

The **African Economic Outlook**, an annual report produced by the OECD's Development Centre in collaboration with the African Development Bank, provides concise and authoritative comparative analyses of recent economic, social and political developments in African countries. The first three editions covered 22 countries; the 2005 edition covers 30 of them and thus 87 per cent of the continent's population.

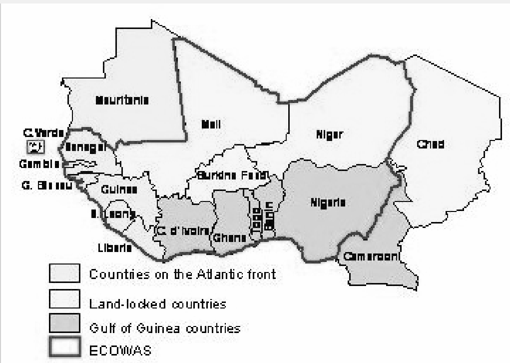
The 2003/2004 volume focused on energy supply, drawing attention to the need to accompany effective national regulation with innovative local micro projects and to the necessity of regional/continental co-operation so that cross-border projects might be successfully developed. The 2005 volume focuses on the financing of small and medium-sized enterprise (SME) development. The Outlook is acknowledged as a key tool for monitoring and advancing the implementation of the New Partnership for Africa's Development (NEPAD) and the pursuit of the MDGs.

In November 2002, NEPAD leaders requested that the Economic Commission for Africa (ECA) and the OECD develop an arrangement to promote mutual accountability among African countries and their development partners. In early 2004, African and OECD countries endorsed the establishment of the biennial ECA/OECD-DAC "**Mutual Review of Development Effectiveness**" in the context of NEPAD, a special consultation mechanism between African policy makers and their OECD counterparts.

The *Mutual Review Report* will focus on empirical progress, good practice and lessons of experience through shared analysis and learning. It will monitor performance and identify good practice among African countries in progress towards the MDGs, political and economic governance and capacity building and among OECD countries in ODA supply, aid quality including capacity building, and policy coherence. The 2005 inaugural Report highlights key trends and issues and sets out recommendations for future action by African and OECD countries.

"Education for All", as developed in Dakar 2000 and re-emphasised in the MDGs, stresses the importance of education to address poverty reduction globally and the need for structural and functional improvements in national education systems in developing countries. The OECD co-operates in the framework of NEPAD with the Association for the Development of Education in Africa (ADEA) on a series of **Peer Reviews of Education Policy**. The recommendations will help these countries, other international organisations and member countries better to target existing resources and donor assistance. The first countries to have reviews will be Gabon, Mauritius and Nigeria.

Launched with NEPAD at the OECD Global Forum on International Investment in Johannesburg in 2003 under the auspices of the OECD Investment Committee, **the OECD-Africa Investment Initiative** uses peer dialogue and experience with policy best practices to assist African countries' reform efforts to create a sound investment climate. It considers ways of raising transparency and relaxing regulatory obstacles to investment, of enhancing the role of ODA in support of investment, and of increasing regional capabilities with public-private partnership in utilities.



With its population growing from 85 million in 1960 to 290 million in 2005, **West Africa** has undergone over the last 45 years an unprecedented demographic shock and rapid urbanisation never before seen. In 2020, the region's population will reach 430 million, of which more than half will be under 20 years old and most will live in urban areas. These dynamics underline the scale of the challenges, particularly those linked to attaining the MDGs.

OECD's **Sahel and West Africa Club** is an "idea" laboratory that encourages decision making by Africans themselves and strengthens partnerships in support of development. The Club attaches high priority to identifying and promoting dynamics and drivers of change. At the Club's creation in 1976, few would have believed that democracy would undergo such progress in the region; that market economies would replace centrally managed economies; and that the rural sector would be significantly liberalised and agricultural production, especially cereals, would follow the rapid population increase. As a facilitator of open and constructive exchanges between West Africa and OECD member countries, the Club supports initiatives by West Africans to promote regional integration and its medium- and long-term development. As recommended by the African Union, ECOWAS and NEPAD, the promotion of a regional market will bring not only accelerated growth to benefit the entire population but also peace.

The **Initiative for Central Africa** (INICA) is hosted by OECD as part of NEPAD co-operation to test the feasibility of long-term networking arrangements using a cross-border approach. It links local actors to regional and international levels. Such networking can bring field-level perspectives to regional co-operation efforts.

Enabling partners to benefit from open markets

Access to markets can influence investment decisions positively.

Tariff liberalisation: Studies at the OECD and elsewhere underscore the importance of market access for developing countries to both developed-and developing country markets. One of numerous important benefits of market access and services market liberalization is the anticipated positive impact on domestic and foreign investment. Under a number of scenarios for multilateral tariff cuts, the findings concur that half or more of the potential welfare gains for developing countries are associated with trade liberalisation in developed countries, while also pointing to significant potential benefits from increased South-South trade in response to developing countries' own engagement in the liberalisation process.

Tariff reductions in both manufactured and agricultural products can enhance welfare in developing countries.

The gains: The OECD has estimated global annual welfare gains from tariff liberalisation, assuming simultaneous progress in trade facilitation, to range between USD 117 billion under a proportional tariff reduction of 50 per cent to USD 174 billion under a scenario with full tariff removal. Under all of the modelled scenarios, substantial gains accrue to developing countries from tariff reductions in both manufactured and agricultural products. Given the much higher reliance in many developing countries on agriculture as a source of employment and economic activity overall, the potential gains to them from further opening of global agricultural markets are of particular importance.

Developing countries benefit from liberalisation in developed countries, and they also benefit when they cut their own tariffs. The sectoral sources of these gains reflect significant contributions from both industry and agriculture. Moreover, roughly two-thirds of them come from removal of tariff-related distortions in just three sectors, namely motor vehicles and parts, textiles and clothing and processed agricultural products.

Partner countries suffer the effects of non-tariff measures in both South-North and South-South trade.

Liberalising non-tariff measures: In South-North trade, studies suggest that customs and administrative procedures and behind-the-border technical and sanitary and phytosanitary (SPS) measures – although these may serve legitimate purposes – particularly concern developing countries. In South-South trade, cumbersome or otherwise difficult customs and administrative procedures, including problems with import licensing, also rank very high among the market-access concerns reported by developing countries. There are also many complaints about fees and charges on imports and other para-tariff measures, which appear to have become more frequent as countries have lowered their import tariffs.

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Anecdotal examples and case studies show that developing countries often have special difficulties and higher costs in showing compliance with technical regulations. Product standards, and the measures used to ensure compliance, may provide benefits to consumers and manufacturers and can facilitate trade. Nonetheless, empirical studies have found that technical regulations in OECD countries can adversely affect firms' propensities to export in developing countries. Lengthy inspection and testing procedures especially have been shown to reduce developing-country export shares by four per cent and nine per cent respectively. Other survey evidence not focused specifically on developing countries indicates that additional costs of complying with foreign standards can be as high as ten per cent. By implication, efforts to rationalise these non-tariff policies further and to help exporting countries build up the infrastructure and capacity needed to show compliance with foreign regulatory requirements could significantly enhance developing country exports and welfare.

