DEVELOPMENT COMMITTEE MEETING

Washington D.C., Saturday 26 April 2009

Statement by
Mr Angel Gurria,
OECD Secretary-General
and
Mr. Eckhard Deutscher, Chairman,
OECD Development Assistance Committee (DAC)

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1. TOWARD A COORDINATED CRISIS RESPONSE

OECD Economic Outlook

The OECD area is in the midst of its deepest and most widespread recession for more than 50 years. The OECD Economic Outlook now forecasts a 4.3% contraction in the OECD area in 2009. By the end of 2010, unemployment rates in many OECD countries are expected to reach double figures for the first time since the early 1990s. The fall in output has been sharp and highly synchronised with a collapse in world trade.

Policy measures have been introduced to support the financial system and aggregate demand, although additional measures are necessary to stabilise banking systems, and monetary and fiscal policy needs to use the remaining scope to bolster aggregate demand. These measures should be implemented in such a way that the productive capacity of the economy is not reduced by crisis-driven, flawed changes in labour and product market policies.

As testified by the spill-over and contagion as the crisis has unfolded, getting the crisis response right in OECD countries, even though this is absolutely necessary, will certainly not be a sufficient condition for helping developing countries deal with the effects of the crisis. The spill-over and contagion of the crisis from OECD countries to the rest of the world underlines the importance of this for developing countries. OECD countries working towards a swift turn-around based on sound policy will help provide a boost to resume global economic activity.

Road to recovery - Update on the OECD's Strategic Response

The broad OECD strategic response to the financial and economic crisis is twofold, (1) a focus on finance, competition and governance; and (2) sustainable long-term growth. In the short-term it aims to foster conditions for effective and appropriate regulations, identifying areas where there may be regulatory gaps, while in the long-term it proposes a path of sustainable long-term growth post-crisis. A level playing field for a stronger, cleaner and fairer economy in the OECD area will be essential for overcoming the crisis also in developing countries.

While the crisis requires tough decisions now, it should not turn the attention away from efforts to address poverty and inequality, scale up development aid, keep global flows of trade and investment open and develop cleaner energy and production processes. These global challenges provide opportunities for a sustainable and strong growth environment, to which an effective and sustainable global response will require the involvement of all major players.

Imperative of open markets

Thus far, protectionist measures at-the-border have been few and limited to non-OECD countries. The World Trade Organisation (WTO) has seen a rise in anti-dumping complaints. However, as unemployment rises, the pressure to resort to protectionism will strengthen and require strong political determination to defend. OECD countries ratified a pledge in late 2008 expressing concern that the financial crisis had raised the spectre of new protectionist pressures on governments in OECD countries and beyond.

In the interest of strengthening the contribution that open markets can make to a dynamic recovery in the global economy, OECD countries strongly supported the commitments regarding trade agreed at the Washington Summit to refrain from raising new barriers to investment or trade in goods and services, impose new export restrictions, or implement WTO inconsistent measures to stimulate exports. In addition, they agreed to strive to reach agreement this year on modalities leading to a successful conclusion to the WTO's Doha Development Agenda with an ambitious and balanced outcome.

An exit strategy toward stronger, cleaner, fairer growth

The crisis response should focus on initiatives that allow their logical removal as conditions in financial markets normalise in order to avoid future instabilities. Forging a path towards long-term sustainable growth should be a criterion in implementing new policies. Some crisis measures will eventually be replaced by discussions on labour market reforms, once recovery takes hold.

Building on its comparative advantage in promoting whole-of-government approaches, the OECD will set up a process to monitor policy developments and assess the impacts and implications of short-term measures on long-term sustainability. It will also develop guidance for governments on designing and implementing exit strategies in the areas of financial markets, debt management, insurance and private pensions markets.

G20 Supported OECD Tax Standard as example of development coherence

Tax havens, located in developed as well as developing economies, can aggravate the impact of the crisis in several ways, most seriously by encouraging opaque and destabilising shifts of regulatory risk. They can also deprive treasuries and ordinary taxpayers, who must bear the cost of immediate efforts to shore up financial systems, of substantial future returns. These distortions can undermine public perceptions of fairness, and ultimately public support for tax systems and crisis recovery programs funded through them.

