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DRAFT REPORT OF THE TRADE AND DEVELOPMENT BOARD ON ITS FIFTY-FIRST SESSION

Held at the Palais des Nations
from 4 to 15 October 2004

Rapporteur: Mr. Patrick Krappie (South Africa)

Speakers:

Officer-in-charge of UNCTAD	Russian Federation
Officer-in-charge of GDS Division	Colombia
Brazil for the G77 and China	China
Netherlands for the European Union	Switzerland
Uruguay for the Latin American and Caribbean Group	Egypt
	Peru
Pakistan for the Asian Group and China	Sri Lanka
Nigeria for the African Group	Cuba
Indonesia	Belarus
Islamic Republic of Iran	Venezuela

Note for delegations

This draft report is a provisional text circulated for clearance by delegations.

Requests for amendments to statements by individual delegations should be communicated by **Tuesday, 19 October 2004** at the latest, to:
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INTERDEPENDENCE AND GLOBAL ECONOMIC ISSUES FROM A TRADE AND DEVELOPMENT PERSPECTIVE: POLICY COHERENCE, DEVELOPMENT STRATEGIES AND INTEGRATION INTO THE WORLD ECONOMY

(Agenda item 3)

1. For its consideration of this item, the Board had before it the following documentation:

Trade and Development Report, 2004 (UNCTAD/TDR/2004 and Overview).

2. The **Officer-in-Charge of UNCTAD**, introducing the item, said that part two of the *Trade and Development Report* (TDR) looked at the issues and challenges arising from greater trade and financial integration from a historical perspective and then at the impact of monetary and financial factors on the supply-side of developing-country exports. It examined the particular effects of sharp and abrupt currency depreciations on the trade performance of developing countries and went on to analyse policy options with regard to exchange-rate management in a volatile international financial environment. Part one of the TDR reviewed, from a development perspective, recent trends and prospects in the world economy.

3. The **Officer-in-Charge of the Division on Globalization and Development Strategies** said that growth in the world economy was gaining momentum but that there were risks that made the outlook uncertain, including the rise in oil prices, the persistently large disparities in the strength of domestic demand among the major developed countries as well as among different regions in the developing world, and the increasing trade imbalances between the major economic blocks. In addition to a favourable international trading environment and favourable microeconomic conditions, the TDR stressed that macroeconomic policies, especially those related to interest rates and exchange rates, also determined whether developing countries reaped the full benefits of their integration into the world economy. It showed that inflows of short-term capital had often led to exchange rate appreciation, jeopardizing the cost competitiveness of domestic exporters. Ensuing sudden and massive outflows of capital had restored competitiveness, with positive effects on the country's trade performance in the short run, but had led to negative effects in the medium and long run. Countries with an open capital account were vulnerable to such international short-term capital movements. An increasing number of developing countries had chosen policies to avoid currency overvaluation by intervening in foreign-exchange markets and accumulating substantial amounts of international reserves. Associated potential inflationary pressures could be countered by non-monetary policy measures. However, not all countries could simultaneously manage the movements of their exchange rate and achieve their target rates. Hence, there was a need to establish a rules-based and truly multilateral monetary system.

4. The representative of **Brazil,** speaking on behalf of the **Group of 77 and China**, said that the pattern of world trade had changed in significant ways since the early 1960s, most notably with the rise of new manufacturing exporters, particularly in East Asia. However,

many developing countries had been trading more but earning less since the mid-1980s. The new geography of international trade provided some hope that this situation might change as the role of developing countries as producers, consumers, traders and resource providers became more important, intensifying complementarities with developed economies. This underscored the need for enhanced growth in developing countries, which was critical to ensure growth in the world economy and maintain prosperity in developed countries. It was thus essential that the developed countries re-evaluate their policies, as well as their development cooperation programmes.

5. The call for more policy space, which had already been at the heart of the first session of UNCTAD, had been formally recognized at UNCTAD XI in paragraph 8 of the São Paulo Consensus. In this regard, he highlighted the importance of the recent "Proposal to Establish a Development Agenda for the World Intellectual Property Organization (WIPO)". The Proposal sought to place development concerns, including the need to safeguard the policy space of developing countries, at the heart of the intellectual property system. Over the past two decades, many developing countries had seen the erosion of their policy options. This could, in part, be traced to the adoption of new rules and obligations in the trading and financial systems, along with heightened surveillance. But just as important had been the influence of assumptions and prejudices that confused the means and the ends of development, and which proved to be simple, technocratic solutions that took no account of national differences and constraints.

