Summary Record

2014 OECD GLOBAL FORUM ON DEVELOPMENT

2 July 2014

INNOVATING FOR DEVELOPMENT

Rethinking Structural Challenges

for Post-2015

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EXECUTIVE SUMMARY

The 2014 OECD Global Forum on Development looked at the role of innovation in addressing structural bottlenecks in development from several points of view:

Policy innovations for productivity and growth *(Session 1)*
"Shifting wealth", the increasing economic weight of developing countries in the world economy, has received a boost through the rise of China, which has also generated positive spillovers on developing economies. However, even at their higher rates of growth since 2000, the per capita incomes in developing countries – including many middle-income countries – will not reach the levels of developed countries by 2050. Boosting productivity growth in middle-income countries could stem this trend and sustain further convergence. The OECD *Perspectives on Global Development 2014* highlighted specific policy options available to emerging and developing economies to unleash new sources of productivity growth.

Innovation in development partnerships *(Session 2)*
Targeted development co-operation can accelerate structural transformation when supporting the appropriate policies in the partner country. Official development assistance (ODA) remains an important pillar in financing development and donors increasingly realise their catalytic role in promoting better policies and mobilising other sources of financing. But innovative financing mechanisms, such as development impact bonds, value-chain approaches and partnerships with the private sector can also play a crucial role in stimulating sustainable development. The session illustrated some of these new models and discussed the challenges of scaling-up.

Inclusive innovation to eradicate poverty and promote social inclusion *(Session 3)*
Innovation policies should no longer focus solely on leading sectors but also on producing opportunities for other players and lagging regions and benefits for the excluded. The effect of innovation and its policies on inclusiveness and the question of how innovation can support more inclusive development have not yet been comprehensively understood and addressed. Examples discussed in the session showed that inclusive innovation initiatives have indeed a large potential when it comes to making basic products and services available for low-income individuals.

About the Forum:

The 2014 OECD Global Forum on Development was organised by the OECD Development Centre and the Development Co-operation Directorate in co-operation with the Science, Technology and Industry Directorate. It was held within the framework of the OECD DEV Week. The Forum gathered about 400 representatives of governments from OECD and non-OECD member countries, private sector, academia, foundations and experts. The 2014 edition of the OECD Development Centre's *Perspectives on Global Development: Boosting Productivity to Meet the Middle-Income Challenge* was launched on that day.

OPENING SESSION

Welcoming Remarks

Angel Gurría, Secretary-General, OECD

Over the coming year, deliberations over the shape and scope of a future global framework to replace the Millennium Development Goals will intensify. The new agenda needs to properly reflect the evolving development reality and fully address the relevant dimensions that support inclusive growth. In 2010 the share of non-OECD countries in the global economy surpassed that of OECD countries, when measured in terms of purchasing power parity. The pace of this shift has been remarkable: just ten years earlier these countries accounted for 40% of the global economy. Large numbers of people have benefited from this rapid change, and it has been an important driver of poverty reduction worldwide. Nevertheless, growth in emerging-market economies is slowing down. Countries such as Brazil, Colombia, Mexico and South Africa are not growing fast enough to reach the average income level of OECD countries by 2050. This growth slowdown also matters for the poorest countries. In today's interconnected economy, their development prospects are increasingly linked to the growth of emerging and advanced economies.

Against this global backdrop, the productivity challenge is now firmly on the international agenda. And it is gaining ground in the consultations on the post-2015 framework. At the OECD, we continue to emphasise the importance of "going structural for development". I am encouraged to see that the issues of production, technology and innovation – which were largely absent from the Millennium Development Goals – are more prominent in the narrative which is emerging around their successors.

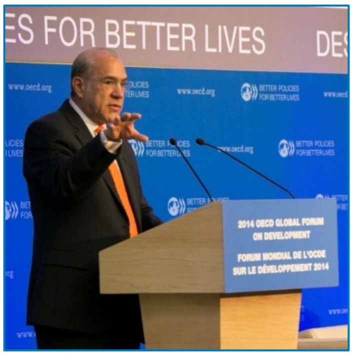
Policy innovations for productivity and growth

What policies are needed to address the challenges of slowing growth in middle-income countries and slowdowns in productivity? Our latest *Perspectives on Global Development* report shows how, in middle-income countries, productivity slowdowns can be brought about by challenges in moving up the value chain. Over time, countries need to move away from growth paths driven by low-cost labour, and towards an upward path driven by innovation.

