

FIRST DRAFT

5th annual Conference Summer Public Management Institute:

“Restructuring Government to Overcome Crisis”

August 1-21, 2009, Latvia

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I would like to thank the sponsors and the organizers of this conference for this timely meeting here in beautiful Riga, Latvia.

I would like to thank the participants for participating and undoubtedly making the event educational for all of us.

I follow other illustrious speakers from our host country, Latvia, from institutions who have contributed extensively to the public administrative reform efforts in Eastern Europe and CIS countries and around the world. UNDP is happy to continue its co-operation with Baltic States, Greece and others and we intend to strengthen our partnership to ensure that reform challenges ahead, undertaken by our partners, are supported in a co-ordinated and effective manner.

The topic of my presentation is 'Financial Crisis and PAR'. It is still difficult for practitioners, all of us, to fully assess the impact of the crisis from political, financial, developmental and social perspectives for this region, let alone assess the impact of the crisis on PAR.

In my presentation and next steps for PAR, I will be looking forward at the recommendations of some of the great thinkers and policy gurus of development, as well as go back to some of the recommendations made by OECD, SIGMA paper and UNDP about going back to some of the fundamentals of PAR.

My presentation is divided into two parts: what does the economic and financial crisis mean to the development and democratic governance agenda and what are some of the reform and PAR issues that need to be addressed in Eastern Europe and CIS countries.

So how did we get here? This was the question that the UN Commission or the Stiglitz Commission reviewed and reported on the impact of the economic and financial crisis on the development agenda. The Commission drew their experts from around the globe and after extensive research and studies, made their report and recommendations public in March of this year.

Allow me to highlight some of their findings:

The rapid spread of financial crisis from a small number of developed countries to engulf the global economy provided tangible evidence that the international trade and

financial system needed to be profoundly reformed to meet the needs and changed conditions of the 21st century. If past financial crises are any evidence, we have seen that the crisis **have a disproportion adverse impact on the poor**, who are least able to bear the costs that have consequences long after the crisis is over.

While it is important to deal with the structural changes to adapt the international system to prevent future crisis, this cannot be achieved without **significant measures and reforms** to promote recovery from the current crisis whose impact may be even worse than in the past. Here, in this region, we are still assessing the full impact of the crisis from social, political, economic and financial perspectives.

The International Labour Organization (ILO) estimates that the rise in unemployment in 2009 compared to 2007 of **30 million** could reach more than **50 million** if conditions continue to deteriorate.

According to ILO, some **200 million people**, mostly in developing economies and middle income countries, could be pushed into poverty if rapid action is not taken to counter the impact of the crisis on these countries. Even in some advanced industrial countries and in this region, millions of people are facing unemployment – this is also the case in Eastern, Central Europe and CIS countries with varying degrees - millions of households are faced with the threat of losing their savings (the loss of household incomes through the remittances has been well documented by WB in all the countries). Loss of revenues has reduced access to health care, while economic insecurity and anxiety continues to increase among the poor, the very vulnerable, elderly, women, rural population, farmers among others, as they lose their life-time

savings and jobs in the collapse of the economic base of their families and communities.

The financial crisis has underlined to us that the welfare of developed, middle income and developing countries is **mutually interdependent in an increasingly integrated** world economy.

It is therefore imperative that short term measures to stabilize the current situation must ensure the protection of the world's poor and the vulnerable, while long term measures – and this includes public sector and public administrative reforms - to make another recurrence less likely- must ensure sustainable financing and reform to strengthen the policy response of developing and middle income countries and of the countries that were hit quite hard by the financial crisis.

However, without a truly **inclusive response**, recognizing the importance of all countries in the reform process, global economic stability cannot be restored, and economic growth, as well as poverty reduction worldwide will be threatened.

This inclusive global response will require the participation of the entire international community; it must encompass more than the G-7 or G-8 or G-20, but the representatives of the entire planet, from the G-194.

I also believe the response to the crisis to address socio-economic development cannot come only from governments, central banks, international organizations or economists and financial or banking experts (who got us into this mess in the first

place) but must include the participation of the public and the private sector, the CSOs, representatives of the poor and the vulnerable, women, minorities, academe, media, schools, unions, local communities – urban/rural, etc. If we are to address the impact of the crisis on poverty and development then all sectors, all groups from all walks of life and according to their ability, must be provided the opportunity to participate and voice their opinion on the responses to the crisis impacting their lives.

The Stiglitz Commission that studied the impact of the crisis from development perspectives makes several recommendations. One key recommendation is the reform agenda of the international system (economic, financial, trade, banking) that must have as its goal the better functioning of the world economic system for **the global good** – robust and sustainable reforms that protect not only the economic and financial systems but also protects the poor and the vulnerable .

