MEETING OF THE OECD COUNCIL AT MINISTERIAL LEVEL

2005

KEY INFORMATION

OECD

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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The OECD is a unique forum where the governments of 30 democracies work together to address the economic, social and environmental challenges of globalisation. The OECD is also at the forefront of efforts to understand and to help governments respond to new developments and concerns, such as corporate governance, the information economy and the challenges of an ageing population. The Organisation provides a setting where governments can compare policy experiences, seek answers to common problems, identify good practice and work to co-ordinate domestic and international policies.

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OECD Publishing disseminates widely the results of the Organisation's statistics gathering and research on economic, social and environmental issues, as well as the conventions, guidelines and standards agreed by its members.

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Les questions clés

Table of Contents

Preface 5

World Economy

Economic Situation and Prospects 8
Energy and Investment 10
Key Indicators 12

Adjusting to Globalisation

Trade and Structural Adjustment 14
Services Sector Performance 15
Active Social Policies 16
Education for All. 18
The Role of SMEs 20

Trade and Development

The Doha Development Agenda 22
Reducing Poverty 24
Progress Towards the MDGs. 26
Coping with Climate Change 27
Co-operation with Partner Economies 28

Good Governance

Corporate Governance. 32
Building Trust in Government 34
Counteracting Tax Abuse in a Global Environment 35

Preface

Dear Minister,

This year's OECD Ministerial Council Meeting (MCM) will be held under the chairmanship of Göran Persson, Prime Minister of Sweden, with the overarching theme of "Enabling Globalisation". We live in an interdependent world – and that's a fact of life, not an option. Our challenge in facing the reality of globalisation in the international community is to enable all countries to reap its benefits while managing the inevitable adjustment process and its costs.

The information notes in this brochure provide background for the main topics that ministers will address:

i) **Implications of globalisation for the economic outlook:** *This session will focus on export markets and market shares of OECD countries, energy and commodity prices, and current account imbalances and their financing.*

ii) **Investing in energy:** *A joint meeting of the MCM and the International Energy Agency ministerial meeting will discuss how governments can improve the framework conditions to ensure timely investment in energy infrastructure that meets the tests of security of supply, economic efficiency, environmental sensitivity and affordability.*

iii) **Globalisation and structural adjustment:** *Ministers will address how OECD countries are adapting to rapid economic growth and technological development in major developing countries. The discussion will be based on the two key projects launched at MCM 2003 "Enhancing the performance of the service economy" and "Trade and structural adjustment".*

iv) **Millennium Declaration and Monterrey Consensus:** *This session will concentrate on the OECD's contribution to the follow-up and implementation of the commitments in these international agreements.*

v) **Trade negotiations under the Doha Round:** *Building upon the framework agreed in Geneva in July 2004 and the momentum generated by that agreement, ministers are likely to focus on how to advance the Doha Development Agenda, and on ensuring the success of the WTO Hong Kong ministerial meeting.*

Many important players from the emerging and developing economies have been invited to join the ministerial meeting. Indeed, discussions on the theme of "enabling globalisation" would not be meaningful without their presence. At the same time, how to respond to the challenges and opportunities of globalisation is an issue for the citizens of all our countries, not just for politicians.

With this in mind, I would strongly encourage you to participate in the OECD Forum 2005 which takes place on 2-3 May 2005 in Paris. The Forum is a "civil society summit" which brings together leaders of governments, business, labour, civil society and the media to discuss and debate the issues on the ministerial agenda.

I look forward to welcoming you to the OECD MCM and to the Forum where we can advance international co-operation to these ends.

Donald J. Johnston

World Economy

ECONOMIC SITUATION AND PROSPECTS

Global recovery set to regain momentum

The global recovery has been marking time, as the adverse effects of higher and more volatile oil prices worked their way through. While growth has barely slowed in the United States and the United Kingdom, notwithstanding a gradual return towards a more neutral policy stance, exchange rate appreciation has been taking a toll in the euro area, with some lag. In Japan, activity has stagnated, only partly reflecting slowing exports. Outside the OECD area, the expansion has remained robust, notably in China but also, despite some deceleration, in India, Latin America and Russia. Going forward, the conditions are in place for the global recovery to pick up momentum, including enterprise balance sheets and profits, which have strengthened markedly.

US economy continues to lead

In the United States, domestic demand has held up well in the third year of the recovery, with buoyant household consumption and business fixed investment. Despite dollar depreciation, imports have risen rapidly, but exports less so, exerting a drag on gross domestic product (GDP) and worsening an already wide current account gap. Employment creation, whilst cyclically sub-par, has gathered pace, and unemployment has shrunk further, although the turnaround in labour force participation is unusually slow in coming. Confidence and other forward-looking indicators point to growth at around potential in the near term.

Euro area has absorbed oil and exchange rate shocks with some difficulty

Growth in the euro area at large has been far less impressive and unemployment has failed to retreat from comparatively high levels. Performance has also been somewhat uneven across countries. In some, the modest expansion in activity was pulled mainly by external demand. Others face growing competitiveness problems. Nevertheless, domestic demand seems poised to gather strength, including where it has long languished. Business confidence remains above historical means, profitability is high and financing terms remain easy, portending an investment revival. Consumer sentiment is creeping up towards long-term averages, despite lingering labour market gloom. Against this backdrop, GDP growth can be expected to broaden and to move back up towards potential.

Japanese recovery has paused but should resume

In Japan, the new national accounts, resting on a sounder methodology, suggest that real GDP stopped growing after the first quarter of 2004, owing in equal measure to weakening export growth and faltering household consumption. Other indicators are more encouraging, however, and foreshadow a pick-up. The sustained rise in business investment is likely to continue, given buoyant machinery orders, and corporate profitability has improved. So have labour market conditions, with unemployment down to levels long not seen, a high job offers-to-applicants ratio, and regular employment growth becoming less reliant on part-time jobs. Wage growth, however, remains in negative territory, casting some doubt on how rapidly household consumption may regain strength.

Removal of monetary stimulus warranted where cycle more advanced

With some cyclical slack enduring in most large OECD economies, wage growth generally remains moderate and core inflation low or broadly on target. Against this background, and as productivity growth seems to revert to a more sustainable pace, the US Federal Reserve's steady and well-anticipated march towards neutrality is gradually withdrawing the exceptionally ample stimulus injected earlier on. Greater cyclical slack in the euro area and persisting underlying deflation in Japan would warrant continued, if vigilant, patience before a return to a less accommodative posture is initiated.

Sustainability of public finance needs to be restored

Fiscal positions remain precarious in most OECD countries, both in headline terms and, more worryingly, when adjusting for the cycle and for various types of one-offs or omissions. Meanwhile, demography is starting to weigh on tax revenue and to boost public spending in some countries – most notably in Japan – or will shortly do so. The ongoing pension and healthcare system reforms, and more, are therefore needed to put public finances back on a sustainable course. More immediately, while in some countries cyclical conditions may call for incremental rather than abrupt fiscal adjustment, spreading it out too much could lead to an unexpectedly sharp back-up in long-term interest rates, with far more deleterious effects on activity.