Trade facilitation can further increase welfare gains.

Trade facilitation: Further welfare gains can come from the reduction of transaction costs generated by inefficient import and export procedures (trade facilitation). Studies suggest that the costs involved in import and export procedures may range from one to fifteen per cent of the traded goods' value, depending on the countries, types of goods and types of traders. The same studies note that a mere 1.5 per cent uniform reduction in these costs could result in global welfare gains of USD 72 billion.

The OECD has estimated that 65 per cent of these worldwide income gains would accrue to non-OECD countries, whatever the assumption on the extent of trade facilitation. To illustrate, the welfare gains as a percentage of GDP in Sub-Saharan Africa are more than twelve times the OECD average in relative terms. These benefits would accrue primarily to countries that actively engage in trade facilitation. Under the assumption that only OECD countries undertake trade facilitation efforts, non-OECD countries actually lose, as trade is diverted away from them.

Developing countries are likely to benefit significantly from liberalising trade in services.

Liberalising trade in services: The OECD has recently estimated the welfare effects of services trade liberalisation in a range of countries and regions at different levels of development. As shown in Table 1, with a single exception, the projected gain to each country or region from unilateral services trade reform far exceeds those from unilateral reform in agriculture or manufacturing. The table also indicates that the case for reciprocity in services is less strong than for goods, implying that countries should not feel obliged to wait for progress in multilateral *fora*. In the short to medium term, however, gains may be negatively affected by the adjustment costs of barrier removal and re-regulation. In this context, attention to the nature, pace and sequencing of liberalisation will be key to both managing adjustment and to ensuring that liberalisation is underpinned by sound regulatory frameworks.

Table 1. **Welfare implications of trade reform in goods and services: selected developing countries and the OECD area**

(Equivalent variation in $US million per year)

Gains to Malaysia from	Malaysia liberalises	All other regions liberalise	Malaysia and all other regions liberalise
Services reform	3 528	–704	2 824
Agricultural liberalisation	–106	885	779
Manufacturing liberalisation	–658	762	104
Gains to Thailand from	**Thailand liberalises**	**All other regions liberalise**	**Thailand and All Other Regions Liberalise**
Services reform	2 563	474	3 037
Agricultural liberalisation	–29	2 180	2 152
Manufacturing liberalisation	–596	1 483	887
Gains to Brazil from	**Brazil liberalises**	**All other regions liberalise**	**Brazil and all other regions liberalise**
Services reform	9 535	3 726	13 261
Agricultural liberalisation	178	1 123	1 302
Manufacturing liberalisation	4 718	4 000	8 718
Gains to Chile from	**Chile liberalises**	**All other regions liberalise**	**Chile and all other regions liberalise**
Services reform	630	259	889
Agricultural liberalisation	–46	435	388
Manufacturing liberalisation	–342	393	51
Gains to Morocco from	**Morocco liberalises**	**All other regions liberalise**	**Morocco and all other regions liberalise**
Services reform	251	138	389
Agricultural liberalisation	205	707	913
Manufacturing liberalisation	–23	869	847
Gains to Zambia from	**Zambia liberalises**	**All other regions liberalise**	**Zambia and all other regions liberalise**
Services reform	204	–34	170
Agricultural liberalisation	4	7	10
Manufacturing liberalisation	–21	48	27
Gains to OECD Area from	**OECD area liberalises**	**All other regions liberalise**	**OECD area and all other regions liberalise**
Services reform	352 607	2 624	355 232
Agricultural liberalisation	14 071	21 973	36 043
Manufacturing liberalisation	–4 015	30 767	26 752

Note: Please see the original document for further information on the assumptions and limitations associated with the modelling of this liberalisation scenario.

Source: OECD Document TD/TC/WP(2004)48, *The Economy-Wide Effects of Services Trade Barriers in Selected Developing Countries.*

Adopting policies to attract business investment

Investment has proven to be a powerful catalyst for innovation, sustainable growth and poverty reduction. Despite positive trends in the past decade, business investment and enterprise development in most non-OECD regions need to grow more strongly to meet development needs.

A Policy Framework for Investment is being developed as a flexible checklist and reference point for creating a favourable investment climate.

A *Policy Framework for Investment* is being developed by a Task Force of OECD and partner governments in co-operation with civil society and other international organisations. Drawing on a wide spectrum of policies such as trade, competition, tax and corporate governance, it will function as a checklist for governments engaged in domestic reform, regional co-operation or international policy dialogue aimed at creating an environment that is attractive to domestic and foreign investors and that enhances the benefits of investment to society. The *Framework* could serve as a reference point for investment promotion agencies and donors as they assist recipient countries in improving the investment climate, as well as for businesses, trade unions and NGOs in their dialogue with governments. It recognises that the needs of countries at different levels of development call for a flexible, non-prescriptive approach that provides constructive policy guidance across a range of areas in order to maximise the contribution of investment to development.

Bilateral and multilateral donors spend a sizeable share of their official development assistance on activities that mobilise more and better private investment, both domestic and foreign. These include initiatives at the macroeconomic level (*e.g.* stability, inflation, debt), at the institutional level (*e.g.* business and investment legislation, governance and infrastructure) and at the enterprise level (*e.g.* investment and trade promotion and facilitation). They use a wide range of instruments including grants and concessional loans, equity stakes, guarantees, debt relief and technical co-operation. As the Monterrey Consensus recognised, meeting the internationally agreed development goals requires the mobilisation of all available resources, domestic and international, including aid. ODA can be used to leverage additional investment. To understand what works, what doesn't work and why, the OECD has identified a need for more detailed information on the impact and efficiency of the different ways ODA is used to stimulate private investment and the synergies between FDI and ODA. The OECD is lending its investment expertise to this task.

The OECD Guidelines for Multinational Enterprises provide voluntary principles and standards for appropriate international business conduct.

The Monterrey Consensus states that multinational enterprises have an important role to play in helping to achieve the internationally agreed development goals. The OECD *Guidelines for Multinational Enterprises* are a government-backed, voluntary code of conduct for international business; they aim to strengthen the basis of mutual co-operation between multinational enterprises and the societies in which they operate so as to enhance economic, social and environmental well-being. The *Guidelines* provide voluntary principles and standards for appropriate conduct by multinational enterprises in such areas as labour relations, human rights, disclosure of information, anti-corruption, environment and consumer protection. They apply to the global operations of multinational enterprises based in adhering countries.

The governments adhering to the *Guidelines* represent countries that are home to most multinational enterprises and the source of most global trade and international investment. Adhering countries comprise all 30 OECD members and to date nine non-OECD partner countries (Argentina, Brazil, Chile, Estonia, Israel, Latvia, Lithuania, Romania and Slovenia).

