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The Export Credit Arrangement, 1978–1998 Achievements and Challenges

The Arrangement on Guidelines for Officially Supported Export Credits celebrates its twentieth anniversary this year. The 'Arrangement', as the Guidelines are usually known, is a unique form of international co-operation: as a 'gentlemen's agreement', it has no formal status in law – and yet it has brought order to the supply of export credits (government subsidies to exporters), thus saving billions of dollars of taxpayers' money. Thanks to the Arrangement, exporters in OECD countries now compete on the basis of quality and price, not according to the degree of support they receive from the state. Progressive improvements in the Arrangement, moreover, have extended its coverage, preventing trade distortion and subsidy in the form of tied aid and unrealistic premium fees.

In this collection of essays, past and present negotiators of the Arrangement's guidelines, Presidents and Chief Executives of export- credit agencies, international institutions, private-sector players, economists and others involved with the Arrangement from its earliest days chart its evolution – its inception and progressive expansion, the difficulties encountered and problems solved. They examine the sources of the flexibility that has made the Arrangement so successful in adapting to the changing, globalising world economy. Some of the contributions offer remarkably candid insights into the closed world of international negotiations. Others document the response of the Arrangement to the growing sophistication of financial and insurance services. All of them shed light on this increasingly important aspect of international trade.

This book will be required reading for anyone interested in the world trading system and the role of export credits in particular, in the relationship between trade and aid, and in international co-operation in general.

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Market Access Issues in the Automobile Sector

At the turn of the 21st Century, the world automobile industry is in a state of ebullition. Millions of potentially new consumers in emerging economies are eager to be part of the 'automobile civilisation'. While automobile and auto parts manufacturers are gearing up faster than ever to reap market opportunities, an overcrowded automobile market is

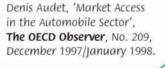
looming as prospective demand growth may not be as strong and rapid as initially anticipated. The automobile industry has a history of trade friction, with tariffs and non-tariff barriers used to shield domestic production from competition and adjustment.

Will the turn of the 21st century be plagued by trade obstacles and bilateral conflicts for the sake of automobiles? What are the globalisation challenges in this industry? How can governments maintain a policy environment that will promote competition, adjustment and open markets?

Senior representatives from major automobile manufacturers, national associations, renowned specialists, labour unions and government officials from OECD countries and emerging countries gathered at OECD headquarters to engage in a dialogue on these crucial questions. These Workshop

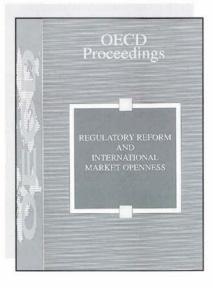
Proceedings include a series of in-depth analytical papers, giving a comprehensive view of the most recent globalisation developments in the automobile industry and their implications.

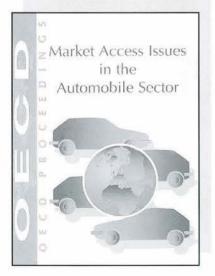
See the article by Steve Cutts and Janet West in this issue of **The OECD Observer**.



Regulatory Reform and International Market Openness

As tariffs and quotas fall and trade potential expands in a globalising economy, social and economic regulations assume more importance because they affect the flow of goods, services, investment and technology. Bringing together the views of experts from different areas, this OECD Symposium is the first attempt to systematically address regulatory reform issues in an international perspective, to reveal the complexity and depth of the problems, and to lend insight into the appropriate direction to take. Very recent developments in the trade-policy field - ongoing negotiations on mutual recognition agreements and burgeoning regional activities - are also described.





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Trade and investment have become major engines of growth in developed and developing countries alike.

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Securing the Benefits

Donald J. Johnston, Secretary-General of the OECD

n the last half-century, world prosperity has risen many times over, with economic growth being sustained at a rapid pace. As long as current trends in technology, investment and trade continue, one can indeed talk of the dawning of a new global age. But to attain the benefits that it will bring, it is vital that the opening of trade and investment continue and that there be no backsliding as protectionist sectional interests ask for exemption from these globally beneficial trends.

Market integration induced by trade and investment has led to deeper forms of economic interdependence among nations, and a growing number of developing and former centrally planned economies have become more closely tied into the global economy. Developing countries rely on OECD countries for more than 60% of their trade. Trade and investment between developing countries are also on the rise, as more than a third of their exports now go to each other.

This integration brought on by trade and investment is the basis of current prosperity and underpins rising living standards. But just as it drives improvements in productivity, such expansion can cause dislocation, impose adjustment on domestic economies and increase the vulnerability of economies to external shocks. Adjusting to the shocks requires that markets function effectively. The OECD has a role to play in this regard in the development of a 'global architecture' that will let markets function better, to the benefit of everyone. Examples include OECD work on combating bribery and corruption, multilateral rules for investment, export credits, taxation and the Jobs Strategy which has stressed the importance of adaptability.

Last year, OECD Ministers asked us to prepare a study of the benefits of trade and investment liberalisation. It is just about to be published.

Support for liberalisation may have weakened somewhat in recent years because of concerns about jobs, wages and the environment. Addressing these concerns requires attention to weaknesses in both communications and policy:

• the communications weakness represents a failure on the part of the proponents of open Developments in technology, communications and trade mean that the world is becoming a global village. The volume of merchandise trade is now 16 times larger than in 1950, and outflows of foreign direct investment have grown even faster than trade in recent years. Trade and investment have been major engines of prosperity in developed and developing countries alike and have been a potent and efficient means of diffusing technology world-wide. In the process everyone has had the chance to reap the benefits of globalisation.

markets to explain clearly what trade and investment can and cannot do and what liberalisation is and is not responsible for

 the policy weakness represents a failure by governments to introduce the measures necessary to help citizens and communities take advantage of the on-going, unprecedented, technology-driven transformation of OECD economies.

Trade and investment play a part, but only a part, in this transformation. The technological change and the displacement of the unskilled which it often entails play a prominent role. Indeed, most of the displacement which has occurred can be related more closely to new technologies than to growing trade and investment.

However, to secure the benefits of trade and investment liberalisation, it is not sufficient to point to incontrovertible evidence that liberalisation creates wealth. It is also necessary to confront the legitimate worries of citizens who are adversely affected.

Integration and Prosperity

The case for open markets rests on a simple, long-standing premise. When individuals and companies engage in specialisation and exchange, the nation will exploit its comparative advantage by using its natural, human, industrial and financial resources to do what it does best. The result is growing prosperity and a wider choice for consumers.

In spite of the clear net benefits generated, and the evidence that open trade produces more winners than losers, the very fact that there are some losers leads to periodic calls to protect industries and workers against cheap imports and against change. Societies pay a high price for heeding such calls. Protection rarely tackles the underlying necessity of adjustment, efficiency gains and competitiveness. It encourages firms to engage in costly and wasteful lobbying and promotes inefficiency and further dependence on protection.

The case for open markets is as compelling for investment as it is for trade. Foreign direct investment creates clear net benefits for host and source countries alike. More open economies enjoy higher rates of private investment, which is a major determinant of economic growth. Although there is little disagreement over the benefits of inward investment, as evidenced by the fierce global competition to attract it, the effects of outflows of direct investment, particularly on employment, are still regarded with some disquiet.

The evidence on outward investment suggests that these fears are not justified. By enabling firms to remain competitive, outward investment supports employment at home. Moreover, 60% of

of Trade and Investment

total foreign direct investment is in services, where a local presence is necessary in order to compete. Investment abroad creates secondary flows – exports of machinery and other capital goods, for example – and increases demand for manufactured intermediary products and the provision of expertise and specialised services. Recent work on a sample of 14 OECD countries found that each dollar of outward foreign direct investment was associated with up to \$2 of additional exports.

Expanded Trade with Developing Countries

Since the 1970s there has been an increase in the share of developing-country trade with OECD countries and, in parallel, mounting concern over unemployment and earnings differentials in the OECD area. The coincidence of these trends has led many to view competition with low-wage, low-labour-standard developing countries as having much to do with the sharp decline in the demand for unskilled labour and the related rise in income inequality observed in some OECD countries.

Studies of this issue agree that increased imports from developing countries do place downward pressure on the wages of industrialised country workers, but most characterise such impacts as modest. Other factors, such as technological change, are also at play. Trade and investment are held responsible for a much bigger impact on wages than the facts warrant. This misapprehension creates a two-fold risk: first, that of assigning the wrong policy instrument to legitimate social and economic policy concerns; second, that of making matters worse by failing to address their root causes.

One has to look to manufacturing to gauge the significance of the potential threat posed by trade with developing countries. The share of manufacturing in OECD employment has seen a decline from 31% in 1960 to 19% in 1996. Yet this decline reflects a natural evolution in the structure of advanced economies. Moreover, the reality is that industrialised countries primarily trade manufactured goods with one another.

Imports of manufactured products from emerging economies have indeed grown steadily during the past three decades, but they still represented a mere 1.6% of OECD countries' combined output in 1994. Furthermore, total trade in manufactures between OECD countries and emerging economies is broadly in balance, a situation that has changed little since the late 1960s.

What about foreign investment? The claim is often heard that outflows of capital from advanced countries have lowered wages, as multinational firms expand or establish overseas affiliates in order to export back to the parent company in the home country. The evidence argues otherwise. Most outflows of investment from OECD countries go to other OECD countries, and those developing countries which receive substantial amounts of inward investment tend to be among the richest economies in the developing world. One reason that low wages do not have the expected allure for foreign investors is because they almost always and everywhere reflect low productivity. Differences in the cost of labour required for a unit of production, where they exist, are much smaller than wage differentials.

A Wide-ranging Adjustment Strategy

Trade, investment and technology interact in ways that raise the wages of high-skilled workers and depress the demand for the low-skilled. The message that open markets lead to gains in aggregate welfare is of little consolation to people whose lives may be adversely affected by change and who may have to uproot their families in search of alternative employment. Nor does the message sit well with displaced workers whose new jobs may pay lower wages.

But postponing adjustment through trade protection or restrictions on capital outflows has been amply shown by theory, history and empirical evidence to be a blind alley. Protection insulates economies from the market signals that point to the importance of early adjustment, inflict damage on the most dynamic firms and most productive workers in society, and provide what

is in most instances a short-term and high-cost palliative to firms, workers and communities for whom delayed adjustment almost invariably translates into worse longer-term hardship.

There is a better way. Labour-market policies that provide adequate income security, by facilitating the re-employment of displaced workers in expanding firms and sectors, can produce important equity and efficiency gains. More fundamentally, governments have to work on the whole range of policies – such as education, training, taxation, pension reform and the portability of health benefits (where that is an issue) – that can help citizens and communities to adjust not only to market-opening but to technology-driven change as well. With the proper mix of policies, governments can maximise the benefits and minimise the costs of liberalisation of trade and investment.

Over the past few years public concern has grown over the possibility that trade and investment may encourage the exploitation of workers in developing countries and lead to unacceptable pressure on the environment. So far as labour standards go, the main policy message emerging from work at the OECD and elsewhere is that developed countries should not regard low core-standards for labour as a substantial competitive factor in their trade with low-wage developing countries. A second message is that, far from being part of the problem, market liberalisation is part of the solution to low labour standards which, above all else, are rooted in poverty. The same arguments can be made about the environmental impact of the liberalisation of trade and investment.

The concerns raised by the environmental community stem from two main sources. The first is the fear that globalisation is stepping up pressures to relax existing environmental laws and regulations and that it is an obstacle to raising those standards. The second is that economic growth is itself a threat to the environment.

There is little evidence to support the first concern. In fact, the pressure is more likely to operate in the opposite direction. Openness to trade and investment translates into increased pressure for more stringent environmental standards, arising from the drive to sell into markets

Securing the Benefits of Trade and Investment

with higher standards and 'greener' consumers. It also reflects the fact that multinational firms increasingly adopt world-wide standards for environmental performance. Moreover, experience suggests that as the developing countries grow richer, their demand for a better environment will grow as they acquire the means to satisfy it.

The concern over economic growth itself as a source of environmental pressure has an element of truth, but misses the key point. Although it is true that liberalisation of trade and investment aids the environment by making the best use of scarce resources, facilitating the transfer of technology and generating increased revenues to pay for cleaning-up the environment, liberalisation can also lead to more pollution and depletion of natural resources. But in most cases, environmental problems can be traced to the inability of the market to put a proper price on the use of environmental resources and to reflect such costs in the prices of goods and services that people and companies consume.

The main policy conclusion to be drawn is that liberal trade and investment policies and

more efficient environmental policies, based on economic instruments that use price signals to guide behaviour, complement each other. Rather than foregoing the benefits of trade and investment liberalisation, progress must be made in putting in place policies that value environmental resources correctly. This task deserves high priority on national and international agendas.

The Multilateral Agreement on Investment

Negotiations are underway at the OECD to develop a Multilateral Agreement on Investment (MAI)

What are the aims of the MAI? Although markets are the main determinant of investment decisions, the investment climate is also a major factor. Investment implies entrepreneurship and risk-taking, so investors require transparency and long-term stability of rules and procedures. They seek open markets and competitive opportunities elsewhere *vis-à-vis* domestic investors

through ensuring the same treatment for foreign as domestic investment and protection for existing ones. In pursuing agreements like the MAI, governments seek to enhance stability and reduce the risks by engaging their sovereignty to establish rules for international commerce. This is what the MAI aims to do, and it is the *raison d'être* of international institutions like the OECD, the IMF, the World Bank and the WTO.

To date, international co-operation has relied mainly on a growing network of bilateral investment treaties, on regional undertakings and on the existing investment instruments of the OECD. The MAI will substitute comprehensive investment rules, incorporate high standards for the liberalisation of investment regimes and offer protection to investors and their investments. It will also provide an enforceable mechanism for settling investment disputes between states and between investors and states. OECD countries' interest in the MAI reflects their dual role as hosts and recipients of foreign direct investment.

Trade and investment agreements do not seek to direct or curtail the objectives of other national policies or regulations. That this is so is apparent from the fact that OECD countries exhibit a striking diversity of economic and social policies and regulatory frameworks. Tax rates, minimum wages, wage-bargaining systems, building standards, retail and distribution systems and social-security systems, to mention only a few examples, vary widely. Thus there is compelling evidence that market liberalisation is compatible with a wide range of economic, social and political preferences. The MAI will not allow foreign investors to stand immune from the host country's regulatory framework. It aims to achieve a situation where foreign investors are not discriminated against, but they are still subject to the same substantive laws and regulations that apply to domestic investors.

There is concern among some citizens that trade and investment liberalisation is somehow drawing societies into a ruinous race to the bottom that will undermine national regulations. The core message of work at the OECD is that these concerns are unfounded. Proponents of market opening have to devote more time and effort to disseminating this message. Efforts must also be made to explain how anxiety over adverse developments in the labour market, particularly for unskilled workers, or over instances of environmental degradation, will be compounded by protectionist responses. Such issues are typically best addressed through other instruments than trade and investment policies.

The liberalisation debate is a debate over ideas and ideals, and it matters enormously that we spread the message that market liberalisation forms part of the answer to the concerns of citizens, rather than being a cause of their misgivings.

Liberal trade and investment policies are not only about more choice but also about fairness in ensuring that the general interest – concern for the welfare of all citizens – prevails over special interests; and in seeing to it that the dividends of liberalisation are distributed more widely.

Trade Policy in 2000

Barbara Fliess and Anthony Kleitz

Perhaps the most commented-on feature of the international economy during the last two decades has been the accelerated globalisation of production and markets. The driving force behind this phenomenon has been intensified international competition, reflecting post-war progress in the opening of national markets and the substantial gains in efficiency that the use of telecommunications and other new technologies have brought. Economic globalisation is reflected in the historically unparalleled surges in international trade and investment, often involving new and dynamic actors on the world stage.

lobalisation is putting considerable pressure on governments to adapt their economic policies so that domestic producers and consumers can profit from the new possibilities for wealth-creation and higher standards of living. Simultaneously, strong public concerns have arisen from the necessity for rapid structural adjustment as well as the risk of international repercussions from the recent financial turmoil in Asia.

For trade policy, these developments mean that governments must re-examine their national measures and regulations as well as the relevance of multilateral trade rules. In particular, they have to consider the increasing international implications of national, behind-the-border regulatory and business conduct. The rapid pace of change means that this process of re-assessment must be continuous. International co-operation in bodies such as the OECD is particularly effective in tackling these issues.

The trade rules that are now institutionalised in the World Trade Organization (WTO) are the result of a half-century of international efforts to liberalise the conditions of trade and to bring them under uniform rules that apply to all trading partners. The process is permanent: as barriers have been liberalised and national economies have evolved, the hierarchy of factors affecting trade has changed. New issues have required changes in the international regime, bringing new nations and interest groups into the policymaking process and modifying the interests of earlier participants.

Trade policy immediately after the Second World War aimed at securing benefits for the world economy from a co-ordinated reduction of high tariffs and other trade barriers and the elimination of discriminatory treatment based on national origin. The GATT, which became the major instrument for achieving this goal, relied on a series of multilateral trade negotiations or 'rounds'. Tariff negotiations were relatively straightforward because tariffs are transparent and their degree of restrictiveness is easy to assess quantitatively. Up until 1973 and the launching of the Tokyo Round, GATT negotiations dealt mainly with tariffs on trade in goods.

As tariffs came down, non-tariff trade barriers (NTBs) gained in relative importance. The Uruguay Round (1986-94) was the most ambitious attempt yet to cut tariffs and strengthen multilateral trade rules, bringing them under a comprehensive framework in the WTO. Some of the strengthened rules covered areas already subject to international disciplines, such as antisubsidy measures and dispute settlement; others were new, such as services, intellectual property and investment. The Uruguay Round also achieved genuine breakthroughs in textiles and agriculture, both of which had effectively been outside the purview of normal GATT disciplines; they have now been brought into the WTO system and are subject to some liberalisation.

The GATT, which initially had only 22 signatories (predominantly OECD countries) has today been transformed, as the WTO, into a full-fledged global system of more than 140 members. There are nonetheless gaps in the membership – China and Russia, for example – and in the commitment of members to all the principles and in the coverage of issues.

As a growing force in international trade, developing countries have been progressively brought into the bargaining process. Since the 1980s, they have accepted heavier responsibilities and now participate more fully in liberalisation. One of the tasks in the coming years will be to ensure participation of the major traders that are currently missing. Moreover, nongovernmental constituencies representing a wide array of consumer, environmental, labour and other interests are joining the business community in becoming increasingly active participants in the making of trade policy, in both national and international fora. Finding novel ways of

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Trade Policy in 2000



Among the items on the built-in agenda that emerged from the Uruguay Round: further liberalise trade in agricultural products and strengthen the rules governing it.

channelling these voices into policy- and rulemaking represents an important challenge for the world trading system.