6. He restated the need for improved systemic coherence in support of development. All countries needed to recognize that their actions could affect others, and had to act accordingly. The policy actions taken in the leading economies reverberated asymmetrically around the system, and those economies that had the financial, technical and institutional capabilities required to correct any potential imbalances in the pattern of trade, capital and technological flows ought to contribute to ensuring the required degree of global economic stability. The TDR recalled that, in the absence of properly integrated treatment of international economic relations, the unrestricted flow of capital could produce sharp discontinuities between international finance and productive development, allowing independent currency movements to once again have a profound impact on trade and growth prospects in poorer countries. The Report's call for a genuinely multilateral solution to currency volatility was timely.

7. Analyzing recent trends in foreign direct investment, the *World Investment Report 2004* (WIR) also considered a relevant aspect of the interdependence debate. While FDI flows to developing countries as a group had risen in 2003, many low-income countries continued to face difficulty in attracting FDI in industries where it could contribute to development. The focus of the WIR on FDI in services was timely given the importance of the services sector in the efficient operation of any economy and in poverty alleviation. Developing the necessary tools to counter restrictive and anti-competitive business practices followed by transnational corporations was important, as an exclusive focus on restrictions from government-mandated regulations had to be avoided. FDI in services could bring capital and help meet domestic financing needs, lead to improved quality of services and transfer technology, but carefully designed and well conceived policies had to be in place to ensure that the potential benefits of FDI would actually be realized. The WIR also made a valuable

contribution to the debate on services outsourcing, which could enable many developing countries to develop export capabilities and create new jobs.

8. The representative of the **Netherlands**, speaking on behalf of the **European Union**, agreed with the view that longer-term growth and the trading opportunities of the more advanced economies also depended on the expansion of industrial capacity and markets in the poorer countries, as well as with the call for a collective approach, at the global or the regional level, susceptible to foster coherence between the international trading, monetary and financial systems. That, of course, still left open the question of what forms these systems should develop into, as well as the modalities of their interplay. While welcoming UNCTAD's contribution to this debate, considering its mandate to provide an interdisciplinary perspective, she stressed that the main protagonists in these matters were the WTO for trade and the Bretton Woods institutions for monetary and financial questions. Regarding the concept of policy space, there was a risk of an inappropriate use of policy space that could lead to negative effects on other countries. The scope of the use of policy space differed from country to country and from situation to situation. Countries would always need to consider the impact of their use of policy instruments on other countries, both in the bilateral and in the broader multilateral context. There was no single formula in the sense of one size fits all. For example, though some advanced developing countries were using their policy space to maintain their currency at deliberately low exchange rates, such an approach could not be recommended for all developing countries, and in particular not the LDCs. She proposed that UNCTAD not limit itself to indicating which strategies, in certain parts of the world and at certain times, had proven successful, but present alternative scenarios, based on certain plausible assumptions, including those which would require concerted actions on the part of the international community.

9. The representative of **Uruguay**, speaking on behalf of the **Latin American and Caribbean Group**, said that meeting the Millennium Development Goals required greater coherence between international processes and negotiations, mainly in the areas of trade, investment, finance and technology, and the different national development strategies to accelerate economic growth and promote sustainable development. As shown in TDR 2004, after a prolonged stagnation, the economies of Latin America and the Caribbean had been recovering since the second half of 2003. However, the fact that this recovery was the result of an increase in the prices of exports from Latin America and a decline in international interest rates confirmed the vulnerability of Latin American economies to commodity price movements and to conditions on international financial markets. There were therefore doubts about the extent and sustainability of the recovery. In order to evaluate to what extent the improvement in the external situation of the region was the result of long-term trends or short-term fluctuations, three elements had to be considered. First, the situation in the different economies of the region was not uniform; second, the short-term factors which had favoured most of the economies in the region could rapidly disappear; and third, structural factors that prevented high and sustained growth, such as unemployment, unequal income distribution, foreign debt and low levels of investment, continued to be present. In order for recovery to translate into sustained growth, domestic policies needed to better promote the recovery in investment and employment, but, at the same time, there was a need to create a new international framework that would be more favourable to development and better reinforce the coherence between the international trading, financial and monetary systems. Regarding the international trading system, substantial improvements in the multilateral

