



United Nations Conference on Trade and Development

Distr.: General
10 February 2012

Original: English

Thirteenth session

Doha, Qatar

21–26 April 2012

Item 8 (c) of the provisional agenda

**Addressing persistent and emerging development challenges
as related to their implications for trade and development
and interrelated issues in the areas of finance, technology,
investment and sustainable development**

UNCTAD XIII Round Table IV – Addressing persistent and emerging development challenges: An integrated approach to promoting structural transformation

Issues note prepared by the UNCTAD secretariat

I. Persistent and emerging challenges

1. UNCTAD has consistently argued that achieving inclusive and sustainable development in developing countries requires structural change and the development of productive capacities. The emphasis on structural transformation arises from the fact that economic development necessitates a shift of resources from low- to high-productivity activities. The industrial sector has historically played a key role as an engine of structural transformation. Furthermore, poor countries need high and sustained economic growth in order to make significant progress in employment creation and poverty reduction. Commodity exports can lead to high growth but, as the experience of oil-exporting countries has shown, it is difficult to sustain and does not always lead to job creation. Consequently, if poor developing countries want to achieve their national development objectives, they have to go through a process of structural transformation involving a decrease in the share of agriculture and an increase in the share of industry and modern services in output. However, the emphasis on structural change does not imply that industrialization should be achieved at the expense of agricultural development. In particular, while structural change results in a decrease in the share of agriculture in output,

it is important that this transformation is achieved in a manner that permits an increase in agricultural productivity and output to enhance food security and create a domestic environment conducive to sustained and inclusive economic growth.

2. Structural transformation occurs through a complex socio-economic process which is not automatic. The experience of the developed countries and the emerging economies suggests that deliberate government action, and more specifically industrial policy, is required in order to promote industries and induce structural change. Nevertheless, while there is a case for industrial policy in developing countries, it is important to recognize that this approach did not always induce structural transformation in the past, particularly when organized around a top-down process focused on providing support to favoured entrepreneurs without challenging them to perform and without due concern for other social and economic policy goals. Avoiding these mistakes of the past requires a new approach based on the following guiding principles: (a) better consultation between the State and the private sector; (b) effective disciplinary mechanisms for underperforming firms and sectors; (c) greater emphasis on education and skills development; and (d) credible mechanisms for the monitoring and evaluation of policies. Also, it is clear now that without a vibrant export sector, structural transformation is likely to be choked.

3. Technological learning and upgrading are closely linked to the process of structural transformation, helping to raise productivity and build dynamic trading advantages. Because the market tends to underinvest in knowledge creation, and because first-mover advantages often give rise to persistent divisions between technological leaders and laggards, active public policy support is usually needed in developing countries to strengthen local learning and science, technology and innovation capacities. UNCTAD has argued that a national innovation strategy can help coordinate the various activities and policies in support of stronger knowledge and learning capacities that are needed in order to close technology gaps in developing countries.

4. Successful development States have been able to rise to the challenges of structural transformation and technological upgrading. However, doing so has not always led to the establishment of inclusive development outcomes. The resulting changes carry social costs as well as economic benefits, and in the absence of effective policy responses, rising levels of inequality can eventually produce destabilizing pressures which undermine long-term growth and development.

5. A new approach to development policy must also be adapted to the rapidly changing global environment. Over the past decade, the global economic environment has changed fundamentally in ways that have serious consequences for growth, employment and poverty reduction in developing countries. Rising food and energy prices have become an important feature of the global economy that policymakers have to contend with. There has also been an increase in the frequency of extreme weather events, due largely to climate change, with policymakers increasingly concerned about how this may affect future growth. And the climate change challenge is, in turn, drawing attention to other types of damage to the natural environment from the development process. Furthermore, the global economic and financial turmoil of 2008–2009 has increased macroeconomic instability and eroded some of the gains in economic performance made by developing countries since the beginning of the new millennium. Finally, large developing countries are increasingly playing important roles in trade, investment, finance and global governance, and this presents new challenges and opportunities for both South–South and North–South relations.

6. All these developments are adding new challenges to the enduring problem of orchestrating a sustained structural transformation. This raises a host of policy issues in the areas of finance, technology, investment and sustainable development. The round table will address policy issues in five areas deemed crucial for promoting structural transformation and engendering development in the new global environment.

II. Key areas of focus

A. Agriculture and food security

7. Successful transformation of developing economies requires that industrialization should complement agricultural development. This is necessary to address the growing challenge of food insecurity in these groups of countries. Many developing countries and least developed countries (LDCs) will not achieve the first Millennium Development Goal of reducing by half extreme hunger and poverty by 2015 because their agricultural productivity has stagnated. Liberalization in the agriculture sector has generally failed to produce benefits for developing countries. On the contrary, trade liberalization has turned many countries from net food exporters to net food importers, increasing food insecurity. Policies aimed at eliminating price controls, privatizing farms, abating taxes on agricultural exports, removing subsidies on inputs and encouraging competition have produced poor results.