Priorities for Action

An original feature of the Uruguay Round is that the agreements it produced contain a clear 'built-in agenda' of future work, involving scheduled reviews of the agreements and their implementation as well as negotiations on particular issues. The implementation of the agreements and this built-in agenda are swallowing up a lot of time and resources for the trade-policy officials in national capitals and at the WTO in Geneva. Yet the agenda is not by itself a complete guide to the issues that will have to be addressed by the international trading system: since it was set at the conclusion of the Uruguay Round in 1994, it does not take account of more recent developments, such as the rapid growth of electronic commerce. Moreover, the disciplines and

institutional arrangements under the WTO may not always be applied evenly across the different sectors and issues that are covered.

In this light, the identification of the highest priorities for trade policy will provide a strong orientation and help keep up the momentum for a dynamic and improved system that in turn contributes to a strong world economy. The first, clear priority should be liberalisation and strengthened disciplines for important sectors or policy areas that have so far lagged behind. Two of the main ones are already ear-marked in the built-in agenda for future negotiations: trade in agricultural products and in services. The commitments that emerged from the Uruguay Round for achieving discipline and liberalisation in these areas must now be given more substance through further action by governments, even though this might be painful for some sectors of the economy in the short term. The concessions that have to be made to further liberalisation will achieve their objectives more efficiently if accompanied by strengthened or improved rules that will, for example, apply such basic WTO rules as nondiscrimination, transparency and due process consistently across all sectors and issues.

Some other areas were not included at all in the built-in agenda. Tariffs offer an example: important reductions were achieved during the Uruguay Round, but they leave uneven geographical coverage and some surviving tariff peaks in sectors such as textiles, shoes and consumer electronics. Other areas were included only partially in the agenda, such as government procurement, which has not yet been subject to true multilateral rules and which is mentioned in the agenda only as far as services are concerned. Investment is also only partially included (although negotiations on a Multilateral Agreement on Investment (MAI) are underway in the OECD).¹

A second major priority should be to ensure that domestic regulations do not restrict trade unnecessarily. It has become increasingly apparent in recent vears that domestic regulations have developed in ways that can have a strong effect on competition both inside and across national borders. Yet they have been surprisingly little affected by international disciplines or standards. Regulations with such effects can be found in consumer health (governing, for example, food additives, the expiry dating of perishable food items, pesticide residues), product safety (through, say, fatigue-testing of bicycle frames and use of toxic or flammable materials) and the environment (packaging, noise and exhaust emissions by autos). Regulations can particularly affect competition and trade in services, where the 'invisible' nature of the product has often led governments to act to assure consumers of the quality of the products they purchase licensing of health-care providers is a prime example.

The growing number of trade disputes arising from domestic regulations suggests that this area may be among the hottest political issues in trade negotiations at the turn of the century.

^{1.} William H. Witherell, 'An Agreement on Investment', The OECD Observer, No. 202, October/November 1996; see also pp. 4–6.

Elizabeth Lynch, 'Protecting Consumers in the Cybermarket', The OECD Observer, No. 208, October/ November 1997.

With the decline of barriers to trade and investment in recent years, the possibilities have grown for taking advantage of global markets and organising global production. Under these conditions, domestic regulations and related procedures for assessing conformity (for instance, product certification, laboratory accreditation) can serve as barriers to trade and investment in two main instances: when the regulations are too stringent, or when there are material differences in regulations affecting different markets.

A characteristic frequently encountered in both these cases is a lack of transparency and predictability, which adds to the cost and risk of entering a new market. But the solution is not necessarily a global harmonisation of regulations. Although in many cases that would reduce the costs for producers, it would not be well adapted to the differences in resources available to countries or in national objectives and preferences. Rather, through a range of domestic reforms and international efforts, it may be possible to make regulations more trade- or investment-neutral and more efficient in achieving multiple policy-goals, thus reducing the additional costs of operating in several markets.

There are some good examples of successful efforts at 'market-access-friendly' regulatory reform: the EU Single Market, which aims to eliminate regulatory barriers to trade and investment within Europe; and the WTO Agreement on Basic Telecommunications Services, which was based on a presumption of increased competition through more open markets.

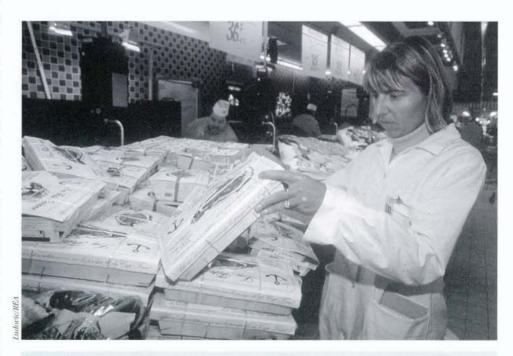
A third important priority should be to enable and encourage private actors to take more responsibility for and to contribute to the smooth functioning of the multilateral trading system. In the event, the business community has been out in front of governments in identifying problem areas and developing recommendations for eliminating trade and investment barriers. But these initiatives often reflect only narrow interests – those of the most dynamic and globalised sectors of business – while governments are under pressure to make sure that broader social concerns are also taken into account, on, say, the environment, health, culture or labour standards.

Those concerns may give rise to trade frictions, in particular where governments address them through trade restraints (as when the EU banned imports of meat treated with growth hormones or when the United States banned imports of tuna caught in ways that killed dolphins). Yet these concerns are also acting as a catalyst for co-operative approaches in which corporations and private groups themselves assume more responsibility for balancing competing interests. Issues of 'corporate responsibility' are not new, of course: they have been debated sporadically over the past fifty years. The fast pace of globalisation is now reviving this agenda.

As part of a broad drive to combat business-related corruption, OECD ministers signed a convention last December which makes bribery of government officials in foreign countries by businesses a criminal offence. Governments are taking a harder look at company practices that can keep competitors out of national markets and at how to reinforce competition policy as a possible remedy. In parallel, more and more

corporations are voluntarily adopting principles for ethical and responsible corporate behaviour towards consumers, workers, investors, suppliers and the communities in which they operate. Such codes of conduct typically commit participating companies and their immediate business partners to respect standards on child labour and other employment practices, healthy and safe working conditions, or environmentally responsible production practices. They take many forms, ranging from the company-specific Code of Vendor Conduct which applies to all factories that produce goods for Gap Inc. or any of its subsidiaries and affiliates, to the Principles for Business Conduct formulated and subscribed to by a broad coalition of enterprises from Japan. Europe and the United States that form the socalled Caux Round Table.

Such self-regulatory activity even extends to cyberspace, where the international business community has started with the development of guidelines on how transactions over the Internet should be conducted.² Governments, too, can



Domestic regulations intended to safeguard consumer health – on the expiry dating of perishable food or on additivies, for example – can have a considerable effect on international competition.

Trade Policy in 2000

play a central role in promoting electronic commerce – and stimulating the jobs that are

created by the demand for information technology goods and services – by removing remaining barriers to trade in services.

Although it is unlikely to replace government policies, self-regulation may come to play an important role in keeping controversies involving safety, animal rights, environmental protection or child labour from undermining confidence in the global trading system. As with mandatory government regulation, the challenge is to ensure that voluntary agreements are transparent, non-discriminatory and do not have adverse effects on trade and investment.

Organising Liberalisation

The spectrum of issues that form the trade-policy agenda is vast. Two 'systemic' issues are particularly important: how to structure future negotiations, and how to deal with the challenge of regionalism.

Replacing the periodic 'rounds' of the last half-century, a variety of other avenues for co-operating on trade and trade-related issues are presenting themselves. Outside the WTO, discussions aimed at removing technical barriers to trade, reducing restrictions on foreign investment, or

streamlining customs procedures are currently underway in fora as diverse as the OECD, the Free Trade of the Americas (FTAA) process, the Asia Pacific Economic Co-operation (APEC) grouping or the Transatlantic Business Dialogue (TABD).

Governments are now examining the options for organising future negotiations and have started to promote, or even try out, different formulas. For example, some governments favour a more continuous kind of negotiating activity. To some extent, the various WTO committees

American style.

American clothing.

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Gap Inc. is one of the growing number of companies whose suppliers must observe codes of conduct – on child labour, health and safety conditions and environment-friendly production practices.

overseeing the implementation of the Uruguay Round and reviewing the operation of the agreements that emerged already function as continuing negotiating fora. Combined with the built-in negotiating agenda of the Uruguay Round, these discussions may well help keep up the momentum for liberalisation.

In 1997, more than 40 developed and developing countries jointly decided to eliminate tariffs on imported information technology products. And the APEC countries have recently committed themselves to examine other product

sectors, such as environmental goods, medical equipment or chemicals. These moves suggest another option: to co-ordinate the removal

of barriers to trade on a sector-by-sector basis, starting out with tariffs but progressively covering also relevant nontariff issues.

Some countries believe that, in such highly protected markets as agriculture or textiles and apparel, only a broader 'package deal' of reforms will be strong enough to overcome domestic opposition to liberalisation. Opportunities for trade-offs across a range of issues facilitate a successful outcome because governments that are asked to make some politically painful commitments on liberalisation can exchange these for desired concessions from their trading partners in other areas. Of course, the more issues are placed on the agenda, the longer a negotiation is likely to take.

Even if the tradition of the GATT is sustained with a new 'round' of negotiations launched in the coming years to tackle a broad agenda of issues, some adjustments to this format will nonetheless be desirable. The business of trade diplomats in the early postwar decades was limited to exchanging concessions involving visible and readily measurable tariffs. But as bargaining has been extended to the domain of less quantifiable and more complex practices and policies and many more countries have joined the

GATT/WTO, it has become more difficult to achieve consensus. The Tokyo Round took seven years, and if the four years spent on launching the negotiations are also counted, the Uruguay Round lasted for more than a decade. If trade policy is to keep up with the fast pace of technological and other change in the world economy, and the WTO is to remain the centre of activity on trade policy, such a drawn-out process will have to be avoided.

As discussions intensify on how to organise liberalisation in the future, solid preparations for

negotiations will become more and more important. The preparatory process is often the most difficult part of a trade negotiation. Countries have to start by defining problems and frameworks for negotiation and generate strong domestic support for their participation. For example, tariff reduction ceases to be an 'easy' item when it comes to sensitive sectors such as agriculture. The preparations leading to the Uruguay Round exposed governments to the new trade issues of the 1980s and brought a clearer understanding of, for example, the extent to which government policies distort agricultural

Two 'systemic' issues are particularly

important: how to structure future

negotiations, and how to deal with the challenge of regionalism.

trade or how services trade takes place. The OECD is an active contributor to this kind of preparation.

The preparatory process will become even more important

because some of the newer concerns and issues in trade policy (such as domestic regulations relating to private anti-competitive conduct, health or safety) are complex and highly technical. This process is taking shape within the WTO work programme. Studies carried out by the OECD are helping to clarify some of the remaining problems and assist progress in negotiations – by, for example, highlighting remaining tariffs, quantifying restrictions affecting services markets or identifying principles or criteria for assessing the international market-access dimension of domestic regulations. Discussions on regional integration can likewise be very useful here.

The second 'systemic' issue involves regional economic co-operation, which was once marginal to the international trade agenda but over the last decade has been gathering momentum on almost every continent. There is no major country that is not now a party to at least one regional economic arrangement. These alliances range all the way from the deep economic integration of the EU to the loose association of countries in the Asia-Pacific region striving for free trade and investment between the years 2010 and 2020 by means of concerted voluntary action, without any plans for the establishment of a free-trade agreement (FTA) or a customs union.

The explosion of interest in achieving closer regional integration in all parts of the world has inevitable consequences for the evolving debate on trade policy. Regionalism is controversial for the simple reason that its effects on world trade and investment and the global trading system are not clear. It is unarguable that regional and other types of preferential trading arrangements have helped sustain the trade-liberalisation momentum well beyond the conclusion of the Uruguay Round. And efforts to build the 'global architecture' for trade in the 21st century can receive considerable assistance from discussions

in regional fora that make existing national policies and practices more transparent, provide the testing-ground for new negotiating approaches and produce models for open-

market rules in areas not currently covered by multilateral disciplines.

Yet selective bilateral or regional arrangements that give specific trading partners more marketaccess privileges than others are inherently discriminatory and can result in major diversions of trade and investment. In addition, the many preferential arrangements now developing or coming under discussion are very diverse, each giving rise to a different set of procedural or substantive rules. Such a world does not present the most efficient framework for businesses that think and operate globally. Existing WTO rules governing the formation of FTAs and customs unions are themselves vague, so that the management of regionalism, including approaches intended to facilitate the convergence of regional trade rules, ought to be subject to further refinement and updating.

It is apparent that further multilateral progress in removing obstacles to market access would mitigate any risks posed by regionalism for third parties. To a large extent, future global negotiations will be driven by the WTO's built-in agenda, which foresees further efforts to liberalise or improve rules before the end of the century in fields

such as agriculture, government procurement and services. In addition, policy recommendations developed by the private sector as well as the perceived necessity of finding effective, common approaches to issues that trigger trade friction are likely to provide impetus for yet broader multilateral action to ensure that the globalised economy is ready for the challenges of the 21st century.



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The Arrangement

Steve Cutts and Janet West

In 1998 the Arrangement on Guidelines for Officially Supported Export Credits – a 'gentlemen's agreement', not an OECD legal act – celebrates its twentieth anniversary. By successfully regulating terms for officially supported export-credit insurance, guarantees and financing, the Arrangement has helped to remove governments from the competitive package. The result is that exporters now compete on the price and quality of the exports and the service they offer, rather than on the basis of the volume and quality of the support they receive from their governments. The development of the Arrangement is nonetheless far from complete: there are many issues which its participants still want to address and for which guidelines have yet to be set.¹

he Arrangement on Guidelines for Officially Supported Export Credits, as its name suggests, sets out guidelines to regulate officially supported (that is, government-backed) exportcredit guarantees and insurance against the risk of non-repayment. An export credit arises whenever a foreign buyer of exported goods or services is allowed to defer payment. Export-credit insurance and guarantees may take the form of 'supplier' or 'buyer' credits where the exporter's bank or other financial institution lends to the buyer or his bank respectively. The Arrangement also regulates official financing support where the government provides such loans directly, offers refinancing or supports interest rates.

The institutions which undertake these official activities, for or on behalf of governments, are export-credit agencies (ECAs). There are many different types of ECA: they can be government-owned (as with the Export Credits Guarantee Department – ECGD – in the United Kingdom, which is a government department), or privately owned institutions which administer an account, separate from their commercial business, for or on behalf of and with the full backing of the state (as with the Compagnie française

d'assurance pour le commerce extérieur – COFACE – in France). Similarly, they can be guarantors of repayment (like the ECGD), insurers (like COFACE) or direct lenders such as Japan's Export-Import Bank or the Export Development Corporation (EDC) in Canada.

Before the Arrangement came into existence, there were no detailed rules (apart from the subsidies code of the GATT) governing the terms which could be offered to ECAs. In this environment a credit race threatened and interestrate subsidies flourished. That led a number of OECD countries to recognise the mutual financial benefits of regulating government involvement so as to provide a framework for the orderly use of officially supported export credits and thus 'level the playing field' for exporters through the elimination of trade distortion and subsidies. The result of these deliberations was the Arrangement on Guidelines for Officially Supported Export Credits, then colloquially known as 'the Consensus', which was formally established under OECD auspices in 1978.

The Arrangement applies to officially supported export credits with a repayment term of two years or more (most short-term business is now underwritten by the private sector) and sets out, *inter alia*, maximum repayment terms and, where official financing support is involved, minimum interest rates. From April 1999, the disciplines will also encompass minimum risk-based premium fees for country and sovereign risk.

The Arrangement also details the circumstances in which trade-related tied and partially untied aid may be given in transactions where aid funds are provided on the condition that the goods/services being supported are purchased from the country providing the aid money (a restriction which is sometimes extended to a limited number of other countries).

There are, of course, provisions for derogations from, and possible exceptions to, the export-credit and aid disciplines of the Arrangement as well as procedures for notifications, exchanges of information, consultations and review.

The Arrangement is extremely effective in terms both of the adherence of its participants to the disciplines and of its ability to adapt to reflect changing market developments. What makes this ability the more remarkable is that the Arrangement is simply a 'gentlemen's agreement', based on transparency and peer review, with no binding mechanism for settling disputes. It thus represents an excellent example of how the OECD approach of 'soft law' based on peer pressure can work.

Most OECD countries participate in the Arrangement² and all except Iceland are either members or observers of the Group on Export Credits and Credit Guarantees (ECG), a subsidiary body of the OECD Trade Committee. The ECG provides a technical forum for discussion of issues in advance of the political negotiations which take place between the participants to the

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on Export Credits

Arrangement. The 'observers' include the International Union of Credit and Investment Insurers (the 'Berne Union'), the Secretariat of the World Trade Organization (WTO) and, when relevant, the European Bank for Reconstruction and Development (EBRD).

Export markets are, of course, highly competitive, which makes the ability to construct an attractive financial package in support of an export deal vital to its successful conclusion. The advent of globalisation and the evolving sophistication of financial markets has caused this competitive pressure to grow, making it necessary to enhance the existing provisions of the Arrangement and, from time to time, to develop disciplines in new areas.

How the Arrangement Has Developed

The participants to the Arrangement have reached a sizable number of agreements since its inception in 1978. Among the most recent, concluded under the Chairmanship of Kurt Schaerer (from the Federal Office for Foreign Economic Affairs, Switzerland), are several that bring important refinements to the multilateral trading system, and especially to export credits. And there are, of course, a number of negotiations currently underway and 'emerging issues' under active discussion.

Guiding Principles for Premium Fees

One of the most note-worthy developments of recent years was the agreement on the 'pricing' of official support reached in June 1997, the so-called 'Knaepen Package' (named after the Chairman of the Working Group on Premia Fees, Pierre Knaepen of the Belgian ECA, OND).³ In essence, these ground-breaking new rules, which come into force in April 1999, provide for minimum risk-based premium fees which should be adequate to cover the risk of non-repayment by an overseas country/government in markets in which OECD exporters are active.

The agreement will also take into account both the quality of the official support being offered to exporters (reflecting the principle that a better quality of product should be reflected in a higher premium fee) and the obligation under the rules of the WTO that premium fees should not be inadequate to cover long-term operating costs and losses.

From a situation where no rules previously existed on risk-pricing, the participants have reached an agreement which should prevent the use of premium subsidies as a competitive tool.

A New Arrangement Text

Another milestone was the agreement, in November 1997, on a revised text of the Arrangement. The new text, which took two years to finalise, is the first revision of the Arrangement since 1992. As such, the task which faced the Redrafting Group (RAG), under the Chairmanship of Bob Crick (from the United Kingdom's ECA, the ECGD), was far from easy. The 1992 text had not been updated to include the numerous amendments to the Arrangement which had been agreed since then; moreover, the text required a complete overhaul in terms of format and language. The result of the work of the RAG is a text which is far easier to read than the old one. Once the European Community has completed a series of legal procedures (it incorporates the Arrangement into 'hard law' through a Decision of the EC Council), the new text will be disseminated publicly.