ENERGY AND INVESTMENT

Global energy demand has risen sharply

Every economy requires energy to function. Last year, global oil demand was equivalent to 82.4 million barrels per day (mb/d). This was up 2.6 mb/d from the previous year, the biggest annual jump in recent times and in line with the buoyant pace of global output growth in 2004. A large chunk of the demand increase was associated with the rapid development in energy-intensive economies, notably China. Energy demand in the OECD area also rose sharply, especially in North America. Looking ahead, the International Energy Agency's (IEA) *World Energy Outlook* reference scenario, which assumes no change in policy, anticipates a 60% increase in global energy needs to 2030. Assuming more decisive progress in energy conservation, such as higher vehicle fuel efficiency and faster development of alternative energy sources, the increase in demand could be reduced by 10 percentage points. Future trends, however, are invariably uncertain.

Supply has struggled to meet demand, resulting in higher and volatile prices

Energy supply has struggled to meet rising demand. This is partly linked to a legacy of insufficient investment over the past decade, in extraction capacity and in refining and energy-distribution capacity. Low investment is due to earlier weak prices and mistaken expectations that these would persist, a regulatory environment that restrained investment and an uncertain corporate governance framework in certain producer countries. Geo-political turmoil has not helped the investment climate either. As a consequence, and given the long lead times applying to capital investment in the energy sector, current capacity to boost production in response to even transitory demand fluctuations is very limited. This situation has resulted in higher and volatile energy prices. Moreover, these market dynamics and generally heightened uncertainty may be inhibiting investment in extraction, refining and energy-distribution facilities, perpetuating short supply.

Macroeconomic costs contained so far, but long-term impact could be large

Higher and volatile energy prices have dampened near-term growth prospects and boosted inflation in the OECD area; perhaps even more so outside the OECD. Inflation expectations, however, have remained well-anchored, muting the monetary policy response and the ultimate impact on output. Today's much smaller intensity of energy in output in OECD economies, compared with the early 1970s, has also served to contain the size of the economic impact from higher energy prices. Nonetheless, energy prices, particularly oil, remain above most estimates of their underlying equilibrium and are still fluctuating wildly, which is bearing on confidence. There is a risk, therefore, that high energy costs may yet impact more strongly on the near-term economic outlook. Moreover, the long-term consequences of a further abrupt rise in energy prices could be very costly, to the extent it leads to a premature scrapping of capital stock and thus a reduction in an economy's productive capacity.

Increased investment in energy is needed

To limit the risk of excessive rises in energy prices stifling growth in the future, large investment in the energy supply chain will be needed to convert potential resources into available supplies. In a well-functioning economy, rising energy prices themselves should stimulate stronger investment as well as better energy conservation. But a variety of institutional factors may be hampering the development of energy supply in the long term. Recent estimates by the IEA, based on projected global energy requirements growing by an average 1.7% per year to 2030, put the cumulative investment needs in the order of USD 16 trillion. This is equivalent to about 1% of global GDP per year, although it is unevenly distributed across countries and energy sources. China accounts for nearly one-seventh of the global total, and, by energy source, the capital-intensive electricity sector dominates.

Optimal investment level needs to consider benefits and costs of higher capacity

It is in the interests of both consumer and producer countries to facilitate investment flows to those with the least costly investment opportunities per unit of energy supplied. In this regard, restrictions on foreign direct investment (FDI) are harmful, especially in countries with large known energy resources and low national savings. In OECD countries, barriers to FDI in the electricity generation sector are on average three times higher than in other sectors and in some, foreign investment in the sector is not permitted. Governments should lift these obstacles to foreign investment. More generally, the economically viable level of energy investment projects forthcoming depends on the investment framework and climate. Here, a more stable macroeconomic environment and transparent and predictable regulatory conditions would reduce certain risks attached to long-term and immobile investments, enabling more attractive financing conditions. Better energy market information and less regulatory segmentation of markets may also improve the efficiency of investments.

Policy reform on demand side should also play a role

While insufficient production capacity is an important factor behind recent high and volatile energy prices, demand-side factors have also played a part and are amenable to policy reform. Energy subsidies, for instance, artificially boost demand and are harmful to the environment. These should be eliminated, where necessary also using other means to effectively meet the societal objectives that energy subsidies are intended to achieve. In addition, prices should reflect the environmental damage resulting from energy use. This may require reform of energy taxes, the use of tradeable emission rights and, in cases where these instruments are impractical, higher energy efficiency standards. This would encourage energy conservation and provide an incentive to invest in research and in developing cleaner energy sources and new technologies that use energy more efficiently, thus moderating demand.

KEY INDICATORS

Making information count

In a rapidly changing, increasingly interdependent world, a host of daunting issues and opportunities call for complex cross-boundary responses. Productive debate and decisions require comprehensive, trustworthy and understandable information. Over the past decade, several OECD countries and the European Union have launched initiatives to establish one or more sets of "key indicators" to evaluate the evolution of economic, social and environmental phenomena, as well as the quality of policies undertaken by public authorities. In several cases, such indicators are widely used to perform benchmarking exercises and to assess relative performances of national or local communities.

Statistics, knowledge and policy

The OECD is acting as a catalyst to convene and promote research- and information-sharing on these issues, allowing countries to compare strategies intended to measure and assess the overall "position" or "progress" of a certain political entity (country, region, etc.) *vis-à-vis* other similar entities. The first OECD World Forum on Key Indicators, "Statistics, Knowledge and Policy", was held in Palermo (Italy) in November 2004. The event was sponsored by the Italian government and attended by 540 people representing various constituencies from 43 countries; it was also followed *via* Web-casting by several thousand people all over the world. The success of this Forum sent a clear message of the importance of statistical information to create common knowledge and support public policies.

Fundamental infrastructure

Unfortunately, statistics are too frequently taken for granted or purely seen as an input for other policy processes. On the contrary, the development and the use of statistics represent a fundamental infrastructure for modern societies and require special attention from an institutional and policy point of view, both at national and international level. In particular, the transparency and accountability of public policies, the people's understanding of the characteristics and the evolution of their societies, the role of the media in contributing to the development of a common knowledge base: all these issues require a special effort by modern societies to promote high-quality statistics and to use them, among other things, to develop a shared understanding of the state and the evolution of society and to build accountable decision-making processes based on reliable statistical evidence.

Facing the facts

To contribute to the assessment of the overall development of OECD countries, the Organisation published in March 2005 the first edition of the *OECD Factbook: Economic, Environmental and Social Statistics*, which presents, in an integrated way, a carefully selected range of statistics covering ten broad thematic areas (population and migration, macroeconomic trends, economic globalisation, prices, labour market, science and technology, environment, education, public policies and quality of life). The 2005 issue also contains a section highlighting energy, developed in co-operation with the International Energy Agency.

