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Introduction

1. The Regional Consultative Meeting on Financing for Development in the European Region was opened by Danuta Hübner, Executive Secretary of the Economic Commission for Europe (ECE). She emphasized that the main objective of the consultation was to exchange views and experiences in attracting public and private flows to the transition economies and in using them effectively for development. The meeting was also expected to provide regional perspectives on issues related to governance in monetary and financial systems at the global level. She recalled that this meeting was part of the preparatory process towards the High-level International Intergovernmental Event on Financing for Development, to be held in 2002.

2. Jørgen Bøjer (Denmark), Chairman of the Preparatory Committee for the High-level Event, was elected Chairman of the meeting. Mr. Bøjer provided details about the preparations for the High-level Event, pointing, inter alia, to the participation of other regional commissions, United Nations bodies, the International Monetary Fund and the World Bank, as well as entities from civil society and the business community.

Conduct of the meeting

3. The meeting was conducted through a series of panel discussions on five specific themes related to the general problem of financing for development.

4. The present report is based on the views expressed and the suggestions made by panellists, member States, NGOs and representatives of the private business sector. It reflects lessons drawn from experience in the region and presents conclusions that might be usefully taken up in the preparations for the High-level Event. The following is not a text agreed by ECE member Governments but a report of the proceedings prepared by the ECE secretariat. The Chairman's summary is contained in annex I, the programme of the meeting in annex II.

Financing the process of transformation and development in the ECE transition economies

5. The plenary session raised some important points which were taken up in more detail in the subsequent working sessions. It was emphasized that Europe is unique for its wide disparities in levels of economic development across countries. Transition economies have a much lower level of real income per capita than Western European countries, but there are also large disparities in the level of economic development among the transition economies themselves, which underlines the importance of the issues related to financing for development in Europe. A major goal of economic policies is to achieve sustained economic growth and a significant reduction of income disparities between East and West. But experience shows that the process of catching up will take considerable time and that it will require massive restructuring of these economies, pointing to the need for huge investments in physical and human capital, which will have to be financed mainly from domestic resources.

6. It was stressed that many transition economies face chronic economic and social problems which are essentially those of underdevelopment, including very low (by international standards) average levels of real per capita income, widespread poverty, inadequate health-care systems and widening income and social differentiation. The problems of transition, however, are in addition to those of development, and both are compounded by the economic and political consequences of an unprecedented transformational depression, as well as numerous conflicts and even wars in some parts of the region. This is a highly complex mixture of problems, which has exposed these economies and their populations to excessively high levels of strain and suffering.

7. Western donors noted that economic development and its financing remains a crucial issue, and that the process towards the high-level meeting is therefore a very good occasion to single out the key factors for economic development and poverty reduction. They emphasized that domestic factors, especially consistent reform policies designed to achieve broadly based economic and social progress, are of prime importance for the transition process and the process of economic development in general. Development aid has to be seen as a catalyst that facilitates/supports domestic efforts. Attention should be paid to measures designed to increase the efficiency of assistance, including improved coordination among donor countries and international financial institutions (IFIs). It was emphasized that efforts should be made by developed countries to meet as soon as possible the objective to

raise the level of official development assistance (ODA) to 0.7 per cent of their gross domestic product (GDP). In view of the heterogeneity of levels of development and the associated diversity of problems, there is a need to tailor both official assistance and debt relief to the specific needs and circumstances of individual countries. It was also noted that enhanced market access for developing countries' exports is a cornerstone for supporting their economic growth.

Strategies

8. It was pointed out that there is no universal recipe for economic development and catching up with the more developed economies. This depends on a host of factors, the relative importance of which is difficult to quantify. It is therefore difficult to emulate successful development strategies adopted in such countries as Ireland. More generally, the key factor is the domestic absorptive capacity, which in turn depends on such factors as effective institutions, macroeconomic stability, structural reforms, close integration with the international division of labour and the quality of human capital.

9. It was also noted that coherent and consistent reform policies are a conditio sine qua non for successful development. The "old" enterprise sector should face a hard budget constraint and there should be a conducive environment for the creation of new firms, especially small and medium-sized enterprises (SMEs).