While observance of the *Guidelines* is voluntary for companies, the adhering governments have committed to promote them actively. The most visible signs of this commitment are the National Contact Points (NCPs), which are government offices (sometimes tripartite in structure) charged with promoting observance of the *Guidelines* by multinational enterprises operating in or from the national territory. The NCPs are responsible *inter alia* for the "specific instance" procedure, which allows any interested party to ask an NCP to engage in dialogue with an individual company regarding its observance of the Guidelines in a specific business situation.

Eighty specific instances dealing with a range of concrete problems of business ethics were brought to National Contact Points' attention between 2000 and 2004.

NCPs have significant flexibility in determining how they go about promoting the *Guidelines* and dealing with specific instances. They engage in annual peer reviews of their activities and publish an annual report. According to the 2004 Annual Report on the *Guidelines*, some 80 specific instances have been brought to National Contact Points' attention since the 2000 Review of the *Guidelines* dealing with a range of concrete problems of business ethics. Examples include resettlement of populations in the vicinity of a Zambian copper mine, questions of responsible supply-chain management in the Indian sporting goods sector and the Ghanaian gold sector, and respect for workers' rights to organise in a Guatemalan export processing zone.

The Guidelines are part of the OECD package of integrity instruments that include the Convention on Combating Bribery of Foreign Public Officials.

The *Guidelines* are part of the broader package of OECD integrity instruments that summarises an extensive body of analysis and experience in how to design and implement good public policy and, in some cases, about the business sector's role in the overall governance framework. The OECD Convention on Combating Bribery of Foreign Public Officials, backed by a strong monitoring and peer review of implementation mechanism, targets the offer or supply side of corruption transactions. By taking steps to cut off this side of bribery in international markets, OECD countries take responsibility for their role in curbing world corruption and poverty reduction.

III. Mobilising resources to achieve the MDGs

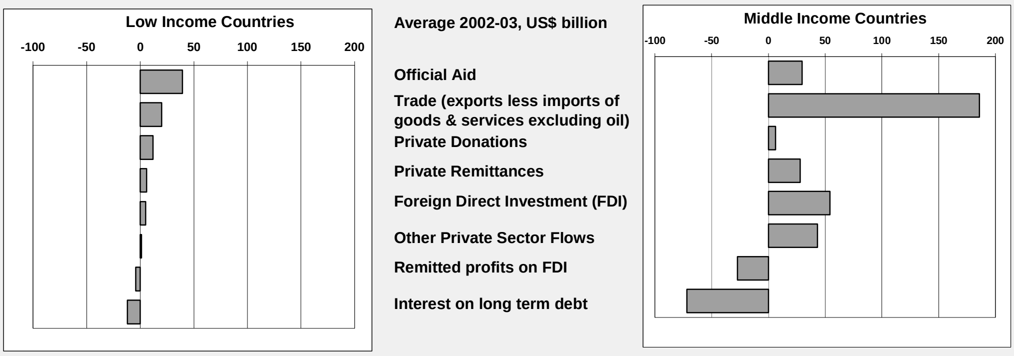
Increases in aid are critical for the poorest countries, but all countries need to develop other financing sources.

Resource mobilisation is fundamental to achieving the MDGs. For many of the poorest countries, aid will continue to be the principle source of finance for some time (Box 4). Significant aid increases have been promised by OECD countries: these amounts need to be reliable and provided for predictable time periods. But OECD members can do more. They can help partner countries reap trade benefits by freeing their markets and strengthening trading capacity. OECD experience can also be put to work to help developing countries mobilise new financial resources and better exploit existing ones, as well as to reduce the costs of corrupt practices and conflicts of interest in the public and private sectors. What are the OECD and its membership doing to:

- increase aid volume and aid predictability;
- help partners mobilise domestic sources of finance through taxes, user charges and economic instruments;
- share special finance strategies for achieving water-related goals;
- help use remittances efficiently and productively;
- analyse innovative sources of financing;
- promote partnerships and results-based management of resources;
- work against conflicts of interest and bribery?

Box 4. **Sources of resources**

The poorest countries rely on aid… … middle income countries benefit more from trade



Increasing aid volume and predictability

Aid volume reached its highest level in 2004.

In 2004, aid reached its highest level ever – at USD 78.6 billion – in both nominal and real terms. Aid levels fell during 1992-97, and the trough continued through 2001. Since then, total aid from DAC members has risen in each of the past seven years, by over a quarter in real terms.

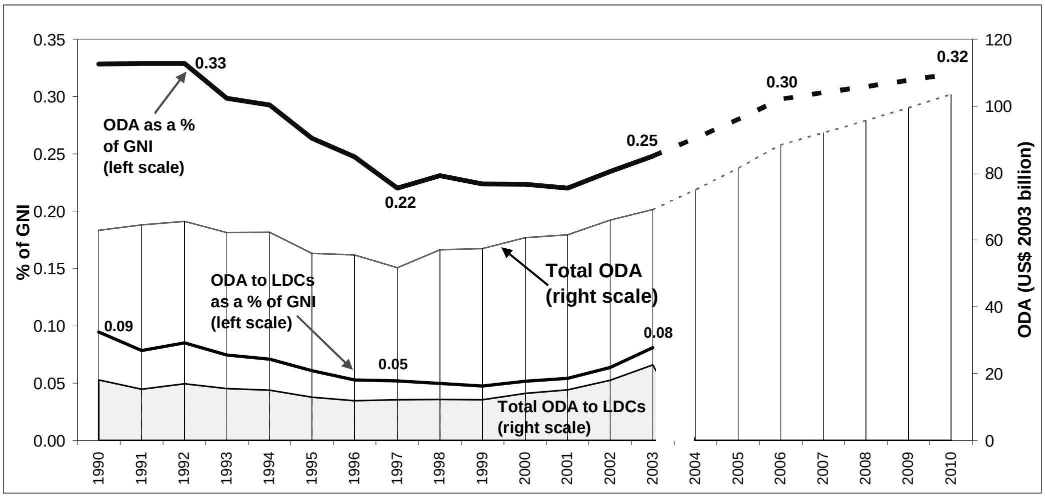
Yet the ODA/GNI ratio at 0.25% remains short of previous averages and the UN ODA target.

Yet ODA growth has not matched donors' economic growth over the past decade, so its recent recovery becomes less impressive when measured as a share of DAC members' combined GNI. The ODA/GNI ratio rose to 0.25 per cent in 2003 and 2004, up from 0.23 per cent in 2002 and 0.22 per cent in 2001, but still well short of the average of 0.33 per cent achieved in 1970-92. While a significant part of the ODA increase over the past four years went to the Least Developed Countries, as Figure 1 shows, most was in the form of debt relief and emergency and reconstruction aid.