Guidelines on Tied Aid for Donors and Project Sponsors

Another important development of recent years was the agreement, in November 1996, on *Ex Ante* Guidance for Tied Aid, which codified four years of experience with the disciplines on tiedaid credits that had been negotiated in 1991.

The disciplines on tied aid are known as the 'Helsinki Package' since they were drafted in the Finnish capital under the chairmanship of Eero Timonen from the FGB, the ECA of Finland. The disciplines had become necessary with the increasing demand for infrastructure projects, particularly in developing countries, and the proliferation of trade-related aid (which many commentators, in both government and the private sector, considered to be trade-distortive as it disadvantaged strictly commercial bids for con-

tracts). Accordingly, the view of the participants was that such aid should be targeted towards projects and to countries with little or no access to market financing. The use of tied aid was therefore to be redirected to projects which were not commercially viable and thus could not be realised with commercial financing.

The development of Ex Ante Guidance, to help export-credit and aid agencies and project planners foresee at an early stage whether a project would be eligible for tied aid or whether it should be financed commercially, was possible only after four years of evaluating individual projects on a case-by-case basis. These evaluations took place monthly in 1992-96 in a Consultations Group at the OECD (under the successive chairmanship of Birgitta Nygren and Frans Lammersen of the Swedish and Dutch Permanent Delegations respectively to the OECD), the aim being to discern trends as to which type of project was likely to be determined as eligible for aid and which was not. The guidance explains, for example, that manufacturing projects are likely to be considered commercially viable and, therefore, ineligible for a tied-aid credit and that the converse is true for many social projects. Experience confirms that these tied-aid disciplines are extremely effective in redirecting aid away from commercially viable sectors to those which require aid funds for the realisation of projects.

A Commercial Interest-Rate Regime, Automatic Country Classification and a Future Work Programme

In 1994, between the conclusion of the tied-aid disciplines in 1991 and the codification of experience under these disciplines in 1996, the participants agreed on another major package

- 1. The Export Credit Arrangement 1978–1998: Achievements and Challenges, OECD Publications, Paris, forthcoming 1998.
- 2. Australia, Canada, the European Community (Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden and the United Kingdom), Japan. Korea, New Zealand, Norway, Switzerland and the United States.
- 3. Details of the principles for setting premium fees (the 'Knaepen Package') can be found on the OECD website at http://www.oecd.org/ech.
- 4. Available from the Export Credit Division of the OECD Trade Directorate.

The Arrangement on Export Credits

of reforms to the Arrangement. The regime of subsidised interest rates was abolished in favour of universal market-based interest rates (termed Commercial Interest Reference Rates, or CIRRs) and an automatic classification of countries was introduced to determine maximum repayment terms, based on GNP per capita figures, so that the longest repayment terms are available only to the poorest countries.

The participants also agreed on a work programme which included further work, in co-operation with the OECD Development Assistance Committee (DAC), on global untying of aid. In order to prevent distortion of competition the participants made a commitment to investigate further both the issue of transparency and the definition of the so-called 'market-window' operations (institutions related to governments which are able to raise finance and lend at very low rates of interest but which may not currently follow all the provisions of the Arrangement). And they undertook to start negotiations on complementary guidelines on export credits for agricultural products. The programme for future work also included an agreement by the participants to investigate guiding principles with a view to produce convergence among ECAs' premium fees. This range of measures has a name-tag: the 'Schaerer Package', after the current chairman of the participants to the Arrangement who led those negotiations.

Extending and Refining the Guidelines

The flexibility of the Arrangement allows it to reflect political and market developments. A main issue now under negotiation, prompted by commitments from the Uruguay Round (as reflected in the WTO Agreement), is complementary guidelines for agricultural products. Although currently exempted from the provisions of the Arrangement, many of the participants feel that such guidelines are required to preclude subsidies and distortions of competition. Against this background, OECD ministers in 1997 urged the participants to conclude an agreement as soon as possible. The current negotiations also seek to take into consideration other relevant international obligations and understandings, such as the Food Aid Convention and the WTO Agreement on Agriculture.

Another major issue facing the participants is that of project financing, a technique that is used increasingly, particularly for infrastructure projects, where loan repayments are made from the revenue generated by the projects them-

> selves. The participants are set to negotiate flexibility in the Arrangement which will better accommodate the structure of such deals (current guidelines, which require equal semiannual loan repayments beginning at six months after the start of the credit, do not reflect the revenue-generating potential of many of the projects in

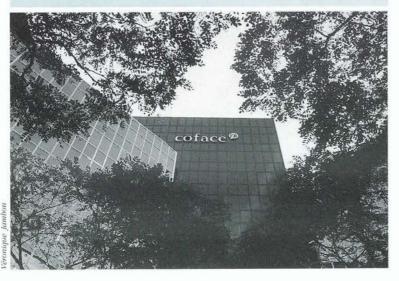
volved). These negotiations follow much analytical and technical work in the ECG over the past year or so.

The participants are also examining the operations of the 'market windows'; the working of the CIRR regime, which is being considered against the background of market developments and ECA practices; and, in conjunction with the DAC, the further untying of aid which some consider desirable since such aid is less likely to be trade-distortive.

In addition, the ECG is examining the issues of the environment and of bribery, and in particular how ECAs providing official support might take account of the environmental impact of projects and of the requirements of the International Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, recently concluded at the OECD. Also, against the background of the likely increase in the membership of the European Community and future developments in the OECD, the ECG is reviewing its membership criteria. And a very recent issue on the ECG agenda is that of an initiative made by the United Kingdom on debt relief for the highly indebted poor countries, which suggests that official support from ECAs for such markets should be focused on productive expenditure only.

The pace of change in the world of export credits has accelerated dramatically over the past four years as the participants to the export-credit Arrangement have refined their agreement to reflect market realities and to drive out trade distorting subsidies. There is every reason to believe that this drive for squeezing out subsidy and trade distortion will continue into the next millennium.

COFACE, the French export-credit agency, is a privately owned insurer acting on behalf of the state.



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Trade Liberalisation in the Transition before transition territories, more economic stabilis imity to alternative rapid progress in to of open trade pla with the initial co-

Blanka Kalinova

The adoption of market-led and outward-oriented economic systems in the formerly communist countries of central and eastern Europe has brought with it the liberalisation of their trade policies. They have implemented trade reform unilaterally, some joining regional integration initiatives and a few participating actively in multilateral trade negotiations. Progress in creating a more transparent and predictable trading environment has been remarkable, but fragile external balances still risk encouraging domestic pressures for protectionism. Adherence to international trade disciplines can help consolidate recent achievements and facilitate the integration of transition countries into the world economy.

rade reform has been an integral part of the 'first generation' of economic reforms and was implemented by most transition countries in central and eastern Europe soon after the fall of communism. The opening of their economies to the outside world was considered critical to overcome the legacies of central planning, not least a distorted and administered price system, lagging productivity and a technological

backwardness rooted in relative isolation from external trade and investments flows. By increasing exposure to world prices and foreign competition, trade liberalisation has helped accelerate adjustments in prices, rationalise the allocation of resources and streamline decisions on investment, thus allowing the transition countries to participate more effectively in the globalised economy.

The extent of trade reform has varied from country to country, reflecting differences in initial economic conditions and the approach to reform that was chosen. The central and eastern European countries (CEECs) in particular benefited from fewer impediments from the period

before transition than in other ex-communist territories, more rapid and successful macroeconomic stabilisation and geographical proximity to alternative markets, all of which allowed rapid progress in trade liberalisation. Their regime of open trade played a decisive role in dealing with the initial contractions in foreign trade that resulted from the collapse of the Council for Mutual Economic Assistance (CMEA). Furthermore, dynamic exports have been a driving element in economic recovery. Nonetheless, despite relatively large inflows of foreign direct investment (FDI) and numerous subcontracting arrangements with western producers, exports of higher value-added products have grown more slowly.

The massive demands of modernisation and its concomitant pressure from imports meant that the external vulnerability, illustrated by the fragile trade balances that still afflict many transition countries, was probably inevitable. Yet widening trade deficits in central and eastern Europe reveal some unresolved fundamental problems. in particular an unclear ownership structure and the disfunctioning of some economic activities, especially in banking. By delaying necessary restructuring and investment decisions, these shortcomings have postponed the development of internationally competitive export capacities in, for example, more technologically advanced sectors, which should prove decisive in sustaining exports and economic growth.

Trade-policy reform has faced more serious obstacles in the New Independent States of the ex-Soviet Union (NIS). The NIS, with the exception of Russia, were less familiar with applying basic trade instruments and inexperienced with the laws and institutions of trade policy. Moreover, their uneven progress in macro-economic stabilisation, high inflation rates and volatile exchange rates have continued to blur price signals, thus preventing domestic producers from adopting longer-term strategies. Delays in structural reforms – privatisation and competition policy in particular – have also hampered trade liberalisation, since powerful sector-specific lobbies with

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Trade Liberalisation in the Transition Economies

FOCUS

Policy Recommendations at the Three Stages of Trade Reform

Initial stage of reform

Typically countries with high inflation or hyperinflation, a volatile exchange rate, direct price controls and a very limited private sector:

- reduce the number of export bans or quotas and replace them with price-based measures
- limit the scope of state intervention by abolishing the system of state orders, export/import registration and the use of barter
- eliminate multiple exchange rates and surrender-requirements of foreign-exchange earnings.

Intermediary stage

Countries where inflationary pressures have decreased, the exchange rate has started to stabilise, prices are partially liberalised, direct state intervention has declined and privatisation programmes have been initiated:

- · abolish remaining export controls
- continue to reduce the discretionary power of authorities
- establish a tariff schedule with the objective of avoiding peaks and excessive dispersion of tariff rates.

Third stage

Countries where inflation has been reduced, most price controls abolished, most specific trade taxes replaced by VAT and large- and small-scale privatisation programmes actively pursued:

- fix a pre-announced timetable for the simplification and reduction of tariffs with the objective of binding tariff rates
- progressively implement multilateral trade principles and disciplines, in particular for non-tariff measures and subsidies
- introduce current-account convertibility (through signing Article VIII of the IMF Articles of Agreement)
- adjust bilateral/plurilateral preferential trade agreements in line with multilateral trade principles.
- 1. 'Designing New Trade Policies in the Transition Economies', OECD, Paris, 1997, available free of charge from the Outreach and Analysis Division of the OECD Trade Directorate.

privileged links to governments (in the automobile sector, for instance) often resist liberalisation efforts. Other factors make the trade re-orientation of the NIS slower than that of the CEECs: excessive concentration of production units inherited from central planning, especially in heavy industry; high energy dependency; relative remoteness from alternative market outlets. As a result, the NIS, including Russia, have had a rather mixed trade performance. The available data (which have to be used with caution) suggest that Russia records a large trade surplus but continues to depend on exports of energy products and that, with the exception of arms, the share of manufactures in total exports remains disproportionately low.

External Support to Trade Liberalisation

Support by OECD countries has been very important for trade reform in the NIS and CEECs. In 1990-93 these countries were granted mostfavoured nation (MFN) status and general system of preferences (GSP) benefits, and the quantitative restrictions that targeted former socialist countries were eliminated. Preferential trade agreements have improved market access, especially after the signature of the comprehensive and far-reaching Europe Agreements concluded between ten CEECs (including the Baltic states) and the European Union. A range of restrictive measures nonetheless continues to hamper exporters in the CEECs and NIS. These restrictions are often concentrated in so-called 'sensitive sectors', such as agricultural products, steel, footwear, textiles and clothing, which are still subject to relatively high tariff and non-tariff barriers and in which some transition countries would appear to have considerable export potential. Exporters of these countries also frequently complain about a large number of antidumping investigations and the special procedures used to assess anti-dumping claims which treat Russia and other NIS as non-market economies. These countries argue that comparison using prices in the 'similar country' rather than local information can be biased because it does not take sufficiently into account the possible comparative advantages of the producers from transition economies.

The export capacities of the CEECs and NIS are limited also by domestic impediments:

- underdeveloped infrastructures
- · protracted customs procedures
- a regulatory environment which lacks transparency and is often corrupt
- an over-complex system of standards and product-certification requirements
- restrictions on freedom of ownership
- · ineffective law and contract enforcement.

Tackling many of these problems requires a substantial volume of investment, not least from abroad. But an essential element is the ability of the governments in the CEECs and NIS to establish sound economic and trade policies. Creating more 'market hospitality' would favour trade expansion and FDI inflows to transition countries and facilitate new trade initiatives by OECD countries.

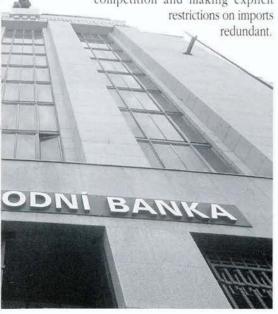
Trade reform has required specific actions to dismantle the centrally planned system. The state monopoly of foreign trade had to be abandoned and, in the NIS, the standard instruments of trade policy, such as tariffs, which were not used previously, had to be introduced. Several CEECs, especially those which were already members of the GATT (and later the World



Republics, Hungary, Poland and Romania – have rapidly adopted multilateral trading rules. The NIS have made slower progress, mirroring the more difficult starting conditions and their uneven achievements in reform.

The Pace of Liberalisation

In its initial stage, trade reform is determined by three main factors: the relative rapidity with which prices are liberalised, progress in reducing inflation, and stabilisation of the exchange rate. Recent developments in trade policy in Russia and other NIS thus followed a pattern of three successive stages (box, p. 16). The effects of removing administrative controls that kept domestic prices divorced from those on world markets were massive inflationary pressures and a substantial depreciation of the exchange rate. To cushion the impact of freer prices on consumers and ensure the availability of vital inputs for domestic producers, the NIS governments relied on export restrictions, in the form of licenses, quotas and surrender requirements on export earnings in foreign currencies. The undervalued exchange rate kept import prices high, thus shielding domestic producers from international competition and making explicit





The concentration of production, especially in heavy industry, has retarded changes in trade orientation.

A 'virtuous' circle of trade reform can be set in motion when a far-reaching liberalisation of prices is accompanied by credible commitments to fight inflation; that then allows exchange rates to stabilise at positions which encourage exports, without making the costs of imports prohibitive. A more realistic exchange rate, together with domestic prices closer to those prevailing on world markets, will reduce the pressure for export restrictions designed to limit lucrative sales abroad and keep vital products at home.

With a loosening of export controls, direct interventions in foreign trade tend to diminish, but the role of the state remains important. As the appreciation in the exchange rate makes imports more competitive in the domestic market, the reliance on traditional trade instruments, such as tariffs, becomes necessary. Yet when they are confronted with intensified protectionist pressures, the authorities are often tempted to adjust the available trade-policy instruments, especially tariffs, and resort extensively to non-tariff measures (complex standard and certification procedures, for example).

To maintain the momentum of trade liberalisation, the anti-export bias that dominated the socialist system has to be suppressed so as to allow increased earnings from exports and improved foreign reserves. Modernisation of production capacities through imports of capital goods can thus be pursued, helping domestic producers become more sensitive to developments in international markets and improving their competitiveness on both domestic and external markets. The necessary next step in trade liberalisation is the gradual adherence to international trading disciplines, such as the acceptance of full current-account convertibility and the initiation of negotiations for WTO membership in the case of the NIS.

Domestic Developments

Trade reform should be sustained by sound macro-economic policies, to assure, in particular, fiscal balance and stable exchange rates. Taxes on foreign trade, for example, are unlikely to be reduced if the government encounters lasting problems in collecting budgetary revenues. And unsustainable appreciation of the exchange rates which exacerbates trade imbalances could provoke outflows of short-term speculative capital, further threatening macro-economic stability.

Trade reform likewise goes hand-in-hand with structural transformation, especially privatisation



The NIS have had a mixed trade performance. And even if Russia records a large trade surplus, it continues to depend on exports of energy products.

and competition policy which facilitate the entry of new firms and discourage market concentration that might allow protectionist alliances among major producers to emerge. Labourmarket policies should also support trade liberalisation by encouraging the mobility of the workforce, especially from uncompetitive import-competing sectors, such as heavy industry, to export-oriented ones (services, for example). Structural improvements in the banking system also aid trade reform, since poorly functioning banks reduce the efficiency of foreign-trade operations and make the financing of modernisation requirements difficult and expensive.

A solid legal basis, with clear and predictable trade regulations, is another prerequisite, since their absence is a major barrier to FDI. An unstable trade environment is usually accompanied by a large amount of discretionary power for governmental officials and, often, by a high degree of corruption. Legal uncertainty and the inadequate enforcement of contracts discourage firms from investing and modernising their production facilities. These problems can be alleviated by adopting more frequent and timely disclosures of regulatory changes and by channelling more resources toward improving the efficiency of trade-related services (in customs, for example).

The Advantages of International Disciplines

Adherence to multilateral trade disciplines prevents backsliding in reforms already achieved and ensures the pursuit of further liberalisation steps. Membership of the WTO serves as an insti-

tutional anchor for reforms in traditional tradepolicy areas through tariff bindings, the acceptance of disciplines in the application of nontariff measures and contingent protection instruments, such as anti-dumping and safeguard measures. In addition, the WTO provides a useful framework for several of the 'new' areas of trade policy that resulted from the Uruguay Round, including trade in services and traderelated intellectual property rights and investment measures.

Some transition countries appear to focus too much on balancing the short-term advantages and disadvantages arising from the acceptance of multilateral disciplines. They see problems in the considerable burden placed on their legal and institutional capacities and in the potential restrictions on their room for manœuvre in setting trade policies. Some government agencies,

supported by sectoral lobbies, believe that multilateral disciplines are too tight for the unpredictable economic environment currently prevailing in their countries. It cannot be argued that these countries would be faced with an enormous task in adopting a range of many new laws and in reviewing their entire legal system for its compliance with international rules. That is especially true for the NIS, which are currently subject to few international disciplines. Also, some recently established regulations – the recent economic and trade re-integration attempts within the NIS, for example – could be in conflict with existing WTO rules.

Instead, the role of new WTO-based trade policies should be viewed in a wider perspective, which takes into account the effectiveness of liberalisation in improving the responsiveness of the economy and in fostering reform. The stimulus it would give to competition would help with restructuring, especially by bringing pressure for the elimination of distortive subsidies that delay the advent of internationally competitive exports. The acceptance of international disciplines and the access to the WTO dispute-settlement mechanisms will also improve domestic and international creditworthiness, which is indispensable for the creation of a more businessfriendly economic environment, not least for foreign investors.

From a forward-looking perspective, the transition economies clearly have a strong interest in participating in the WTO's discussions on further developments in the international trading system and ways of strengthening multilateral disciplines. They will find, furthermore, that several issues under discussion, such as links between trade and competition and investment, are of direct interest to them.

