



PART I

UNECE ACTIVITIES IN THEIR BROADER CONTEXT – SELECTED ESSAYS

OVERVIEW

Robert C. Shelburne

One of the first requests made by Executive Secretary Marek Belka upon arriving at UNECE was that the staff should be encouraged to broaden their focus from the narrow and technical activities of their particular jobs and the mandates of their sectoral programmes towards a fuller appreciation of the problems and challenges facing a wider Europe and the possible role that an international organization might play in addressing them. The 10 essays presented in this section of the 2008 Annual Report represent voluntary contributions from several senior staff to this initiative. In these papers, the authors attempt to provide the broader context in which a number of more specific activities of UNECE are conducted. Each paper attempts to describe the essence of the overall issue: what the current situation is, where the problems lie and what the possible policy alternatives are. These essays provide the individual authors' perspectives on subjects that they have chosen; in most cases their assessment is based upon years if not decades of working on the more technical aspects of the issue. Often this work has taken place here at UNECE but in some cases at other international organizations, government agencies or even in the private sector. As such, these papers should be taken for what they are – thoughtful discussions of important issues by knowledgeable experts to help the reader more fully understand and appreciate the subject and the context in which various UNECE activities take place. They should not, therefore, be interpreted as necessarily reflecting the “official position” of the secretariat or any official proposal for altering UNECE activities. These papers are really not targeted to experts or government officials overseeing specific subprogrammes of UNECE, but to a wider audience of those interested in being generally informed about European economic affairs and the challenges that the region faces.

If there is one issue that unites all the economies in the UNECE region it is a desire for strong economic growth. Growth in turn is dependent on increased investment in public infrastructure, private plant and equipment, and human capital in the form of education and health services. This investment, however, must come from somewhere, and the first four papers in this series examine issues regarding the financing of this investment. The first paper examines this issue at the most general level: do the funds come from domestic savings or are they obtained from abroad? If the latter, what form do they take; that is, are they private capital flows, remittances or aid, and how does this vary across regions? The second paper examines official aid flows more closely by discussing a general polarization that has developed between the donors and recipients and how the European experience with assistance may provide some common ground towards its resolution. The third paper discusses how public infrastructure can be financed from private sector resources using public private partnerships. The final paper in this first group looks at a very small but quite important segment of financial markets by asking how do new entrepreneurial firms get start-up capital. The next set of papers begins with two examining competitiveness in the region; one examines the role of innovation and the other considers the implications of environmental standards. This is followed by a paper describing how pan-European environmental policy is being formulated. Next we have papers addressing the challenge of increasing energy security and one discussing the interaction between transportation systems and a number of important global trends. The final paper describes the progress that is being made in achieving the Millennium Development Goals (MDGs) in the pan-European region.

The emerging markets in the UNECE region have recently experienced fairly robust economic growth which has been supported by strong investment. The first paper examines the question of the origin of the funds that were used to finance this investment. Exactly where countries can obtain scarce investment resources has become a central theme of United Nations developmental activities since the global conference on Financing for Development (FfD) which was held in Monterrey, Mexico in March 2002. This question of financing development arose after it became apparent that the development objectives



incorporated in the MDGs could not be achieved unless the developing countries were provided far more in terms of external resources. The General Assembly has now decided to hold in Doha, Qatar in Autumn 2008 a major follow-up conference to review the implementation of the conclusions, referred to as the Monterrey Consensus, of that first conference. Preceding the Doha meeting that will evaluate progress to date, a number of preparatory events are scheduled in order to ensure that all the important facets of this issue are fully explored and studied beforehand. Some of these events have already occurred while others are planned for the first part of 2008. UNECE, being a Regional Commission, is an integral part of the United Nations system and thus has an interest in supporting this initiative as it does for all of those that come out of United Nations global conferences. As a more general part of this process Mr. Belka has been asked to discuss the status of the Monterrey commitments in regard to the UNECE region in several recent forums including the Dialogue of the Second Committee and a General Assembly roundtable at United Nations Headquarters.