Adjusting to Globalisation

TRADE AND STRUCTURAL ADJUSTMENT

With the emergence of new sources of competition, accelerating technological change and shifting societal concerns, adjusting to globalisation is an issue of concern to both developed and developing countries. Against this backdrop, an OECD study on trade and structural adjustment was developed from a Swedish proposal at the OECD Ministerial Council Meeting in 2003 and was launched as a horizontal project by the Council after deliberations in relevant substantive committees. The request from the Council called for a sector-focused and forward-looking analysis of trade and structural adjustment, supported by country-specific case studies. The goal was to complete the project in time for the MCM in 2005.

The aim of the study is to identify, for both developed and developing countries, the requirements for successful trade-related structural adjustment by reallocating labour and capital to more efficient uses, while limiting adjustment costs for individuals, communities and society as a whole. Eight sectors have been chosen for particular attention: agriculture, fisheries, textiles and clothing, steel, shipbuilding, motor vehicles, health services and international sourcing of IT and business process services.

Role of appropriate policy framework

The study finds that in tackling the challenge of structural adjustment, all countries, developed and developing – albeit with differing degrees of emphasis – will benefit by adopting at the national level an appropriate policy framework: macroeconomic policies which promote stability and growth; labour market policies which help develop workers' skills and which facilitate a smooth transfer of resources from declining to expanding activities; an efficient regulatory framework; a sound institutional and governance framework; and liberal trade and investment policies which support structural adjustment by contributing to growth, innovation and competitiveness. For the poorest countries, the study emphasises the importance of appropriate institution building and the development of human and physical capital.

The study further emphasises that governments are strongly encouraged to pursue reform across different policy areas in a complementary way – to reduce resistance to change, by helping ensure that those disadvantaged by one reform benefit from another, and to foster synergies between policies. Governments are also encouraged to rely, as much as possible, on generally applicable measures to address adjustment costs, including through the tax and social security system, for reasons of both equity and efficiency.

The study finally underscores that multilateral efforts including through the Doha Development Agenda, the work of the international financial institutions, donor co-ordination and greater efforts to enforce core labour standards are of particular importance in promoting the mutual interests of trade liberalisation, locking in domestic reform and building mutual confidence between enterprises and the societies in which they work.

SERVICES SECTOR PERFORMANCE

The services sector now accounts for over 70% of total employment and value added in OECD economies. It also accounts for virtually all employment growth. But despite its growing weight, productivity growth in services has been slow in many countries and the share of the working-age population employed in services remains low in several countries. To improve the growth prospects of OECD economies, a more dynamic services sector is needed.

The experience of Australia, Canada, the Slovak Republic and the United States shows that this is feasible; in these countries, services have made a large contribution to employment and productivity growth over the past decade. Moreover, many of the jobs that were created involved highly-skilled workers. Services are increasingly tradeable. Analysis of trade and occupational data for several OECD countries to determine what share of total employment could potentially be affected by international sourcing of IT and ICT-enabled services has yielded estimates close to 20%.

Improving the business environment

Addressing these challenges will require a combination of policies. The opening of domestic and international services markets is key, as it creates fresh opportunities to develop new services, meet emerging demands and increase employment. It also increases incentives to innovate and improve productivity. OECD work shows that the benefits of international trade and investment in services are highly significant. Both unilateral steps, such as reducing barriers to foreign direct investment, and multilateral steps, notably through the Doha negotiations, are important to open international services markets.

Helping workers adapt

Effective labour and social policies are essential to help workers adapt to the shift to services. High labour taxes are particularly burdensome for the growth of services, as they affect job prospects for low-skilled workers and the development of a personal services sector. Overly strict employment protection legislation can also be a barrier to employment and productivity growth in services. Education policies are important to help provide the qualifications needed by services workers, but will need to be supplemented with partnerships and co-financing by firms, workers and governments to foster lifelong learning.

Fostering innovation

Innovation policies remain ill-adapted to services. Public research and development (R&D) often does not address the needs of services and the links between services firms and public research institutions are poorly developed. Intellectual property regimes for services may also need further consideration, and will require a careful balance between innovation and diffusion of service innovations. To seize the benefits of ICT in services, effective competition in infrastructure, network services and applications is needed. More can also be done to enhance the trust in electronic business, *e.g.* by improving regulatory frameworks. Reforming regulations that date from a time before electronic business was an option is particularly important.

ACTIVE SOCIAL POLICIES

Social policies have traditionally aimed to alleviate social distress through benefits paid to individuals and families in a few, well-defined circumstances: temporary unemployment, sickness and disability, and retirement during old age. While this traditional model for social policies has helped to reconcile economic growth and social development, it rested on assumptions that no longer hold and is now running up against its limits.

At their meeting on 31 March-1 April 2004, OECD social policy ministers agreed on the need to become more ambitious faced with the challenges posed to social protection by ageing populations and globalisation. Active social policies go beyond insuring individuals against risks, towards investing in peoples' capabilities, and enabling them to realise their full potential throughout their lives. Their goal is to encourage people to participate as fully as possible in economic and social life.

There are three main goals of active social policies.

Giving children the best possible start in life

The first is **giving children the best possible start in life**. Children who grow up in poor families are more likely to do poorly at school, to struggle to find a job and to be dependent on social assistance when they become adults. A mixture of reforms to the tax and transfer system, childcare support and help for working parents to reconcile their work and family responsibilities is needed. These policies would also create more favourable circumstances for raising fertility rates, whose currently record-low levels could impose large social and economic costs on society. Policy priorities are:

- *Investing in children,* including early childhood intervention programmes.
- *Boosting maternal employment*, for example, by adjusting tax and benefit systems so as not to discourage second earners.
- *Reconciling work and family responsibilities* through childcare provision, parental leave and family-friendly workplaces.
- *Creating a framework favourable for raising fertility rates*, for example through policies that allow young couples to get a secure footing in labour markets.

Finding quality jobs

The second goal is **helping prime-aged individuals overcome barriers to finding quality jobs.** Getting the jobless into work, and helping the disadvantaged to acquire the skills to get higher pay, are the best ways to reconcile economic and social progress. The success that some OECD countries have achieved in slashing some benefit rolls and moving people into jobs needs to be extended to other groups such as lone parents and those with disabilities, through tailored interventions that give greater emphasis to labour-market integration. Active social policies, however, are not a silver bullet: not everyone can be expected to participate in the labour market, and getting people into jobs will be insufficient to avoid exclusion if people do not keep the jobs, if the income from work is not high enough to escape poverty, or if there is little prospect of skills development and career progression. A comprehensive strategy against poverty and exclusion among prime-aged persons needs to combine:

- Completing the welfare-to-work agenda, in particular with regard to lone parents and, in most countries, people with disabilities.
- Improving "welfare-*in*-work", including through policies to make work pay and to improve the career prospects of low-paid workers.
- Strengthening the effectiveness of social programmes, by extending coverage and take-up of existing programmes to all persons in need, and assuring the adequacy of the benefit provided.
- Promoting the coherence of different policies affecting poverty across departments and levels of government.