Better policies play a crucial role. Diversification isn't an automatic process. Policies need to be designed and implemented in a coherent manner: from skills development to access to credit; from logistics and trade facilitation, to innovation. Technology policy is also crucial: countries need to be able to adopt and adapt existing knowledge. We also need to look more closely at the services sector, which is more and more interlinked to competitiveness of industry. As India has shown, services can be an important source of export earnings. Tools such as the OECD's Services Trade Restrictiveness

Index can help us do that by showing where countries are in relation to the best practice frontier, and where they can do better.

Innovation in development partnerships



Earlier this year, the Government of Mexico hosted the first ever ministerial meeting of the Global Partnership for Effective Development Co-operation, which I was privileged to attend. It came only a few days after the OECD released data showing that aid to developing countries had reached an all-time high of USD 135 billion in 2013.

The deliberations in Mexico proved that aid is far from “dead”, as some have suggested it should be, but rather that development co-operation – in the broadest sense – continues to evolve and innovate. Some said: “Beyond Aid”; No! It is Aid and Beyond! We must not forget that aid – or Official Development Assistance – can mean the difference between life and death in some countries. Between 2005 and 2010, it accounted for 60% of external financial flows to the poorest and most fragile countries. Targeting aid well – at infrastructure, at education, at public administration – can help accelerate structural transformation, and help put these countries on a firmer path towards inclusive growth.

“Innovation” and “partnerships” seem to have infiltrated the development discourse over the course of the last decade. Newer tools and approaches – such as Advance Market Commitments for vaccines, development impact bonds, and impact investment – now form part of a bigger, more forward-looking toolkit to support development. The OECD’s growing partnership with foundations and philanthropic organisations promises to bring about further innovation. And cross-OECD efforts will continue to push countries to look at the development footprint of all of their policies: only last year, we released our first ever assessment of OECD members’ own efforts to curb illicit financial flows – flows which have devastating effects on developing countries.

Innovation to eradicate poverty and promote social inclusion

Not all innovations are equal. Some are better than others in reaching poor and marginalised social groups. When we look at innovation policies, we tend to look at them as a source of growth. But we haven’t really looked at them as a source of inclusive growth yet. Our thinking around innovation policy cannot just be aimed at leading firms, high-tech sectors, or central regions. It also needs to help create opportunities for outsiders – young and small firms, traditional sectors, and outlying regions – to participate in the innovation process.

Inclusive innovation initiatives can provide low-income households with access to new products in their everyday lives. Kenya’s M-Pesa mobile payment technology is perhaps one of the best known examples, bringing access to basic financial services to many people for the first time. Company figures show that over one month in 2012, the value of transactions undertaken using M-Pesa was equivalent to almost a third of Kenya’s GDP!

Bringing inclusive innovations to a scale that really benefits large numbers of people remains challenging. And this is where public policy can play an important role. For example, it can shape incentives to include poor people in the product development process. It can encourage the private investment that will be critical to achieving scale and financial viability. And it can help connect innovation in the public and private sectors. The OECD project on Innovation for Inclusive Growth will help develop policy solutions, and will build a bridge between the innovation and inclusive development agendas.

Keynote Speech

Jean-Marc Châtaigner, Deputy Director General of Global Affairs, Development and Partnerships, Ministry of Foreign and European Affairs, France (on behalf of **Annick Girardin**, Minister of International Development Cooperation and Francophonie, France)

Innovation implies structural challenges. It is a major opportunity for key dimensions of development such as climate change, natural resources, food security, conflicts, pandemics and migration. All these challenges require that we rethink our interventions and consumption models. We need to move from an "aid" approach to a "development finance" approach and from "aid efficiency" to "development efficiency".

Innovation also requires all the development stakeholders to be involved in a coherent and complementary way, including the private sectors. A recent report by two Innovation leaders, Emmanuel Faber (Deputy Director General of Danone Group) and Jay Naidoo (Former Minister of Nelson Mandela's government) provides 10 proposals for innovative inclusion of stakeholders. The French Development Agency (AFD), through its private-sector branch (Proparco), finances social businesses that are in essence more risky than traditional businesses but also more innovative. The G8's Social Impact Investment Taskforce, launched within the framework of the London G8 Summit, is working on the upscaling of these models.