This entails simultaneously pursuing long term objectives, such as sustainable and equitable growth, the creation of employment in accordance with the “decent work” concept, the responsible use of natural resources, and reduction of greenhouse gas emissions, and more immediate concerns, including addressing the challenges posed by the food and financial crises.

As the world focuses on the very urgent matters the long standing commitments to the achievement of **the Millennium Development Goals** and protecting the world against the threat of **climate change** must remain the overarching priorities; indeed, appropriately designed global reform should provide an opportunity to accelerate progress toward meeting these goals.

As part of our next generation of PAR efforts we must ensure that MDGs and climate change priorities remain at the centre of our attention and focus.

Responding to the Global Financial Crisis

Sustainable responses to the crisis require identifying the factors underlying the crisis and its rapid spread around the world.

It is now generally agreed that loose monetary policy, inadequate regulation and lax supervision interacted to create financial instability. The results were manifesting in the large global imbalances whose disorderly unwinding, in the absence of prompt countercyclical measures, aggravated the crisis.

Although some would say US, EU and Asian countries reacted quickly to address the crisis.

Part of the reason for inadequate regulation was an inadequate appreciation of the limits of markets—what economists call “market failures.” While such failures arise in many markets, they are particularly important in financial markets and can have disproportionately large consequences as they spill over into “real” economic activity.

Addressing the inadequate financial regulatory system is being discussed at the International Financial Institutions, G8, as well as in countries we represent here today. There are many schools of thoughts on how far the financial systems should or

should not be regulated. But for the purpose of our discussion, pertaining to E & CIS countries – my question is do we have the space, the capacity and the instruments to properly assess the past inadequacies of the regulatory systems in order to identify and implement appropriate measures and recipes?

The financial crisis, as we all agree, reflects problems that go beyond the conduct of monetary policy and regulation of the financial sector. It also involves deeper inadequacies in areas such as **democratic governance, accountability of institutions, corporate governance and competition policies**. Many of these failings, in turn, have been supported by a flawed understanding of the functioning of markets, which also contributed to the recent drive towards financial deregulation. These views have been the basis for the design of policies advocated by some of the international economic institutions, and for much of the architecture of globalization. **(this issue will be subject of many global discussions for the months and years to come).**

My concern for E & CIS countries is, as I stated earlier, what space, capacities and instruments do we have for policy and regulatory reforms, what type of public policy dialogue should we be embarking? How broad-based is the international, but more importantly the national discussions, to look at regulatory and deregulation issues – above and beyond the financial sector.

More generally, the current crisis has exposed deficiencies in **the policies of some national authorities and international institutions** based on previously fashionable

economic doctrines, which held that unfettered markets are, on their own, quickly self-correcting and efficient. (true for this region).

Globalization too was constructed on these flawed hypotheses; and while it has brought benefits to many, it has also enabled defects in one economic system to spread quickly around the world, bringing recessions, poverty, unemployment, social unrest to developing countries as well as to middle income countries, and even to countries that had developed good regulatory frameworks, created effective monetary institutions, and succeeded in implementing sound fiscal policies.

Stiglitz Commissions recommendations – on general responses to the financial crisis are two fold:

- a) quick action on interim measures – stimulus packages, support to national financial institutions – to stabilize the situation. and
- b) deeper medium and longer reforms that are necessary if we are to make another crisis less likely and if we are to strengthen national and international institutions' capacity to respond to future crisis – to address socio-economic, development and poverty issues. (group discussion on this)

I know the organizations represented here are already reflecting on what should those medium and longer term reforms look like.

But while reflecting on these reforms, we need to ask – what are **the key principles that should be guiding us** as we embark on new reform agenda? Here are some points of reflections or priorities to address:

First, failure to act quickly to address the global economic downturn inevitably would increase its **depth and duration** and the eventual **cost** of creating a more balanced robust recovery.

Some countries have been more successful than others – EU, US, Canada, China, others. (a question to the audience how did these countries become more successful in preparing for a crisis?)

Second, in a globally integrated world, the actions of any one country have effects on others. Too often these *externalities* are not taken into account in national policy decisions – this is also a capacity issue.

Countries in this region particularly need to be aware of the adverse consequences of these externalities and need to develop frameworks to help protect themselves from regulatory and macro-economic failures in western and other countries.

This is where the next generation of PA reforms must focus and put in place measures to address regulatory, policy and administrative short comings.