Protecting the well-being of the elderly

The third goal is **protecting the well-being of the elderly by enhancing their participation in economic and social life.** Pay-as-you-go pension systems have been crucial to improvements in the well-being of the elderly, but their rising costs threaten their financial sustainability, as well as the capacity to invest in younger generations. Moreover, social policy has been less successful in addressing the barriers that older workers face in retaining work, the risk of disability and isolation in old age, and those elderly persons without their own pension rights sometimes still face a high risk of poverty. Priority areas include:

- Limiting the costs of old-age pensions on public budgets, by promoting diversification of retirement income.
- Favouring a longer working life, through a combination of steps to close pathways to retiring early, to reverse disincentives to retire early and to encourage employers to hire and retain older workers.
- Improving quality and access to long-term care, through policies to support informal carers, to increase the availability of care to frail elderly at home, increase users' choice among alternative types of provision and better monitor care quality.

OECD societies need to look beyond public programmes to achieve social goals. Private financing and delivery of social protection can result in more efficient and responsive forms of social protection, just as non-government organisations can often mobilise resources and enthusiasm to an extent unavailable to publicly-run organisations. But changes in the welfare mix also raise difficult challenges for public policies – *e.g.* about the extent and fairness of access, and the quality of the services provided – calling on OECD governments to assume the more complex functions of steering the overall system.

EDUCATION FOR ALL

In April 2000, 164 countries gathered in Dakar, Senegal, for the *World Education Forum* where they adopted the *Dakar Framework for Action, Education for All: Meeting Our Collective Commitments*. This document commits governments to achieving quality basic education for all by 2015 or earlier, with particular emphasis on girls' education, and includes a pledge from donor countries and institutions that "no country seriously committed to basic education will be thwarted in the achievement of this goal by lack of resources".

High-quality lifelong learning for all

The OECD has been working for the past 40 years to help its member countries achieve high-quality lifelong learning for all that contributes to personal development, sustainable economic growth and social cohesion. Capitalising on this experience, since the mid 1990's the OECD has progressively developed working relationships with non-member countries to facilitate the achievement of the Dakar Education for All objective. This was done notably by:

- Conducting policy reviews of educational systems of developing countries;
- Integrating non-member economies into the Programme for International Student Achievement (PISA);
- Including several developing countries in joint work with the World Bank and UNESCO for World Education Indicators (WEI);
- Initiating a number of projects relating to the special education needs of children with significant disabilities; and
- Developing "Guidelines on quality provision in cross-border higher education".

In several countries that have undergone policy reviews, there has also been an important impact on legislation. Recommendations from reviews have usually led to continuing co-operation through follow-up activities in specific areas and have also permitted member countries and international financial institutions to enter into fruitful co-operation agreements.

Another important aspect of education work has been setting up national, regional and international networks of experts and policy makers in the areas covered by individual activities. To allow for greater synergies and to broaden the horizon beyond the programmes and regions covered, the OECD will be organising a Global Forum on Education in partnership with the Chilean authorities on 24-25 October 2005.

As co-ordinator for education policy in the Stability Pact for South Eastern Europe, the impact of OECD work has also included better targeting of international aid to the region to assist sustainable reforms for more responsive education systems

Primary education for all

One of the goals of Education for All is to achieve universal primary education for all children, including those with disabilities, by 2015. A major problem in achieving this goal is a lack of data on the numbers and proportions of children who have significant disabilities which makes attendance in school difficult for them. In addition, a lack of such data makes planning and economic investment impossible. In collaboration with the

World Bank and a number of OECD overseas development ministries, the Centre for Educational Research and Innovation (CERI) is mounting a number of projects intended to gather the relevant data to form the basis of discussions leading to the identification of needed services, provision and training that will create the conditions for all children to be included in universal primary education.

Cross-border higher education

The OECD, together with UNESCO, is working on developing "Guidelines on quality provision in cross-border higher education". Over the past two decades, cross-border higher education through mobility of students, academic staff, programmes/institutions and professionals has grown considerably, including new forms such as campuses abroad, electronic delivery and for-profit providers. This development offers increased opportunities for individual students globally. It could also contribute to the quality of national higher education systems.

One of the main challenges to maximise these benefits is to protect students from low-quality provision of cross-border higher education that can be caused by the lack of a comprehensive framework for assuring the quality of cross-border higher education at international level. The Guidelines aim to respond to this challenge by providing such a framework. They support and encourage international co-operation and the understanding of the importance of quality provision in cross-border higher education while respecting the diverse national contexts. The Guidelines also recognise the importance of capacity building of national quality assurance and accreditation systems, especially in some developing countries, which will assure access to quality higher education for students in these countries. Implementing the Guidelines could serve as a first step.

All these activities are capacity-building exercises helping a very large number of countries to take policy decisions with far-reaching effects in response to calls for greater equity of access, improved delivery systems and other important education reforms.

THE ROLE OF SMEs

Access to international markets key to SME development

Representing over 95% of firms and accounting for between 40% and 70% of employment in many countries, small and medium-sized enterprises (SMEs) are widely recognised to be a key source of innovation and flexibility. Yet they are still largely under-represented in world trade, only contributing 25%-35% of world manufactured exports. However, innovative SMEs have been increasingly adopting new strategies to enlarge their foothold on international markets.

An OECD study has found that, for many SMEs, especially young enterprises, gaining access to international markets is a strategic instrument based on an ongoing development of their innovative capacities. Participation on international markets offers many opportunities to SMEs: new niche markets; economies of scale and scope; technological co-operation with partners and suppliers; possibilities to lower costs and to access finance. Besides exports and imports, other instruments for SME internationalisation are cross-border strategic alliances, mergers and acquisitions, inter-firm networking, and joining global value chains. Evidence shows that about one-fifth of manufacturing SMEs in OECD countries draw between 10% and 40% of their turnover from cross-border activities. Most SMEs rely on co-operation forged on alliances and networks, frequently with large or multinational enterprises, to help grow their business. ICTs have also spurred SME internationalisation, including through the Internet. In advanced OECD countries, most small firms, including micro-enterprises with fewer than ten employees, have at least one computer terminal, usually with Internet access.

Impediments to SME internationalisation should be removed

Many barriers hamper internationalisation (high fixed costs, laws and regulations, and lack of information). Eliminating such impediments could unleash new momentum for expanding SME activities abroad. To date, little research has been undertaken to measure impediments to SME internationalisation. Following a recommendation by ministers at the 2004 OECD SME ministerial meeting in Istanbul, a new OECD study will be carried out jointly with APEC in 2005-2006 to identify appropriate ways of removing the above barriers.

Entrepreneurship can promote local renewal and SME internationalisation

Entrepreneurship can serve as a catalyst for urban regeneration in deprived areas. Tailor-made approaches need to be designed, taking account of cultural, human, economic and social factors. Businesses based in inner city locations have economic advantages: a strategic location in the centre of urban areas, transportation nodes, untapped local markets and a large, diverse and available pool of human capital. Urban renewal and entrepreneurship are mutually dependent. Better infrastructure attracts entrepreneurs from both domestic and foreign markets. In turn, a revival of the entrepreneurial spirit lends further impetus to infrastructural improvements. In this way, competitive disadvantages of distressed urban areas (*e.g.* poor infrastructure, racism and crime) can be eased.