France is actively involved in the identification of new financing mechanisms. It hosts the permanent secretariat of the Pilot Group on Innovative Finance, chaired this year by Chile. Innovative finance can be achieved through two pillars: (i) creating innovative mechanisms, such as the French "solidarity taxes" on flight tickets and financial transactions, which could be implemented in other countries and (ii) reinforcing the leveraging role of aid as a catalyst for other sources such as partnerships with the private sector.

We need to rethink official aid to make it more adapted to the new global challenges. The role of official aid is to overcome market failures and aid needs to be focused on where neither the private sector nor NGOs can play a role: in least developed countries and in risky or particularly complex areas. Legal and financial tools need to be innovative. The Framework Act on Development that has recently been approved by the French Parliament, in co-operation with all development stakeholders, supports innovative approaches, such as social entrepreneurship and social impact investment.

SESSION 1:

INNOVATION TO OVERCOME THE MIDDLE INCOME TRAP

Introduction: **Hans-Juergen Heimsoeth,** Ambassador, Permanent Representative of Germany to the OECD, and Chair of the OECD Development Centre

This Forum is part of a three-year cycle to shape the post-2015 agenda. The work of the OECD Development Centre through its policy dialogue initiatives and evidence-based, policy-relevant research plays a crucial role in those discussions. The 2013 Forum focused on “What is needed to end poverty?”. This year, the production side receives attention. Development challenges on the production side – such as lagging productivity levels, innovation and structural issues more generally – are crucial for developing countries to achieve sustainable, inclusive growth. However, those aspects were missing in the MDGs. In 2015 the forum will focus on how countries and firms can become innovators, what are innovative approaches to development aid and how innovation can contribute to inclusive growth.

Mario Pezzini, Director, OECD Development Centre *[Moderator]*

The *Perspectives on Global Development* series was launched by the OECD Development Centre in 2010 with the then provoking topic “shifting wealth”, a shorthand for the increasing economic weight of emerging and developing countries in the world economy. The following editions of the report have focused on the important aspects of social cohesion and industrial policies in a shifting world. This year’s edition also studies shifting wealth and the changes in its patterns, concluding that shifting wealth drivers (particularly demand from China) may not be enough for developing countries to climb up the income ladder. The 2014 report also shows that each region and each country faces different development conditions, including challenges and opportunities. These conditions have to be addressed differently in each country.

Presentation of the 2014 *OECD Perspectives on Global Development: Boosting Productivity to Meet the Middle-Income Challenge*

Carl Dahlman, Head of Global Research, OECD Development Centre

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"Shifting wealth", the shift in global economic activity, is happening not only in terms of GDP, but also in terms of consumption, investment (domestic and foreign) as well as exports and imports. The process started to accelerate in the 2000s and peaked in 2009 (during the global financial and economic crisis). However, more recently the differential rate of economic growth between non-OECD and OECD economies has been shrinking. Moreover, interest rates in emerging economies are rising (which is related to the tapering of the quantitative easing in the United States), making the economic situation in these countries even tougher. Even at their higher rates of growth since 2000, many countries will not converge to OECD average income levels by 2050 – including some which are currently upper-middle income countries, such as Brazil, Mexico and South Africa.

This raises the question of whether these countries are in the so-called "middle-income trap". The report argues that there is no agreed, common framework to identify "the trap", but evidence does show that many middle-income countries face sustained periods of lower economic growth. Growth slowdowns are often associated with significant slowdowns in total factor productivity and therefore the report focuses on productivity.

Productivity slowdowns can be associated with difficulties to move up the value chain, away from a growth path which is driven by low-cost labour and factor accumulation to one which is driven by innovation. In many of today's middle-income countries, things which may have led to increases in productivity in the past may no longer be effective. For example, the boost provided by the demographic dividend is fading and labour inputs may now be decreasing due to ageing populations. And the efficiency in the use of labour is declining in some countries. However, despite these trends, many middle-income countries still have a lot of potential to exploit "traditional" drivers of growth by shifting labour from lower to higher productivity sectors and fully reaping factor accumulation-led growth. For example, South Africa has low rates of labour participation, and unemployment rates are around 25%. Also, most middle-income countries still have significantly lower capital stocks than advanced countries.