One can expect further substantial growth in real ODA in line with the Monterrey commitments. Denmark, Luxembourg, the Netherlands, Norway and Sweden remain the only countries meeting the United Nations ODA target of 0.7 per cent of GNI. So far seven others have committed to reach it before 2014: Belgium, Finland, France, Germany, Ireland, Spain, and the United Kingdom. The European Union has launched proposals for all EU DAC members to reach 0.51 per cent by 2010 as an interim step towards 0.7 per cent by 2015. Canada and Switzerland have also made commitments to reach higher ODA targets, and the United States has already increased its aid by more than the 50 per cent it pledged at Monterrey. If these existing commitments are met, ODA will reach some USD 115 billion (at 2004 prices and exchange rates) by 2010 — still short of estimates of the amounts required to help many more countries attain the MDGs by 2015 than those currently expected to do so.

Aid flows from non-DAC/OECD donors are growing, a development that is welcome and encouraging. A dialogue with these donors is being built around aid flows, statistics and effectiveness. At a joint meeting in February 2005, it was acknowledged that significant scope exists for stronger co-ordination and mutual learning between DAC donors and the growing non-OECD donor community.

Figure 1. **DAC members' ODA: 1990-2003 and simulations to 2006 and 2010**



Note: LDCs represent the 50 countries classified by the UN as Least Developed Countries.

Aid predictability is key to medium-term budget planning, which is at the core of Poverty Reduction Strategies.

Effective ODA flows must be predictable. Aid programming is vital for recipients' fiscal planning and has always played a key role in the World Bank Consultative Groups and UNDP Round Table discussions. Unpredictability deeply compromises the ability of governments to plan future public expenditure. The problem arises mainly in programme-type assistance, particularly if the time frame extends to three or five years. Donors' annual budget cycles may prevent them from giving firm multi-year commitments but they can give indicative projections. The absence of such commitments or at least indications undermines the credibility of recipients' medium-term budget planning, which is intended to provide the centrepiece for donor-supported Poverty Reduction Strategies.

Among African recipients, volatility is lower in more stable countries and higher in those more fragile. A substantial number of recipients experience year-to-year ODA variations averaging only 10 per cent to 20 per cent, but the figure can rise to 50 per cent or more for recipients suffering conflict or unrest. The problem is most acute in aid-dependent countries with low international reserves, where donors are unsure about government commitment and capacity to reform. Some success stories of countries that have managed to increase aid predictability provide lessons that could have application elsewhere. A closer look at streamlining conditionalities may also be warranted.

Mobilising domestic resources: OECD policy experience

OECD experience can help partner countries to improve tax administration, reduce tax avoidance and evasion, and reform tax design.

Taxes: The Monterrey Consensus recognises the need for and responsibility of developing countries to finance their own development. In addition to the mobilisation of domestic savings, proper tax design and administration also have a major role to play, not least in ensuring a growth-friendly environment. Yet many developing countries have difficulty in raising revenue to finance physical and social infrastructure to support market-based economies. They struggle to replace revenues lost through tariff reductions. To some extent, these difficulties arise from the structures of their economies, often with large informal sectors and many people below any acceptable poverty line.

Yet most developing countries still have scope to increase revenues by improving tax design and administration. Bringing enterprises into the formal economy has important fiscal implications. Countries can further broaden the tax base through measures such as a low, but consistently applied, tax rate. They can ensure effective taxation of corporate income, regardless of home country. This may call for measures to check tax evasion and cross-border tax avoidance. The experience of OECD countries can provide useful input to the improvement of tax collection.

The OECD Model Tax Treaty is a major contribution to improving the operation of tax systems worldwide. It provides a framework within which countries can agree bilaterally about how to minimise and resolve cross-border tax issues and ensure taxation in the appropriate country, while giving migrant workers and multinational companies certainty about their tax liabilities and ensuring no double taxation.

Two provisions of the Model Treaty have particular relevance for ensuring effective taxation of FDI and reducing tax avoidance and evasion opportunities: the allocation of profits to subsidiaries of multinational companies through the arm's length principle and the exchange of information between tax authorities. The *Transfer Pricing Guidelines* aim to ensure that rights to tax the profits of multinationals are allocated equitably between countries. Correct application of these principles reduces the tax that companies can avoid by making their profits (but not their real activities) appear in low-tax jurisdictions. The treaty provisions on exchange of information have also been clarified to ensure that countries assist each other in enforcing their tax laws and that taxpayers cannot evade tax simply by hiding income or activities offshore.

OECD experience with non-tax revenue sources is growing.

User charges: No country claims to have found the ideal tax system, and all countries look continually for ways to improve theirs. This, combined with the general unpopularity of taxes, has prompted a search for non-tax revenue sources. One source gaining ground in many countries but rarely a major source of revenue is user charges: payments made by users of government services. They have a number of advantages. They are relatively easy to collect, can be used to motivate the providers of government services and are seen as less onerous than taxes. They are often more inequitable, however, because they take no account of ability to pay and so cannot replace taxation. They also often fall disproportionately on individuals rather than companies and on residents rather than non-residents. Experience with user charges within OECD countries is growing quickly, making this an area where developing countries can draw on OECD expertise.

Using economic instruments for environmental policy: The OECD has also worked extensively on improving environmental effectiveness and economic efficiency through economic instruments for environmental policy. Such instruments include reform of environmentally harmful subsidies, environmental taxes and charges, domestic tradable permits and voluntary approaches, as well as public environmental expenditures. The results of OECD analysis, based on case studies and the recent experience of member countries in implementing sustainable development, have been shared with developing and transition economies by means of regional and country workshops. OECD has also analysed the environmental effectiveness and economic efficiency of other policy instruments, in particular, voluntary approaches.

Giving greater prominence to such instruments in the mix of policies used to address environmental and sustainable development objectives can help cost-effectively to meet MDG 7, and "... reverse the loss of environmental resources". It may help to alleviate poverty directly by addressing environmental problems that impact the poor – such as water contamination and air pollution – and indirectly by generating or freeing resources for investment in infrastructure, such as water supply and sanitation, which is critical for the poor. Such instruments can also free budgetary resources for other kinds of pro-poor investments, like health and education.

Developing finance strategies for achieving water-related goals

The international community has agreed to halve the proportion of people without access to safe water and sanitation by 2015.[1] This presents a major challenge demanding strengthened efforts from all stakeholders and, according to the Camdessus Panel, a doubled financial commitment.[2] Currently, 1.1 billion people do not have access to safe water, and 2.6 billion have no access to basic sanitation. Without substantially increased efforts by developing countries and their partners, it is unlikely that the internationally agreed water targets will be met. Achieving them would provide important support for attaining several other goals including those on poverty, education and gender equality.

A decision-tool model called FEASIBLE can enhance reforms in governance of the water sector.