This continued diversion especially hurts developing economies already suffering from thin domestic resource bases, often disproportionately affected by capital flight toward tax havens.

The OECD's longstanding work to implement an internationally agreed tax standard was recognised and strongly supported by the G20 Summit meeting. Since the Summit, all the jurisdictions surveyed by the OECD have now officially committed to this standard, although several of them have yet to implement it substantially.

The crisis could be a new driver for corruption world-wide as opportunities for legitimate economic activity and enterprise decline and as those involved in corruption seek safe havens for illegally acquired assets. The G20 imperative to improve the international regulatory environment could, however, provide entry points for donor countries to make faster progress in the field of anti money laundering, asset tracing, freezing and recovery, as they have committed to do in the Accra Agenda for Action.

The MDGs must not be left behind

The crisis should not be a reason for any of us to let up on achievement of the MDGs. Indeed they provide clear, monitorable benchmarks for what we now mean by a fairer global future for all, which relate closely to our vision of an exit strategy from the crisis.

Moreover, if even a "perfect" recovery from the crisis is held to mean a return by 2011 to conditions obtaining for most of humanity in 2007, we shall at best have lost four more years toward 2015. That is an unacceptable loss, and a false interpretation of our common task, which we should firmly reject.

In this context, we did not only pledge ourselves to open markets and continued support the trade credit system, but OECD-DAC countries also signed up to the aid pledge, reaffirming their aid commitments and refraining from any budgetary action that is inconsistent with such commitments. The triple pledges taken by the OECD members received strong support at the Monterrey Follow-up Conference on Financing for Development in Doha last year.

The crisis will require us to do much more than not slip into reverse, however. In terms of financing, for example, we must use every possible opportunity to accelerate existing commitments.

2. DAC PERSPECTIVES ON DEVELOPMENT COMMITTEE AGENDA

Vulnerabilities – lessons from past crises

Just as the crisis must not deflect us from working toward the MDG horizon in 2015, we must not allow it to impose additional long-term, perhaps irreparable, damage to social and human capital, which on the contrary should provide the backbone of sustainable overall recovery and growth.

Previous crises have shown that this is not a theoretical risk. Indeed, one of the key lessons of the Asian, Latin American and Eastern European crises of the 1990s was the importance of early public interventions to maintain basic health coverage and keep children in school, for example, in the face of otherwise devastating pressures to the contrary. In some cases, notably infant nutrition, small short-term investments can avoid massive irreversible losses.

There are other vulnerabilities in developing countries, especially low-income countries, which preceded the crisis and could aggravate its severity. Structural weaknesses in domestic resource mobilisation sharply increase countries' sensitivities to even modest balance of payments and fiscal shocks. Safety-nets supported by formal labour markets and welfare systems have limited coverage, where they exist at all. Household assets are mostly scarce and illiquid.

Climate change is another and growing source of vulnerability. The need to adapt for its unavoidable effects will entail large additional private as well as social costs. This will be especially hard in low-income countries, which are negligible sources of greenhouse gases.

The Gleneagles Gaps and forward plans to help close them

Aid flows represent an important share of GDP in the poorest developing countries, amounting to 8.5% of the GNI of least developed countries. In Sub-Saharan Africa, ODA represented 65.4% of net capital flows from 2000-6. This reveals just how important ODA flows are for sustaining public expenditures, at least in the medium term. Looking further ahead, taxation is the long term antidote to aid dependency. We must be alert to the risks that aid dampens domestic efforts to raise revenues. Rather than substituting domestic revenues, the objective of ODA is to support the development of capable states that are not aid dependent. More should be done to support local efforts – less than 1 percent of bilateral ODA is devoted to revenue related tasks.

The OECD has indeed just published the 2008 ODA figures and surveyed the forward intentions of bilateral and multilateral donors through 2011. Despite the record level of aid in 2008, which is estimated at $120bn, the figures still show a 21% global gap ($25bn in 2008 terms) with respect to 2005 commitments to scale up by 2010. This is over and above the reduced value of the pledges, which are expressed as a share of national income, as a result of the fall in GNI. The Gleneagles pledges of aid to Africa are falling short by a far greater proportion (58%) than the global gap.