Productivity levels in middle-income countries are still very low compared to the OECD average. The gap is even widening in some countries – including Brazil, Mexico and Turkey. In 2008, labour productivity was below 30% of that of the United States in all middle-income countries. The findings in the report are based on detailed data analysis to assess productivity and competitiveness: Productivity is examined at the macro level to identify its contribution to overall economic growth and also at a more detailed level for up to 18 manufacturing and 16 services sectors in over

40 countries. A special feature of the report is that it also studies productivity, technical efficiency and mark-ups at the firm level for nine countries – the BRIICS (Brazil, the Russian Federation, India, Indonesia, China and South Africa) plus Columbia, Cameroon and Senegal, using data from over 1 million firms. It also investigates these competitiveness indicators across regions within countries.

The report suggests that middle-income economies can boost productivity by (i) diversifying into higher value-added sectors in agriculture, industry and services; (ii) innovating by tapping global knowledge but also by developing domestic capabilities; (iii) reforming product, labour and financial markets, and developing skills; (iv) fostering competitive service sectors. Developing services has potential in developing countries as they can support productivity improvements in other sectors such as manufacturing; demand for specialised services is increasing with development and services can increasingly be exported.

The forces to specialise generally prove to be stronger than the forces for diversification. This can lead to absorption challenges and rents. The “shifting wealth” process created a commodity price boom that may have fostered specialisation too early for some countries’ stage of development. As an example regarding international trade, in the case of the BRIICS, except for China and India which are still far from high income levels, Brazil, the Russian Federation, Indonesia and South Africa all experienced exports specialisation. This suggests that these natural resource-rich countries need to foster diversification. Many Latin American countries have a strong focus on natural resource-based exports and thus also face the challenge of diversification.

Even the more advanced middle-income countries still have a lot of room for technological catch-up on innovation. Besides better integration into the global trading system and tapping foreign knowledge through trade, foreign direct investment and other means, countries also need to develop capabilities to innovate new products and processes to better suit their own needs, and create their own competitive edges. China stands out among emerging economies by being already the world’s second biggest R&D investor, after the United States.

Governments also need to prioritise social and environmental sustainability in their development strategies. On the social side, this includes ensuring equal opportunities and developing effective regional policies to support more equitable growth and reduce regional disparities. Inequality is increasing in some of the BRIICS (e.g. in China, India, Indonesia and South Africa). It has, however, gone down in Russia and Brazil. Moreover, a disgruntled middle class could jeopardise convergence. Full participation of the middle class is crucial to sustainable economic development: they provide the educated labour supply and the entrepreneurs required for modernisation; and are the backbone of domestic consumption.

Isher Judge Ahluwalia, Chairperson, Board of Governors, the Indian Council for Research on International Economic Relations (ICRIER), India

ICT-enabled innovation had allowed India to leapfrog and develop a sophisticated service sector. This was possible thanks to the long-term development of higher education institutions, particularly in engineering, which started first in southern India and then developed elsewhere in the country. The development of the ICT sector also benefited from the know-how gained by the Indian diaspora working in hi-tech sectors abroad, particularly in Silicon Valley. These links to the diaspora community were particularly pivotal as India was a closed economy at the time. The ICT-enabled service sector was also able to take off as it wasn't hampered by the physical infrastructure constraints that have limited the development of India's manufacturing sector. The private sector, rather than the state, played the driving role in developing the ICT-sector.

India's manufacturing sector, by contrast, has been constrained by poor physical infrastructure and inflexible labour legislation. While state governments can have their own labour laws, legislation must be endorsed by central government. So far, no state law regarding labour legislation has been endorsed, largely due to pressure from strong unions, although Rajasthan has recently submitted a proposal. This will be the first state law proposed since the new government came into power, and is therefore seen as a test case. If successful, more flexible labour legislation could spread throughout India due to the demonstration effect.

There is large scope for innovation in the long-neglected urban sector, which can be supported through innovative financial mechanisms. For example, in some cases in India, central and state government funds have been devolved to city governments for urban development, conditional on certain reforms and in combination with capacity building. Incorporating IT into government processes, such as e-procurement, can also help make people more accountable and address corruption problems.

In the next 40 years, the proportion of working-age population in India will increase, creating a need for development that is employment intensive, which in turn will require building up relevant skills in the workforce. Decentralisation, transparency and ICT can all contribute, but ultimately what make the most difference are human leadership and a change in mind-set.

Mario Cimoli, Director, Division of Production, Productivity and Management, United Nations Economic Commission for Latin America and the Caribbean (UN-ECLAC)

Latin America has experienced strong growth in the last decade, but this has not been accompanied by growth in productivity. There are now questions about whether the huge social spending that has been seen in the region is sustainable, given the poor productivity performance and the effect this could have on long-term economic growth.