Trade and Development

THE DOHA DEVELOPMENT AGENDA

The overarching goal of the Doha Development Agenda (DDA) is to achieve concrete progress across the board in all the core areas of negotiation. The OECD meeting of the Council at ministerial level (MCM) offers a timely opportunity to provide much-needed momentum in the lead-up to the World Trade Organization (WTO) ministerial meeting in Hong Kong in December 2005.

Non-Agricultural Market Access (NAMA)

The DDA goal in NAMA is to reach early agreement on a non-linear tariff-cutting formula that will achieve genuine market opening. Recent OECD analysis shows that potential welfare gains from dismantling tariff barriers are substantial for all regions of the world: up to USD 100 billion globally, with up to 70% of those gains going to developing countries. While developing countries have much to gain from improved access to developed country markets, a substantial share of their potential gains is associated with liberalisation of their own tariff regimes.

The OECD has also taken stock of the range of non-tariff measures that are of concern to exporters in both developed and developing countries. While the range of existing barriers remains broad, quantity and price control measures have decreased in importance while customs-related and behind-the-border measures deserve greater attention. Initiatives to reduce these barriers would offer significant economic benefits.

Agriculture

OECD analysis shows that in agriculture there are strong reasons to pursue reform across all "three pillars" of the Uruguay Round Agreement on Agriculture (URAA):

- **Eliminating all forms of export subsidies** would remove the negative impacts on competitive suppliers in both global and other country domestic markets.
- **Reducing trade-distorting domestic support** would not only benefit global markets, but less trade-distorting policies have been shown to be more efficient and effective in achieving stated domestic policy goals.
- **Opening up agricultural markets** would contribute the most to improving world market conditions and to enhancing global welfare; in this respect, tariff rate quota (TRQ) administration, as well as out-of-quota tariff reductions, need to be addressed if trade flows are to increase.

While there is already widespread agreement on the first two points in the DDA negotiations, the approach to improving market access is still controversial. Yet, substantial tariff reductions and redressing tariff peaks and tariff escalation are a cornerstone to reaping the full benefits of trade liberalisation in agriculture.

Services

In services, momentum is needed to improve liberalisation offers and to encourage transition and developing countries, which have not yet tabled their initial offers, to do so. There is also a need to make progress in the other areas under negotiation on services (domestic regulation, subsidies, emergency safeguards and government procurement), since they are all elements of a successful outcome. OECD analysis suggests that the welfare gains from dismantling barriers in core sectors, such as telecommunications, financial, transport and business services, far exceed those from liberalisation of agriculture and manufacturing and can increase GDP by up to 7% in some developing countries. Gains derive in particular from spillover benefits from the associated movement of factors of production and the importance of services as inputs in the production of other services and goods. OECD work has also focused on ways to manage trade-related adjustment and to ensure that liberalisation is underpinned by sound regulatory frameworks.

Rules

Since the Doha ministerial conference, a significant number of formal and informal submissions have been made to the WTO Negotiating Group on Rules relating to anti-dumping, subsidies and countervailing measures, including fisheries subsidies, as well as to Regional Trade Agreements. Nevertheless, it is widely felt that there is a need to intensify and accelerate work in these areas to ensure parallel and substantial progress compared with other areas of the negotiation.

Trade facilitation

In 2004, WTO members agreed to launch negotiations on trade facilitation with a view to further expediting the movement, release and clearance of goods. The Negotiating Group is devoting particular attention to technical assistance and capacity building necessary for countries to participate in the negotiations and to implement commitments arising.

The OECD has analysed the potential gains from international co-operation in the area of trade facilitation, possible approaches for putting any agreement into practice at national level and the costs of introducing and implementing trade facilitation measures. The aim is to allow countries to better elaborate negotiating positions and reform strategies, and donors to efficiently target technical assistance and capacity building.

Developing country concerns

Developing countries have expressed concerns that multilateral tariff reductions may have negative economic impacts associated with declining tariff revenues and shrinking preference margins. The OECD has examined both of these concerns.

Revenue loss from tariff liberalisation can be recovered by improving the domestic tax system in a way that preserves the benefits of the trade reform. However, the required tax adjustment may be more difficult for some countries than others. This calls for targeted technical assistance involving, among others, the donor community and the international financial institutions.

Generally, developing countries will experience welfare gains from deep multilateral tariff reductions. According to OECD estimates, only a few extremely preference-reliant countries – mainly in Africa – will be vulnerable to net welfare losses (ranging up to –0.4% on a per capita basis). Finding a response to such losses will pose a challenge for policy makers, but should not prevent realisation of the broad gains for most developed countries from trade liberalisation.

REDUCING POVERTY

With just a decade left to the target date of 2015, the governments of developing countries and their donor partners are struggling to achieve the first Millennium Development Goal (MDG) of halving the proportion of people with incomes below one dollar a day. In many countries, progress in reducing income poverty has been slow, and the danger of failing to deliver on the goal is all too evident. What is less clear, however, is how to bring about the dramatic change in the rate of poverty reduction necessary to fulfill it.

The DAC Network on Poverty Reduction (POVNET) was originally established in 1998 to consider how bilateral aid agencies could sharpen the focus and impact of their poverty reduction efforts.

Developing policy guidance for donors

POVNET developed the *DAC Guidelines on Poverty Reduction* which synthesize state-of-the-art good practice and set out a vision for working with development partners and stakeholders towards poverty reduction. Recognising that the quantity and quality of growth in the productive sectors will have an important bearing on achieving the MDGs, a meeting in June 2003 tasked POVNET with a new mandate to develop policy guidance for donors on using aid effectively to promote economic growth and poverty reduction. POVNET is currently mandated to:

- Focus on the multidimensionality of poverty and on the relationship between inequality, economic growth and poverty reduction in developing countries.
- Provide a forum for the exchange of experience and best practice on pro-poor growth, *i.e.* involving the poor in generating growth and benefiting from growth and globalisation.
- Address strategies and policies in areas such as infrastructure, agriculture, trade and investment capacity building, information and communication technology, the role of the private sector and public-private partnerships.
- Promote the pursuit of the MDGs and a central role for broad-based growth and its determinants within the framework of national Poverty Reduction Strategies.

POVNET has three country-led Task Teams to focus on the following sectors:

Agriculture: The Task Team on Agriculture, led by the United States, aims to develop a shared understanding of emerging issues underlying the role of agriculture in pro-poor growth. A publication currently under preparation, entitled ***Enabling Pro-Poor Growth through Agriculture*** is to be finalised and approved by the DAC High-Level Meeting in 2006.

Infrastructure: The Task Team on Infrastructure, led by Japan, aims to formulate – in the context of the new discussion on the MDGs – a joint position of DAC members to enhance the impact of economic infrastructure on pro-poor growth. ***Guiding Principles on Infrastructure for Poverty Reduction*** will be endorsed by the DAC High-Level Meeting in 2006.