trading system under the Doha objectives were required, in particular fair rules for trade in goods and services of interest to the region and non-distorted access to all markets. Likewise, destabilizing effects that international financial markets could have on the developing economies should be avoided, as they could nullify the gains obtained through trade. This was a key factor, because, apart from a favourable international trading environment, developing countries needed to have competitive companies in international markets to maximize their benefits from integration into the global economy. Among the many factors that affected competitiveness, macroeconomic policies had to be taken into account, mainly those related to interest rates, a key factor for domestic investment, and exchange rates, a key factor for performance in international trade. Only coherence could ensure that greater trade and financial integration would allow developing countries to establish a virtuous circle between external finance, domestic investment and expanding exports. Given its mandate, UNCTAD played a major role in identifying the elements required to elaborate a coherent global strategy that would integrate the development dimension in the global processes.

10. The representative of **Pakistan,** speaking on behalf of the **Asian Group and China**, said that globalization might be a virtual ideology of modern existence with potentially far reaching developmental implications, but the reality so far belied the expectations. Economic and social transformations unleashed by globalization had outrun the capacities of many developing countries to handle their consequences. While developed countries were enjoying the dividends, developing countries continued to suffer from a host of problems, including poverty, lack of financial resources for development, heavy debt burdens with the associated reverse flows of capital from developed to developing countries, deteriorating terms of trade, increasing financial risks, and low levels of technological development. These problems not only hampered the healthy development of the global economy but also posed a threat to global security. They were aggravated by diminishing policy space as developing countries battled to retain some measure of control over their sovereignty so as to prevent the emergence of underdevelopment. It was rather paradoxical that the protagonists of globalization called for the improvement in national governance while the present set of global rules progressively encroached on the essential policy space.

11. Concerning the doubts expressed in TDR 2004 about the sustainability of the current growth pattern of the world economy, particularly its dependence on further expansion in the United States, the latest developments in Asia could to some extent contribute to redressing this imbalance. The fast-expanding external sector in Asia had been complemented by robust domestic demand in the region. Import growth was expected to outstrip that of exports this year. As the trade surpluses narrowed, Asian reserve accumulation could slacken. The pass-through of the income effect of trade expansion was partly the reason for this phenomenon. Another reason was that fast economic growth induced income demand for a variety of goods.

12. Slow growth, stagnation of per capita incomes and continuing commodity dependence in much of sub-Saharan Africa, and the growing likelihood that the Millennium Development Goals would not be attained in that part of the world, were serious concerns. The fragility and hollowness of the current growth pattern in the global economy underscored the need for a collective rethink aimed at broad-based and synchronized development. In order to prevent the development gap from widening and eventually to close it, he proposed a comprehensive

and collaborative seven-point approach: (i) a measure of intellectual rectitude based on a people-centred, inclusive approach to development; (ii) good governance of globalization ensuring inclusive and transparent structures of international economic decision-making; (iii) conclusion of the Doha Work Programme aimed at seeking an equitable and just multilateral trading system; (iv) fair access to knowledge and technology; (v) adequate and innovative financing for development involving debt relief and debt swaps; (vi) corporate social responsibility; and (vii) economic policy space at the national level to formulate and tailor development strategies in accordance with country-specific needs and circumstances. The São Paulo consensus provided UNCTAD with a sound mandate for substantive work in each of these areas.