Third, I believe, E & CIS countries should expand the scope to implement policies and **strengthen or create institutions** that will allow them to implement appropriate counter-cyclical policies to counter external pressures.

Fourth, as the article stated on the recovery measures for the Baltic states – what can we draw from the lessons learned of past experiences and how to diversify local, Balkan economies – and strengthen other sectors, including fisheries, forestry, manufacturing, new value added industries, **for example environment**, among others.

Fifth, we need to inject greater **transparency and accountability** on the part of all parties – national and international institutions - in responding to the crisis through national consultations, starting at parliamentary level. More specifically, democratic principles, including inclusive participation in the decision making, should be strengthened and respected in public policy dialogue, policy making and reform. (Canadian experience on strategic review and 4 yrs accountability measures)

On this point, I know in this region, UNDP is working with national counterparts to develop stronger transparency and accountability frameworks as part of our PAR mandate and reform initiatives.

Sixth, the crisis is, in part, a result of excesses in deregulation of financial markets and in international trade. Restoring the global economy to health will require restoring a balance between the role of **the market and the role of the state**. And from the citizens' perspective and PAR – we need to ask - what measures should we

be putting in place to ensure that we hold both the markets and the states accountable?

In responding to this crisis, it is also imperative that actions to improve conditions in the short term do not result in structural changes which **increases instability, reduces growth in future and further impoverishes the conditions of the poor.**

Seven and finally, it is essential that governments undertake reforms that address some of the underlying factors that contributed to the current economic crisis if the world is to emerge from the crisis into sustainable and balanced growth. It is not enough simply to return to the status quo *ex ante*.

Appropriately designed short turn measures should be complementary to the long term goals, especially those related to socio-economic development, poverty reduction, climate change and the environment.

Priority PAR measures for the short, medium and long term

In this second part of my presentation I would be addressing some of the fundamental PAR policies and frameworks that national and international organizations undertake - in other words, going back to basics in this post financial crisis.

Everyone in the audience would agree with me that in E & CIS countries, in the past 20 years the fundamental legal PAR reforms have been successfully introduced and implemented, to varying degrees and successes. But the financial crisis have

underlined some gaps and that there is a need to revisit some of the fundamental PAR requirements within the new context and realities.

I will not focus on some of the global macroeconomic and financial issues here, or the economic diversification measures of the region or the new revised international credit systems.

I will, however, focus on the following for our region:

1. Co-ordinating regional and global reforms
2. Establishing a broader policy and risk mitigation space;
3. Establishing stronger policies and institutions that is accountable to citizens
4. Learning from other countries, who had buffered their economies & citizens better from the economic and financial downturn;
5. Learning from successful policies to undertake regulatory reforms.
6. Creating an environment where the capacity of human capital can be developed or enhanced so that it copes with PAR issues at hand.

Although the financial crisis have underlined the reform gaps but it has also created an opportunity for the policy makers of this region to revisit the unfinished or incomplete public sector and PAR reform issues – going deeper into reform – going beyond legal reforms.

a) to revisit some of the fundamentals of PAR but more importantly to go deeper into the reform agenda; and

b) to address some of the legal, policy, regulatory and administrative gaps that have been underlined by the crisis.

I will not repeat here some of the weaknesses of the public administrative reform assessed by SIGMA and OECD – for the Central European region, but I would say some of the recommendations should be revisited before embarking on any meaningful post crisis reforms.

Medium and long term measures

As part of the EU accession requirements, new European member states and future candidates have established legal and policy and legal frameworks in most sectors. I believe, policy impact and risk assessment, implementation, quality control and accountability have had a more patchy success. New members and future candidate must acquire the space to assess the impact and risks of EU accession policies and their impact to their own environment. But new members and future candidates must also strengthen the fundamentals of policy development and impact assessment instruments first.

1. Global and regional co-ordination of reform

At the G8 summit, at EU, and around the globe there are efforts to consult and co-ordinate the short and long term response to the crisis.

Stiglitz Commission makes several recommendations: For example: the establishment of new credit facility under the umbrella of the WB or regional development banks. As well, within a UN system, an independent body on global economic policy analysis, a Global Economic Co-ordination Council and of course major reform of IFIs – WB. IMF.

Although global economic and financial reforms must be co-ordinated but what are some of the reforms that need to be co-ordinated at the regional level, within EU and E & CIS countries? Regulatory policy reforms, - but what else? Social, environmental and other sectors?