Fixed investment and foreign direct investment

10. Fixed investment is the carrier of technical change and is therefore at the heart of the process of creating competitive economic structures in the transition countries. The direction of causality between investment and economic growth is difficult to establish and is best thought of as a mutually reinforcing process. There were concerns that a lack of fixed investment and disappointing rates of economic growth could lead to a loss of human capital in the transition economies, either because of a deterioration of skills associated with high and persistent unemployment or outward migration.

11. Foreign direct investment (FDI) can play an important catalytic role in the transition process: it is a source not only of funds for financing external deficits but also of new technology and know-how.

Domestic and external financing

12. It was noted that transition economies differ widely with regard to their external financing problems. The bulk of domestic investment is, in any case, almost always financed internally.

13. In the leading European Union (EU) accession candidate countries, the main challenge is the savings-investment imbalance. Low domestic savings (partly reflecting demographic factors) contrast with very high investment needs. These partly reflect the need to meet the high standards of the *acquis communautaire* in the fields of energy, environment and transport. But in these countries, (foreign) private capital is increasingly available, thus reducing the need for official bilateral and multilateral assistance.

14. In contrast, in the less developed transition economies the domestic savings base is weak and financial intermediation underdeveloped. Governments face an inadequate domestic revenue base which does not even allow them to fulfil their basic "night watchman" role. Private capital inflows are forthcoming only to a limited extent. These countries continue to rely strongly on official assistance, a main priority of which should be the financing of public infrastructure projects.

Role of official assistance

15. It was emphasized that Western official assistance is essential for the transition process to succeed and to create the basis for a sustained process of economic development. But it was stressed that official assistance can only complement domestic efforts. Western donors, however, should remind themselves that a successful outcome of the transition process is in their self-interest since this will help to ensure the long-term economic and political stability of Europe as a whole. This was one of the lessons to be learned from the Marshall Plan, which represented a realistic and farsighted appraisal of what was required to ensure economic recovery and political stability in Western Europe after the Second World War.

I. Mobilizing financial resources for transformation and development: the domestic dimension

Issues in domestic resources mobilization during economic transformation

16. Mobilizing domestic resources has been important for growth since the time of the industrial revolution because much of the domestic investment that propelled this growth was financed through domestically generated savings. The same is true today, but countries in the Eastern region of ECE are facing exceptionally large social and economic costs associated with economic transformation. Despite an increase in savings during the second half of the 1990s, there appears to be a significant gap between the demand for investment and the availability of domestic resources in the region.

The savings-investment nexus and inadequate financial intermediation

17. It was reported that, according to a recent study made by the ECE secretariat, there is a strong correlation between savings and investment rates across the transition economies. But the role of savings in economic growth is ambiguous in economic theory. Higher savings can translate into higher investment, which in turn leads to higher growth, but higher growth can also stimulate savings (reverse causality). Nevertheless, the high savings and investment ratios observed in most of the countries undergoing economic transformation contrast with a relatively high variance in their economic growth rates.

18. Most of the participants agreed that missing or ineffective institutions appear to be a major reason why domestic savings are not always channelled into investment. Poor regulatory frameworks hinder the development of financial markets, which in turn restrain the mobilization of domestic savings. Poor governance of the banking sector can also hinder investment. The development of real estate markets can make an important contribution to the improvement of intermediation, but these require well-defined property rights. Ineffective financial institutions can lead to a lack of confidence of households and firms, thus enlarging the financial gap.

19. The development of financial systems and capital markets in the transition economies was therefore considered to be very important for the mobilization of private savings. There is strong evidence that countries with more developed financial systems channel more savings into investment. Hence, the acceleration of financial reforms in the transition economies is likely to stimulate private savings and consequently contribute to higher rates of economic growth. In the meantime, if there is a surplus of savings but ineffectual or missing institutions, then the IFIs should step in and mobilize local funds for investment.

20. In addition, there was agreement that the macroeconomic environment also plays an important role in closing the financial gap. Sound macroeconomic policies must be in place for the savings rate to increase, and consistent external and internal policies can also help channel domestic savings to investment.

21. There was also some concern among participants that the region had an unfavourable age structure, that is, an increasing proportion of elderly persons with a low savings propensity. This has important implications for social security. As the population ages, government expenditures for pensions tend to rise as a percentage of GDP. This will, ceteris paribus, lead to lower national savings rates. There is also evidence that people do not save in the prime of their lives as suggested by the life-cycle hypothesis.