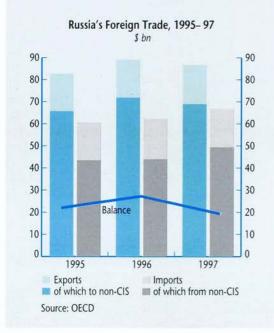
If credible trade liberalisation is to yield the gains expected, and the inevitable adjustment costs are kept to a minimum, it will require support from macro-economic and structural measures and a well-designed regulatory framework that can be adequately enforced. The transition countries should then be able to face the difficulties generated by current economic reforms and take ad-

vantage of the continuous process of globalisation. To this end, the OECD is sharing its policy analysis on the experience of those CEECs which have undertaken reforms more swiftly and on the links between trade and other economic policies, by making available the experience of OECD countries in some specific areas, such as the interface between trade and competition policies, and by facilitating the exchange of views among trade officials and representatives of the private sector.

FOCUS

Russia's Foreign Trade

Since 1992 Russia has regularly recorded sizable trade surpluses, in 1996, corresponding to some 5% of its GDP. But in 1997 the positive trade balance (amounting to almost \$20bn according to Russian preliminary data) shrank in comparison with the previous year. This situation reflects the loss of export dynamism (-3%), which suffered from declining petroleum prices, and continuing import growth (by some 7%), sustained by recent real exchange-rate developments. Russia continues to depend on exports of energy products (47% of total exports), while the share of machinery and equipment remains chronically low (less than 10%).





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Uncovering Real

Willem Adema

otal government expenditure on social policy covers a wide range of areas: cash benefits for disability, old age, survivors, occupational injuries and diseases, sickness, families, unemployment and housing; health care; services for the elderly and disabled; active labour-market policies; and other payments such as those to people on low income and to refugees. But the spending figures on the state budget fail to reflect the true expenditure on social-policy objectives, for two reasons.

First, budgetary allocations do not fully account for the impact of the tax system, which affects social spending in a country in three ways: the government can give tax advantages to benefit recipients (tax allowances for parents, for example); benefit income can be taxed directly; and recipients have to pay indirect tax on their consumption. Net (that is, after-tax) spending can thus often fall well below gross expenditures.

Second, the budget does not account for certain social benefits which, although mandated by the state, are not paid out of the public purse. Governments often oblige employers to pay benefits to their employees, and sometimes force self-employed people to take up social insurance. For instance, the new Sickness Act in the Netherlands - implemented in 1996 - stipulates that employers have to continue to pay employees 70% of their full wage for the first year of sickness. These benefits were previously paid through the state social-insurance system and have thus been shifted from the public budget to the private sector. And in the United Kingdom, under given conditions, firms and individuals are allowed to opt out of the 'State Earnings Related Pension Scheme' (SERPS), as long as they make alternative pension arrangements.

The data on gross expenditure recorded in public budgets require a number of corrections to get a better view of that part of GDP to which

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There is growing interest in comparing the social-protection systems of different countries. The OECD has therefore set up a 'social expenditure data base' which contains detailed information on a wide variety of social policy areas. Since the gross data on public expenditure recorded in national budgets give an incomplete picture of spending on social-policy aims, the OECD is now developing indicators on net social spending. The results are surprising.

recipients of publicly decided direct and indirect social support lay claim.1 To account for these institutional differences, adjustments in the statistical treatment of cash benefits and fiscal measures are necessary if comprehensive international comparisons of social protection systems are to be possible. For example, direct taxes and social-security contributions are low in the United States and as a result net expenditure is not much less than gross expenditure (Table, p. 22). But in the Netherlands cash benefits are rather heavily taxed, so that the Dutch government claws back about 20% of expenditures on cash benefits. Such adjustments do not, of course, apply to all expenditures. For example, the value of social services provided directly to clients (benefits in kind - hospital treatment or child care, say) in principle remains unaltered by the calculations.

Initially, estimates of net social expenditures have been prepared for the six countries for which data are available: Denmark, Germany, the Netherlands, Sweden, the United Kingdom and the United States.²

Taxation and Benefits

In some OECD countries, such as the United Kingdom and the United States, several kinds of benefit are paid net of tax; in others such as the Netherlands and Sweden they are taxed in the same way as income from work. In the United

Kingdom, for example, the recipient of an unemployment benefit whose last earnings were those of an average production worker (APW) and who lived in a 'one-earner' family with two children received (including housing and family benefits) £11,830 in 1995 (equivalent then to \$18,659) on which he or she did not pay tax. By contrast, a similar unemployed person in the Netherlands in 1995 received annual unemployment benefits of 39,323 guilders (\$24,613) on which he or she paid 12,385 guilders (\$7,716) in income taxes and social-security contributions. Including housing and family benefits his or her net income was 31,704 guilders (\$19,753).3 Unemployment benefits in the Netherlands are still slightly higher than in the United Kingdom, but differences are not as high as gross expenditures

The first step in the measurement of net government effort is the deduction of direct taxation and social-security contributions from the gross spending totals to arrive at 'net cash direct public social expenditure' – line 2 in the Table. Correcting for the taxes and social-security contributions paid on social transfers both facilitates international comparisons and gives a clearer picture of spending over time. In Denmark in 1994, for example, old-age cash benefits and social-assistance benefits became taxable. Simultaneously, social-assistance benefits were raised to preserve their net value, leading to an increase in gross expenditure of about 0.5% of GDP. Moreover, specific tax allowances for pensioners

Social Spending

were abolished and benefits increased by an equivalent amount: gross expenditures thus grew by about 1.8% of GDP.⁴ In both cases, net government spending was unaffected, but gross expenditures went up substantially.

Cash transfers made under social-policy programmes are generally spent by their recipients on goods and services such as housing, food, clothing and so on. To take one item of household spending to show how benefit spending can return to the exchequer, in Germany in 1993 taxes on coffee amounted to \$1,309 million,5 part of which was paid by benefit recipients. The government claws back part of its welfare spending through indirect taxation. To account for this 'give-and-take', the flowback of indirect tax receipts to the exchequer following the spending of cash transfers is estimated and deducted from net cash direct social transfers to obtain a measure of 'net direct public social expenditure' (line 3 in the Table).

In practice, of course, policy-makers have recognised the link between indirect taxation and the position of people with low incomes or in receipt of benefit income. The extension of VAT to cover domestic fuel in the United Kingdom in 1993, for example, was accompanied by changes in benefit payments (particularly to the elderly) to compensate them for the reduction in the real value of the benefits.

Many OECD governments pursue some of their social-policy objectives through the tax system, often offering tax-breaks to replace cash benefits or to stimulate private spending (on child-care facilities, for example). When the revenue forgone is added to direct government expenditure, a figure is obtained for 'net current public social expenditure' (line 4 in the Table).

'Social tax-breaks' serve a variety of purposes in the OECD countries. There are tax-breaks for housing for older people (Denmark), low-income groups (Germany, the Netherlands), lone-parent families (the Netherlands, the United Kingdom), severance pay (the United Kingdom) and supplementary unemployment benefits (the United States). And they can be substantial: in Germany, the value of tax allowances – which mirror cash benefits paid in other countries – for the costs incurred in raising children amounted to almost



An examination of the state budget will not show the impact of the tax system – allowances for child care, for example.

0.6% of GDP in 1993. Tax-breaks which promote the purchase or use of private-sector facilities are also important: those made towards employer contributions to health-insurance programmes amounted to 0.75% of GDP in the United States in 1993.

Many countries have tax-breaks aimed at stimulating the take-up of private pensions. Statistically, allowances on occupational and individual pension programmes are difficult to deal with, both conceptually and in practical terms,

1. A detailed discussion of methodological concepts and data issues can be found in Willem Adema, Marcel Einerband, Bengt Eklind, Jorgen Lotz and Mark Pearson, Net Public Social Expenditure, Labour Market and Social Policy Occasional Papers, No. 19, OECD Publications, Paris, 1996.

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- 5. Revenue Statistics of OECD Member Countries 1965-94, OECD Publications, Paris, 1995.

since they are aimed at yielding benefits in the future: taxation occurs at, and tax reliefs are given at, various stages of what is a form of contractual savings. And because of the complexity of calculations arising from these issues, there is no set of comparable data available on the value of tax-breaks for pensions. What data are available indicate that they, too, can be substantial. In the United Kingdom tax-relief for these kinds of pension programme and the contracted-out rebate of National Insurance contributions amounted to 3.1% of GDP in 1993. Similar reliefs in the United States amounted to 1% of GDP in 1993. These data reflect only the cost to public budgets - on a cash basis - of the current tax system in the current financial year arising from tax-breaks for pension contributions.

Mandating Private Expenditure

Politically determined expenditure to social ends goes further than the amounts that show up in government budgets. Those figures have

Uncovering Real Social Spending

Table	
Indicators of Public Social Expenditure,	1993
% of GDP at factor costs	

	Denmark	Germany	Netherlands	Sweden	United Kingdom	United States
1. Gross direct public		22.4	24.0	10.1	260	14.3
social expenditure	35.2	32.4	34.0	42.4	26.9	16.3
Direct taxes and social contributions						
paid on transfers	4.5	2.9	6.5	5.9	0.2	0.1
2. Net cash direct public		20.5	27.5	200	267	14.2
social expenditure	30.7	29.6	27.5	36.5	26.7	16.2
Indirect taxes on consumption purchased out of net	1000					
cash transfers	4.5	3.3	2.7	4.1	2.6	0.5
3. Net direct public	222	4.74				
social expenditure	26.3	26.3	24.7	32.4	24.0	15.7
Tax-breaks for social purposes on public						
and private social						
expenditure	0.1	0.9	0.1 ^a	0.0	0.4	1.2
Net current public social expenditure	26.4	27.2	24.9	32.4	24.4	17.0
5. Gross direct mandatory	20.4	27.2	21.2	32.1		17.10
private social expenditure	0.7	1.8	,,	0.7	0.3	0.5
Direct taxes and social						
contributions paid on mandatory private						
cash transfers	0.2	0.6		0.2	0.0	0.0
Indirect taxes on consumption						
purchased out of net mandatory private	100					
cash transfers	0.1	0.2	4.	0.1	0.0	0.0
6. Net current mandatory						
private social expenditure	0.4	1.0	,,	0.4	0.2	0.5
7. Net current publicly						
mandated social expenditure (4+6)	26.7	28.2		32.8	24.6	17.5
Memorandum items:						
Pensions under			0.7			
administrative extension Indirect taxes	20.2	15.2	13.9	17.3	16.3	9.1
Related to GDP at market prices:		1,400	10000			
Gross direct public	26.7	20.7	20.4	20.2	22.4	15.0
social expenditure Net current public social	30.5	28.7	30.6	38.3	23.4	15.0
expenditure	22.8	24.0	22.4	29.2	21.2	15.6
Net current publicly						
mandated social expenditure	23.1	24.9		29.6	21.4	16.1

^{..} not applicable.

to be complemented by information on the amount of social support the private sector is mandated to provide. Governments exercise control over the terms – benefit rates, coverage and duration – under which such private benefits are provided. It can therefore be argued that mandatory spending of this sort, though private, is in many ways similar to government expenditure. The total of these mandated private expenditures is captured as 'gross direct mandatory private social expenditure' (line 5 in the Table).

As with public spending for social ends, gross mandatory private social expenditure is subject to adjustment for direct and indirect taxation, and recipients have to pay indirect tax on the services they consume. Making these adjustments gives a figure for 'net current mandatory private spending (line 6). Adding this indicator to 'net current public social expenditure' (line 4) leads to 'net current publicly mandated social expenditure' (line 7) – a comprehensive indicator of net government 'social effort'.

It is not always possible to separate mandatory from non-mandatory private social spending. Some transfer payments cannot be considered as directly comparable with mandatory expenditures without also taking their voluntary elements into account. In the Netherlands, for example, initially voluntary collective agreements which also cover pensions are often forced on an entire industry by 'administrative extension'. In this event, the data do not separate the expenditures made by employers who were party to the initial (voluntary) agreement from those by employers who were not. Such borderline cases nonetheless have clear elements of compulsion; the value of such expenditures is therefore noted in the Table as a memorandum item.

Cross-country Comparisons

To facilitate cross-country comparisons gross spending indicators are related to GDP at market prices – the most frequently used indicator of national output which includes the value of indirect taxation. But the indicators of net social

a. 1994.

Source: OECD

spending discussed above deduct the value of indirect taxes on consumption generated by cash transfers. These indicators should therefore be related to GDP at factor costs – a measure which does not include the value of indirect taxation (the two lines marked 1 in the Table⁶).

The size of the various adjustments to 'straight' budgetary data presented in the Table reflects the importance of particular institutional features in each country:

- direct taxes and social-security contributions the United Kingdom and the United States tax benefits only to a very limited extent whereas Denmark, Sweden and, in particular, the Netherlands tax benefits rather heavily; Germany is in an intermediate position
- indirect taxes indirect taxation in the United States is much lower than in European countries so the value of benefit income clawed back through taxes on consumption in European countries is much higher than in the United States
- tax-breaks for social purposes (excluding pensions) are most prominent in Germany and, especially, the United States
- mandatory private benefits are largest in Germany, where employers are forced to pay sickness benefits for up to six weeks; the data do not reflect reforms of sickness programmes in the Netherlands and the United Kingdom after 1993, which increased the importance of mandatory private benefits in both countries.

The net effect of the corrections is that, except for the United States, net 'social effort' – measured as net publicly mandated direct social expenditure – is substantially lower than the figures offered in gross budget data (compare the second part of line 1 and line 7 in the Table). For Denmark, the Netherlands and Sweden, net social effort as a percent of GDP at factor cost is almost 10% lower than gross social spending.

6. GDP at market prices captures gross expenditure on the final uses of domestic supply of goods and services at purchasers values; indirect taxes also form a substantial part of GDP at market prices. But net social spending also accounts for the value of indirect taxes which are levied by the government on benefit income. There is thus a strong case for relating data on net social spending to indicators of GDP at factor cost. GDP at factor cost does not include the value of indirect taxation and government subsidies to private enterprises and public corporations.

7. Health Data 1997, OECD Publications, Paris, 1997.



Payments made by employers to employees do not come from public funds – but they nonetheless form mandatory social spending which must be taken into account in international comparisons.

The corrections are less dramatic for Germany (4.2%) and the United Kingdom (2.3%). The budget data for the United States, by contrast, underestimate total social spending, and the available data on tax-breaks for pensions strengthen this message.

Making these adjustments casts a somewhat different light on firmly embedded preconceptions on the magnitude of the welfare state in certain Continental and Nordic European countries. Countries such as Denmark and the Netherlands, which are normally regarded as the undisputed big social spenders, appear to be in the same spending league as the United Kingdom. Sweden is still ahead of the other countries, but its ratio of social spending to GDP is also high because of the adverse demand shock, and thus relatively low GDP, in the beginning of the 1990s. Public social spending in the United States, whether measured gross or net of fiscal effects, is relatively low compared with the European countries. Private social spending non-mandatory but fiscally induced - is nonetheless substantial in the United States, on health care in particular.

When social expenditure is considered within a more comprehensive framework which accounts for fiscal and legislative arrangements rather than merely budget allocations, there is a convergence in its volume across countries. That suggests that inter-country comparisons of the 'social effort' of government which do not take into account the role of mandatory private expenditures, direct taxation of cash transfers and indirect taxation of consumption out of benefits and tax-breaks for social purposes can be misleading. Instead, the apparently large international differences in gross direct public social expenditure can be ascribed in part to institutional differences in the ways in which governments pursue common social objectives.

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Firms, Knowledge and Competitiveness

Keith Drake

Only recently, most firms assumed a given degree of technology and organised their tangible resources – human and physical capital – to produce goods or services as cheaply as possible. Now, a growing number see themselves in the first instance as creators, organisers and exploiters of knowledge, strongly focused on learning, innovation and continuous improvement of products.¹

he new knowledge-based international economy of learning individuals, organisations and economies has evolved from the machine-based economy which dominated the developed world throughout the twentieth century.² The emergence of a new type of firm is signalled by the familiar symptoms of corporate change such as devolution of managerial responsibilities, more flexibility and skill in the workforce, more recourse to outsourcing, and increased networking both inside and outside the firm the better to transform knowledge into business value.³

Any attempt to produce a single model of 'the new firm' is made impossible by the continuing importance of context. The strategic decision-making of even the most progressive firms is still influenced strongly by the fact that firms are social phenomena. Far from acting quite independently of one another, they are pro-

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foundly affected by their own history and by the behaviour of other firms in their industry. In automobile or aircraft production, where many of the technologies are used in common, firms also depend considerably on their management of long-term relationships with specific suppliers, and, in aircraft manufacture, with equally specific customer networks. Inter-firm alliances and customer networks can be major components in the matrix of knowledge assets which give a successful firm its competitive edge.

Corporate capacity to change radically and quickly is nonetheless an important characteristic of successful companies. Swatch AG, manufacturing successfully in one of the world's highest-cost economies and regaining lost market-share, and IBM, snatched back from the brink of competitive extinction, are dramatic examples. But there can be a more evolutionary growth in the capacity for change. SOL, the Finnish waste-management and cleaning-services company, has been developing a very flat, loose organisational structure in the 1990s, combining high degrees of trust and freedom for employees - half of whom are part-timers - with tight performance goals, measurement and reward systems to achieve recurrent growth of turnover, profits and employment in a country

with 17% unemployment. Asea Brown Boveri (ABB) is transforming itself from a multinational manufacturer of products which generate, transmit and use electricity into a systems designer, supplier and maintainer – that is, a builder of networks and integrator of processes. As it evolves into a knowledge-based service company, transferring more and more know-how across borders, ABB has become a firm which is both global and local, large and small, centralised and decentralised.

It is a defining characteristic of the new firm that its capacity to change itself is increasing. At the extreme it may become a 'virtual firm', a linked cluster of legal entities - for instance, in sectors such as insurance, computing, electronics and electrical engineering - which work with suppliers, employers and customers in relationbased transaction systems which could become even larger, and operate across more borders, than the consolidated behemoths which dominated international trade and investment in the 1970s and '80s. Well-known, formerly hierarchical firms are being disintegrated into flatter and looser structures in which the central task of managers becomes the management of relationships rather than materials or numbers; and influencing this complex of relationships into sympathy with public-policy goals becomes important for government.

Another feature of the emerging firm is that its investment in intangibles – for instance, human capital, R&D capacity, work systems for shopfloor and management, bespoke software, customer databases, brand and reputational capital – exceeds that in tangibles; and its market value depends increasingly on how well it manages its intellectual capital. Such firms depend heavily not only on a continuous growth of corporate knowledge but also on how well they manage this know-how, know-what, know-why and know-whom. Intangibles are important. Commissioner Steven Wallman of the US Securities and Exchange Commission predicts that ten years

hence measures of intellectual capital will be the numbers that are most watched and that financial accounts will take a back seat. Yet they are difficult to measure. The diversity and incommensurability of pay-offs and the subjective elements in evaluation disable the costbenefit analysis of R&D expenditures. Measuring what people know and how efficiently the human resource is being managed is no less difficult.4 It is possible that firms use little more than 20% of their intellectual capacity on a day-to-day basis.