Greater labour market flexibility, education, and integration into global value chains are all important components, but these alone are not enough to increase productivity. There is already a large degree of labour market flexibility in many Latin American countries, and this has not led to productivity growth. Countries in the region need new industrial policies. Innovation is, of course, important but governments need to select certain sectors to support. India's experience with the pharmaceutical sector is an example of how active government policy had played a pivotal role in supporting the growth of a sector, as a result of which India is now a world leader in the generics market.

Latin American countries could learn from the United States, which has an industrial policy, although it is not referred to by this term. Similarly, other OECD countries such as Germany are aiming to spend 5% of GDP on research and development (R&D), whereas the figure for Latin America is closer to 0.6%. We need a new roadmap for development which is practical rather than ideological, and which includes roles for the market, public-private partnerships and intervention by the state, in order to boost productivity in the region.

Pierre Ndiaye, Director, Prevision and Economic Studies of the Ministry of Economy and Finance, Senegal (on behalf of **Amadou Ba**, Minister of Economy and Finance, Senegal)

Part of the growth problem in Senegal is that it faces significant difficulties in being integrated into international exchange of goods, services and knowledge. It has a big informal sector with a lot of potential to foster stronger growth. The informal sector makes up around 90% of all jobs in all types of economic sectors (agriculture, mining, manufacturing and services). Many of the informal workers have important professional skills, but difficulties to bring their businesses to the market.

In Senegal "informal" is "normal". Therefore, reforms should aim at improving the conditions for informal businesses and workers. The informal sector needs to be supported to facilitate its connections with foreign markets and lower costs of production, particularly energy costs. Moreover, Senegal has a very rigid labour market and access to finance is an issue of concern and dampens growth dynamics.

Although Senegal is still a lower middle-income economy, it does face the risk of running into a middle-income trap: not being able to reduce the per capita income gap with advanced economies. Senegal would need to triple its growth rate of recent years in order to reach per capita income levels of advanced economies by 2050. Senegal has to do more if it wants to accelerate industrial output and growth and has prepared a set of tools and a new development strategy helping the country going forward. The strategy includes tools to foster more inclusive growth, particularly targeted towards the large informal sectors. The strategy aims at promoting agri-businesses and growth in various export sectors (including mining and services).

Recent reforms have already improved the business environment in Senegal. About 30 pending reforms to further improve the business climate will make it possible in Senegal to accelerate growth considerably. Among others, targeted policies to regional and sub-regional markets, the development of trade hubs, hubs for wholesale businesses for crops and specific support for SMEs are among the reforms under way. The role of the OECD through its advice and analyses is important for Senegal to identify the right policies going forward.

Discussion

Demand will be an important variable for countries aiming to graduate from middle-income to high-income levels. The BRIICS countries stimulated global demand during the crisis through measures such as expanding credit. However, more recently, the demand for commodities has been falling, and commodity prices have therefore fallen. Increasing demand will be particularly important in countries which still have the youth dividend to reap. India’s potential youth dividend could become a time-bomb if there is no productive employment for these young people coming onto the labour market. In the case of Senegal, ECOWAS represents a potential market of 90 million people, and in addition to this a growing middle-class is demanding goods which currently need to be imported. Brazil has supported domestic demand, but not productivity, and this is now a problem for the country.

Businesses in middle-income economies will need medium-level professional skills, such as technicians, which are not provided through higher education but rather through technical and vocational education and training (TVET). Some countries are facing this challenge of skills mismatch, where higher education graduates need to be re-trained with more practical skills after university. The private sector needs to be a close partner in skills development. To address the skills challenge lifelong learning, continued training and flexible pathways for training and education all have a role to play.

In some countries policies such as offering government-provided services, including premises, in exchange for starting the process of formalisation has been successful in addressing the informal sector. The informal sector is often sustained due to high transaction costs associated with becoming formal (e.g. registration procedures, prohibitive tax regimes etc.). Mario Cimoli argued that industrial policy could be used to create new jobs and new sectors that could absorb people from the informal sector, thereby reducing its share in the economy. Isher Ahluwalia offered a word of caution to this policy, arguing that India’s manufacturing sector is littered with failed examples and that vested interests should not be underestimated when ”picking winners”. Any government support for particular industries or sectors needs to be time-limited from the outset.