Finance for SMEs

22. It was considered important to ensure a conducive environment for the financing of SMEs. Foreign bank loans are typically channelled towards the more profitable sectors, which do not generally include SMEs. Despite support for SMEs by the international lending institutions, local banks do not provide support for SMEs because of missing institutions, poor governance or lack of competence. Nevertheless, SMEs are thriving in some countries because the bulk of their investments is self-financed.

Public-private partnerships

23. Governments and official institutions can mobilize local private resources to finance commercially viable infrastructure ventures. The direct effects include the utilization of the local labour force, the mobilization of other local resources, the sharing of risk between government and the private sector, and the use of local professional advice (legal, technical etc.).

Revenue for social development

24. There was concern that the current need for domestic resources for economic restructuring might hinder social development in the region; in fact, social problems have to be handled simultaneously with economic ones. Social development is seen as a human investment (in education, health and social services) that not only improves the social welfare of society but also increases the human capital needed to sustain economic growth. In Western Europe, the state, private sector and civil society all provide social welfare, but in the transition economies the role of the state has diminished, the private sector is only just emerging (but providing only for those who can pay) and civil society is not yet ready to accept such responsibility.

Concluding observations

25. External financing, such as FDI, appears to be an important factor for stimulating growth. This may reflect the fact that it is a type of investment that also brings technology and new organizational methods. But empirical research in this area is still limited and existing modelling frameworks are not adequate to establish the scale of these benefits or the conditions which are most likely to give rise to them.

26. However, in general it can be expected that the transition economies will follow the traditional path of primary reliance on their domestic savings as the main source of financing future development and growth. Hence, domestic policy must play a very important role in mobilizing private savings and investment.

II. Role of official assistance in creating the conditions for sustainable development

27. The discussion focused on how official financial institutions could help to create the conditions for sustainable economic growth in the transition economies. At various times during the past decade, these economies have been faced with the simultaneous tasks of macroeconomic stabilization and systemic and structural reform, tasks which have required considerable resources that, at least early in the transition, could not generally be mobilized internally or from private foreign investors. Bilateral and multilateral institutions, including the specially created and transition-oriented European Bank for Reconstruction and Development (EBRD), have sought to fill the gap.

28. Participants agreed that the global supply of official finance (especially ODA) is limited, and that the financing needs of the transition economies would have to be met increasingly from private sources. In fact, due to the improving investment climate in many transition economies, the private sector now represents the major share of capital inflows. As for official funds, it was repeatedly noted that they should act as a catalyst for the development of the private sector and the mobilization of private capital. A number of delegations from countries with transition economies underlined the importance of official assistance in the early phases of the transition process, which had helped them to achieve macroeconomic stabilization and put them on the path to economic recovery. In addition to providing badly needed funds, arrangements with official institutions help to generate confidence in the investor community. However, it was also stressed that official assistance should be viewed as temporary, and that in the longer term it is not a substitute for domestic adjustment, restructuring and the mobilization of local savings. Even as foreign capital inflows increase, domestic savings are expected to provide the bulk of development resources.

Regional heterogeneity and the continuing needs for assistance

29. A major theme was the heterogeneity of the transition countries and their future requirements for official assistance. These large differences are reflected, inter alia, in the levels of income (seven countries are eligible for International Monetary Fund (IMF) poverty reduction and growth arrangements), progress towards stabilization, the stage of economic reform and the degree of access to the international capital markets. There was a consensus that while the need for official assistance has generally diminished, it still has an important role to play in the transition. However, tailoring it to countries’ changing needs and sectoral developments remains a challenge.

30. As countries progress towards a more advanced stage of reform, their circumstances and financial needs change and evolve. In the middle-income, advanced transition economies, which have generally been successful in attracting various types of private capital, the IFIs are to continue to foster systemic reforms, finance infrastructure and help, inter alia, with

environmental clean-up and training. It should be borne in mind that access to the international capital markets does not currently guarantee maturities of the duration required for projects with long gestation periods. In the case of the less advanced reforming countries, relatively larger volumes of the more traditional assistance — for economic development, macroeconomic stabilization and structural reform — are still required.