Donors' forward intentions, second, show that about one third of this gap could well be closed by the end of 2010. However, they confirm that the increase is not yet significantly allocated either to Africa or to countries which are thought to be more crisis-exposed. In particular for Africa, exceptional measures are needed starting now. If donors were to meet their Gleneagles target for Africa, without exceeding their current targets for total aid, this would imply reallocation of resources from other parts of the world.

This indicates the urgent need for a more balanced, concerted approach, and flags the risks of potential delays in addressing imbalances. And none of this makes allowance for additional resources for crisis-related interventions, over and above past commitments. It must be repeated here that it would be totally wrong for us to recover fully from crisis in 2011 and find ourselves in MDG terms only where we were, sadly, in 2007.

Need for scaled-up, frontloaded responses

The crisis comes as an exogenous shock for the developing countries, which were already in a weak position due to last year's food and energy crisis. Developing countries are now faced with decelerating growth, putting a severe strain on their development outlook: most low-income countries do not have sufficient fiscal space to embark on countercyclical spending. Indicative estimates of financing needs range from $25bn to $700bn to fill the financing gap, and these estimates do not take into account any additional costs related to reaching the MDGs.

Given the – often absolute – lack of fiscal space of low-income countries, which is further exacerbated by the crisis response of developed and emerging economies, it is imperative that donors not only meet their commitments to scale-up, but also front-load these commitments. To this end speedily disbursed resources in the short term are critical and donors need to address the need for and the challenges in adjusting aid delivery mechanisms and modalities in time of crisis.

Opportunities to galvanise development effectiveness

In October 2008 at the Annual Meetings here, we presented the Accra Agenda for Action, agreed at the Third High Level Forum on Aid Effectiveness (HLF3) held in Accra, Ghana a month before. We explained that this represented a step change in the relationship between developing countries and their donors.

This agreement was based on one of the most extensive consultation processes ever held, the cornerstone of which is the Working Party on Aid Effectiveness – an international partnership of donors and developing countries hosted by the OECD-DAC. We think this could be a model for inclusive problem-solving in other future contexts, including the crisis response, as discussed below.

The Accra partners – over 100 governments, most multilateral agencies, hundreds of CSOs from around the world, many non-traditional aid providers, global funds and middle-income countries – called for progress in six key areas:

1. Conditionality
2. Multi-annual predictability of aid
3. Untying
4. Complementarity and the division of labour
5. Incentives for donor staff to implement the Paris Declaration; and
6. Capacity development

Each of these themes has subsequently been developed further by the Working Party on Aid Effectiveness, whose outcomes are regularly posted on the DAC website.

How does the crisis affect this agenda?

Our contention is that, far from being a source of delay and frustration, the crisis presents a **major opportunity to accelerate progress** towards much greater aid effectiveness in all its dimensions, for the following three reasons.

First, public scrutiny of aid effectiveness, along with other uses of tax resources, will become more acute than ever. Demonstrable impact from current levels of assistance will have to underpin our calls for expanded support.

Second, international experience has shown that "emergency" approaches, for example those of streamlined relief operations following upon natural disasters, can achieve much faster impact at lower transaction costs, without the much-feared side-effects of higher corruption or greater leakage of funds. Why not then turn the tables and make the exceptional procedures the general rule, using the license provided by the urgency of the crisis? For example, general budget support is the most rapid disbursement modality available to scale-up development assistance. It will also ensure that all funding respects country priorities, where these rest on broad-based ownership and accountability.

Third, the crisis is also an opportunity to concentrate efforts toward partner country led division of labour. Most likely in the short term, this will happen through an enhanced role of some major multilateral fund holders, which can provide a cost-effective common platform based on national systems, especially for smaller donors who are unable or unwilling to mount separate parallel crisis response initiatives. Multilaterals can also have broader geographic reach and greater thematic expertise. The World Bank's Vulnerability Financing Facility is a case in point.

It will be crucial however, that any such shifts in the overall and in-country architecture of donor collaboration and in the targeting of crisis-affected countries and sectors obey the Accra Agenda requirement that overall funding levels are not reduced, even when the number of actors on the ground is rationalised. This cannot be done without efficient, real-time information sharing, with which the DAC can help.