There is a contrast between the traditional idea of the firm as an organiser of human, physical and finance capital, all bought on the open market and assuming a given degree of technology, with the new firm, a creator of knowledge-based assets, an innovator, learner and continuous improver of products. In this concept the assumption of a given set of intangibles – such as process-technology or marketing

capital – is not merely abandoned. The firm not only organises but also creates intangible assets and exploits networks which give access to other clusters of knowledge assets belonging to its suppliers, to its customers and to universities. For example, a multinational financial-services company like Skandia sees itself as a virtual corporation run by a collection of specialists in knowledge-sharing and co-operation. It has thirty business allies per employee, and a federative structure for staff, allies and customers which is designed to economise working (intellectual) capital compared with a group of subsidiaries.

Indeed, the most valuable resources of organisations remain almost unmeasured. Intellectual capital is the sum of human capital – the abilities of employees – and structural capital, such as trademarks, software and customer databases – all the elements of the firm's capability which

remain when the employees go home. The best practice of enterprises in managing this critical asset is coming under the spotlight only now.5 As a result, what begins to appear is a new set of tools with which investors and other stakeholders can measure and value the performance and prospects of firms whose published accounts are simply a visible illusion, and managers can show the true vield from their stewardship of major assets which are valued at zero in the balance sheet. The interest of government in this revolution arises from the fact that workplace practice in total has so fundamental an influence on pro-

total has so fundamental an influence on productivity, the growth and distribution of income, employment and social cohesion. 'Micro' best practice in the firm can serve the 'macro' objectives of public policy.⁶

Designing Policy in the Dark?

Where are the measures and policy instruments to bring to bear on the characteristic inputs, processes and outputs of knowledge-based firms? Countries routinely produce statistics for macroeconomic policy-making, but far less for structural policies in a semi-borderless economy. Firms cannot be asked for data they do not yet have and may not be able to produce. Measures of changes in competitiveness and productivity from

investment in intangibles are scandalously deficient.

Yet governments require data to operate structural policies in aid of competitiveness. Every chief executive says that the intangible asset most critical to the competitiveness of the firm is human capital. But it does not appear on the balance sheet. Only an uncalculated (and highly variable) fraction of a firm's training costs appears in the profit-and-loss account. Its impact is allegedly exhausted within the accounting year, as is government expenditure on education. Regulators, competition authorities and the investing community are afforded only tantalising, management-controlled and very partial glimpses of the private life of knowledge-based firms.

Information about the success of firms in creating value from knowledge has to accompany reform of business-support structures and other government measures. Dissemination of good practice presupposes its identification and measurement, and an understanding of the limits and most effective means of transferability. If structural policy is to become better informed, coherent and effective, it cannot be based on the bizarre model of the world reflected in company or public accounts. It has to address the currently invisible reality of firms which are primarily creators and exploiters of knowledge. A

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Firms, Knowledge and Competitiveness

vital first step will be the development of an internationally understood language for intangible investments and the establishment of measures which are technically feasible and commercially acceptable to firms. Only then will it be possible to evaluate necessary reforms in policy areas such as competition, regulation, the efficiency of financial markets, innovation and R&D policies, and the reconstruction of the business-support infrastructure into one which is effective in a knowledge-intensive economy.

It is widely accepted that covert, non-tariff protectionism, and pervasive rigidities and distortions, including a European 'social model' which leaves eighteen million unemployed, seriously hamper the functioning of markets in goods and services and factor markets. Severe structural problems and low growth in European, Japanese and American economies make microeconomic reforms difficult but more necessary. They prevent economies from benefiting fully from the growing international division of labour which is both cause and effect of increased globalisation. In particular, protectionism insulates very many firms from precisely those market pressures which cause firms, institutions and governments to innovate. The barriers to further globalisation inhibit the development of the knowledge-intensive firm and full exploitation of human capital.

The role of government in promoting the shift to a more knowledge-intensive, competitive economy is sometimes direct (for example, through provision of initial education) but mostly indirect, by creating conditions which foster technical, commercial and organisational innovation. Policy should thus exhibit ten major characteristics:

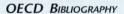
- · increased reliance on structural policy to improve competitiveness
- · more frequent adoption by government or its proxies of the middleman role as a knowledgebroker providing an enabling environment for firms
- · a focus on correcting under-investment in intangibles rather than in tangibles like new factories or machinery
- bold institutional re-engineering which recognises that the efficiency of the market economy

is not primarily the responsibility of the finance function of government but depends on substituting massive and systemic policy co-ordination to bring together the finance and science and technology, employment, education and training and regulatory functions of government

- · the beggar-my-neighbour concept of competitiveness is replaced by a win/win version that combines effective support for the competitiveness of national assets with more international co-operation to foster trade liberalisation - especially in sectors like telecommunications - and foreign direct investment to remove factors that inhibit innovation; in a semi-borderless world action has to be concerted across national borders to enhance the effectiveness of government leverage on the national industrial structures within which most firms still operate
- · fundamental re-assessment of the scope for a better balance between the importance of rewarding innovation, thus encouraging entrepreneurial risk-taking, and the maximisation of social and economic benefits from improved diffusion of innovation
- · competition policy focused on safeguarding competitive forces where the abuse of market power most directly threatens innovation and its social benefits (the creation, distribution and commercialisation of information, for example)
- the updating of skills to avoid the reduction of competitiveness which comes from uncontrolled and rapid obsolescence of people's skills
- · the recognition that the comparative advantage of OECD countries lies in production that is intellectually capital-intensive should lead to policies that encourage organisational innovation, reform of the labour market and more efficient use of human capital (for example, reducing minimum wages to increase hiring and development of young people in the workplace, and reversing the trend to early retirement to improve output per person of working age)
- as a protection from change, but as the ability to change', strong and continuous action to counter

· social policies and institutions which, in Gordon Betcherman's phrase, 'offer security not access-narrowing and polarising effects of the way in which markets for human capital operate and to remedy the increasing inequality of opportunities and of income which accompanies the information revolution and threatens popular acceptance of the rate and extent of social and economic change.

In the public domain, knowledge about the creation, use and competitiveness-value of knowledge assets is highly fragmented and frequently non-existent. That makes the reform agenda for governments more difficult. As industrial economies mutate into finance- and knowledge-based, service-led systems, the characteristics of a complementary almost-new style of government are being worked out piecemeal. It is a style in which policy-making and implementation have to be more open to the creators and users of knowledge, where government will more often be promoter than provider, where policy has to be transparent and consistent across national borders and therefore depends on more collaboration between governments.





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Why Integrated Transport Systems?

Thomas Andersson and Patrick Hasson

The ability of individual countries and the world as a whole to capture the benefits of the globalising economy can be enhanced by an improvement in the organisation of transport systems. There is presently a costly fragmentation of modes of transport – road, sea, rail, air – as well as of transport systems in different countries. The results are three-fold: barriers to transport which has to change mode, economic inefficiency and high social and environmental costs. Among the issues that require urgent consideration are the role of government in transport, regulatory reform and innovative ways of financing transport infrastructure.

he development of transport systems has always been partly demand-led. For example, trends like increasing motorisation in the last century, more use of transport containers in the last 25 years and the ever-rising demand for mobility have all represented a response to the demand for more and better transport facilities.

Transport has likewise proven vital in expanding international trade and generating economic development. Indeed, improvements in the cost-efficiency of transport over the last 200 years have accounted for tremendous leaps in the pace and quantity of trade as well as expansion in economic activity. The development of the clipper ships, for instance, dramatically improved

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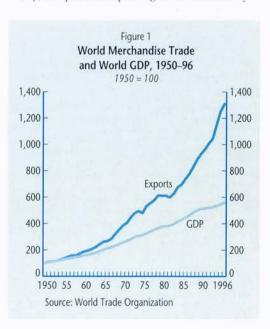
the speed and reliability of transcontinental sea voyages. The invention of the railroad made it possible to move vast quantities of people and goods rapidly overland, thus opening up huge economic opportunities. And the explosive growth of the motor-vehicle and aviation sectors contributed directly to the current focus on globalisation.

Naturally enough, transport systems evolved with an emphasis on individual modes – maritime, road, rail or aviation – forming in turn institutional structures that are still in place. These structures can benefit from specialisation, but also create barriers by isolating policymaking and priority-setting for each mode even when there are distinct benefits to be gained by co-ordinated decision-making. There are now new demands on transport systems, calling for enhanced co-ordination between the

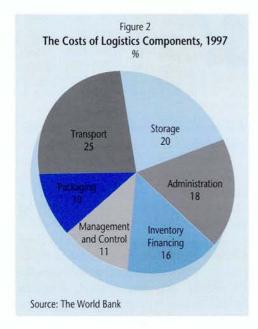
1. World Investment Report 1997, United Nations Conference on Trade and Development, New York and Geneva, 1997. different modes and in the design and management of transport in different countries.

World trade continues to grow faster than world GDP (Figure 1), with the expansion especially rapid between the OECD area and the rest of the world. This growth is paralleled by an even bigger increase in foreign direct investment (FDI), which grew fourfold between 1982 and 1994 – twice as rapidly as gross capital formation. Extensive industrial restructuring underlies this development, which serves to strengthen business responses to demand, to improve the links between research, production and marketing and to locate each activity where it is most effective.

There is increasing pressure on firms to provide more rapid and reliable delivery ('just-in-time', or JIT) and minimise costs for warehousing and other aspects of production and distribution. With the progressive decentralisation of production, both domestically and internationally, companies are pushing for a wider variety



Why Integrated Transport Systems?



of, and more sophisticated options in, transport logistics – managing the flow and storage of raw materials, work in process, finished goods and any associated information from the point of origin to that of final consumption.

The cost of transport is the single largest element in bringing goods to market in the OECD countries (Figure 2).² In addition, although total logistics costs as a percentage of GDP have decreased over time, transport has been absorbing a larger share of them. Moreover, an efficient and reliable transport system usually makes it possible to reduce costs in virtually all other areas. For example, JIT transport can help a manufact-

2. K. Gwilliam, Multimodal Transport Networks and Logistics', OECD Conference on Intermodal Transport Networks and Logistics, Mexico City, 3–5 June 1997; available free of charge from the Transport Division of the OECD Directorate for Science, Technology and Industry.

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4. M. P. Huerta, 'The United States Intermodal Transport Sector', OECD Seminar on Prioritisation of Multimodal Transport Infrastructure, Noordwijk aan Zee, The Netberlands, 12–15 May 1996; available free of charge from the Transport Division of the OECD Directorate for Science, Technology and Industry.

5. Cost 310: Freight Transport Logistics, Commission of the European Community, Brussels, 1993.

6. 'Activities of the Ministry of Transport: Cargo Distribution', Ministry of Transport, Tokyo, 1997 (http:// www.motnet.go.jp/info/cargo.htm). uring company reduce the costs of storage, inventory financing, packaging and administration through a small increase in management and control costs.

But the differences that currently exist between modes of transport and in national regulatory frameworks, administrative procedures and in the assignment of liabilities for cargoes raise transaction and logistics costs considerably. They also impede efficient management and the ability of firms to innovate and capture new opportunities arising from technical progress – with potential benefits for the entire value-added chain.

A Sector in Evolution

Information technologies are central to the improved logistics options now available to companies and are contributing to the emergence of Intelligent Transport Systems (ITS). Applications

such as Geographic Information Systems (GIS) and Global Positioning Systems (GPS) for tracking shipments, and the provision of real-time information on infrastructure and service performance, enables more responsive, efficient, safe and reliable transport. For example, through currently available ITS applications, a truck driver can determine whether or not a chosen route is congested and, if so, which alternative route will be the fastest to his destination. At the same time, with GPS, the business waiting for the product being transported knows exactly where the shipment is and when it will arrive so that they can schedule critical JIT or other processes that depend on the timing of the delivery.

The degree to which well-connected services which switch easily between modes of transport can be developed will be crucial to improved performance. Transport carriers are responding vigorously to the opportunities opened up by technical advances as a means for staying competitive. Whether it is improved container management and facilities in seaports or ITS technologies in freight vehicles, technology is

the means to improved transport efficiency and productivity. The evolution of container trades in the maritime industry - increasing from about 23% of all sea trade in 1980 to approximately 55% in 1995 - indicates the increase in international intermodal shipments (Table).3 The use of maritime containers implies that the land-based transport systems, whether rail or road, are adapted to take containers directly from ships and transport them on the next leg of their journey. As soon as the container leaves the ship and is placed on a truck or rail car, an intermodal movement has been made. Equally revealing is the increase of road-rail ('piggy-back') transport in the United States (roughly a 75% increase over 10 years),4 Europe (about 150% increase over 10 years),5 and Japan (nearly a 500% increase over 5 years)6 (Figure 3).

These figures show how technological developments are allowing transport equipment to be adapted for use in other modes in order to facilitate movement, which in turn provides new options for shippers and generates further use

Table
The Evolution of Container Trade, 1980–95

	1980	1985	1990	1995*
Total miscellaneous goods trade (million tonnes)	527	552	673	740
Containerised goods: million tonnes %	120 23	172 31	269 40	408 55

a. estimated. Source: OECD

of intermodal transport. The growth in the use of stackable maritime containers, for instance, has forced rail and trucking companies to adapt their equipment to carry these containers. Their use, moreover, is creating opportunities for strategic alliances and partnerships between rail and maritime freight companies. And the use of lighter-weight, non-stackable land containers by trucks follows a general trend to larger and heavier truck loads and the adaptation of rail

stock to handle the containers. The continued emergence of such intermodal options will be a major factor in the development of transport systems.

Meanwhile, economic, technological and environmental issues have become more deeply intertwined. Nearly a third of the energy consumed in OECD countries is for transport⁷ and road transport alone burns up some 50% of petroleum products. Separate modal systems, operating in isolation, cannot produce effective energy savings in transport as a whole. Tackling such issues as air quality, noise, water pollution, the handling of hazardous materials and emergency responses requires an approach that reaches across different modes of transport. Such approaches can ensure that when a demand is placed on one mode - for example, congestion on the roads creating environmental and energy problems - the others can fairly readily adapt to relieve it. That, too, will push towards intermodal

The present framework of infrastructural policies, regulations and the management of operations broadly limited to the requirements of individual modes produces a number of barriers to comprehensive and efficient development and operation of transport systems. Naturally, different transport modes are not perfect substitutes for one another, since each has distinct advantages over others, according to the type of cargo, the distance to be travelled, the location of the pick-up and drop-off sites, the degree of traffic congestion, the medium of transport (over water or land), the existence or lack of infrastructure, the quality of the infrastructure (how well it is maintained, for example) and taxes and prices for using it, and many other factors. In essence, any feature that affects either the 'price utility' or 'time utility' of a product can influence the use or avoidance of a particular means of transport.

One factor that can seriously distort transport use is the discrepancy between private and social costs. It has been estimated that, at current market

7. Energy Balances of OECD Countries: 1993–1994, IEA/OECD Publications, Paris, 1996.

8. Economic Benefits of Intermodal Transport: Examples from Europe, NEA Transport Research and Training, Rijswik, 1997.

prices, the break-even point between road and intermodal transport in Europe is about 1,000 kilometres, that is, only for traffic beyond this distance does it pay to shift from unimodal transport by truck to intermodal transport.⁸ But when other costs – external impacts on the environment and accidents – are taken into account, the break-even point is reduced to about 500 km.

Different modes of transport can no longer be evaluated against one another in a marginal fashion whereby intermodal concerns are considered only as a matter of convenience or when there is overwhelming pressure to include an intermodal option in the evaluation process. The evolution of world trade over the past two decades, as well as mounting environmental and social concerns in response to transport impacts, require an approach to planning, building, designing and operating a transport system that emphasises the optimal use of, and connections between, individual transport modes. Such an approach should encompass a range of crosscutting issues that are affecting various facets of life in the modern world. The ability of countries to allow for sustainable transport systems which are efficient, flexible, rapid, secure and consistent with those of neighbouring countries

Figure 3 Increase in Road-rail ('Piggy-back') Transport, 1980-93 500 500 450 450 lapan 400 400 1987-92 Europe 350 350 1980-90 300 300 **United States** 250 250 200 200 150 150 100 100 50 50 Sources: Ministry of Transport, Japan; Department of Transportation, United States; Commission of the European Communities

will have enormous implications for their ability to attract or maintain business, for consumers to obtain affordable products, to meet the demands of a burgeoning tourist industry, and for preserving the environment.

Planting the Seeds of Change

Intermodal transport has arisen as a result of customer demands for more efficient, rapid and reliable deliveries: competition in the supply of transport is increasingly globalised and is growing fiercer. Transport providers are adapting transport infrastructure and stock to make more use of intermodal services. Businesses are also changing, to take advantage of the efficiencies and cost savings inherent in improved transport systems by adopting JIT, advanced logistics management and other practices. The success of intermodal transport therefore hinges on a high degree of flexibility and responsiveness to market conditions. Its further development will depend on regulatory reform that can allow for more compatibility between modes and countries and thus more transparency in policy- and decisionmaking. This, coupled with improved transport pricing will contribute to more rapid adoption of new technologies, market entry by new competitors, less restricted (and thus more rational) choices by carriers, quicker adjustments of prices to maintain competitiveness, and more freedom in the forms of ownership and operation of multimodal transport companies.

Financing the maintenance and further development of transport systems is moving away from almost total reliance on public budgets, largely because deficits and the increasing mobility of tax bases have made it more difficult for governments to mobilise the resources required. And with private investment comes the additional advantage of increasing customer influence on transport infrastructure. This brings more pressures for solutions in transport as a whole rather than within individual modes, thus raising the prospects for effective investment.

But there are practical barriers to comprehensive investment and involvement by the private

Why Integrated Transport Systems?



The expansion of road-rail transport over the past few years has been spectacular in Europe, the United States and Japan alike.

sector. Transport systems continue to be plagued by extensive subsidisation that is provided to some modes but not to others, regardless of social benefits, and particularly when some modes are owned and operated by the public sector and other, competing, ones by the private sector. In the United States, for example, the road system is almost entirely in the public sector and the rail system is almost entirely in the private sector. In Europe, subsidisation and protection of rail services by the public sector inhibits the expansion of rail freight services and encourages the use of road transport. Still, the current trend is towards privatisation in more or less all means of transport, which is no longer viewed as simply a support to commercial enterprises - the supply of transport facilities is now a fully fledged commercial enterprise itself. Policies in the transport sector are therefore evolving to release market opportunities by promoting private ownership of infrastructure and privatisation of most transport services. The success of such policies will be measured by the benefits derived, including their capacity to increase transport choices that are governed by true cost rather than the extent of subsidy.