Presentation of the Commitment to Development Index

Owen Barder, Senior Fellow & Director for Europe, Center for Global Development

The Center for Global Development's Commitment to Development Index analyses the extent to which OECD countries pursue development-friendly policies. There is more in development co-operation than just giving aid. When discussing development co-operation policies it is crucial to include the policies of OECD countries as a whole: trade, finance, environment, migration and technology transfer and support for innovation, among others.

Launched in 2003, Index analyses where OECD countries stand with the impact of their policies on the development of other countries. It is a major development co-operation assessment tool for OECD policy makers who should be astonished by, on the one hand, the gap between their rhetoric or narrative that policies should be more coherent and on the other hand, the poor impact of their policies in security, migration and intellectual property rules vis-à-vis developing countries.

Today the reflections of development co-operation actors no longer focus only on the amount of money rich countries need to give to poor countries. The international community now also discusses how to tackle the structural impediments to growth, how to achieve shared prosperity and the importance of new actors, new approaches and new kinds of partnerships. Within this framework one must reaffirm the following three assertions: (i) development policy is more than aid; (ii) there is a growing gap between the rhetoric and the development policies that should be bridged; (iii) a lot can be learnt from peer reviews. Hopefully, the OECD will continue leading the process of information exchange on policy issues.

Introduction: Erik Solheim, Chair of the OECD Development Assistance Committee (DAC)

We need growth and that growth needs to be inclusive. This session will thus look at innovative approaches to that end. As an illustration of the magnitude of the problem, every month sees an additional 1 million young people in Africa joining the job market. This means that we need to create an additional 12 million new jobs every year in Africa alone just to deal with that dimension.

Shada Islam, Director of Policy, Friends of Europe *[Moderator]*

The debate has now moved on from official development assistance (ODA) to a new discussion that looks beyond ODA to also consider elements such as ownership, partnership and new modes of working together.

Dorothy Ng'ambi Tembo, Deputy Executive Director, International Trade Centre

The International Trade Centre's (ITC) approaches can nurtur business and help it better connect with value chains. Based on lessons of experience on the deficiencies of *ad hoc* interventions, the approach now focuses on small and medium enterprises (SME) competitiveness and exports, as SMEs are the backbone of local economies and major drivers of innovation and employment. The essential thrust of work is to take a value chain approach as some 80% of global trade is value chain trade and some 60% is in intermediate goods. The IFC therefore seeks to improve productivity by identifying key areas for action by looking at backward linkages through the value chain. This work not only helps to connect up previously marginalised groups (e.g. in the fashion industry), but helps promote regional integration and pan-African approaches. The results to date are promising and suggest an approach that can be more broadly replicated.

Frank Matseart, CEO, Trademark EastAfrica

Trademark EastAfrica (which functions more as a private sector operator than a traditional donor) focuses on small businesses and helps them to link up to markets. Transport inadequacies represent, for example, a huge barrier to trade, where a 10% reduction in transport costs can lead to a 25% increase in trade. Trademark EastAfrica promotes improved access to markets (e.g. by reducing the thickness of borders), improving business competitivity (e.g. though a fund supporting logistics innovations) and by improving the trade environment (e.g. through streamlined customs systems and harmonised trading standards). Throughout, efforts are made to make these approaches more inclusive, e.g. by focusing on women enterprises and enterprises in the informal economy.

Christiane Bögemann-Hagedorn, Deputy Director-General, Federal Ministry of Development Co-operation, Germany

Jobs, especially for young people, are a key engine for inclusive growth and poverty reduction. Youth unemployment is now a major problem, with economic, social and political implications. Germany is contributing to efforts to tackle this through investments supporting high quality job creation. The main components of the strategy include efforts to boost demand for labour e.g. through an improved business climate, initiatives to strengthen the supply side through improvements in skills, training and capacity development and actions to strengthening the functioning of labour markets. The focus is not just on government actions, but also on the private sector and civil society: after all, most jobs are not created by government. The National Employment Pact in Egypt represents an innovative approach to tackling the mismatch between the unemployed and vacancies for motivated and qualified youth, strengthening the functioning of job centres to bridge the gap between vacancies and job seekers.