Substantially increased financial flows to the water sector are necessary but not sufficient for reaching the water targets. Fundamental reforms in the governance of the water sector must ensure that existing and increased resources get used efficiently and effectively. OECD and the Danish government have developed a decision-support tool to support developing and transition countries in this task.[3] The FEASIBLE model (Box 5) focuses on the realism and affordability of water-related financing. It also provides a basis for addressing the social issues often associated with raising water tariffs to consumers connected to water networks and the policy and institutional reforms needed to use financial resources efficiently. The more a finance strategy is grounded in a process involving key stakeholders, the stronger will be the link between policy development and implementation.

Box 5. **Lessons from FEASIBLE**

Experience in applying FEASIBLE so far comes from the urban sector, but the model is being extended to rural applications. Some key lessons emerging from this work are:

- No “magic bullets” for financing water infrastructure exist. Innovation in financial instruments may yield some progress, but a paradigm shift is unlikely. “Smart blending” of sources to enhance synergies, avoid crowding out other resources and maximise leverage on total flows is probably the best path.
- Operation and maintenance (O&M) costs and their coverage by tariffs often do not receive sufficient attention in finance strategies, as a legion of under-used and abandoned facilities testifies.
- Financial sustainability requires that user fees cover O&M costs, but appropriate provision should be made to ensure adequate access to water services for poor and vulnerable groups. Improving billing and collection systems can often generate important revenues without increasing tariffs.
- Improving water utilities on a sound financial basis is a key prerequisite for extending the coverage of water networks.
- Grant financing – from either national governments or donors – will remain an essential source of finance, particularly for capital investments.
- The main governance challenges include effective fiscal decentralisation, a clear separation of the roles and responsibilities of local governments and water utilities and selecting a fair, realistic and predictable mechanism for establishing tariffs.
- The private sector will be a potential source of technical and managerial know-how rather than capital for the foreseeable future.
- Concessional loans will provide a small but sometimes important contribution to finance in middle income countries.

OECD analysis shows that donor aid to the water sector has declined, is poorly targeted, and is slow in disbursing.

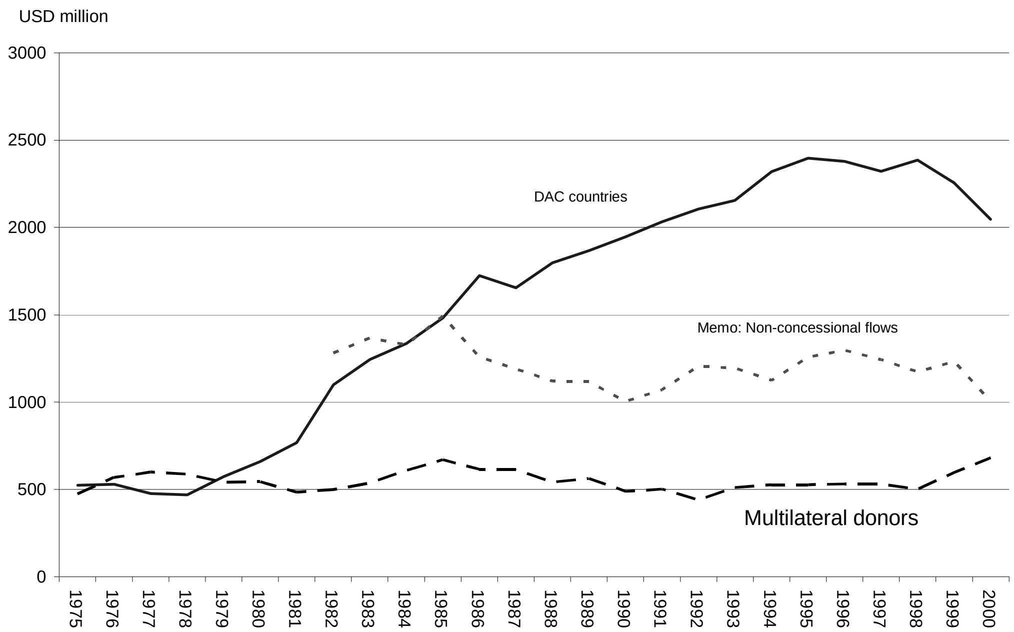
DAC data on aid to the water sector show a recent decline (Figure 2), but the most recent data are for 2002 and thus may not reflect the more recent upturn in overall aid trends. Some other key findings include:

- half of donor commitments were allocated to just ten countries;
- a significant proportion of resources went to countries with already high access to water services, although it was not clear whether they were used to improve access; and
- on average commitments for water projects took eight years to complete disbursement.

These issues will need to be addressed if donors are to make a more decisive contribution to achieving the internationally agreed water targets.

Figure 2. **Trends in aid to water supply and sanitation, 1973-2002**

(5-year moving averages, constant 2002 prices)



Source: DAC Statistics, CRS.

Using remittances productively

Emigrant workers' remittances constitute a considerable source of hard currency for their home countries.

Remittances have grown due, in part, to renewed interest in migration for employment, the international mobility of skilled and highly qualified workers, and the increase in the number of foreign students. Emigrant workers' remittances of savings from wages and other work income (notably pensions and family allowances) are a considerable source of hard currency for countries of emigration. In 2000, estimated remittances to developing countries originating in DAC member countries amounted to USD 34 billion, just over half of DAC ODA. According to the World Bank, worldwide workers' remittance flows into developing countries were estimated to be USD 126 billion in 2004.

The OECD has long experience in migration issues. It has studied the role that remittances have played in the development of sending countries such as Italy, Ireland, Greece, Spain and more recently Portugal, Turkey and Mexico. It can share this experience and draw the lessons of best practice for optimal use of emigrants' money transfers through savings and investment. In co-operation with other organisations such as the World Bank and the IMF, the OECD could contribute in other ways. They include, for example, improved estimates of the magnitude of remittances and the design of policies to reduce informal remittance channels and increase migrants' confidence in the financial intermediaries that effectuate the transfers. It is also important to explore ways to increase the use of new technologies to reduce transfer costs, help modernise the formal transfer system, and offer better banking services to migrants.

The OECD is working on the role that remittances play in the economic and social improvement of receiving countries, especially their impact on poverty reduction and improving levels of education and healthcare. Greater coherence is needed between migration policies and development policies. New forms of co-operation between sending and receiving countries are necessary to optimise transfers of funds by emigrants and consolidate development and job creation in countries of origin. Attention should also be focused on the implications of OECD country policies that actively recruit doctors, nurses, scientists and other skilled professionals to migrate to the developed world without any compensation for the investment in those skills made by the low income countries.

Developing innovative sources of financing

Recent pledges by donor countries in Monterrey and elsewhere have improved prospects for higher aid flows but still leave the annual target to achieve the MDGs underfinanced. The simplest solution is to raise aid further, but government budgets are tightening, and new sources of development finance need to be explored for governments to have certainty of keeping their pledge to the world's poor. OECD research has helped to rationalise the debate on alternative forms of development finance.

The OECD has classified alternative forms of development finance to structure and inform the debate and clarify policy choices.