Private Sector: Under the leadership of the United Kingdom, Phase 1 of the Task Team's work concentrated on preparing an Analytical Framework paper, *Accelerating Pro-Poor Growth through Support for Private Sector Development*, which was published in February 2004. This paper explores the ways in which the private sector affects poverty reduction, identifying the conditions for pro-poor growth and providing some tentative policy recommendations. During its second phase, the Task Team aims to identify the strategies and tools necessary to strengthen the private sector's contribution to pro-poor growth, including guidance on making donor interventions more effective. Sweden is leading the Task Team for this phase which started in August 2004.

The *ex officio* POVNET members GENDERNET and ENVIRONET are contributing to the work of POVNET which will also draw on other ongoing work in the DAC in areas such as: information and communication technologies (ICTs); trade capacity building; investment; and small and medium enterprises and the Bologna Process.

Using aid effectively

A very important part of the POVNET mandate is to develop policy guidance for donors on using aid effectively to promote economic growth and poverty reduction. This will imply strengthening the growth component of national development and poverty reduction strategies and contribute to donors' collective efforts to promote aid effectiveness through country ownership, harmonisation, alignment and managing for development results. The progress achieved in identifying principles of good practice in aid effectiveness should be highlighted in this context.

In Monterrey in 2002, the international community resolved to increase aid and to improve the effectiveness of aid delivery for the goals set in the Millennium Declaration. In Rome in 2003 they committed to harmonisation and alignment, as key to effective aid delivery.

Since then a multi-stakeholder effort – developing and donor countries, international institutions including the African Development Bank, Asian Development Bank, European Bank for Reconstruction and Development, Inter-American Development Bank, the United Nations and the World Bank – has sought to translate these commitments into reality. This work has been done in the Working Party on Aid Effectiveness, hosted by and operating under the co-ordination of the OECD Development Assistance Committee (DAC).

This year, over 100 countries, as well as development institutions, attended a High-Level Forum on Aid Effectiveness in Paris. Participants committed to the Paris Declaration on Aid Effectiveness, a practical blueprint to provide aid in more streamlined ways that better meet the needs of developing countries. They also agreed to improve accountability by monitoring the blueprint's implementation.

The Paris Declaration has some 50 commitments to improve aid quality, which will be monitored by twelve indicators. Participants agreed to preliminary quantitative targets for five of them. They will finalise targets by the time of the United Nations' five-year review of the Millennium Declaration in September.

"In 2005, poverty and development are the issues of the year. Aid flows to developing countries are on the increase after a sustained drop for many years. So we must demonstrate that we are using that aid effectively. This will give people the confidence that aid helps the poorest people in the world, and that more aid is a sound investment in all our futures," said Richard Manning, the DAC Chair.

PROGRESS TOWARDS THE MDGs

The Millennium Declaration set specific goals for achievement by 2015 from a baseline of 1990. Heads of State will review progress in September 2005.

Halve extreme poverty and hunger by 2015

This goal is likely to be met globally, led by growth in Asia. But nearly half the population of sub-Saharan Africa remains in extreme poverty. There is progress against hunger, but not fast enough to achieve the goal.

Achieve universal primary education by 2015

Five developing regions are approaching universal enrolment. But a third of primary school age children are out of school in sub-Saharan Africa, a quarter in Oceania, and a fifth in Southern Asia; 115 million worldwide.

Achieve equality in education by 2015 and promote empowerment of women

Five regions may reach the 2005 goal for gender equality in primary education. In the other five regions, despite major improvement in Southern Asia, as few as 85 girls are in school per 100 boys. And in most regions, women represent a smaller share of wage earners than men.

Reduce child mortality by two-thirds by 2015

Death rates of children under five have fallen in all regions, but at half the required pace. Eleven million children a year die from preventable or treatable causes. Most of them could be saved by expanding programmes that promote simple, low-cost solutions.

Reduce maternal mortality by three-quarters by 2015

More than half a million women die each year during pregnancy and childbirth. Globally three in five births are now attended by skilled health personnel, up from two in five in 1990. But in Southern Asia and sub-Saharan Africa, three mothers out of five still have no such support.

Reverse spread of HIV/AIDS and incidence of malaria and other diseases by 2015

AIDS is the leading cause of death in sub-Saharan Africa and the fourth largest killer worldwide. HIV is spreading at an alarming rate; intensified prevention efforts are needed. Malaria and tuberculosis each kill well over one million people a year; affordable prevention and treatment efforts are being scaled up.

Ensure environmental sustainability including halving lack of access to safe water and improved sanitation by 2015

Commitment to sustainable development has yet to reverse the loss of the world's environmental resources. Eight regions are progressing fast enough to halve the lack of access to safe water by 2015, but nearly half of Oceania and sub-Saharan Africa are not. Nearly half the developing world still lacks basic sanitation and the number of slum dwellers is increasing rapidly.

Develop a global partnership for development

Goal 8 represents a social compact: developing countries do more to ensure their own development and developed countries support them through aid, debt relief and trade access. Aid is at an all-time high, but further commitments are needed to meet the MDGs. Progress is also required on the Doha Round, accelerated technology transfer, access to essential drugs, and promoting youth employment.

COPING WITH CLIMATE CHANGE

Work on international climate change agreements reached an important milestone in 2005, with the coming into force of the Kyoto Protocol. Many domestic policies have also been implemented in OECD countries that help respond to the challenge of climate change (*e.g.* carbon/energy taxes, climate-related voluntary approaches with industry, and emissions trading). Partly as a result of these policies, and partly as a result of general structural changes, OECD CO_2 emissions grew by only 14% between 1990 and 2002, while OECD GDP grew more than 30%. Eleven OECD countries also had lower greenhouse gas emissions in 2002 than in 1990. Despite the progress, more needs to be done.

Mitigation

The OECD has consistently advocated market-based instruments as the best way to achieve climate change policy goals. The OECD helped lay the groundwork for including market-based instruments (Clean Development Mechanism, emissions trading, and Joint Implementation) in the Kyoto Protocol, contributing to a wider understanding of the potential of these approaches for reducing mitigation costs and for stimulating carbon-friendly investments and innovations.

Adaptation

Adaptation unites both developing and developed countries, because all countries will suffer the effects of climate change, and will need to adapt to them (even though developing countries' capacity to adapt will be considerably lower). The OECD has begun to assess adaptation options in selected economic sectors (*e.g.* agriculture, transport, energy), and in several thematic areas (*e.g.* mountain systems, Arctic ecosystems, sea levels).

Climate change and development

Since 2001, the OECD Development Co-operation and Environment Directorates have co-operated on a project to integrate climate change objectives into development policies – including into donor portfolios on development assistance. A focus of this work is on adaptation to climate change, with emphasis on natural resource management. Case studies have been completed for six developing countries; a Global Forum on Sustainable Development event also focused on issues related to mainstreaming responses to climate change into sectoral development policies.

Technology co-operation

Investment in low-carbon technology is a necessary element of any climate change response. Most OECD countries already have explicit policies related to climate-related technology development and diffusion (*e.g.* renewable resources).The OECD has been working to better understand how investments in these technologies could be developed and diffused in a cost-effective manner. It has also been exploring opportunities for enhanced international technology collaboration.