13. The representative of **Nigeria,** speaking on behalf of the **African Group**, said that recent developments in the world market for oil showed that actions or events in one country could have reverberations in the rest of the world. Such interdependence could benefit the global economy, as shown by the trade and finance links between the United States and Asia, especially China, that were not only propelling global growth but also benefiting other developing country regions through, for instance, a higher demand for primary commodities. Africa, in spite of widespread pessimism and the realization that the continent might not be able to meet the Millennium Development Goal of halving poverty by 2015, was also benefiting from these links, as Africa's trade with China had sharply increased during 2003. But interdependence could also have adverse effects. Global growth could be threatened by a simultaneous slowdown in the United States and Asia, without being counterbalanced by growth in other major economic centres. The widespread feeling that the macroeconomic imbalances in the United States and the investment boom in Asia might not be sustained over time pointed to a possible hard-landing of the world economy. Moreover, a further sharp dollar depreciation might curtail demand in the United States and choke off the export-led growth in Asia. The exchange rate could be a major trade policy instrument, yet large depreciations might not bring about the desired increase in cost competitiveness and might even bring about pressures for trade protectionism, with attendant risks to the world economy. This lack of coherence between the international trading system and the international monetary and financial system made it worth considering the proposal of the TDR to search for an appropriate exchange rate system at the regional and global levels.

14. Rising oil prices posed another risk to global growth. While part of the rise in oil prices was due to the huge demand in the two growth poles, combined with supply constraints, fears of supply disruption were fuelling speculation. Some viewed the rise in oil prices as temporary and unlikely to harm the developed economies due to their prevailing low inflationary environment. But it was also possible that the situation might not be easily reversed. Some had argued that the situation was serious enough to warrant cooperation between producers and consumers to stabilize prices. This was an intriguing suggestion for policy coherence, because cooperation between producers and consumers was not often admitted as a possibility in the handling of other commodities. Oil-importing developing countries, especially the least developed ones, would face additional difficulties as a result of higher oil prices and require assistance. Recent proposals for debt relief for some of them were welcome in this respect. In addition, concrete efforts would be required to increase the quantity, quality and effectiveness of aid.

15. Policy coherence required broadening and strengthening the participation of developing countries in international economic decision making and norm setting, not only because of the contribution of some developing countries to global growth but also because the governance of globalization needed to ensure policy coherence in favour of development. Many countries in Africa had severe capacity constraints but were undertaking negotiations at the bilateral, regional and multilateral levels. He supported the call for developing countries to have greater policy space, implying that there could be no one-size-fits-all approach to development and that the scope and options for domestic policy should not be choked off by international rules.

16. The representative of **Indonesia** said that while global economic recovery was under way, it might not be sustainable given the challenges posed by the economic conditions in the United States and by instability in oil prices and exchange rates. These challenges needed to be managed carefully so as not to harm economic development in developing countries. Given that volatility in international financial markets and short-term capital flows could adversely affect trade and reduce the competitiveness of developing country exporters, the question arose as to how the international trading system could address the effects of exchange rate uncertainty on trade. While the GATT included balance-of-payments provisions, the associated stringent conditions had made it difficult for developing countries to invoke them. The provision regarding instability in financial flows and the capital account also deserved further attention in future trade negotiations. New policy instruments were needed to help developing countries to converge with the levels of efficiency and affluence seen in the advanced countries, and to improve the welfare of all groups of their populations. In today’s interdependent world, the successful development and integration of the developing countries was in the mutual interest of all countries. He called on UNCTAD to continue and sharpen its analytical work, and to broaden its technical assistance programmes to meet the increasing needs of developing countries as they encountered complex challenges arising from trade liberalization and globalization. UNCTAD should also conduct further studies on how the WTO could address exchange rate instability and operationalize the concept of policy space, as well as strengthen its analytical work to encourage TNCs to implement the provision of corporate social responsibility. Promoting coherent policies within and between the major stakeholders and international institutions was crucially important in efforts to attain the Millennium Development Goals.

17. The representative of the **Islamic Republic of Iran** said that several recent or upcoming meetings and reports were giving new impetus to multilateralism and collective decision making at the international level. The new international trade geography had been shaped by the rising importance of South-South relations, as well as by effects of the enlargement of the European Union, new measures in regional organizations, and bilateral treaties. UNCTAD should analyse the impact of these impacts on international trade with a view to mainstreaming development in international trade negotiations.