Risks of fragmentation and uncertainty

All innovation in the face of the crisis is not necessarily an unmitigated blessing. There will be legitimate pressure to design new cross-country programs around thematic interventions, whether for food security, social safety nets, health systems, microfinance or many other threatened sectors.

These thematic priorities are not automatically aligned with country-owned programs. This fit depends on how proposals are actually generated and assessed and what particular modalities are used and by whom-i.e. the devil is in the details. The lessons of Accra-including the encouraging and intensive participation by existing global funds in the entire process-can help here.

A second potential risk is that it may not be easy to judge whether the new activities are truly "additional" and complementary to other programs previously available at country level, or whether a significant degree of substitution may be occurring. At the margin, crisis-oriented activities can mask a reduction of longer-horizon ones, when both are needed.

A third tension arises between the legitimate twin aims of, on the one hand, greater predictability of aid allocation and disbursement toward all existing recipients, and on the other, retaining sufficient flexibility to respond quickly to the worst-exposed countries, realising that we do not have enough information to predict exactly where that will be even a few months out.

If aid budgets are broadly static and donors hold back substantial reserves to face such uncertainties, they will tighten liquidity overall, and may even lower predictability at the country level.

Climate change financing should complement crisis response

In the coming months, DAC members will face decisions on scaling up crisis response assistance. At the same time, they will be negotiating on the financing component of the post-Kyoto Climate Change regime. These new demands will need to be carefully distinguished and explained to the public, along with the fundamental linkages between the development and the climate change agendas. Climate change financing should complement the response to the financial and economic crisis, but it should not be counted as a response to the crisis itself. The complex issues of ODA targets and additionality will also need careful treatment.

A DAC contribution to a concerted global response

There are five areas in which the DAC is already helping and stands ready to provide more help.

The **first** is what we have just discussed – ensuring that the development community sticks to its commitments, by monitoring and publishing progress and exerting peer pressure. This applies of course to the aid pledge taken by the OECD-members and to the Gleneagles and related commitments just mentioned. As things stand, they fall short of expectations, especially for Africa. But it also applies to members' trade and export financing pledges, reinforced by the G20, and to related commitments, for example on investments, on tax havens, and on anti-corruption work, as well as on not reversing past progress on untying of aid.

The **second** role is to help create and sustain an effective "crisis contact network" to share time-sensitive information on current and future responses and discuss the pattern of aid allocations and how this maps to crisis needs on the ground-and at senior level. For this the previously mentioned 2009 survey of forward aid intentions is an important tool: It is the only such instrument available and covers most multilaterals and some non-DAC donors as well as the DAC as such. We offer our support, along with partners like the World Bank, to set up such a crisis contact group.

The **third** role, again related to the first two, is to help explore all possible ways of frontloading existing aid commitments, including innovative funding options, to get more resources into countries as fast as possible within constrained commitments. We should worry about what works best, whether multilateral or bilateral, whether strictly speaking ODA or "something else", but absolutely make sure it is truly complementary to other efforts, not a mere displacement activity.

The **fourth** role is to seize the opportunity to galvanise the Accra Agenda for Action, as mentioned above, by brushing aside some of every donor's bureaucratic restrictions designed for "normal" times. We know these have been quietly dropped in emergency situations without sacrificing results. This may also need to involve a fundamental rethink of who does what at both country level and sometimes across countries. For example, we know that 25% of all aid relationships add up to at most 3% of total aid volume. Can we figure out how to pool, delegate, or otherwise manage the same volume and same (or better) results at country level, within a far lighter burden on country governments? And within the aid relationships that remain, can we get much more flexible, using rapidly disbursing and more predictable forms of support, responsive to expressed country needs?

The **fifth** is to accept that this is no longer a task for DAC members alone, if indeed it ever was. To be truly effective the process, to which we will gladly provide an anchoring, needs to reach out to partner countries- as with the Working Party on Aid Effectiveness process we have discussed here. It also needs to involve non-traditional donors and aid providers, such as emerging economies and nongovernment actors, from whom we stand to learn a great deal. The global governance framework for development cooperation should follow an inclusive process that provides substantive voice to all stakeholders. We in the DAC are prepared to for the greater complexity, but also greater transparency of a more inclusive process.