Benefits of policy responses

A key question is how much (and how fast) the public policy response to climate change should be. The answer hinges partly on the size and distribution of anticipated impacts of climate change on economies and ecosystems. OECD work in this area has been developing an improved framework for organising information about these impacts. Such a framework would be risk-based, and may not need to quantify all impacts in monetary terms, in order for it to be useful to policy makers.

CO-OPERATION WITH PARTNER ECONOMIES

With the rapid spread of globalisation and the emergence of new important actors on the world economic scene, co-operation with non-members has come to form an integral part of the Organisation's core activities. The engagement of partner economies in OECD work ensures the continuing relevance and effectiveness of policy initiatives pursued within the OECD framework and helps promote the worldwide implementation of OECD guidelines and agreements.

Throughout 2003 and 2004, the OECD undertook a strategic reflection on its relations with partner economies. The Council welcomed the resulting report entitled *A Strategy on Enlargement and Outreach* which calls for a coherent, co-ordinated and pro-active approach. The Council is now actively engaged in a strategic review of OECD's outreach instruments and orientations. It has also asked all OECD Committees to develop their own outreach strategies and to take a pro-active approach to engage relevant partner economies in their work, including as observers or full participants.

Forum for building consensus

The OECD provides a forum for participating countries to develop, through a consensus-building process, best practices, guidelines, principles and other "rules of the game". Consensus is built through shared analysis of the issues and mutual understanding of other partners' positions; formulating a common market-based response to the issues; and surveillance of the follow-up given by each one in a "peer review" process. This method of co-operation is highly valued by non-member economies working with the OECD.

Sharing knowledge and expertise

The Organisation works with non-members in a wide range of socio-economic policy areas to support the reforms required to reap fully the benefits of globalisation. Currently, there are three avenues for co-operation: OECD Global Dialogue and Global Forums, Regional/Country Programmes and participation in OECD committees, bodies and instruments. Non-members are also invited to participate in several sessions of the annual ministerial meeting.

The Global Dialogue is a new instrument designed as an overarching forum for policy dialogue on important issues of global interest between high-level officials from members and selected non-members.

The nine OECD Global Forums help enhance mutual understanding among policy makers and experts on difficult issues in a neutral, non-negotiating context. Currently, the Global Forums focus on sustainable development, knowledge economy, public and private governance, international taxation, trade, international investment, agriculture, competition and education.

Co-operation with non-members also takes place through targeted geographical programmes. A flagship activity in Russia this year has been the *Regulatory Reform Review*, the OECD's first review of this kind with a non-member. The review deals with economy-wide reform issues and includes recommendations on improving regulations in competition, trade and the energy and railway sectors. The fifth *Economic Survey* (July 2004) examined the competitiveness of Russian industry in the light of both macroeconomic and structural developments, with particular focus on the role of financial intermediaries and corporate governance. An *Investment Policy Review* of Russia presented policy options to improve the investment climate.

The Anti-Corruption Network for Transition Economies brings together 23 countries from Central, Eastern and Southern Europe, Caucasus and Central Asia. Close co-operation continues with South East Europe within the framework of the Stability Pact, in particular in the area of investment, enterprise, competition and education policies. The Baltic Regional Programme ended in 2004 with wide acclaim for its success.

In Asia, several OECD events are hosted by Indonesia including an expert meeting on "Corruption Prevention in the Tsunami relief", and a conference on "Investment for Development: Lessons from Asia". Relations with India have also strengthened. In November 2004, the OECD Secretary-General met in Delhi with the prime minister. India hosted the OECD Global Forum on International Investment (GFII), supported by the Confederation of Indian Industry, followed by an OECD-India Investment Roundtable.

With China, the OECD is completing work on the reform of governance systems and practices. A key message is that China should continue its efforts to address governance weaknesses across various levels of government that affect public sector management, public finances and the market forces framework and to reform the governance of state-owned enterprises. New activities with China in 2005 include: an economic survey, an agricultural policy review and a pilot project on policies towards cross-border mergers and acquisitions.

OECD work with Latin America included the 2005 *OECD Economic Survey of Brazil*, a peer review of Peru's competition law and policy, now being followed by a similar review of Brazil, and a review of education policy in Chile. In June 2004, the Secretary-General visited Brazil and Chile where he met with the President and senior ministers.

In 2004, the Middle Eastern and North African countries (MENA) and the OECD launched a joint Initiative on Governance and Investment for Development. The three-year initiative, developed and led by the MENA states, aims to modernise government structures and processes, and to improve investment climate and policies in the region. A ministerial meeting in Jordan on the governance pillar of the Initiative as well as meetings of five Working Groups of the investment pillar laid the ground for an ambitious substantive work programme to be carried out in partnership with other international organisations.

The OECD contributes to policy reform in Africa in co-operation with a number of African organisations, such as NEPAD, the African Union, the African Development Bank and the Pan-African Conference of Public Service Ministers, as well as at regional level through the Sahel and West Africa Club (SWAC) and the Initiative for Central Africa (INICA), both hosted by the OECD. Co-operation with South Africa has strengthened. A joint OECD-UN Economic Commission for Africa (UNECA) *Mutual Review of Development Effectiveness* was launched in 2004, with the first report to be published in 2005.

Partnerships with other international organisations

For several years, the OECD has had partnership agreements with the World Bank, UNCTAD and the Inter-American Development Bank. A partnership agreement with the Asian Development Bank was signed in March 2005. Last year, co-operation intensified with APEC in the field of regulatory reform and investment. The International Tax Dialogue – a joint initiative of the IMF, the OECD, the World Bank with the UN as an observer – held its first global tax conference in Rome in March 2005 on the topic of Value Added Taxes (VAT). Civil society and business associations are active partners of the OECD in various parts of its outreach activities.

Good Governance

CORPORATE GOVERNANCE

In recent years, OECD governments have reacted decisively to a string of corporate governance scandals. It is now a priority to ensure that these reform efforts contribute to key policy objectives including improved corporate competitiveness, financial stability and better access to risk capital. As issuer of the globally endorsed OECD Principles of Corporate Governance, the OECD is leading that forward-looking inquiry, co-operating closely with other international organisations, business and other stakeholders.

The revised OECD Principles are a more effective guide for policy

The OECD Principles of Corporate Governance were revised in 2004 through an inclusive and open process that greatly contributed to their quality, usefulness and relevance around the world. The new Principles include a special chapter that emphasise the need for a legal and regulatory framework that promotes efficient markets. The policy challenge is to ensure that the necessary corporate governance rules and regulations are effective and come with minimum cost to market participants and the economy as a whole. The corporate governance framework is typically a fairly complex web of legal, regulatory and voluntary provisions. It is therefore important to focus on the overall economic outcome whatever approach to regulation is adopted and to ensure that measures taken have the intended effect on the behaviour of investors, managers, auditors, board members and other market participants.