31. *Governments made the following suggestions:*

(a) Official assistance be additional to any funds forthcoming from the private sector. Public funds should not displace private funds;

(b) Official assistance not be withdrawn too quickly since this could endanger other domestic programmes;

(c) Potential recourse to IFIs as a source of emergency stand-by assistance be maintained;

(d) One delegation proposed that the developed countries fulfil their commitment to devote 0.7 per cent of their GDP to providing ODA;

(e) A proposal was made to provide debt relief to several low-income transition economies which appear to have unsustainable debt burdens.

Assistance for sustainable economic growth

32. In addition to providing resources, there was consensus on the proposition that the IFIs should promote policies and long-lasting market reforms which would set the stage for sustainable economic growth. Their classic function of infrastructure financing and its positive externalities were mentioned. However, discussion focused on the fact that the leverage provided by official funds should be used to maximize its "transition impact". Mechanisms or policies which could be used to this end include the judicious application of conditionality, closer interaction between IFIs and the private sector, and the strengthening of market-supporting institutions. In particular:

(a) A number of recipient Governments noted the benefits accruing to them from conditionality (i.e., the terms attached to IFI resources). These benefits — deriving from IFI help with policy and project design, technical assistance, monitoring compliance with programme parameters etc. — were often viewed to be as or more important than the availability of funds;

(b) IFIs should continue work on improving banking, financial, legal and regulatory institutions, but it was felt that it is also important to recognize and address the important political obstacles that have prevented effective action in the past;

(c) The ability of the IFIs to mobilize private funds by lending their name to projects and sharing risks with the private sector was considered a major asset. IFIs can take the lead in projects, regions and countries where the private sector is reluctant to enter;

(d) The involvement of IFIs in projects can provide the basis for the improvement of corporate governance in the host economy.

33. Another beneficial commitment mechanism singled out by recipient countries was the pre-accession negotiation process with the EU. This was regarded as a blueprint for structural reforms, and was considered to supply a crucial motivation for internal adjustments and the introduction of structural measures, such as privatization and deregulation, as well as enhancing their sustainability. The pre-accession programmes have been financed by various EU funds and technical assistance.

34. IFIs have been instrumental in supporting the development of SMEs through loans, equity participation and policy advice. In addition to their key role in economic recovery — an observation made by some speakers — the role of SMEs in the development of civil society and open markets was seen as essential for the evolution of an efficient market system.

35. *Governments suggested that:*

(a) The effectiveness of conditionality can be further increased if more efforts are made to customize it to country-specific circumstances. Where it isn't already practised, a policy dialogue between donor and recipient is desirable;

(b) Competition among IFIs and other official donors to soften conditionality should be avoided since it is likely to result in the postponement of necessary reforms, with long-term negative consequences for the recipient countries;

(c) Competition between donors can lead to excessive and sub-optimal grant elements, which also reduce the aid available for other recipients;

(d) Public private partnerships (PPPs) should be further explored as a means of mobilizing finance and sharing risk, but some Governments warned that they are not a panacea.

Coordination of aid and regional issues

36. Several issues relating to aid coordination by donors and the need for measures to enhance regional ties were raised in the debate.

37. Although some progress has been made in the coordination of assistance between donors (multilateral and bilateral), participants felt that further improvements were desirable. Coordination is difficult because of the differing objectives of multiple donors, donors' differing assessments of country needs and differing national aid preferences. However, one participant noted that the lack of experience in the area of aid administration meant that the transition economies sometimes had difficulties in using aid efficiently. Another drew attention to the fact that disbursement of aid has often been delayed.

38. More effective regional cooperation could bring benefits to certain areas in the ECE region. This is especially true of trade and infrastructure because economic relations under the former economic system were shaped by Governments rather than by market forces and comparative advantage. In this area, too, some progress has been made, but it was agreed that more needs to be done. Many of the countries in South-East Europe provide the latest challenge for such a new approach.

III. Foreign direct investment and the restructuring of transition and emerging economies

39. FDI was regarded as a major source of funds in closing the financing gaps of the transition economies. However, FDI inflows into the transition economies have been relatively weak (with a few exceptions) and highly differentiated across countries. The major impediments to a faster growth of FDI in the transition economies are the lack of or weak implementation of necessary policies (which may have been already passed by legislatures) and the rather low responsiveness of domestic agents (weak capacity of a society to adjust to the new market environment).

