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INTERVIEW WITH HEINER FLASSBECK

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1. What is the main message of this year's Trade and Development Report (TDR)?

HF – The main message is that there is hope for the developing economies. In the past four to five years they have considerably improved their performance. And we see that under favourable conditions, like high commodity prices, low interest rates and competitive exchange rates, many developing countries have the potential to grow fast, to catch up and to reduce poverty. This means that if developing countries can implement pro-growth policies, their economies will respond quickly despite shortcomings regarding the traditional "reform agenda". If that is understood well at both the national and international levels we can be optimistic that good progress in achieving the Millennium Development Goals (MDGs) is possible.

2. The subtitle of the TDR 2006 is "Global Partnership and national policies for development". The Global Partnership for Development refers to one of the Millennium Development Goals (MDGs). What development strategies does the TDR advocate to support the achievement of the MDGs?

HF – Overall, I believe we need more insight into the restrictions imposed by international rules and disciplines, and the opportunities offered by globalization. Developing countries need more flexibility in implementing policies that impact on their structure and economic growth. This concerns mainly the multilateral trading system. We believe the system should be more flexible to allow developing countries to integrate trade into their overall development strategies more effectively than in the past.

At the same time, there is a need to build a multilateral monetary system as trade flows are also determined by monetary factors like exchange rates. But the consequences of building a new global monetary system are far from clear. Sure, the establishment of a multilateral monetary system would take away some of the developing countries' "room for manoeuvre", but the benefits would outweigh the disadvantages. Changes in countries' competitive positions would be less chaotic; the danger of financial crises would wane. Even more important, an effective monetary system would help countries adjust and integrate more smoothly into the globalized economy. It would reduce the need to protect their economies by running huge current account surpluses and by piling up huge amounts of reserves.

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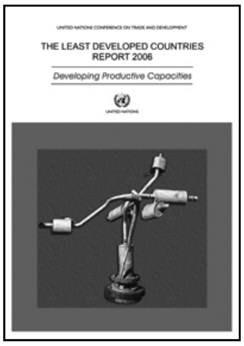
Least Developed Countries Report: Developing Productive Capacities



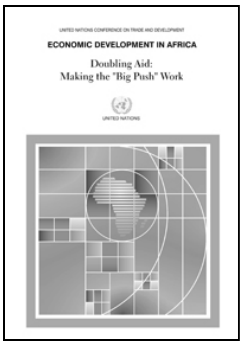
The economies of the world's 50 poorest countries have perked up recently – at least on average. The growth rate for LDCs as a group was 5.9% in 2004. But one-third of LDCs are still experiencing economic decline or sluggish growth. Even in those which are growing rapidly, there is a widespread sense that this is not translating effectively into reduced poverty and improved well-being. The sustainability of the recent growth surge is also questionable as it reflects higher commodity prices and aid inflows.

The key to reducing poverty sustainably in the world's poorest countries, the report contends, is to **develop productive capacities**. It urges governments and international aid programmes to focus on enabling such countries to develop the ability to produce, efficiently, goods and services that can be sold both at home and abroad – goods and services that gradually increase in quality and sophistication. This will encourage a "virtuous circle" of increasing employment and stable growth. A country that succeeds at this process will eventually no longer need international aid.

Doing this requires shifting the focus of current aid programmes, the report says. International assistance for such matters as infrastructure improvement and enhancement of productive sectors in LDCs accounted for only 24% of aid in 2003-2004 – down from 48% in 1992-1994.

In the LDCs, 70% of the labour force still earn their living from agriculture. But the report shows that, for the first time, during the decade 2000-2010, the increase in the number of people seeking work outside agriculture is predicted to be greater than within agriculture. Governments thus need to develop productive capacities in a way that creates jobs and livelihoods both within and outside agriculture.

Economic Development in Africa – Doubling Aid: Making the «Big Push» Work



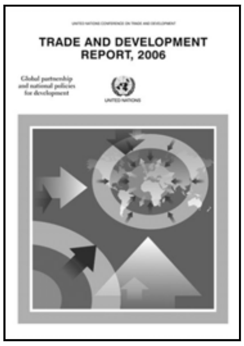
Donor countries have committed themselves to doubling aid to Africa. But simply increasing international assistance will not lift the continent out of poverty, this report argues. The current aid system is a chaotic mixture in which too many agencies – some bilateral, some multilateral – are pushing too many development projects that sometimes compete with each other. They are often determined by donor preferences rather than recipients' development goals, are costly to administer, and frequently leave African governments confused and stymied by their numerous rules and conditions.

The system should be changed, the report says, and most assistance should be distributed multi-laterally, perhaps by a UN fund independent of political pressures and unwedded to a particular development ideology. The money should be released in predictable doses over a long-term period. It should be focused more than currently on enabling African economies to produce a broader range of goods and to create more jobs, and should be channelled to those countries' general budgets.

Such a new "aid architecture," UNCTAD economists say, would share some characteristics with the Marshall Plan that helped revitalize European economies after World War II. That plan, paid for by the United States, recognized that shock therapy and piecemeal approaches had not helped in getting Western Europe back on its feet. Instead, it offered a generous, multi-year and coordinated funding approach, with each State drawing up its own long-term recovery plans with no outside interference. It released aid in predictable tranches, predominantly through grants.