Given the important role this issue will occupy in United Nations discussions during 2008, I provide in the first essay a description of what the motivations and logic were behind the FfD initiative and assess what has been achieved in the UNECE region and what still needs to be done. An important conclusion is that Central, Eastern and South-East Europe, along with several of the non-energy exporters in the Caucasus and Central Asia, have been following a development model that differs in several important ways from what most other emerging markets have been doing. In particular, these economies have relied much more extensively on obtaining private external resources to finance their development. Why this has happened is discussed along with its implications not only for these economies' future development but for world development in general.

An important source of finance for poorer economies, including some in the UNECE region, is foreign aid; the second paper examines some controversies surrounding its provision. The advanced economies have provided hundreds of billions of dollars in aid to the developing world over the last several decades; although this has done much good in some cases, many of these countries have grown very little, especially during the last two decades of the twentieth century. In fact some have argued that this aid has actually hindered development by creating perverse incentives and hindering democratic governance. Thus it would appear that much of this money has been wasted, but whose fault has it been and what can be done to improve the situation in the coming decades? Abdur Chowdhury, the then Director of the UNECE Technical Cooperation Unit, and Deputy Executive Secretary Paolo Garonna analyse these aid issues and propose that the answer to these questions can be partially found by examining the European experience in providing assistance to its disadvantaged regions. Of particular importance in this regard has been the way aid has been used to promote economic integration and how it has been distributed using the subsidiary principle.

The third paper dealing with financing development addresses how public infrastructure can be paid for and managed in an environment where public resources are limited but the investment needs for these services are great. This is a characteristic that succinctly describes many of the emerging markets of the region. With insufficient resources in government budgets there has been a need and an increasing tendency to rely more on the private sector to build, maintain and manage infrastructure projects. Public-private partnerships (PPPs) represent a flexible institutional arrangement that allows the public and private sectors to share responsibility in achieving social objectives with specific responsibilities entrusted to the entity that can accomplish it most effectively. However, as with any other institutional structure, the devil is in the details, and in many of the transition economies in the 1990s the details were not appropriately designed. In the next essay, Geoffrey Hamilton, Chief of the Cooperation and Partnerships Section of the Economic Cooperation and Integration Division, who has spearheaded UNECE's PPP activities, focuses on what is required for governments to be able to effectively use this financial model. Eight lessons are provided based upon an analysis of many PPPs that have been implemented in a number of different sectors and countries. In addition, it is emphasized that the effective use of PPPs, which properly considers developmental objectives, can help society not only achieve the cost-effective provision of services but can also increase accessibility of services to the poor and to geographically disadvantaged regions. It is interesting that he raises this last issue, because failure to provide services to the poor is often alleged to be a disadvantage of the PPP approach, however he argues that if properly implemented, it is an advantage.

Creating more innovative and dynamic economies is one of the fundamental challenges facing the entire UNECE region, both its advanced and emerging market economies. An important ingredient of this involves the creation of entrepreneurial firms which can quickly translate creative ideas and scientific discoveries into viable products. These firms, however, need financing because it takes time and money to turn ideas into marketable products. However, investing in these types of activities is risky as a lot of new ideas simply do not work out in practice. Due to these risks, banks tend to avoid lending to these types of firms. There is, however, a small segment of the financial sector referred to as the venture capital market that specializes in finding and developing these entrepreneurial businesses. José Palacin, UNECE's focal point on innovative finance in the Economic Cooperation and Integration Division, provides an overview of this important financial sector and concludes that public policies have historically been quite important in nurturing a venture capital industry as it is an area characterized by numerous market imperfections. From these experiences some lessons are drawn as to what actions Governments can take



to overcome the obstacles in establishing a venture capital market which can adequately finance dynamic new companies. It is also emphasized that although obtaining finance is often a significant constraint, it is nevertheless just as important to ensure that the other ingredients for entrepreneurship are also present; these include a proper regulatory and legal framework including protections for intellectual property, low start-up costs with minimum paper work, a favourable tax regime, and a well-educated workforce. More generally, it is pointed out that the policies needed to promote innovation in advanced economies may not be appropriate for catching-up economies.