40. The current situation in the transition economies reveals several important patterns of FDI and its impact:

(a) The distribution of the FDI stock accumulated during the last 10 years among the recipient countries is rather diversified. In terms of the total stock, the bulk of FDI is concentrated in four or five transition economies. While the Russian Federation is included in this list, it ranks nearly last in terms of FDI per capita;

(b) FDI inflows as a percentage of the stock of fixed capital in the transition economies also vary, but less considerably, and even in the most successful countries it is less than 10 per cent of the total stock, indicating that even in these countries FDI is not the main source of capital formation;

(c) The observed performance in the manufacturing sector reveals higher productivity, stronger export orientation and a high rate of reinvestment capacity in firms with foreign participation. There is also strong evidence of an increasing gap between the performance of foreign and domestic enterprises within the same industry and also within the same country;

(d) A side-effect of foreign takeovers (in particular by transnational corporations), which sometimes has a negative impact on public opinion, has been the conversion of independent domestic companies into subsidiaries of foreign concerns, which implies a certain loss of sovereignty in decision-making and entry into a different sphere of competition (mainly within the multinational corporations distribution networks);

(e) Government policies related to FDI differ among recipient countries in a number of ways. These include: methods of privatization (scope and terms); national treatment (incentives for FDI or non-discriminatory); potential bias towards big investors, hence FDI; and incentives for start-ups or greenfield investments. However, investment promotion (both domestic and foreign) in the transition economies often faces budgetary constraints due to the low levels of public revenue.

41. Considerable attention was devoted to public policy issues, in particular those related to FDI. The central question was which policies were more efficient in attracting FDI, in particular what should be the role

of incentives, if any, in stimulating inward investment. There was consensus among the participants that the keys to success are: (a) consistent and coherent economic policies, and (b) a generally favourable environment for business investment (both foreign and domestic). Policies aimed at providing selective incentives to foreign investors created distortions in the economy and were not considered efficient in terms of social welfare in the long run.

42. The success stories among the transition economies are mostly in countries that have managed to provide a stable environment (both economically and politically) and to maintain consistent, transparent and predictable policies. In turn, microlevel success stories indicate the importance of cooperation and policy consistency between the different levels of government: general, local and municipal. In contrast, the inflow of FDI has been much smaller in countries and regions characterized by political and economic instability, crime and corruption, a weak judiciary and poor infrastructure.

43. The experience of some West European countries in instigating FDI-led growth could also be instructive for the transition economies. Thus, Ireland's experience shows that an individual country can do a lot to attract FDI, not only because it could offer relatively easy access to a large market (EU membership), cheap skilled labour and tax incentives but also by consistently delivering on policy commitments (the same policies were pursued over several decades) and by providing supplementary support through related policies (such as education and training and the development of necessary skills) to make those investments long-lasting.

44. One word of caution for the transition economies was that they should take note of the fact that local businesses may not always be interested in promoting FDI since this will increase the competitive pressure they have to face. And when public governance is weak, such interest groups may create serious obstacles to the inflow of FDI. Cartel agreements among local firms and directed against firms with foreign participation are also common in some countries.

45. The transition economies that aspire to EU membership must also gradually harmonize their investment-related policies with those in the EU. Thus, the latter excludes the granting of special privileges to foreign investors, or for that matter to any selected group of businesses. Therefore, some of the special incentives that are in place in some countries (such as duty-free zones, tax holidays and the like) will need to be gradually phased out.

46. It was pointed out during the discussion that while most of the attention has been focused on the policies of recipient countries, there has been considerably less debate on the policies related to outward investment in the countries of origin: there are considerable divergencies among these which may also create distortions. It was felt that there is a need for more cooperation and exchange of information in this field in order to achieve greater uniformity and cohesion.

47. Internationally agreed trade-related policies and rules, in particular in the context of the World Trade Organization (WTO), also have an important impact on FDI, but in terms of policies strictly related to inward and outward investment, progress has been limited. Within the WTO-led negotiations, there have been some attempts during the last three years to unify the international rules that apply to FDI (and to some extent to portfolio investments by foreign agents), and there are some internationally agreed rules on trade in services which partially cover aspects related to foreign investment.