The most popular new forms for financing the MDGs are now inventoried and classified. The classification criteria derive from public-finance principles, *i.e.* according to funding sources (global taxes, financial engineering and the private-sector) and criteria for choice (political feasibility, revenue potential, additionality to traditional ODA and speed of availability). This exercise has structured and informed the debate and clarified the policy choices, analysing the advantages and risks associated with various approaches.

Partnerships and results-based management

The consensus model of development co-operation has improved development partnerships, but has weaknesses.

The present consensus model of development co-operation unites donors and partner countries around the shared goals of poverty reduction and the fulfilment of the MDGs by 2015. Implementation is complicated by donor diversity and fragmentation, making stronger partner leadership of development co-operation a challenge for many countries. Poverty Reduction Strategy Papers are being reviewed by the World Bank, International Monetary Fund and the UN Economic Commission for Africa's PRSP Learning Group, following an evaluation by independent evaluators, to improve their usefulness as a basis for donor alignment. The UN Millennium Project Report has made strong proposals about integrating the goals into PRSPs and specified costed sector investment strategies.

As a result, a "second generation" PRS model is emerging that integrates the goals and the growth agenda, including the central role of the private sector. This model is based around domestic policy and consultation processes to achieve shared results, rather than being driven by the process of multilateral institutions and other donors. The reform of aid practices endorsed by donors and development partners in the Rome and Paris Declarations is a major influence shaping this "second generation" model. As a contribution to evolution of the consensus model of development co-operation, the OECD is researching successful models of stakeholder involvement, predictable financing, and results-based management.

Preventing bribery and conflicts of interest

The OECD Anti-Bribery Convention provides a framework to guide partner countries' anti-corruption agenda.

Significant resources are lost through dubious and illegal practices by economic agents. By adopting and implementing the Convention on Combating Bribery of Foreign Public Officials, OECD countries have taken responsibility for their role in reducing corruption and poverty in developing countries, but effective results also depend on the capacity of partner countries to combat bribery of their own officials. Drawing on the experience of applying the Convention, the OECD also helps developing countries through anti-corruption initiatives at the regional and country level, addressing all aspects of an effective anti-corruption system.

OECD Guidelines and practical tools can help partner countries develop a comprehensive conflict-of-interest policy.

As conflict of interest in both the public and private sectors has become a major problem worldwide, partner countries are also using more extensively the OECD *Guidelines for Managing Conflict of Interest in the Public Service.* They provide a unique international benchmark for developing and implementing a comprehensive conflict-of-interest policy. The *Guidelines* introduce a deliberately simple definition of conflict of interest and a principle-based approach to support public organisations' review and modernisation of their policies and practices. In addition, a set of practical tools, such as checklists, self tests, model provisions and training materials have been developed and tested to help managers in the daily application of the conflict-of-interest policy.

Notes

1. The target for water was established as part of the MDGs, adopted at the Millennium Summit in New York, 2000. The complementary sanitation target was agreed at the World Summit on Sustainable Development in Johannesburg in 2002.
2. Report of the World Panel on Financing Environmental Infrastructure, March 2003.
3. See OECD (2003), Financing Strategies for Water and Environmental Infrastructure, Paris, OECD.

IV. Harnessing policy networks for capacity building

Improving OECD country policies and scaling up resources to meet the MDGs require sufficient capacity in partner countries for them to bear fruit. The OECD has intensified its capacity building programmes in several key areas, notably in statistics, investment, taxation, trade, entrepreneurship, environment, budget management, and science and technology, as well as in helping make aid more effective. All capacity building efforts require long-term commitment.

Statistical capacity building and PARIS21

National Strategies for the Development of Statistics provide a framework and action plan to strengthen statistical capacity

Timely, reliable statistics that support and monitor development policy and progress towards the MDGs are of increasing international interest. This has led to a formal call for low-income countries to design and implement National Strategies for the Development of Statistics (NSDS) by 2006. Achieving the MDGs, and indeed reaching all development objectives, requires good statistics, which in turn require a healthy national statistical system that produces and analyses reliable data. The NSDS provides a robust framework and action plan for exactly that. Because statistics furnish an essential input to policy formulation, the NSDS is intended to align with wider poverty-focused national development programmes and strategies.

The Partnership in Statistics for Development in the 21st Century (PARIS21) – a Consortium hosted by the OECD and guided by representatives from developing countries, bilateral donors, and multilateral institutions – drives this work. It promotes NSDS development so that countries can have, *inter alia*, nationally owned and produced data for all MDG indicators by the next major MDG review in 2010. PARIS21 has already produced a guide for designing an NSDS and an advocacy document, which makes the case for adopting a strategic approach to developing national statistical capacity. A guide for implementing the NSDS, as well as an NSDS knowledge base compiling general background documentation on statistics, notes to support technical areas of the design process, and sample national strategies, are in development.

Investment capacity building

In support of the Millennium Declaration and the Monterrey Consensus the OECD launched the *Initiative on Investment for Development* in 2003 in Johannesburg. It includes three closely inter-related projects: the development of a *Policy Framework for Investment*; drawing lessons on the use of ODA in support of efforts to mobilise investment for development; and sharing the OECD's experience with investment policy peer reviews as capacity-building mechanisms.

Country investment policy reviews and global and regional fora enhance peer learning and development of best practice.

The OECD has a long history of peer learning and consensual approaches towards the development of best practice. It has become a forum for countries to share their experiences, develop common understandings and elaborate policy guidance and capacity aimed at enhancing the contribution of domestic and foreign investment to development. Multiple initiatives support this function. *Global Fora on International Investment* have been held in Mexico, China, South Africa and India. OECD investment policy reviews of China and Russia have recently been completed. And regional programmes to date include the OECD-SEE (South East Europe) Investment Initiative and the new OECD-MENA (Middle East and North Africa) Initiative on Governance and Investment for Development.

An important complement to these efforts concerns OECD work on legal issues associated with international investment, as for example recent work on most-favoured-nation treatment in international law. A better understanding of such legal issues is a precondition for informed development of international agreements dealing with investment and a favourable investment environment.

Capacity building in taxation

The OECD provides partner countries with assistance over a range of tax issues important to attracting investment and taxing it equitably.

Through its multilateral, regional and country-specific tax programmes, the OECD provides developing countries with assistance over a range of tax issues important to the twin goals of attracting investment and collecting fair tax revenues from domestic and foreign investment. Tax advice and technical support have been provided most recently to countries in South East Europe. Follow-up capacity building continues in the form of workshops on micro-simulation tax modelling, tax incentive policies, and tax expenditure reporting for proper budget management. Work currently underway will provide similar assistance under the MENA-OECD investment programme.