A recurrent theme in many of the previous papers concerns the issues of competitiveness and innovation and their role in fostering higher living standards. The next two papers look at these issues in more detail. Rumen Dobrinsky, Chief of the Innovative Policies Section of the Economic Cooperation and Integration Division, examines the link between these two concepts at the level of both the firm and the country and then outlines some important policy implications. It appears that the innovative capacity of many of the UNECE emerging markets would be enhanced considerably if the link between knowledge creation and its incorporation into marketable products could be strengthened. In many economies the basic national institutions supporting innovative activities could be improved, and the management of private firms has yet to fully appreciate the importance of innovative activity. The interrelationship between various economic policies, such as those for competition policy which seeks to limit firms' market power, is also explored; it is found that these other policies often conflict with the objectives of increasing innovation and thus all these policies need to be formulated within a coherent framework that considers all these interactions.

The next paper addresses another set of conflicting national objectives, that between economic competitiveness and environmental quality. Although this is a fundamental trade-off that confronts all economies, it is particularly acute in the emerging markets of the UNECE region. These economies find themselves sharing the atmosphere and water networks with many wealthy economies that highly value environmental quality while at the same time they are having to compete against countries from Asia and elsewhere where environmental standards are lower. In lower-income economies, the perceived benefits of improved environmental quality may be valued less than in richer economies, while the perceived opportunity costs of abatement or compliance may be valued higher, especially when they have an impact on employment levels or result in lower wages and profits. There is also the fear that more stringent standards might have a negative impact on foreign investment as multinationals seek out locations where operating costs are low. As such, these countries are therefore quite concerned about mandating environmental regulations that could impose significant costs on their enterprises and thereby reduce their global competitiveness. In addition there is a free rider problem regarding transboundary pollution as a country can benefit from the higher environmental standards negotiated amongst its neighbours while avoiding all the costs by deciding not to participate themselves.

Dieter Hesse, former Senior Economic Expert in the Environment, Housing and Land Management Division, however, argues that this trade-off is far more nuanced than is commonly believed. In examining environmental policy in the former transition economies he finds that their environmental institutions, especially the government ministries, are weak, their regulations are often inadequate, and their enforcement efforts need to be improved. At the same time he finds these economies attach a high priority to increasing living standards and view that this can only be achieved by increasing their global competitiveness in a number of non-traditional industries. Nevertheless it is argued that high environmental standards are only a minor factor in determining cost competitiveness for most industries and locational decisions for multinationals. Even to the degree that they might be a competitive disadvantage in the short-run, they can actually turn out to be an advantage in the longer-term as they promote technological upgrading, the efficient use of resources, and can reduce adjustment costs involved with future trade policy initiatives or integration into production-sharing networks. In addition there are other benefits external to the firm including improved public health, increased tourism and additional recreational resources. Furthermore, the costs of undoing degradation, which will be desired at some future date as national incomes rise, can be avoided altogether. Thus in essence, when these dynamic factors are combined with the social benefits, the real costs of setting high environmental standards are much less than what their current costs might suggest. However, environmental policies need to be integrated fully into a country's overall economic development plan, be cost-effective, conform with international agreements and be gradually implemented as part of a predictable regulatory framework; income distribution effects may also need to be addressed. These messages are important not only for the less developed former transition economies in their attempts to integrate and compete with the more advanced economies of the region, but are important for the advanced economies as they contemplate environmental policies to deal with the newer global challenges facing the world such as global warming.