18. The issue of energy was becoming ever more important and complex. The challenges faced by some developing countries in accessing all sources of energy would undermine their efforts to achieve sustainable development. The absence of some of the most important energy exporters in the decision making process of WTO was an impediment to concluding long-standing solutions in this sector. The establishment of the UN Energy Task Force and

the preparation of the UN Energy Programme, the dialogue between producers and consumers, and the involvement of international and regional organizations in different initiatives could lead to long-term cooperation of all stakeholders. He encouraged UNCTAD to take part actively in this process and expand its relations with OPEC, WTO and regional organizations. During the past decades, many developing countries had tried to establish coherence between national development strategies and global processes, but the failure of the openness model and the Washington Consensus had made attaining development objectives more difficult than 20 years ago. Most developing countries were suffering from the lack of attention to their specific development needs and the lack of coherence between the international trading, monetary and financial systems. Balancing national policy space and international disciplines could allow developing countries to fully integrate into the multilateral trading system.

19. The representative of the **Russian Federation** said it was increasingly clear that addressing global challenges and threats in the socio-economic area and settling global political issues were interrelated. The uncontrolled and uneven character of globalization was an additional burden on the world economy and deepened the socio-economic differences between countries, nourishing crisis elements in many countries and regions of the world. This, in turn, worsened existing international security problems and created new risks and challenges, such as international terrorism, which became an obstacle to the normal functioning of international trade and economic relations and the implementation of development objectives. A comprehensive and joint approach was required to ensure effective management of the globalization process and minimize negative impacts. Increased coordination of trade, monetary, financial, investment and social policies at the national and international levels was of prime importance in this context. In the current globalization era, poverty eradication and sustainable development could be achieved by combining the efforts of all members of the world community. For its part, Russia was contributing to achieving set goals, as it was one of the countries among the G-8 that provided most debt relief in the framework of the HIPC Initiative and was ranked first in terms of the debt relief to income ratio. Russia also granted important trade preferences to the developing countries, and the products of the least developed countries were imported duty free. Efforts undertaken at the international level could succeed only if they were accompanied by well-conceived socio-economic, infrastructure, financial and investment policies at the national level.

20. The representative of **Colombia** noted the importance of global security when talking about interdependence and international economic questions from the perspective of trade and development. The poverty that affected millions of people in the world was an important source of instability. Globalization was reflected in many factors, such as trade rules, exchange rates, environmental degradation, migration, conflict situations, drug trafficking and sustainable development. Concerning trade, it was fundamental that the multilateral system functioned in accordance with the wider objectives of human development. International cooperation needed to fulfil the objectives of the Social Summit in Copenhagen. There was also a need for more technical cooperation, the elimination of tariff and non-tariff barriers to trade, and progress towards the free movement of people and the liberalization of trade in services. In general, there should be progress towards meeting all the commitments established in the Doha Work Programme and at UN Conferences. Fighting poverty was a major component for global security in an interdependent world. For developing countries in situations of violence and conflict, there was the challenge of attaining equity and social

cohesion, while defending the civil population through legitimate action by the authorities. Continued support from the multilateral banks and better understanding of the specific needs of developing countries from financial markets were also needed. In order to consolidate global security, the principle of shared responsibility should function effectively. Lasting stability would be attained through shared responsibility for cooperation to finance and promote development, eradicate poverty, fight terrorism and corruption, and solve the problem of illicit drugs. UNCTAD and the Board should further reflect on the issue of inequality.

21. The representative of **China** said that the global economic recovery was continuing. World trade was also growing, with more flows of cross-border investment, but there was still an imbalance between trade growth and capital flows. In order to cope with the challenges posed by globalization, various forms of economic and trade cooperation had emerged, with the number of regional and bilateral free trade arrangements increasing sharply. It was widely hoped that the new round of the WTO multilateral trade talks would lead to a framework convention to improve international multilateral economic and trade cooperation and create the conditions for steady global economic development. Only if the international policy environment was compatible with national development strategies could developing countries integrate smoothly into the world economy.

22. One major current challenge for developing countries was how to ensure an open process of liberalization while maintaining the necessary policy space. The current effort to shape international economic rules needed to take account of the interests of developing countries. In the Doha Round it was particularly important to take account of the disadvantageous position of the developing countries and assist them in upgrading their negotiating capacity. The developed countries needed to face up to the need for structural reform in their economies and abandon protectionism. The international community needed to further enhance the coordination of development policy aimed at facilitating development financing, enhancing technical and financial support for the developing countries and improving the international economic environment. Only with a fair international economic order could developing countries effectively undertake policies for their self-development or conduct economic reforms adapted to their national conditions.