48. Another issue which was debated during the meeting was that of the spillover effects and backward linkages of FDI. It was pointed out that these spillovers are widely considered to be positive (diffusion of new technologies, know-how, managerial skills), but some participants stressed that they can also be negative (the emergence of a dual economy with enclaves of high productivity surrounded by unrestructured sectors of the economy). Policy should aim at maximizing the positive spillovers and minimizing the negative ones. Participants considered that the international community could also do more in this respect by maintaining a regular dialogue between Governments, the private sector, NGOs and other bodies, and by actively disseminating information about best practices and success stories. It was suggested that the business community be involved in discussions during the preparatory phase of the High-level Meeting and be invited to participate in it.

IV. A regional perspective on global financial issues

49. The benefits derived from the mobilization of scarce financial resources — via international capital flowing to the most productive uses — have contributed to economic growth and increased standards of living in all regions of the world.

50. But the recent financial crises in Asia and the Russian Federation have also shown that international capital movements are inherently instable and can trigger severe financial (banking, currency, debt) crises, with attendant severe economic and social costs. In view of their strong dependence on foreign capital, developing countries and transition economies are especially vulnerable to the excessive volatility of such flows. Efforts to mitigate or prevent such financial crises should therefore be at the top of the policy agenda. This is all the more urgent because such crises reflect the impact of both policy failures and market failures.

51. While there is no general agreement as to the future international financial architecture, there is, nevertheless, a general acceptance of the clear responsibility of domestic policy makers to create a sound legal and regulatory framework for the optimal working of markets. International reform efforts are important but are no substitute for sound domestic economic policies.

Codes and standards

52. Codes and standards for improving the quality and timeliness of information concerning major macroeconomic variables and the reporting of financial and non-financial firms were regarded as a necessary condition for allowing more rational decision-making by lenders and investors. It was noted that such standards as the IMF Special Data Dissemination Standard can help central banks to identify data needs. Increased transparency should also allow markets to exercise greater discipline over policy makers and strengthen policy surveillance by the IFIs. Progress in this area has been uneven. It was noted that less progress has been made in the financial reporting of banks and other financial institutions than in the public sector. It was emphasized, however, that global standards and codes should not become straitjackets but rather serve as broad guidelines which should allow for the diversity of countries in terms of development level, history, culture etc.

Financial regulation and supervision

53. The strengthening and restructuring of the financial sector will not be possible without a coherent national regulatory framework. Regulatory reform is therefore a necessary condition for reducing the probability of financial crises and, when they occur, limiting their adverse effects. It was also stressed that there is scope for improving the coordination between national regulatory authorities, particularly in the area of data exchange. There was a consensus that a global regulatory institution (World Financial Authority) is unlikely to be more effective than the coordinated efforts of national authorities in applying global standards.

Conditionality

54. The overriding principle of IFI assistance, including in the field of finance, must be “country ownership”. Conditionality is an essential part of concessional lending, but the nature of conditionality should be reviewed in the context of prevailing domestic economic fundamentals, which will differ across countries. It was noted that conditionality is an important indicator for private investors and lenders.

Capital account liberalization

55. It was acknowledged that “boom-bust cycles” in short-term capital flows can create serious problems for macroeconomic management and financial supervision in the transition economies and other emerging markets. It was suggested that controls on private short-term capital flows may be necessary for reducing excessive volatility and thus ensuring greater stability of the financial system. Such controls should be market-based instruments (e.g., taxes, minimum reserve requirements) and are best seen as complementary to regulatory reform and supervision as well as to increased transparency regarding the activities of Governments, financial institutions and private enterprises.

56. Some participants believed capital controls to be measures to which resort should only be made in case of emergency; others regarded them as essential for economies with fragile financial systems. In any case, capital account liberalization should only occur as the

culmination of a carefully sequenced process of economic reforms and strengthening of domestic financial institutions.

Exchange rate arrangements

57. The general view was that exchange rate regimes cannot be discussed independently of the underlying capital account regime. Any recommendations for exchange rate regimes have to take into account the economic conditions in each individual country. Given that these differ, the appropriate regime will also differ across countries.