This, along with the experience of East Asia in the 1950s and '60s, and Ireland in the early 1970s, indicates that increased aid, if well managed, could give a "big push" to the African region. It could spark a virtuous circle of higher rates of savings, investment and economic growth as a route to a permanent reduction in poverty, the report says.

Trade and Development Report, 2006: Global Partnership and National Policies for Development



The world economy has been growing at a rapid pace, yet mounting global imbalances pose a significant challenge. The United States has been pulling the global economy, but at the cost of an ever-widening trade deficit. This pattern can't go on forever.

In this new report, UNCTAD economists call for a multilateral effort to redress global imbalances. This can be achieved, in part, through an expansion of demand in key industrialized countries other than the US – countries such as Japan and Germany, which have huge surpluses. In this way, a recessionary adjustment and financial turbulence that might reverberate through the developing world could be avoided.

Meanwhile, governments of developing countries are urged to take a pro-active stance in macroeconomic, trade and industrial policies. This would accelerate private investment and technological upgrading and stimulate the creative forces of markets.

Until domestic producers can meet international competition in the sale of increasingly sophisticated products, governments should promote fledgling enterprises, including through the careful application of subsidies and tariffs. They should also aim at pro-growth macroeconomic policies, through moderate interest rates and competitive exchange rates. This is in contrast to the 1980s and '90s, when they were advised to keep their hands off and let market forces do the work of "getting the prices right."

In addition, the report says, developing countries should not be overly restricted by international trade rules or by conditions imposed by international lenders from doing what's best for their economies. Such freedom of action has become a major issue in recent years and is often referred to as "policy space."

Interview with Heiner Flassbeck (part 2)

3. Although no crisis seems imminent, the report warns that a tumbling dollar could lead to financial shocks and threaten the growth performance of the world economy. What can be done to redress the situation?

HF – Well, the systemic reasons for the global imbalances have to be removed. What we call systemic reasons are the attempts by developing countries to defend the favourable positions they found themselves in after their financial crises. In Asia that was the crisis of the 90s. In Latin America it happened a little later. Following these crises and the devaluation of their currencies, many developing countries defended their favourable competitive positions by implementing their own pro-growth national policies.

Many countries, and we confirm that this was the only reasonable way to react, stabilized their exchange rates at low levels (some experts say undervalued levels) – a level where countries are not threatened by currency depreciation. On the contrary, if under pressure, currencies are more likely to appreciate.

Stabilizing their exchange rates gives governments and central banks sufficient autonomy to buy foreign currency on the money market with their own currencies – and the latter is available at infinite amounts because it can be printed! If you are intervening with your own money you can always fight speculation. If you are intervening with foreign money, with your reserves, it is more difficult. Developing countries learned this the hard way during the financial crises.

This explains why countries would rather avoid current account deficits and short term capital inflows. They try to preserve their independence from the international capital markets. That is an important achievement for these developing countries individually but, on a global level, it has resulted in huge imbalances. Only concrete steps towards a new multilateral system – somewhere along the lines of the old Bretton Woods system – can help to unravel the global imbalances without major exchange rate shocks. Unilateral pressure on certain developing countries doesn't work.

4. You have just mentioned policy space and have defined it as room for manoeuvre. Could you explain why it is such a controversial issue?

HF. UNCTAD's constituencies in developing countries and the mandate UNCTAD was given in 2004 at its 11th Conference, have asked us to look at the restrictions globalization and international rules and disciplines have imposed on them. In other words, we were asked to analyse the effects on developing economies of the opening of both the global economy and the goods and the capital markets.

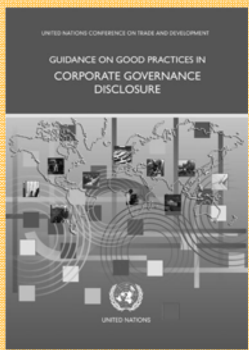
Many developing country governments feel they no longer have the options the developed countries had in the past to take the measures they need for their development strategies. This is what Cambridge economist Ha-Joan Chang referred to as "kicking away the ladder".

That is why we looked systematically into the question of policy space: is policy space too limited or not? On the one hand, multilateral agreements – mainly the WTO agreements – restrict the ability of developing countries to adopt national economic instruments in the areas of trade and industry. On the other hand, multilateral rules offer stability and protect against unfair practices. Unfortunately, as we have shown in the report, even with fair rules, economically powerful nations may be better off than the less powerful.

On the trade side, we could achieve more flexibility for developing countries if the design of some of the rules was changed slightly. Regarding finance, a multilateral agreement would no doubt reduce their "room for manoeuvre", but it would give them more stability and some kind of guarantee that they will not face the same kinds of crises they experienced in the last ten years.

Other publications

FDI in Least Developed Countries at a Glance:2005/2006



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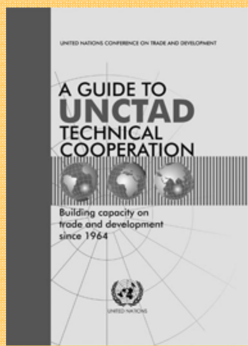

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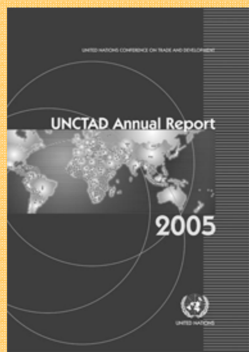

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