23. The representative of **Switzerland** said that strong intra-regional trade in East Asia, driven by China and India, had had a positive impact on economic growth in the countries of the region. An important challenge consisted in ensuring that progress in Asia had positive implications for sub-Saharan Africa. Chapter 4 of the TDR was full of useful data, analyses and ideas. He agreed that the impact of exchange rate policies on international trade deserved attention, but he did not share the chapter’s main conclusion. The proposed multilateral exchange rate arrangement amounted to suggesting a pegged exchange rate system where exchange rate adjustments needed to be approved under a multilateral arrangement between the countries involved, using purchasing power parity as a decision criterion. The mechanism was only briefly explained in the Report, lacked conceptual foundation and was unlikely to lead to any net improvements over existing exchange rate regimes. Some of the suggested components would make the arrangement appear hard to implement because (i) pegged exchange rates were vulnerable to speculative attacks; (ii) selecting an appropriate exchange rate system needed to take into account a country’s structural characteristics; (iii) judging the

extent of a currency's over- or under-valuation was difficult and negotiations could prove cumbersome in the absence of a generally accepted approach to defining the equilibrium exchange rate; (iv) the enforcement mechanism was left open; and (v) the issue of a country losing monetary independence was downplayed in the Report.

24. The representative of **Egypt** said that the importance of the issue of policy space in a globally interdependent world and the ensuing need for policy coherence had already been recognized at the first session of UNCTAD and had now been reaffirmed in paragraph 8 of the São Paulo Consensus adopted at UNCTAD XI. While the need for policy space as such was obvious, it was less clear how to operationalize and implement it. Thus, further elaboration of what the concept did and did not entail was required, as mandated in paragraphs 8 and 26 of the São Paulo Consensus. This work should be based on three separate, though interrelated, pillars: (i) further conceptual work by UNCTAD to elaborate on the concept, its implications and means of operationalizing it without prejudicing the current multilateral economic regimes; (ii) a continued dialogue at the intergovernmental level and through future hearings of civil society to allow all stakeholders to voice their views; and (iii) a mainstreaming of this issue in all aspects of UNCTAD's future research.

25. The representative of **Peru** said that the rise in the prices of oil and commodities in general and of minerals in particular were of major concern for Peru. Rising commodity prices did not necessarily imply a redistribution of income from consuming to producing countries, because higher prices did not automatically translate into higher fiscal revenues. In addition, the high volatility of commodity prices led to high vulnerability of commodity export countries due to the adverse effects associated with price declines. The UNCTAD secretariat might consider further exploring the situation of mineral-producing countries and associated problems regarding exchange rate management and the development of non-mineral sectors.

26. The representative of **Sri Lanka** said that the issue of free open source software (FOSS) was becoming increasingly important in the context of global interdependence. FOSS was not just a technological issue but could confer benefits in the form of choice and empowerment, development of local industries and skills, sovereignty and security, as well as financial benefits. It was evolving into a fundamental global policy issue.

27. The representative of **Cuba** recognized the need for policy coherence at the global level and between global and national policies in order to support growth, investment and employment. Improving global governance required coherence between the international trading, monetary and financial systems, as well as reforms of these systems, where needed. Big economies had a particular responsibility to the extent that they designed and applied macroeconomic policies that had an immediate negative effect on the economies of developing countries. UNCTAD had an important role to play in promoting international dialogue and initiatives designed to foster coherence. Neo-liberal policies had received increasing criticism, including from the academic circles and institutions that had designed them. This criticism was based on persistent underdevelopment and poverty in countries that had adopted liberalization. In that connection, there was a need to preserve national policy

space for developing countries, and UNCTAD should further develop the policy space concept and make it operational.

28. She was concerned about recent trends in international cooperation. Official development aid (ODA) was decreasing, and there was a lack of political and financial support for international development institutions. The resulting increased bilateralism had meant rising conditionality and declining capacity to channel resources to those countries that needed them most. Concerning commodities, the international community should create mechanisms to improve market access and commodity price stability. It was important to define corporate responsibility in international commodity trade and ensure that developed countries abolished or reduced non-tariff barriers. Developing countries also needed better access to communications technology. While important, South-South trade was not a substitute for North-South trade. External debt was a matter of absolute priority because of its link with poverty. As existing international programmes to reduce the social impact of debt were not sufficient, the only realistic alternative was debt cancellation. New options should be considered to obtain additional financing, while increased efforts should be made to meet the commitment of allocating 0.7 per cent of GDP to ODA.