58. Between the extremes of freely floating exchange rates on the one hand and strictly fixed exchange rates on the other, there exists a range of intermediate solutions which may fit the specific circumstances of individual countries.

59. It was noted that the instability of freely floating exchange rates can have severe macroeconomic costs in the event of major misalignments. In a region with relatively strong mutual trade links among its constituent economies, an arrangement which aims to limit exchange rate fluctuations (such as the exchange rate mechanism in Western Europe) may be useful but will also require policies to promote real convergence among its members.

60. It was also suggested that the choice of a particular exchange rate and capital account regime not become part of the IMF's conditionality.

V. Conclusion

61. At the closing session, the Chairman presented his conclusions, which were subsequently distributed by him to member States (see Chairman's summary in annex I below). The Chairmen of the working sessions reported briefly on the discussions of their respective subjects along the lines given above. The Executive Secretary of ECE made a closing statement, in which she emphasized that the transition economies in the ECE region had had a decade of experience in dealing with the problems of financing their development, and the meeting had provided an opportunity to draw lessons from success stories and from mistakes.

62. Among the many issues on which she concluded there was general agreement is the importance of mobilizing domestic resources for development, as well as the need to support national efforts with a conducive and enabling international environment. The key role of effective institutions was repeatedly emphasized, as was the importance of implementing agreed rules and policies. The complementarity of all the various forms of finance was stressed, and while agreeing on the importance of private investment, the continuing relevance of public funds in playing a catalytic role was also underlined. Another important theme was the need to deal with the social costs of transition, not only on grounds of social justice but also to avoid social discontent undermining the transition process itself. Reducing government expenditure on unproductive subsidies to inefficient enterprises was obviously necessary, but the resources released could be productively used to support well targeted social expenditure. The important role of the local level with regard to financing for development was stressed, as well as the fact that state decentralization reforms could be seen as a catalyst for a larger active participation of the local community in regional development projects. The necessity to generate new and innovative forms of financing was also emphasized. Another point on which there was agreement was the need for close regional and subregional cooperation as a means of optimizing the use of limited resources. The positive role of conditionality was also recognized, but it was stressed that donors and recipients should enter into a constructive dialogue so that eventually conditionality would be subsumed into an effective partnership. The Executive Secretary also highlighted the considerable diversity of Europe, which in turn underlined the need for partnerships between all the actors involved, from Governments to private enterprises and NGOs etc., and the importance of maintaining a dialogue on all the issues affecting the economic and social development of the region. From this perspective, the meeting had made a constructive and significant contribution.

Annex I

Chairman's summary

Representatives of the member States of ECE and of the Bank for International Settlements (BIS), the European Community, the European Investment Bank (EIB), EBRD, the United Nations Conference on Trade and Development (UNCTAD), the World Bank, IMF and several commercial banks, private companies and NGOs met in Geneva on 6 and 7 December 2000, for a regional consultation meeting, as requested by the Preparatory Committee for the High-level International Intergovernmental Event on Financing for Development, to:

(a) Exchange views and experiences on attracting foreign and domestic public and private financial resources in transition economies and using them for development;

(b) Highlight the lessons and conclusions which could usefully be taken up in the overall substantive preparatory process leading up to the High-level Event, as well as their shared views and ideas on the global aspects of financing for development, with which they can contribute to promoting the overall financing for development process.

Participants noted that their heads of State and Government, in the Millennium Declaration of 8 September 2000 (General Assembly resolution 55/2), had resolved, inter alia, to create an environment — at the national and global levels alike — which is conducive to development and to poverty elimination; had expressed concern about the obstacles that developing countries face in mobilizing the resources needed to finance their development; and had therefore committed their Governments to make every effort to ensure the success of the High-level Event.

It was recognized that the ECE region has a vast and varied fund of experience, particularly from the last 10 years, but also from the post-war years of reconstruction, that is relevant to the work of the financing for development process. This experience highlights the diversity of the situation of individual countries — calling for diversity in ways of addressing their situation — and illustrates the fact that broad local ownership of development strategies is the key to success of development policies.