As privatisation progresses, governments retain a responsibility for the negative externalities of transport, such as its adverse impact on the environment and safety. Other goals that the

government deems important (emergency response, for instance, or meeting the basic mobility and access requirements of some regions or segments of society) could be marginalised. An adequate balance between public and private funding, coupled with a proper mixture of complementary means, is therefore required to allow market forces to optimise transport systems while still providing to the entire population a guarantee, through public or private means, for the provision of such central services as emergency medical care, access to schools and public transport. Under all circumstances, however, fostering competition and innovation is required to stimulate efficiency and improved use of public as well as private funds.

Furthermore, private-sector requirements for higher-quality service is a driving force for improved intermodal infrastructure and services that can contribute to lower production and other costs. Government has been responding in a concrete fashion. In 1991, the United States introduced the Intermodal Surface Transportation Efficiency Act; in 1996 the Netherlands issued a memorandum entitled *Transport in the Balance* which establishes an intermodal policy to ensure a balance between high growth in goods transport and environmental protection; and last year the European Commission published a 'communication' on *Intermodality and Intermodal*

Freight Transport in the European Union, which is the first step in developing a framework for an optimal integration of different modes so as to enable an efficient and cost effective use of the transport system.10 Likewise, the United Nations¹¹ and the European Conference of Ministers of Transport have adopted intermodal frameworks for their work programmes. A newly formed Transport Division in the OECD Directorate for Science, Technology and Industry is consolidating research in road transport, maritime transport and shipbuilding, as well as in transport issues associated with tourism. All of these initiatives are indicative of a new commitment to seek solutions to transport problems in a broader context.

The reform of transport policy and institutions must take account of the movement away from isolated, individual modes towards a cohesive and unified framework for transport systems. The specific elements of reform will depend on cultural, political and performance conditions that vary from country to country. Nonetheless, countries will be obliged to move in concert with one another. Sharing experiences on 'best practices' could lead to improvements in the following areas:

- the establishment of a regulatory and institutional framework more conducive to innovation and technology diffusion
- · funding strategies and initiatives
- transparency in government decision- and policy-making processes
- consistency in international rules and regulations governing transport ownership and operation, so as to facilitate an open and competitive environment for efficient global transport
- research and education on the importance of a systems approach to decision-making in transport, covering the range of economic, technical and environmental issues

^{9.} Ministry of Transport, Public Works and Water Management, The Hague, 1997.

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^{11.} Multimodal Transport Handbook, United Nations Conference on Trade and Development, New York and Geneva, 1996

The Professional Development of Teachers

John Walshe

In-service training is taken for granted in professions such as engineering and medicine. It is assumed that doctors and engineers will acknowledge their responsibilities and thus take time out to brush-up on their skills and acquaint themselves with the latest advances in their disciplines. Yet in most OECD countries no such assumption is made about teachers. Fewer resources are committed to their development than those allocated to other professions. The short in-service courses that are available are all too often given in isolation.¹

eacher-training is not generally designed with the longer term in mind; it is not anchored in the classroom; and it is not geared to meet the shortcomings perceived by policy-makers. These challenges have to be met, particularly as economic globalisation is making the ability to adapt more urgent. Increased competition between, and integration of, the world's economies put pressure on countries to raise skills through education and training institutions.

1. Staying Abead: In-Service Training and Teacher Professional Development. CERI/OECD Publications, Paris, forthcoming 1998. The series in which it appears, What Works in Innovation in Education', publishes empirical studies which offer a focused, policy-oriented assessment of important innovative practices. Earlier titles in the series are School: A Matter of Choice. 1994. Schools under Scrutiny, 1995; Mapping the Future, 1996: Young People and Career Guidance, 1996: Parents as Partners in Schooling, 1997.

Simultaneously, increasing participation rates in upper-secondary school and in higher education are calling for apposite programmes for a broader intake of students.

Yet while globalisation puts every country under pressure to remedy perceived shortfalls in educational performance, not least in maths and science, it does not always stimulate change in a common direction. Some countries, such as the United States and the United Kingdom, believe that their education systems have not been able to maintain high-enough standards, with the result that many young adults leave

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• better data on domestic and international trends in intermodal transport development and use

 new partnerships and working relationships including those that cross modal barriers, that are government-wide and include the private sector.

Addressing transport issues through international co-operation at the OECD has proven effective in meeting the research requirements of member countries. But now a balance has to be established between consolidating existing approaches and formulating altogether new strategies to overcome prevailing obstacles. The OECD, like other institutions, used to view transport issues mode by mode through an organisational approach that encouraged a compartmentalised perspective. The Organisation will now improve its work on issues related to integrated transport, including regulatory reform. In fact, this attention will also enhance single-mode activities, but from the perspective of overall system efficiency. For example, horizontal cooperation between different transport and transport-related divisions will be stimulated by addressing road transport and its intermodal linkages in a wider economic, social and institutional context. Through this type of approach, the OECD can inspire structural improvements in areas where its member countries are confronted with obstacles to capturing the benefits of globalisation.

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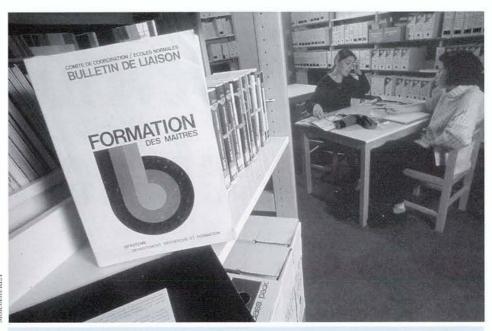
The Professional Development of Teachers

school without the basic skills one might expect them to have acquired. Others, such as Japan, judge that even though their students obtain good results they are being taught too rigidly and thus lack the creativity and flexibility desired in modern economies. The result is that different countries are trying to change the culture of teaching in more or less opposite directions.

Change - such as the dramatically changing employment market, the drug culture and concern about child abuse - has made it impossible for schools to address children's intellectual development without also considering their social requirements. Schools now pay more attention to the supply of career guidance and many countries are introducing programmes designed to increase awareness of abuse and the dangers of illicit drugs. Schools are also providing a wider variety of courses, especially in upper secondary. One reason is that relatively high degrees of achievement are being sought from children who come from a wider range of social backgrounds than in the past, when only an 'academic' and privileged minority was expected to do well at school. Many countries have found that simply opening-up to people from all social backgrounds, without enough adaptation of the curriculum or teaching styles, has led to high failure

Concomitantly, the decline of strong stabilising factors such as the nuclear family and full employment, and the rise of some destabilising ones, such as unemployment and single-parent families, have had important influences on the background of children at school. There is a growing recognition in both policy and practice that teaching strategies have to be sensitive to social contexts and that schools should work in partnership with parents or guardians and others outside education.²

It is now generally agreed that traditional methods of teaching – where there is no scope for activity learning by students – are inadequate to assure the educational performance that globalisation will demand and that, instead, students have to be actively involved in the learning process and their individual approaches accommodated. Information and communication technologies (ICTs) offer exciting opportunities



The most costly aspect of in-service training is the replacement of absent teachers.

for change in teaching styles. Students and teachers can use the Internet to gain access to information much quicker than in the past. ICTs and the use of e-mail facilities can also help ease the sense of isolation of many schools in sparsely populated rural areas. But the provision of ICTs to schools is by no means guaranteed to affect the culture of teaching automatically: teachers, especially older ones who are uncomfortable with the new technologies, will require training.

All of these factors influence and re-enforce the determination of politicians and other policymakers to introduce reforms in order to:

- · raise standards
- make the schooling process more 'relevant' to the diverse requirements of students
- · alleviate educational disadvantage
- combat social exclusion
- equalise opportunities between males and females

2. Co-operation between the School and the Family, CERI/OECD Publications, Paris, 1997; Successful Services for Our Children and Families at Risk, OECD Publications, Paris, 1996; Peter Evans, 'Co-ordinating Services for Children at Risk,' The OECD Observer, No. 202, October/November 1996.

3. N. K. Shimabara, 'Teacher Education Reform in Japan: Ideological and Control Issues' in N. K. Shimabara and I. Holowinsky (eds.), Teacher Education in Industrialized Countries, Garland, New York, 1995.

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- give parents a bigger say in the governance of schools
- decentralise some decision-making.

Pre-service training no longer provides – if it ever did – the tools and skills necessary to meet these rising expectations. It has to be supplemented with in-service training – which is not simply an 'add-on' to be applied when a particular problem arises. It has to form part of an approach to professional development which allows teachers to become 'reflective practitioners' in their classrooms.

What Works?

The Centre for Educational Research and Innovation (CERI) at the OECD has examined policy and practice in the in-service training and professional development of teachers in eight OECD countries: Germany, Ireland, Japan, Luxembourg, Sweden, Switzerland, the United Kingdom (England and Wales) and the United States. These countries have very different cultures, educational traditions and administrative structures, which will make it easier to perceive common advances that are bearing fruit

and to draw out the policy implications on how these innovations might be built on and practice improved.

The manner in which practising teachers learn depends on many factors. There are national traditions and institutions; and education systems can be 'steered' by politicians. Attitudes to teacher-training are also influenced by the character and status of the profession, by opinions about curriculum and pedagogy and by political and administrative relationships as between those who shape and implement policy in the education system.

In-service training and professional development ought to be a collaborative effort from start to finish, involving the policy-makers, providers and teachers, but the reality often falls far short of that ideal. The reasons for particular initiatives in in-service provision are not always clear, nor are the objectives and aspirations of the decision-makers. As a result, it is sometimes unclear in advance what the course is supposed to offer, nor is the most appropriate mode of delivery always chosen. In short, many in-service programmes achieve very little.

In-service training can take many forms. Provision can range from courses of the 'short-burst' variety to longer, 'whole-school' programmes run in co-operation with universities or other institutions of higher education. In Japan, for instance, there are networks of teachers who have developed numerous self-initiated, voluntary associations to promote teaching as an alternative to government-sponsored courses.3 Japanese teachers also go on placement in various businesses, including hotels, where they learn the importance of a customer-focused approach by joining the normal training programmes alongside the firm's own employees, a practice that can give them valuable insights not only into how business perceives its own customers but also its views on the schooling process.

The choice of environment for learning depends to a large degree on the nature and aims of the course in question. Courses to update subject knowledge can often be most easily delivered in university institutions. But efforts to change the ways in which teachers think and the style in which they work have to be based more around the school. External courses can give an understanding of new approaches but not the authority to practise or disseminate them in their everyday work. Teacher development does not require simply that individual teachers learn how to do things differently; groups of teachers also have to agree to do things differently.

Time and Money

The amount of resources invested by governments in in-service teacher-training varies enormously and is hard to quantify. Few countries match the generosity of Israel, where teachers are allowed to take a sabbatical every seven years during which they receive two-thirds of their salary with the option of teaching parttime to make up the remainder. The most expensive aspect of in-service training is not the training itself but the provision of substitute cover for absent teachers, and different countries have different policies on substitution. In Ireland and Germany, for instance, very little use is made of substitute teachers. The result can be either reduced learning time for students or extra duty for colleagues who are expected to 'double-up' for those who are absent. A third option,

increasingly used in Sweden, is to expect teachers to take at least some courses during the summer holidays – a solution which is not always possible in other countries because of opposition from teachers' unions.

Private investment is also beginning to play a role. Teachers are paying fees to attend courses. School-owners are initiating programmes, particularly in management-training for their own senior staff, and business is investing in development activities. As well as Japan, other countries such as Switzerland also offer placement for teachers to give them an insight into business practices and indicate what lessons teachers can bring back to the classroom. And commercial companies are putting resources directly into schools. In the United Kingdom and Ireland, for instance, the education ministries are actively encouraging computer firms to join in local partnerships to help increase the investment in hardware and software in schools. As a rule, these various types of private investment are harder to measure than that of governments and is more varied from country to country.

In the United States the business sector has long taken a direct interest in what happens in schools. Its involvement with educators, researchers, state and district leaders and others in a coalition of concerned groups and individuals resulted in the establishment of the National Commission on Teaching and America's Future in 1994. From the Commission and similar organisations, such as the National Board for Professional Teaching Standards, have emerged proposals for far-reaching reform that are having a direct impact on teachers' professional development. New learning goals have been defined



Information technologies could have a dramatic effect on teaching styles.



Initial training will not equip teachers for the new social context of mass education.

but there is concern over the capacity of US schools to respond to alternative practices, especially those involving increased interaction among teachers, such as providing them with the opportunity to explore and evaluate their own work, carry out peer review, mentoring and so on.

How effective is this investment of time and money? It is very hard to say. In only a few countries are the outcomes evaluated in a rigorous manner. Elsewhere, evaluation appears to be limited and the results poorly disseminated so that models of best practice are not readily available to policy-makers or to practitioners, even domestically.

Ten Policy Principles

It is difficult to give detailed policy proposals, applicable to a wide variety of countries tackling a vast array of issues of educational development. Analysis of the countries examined by the OECD nonetheless suggests ten principles worthy of consideration:

- systematic studies to identify shortcomings in in-service provision would bring more clarity to the discussions and decisions about what is expected from particular initiatives
- a balance should be maintained between the goals of system-wide policy objectives with the importance of teachers' maintaining a sense of 'ownership' over their learning
- school-focused development should not be insular or introspective – contacts with higher

education, with teachers in other schools and with outside organisations and groups, for example, should create opportunities for teachers to reflect on their teaching objectives, strategies and development

- with the support of people from outside the education system, teachers should strive to develop new ways of thinking and behaving that address new challenges in fresh ways placement in private business has been seen to help teachers look again at their teaching practice
- teacher-development should be balanced between out-of-school learning, classroom practice and collegiate discussion on site, and all three elements should be co-ordinated
- in partnership with their immediate managers, teachers should take individual responsibility for ensuring the different aspects of their development as part of a coherent whole
- teachers, schools and educational authorities should all make a contribution, in both time or money, to the process of development, so as to create a common investment
- central government should take some responsibility for maintaining, regulating or certifying an adequate supply of external courses of recognised quality
- teacher development should be oriented towards fostering a culture of lifelong learning, rather than focusing solely on subject knowledge or particular aspects of pedagogic techniques
- there should be more systematic evaluation, not relying solely on questionnaires filled in by teachers, but also using other techniques such as observation, video-recording, qualitative surveys and follow-up studies of programmes in

the classroom with the focus on student outcomes.

There is no question that evaluation is difficult, but that should not be used as an excuse for failing to attempt to learn how successful, or otherwise, particular courses or initiatives are. It is difficult to justify the use of taxpayers' money when one has little idea whether it is being spent effectively.

Parents, like politicians and other policy-makers, are no longer content with simply broadening access to education – they are also concerned with its quality. In-service training and professional development, which are essential if these goals are to be achieved, then become much more than a personal matter for each individual teacher. They should be seen as an integral part of change that is sweeping through education systems, based around the creation of new, dynamic strategies in schools themselves.

Simply investing more resources into inservice courses will not necessarily improve the results for students unless that investment is accompanied by the formulation of coherent, comprehensive and consistent policies for teachers too.

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What Agricultural Policies for Tomorrow?

Carmel Cahill and Wayne Jones

The agriculture ministers of the OECD countries met in March to discuss progress on policy reform – six years after their last ministerial meeting, during which time OECD membership has expanded to include Mexico, the Czech Republic, Hungary, Poland and then Korea, and ten years since the OECD Ministerial Council formulated the principles and actions for agricultural policy reform and committed OECD countries to their implementation. How have they held the course?

ver the past decade much progress has been made in implementing the reform of agricultural policy. The Uruguay Round Agreement on Agriculture has been put in place. The North America Free Trade Area (NAFTA) has been formed and the EU has been enlarged. Domestic agricultural policies have also evolved. The market itself, especially for cereals, has improved substantially. Growth in south-east Asia and elsewhere has generated substantial increases in agricultural trade, much of which is in processed agricultural products.

And the world itself has changed. The countries of central and eastern Europe and the ex-Soviet Union have moved to market-based economic systems. Globalisation and new technologies are transforming the agro-food sectors of OECD and non-OECD economies alike.

With change on this scale, the time was right to try to forge a common view among the OECD

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countries on the kinds of policies that can advance the reform process and respond to the changing expectations of the role of the agricultural sector, expectations that go beyond the basic provision of food and fibres, to encompass the environment, amenities and rural development and that place increasing demands in terms of food quality, variety and safety. That was the aim of the meeting held at the OECD in March.

To begin with, the ministers reviewed the progress made in reform and then explored the issues likely to arise in the years ahead. Among the outcomes of the meeting was agreement on a set of shared goals for the agricultural sector (box, p. 37), comprehensive policy principles and an outline of the operational characteristics of the kinds of policies most likely to lead to the achievement of those goals (box, p. 38).

Progress to Date?

There was general agreement on the achievements of policy reform and that it should be continued: subsidies and protection are still high. Although support to agriculture in the OECD area

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(as measured by the Producer Subsidy Equivalent – PSE²) has indeed fallen – from an average of 45% of the value of production over the period 1986–88 to 35% in 1997 – the amount of total transfers (\$280 billion) is still substantial. And much of it continues to distort production and consumption and raise prices to consumers because it is paid per tonne of production or linked to land or other agricultural inputs.

Australia, Canada, New Zealand and the United States have carried out sustained reform of their agricultural policies, involving reductions in assistance and deregulation.³ In the European Union, reform has started to move support away from market-price support towards direct payments, with some degree of decoupling from production but with a relatively small reduction in the volume of support (Figure, p. 37). Japan, Norway and Switzerland have also begun to change the way in which support is delivered and have reduced its volume, though their rate of support remains among the highest in the OECD area. The degree of support and protection in the five new member countries is (with the exception of Korea) well below the OECD average. In the three central-European member countries, where wholesale reform of the agricultural sectors has proceeded apace with wider economic reforms, the degrees of support and protection are generally low. And Mexico undertook widespread reform and overhaul of its policy instruments as part of its entry into NAFTA.4

1. Agricultural Policy Reform: Stocktaking of Achievements and Agricultural Policy: The Need for Further Reform, available free of charge from the Country Studies I and Structural Adjustment Division of the OECD Directorate for Food, Agriculture and Fisheries.

2. See note 1 in the Figure, p. 37.

3. Paul E. Atkinson, 'New Zealand's Radical Reforms', The OECD Observer, No. 205, April/May 1997.

4. Gérard Bonnis and Wilfrid Legg, 'The Opening of Mexican Agriculture', 'The OECD Observer, No. 206, June/July 1997; Denis Besnainou and Laurent Davezies, Regional Policy in Mexico', 'The OECD Observer, No. 210, February/March 1998.

What Agricultural Policies for Tomorrow?



Agriculture is no longer the sole determinant of the economic health of rural areas.

One of the most important events affecting agriculture in the last ten years was the conclusion of the Uruguay Round in 1994, not simply the agreement on agriculture itself but also the Agreement on Sanitary and Phytosanitary Measures and the new mechanism for resolving disputes. Access to foreign markets and the degree of domestic support and export subsidies are now all subject to a series of binding disciplines which, even if their impact to date has not been enormous in practical terms, have transformed the domestic and international context in which agricultural policy is designed and implemented. Indeed, countries have been making a genuine effort to design new policy measures in conformity with the 'green box' requirement of minimal or no distortion of production or trade.