A host country's tax regime may negatively or positively impact investment flows. Poorly designed tax systems (laws, regulations and administration) discourage capital investment. Experience shows that a high host-country tax burden is not just a question of tax rates. Too often, imprecise or non-transparent tax rules and their application add to compliance costs, perceived risk and uncertainty over investment profitability. Systems leaving excessive administrative discretion in the hands of tax officials (*e.g.* to assign tax incentives) have also repeatedly invited corruption, thus undermining the good governance objectives so crucial to attractive investment environments. Through its outreach tax programme, the OECD encourages policy makers to make their tax systems accessible, determine acceptable tax burdens, reduce rather than contribute to project risk and keep compliance and administrative costs in check. Moreover, all countries should target tax incentives with care, because tax revenues must provide the main source of finance for public programmes critical to business, investment and social development.

While treaties, transfer pricing and exchange of information provide a framework for effective taxation of cross-border activities, they can benefit a country only if it develops a treaty network and has the technical expertise to make full use of it. The OECD assists developing countries in their efforts to derive these benefits through its global programme of tax policy events. The tax events provide for sharing experience on tax administration issues, such as the administration of value-added tax and the auditing of taxpayers (particularly multinational companies), to help in efficient and effective revenue collection. They include discussions of tax policy experience and methods of tax policy analysis, so that developing countries can learn from both the successes and failures of tax policy in other countries in designing tax systems that suit their own circumstances.

Exchanges with OECD countries can play a vital capacity-building role in tax administrations and ministries of finance, and help mobilise domestic resources. The International Tax Dialogue is a recent joint initiative of the IMF, the World Bank and the OECD in response to the call in Monterrey for greater international tax co-operation. To be successful, this process must involve real dialogue and not promote a single OECD position. The very different economic conditions in each country require careful analysis of the implications of OECD experience for policymaking, but this is facilitated by the wide variety of economic conditions and tax systems within the OECD itself.

Trade capacity building and monitoring

Trading challenges facing the poor countries cannot be addressed through trade negotiations alone.

At Doha in 2001, trade ministers made clear that trade negotiations alone cannot address all the trading challenges facing the poor countries. To reap the maximum benefits from future trade liberalisation these economies need to address the supply-side constraints they face. This typically involves domestic policy reforms to reduce trade costs at the border, help domestic firms meet the price, quality and technical requirements of global supply chains, and build legal and physical infrastructures conducive to international business development. Trade ministers have renewed their commitment to continued work with national and international agencies to help the poor countries mainstream trade into their national strategies for economic development and poverty reduction.

OECD Guidelines help improve donor trade-related technical assistance and capacity building – programmes that the OECD studies and monitors.

OECD countries have intensified their trade-related technical assistance and capacity building programmes, which the Doha Ministerial Meeting in 2001 called "core elements of the development dimension of the multilateral trading system". The OECD *Guidelines on Strengthening Trade Capacity for Development* is a reference document for donors and their partners. The OECD has also played an important role in monitoring the donor programmes. In November 2002 it created jointly with the WTO the Trade Capacity Building Database,[1] a user-friendly tool to help the development and trade communities share information, improve co-ordination and monitor the implementation of the Doha commitments.

In 2003 bilateral donors and multilateral agencies significantly increased their aid commitments for trade-related technical assistance and capacity building.[2] Commitments to activities aimed at supporting beneficiary countries in trade policy and regulations increased in real terms by 31 per cent to almost USD 1 billion in 2003, while aid committed to trade development rose by 18 per cent to almost USD 1.8 billion.[3] The share of trade-related technical assistance and capacity building in total aid commitments rose from 3.6 per cent in 2002 to 4.2 per cent in 2003.[4]
Bilateral donors and multilateral agencies increased their funding to multilateral trust funds and programmes-such as the Doha Development Agenda Trust Fund, the Integrated Framework and the Joint Integrated Technical Assistance Programme (JITAP)-by 24 per cent between 2002 and 2003. This is consistent with the Doha commitments to increase longer-term funding and donor co-ordination. Donors also focused more of their assistance on Least Developed Countries (LDCs). In 2003, LDCs represented 40 per cent of total commitments for support to trade policy and regulations – in line with their share of total aid – and 27 per cent of commitments for support to trade development.

These public-sector initiatives need enhancement with new partnerships featuring recipient and donor governments, business and civil society. They offer a way to resolve complex issues of policy ownership and implementation so that the benefits of trade-linked investment actually materialise and improve the lot of the poor. Public-private partnerships are integral to capacity building, and OECD countries can contribute much to their successful creation and operation. Such partnerships can be particularly important in helping developing country smallholders participate in supply chains where meeting standards set by importing countries or by retailers is essential and can create added value for the farmer.

Increasing capacity for entrepreneurship, SMEs and local development

Fostering entrepreneurship – including women's entrepreneurship – and developing small and medium-sized enterprises are key drivers of economic growth, job creation, regional and local development and social cohesion. SMEs play a crucial role in transition and developing countries. They typically account for more than 95 per cent of all firms, constitute a major source of employment and generate significant domestic and export earnings. Globalisation, the acceleration of technological change and innovation create opportunities and challenges for SMEs in both developed and developing countries.

Capacity building to promote entrepreneurship is vital for local development strategies to combat poverty. It can work through at least three channels. First, entrepreneurship works as an important catalyst for employment and income creation in distressed urban areas. Second, the non-profit sector, which tends often to contain many relatively small and highly entrepreneurial groups, plays a fundamental role in making OECD member countries more inclusive through "social entrepreneurship". The OECD shares with partner economies what it has learned about best practices and contributes to capacity building in this field. Third, an asset building approach, through small savings and loans from microfinance institutions, is rapidly developing as an effective tool for job creation and social inclusion.

The "OECD Bologna Process" has become the mechanism to share experience and best practices to foster entrepreneurship, SME growth and local development.

With its long standing expertise and peer review methodology, the OECD has become a renowned forum for policy dialogue and co-operation on SMEs, entrepreneurship and local development. Building on this, and for the past five years, the *OECD Bologna Process* for SME and Entrepreneurship Policies, provides guidance to both member and non member governments to help entrepreneurs and SMEs worldwide meet the challenges and reap the benefits of globalisation. Based on multidisciplinary analytical work and policy recommendations, *the OECD Bologna Process* is further deepening and improving the high-level dialogue and co-operation among the different stakeholders (policy makers, business community, international bodies and NGOs) at the global level. In this context, the dialogue with developing economies, at national and local levels, is well advanced.

Enhancing capacity for environmental management

To help meet MDG 7, the OECD shares experience with environmental information and indicators and carries out performance reviews.

Environmental institutions in partner countries face severe challenges to devise and implement policy reforms and to undertake and facilitate prioritised investments. To strengthen capacity for achieving environmental sustainability (MDG 7), the OECD works with partner countries in a number of ways. Co-operative programmes have been established with several UN regional organisations to share OECD experience with environmental information and indicators; the use of economic instruments in environmental policy; and in undertaking environmental performance reviews (EPRs). In 2005, the OECD and UNECLAC reviewed Chile's environmental performance, and plans are underway for an EPR of China. Several non-members are full participants in the mutual acceptance of data programme, which facilitates chemical risk management.