29. The representative of **Belarus** shared the view that the condition for successful integration into the world economy was coherence of national economic policies. Regarding the issue of policy space, countries at different levels of economic development needed to commit themselves to different obligations in order to benefit from integration into the world economy. The continued lack of stability in the world economic situation was a matter of concern. He noted with regret the use or threatened use of unilateral measures in international economic and trade relations. This did not go hand in hand with international law and created an obstacle to political and social development of developing countries and transition economies.

30. He noted that developing countries and transition economies were playing an increasingly important role in international trade. Access to developed country markets was key for future trade and economic growth of developing countries and transition economies. Inflows of FDI were vitally important for economic development, but most FDI was still concentrated in developed countries. This was true despite the fact that most developing countries and transitions economies had created favourable conditions to attract foreign investors. The international financial system required reform because it could not ensure global financial stability. Developing countries and transition economies were very vulnerable to financial upheavals.

31. The representative of **Venezuela** said that developing countries needed further structural reforms to sustain the current economic recovery. Greater policy coherence in the global economy would help developing countries to maximize the benefits from integration and minimize the adverse effects of economic policies followed by other countries that had a systemic impact in the monetary sphere. However, a multilateral approach to coherence should not limit the policy space of developing countries. Countries at very different levels of development should accept different commitments. What should be disciplined was not the

policy space of those countries that tried hard to reach their essential developmental goals but instead the policies of big actors with a systemic impact.

32. The historic perspective of the TDR represented a significant contribution. The current monetary system, characterized by a large degree of exchange rate volatility, would not work properly or provide predictability for trade and investment unless new rules were adopted making it possible to restrict and discipline policies or measures taken in order to obtain unfair advantages. In a similar way, new trade negotiations would not benefit developing countries unless rules were strengthened making it possible to discipline policies and protectionist measures or minimize their damage. Exchange rate fluctuations had in many cases nullified advantages obtained through hard-negotiated tariff concessions, and in some cases had caused financial crises. Given the international dimension of exchange rate policies, it was necessary to consider the benefits of establishing multilateral mechanisms in the international monetary and financial system similar to existing mechanisms in the international trading system. These mechanisms should preserve the possibility of countries to protect their production and the value of their exports and to maintain a competitive exchange rate. The structure of these rules and their effectiveness could be discussed at a later stage. Some interpretations wrongly held that the concept of policy space could undermine multilateral rules and disciplines, particularly in the multilateral trading system. By contrast, it was obvious that countries could raise legitimate questions for negotiations at the WTO without excluding discussion of these issues elsewhere.

33. In response to specific questions raised by delegations, the **Officer-in-Charge of the Division on Globalization and Development Strategies** said that using non-monetary policy instruments to combat inflation would allow using monetary policy instrument to manage the exchange rate. Regarding the question as to what non-monetary instruments could be used, much depended on the specific characteristics of each country, such as its institutional set-up and the structure of the labour market. There could be no one-size-fits-all approach to this question. Under the current monetary and financial system, with highly volatile short-term capital flows, developing countries with an open capital account and a rate of inflation exceeding that in developed countries were faced with the dilemma of either adopting freely floating exchange rates, which for many reasons was far from an ideal solution, or, as presently done by many developing countries, unilaterally fixing the exchange rate at a competitive level, which entailed the risk of igniting a process of competitive devaluations. The TDR had proposed a rules-based international monetary system as a way out of this dilemma. While there was no generally accepted measure to determine the level of the equilibrium exchange rate, adopting a rule based on purchasing power parity was likely to be the least bad solution. A fixed exchange rate regime did not entirely protect against exchange rate instability, but it nevertheless provided a higher degree of stability than a regime of freely floating exchange rates, though only if the exchange rate was not fixed at an overvalued level and if the country fixing the exchange rate had a current account surplus.

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