But the reform of agricultural policy concerns not only traditional forms of support and protection. At their OECD meeting the ministers also examined achievements in the environment and rural development. And indeed, much more attention is being paid to environmental measures in the design of agricultural policy and to using agricultural policy to achieve environmental objectives; the environmental performance of the sector is improving accordingly. Traditional production-based agricultural policies are having a declining impact on rural economies, but policy reform, by paving the way for viable, efficient agricultural practices, can enhance the sector's contribution to rural development.

Domestic Developments

A wider range of objectives now has to be accommodated under the umbrella of agricultural policy, and more interests are involved. The entire agro-food sector, and not solely its farm component, has to be taken into account when designing and implementing policies. Structural change – bigger farms and the pursuit by farm

households of non-farming sources of income and growing concentration and integration among the different elements in the food chain have all changed the emphasis in policy. The generalised provision of income-support to a sector where relatively low incomes were once endemic is no longer the main aim of policy. More attention is being paid to the development of instruments to manage risk, in view of the possibility of increased price and income volatility in a more market-oriented sector, where intervention and protection are no longer axiomatic, and where incomes are on average much healthier. It is increasingly acknowledged that agriculture alone cannot ensure the economic viability of rural areas and intense efforts are being made to develop policies that reflect this new reality.6

As a result of the Bovine Spongiform Encephalopathy (BSE) crisis in Great Britain and outbreaks of food-borne diseases in several other countries, combined with debate about genetically modified organisms and other factors, consumers are becoming ever more demanding about the quality and safety of the agricultural products being offered to them and are also increasingly concerned about the processes by which food is produced.7 There is likewise much insistence from the public that damage to the environment from agriculture be reduced, that the sector provide a range of environmental benefits and that its productive activity should be carried out sustainably. Macro-economic difficulties, especially the pressure for fiscal restraint, are intensifying the scrutiny of government spending. And the progressive shift that is occurring in support away from measures financed by consumers through higher prices to direct payments paid for by taxpayers - has brought these issues under the spotlight. The result is a growing demand for information about and evaluation of the distributional impacts.

International Concerns

The resumption of multilateral negotiations on agricultural trade, to be launched under the

Wilfrid Legg and Micbel Potier, 'Reconciling Agriculture and the Environment', The OECD Observer, No. 210, February/March 1998.

^{6.} Heino von Meyer, 'The Insights of Territorial Indicators', The OECD Observer, No. 210, February/March 1998.

^{7.} Reza Labidji, 'The Agro-food Sector in the 21st Century', The OECD Observer, No. 210, February/March 1998.

David Blandford and Gérard Viatte, 'Ensuring Global Food Security', The OECD Observer, No. 203, December 1996/January 1997.

auspices of the WTO before the end of 1999, is viewed in differing lights. Some countries see it as an opportunity to build on the foundations of the Uruguay Round, continuing the integration of the agricultural sector into the multilateral trading system. Others regard the approaching negotiations with some foreboding, anxious that their agricultural sectors might find it difficult to adapt or that their rural areas might find longerterm viability difficult with a diminishing economic contribution from agriculture.

The OECD agriculture ministers were unanimous in their determination to achieve improved food security world-wide through the actions agreed at the World Food Summit held in Rome in 1996 under the auspices of the FAO8 - although some OECD countries, such as Japan and Korea, already heavily dependent on food imports, expressed an anxiety about food security if their dependence on imports increases apace with the liberalisation of agricultural trade.

A vigorous debate is currently underway on the relationship between 'multifunctionality' and the continuing process of domestic reform and the liberalisation of agricultural trade. 'Multifunctionality' has come to be used in some countries, especially in Europe and Japan, as shorthand for the notion that the agricultural sector fulfils many roles in the economy beyond the primary one of producing food and fibres.

> Environmental qualities such as landscape and leisure facilities, thriving rural economies, the continued occupation of areas that might otherwise be denuded of their populations are some of the facets of 'multifunctionality'. Some advocates even go so far as to claim that the traditional modes of social organisation and culture, such as closer family ties. associated with agricultural and rural life form part of the 'multifunctionality' of the sector.

> Many of the politicians and civil servants involved in the design and implementation of agricultural policies believe that the reform of domestic policy towards reduced support and the liberalisation of trade are essentially inimical to the ability of agricultural activities to achieve



Shared Goals

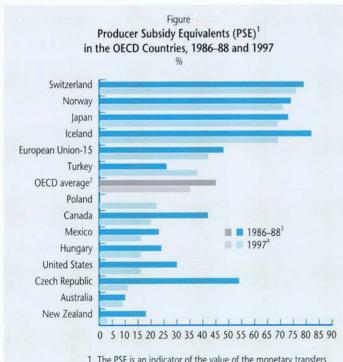
The OECD agriculture ministers agreed that governments should provide the appropriate framework to ensure that the agrofood sector:

- · is responsive to market signals
- · is efficient, sustainable, viable and innovative, so as to provide opportunities to improve standards of living for producers
- · is further integrated into the multilateral trading system
- · provides consumers with access to adequate and reliable supplies of food which meets their concerns, in particular with regard to safety and quality
- · contributes to the sustainable management of natural resources and the quality of the environment
- · contributes to the socio-economic development of rural areas, including the generation of employment opportunities through its multifunctional characteristics, the policies for which must be transparent
- · contributes to food security at the national and global levels.

these multiple goals. In fact, a crucial feature of reform - as defined by the 1987 principles and already implemented in a number of OECD countries - precisely involves moving away from generalised programmes of price support towards carefully targeted measures designed to meet just such specific objectives.

Many of these objectives are environmental in nature, or seek to support a more general process of rural development and structural adjustment and respond directly to concerns about 'multifunctionality'. The ministers' meeting provided them with an opportunity to discuss this issue thoroughly, and they left Paris confident that the pursuit of multifunctionality was inherently compatible with continuing reform and, indeed, that one could be harnessed in support of the other. The OECD itself will nonetheless have to clarify these complex ideas so as to ease the path towards continued reform and liberalisation.

There are important international aspects to the questions of food safety evoked by the



- 1. The PSE is an indicator of the value of the monetary transfers to agriculture resulting from agricultural policies. Both transfers from consumers of agricultural products (through domestic market prices) and transfers from taxpayers (through budgetary or tax expenditures) are included. The percentage PSE is the value of transfers as a percentage of the value of production. 2. Excludes the Czech Republic, Hungary, Korea, Mexico
- 3. 1989-91 average for the Czech Republic, Hungary, Mexico and Poland (% PSE = 0)
- 4. Estimates.

What Agricultural Policies for Tomorrow?

FOR THE RECORD

Policy Principles

Ministers adopted a set of policy principles as follows:

• reaffirm the support for Article 20 of the Uruguay Round Agreement on Agriculture* and the commitment to undertake further negotiations as foreseen in that Article and to the long-term goal of domestic and international policy reform to allow for more influence of market signals:

*'Recognising that the long-term objective of substantial progressive reductions in support and protection resulting in fundamental reform is an ongoing process, members agree that negotiations for continuing the process will be intiated one year before the end of the implementation period, taking into account:

- the experience to that date from implementing the reduction commitments

 the effects of the reduction commitments on world trade in agriculture

 non-trade concerns, special and differential treatment to developing country members, and the objective to establish a fair and market-oriented agricultural trading system, and the other objectives and concerns mentioned in the preamble to this Agreement

 - what further commitments are necessary to achieve the above mentioned long-term objectives.'

 address the problem of additional trade barriers, emerging trade issues and discipline on export restrictions and export credits

• strengthen world food security, in particular through the actions agreed in the Rome Declaration and Plan of Action of the 1996 World Food Summit

 promote innovative policies that facilitate responsiveness to market conditions by agricultural producers • facilitate improvement in the structures in the agricultural and agro-food sectors, taking into account the needs of farmers affected, in particular those in disadvantaged regions

• enhance the contribution of the agro-food sector to the viability of the rural economy through, for example, efficient and well-targeted agricultural policy measures, facilitating the mobility of labour, new market opportunities, alternative uses of land (both within and outside agriculture), and the provision of rural amenities

• take actions to ensure the protection of the environment and sustainable management of natural resources in agriculture by encouraging good farming practices, and create the conditions so that farmers take both environmental costs and benefits from agriculture into account in their decisions

• take account of consumer concerns by improving the effectiveness and reliability of food safety regulations, strengthening standards on origin and quality, and improving the content and availability of information to consumers, within the framework of international rules

• encourage increased innovation, economic efficiency and sustainability of agro-food systems through, inter alia, appropriate public and private research and development efforts, respect for the protection of intellectual property, and improvements in public infrastructures, information, advice and training

 preserve and strengthen the multifunctional role of agriculture in order to combat territorial imbalances, to encourage the sustainable management of natural resources and to favour diverse farm development strategies. problems and opportunities facing the agro-food sector in the coming years, the agricultural ministers who met at the OECD in March were able to agree to a progressive and attainable set of shared goals and to make policy recommendations on how to achieve them. And without exception, they were able to assert their confidence in the ability of the sector to bring an ever-growing range of high-quality products to the consumer's table, to be increasingly responsive to market signals, and more and more ready to claim a full place as an innovative, growing, modern sector within the modern, global economy.



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meeting. Can consumer worries about safe food be answered in ways that do not unnecessarily put a brake on trade liberalisation? Are the international institutions charged with developing and implementing standards and guidelines adequate for the difficult tasks they face?

Such issues are very difficult to resolve, particularly where consumers are confused by the insufficient or sometimes conflicting advice given by scientists. Answers to these questions that also support the international trading system will obviously be the most economically efficient. There are a number of international institutions working on food-safety questions, such as the Codex Alimentarius and the International Office of Epizootics. And international mechanisms can be developed to nip problems in the bud – before they become the object of trade disputes.

In spite of the inevitable lively disagreement on a number of issues that go to the core of the Spotlight

Romania Macro-economic Stabilisation and Structural Reform

Maitland MacFarlan and Joaquim Oliveira Martins

he complementarity between macroeconomic and structural policies is widely recognised. Yet it is often neglected when macro-economic indicators head in the right direction. With high growth rates of GDP, it is not always easy to focus on structural weaknesses and question whether the policies intended to sustain macro-economic stabilisation are well judged. Coherent design, both of macro- and microeconomic policy, is particularly relevant for countries making the transition from central planning to a market economy in view of the large economic dead weight inherited from the previous structures. The tortuous story of Romania between 1989 and 1997 illustrates the importance of these links in a particularly striking way.1

At the outset of transition Romania was, in many respects, in a more difficult position than most of the other countries in central and eastern Europe. In the early 1990s, the room for manœuvre for structural reforms seemed limited, particularly given the difficult social conditions of the previous decade. Indeed, during the 1980s, the population had had to pay for the quick reimbursement of a sizable foreign debt and some public-construction projects on a pharaonic scale. The 'People's Palace' in Bucharest is a notable example. The pressure on already low disposable incomes meant a contraction of household

consumption. The emphasis of the Ceaucescu regime on economic self-dependence led to the accumulation of a technological lag and put excessive focus on heavy industry. This led to the depletion of domestic energy sources, inducing shortages and subsequently costly dependence on imports of energy and raw materials.

This difficult legacy argued in favour of a gradualist approach, seeking to minimise the social costs associated with the transformation to a market economy. Although these social concerns were understandable, the strategy was illconceived and failed to produce sustainable gains in either economic or social conditions. The experience of the first seven years of transition suggests that the costs of a gradual strategy have probably been higher than if a bolder approach to structural transformation had been adopted. In 1993, the OECD pointed out clearly the risks that arised from delaying structural reforms.2 In particular, if loss-making industrial and agricultural enterprises were artificially maintained through state subsidies and easy access to credits, both fiscal and monetary policy would be

The importance of the links between macroeconomic and structural policy was disguised for a while by the boost in exports and resumption of growth in 1993, and the apparent success in reducing inflation under the stabilisation policy of 1994. But the export performance of 1993–94 was to a large extent based on unrestructured heavy industry and could not be sustained without massive imports of energy and raw materials that led to a progressive deterioration in the external position. In 1995 the growth rate of GDP peaked at 7.1%, but the sizable increase in the current-account deficit (Figure, p. 42) resulted in a fall in confidence in the currency. In November of that year, the authorities were forced to accept a sharp depreciation in the official exchange rate.

In 1996, output continued to grow at around 4%, apparently suggesting that the exchange crisis had had only a moderate impact. But during the year macro-economic conditions progressively deteriorated. The official budget deficit almost doubled over the 1995 figure, at a substantial 5.8% of GDP. In fact, when 'quasi-fiscal' items are included, such as the National Bank refinancing of credits to the agricultural sector and other indirect subsidies, the overall deficit exceeded 10% of GDP. This serious slippage was mainly the result of pervasive lack of financial discipline in large state-owned companies, aggravated by the populist policies adopted during the election campaign that boosted incomes and expenditures. The public deficits were financed mostly by printing money, with the predictable result that at end-1996 inflation accelerated to 57%. The overall approach to economic policy was clearly unsustainable. As international financial institutions withdrew their financial support, policies in Romania were at an impasse.

A New Approach

In 1997, the new coalition government elected in November of the previous year decided to abandon the gradualist approach and implement

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^{1.} OECD Economic Surveys: Romania, OECD Publications, Paris, 1998.

^{2.} **OECD Economic Assessment of Romania**, OECD Publications, Paris, 1993.

Romania

Macro-economic Stabilisation and Structural Reform

FOCUS

Regional Development in Romania

Paul Paradis

Regional problems in Romania, strongly linked to the unsuitable location of obsolete heavy industries, are the legacy of forty years of central planning. After the Second World War, the communist leadership decided that the expansion of industrial activity was the best instrument to develop the economy. The objective was to use human resources to the maximum and to attempt to diminish regional disparities. The outcome of this policy was the creation of an industrial base regardless of the economic viability of its location.

After the collapse of socialism in Romania at the end of 1989 and the introduction of a market economy, it was the regions – often the poorest ones – where the industrial base was artificially created and sustained by subsidies,² that had to face the most severe effects of transition: extreme environmental degradation, high unemployment and low standards of living.

A study conducted recently by the EU Phare Programme³ revealed a concentration of poverty and backwardness in the largest agricultural areas: the North-east (historical region of Moldova) and the Romanian Plain in the south. Aside from the capital, Bucharest, the western and central parts of the country are wealthier and better-off in terms of household revenues, social and technical endowment and economic assets. The highest unemployment in 1994 was found in those judets (counties) with a low stage of development at the onset of transition, and with a very high rate of decline in industrial employment.

The Arrival of a Policy Framework

Since 1989, Romania has not had an explicitly formulated regional policy, although the government exercised a good deal of influence on the development of the 42 counties through attempts to induce an equal degree of industrialisation throughout the country, and other instruments of central planning. At the advice of the Phare Programme, the Romanian gov-

ernment has created a regional-policy taskforce, and a Green Paper on Regional Development Policy was published in 1996 and discussed at high level.

The new administration is now designing a policy for regional development. It is studying a new approach that could lead to the creation of 'macro-regions', of regional agencies and to the establishment of a fund to promote regional development. The main objectives are to reduce regional disparities on the one hand, and to promote balanced growth of all regions through expansion of important sectors such as infrastructure, education, small and medium-sized enterprises (SME).

The OECD is contributing to this process through an analysis of regional problems and policies in Romania. The principal issues examined include improvement and expansion of infrastructure, impediments to the expansion and diversification of tourism, regional strategies for restructuring heavy industries in the Jiu Valley (covering also retraining and human resources), the promotion of SMEs and strategies for the restructuring of thousands of small private farms into associations to raise productivity. The purpose of the study is to assist the Romanian authorities in their way of thinking about regional problems and to offer advice on how regional policy may help them tackle problems in these specific fields.

The regional and local authorities are aware of the benefits of regional development policy, recognising that growth does not depend solely on the national government. One of the most difficult questions facing the central government concerning regional develop-

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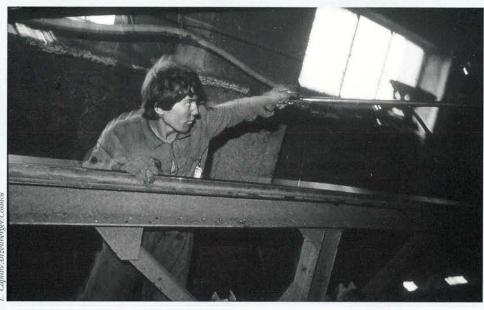
ment will be whether to focus limited resources on policies to combat disparities, or to devote them towards promoting stronger regions and overall competitiveness as an engine for growth for the entire country. The recent trend in OECD countries has been away from the former and towards the latter. But in the difficult circumstances of transition to a market economy it may be necessary to adopt a combined approach.

- 1. **Regional Problems and Policies in Romania**, OECD Publications, Paris, forthcoming 1998.
- 2. For example, in the counties of Vaslui, Olt, Salaj, Ialomita, Mehedini, Buzau, where machinery and equipment, chemicals, metallurgy, textiles and clothing industries were established.
- 3. Regional Disparities in Romania 1990–94, Phare Programme Romania, Regional Policy Analysis and Development, Bucharest, 1996.

a shock therapy. The main novelty in the government programme was a firm intention to accelerate structural reforms towards privatisation, the liquidation of loss-making firms, the liberalisation of prices, the reduction of trade barriers and the promotion of foreign investment. Most indirect subsidies were stopped, and direct subsidies and easy refinancing from the central bank were phased out. The previous system of an official exchange rate was abandoned and the currency was allowed to float according to market forces. On the basis of this programme, the IMF and the World Bank accepted to re-negotiate a stand-by credit line and a package of structural loans of roughly \$1 billion.

The programme implemented in 1997 represents an additional, but largely unavoidable, transition shock for Romania. Social and economic conditions have deteriorated in a country where poverty was already widespread. By mid-1997 real wages had fallen by 30% from their position a year earlier. Both large and small enterprises have been hard hit by the contraction in demand, soaring interest rates and - especially large industries and state farms - the phasing-out of state subsidies. For 1997 as a whole, GDP probably fell by 6% or more. Unemployment has remained surprisingly low, at around 7%, in part because the private agricultural sector has played the role of buffer, but its ability to do so is unlikely to last as restructuring progresses and the capacity of rural areas to absorb the unemployed reaches its limits. Prices of energy and other public utilities have doubled or more, causing prices to rise by over 30% in March 1997 alone. Since then, tight monetary conditions have brought inflation down, but it persisted at 3-4% per month at the end of the year. Inflation for 1997 as a whole was over 150%.

There are nevertheless some encouraging signs. Exports have picked up and the current-account deficit has declined. Improved trade performance could re-ignite economic growth – as in 1993, but this time on a sounder basis. The target of 4.5% of GDP for the government deficit in 1997 was reached despite difficult fiscal conditions. And capital inflows have increased, helping to stabilise the exchange rate and increasing the reserves of the central bank.