8. The recent food crisis has highlighted the vulnerability of developing countries to external shocks and should be seen as a wake-up call for governments and the international community to take proactive measures to boost agricultural productivity and output and also to enhance access to food in poor countries. This requires increased investment in agriculture, promoting technological change including through the application of information and communications technologies (ICTs) and innovation for all farmers including smallholder farmers, and the articulation of dynamic linkages with industries and services, at both local and national levels.

B. Domestic resource mobilization

9. National ownership of the development process and outcome is crucial for successful structural transformation. Evidence has shown that progress in domestic resource mobilization gives governments more control over the choice of development policies. It also provides easier access to the long-term finance needed for structural transformation. In this regard, developing countries should strengthen domestic resource mobilization by, for example, promoting broad-based growth, broadening the tax base, improving efficiency in the use of public resources, reforming the customs administration, and stemming capital flight.

C. Fostering scientific and technological innovation

10. Building science, technology and innovation (STI) capacity is one the most important challenges facing developing countries. Developing countries that have succeeded in improving their STI capabilities have reaped significant benefits in terms of economic growth and development. This is a complex activity and should be a key priority of all national development strategies. Most solutions to current global and local economic and social problems have an important technology component. Today, it is widely recognized that the challenges of economic development are not going to be addressed properly until issues of science and technology are integrated into the basic economic development strategies of low-income countries. With increasing frequency, policymakers in low- and middle-income countries are coming to the conclusion that they must build up their STI capacity in order to (a) make progress in achieving the Millennium Development Goals; (b) raise productivity, wealth, and standards of living by developing new, competitive economic activities to serve local, regional and global markets; and (c) address social, economic and environmental problems. Building STI capacity and also explicitly

promoting technology transfer will enhance prospects for structural transformation in developing countries.

D. Climate-resilient transport infrastructure development

11. One of the key obstacles to structural transformation and growth in developing countries is the poor state of infrastructure, in particular transport, which has increased transaction costs and made it difficult for domestic firms to compete in global export markets. Therefore, lifting the transport constraint is a necessary condition for structural transformation and growth in developing countries.

12. Inadequate and insufficient transport infrastructure – including rail, road and ports – contributes to increased transport and trade costs, especially in developing regions where freight expenses are relatively higher. For example, transport costs in African LDCs are estimated to absorb as much as 40 per cent of the value of traded goods; in comparison, the average cost in developed countries is estimated at 4 per cent. A deficit of transport infrastructure, resulting in high transport costs, inefficient transport services and low connectivity, acts as a barrier to trade and remains among the persistent development challenges that many developing countries face.

13. In addition, transportation infrastructure, operations and services may be affected, directly and indirectly, by the predicted effects of climate change. The associated risks, vulnerabilities and costs may be considerable, in particular for developing nations with low adaptive capacity, including the LDCs and small island developing States. Given the long service life of transport infrastructure and the strategic importance of avoiding any disruptions to the operation of global supply chains, effective adaptation in transportation requires rethinking established approaches and practices early, despite some of the uncertainties surrounding climate change and its broader long-term implications for transport and trade. This is of particular importance in respect of maritime transport infrastructure. Given that ports handle more than 80 per cent of the volume of world merchandise trade, their integrity and climate-resilience is vital to the ability of all countries – including landlocked countries – to access global markets.

E. Energy supply

14. Successful structural transformation requires reliable and stable access to energy. But developing countries continue to face challenges in providing individuals and firms with an adequate, reliable and affordable energy supply. Addressing this challenge requires, inter alia, more public and private investments in the energy sector; it also requires new methods to be found for financing energy supply.

15. Developing countries are confronted with an important policy challenge with regard to deciding what mix of traditional, low-carbon and renewable energy technologies will set them onto a sustainable development path, and how the chosen energy strategy will play out in terms of job creation and export potential as well as the contribution to global efforts for climate change mitigation. Objectives can be complex, as they need to include components for poverty alleviation and the development of productive capacities. Of particular note are service infrastructures, such as telecommunications and transport, which are entirely dependent on energy access. Building technological capabilities for the adaptation, dissemination and use of current low-carbon and renewable energy technologies is key to enabling the structural transformation that is needed to boost economic growth in developing countries. Promoting high levels of enterprise growth in the early stages of structural change requires a facile and affordable access to energy.

III. Questions for discussion

1. How does agriculture fit into the structural transformation process? How self-sufficient do countries need to be to achieve food security?
 2. What role should domestic resource mobilization play in financing the structural transformation process of developing countries? How can governments boost capacity for domestic resource mobilization?
 3. What are the constraints to building effective capacity for scientific and technological innovation in developing countries, and what policies are needed to lift these constraints?
 4. How can developing countries best finance their transport infrastructure needs in order to achieve structural transformation?
 5. How can countries promote wider energy access and an appropriate and efficient energy mix for structural transformation?
 6. How can developing countries achieve structural transformation without compromising environmental sustainability?
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