Owen Barder, Senior Fellow and Director for Europe, Centre for Global Development

Development impact bonds are a key opportunity for development. Aid agencies should support private investment in developing countries, as there is still a massive shortfall in development finance, but traditional means of support such as loan guarantees are not the best way of supporting badly needed investment. The rationale for guarantees is that market failure results in risks being too high, such that aid agencies underwrite that risk. Yet the private sector, not governments, is the best judge of risk and aid agencies should not override their judgement – to do so would result in more debt or unsustainable business. A good alternative would be to use concessional ODA in the form of development impact bonds to increase the return on investment, thereby helping the private sector to take up more investment opportunities, with accompanying benefits not only in terms of more private sector money but also in terms of improved management and skills. The focus should therefore be on increasing returns and not on reducing risk. The former accentuates the incentive to take risks by the private sector whereas the latter can blur the real risk facing private enterprise and insulate it from the discipline resulting from risk.

Open Discussion

There was some discussion over the extent to which guarantees can crowd in the private sector and facilitate market involvement. More attention should be devoted to the best ways and means for public policy and instruments to close the ”viability gap” and to get to positions where the private sector will invest. Equally, more effort should be given to strengthening trade support institutions and south-south collaboration to unleash potential for growth and employment.

Efforts to support more inclusive growth also need to take account of major trends and shifts such as massive rural to urban migration, the dominance of extractive industries in certain countries as well as the growing role of new players such as China. In identifying their value added, donors need to take such developments fully into account and promote a more collective engagement with and involvement of all stakeholders. Donors also need to develop less onerous approaches to working with the private sector (e.g. reporting requirements) and see the situation through private sector perspectives, paying more attention to specific issues such as competition, productivity, viability, predictability and transaction costs rather than broad generalities. The discussion needs to be with, rather than about, the private sector.

SESSION 3:
INNOVATION POLICIES FOR INCLUSIVE DEVELOPMENT

Dirk Pilat, Deputy Director for Science, Technology and Industry, OECD *[Moderator]*

The topic of innovation policies for inclusive development is at the heart of the OECD project “Innovation for Inclusive Growth” (http://oe.cd/inclusive). Innovation has long been identified as a source of growth, as it fosters competitiveness, productivity and job creation. So far the effect of innovation and its policies on inclusiveness and the question of how innovation can support more inclusive development have not been comprehensively addressed. Three different dimensions arise: first, what is the influence of innovation on different groups of society and can policies be identified that are more pro-poor than others (social inclusiveness)? Second, what is the impact on different parts of the economy (industrial inclusiveness)? And third, how are equalities between urban and rural areas or neighbourhoods in the same city affected (regional inclusiveness)?

Ramesh Mashelkar, Chairman of the National Innovation Foundation of India, President of the Global Research Alliance, India

One major question that has to be addressed is how innovation policies can support developing countries in achieving competitiveness without compromising the three dimensions of inclusiveness. However, it is necessary to recognise that global competitiveness (excellence) and equity (affordability) are not mutually exclusive: inclusive innovations have an important role to play in reconciling these two aspects. Focus should be put on producing quality products for less rather than on the mistaken idea of seeking to supply low-income markets with second-rate goods and services. Public-private partnerships in the form of grant challenges might be one tool to achieve this objective of affordable excellence. Universities and research institutions can also provide substantial support to inclusive innovation initiatives. Given the large potential of the market for the poor, the private sector itself can most likely become a driver of inclusive innovation. Although there has been substantial progress in India, there is still a lot of untapped potential for more inclusive innovation initiatives. One main challenge is how to scale up inclusive innovations. This is closely linked to the issues of affordability, sustainability and quality. The process of spreading inclusive innovations has already started with growing interest from the business sector and the EU but has to be pushed further. This is not only relevant in the developing country context, but also for OECD countries. Finally, there is the issue of financing inclusive innovation. Finding a solution to these challenges will require innovation in innovation itself.

Subathirai Sivakumaran, Team Lead for Impact Measurement, Knowledge and Capacity Building, Business Call to Action, UNDP