Industrial restructuring by the new government has laid off 70,000 workers, though severance payments were generous.

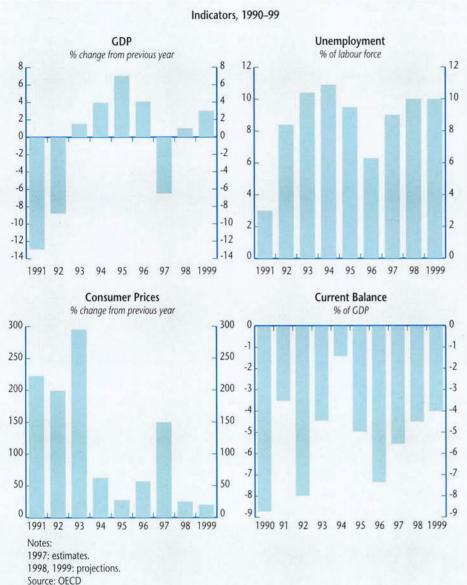
Against this background, the question of adequate macro-structural links again becomes the core issue. If structural reforms do not move ahead rapidly enough, the short-term costs of the austerity programme imposed by the shock therapy of 1997 will not be balanced by the longer-term gains of a more efficient economy. Indeed, if the population does not see some result from the difficulties they have been through, the political consensus formed after the elections of end-1996 may come under threat.

How Rapid and Deep are Structural Reforms?

Time is one of the most precious resources for transition and much time has been lost in Romania. In its initial programme, the government set out an ambitious list of structural reforms, and parliament has since been legislating actively to pass around 100 new laws. The implementation of reforms has nonetheless lagged behind initial expectations.

For example, a bolder approach to privatisation has been instituted, but only half of the initial target of roughly 2,700 companies to be privatised in 1997 was achieved. As part of the new approach, the State Ownership Fund announced that there would no longer be a minimum price on the sales of state property and that enterprises that could not be sold would be liquidated. In parallel, the government attempted to impose tough financial conditions on stateowned enterprises: subsidies were considerably reduced, imposing a *de facto* budget constraint on cash flows, and stocks of unpaid tax-arrears to the state budget incurred heavy penalties.

But practical difficulties meant that this bold strategy could not be fully implemented. Assessment of financial viability of companies is often problematic because accumulated losses arose in part under the distorted price system of the administered economy. Many enterprises, particularly large ones with sometimes a heavy burden of financial arrears, did not find a buyer. The liquidation of non-viable enterprises also faced strong resistance, both on political and social grounds. Indeed, large firms such as oil refineries and steel plants are often viewed as valuable assets both by the authorities and the public opinion. Selling them off cheaply is politically



The reform of the banking sector is another key macro-structural link in the economy. Experiences in other transition economies show that a fragile banking sector is the weakest link in the chain of economic adjustment.³ This sector is dominated by four major state-owned banks, two of which are severely burdened by non-performing loans – mainly a legacy of the pre-1997 policy when the banks were required to

3. John Litwack, 'The Russian Federation – Commercial Banking, **The OECD Observer**, No. 210, February/ March 1998.

provide low-interest (and largely unrecoverable)

credits to the agricultural and energy sectors.

mining sector has been largely restructured, inducing massive lay-offs of around 70,000 workers; to minimise distress and social tensions, lay-offs were accompanied by substantial severance payments. In addition, the official stance towards foreign investment is now open and liberal, although a 1.5% transaction tax is applied to foreign portfolio investment. This openness should stimulate private capital inflows and help improve corporate governance. The start-up of an over-the-counter market (based on the US NASDAO model) and the use of the stock market for privatisation purposes have invigorated capital markets. The government also intends to begin privatising the state-owned banks in 1998, and has announced major restructuring packages for the two most problematic ones. These moves will be supported by recent improvements in the supervisory regime of the National Bank.

The government has nevertheless made firm and sometimes difficult choices that should foster

structural change. A number of loss-making agricultural farms have been closed down. The

Romania has embarked on a long overdue programme of difficult economic reforms, but the scope for development is nonetheless widely recognised. Romania has the second biggest population in central and eastern Europe, a large pool of skilled labour and generous agricultural land. With better management of its endowment of natural and human resources, it has the potential to be a well-performing emerging market economy.

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concentrated in large state-owned firms, notably in the large public utilities (*regies autonomes*). As a result, the amount of non-performing loans in the banking sector has also increased and, by mid-1997, over 50% of total bank credits were either unlikely to be repaid or were already

sensitive, especially when the potential buyers

dilemmas will threaten the coherence of the re-

form package. For example, the amount of arrears

in the economy, which reached 36% of GDP at

end-1996, is rising again. Most, indeed, are still

If they are not rapidly solved, these policy

are foreign investors.

obviously losses.

The OECD OBSERVER No. 211 April/May 1998

Indicators

2 in	period	from	% change from previous	
Cance Demonths Deadust	04.07	period	year	
Gross Domestic Product	ORIGINATION OF THE PERSON OF T	0.4	3.1	
Leading Indicator	Dec. 97	0.1	3.2	
Consumer Price Index	Q4 97	0.3	-0.2	
		current period	same period last year	
Current Balance	Q4 97	-3.97	-3.96	
Unemployment Rate	Jan. 98	8.2	8.6	
Interest Rate	Jan. 98	5.01	5.79	

	BELGIU	M	
-			hange previous year
Gross Domestic Product	Q3 97	0.5	3.0
Leading Indicator	Dec. 97	-1.6	2.3
Consumer Price Index	Jan. 98	0.0	0.4
		current period	same period last year
Current Balance	Q3 97	2.97	3.17
Unemployment Rate	Dec. 97	9.3	9.5
Interest Rate	Feb. 98	3.55	3.13

100	DENMAI		
10/0-	period		hange previous year
Gross Domestic Produc	t Q3 97	-0.2	2.1
Leading Indicator	Dec. 97	0.5	3.4
Consumer Price Index	Jan. 98	-0.1	1.7
		current period	same period last year
Current Balance	Q3 97	0.67	1.28
Unemployment Rate	Dec. 97	5.6	6.3
Interest Rate	lan. 98	3.80	3.60

	GERMAN	VΥ	
	period		hange previous year
Gross Domestic Product	t Q4 97	0.3	2.3
Leading Indicator	Dec. 97	-0.2	7.4
Consumer Price Index	Jan. 98	0.0	1.3
		current period	same period last year
Current Balance	Dec. 97	4.28	-0.43
Unemployment Rate	Dec. 97	10.0	9.2
Interest Rate	Feb. 98	3.51	3.19

	ICELAN	D	
	period	% c from period	hange previous year
Gross Domestic Product	1996		5.2
Leading Indicator			
Consumer Price Index	Feb. 98	-0.2	2.0
		current period	same period last year
Current Balance	Q3 97	-0.03	-0.01
Unemployment Rate	Jan. 98	2.6	3.4
Interest Rate	Jan. 98	7.30	7.10

	period	from	hange previous
		period	year
Gross Domestic Product	Q4 95	0.0	0.3
Leading Indicator	Oct. 97	0.6	8.1
Consumer Price Index	Jan. 98	0.1	1.2
		current period	same period last year
Current Balance	Nov. 97	-0.83	-0.88
Unemployment Rate	Dec. 97	4.4	4.3
Interest Rate	Jan. 98	3.70	3.33

	CANAD	A	
	period	% change from previous period yea	
Gross Domestic Product	Q4 97	0.7	4.2
Leading Indicator	Jan. 98	0.1	1.3
Consumer Price Index	Dec. 97	-0.1	0.7
35 V		current period	same period last year
Current Balance	Q4 97	-3.56	0.72
Unemployment Rate	Dec. 97	8.6	9.7
Interest Rate	Feb. 98	4.96	3.10

Y.			
	FINLAN	D	
	period		hange previous year
Gross Domestic Product	Q3 97	1.1	6.0
Leading Indicator	Oct. 97	0.2	5.6
Consumer Price Index	Jan. 98	0.1	2.1
		current period	same period last year
Current Balance	Dec. 97	0.76	0.50
Unemployment Rate	Dec. 97	12.6	14.7
Interest Rate	Feb. 98	3.42	3.07

6.55				
12	Greece			
1	period	from period	change n previous year	
Gross Domestic Product	1996		2.6	
Leading Indicator	Jan. 98	-0.3	1.8	
Consumer Price Index	Jan. 98	-0.9	4.4	
		current period	same period last year	
Current Balance	Oct. 97	-0.41	-0.70	
Unemployment Rate		THE WORLD	227	
Interest Rate	Feb. 98	12.70	10.71	

2	IRELANI	D	
	period		hange previous year
Gross Domestic Product	1996		8.6
Leading Indicator	Jan. 98	0.2	15.1
Consumer Price Index	Jan. 98	-0.6	1.8
		current period	same period last year
Current Balance	Q3 97	0.77	0.93
Unemployment Rate	Dec. 97	9.8	10.9
Interest Rate	Jan. 98	6.05	5.84

Definitions and Notes
Gross Domestic Product: Volume series, seasonally adjusted except for Czech Republic and Portugal
Leading Indicator: A composite indicator, based on other indicators of economic activity (employment, sales, income, etc.), which signals cyclical movements in industrial production from six to nine months in advance
Consumer Price Index: Measures changes in average retail prices of a fixed basket of goods and services
Current Balance: \$ billion; not seasonally adjusted except for Australia, the United Kingdom and the United States
Unemployment Rate: % of civilian labour force – standardised unemployment rate; national definitions for Czech Republic, Iceland, Korea, Mexico, Poland, Switzerland and Turkey; seasonally adjusted apart from Turkey Interest Rate: Three months, except for Greece (twelve months)
... not available
Source: Main Economic Indicators, OECD Publications, Paris, March 1998.

	period	from	hange previous
		period	year
Gross Domestic Product	Q3 97		0.8
Leading Indicator			W.
Consumer Price Index	Jan. 98	4.0	13.1
		current period	same period last year
Current Balance	Q3 97	-0.68	-1.32
Unemployment Rate	Jan. 98	5.0	3.6
Interest Rate	Feb. 98	15.92	12.32

7	FRANC	Е	
48	period	% change riod from previou period	
Gross Domestic Product	Q4 97	0.8	3.2
Leading Indicator	Jan. 98	0.2	4.3
Consumer Price Index	Jan. 98	-0.3	0.5
		current period	same period last year
Current Balance	Nov. 97	1.79	0.65
Unemployment Rate	Dec. 97	12.3	12.5
Interest Rate	Jan. 98	3.62	3.35

400	HUNGAI		hange
	period	from period	previous year
Gross Domestic Produc	t		
Leading Indicator			
Consumer Price Index	Jan. 98	3.0	17.7
		current period	same period last year
Current Balance			
Unemployment Rate	Jan. 98	10.3	10.1
Interest Rate	Dec. 97	19.20	21.70

ALC: N			
	ITALY		
12	period		hange previous year
Gross Domestic Product	Q3 97	0.4	2.1
Leading Indicator	Jan. 98	1.9	10.3
Consumer Price Index	Jan. 98	0.3	1.6
		current period	same period last year
Current Balance	Oct. 97	3.67	4.56
Unemployment Rate	Oct. 97	12.1	12.0
Interest Rate	Jan. 98	6.09	7.23

	JAPAN	% (hange
7"	period		previous year
Gross Domestic Product	Q3 97	0.8	1.0
Leading Indicator	Jan. 98	0.3	-2.2
Consumer Price Index	Jan. 98	-0.1	1.8
		current period	same period last year
Current Balance	Dec. 97	10.01	7.24
Unemployment Rate	Jan. 98	3.5	3.3
Interest Rate	Jan. 98	0.95	0.53

	KOREA		
A STATE OF THE PARTY OF THE PAR	period		hange previous year
Gross Domestic Product	Q3 97	1.5	6.3
Leading Indicator		34	122
Consumer Price Index	Feb. 98	1.7	9.5
		current period	same period last year
Current Balance	Nov. 97	0.54	-2.07
Unemployment Rate	Dec. 97	3.1	2.3
Interest Rate	Dec. 97	18.60	13.50

Li	JXEMBO	URG	
	period		hange previous year
Gross Domestic Product	1996		3.0
Leading Indicator	Dec. 97	-1.5	11.3
Consumer Price Index	Jan. 98	0.1	1.4
		current period	same period last year
Current Balance	Die Li		
Unemployment Rate	Dec. 97	3.6	3.6
Interest Rate			

	MEXICO)	
	% change period from previous period year		
Gross Domestic Product	Q4 97	-0.4	6.6
Leading Indicator	Jan. 98	0.5	5.7
Consumer Price Index	Jan. 98	2.2	15.3
		current period	same period last year
Current Balance	Q3 97	-2.55	-0.84
Unemployment Rate	Jan. 98	3.5	4.4
Interest Rate	lan. 98	19.37	24.60

	period		hange previous
4	((0))	period	year
Gross Domestic Product	Q3 97	0.7	3.1
Leading Indicator	Jan. 98	-0.3	2.5
Consumer Price Index	Jan. 98	-0.4	1.8
		current period	same period last year
Current Balance	Q2 97	4.64	4.96
Unemployment Rate	Nov. 97	4.7	6.1
Interest Rate	Feb. 98	3.44	3.01

	period	% c from	hange previous
7		period	year
Gross Domestic Product	Q3 97	0.9	3.3
Leading Indicator			
Consumer Price Index	Q4 97	0.6	0.8
		current period	same period last year
Current Balance	Q3 97	-1.43	-1.35
Unemployment Rate	Q3 97	6.8	6.3
Interest Rate	lan. 98	8.95	7.55

	Norwa	Y	
1	period		hange previous year
Gross Domestic Product	Q4 97	1.5	4.5
Leading Indicator	Dec. 97	-0.3	2.5
Consumer Price Index	Jan. 98	0.4	2.0
		current period	same period last year
Current Balance	Q3 97	1.96	2.85
Unemployment Rate	Q4 97	3.8	4.8
Interest Rate	Feb. 98	3.84	3.52

	POLANI)	
	period		hange previous year
Gross Domestic Product			
Leading Indicator			
Consumer Price Index	Dec. 97	1.0	13.0
		current period	same period last year
Current Balance	Nov. 97	-0.28	-0.13
Unemployment Rate	Jan. 98	10.5	12.8
Interest Rate	Jan. 98	23.31	19.45

	Portug	AL	
7	period		hange previous year
Gross Domestic Product	Q4 96	1.2	4.5
Leading Indicator	Dec. 97	0.9	9.9
Consumer Price Index	Dec. 97	0.2	2.3
		current period	same period last year
Current Balance	Q4 97	-1.01	-0.87
Unemployment Rate	Dec. 97	5.9	7.1
Interest Rate	Jan. 98	4.84	6.18

	SPAIN		
1	period		hange previous year
Gross Domestic Product	Q4 97	0.9	3.6
Leading Indicator	Dec. 97	-1.1	3.7
Consumer Price Index	Jan. 98	0.2	2.0
		current period	same period last year
Current Balance	Dec. 97	-1.47	-0.79
Unemployment Rate	Dec. 97	21.0	21.4
Interest Rate	Feb. 98	4.64	5.89

	SWEDE	V	
	period		hange previous year
Gross Domestic Product	Q3 97	1.5	2.4
Leading Indicator	Jan. 98	0.9	5.8
Consumer Price Index	Jan. 98	-0.8	0.9
		current period	same period last year
Current Balance	Oct. 97	0.70	0.83
Unemployment Rate	Dec. 97	9.1	10.6
Interest Rate	Feb. 98	4.33	3.93

1	period	% c from	hange previous
	27	period	year
Gross Domestic Product	Q3 97	0.4	0.8
Leading Indicator	Jan. 98	0.5	9.5
Consumer Price Index	Feb. 98	0.1	0.0
		current period	same period last year
Current Balance	Q3 97	4.98	5.23
Unemployment Rate	Jan. 98	4.7	5.3
Interest Rate	Jan. 98	1.23	1.70

4	TURKEY	t .	
	period		hange previous year
Gross Domestic Product	Q3 97	-2.3	5.5
Leading Indicator			300
Consumer Price Index	Jan. 98	7.2	101.6
		current period	same period last year
Current Balance	Q3 97	1.05	0.75
Unemployment Rate	Q2 97	5.9	6.3
Interest Rate			

UNI	FED KIN	GDOM	
急	period		hange previous year
Gross Domestic Product	Q4 97	0.4	3.2
Leading Indicator	Jan. 98	-0.2	1.5
Consumer Price Index	Jan. 98	-0.3	3.3
		current period	same period last year
Current Balance	Q3 97	0.32	-0.96
Unemployment Rate	Dec. 97	6.6	7.7
Interest Rate	Feb. 98	7.45	6.19

U	NITED ST		hange
	period		previous year
Gross Domestic Product	Q4 97	1.0	3.8
Leading Indicator	Jan. 98	-0.3	4.4
Consumer Price Index	Jan. 98	0.2	1.6
		current period	same period last year
Current Balance	Q3 97	-42.16	-42.83
Unemployment Rate	Jan. 98	4.7	5.3
Interest Rate	Feb. 98	5.54	5.37

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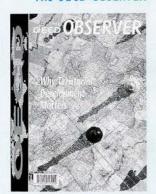
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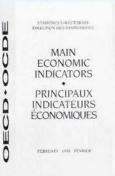
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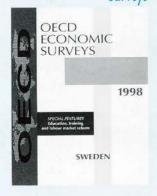
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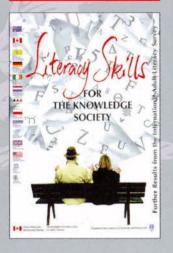
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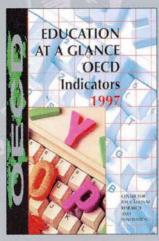
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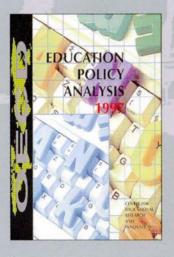
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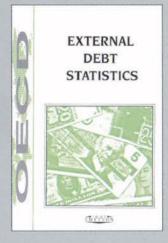
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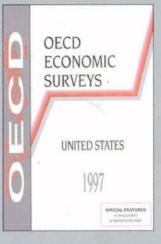
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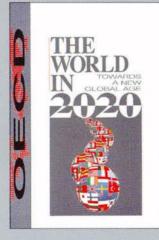






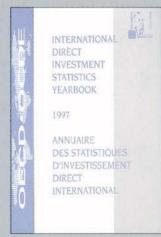


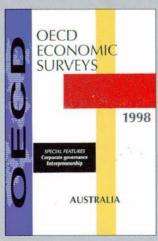


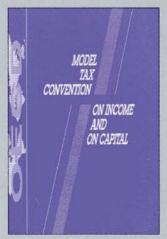


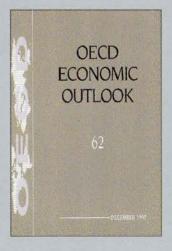
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