Staying focused on the need to enhance governance and putting in place domestic policies and regulatory frameworks conducive to savings and investment, including foreign investment, was thought to be important to growth and social advancement. In this regard, many considered the advice contained in adjustment arrangements of the IFIs to be important. There was general agreement on the cardinal importance of supporting the development of the capacity and institutions necessary for the good functioning of market economies, including the ability to ensure sustainability of development from a human and social perspective through a fair social distribution of the development outcome.

Corporate governance was believed to be an area in need of special attention, as was the development of domestic financial sectors. Furthermore, SMEs were seen to have a strong role to play in sustaining and broadening growth and in providing a conducive economic environment and a constituency for reform. It would also be fundamental to bring the knowledge, innovative spirit and capital of informal entrepreneurs into the mainstream of development.

Regional cooperation was highlighted throughout the meeting as crucial to enabling developing and transition countries to enter the global economy and to stimulating foreign direct investments, and as a determining factor contributing to peace, conflict prevention and reconstruction. The Stability Pact aimed at assisting the countries in South-East Europe to cope with the effects of war and the need for peace-building and reconstruction was emphasized by several as an example of such cooperation, but it was stressed that it had been preceded by many others, such as the Central European Initiative.

There was general agreement that a more open and accessible trade environment, providing access for the least developed countries to the markets of the developed countries, is key to their integration into the international trading system and to the success of their efforts to combat poverty.

It was agreed that a stronger effort was needed to prevent financial instability and crisis. A less rigid understanding of the right approach to capital account liberalization and choice of currency regime seemed to be emerging. Access to capital markets was a key to development in the longer run. However, it should be recognized that markets were volatile and access consequently not guaranteed.

Greater mobilization of resources and more effective cooperation are keys to achieving the international development goals endorsed by the international community. There was widespread agreement that more genuine collaboration among the various partners in development, such as Governments, the United Nations system, the Bretton Woods institutions and the regional development banks, as well as non-governmental organizations and the private sector — which is the essence of the financing for development process — was required to meet the goal. Attention was drawn to the special value of the participatory approach followed by EBRD and others. The United Nations Development Assistance Framework, the comprehensive development framework and the poverty reduction strategy papers were mentioned as timely and appropriate types of instruments aimed at fostering a spirit of cooperation.

Cooperation, however, must respect the diversity of situations and of cultural and historic backgrounds. Many participants pointed to the need for a properly customized and phased approach to development cooperation. Several representatives also underlined the need for external partners to stay engaged and not withdraw from countries too early since this might put achievements into jeopardy. Yet, in the longer perspective, assistance should be considered a transitory phenomenon. As countries developed, they themselves should become providers of support to less advanced nations.

It was recognized that ODA remains an indispensable component of development finance. Representatives of the donor countries committed to the 0.7 per cent of GDP target for ODA reaffirmed their commitment to reach this target as soon as possible. ODA is additional and complementary to national resources. The view that ODA should play a catalytic role in mobilizing private resources, including foreign direct investment, was widely held. Selectivity was also considered a precondition to the effectiveness of assistance, with such criteria as the quality of policy, the opportunity for making a difference and the availability of funding from other sources being mentioned by participants.

Timely implementation of the heavily indebted poor countries (HIPC) initiative is fundamental to enabling countries concerned to set aside sufficient resources for poverty reduction and investment in the social sectors.

With respect to middle-income countries, it was found desirable to concentrate efforts in countries where the proportion of the population below the poverty line remains high.

The financing for development process should be an occasion not only for mobilizing resources for development but also for taking stock of the goals formulated by the United Nations conferences on sustainable development of the 1990s.

Participants saw the financing for development process and the High-level Event as a unique opportunity to strengthen the international community's understanding of a number of factors essential to development and poverty reduction. It was seen as a response to the necessity for greater coherence in policies and among actors at both the national and international levels, representing a comprehensive approach that takes all policies into account, with particular regard to financing and trade.

The Financing for development process holds the potential of developing coordinated leadership for the promotion of sustainable human and social development on an equitable and participatory basis.

By uniting all major actors and stakeholders around a shared analysis of how financing for development can be achieved, a shared sense of purpose and of direction can provide a strong and continuous motivation for political and economic action with the involvement of all for the benefit of all.

Annex II

Programme of the meeting[1]