As one of the twelve key standards identified by the Financial Stability Forum, the Principles form the basis for all the work carried out by the OECD Steering Group on Corporate Governance. Enhanced policy dialogue among member countries will be supported by developing a new methodology that could also be used in the World Bank/IMF Reports on the Observance of Standards and Codes (ROSC) that assess country reform progress. The Principles also play a key role in the OECD's Regional Corporate Governance Roundtables that promote good corporate governance in non-OECD countries. Building on the five Regional White Papers that set out reform objectives in Asia, Latin America, Eurasia, Russia and South Eastern Europe, the Roundtables now focus on promoting effective implementation and enforcement.

A good corporate governance framework encourages investment and growth

Better corporate governance is not only about protecting investor rights. It is an essential precondition for growth. Empirical evidence shows that improved corporate governance, including stricter enforcement and more transparency, will lower the cost of capital for domestic enterprises and also serve to attract foreign capital. Just as important as the level of investment is the efficient use of the existing capital stock. Many countries have had high rates of investment at different times, only to sink back later into slow growth and both domestic and international payments and banking crises. The role of corporate governance for the investment climate is addressed in the context of an OECD project, the Policy Framework for Investment.

New technology and forms of business organisation are making new demands on corporate governance. One important example is the increasing significance of intellectual assets, such as trade secrets, patents and highly skilled individuals, and the need to understand their impact on company value. This trend has prompted new evaluation problems for investors and challenges for corporations' non-financial reporting. In fact, the ability of countries and corporations to innovate and provide corporate governance arrangements that meet the changing needs of investors and industries will be an important part of their future competitive edge.

An important feature of the investment climate is zero tolerance of bribery and corruption. This is not just an enforcement issue but also one for corporate governance. The OECD Principles call on boards to have effective compliance mechanisms in place underpinned by a policy which should address company compliance with anti-bribery requirements, especially the OECD Convention on Combating Bribery in International Business Transactions.

Improving corporate governance of state-owned enterprises

State-owned enterprises, including banks, still play an important role in many countries. Following partial privatisations, the state may also appear as a large owner of shares in publicly traded companies. State ownership raises a number of specific governance issues, notably the need to ensure a level playing field where private enterprises do not face discrimination. To deal with these issues, the OECD countries have developed the Guidelines for the Corporate Governance of State-Owned Enterprises. The Guidelines include recommendations about the state's ownership role and how to promote effective boards. The Guidelines will also underpin the work of the Regional Corporate Governance Roundtables.

BUILDING TRUST IN GOVERNMENT

Given the growing number of public and private actors engaged in governance, governments are increasingly obliged to rely on co-operation rather than command. This new way of working requires an environment of trust, openness and accountability, as well as the ability to adapt to change. OECD work on public governance promotes transparency and coherence of government action to build public trust while creating a predictable climate for economic activity.

In many countries, public management reforms have made public administration more flexible, transparent and focused on performance. However, changes in rules, structures and processes have often not resulted in the intended changes in behaviour and culture. Modern governments need a whole-of-government and more open public management policy capability, to ensure the coherence of the system. A recent OECD review of public sector modernisation draws lessons from the past 20 years of reform, with the aim of helping governments choose appropriate reform strategies for the future.

Ministerial meeting on building trust between citizens and government

At a meeting to be hosted by the Netherlands in November 2005, ministers responsible for public administration reform will discuss how to bridge the gap between citizens' expectations and government's capacity to deliver on those expectations, as well as how to reconcile short-term needs with long-term policy objectives. They will also look at the machinery of government for decision-making, and examine partnerships with the private sector. These discussions will frame the strategic orientations for future OECD work in this area.

Promoting integrity and preventing corruption

The OECD has developed a framework to help public institutions assess the impact of efforts to promote integrity and prevent corruption. A report to Council next year will examine progress in implementing the OECD Guidelines for Managing Conflict of Interest in the Public Service and will also review critical issues, such as lobbying. Ongoing work focuses on applying good governance principles, notably transparency and accountability in public procurement.

Regulatory reform

To help countries ensure that their regulatory structures and processes are relevant and robust, transparent, accountable and forward-looking, two major OECD policy instruments have recently been adopted:

- The expanded and updated 2005 OECD Policy Recommendations for Regulatory Quality and Performance draw upon 20 country reviews of regulatory reform, and include a greater focus on policy coherence and multi-level co-ordination; prior assessment of policy proposals; competition policy; market openness; risk awareness; and implementation.
- The APEC-OECD Integrated Checklist on Regulatory Reform is a self-assessment tool based on policy principles common to both APEC and OECD. It integrates regulatory quality, competition, market openness and transparency and accountability.

Globalisation increasingly tests regional economies' ability to adapt and exploit their competitive edge, offering new opportunities for regional development. This is particularly relevant for cities as vital parts of the global economy. A series of OECD metropolitan reviews provide practical policy advice to governments focusing on regional competitiveness and multi-level governance.

COUNTERACTING TAX ABUSE IN A GLOBAL ENVIRONMENT

The more open and competitive global market has had many positive effects on tax systems. Tax rates have generally fallen and tax bases have been broadened. Some tax and tax-related practices, however, undercut the gains that tax competition generates. This occurs especially if some countries engage in practices that encourage non-compliance with the tax laws of other countries. The ultimate losers are honest taxpayers. They end up paying for dishonest practices by shouldering a greater share of the tax burden, and their confidence in the integrity and fairness of their tax systems, and in government in general, declines. Since 1998, the OECD has co-ordinated action so that countries – large and small, rich and poor, OECD and non-OECD – can work together to promote integrity in the operation of tax systems, especially as they apply in the financial area. Only in this way will the international community be able to reap the full benefits of today's more competitive environment.

Why is this project important?

Tax fraud, tax evasion and avoidance are facilitated by the abuse of bank secrecy, nominee shareholdings, bearer shares and undisclosed offshore trusts. Transparency and effective exchange of tax information are tools which can effectively counter such abuse.

What outcomes are sought from this project?

- An effective network of bilateral agreements on exchange of information is put in place so that revenue authorities are able to request, within the constraints required to protect taxpayers' privacy, the information they need to ensure compliance with their tax laws. Such agreements also have a deterrent effect on potential tax evaders.
- Tax evaders can no longer hide behind elaborate arrangements designed to mask their true nature and ownership.
- Competition takes place on the basis of legitimate commercial considerations rather than lack of transparency and lack of effective exchange of information.
- A potentially fairer tax system for all; one where issues of anonymity have no role to play.

What has been achieved?

- Thirty-three jurisdictions have committed to improve transparency and establish effective exchange of information and are working together with OECD members to develop high standards of transparency and information exchange.
- In 2002, they developed a Model Agreement for Exchange of Information in Tax Matters, which is being used to establish bilateral agreements between OECD members and offshore financial centres and which was endorsed by the G-20 finance ministers in November 2004.
- Of the 47 member country preferential tax regimes identified in 2000 as potentially harmful, 18 have been abolished or are in the process of being abolished, 14 have been amended so that any potentially harmful features have been removed, and 13 have been found on further examination not to be actually harmful.

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