The OECD has developed a range of tools, including guidelines, good practices, handbooks and software applications, to enhance the environmental management capacity of non-member countries, mostly in the fields of environmental expenditure management, water supply and sanitation, environmental permitting and environmental compliance assurance. Demonstration projects in pilot countries have been used to test the tools and adapt them accordingly. The OECD manages three networks of officials from Eastern Europe, Caucasus and Central Asian countries around similar topics to facilitate knowledge transfer and peer learning. Policy dialogues between OECD and partner countries through the *Global Forum on Sustainable Development* also enhance capacity for environmental management.

Strengthening budgeting and public expenditure management systems

Aid effectiveness depends on strengthened partner capacities and systems. Donor alignment with country priorities depends on sound development strategies for poverty reduction that are guided by clear priorities, are linked to budgets and expenditure plans, and are results oriented. The effectiveness and efficiency of assistance depends crucially on the capacity of the budgeting and public expenditure management systems in the recipient countries to effectively allocate, manage and account for all the funds spent and to show development results.

The OECD's capacity building programmes feature senior budget officials from member countries.

The OECD provides assistance to developing countries in this area through its series of regional and country-specific programmes on budgeting. Senior budget officials from OECD countries provide unique insights for fellow practitioners, offering immediate credibility and operational value for partner countries. These programmes take a holistic view of the budget process rather than focusing on specific instruments and recognise the intensely political nature of the budget process. The OECD has also developed guidelines for various aspects of the budget process including the *Best Practice Guidelines for Budget Transparency*, which have become a recognised reference in this field. As part of its work on aid effectiveness, the DAC has issued guidelines on *Strengthening Procurement Capacities in Developing Countries*.

Science and technology for sustainable development

To harness S&T for sustainable development partners need to develop capacities through education, research and recruitment.

A major conclusion of the World Summit on Sustainable Development in Johannesburg was that science and technology (S&T) should play a greater role in contributing to sustainable development. The Task Force on Science, Technology and Innovation of the UN Millennium Project likewise stresses furthering the role of science, technology and innovation in meeting the MDGs. To harness S&T, developing countries need to develop capacities to conduct research in response to local needs and to transfer and adapt necessary scientific and engineering knowledge. Building such capacities encompasses science and engineering education at all levels, creating or strengthening research institutions, building research infrastructures and recruiting and retaining qualified scientists and engineers. Above all, it requires the existence of incentives for the research and development necessary to create needed new technologies.

Effective, efficient technology transfer implies fostering a dynamic private sector that can choose, adapt, develop and market advanced technologies suited to local needs and has the necessary incentives to do so. Markets and appropriate institutions – notably for financing and intellectual property protection – need development. OECD and partner countries could draw lessons about how to build scientific and technological capacities from the countries that have done so and from their experiences with well-designed international co-operation programmes. To this end, an OECD-South Africa workshop in late 2005 will follow-up on the OECD Science and Technology Ministers' 2004 Declaration on international S&T co-operation for sustainable development.

Notes

1. For the database, see http://tcbdb.wto.org and for further information *www.oecd.org/dac/trade.*
2. See “2004 Joint WTO/OECD Report on Trade-Related Technical Assistance and Capacity Building (TRTA/CB)” *www.oecd.org/dataoecd/27/4/11422694.pdf* for further details.
3. “Trade policy and regulations” include support to aid recipients’ effective participation in multilateral trade negotiations; analysis and implementation of trade agreements; mainstreaming of trade strategies and policies in broader development or poverty reduction plans; understanding and complying with technical and sanitary and phytosanitary standards; trade facilitation including simplification of tariff structures and support to customs departments; support to regional trade arrangements and (general) human-resource development in trade. “Trade development” covers business development and activities aimed at improving the business climate, access to trade finance, and trade promotion in the productive sectors (agriculture, forestry, fishing, industry, mining, tourism, services), at the institutional and enterprise level.
4. OECD estimate, calculated on sector-allocable ODA.

For Further Reading

African Economic Outlook 2003/2004 ISBN 92-64-01624-4.

Analysis of aid in support of gender equality, 1999-2003 The publication, which includes all data series used for this study, is available for purchase on OECD's online bookshop. ISBN 92-64-00816-0.

Annual Report on the OECD Guidelines for Multinational Enterprises: 2004 Edition: Encouraging the Contribution of Business to the Environment ISBN 92-64-00706-7.

Conducting business with integrity in weak governance zones *http://www.oecd.org/dataoecd/8/13/34304653.pdf.*

DAC Guidelines & Reference Series: Security System Reform and Governance: Policy and Good Practice – DCD/DAC.

DAC Guidelines: Poverty Reduction (2001).

DAC Guidelines: Strengthening Trade Capacity for Development (2001).

Environmental Finance Financing Strategies for Water and Environmental Infrastructure ISBN 92-64-10276-0.

Financing Education: Investments and Returns: Analysis of the World Education Indicators 2002 Edition ISBN 92-64-19971-3.

Foreign Direct Investment for Development: Maximising Benefits, Minimising Costs, OECD, 2002.

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Abbreviations and Acronyms

ADEA	Association for the Development of Education in Africa
CDM	Clean Development Mechanism
CPIA	Country Policy and Institutional Assessments
DAC	Development Assistance Committee
DRC	Democratic Republic of Congo
ECA	Economic Commission for Africa
ECOWAS	Economic Community of West African States
EDI	Energy Development Index
EPR	Environmental Performance Review
FDI	Foreign direct investment
GDP	Gross Domestic Product
GNI	Gross national income
HDI	Human Development Index
ICT	Information and communication technologies
IEA	International Energy Agency
IMF	International Monetary Fund
JITAP	Joint Integrated Technical Assistance Programme
LDCs	Least Developed Countries
MDGs	Millennium Development Goals
MENA	Middle East and North Africa Initiative (on Governance and Investment for Development)
NCPs	National Contact Points
NEPAD	New Partnership for Africa’s Development
NGOs	Non-governmental organisations
NSDS	National Sustainable Development Strategies
ODA	Official development assistance
O&M	Operation and maintenance
PARIS21	Partnership in Statistics for Development in the 21st Century
PPPs	Public-private partnerships
Povnet	Poverty Network of the DAC
PRSPs	Poverty Reduction Strategy Plans
S&T	Science and Technology
SEE	South East Europe
SME	Small and medium sized enterprises
SPS	Sanitary and phytosanitary
SWAps	Sector wide approaches
TBTs	Technical barriers to trade
UN	United Nations
UNDP	United Nations Development Programme
UNECLAC	United Nations Economic Commission for Latin America
WTO	World Trade Organisation

OECD PUBLICATIONS, 2, rue André-Pascal, 75775 PARIS CEDEX 16
PRINTED IN FRANCE
(00 2005 1T 1 P) – No. 83249 2005

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