Business Call for Action is an alliance between five governments (Australia, Netherlands, Sweden, UK and US), the UN and the Clinton Foundation, which aims at promoting inclusive business models that are competitive and have an impact on poverty alleviation. These inclusive innovation initiatives are distinct from "traditional" concepts of corporate social responsibility (CSR) in that for those businesses, the focus on inclusion is part of the core business. They observe that innovations take all kinds of shapes and forms when private sector firms work in the market for the poor resulting in unexpected product innovations. Creating products for excluded groups, however, is not sufficient as the bigger challenge of distribution of these products needs to be addressed. Moreover, inclusive innovation also means including the very poor in supply chains etc. In order to avoid obstacles when scaling-up initiatives, three points need to be taken into account. First, the iteration of business models is essential for success, but this is expensive and requires a high level of investment. This is problematic as usually high margins are not possible for these firms and profitability is not immediate. Second, the markets of the poor are different from traditional markets and distribution might require novel approaches (such as word-of-mouth distribution). Finally, governments and development agencies need to help building trust in these inclusive businesses by providing appropriate information, e.g. safety information. Additionally, attention must be paid to the measurement of results and impact evaluation as well as building capacity on the field level.

Yu Shi, Senior Economist and Deputy Coordinator, Ministry of Science and Technology, China

Supporting developing countries' quest for competitiveness might, in some cases, also promote inclusiveness. China's successful economic growth contributed substantially to inclusiveness lifting more than 10 million people out of poverty. However, the relation between competitiveness and inclusiveness is not simple. In some countries, especially those with an unstable political environment, inclusiveness might be critical. In order to achieve inclusive developments, the

Chinese government has identified five ways to enhance the contributions of innovation to inclusiveness: this includes policies to support public wellbeing, support for the agricultural and rural economy, policies aimed at addressing regional development, industrial development policies as well as support policies for small and micro enterprises. On the grassroots level, S&T organisations such as innovation incubators provide funds and technical consultation. A major challenge for policy makers at regional/local levels is often to select between short-term and long-term policy tools as this choice introduces a trade-off between visible, easily measured economic development in the short run and less tangible, longer term social benefits.

Carl Dahlman, Head of Global Development Research, Development Centre, OECD

Understanding the dynamics of inclusive innovation is important for four distinct reasons: first, market failures impede excluded groups from accessing certain basic goods and services. Second, some governments are already explicitly supporting inclusive innovation through the public and private sector. Third, domestic and transnational companies (TNCs) have recently begun to explore low income markets.

A common pitfall is that there is too much focus on supporting R&D for inclusive innovation and creating the initial prototypes. In order to have an economic impact, innovations need to be carried forward into production and mass dissemination. Hence, the issue of scaling-up and diffusion is of utmost importance. To this end, access to finance for producers as well as consumers and networks of suppliers and distributors has to be provided for. Moreover, developing information technology platforms to reduce transaction costs is crucial to facilitate massive scale-up and should be supported. Different agents in the innovation cycle have different strengths and weaknesses that need to enter policy design. Government can take on different roles in promoting inclusive innovation (direct actor, facilitator and/or co-ordinator); however, the private sector needs to be the main agent of inclusive innovation.

Open Discussion

In order to promote inclusive innovation, new strategies of regional and global co-operation are critical. There is high potential for South-South co-operation as developing and emerging countries can learn from the success stories of South Korea, China and India. Finally, intergovernmental co-operation and public-private partnerships can only be successful if emphasis is set on aiming for full product development rather than only initial product development.

CONCLUSIONS AND WRAP UP

Jon Lomøy, Director of the Development Co-operation Directorate, OECD

The development challenge is linked to having to run faster than those already running in order to move up the value chain and to make substantial inroads towards poverty reduction. Growth needs to be rapid, sustained and inclusive to meet massive challenges e.g. in the area of youth unemployment. Innovations need to scale up from pilot phases. All this requires a better partnership between policy makers and the private sector and a need to move the conversation to developing countries and to make it a conversation with the private sector rather than about it. These Global Forums on Development contribute to this. In fact, there is a unique opportunity for next year's Global Forum – which will focus on development finance – to make inputs to the July 2015 Financing for Development Conference in Addis Ababa and provide answers to the question of how best to use public finance to boost private investment and mobilise domestic resources.

Mario Pezzini, Director, Development Centre, OECD

Convergence between countries requires improving productivity and therefore rethinking innovation not only for products, technologies and production processes but also organisation, skills, etc. In this context, policies matter a lot. We need to discuss what we mean by industrial policies, but also to have a clearer vision of the role of unions, social policies and inclusion. The OECD is working on developing countries to bring these issues together. The Development Centre contributes to these debates by working on strucural transformation and areas such as local development to improve productivity and innovation (which will be the topic of the 2014 African Economic Outlook), and through two policy dialogue initiatives on (i) natural-resource based development and (ii) global value chains, production transformation and development.