This issue as to what degree there is a trade-off between economic growth and environmental quality was one of the topics discussed at the recent "Environment for Europe" Ministerial Conference held in Belgrade in October 2007. In our next paper, Kaj Bärlund, former Director of the UNECE Environment, Housing and Land Management Division, provides his



overall assessment of that conference in Belgrade and describes its conclusions and decisions. This was the sixth Ministerial Conference (and Mr. Bärlund's fifth) under this process in which Governments of UNECE member states, United Nations and other intergovernmental organizations, non-governmental organizations and other stakeholders come together to appraise the state of the environment in Europe. Since they began in 1991, the UNECE has had a leadership role as the secretariat of this process. The conference is important because it is here that the future priorities are discussed as to where cooperative actions can be implemented in order to promote pan-European environmental protection and sustainable development. More specifically, the focus of this process has been on upgrading the environmental policies in those economies with lower environmental performance standards.

In his essay, Mr. Bärlund evaluates the "Environment for Europe" as a political process and generally concludes that it has been a success although he provides several suggestions as to how the process might be reformed in order to increase its overall effectiveness. In regard to the substantive issues concerning the state of the environment in Europe, the conference concluded that significant progress is being made but that the results obtained so far in Eastern Europe, the Caucasus, and Central Asia have fallen below expectations. The problem there seems to be related to the failure to strengthen environmental institutions in these economies and the need to focus more on the implementation of commitments. The importance of donor support and private sector involvement are likely to be additional important components in improving this situation.

Central to the goals of competitiveness and sustainable development is the issue of energy. Is there enough? Where will it come from? What will it cost? Is its production and use environmentally sustainable? Many of these questions are now discussed under the general topic commonly referred to as "energy security." George Kowalski, then Director, and Sead Vilogorac, Senior Economist, both of the Sustainable Energy Division, in their paper discuss more specifically what is meant by "energy security" and provide some reasons why it has been so difficult to forge a common approach to its achievement. A key factor includes substantively different views amongst countries on the optimal role of the market mechanism, the private sector, and Governments either as an owner or regulator. Although different types of insecurity are discussed, the focus in this essay is on the long-term physical availability of energy supplies. Interestingly, it appears that long-term security is not just an issue for consuming nations but also for the supplying nations, due to concerns that future markets might not exist which would justify massive long-term investments today. However, long-term commitments by consuming and producing nations could lower the risks faced by each. In order to achieve increased security, the consuming countries need to diversify the types of energy used and their geographical sources, yet in many ways the trends have been the opposite as the geographic concentration of energy reserves, especially oil and gas are projected to increase. The ability of countries to increase alternative sources, such as renewables or nuclear, have considerable potential in the long term but in the medium term are limited by technological, environmental and political constraints. For oil and gas which will remain for the near future the most important energy sources, the most immediate problem is not one of insufficient supplies under the ground, but the lack of either government resources for public development or of a sufficiently investment friendly environment for private sector development in those countries that have the reserves. In addition there are a number of other complementary issues that need to be addressed such as improving the transport infrastructure and enhancements for research activities and technology transfer.

Next, Eva Molnar, the new Director of the Transport Division, examines the two-way interaction between transport systems and several mega-trends that have been and are likely to continue to characterize the world. These trends include globalization, technological change, increased intergovernmental cooperation, the changing role of the public sector, the increased emphasis on security, and the need to ensure that economic growth is more environmentally sustainable. It is stressed that numerous policy responses are needed to address these developments, some at the global level, others at the regional level and some at the national level.

Besides creating a growing, prosperous, and peaceful Europe, we all have an interest in ensuring that the benefits of this extend to the most unfortunate of those amongst us. The MDGs provide a yardstick for how well this objective is being addressed. In the final paper Patrice Robineau, Senior Advisor to the Executive Secretary, provides a concise overview of the progress that is being made in achieving the MGDs in the region. The central message is that although significant progress is being made based upon strong economic growth, the fulfilment of these objectives is likely to require some new policy initiatives that more precisely target the needs of the region. The importance of resolving existing political conflicts and maintaining the momentum in promoting pan-European economic integration are also emphasized.

In sum, these essays provide some important background information for understanding the context in which UNECE technical activities take place. Hopefully you will also find them interesting and enjoyable to read.