2. Policy development, impact and risk assessment

In this region policy PS reforms have always been a sensitive and political issue. But if we are serious about reforms, at a minimum, the following four tracks processes are needed :

- a) create or strengthen the strategic policy units with Central Agencies and strengthen policy impact and risk assessment capacities in ministries (with Min. of Finance leading) at the national and sub-national levels – at the state and municipal levels.
- b. introduce strictly enforced, substantive quality control and scheduling processes for the council of ministers. Include the Executive as well as Parliament in the policy development and impact and risk assessment to build their capacities.
- c. develop policy development and impact assessment skills at the national schools of public administration and build the capacities of new generation of civil servants.
- d. build the capacities of institutions and civil servants at the sub-national levels.

It should be recognized that government bail-outs have substantial redistributive consequences that must be analysed in assessing their impact on recovery. In addition, because of the urgency of the situation they often fail to observe principles of good governance and especially of democratic transparency. This may lead to the introduction of inappropriate incentives, as well as failure to recognise possible adverse effects on other countries, especially on developing countries that lack equivalent financial resources.

As part of policy impact assessment, it is imperative that E & CIS region build its own capacity to assess the impact of the government bail-outs in other countries, of trading partners etc.

Ultimately, new members and future candidate countries must be provided the opportunity and support to ensure that external policies and conditions meet the national priorities and interests.

3. Public accountability and institutional reforms

Most E & CIS countries, again, have established the legal frameworks for budgetary reforms but usually it is focused on the budgetary processes of the ministries of finance. According to OECD report, the positions and the capacities of human resources in ministries of finance and other ministries remain weak to enable to protect revenues and expenditures plans or act as administrative reform.

The capacities of revenue and expenditure management system, as well as the internal and external audit capacities must be strengthened and capacities developed.

It is equally important to build the revenue and expenditure management capacities at the sub-national, state and municipal levels. On this latter, most E & CIS countries have a long way to go.

Stiglitz Commission also recommends strengthening the mandate of UNODC on anti-corruption and public accountability.

4. Learning from other countries

Some countries, Canada, Scandinavian countries, Australia, China, India and others have been successful in buffering their economies and financial institutions from the worst of the economic and financial crisis. In interviewing senior officials from the federal government – Treasury Board – they described to me how they started on the difficult and arduous task of establishing a comprehensive regulatory management system at the federal and provincial levels, some 20 years ago. OECD, is the institutions that not only measures the capacity of regulatory management systems in its member states but also develops policies and programmes on regulatory management systems – sectoral and general.

It is strongly recommended that E. and Central European countries assess the programmes of successful countries in all or specific sectors of the economy.

UNDP Bratislava have initiated discussions with OECD and SIGMA to see how we can join hands to provide regulatory management system and building the capacities of E & CIS countries. Some of these successful countries will be able to provide capacity building support to E & CIS in specific sector. I recommend Canada to review and assess their regulatory sector in banking.

5. Regulatory management system

As I stated, OECD/SIMA have developed leading edge programmes in almost all sectors of the economy. Priority sectors for this region will include: banking, financial institutions, insurance companies, then moving to others sectors. But as the Stiglitz Commission recommends, it is important to go beyond the financial sector and address the regulatory issues surrounding taxation, trade and other sectors.

There are also regulatory and enforcement agencies in several countries that are worth assessing for their lessons learned and experiences.

This issue requires in-depth discussion within EU members and future candidate countries to EU as to what type of regulatory management systems in all sectors must be established and national capacities strengthened.

Stiglitz – establish a Global Financial Regulatory Authority and a Global Competition Authority.

6. Creating new sustainable human development through PAR

It is difficult to generalize any public sector and public administrative reform initiatives to such a diverse grouping of countries but despite the differences among the countries this region shares a common historical, economic, political and environmental thread among them.

As the article underlined the fragility of this region, economic and institutional weaknesses dominate the context for most of the countries. Economic and financial

stress – albeit brought upon the region by other countries – reduces the budgetary space for building public institutions or strengthening social programmes and poverty increases creating social tensions. The vicious cycle continues weak institutions make economic reforms and human development more difficult and reduces the capacity to finance public sector and public administrative reforms.

It will be imperative that in the short or medium term PS and PAR reforms stay on the national agendas; It is also imperative that through PAR policy and programme reforms the full potential of all sectors and all segments of the society are addressed.

It is important that economic policy and regulatory reforms, administrative legal frameworks, civil service reforms, public accountability and control systems address the human development potential at the local community and national levels while bearing in mind the interconnectedness of the regional and the global market place. While most countries in the region have successfully launched the first generation PS/PAR reforms much more work needs to be done.

The economic and financial crisis underlined the weaknesses or the gaps of past reforms. Although the crisis have created a new set of challenges it has also provided opportunities to revisit some of the fundamentals of PAR while developing a new socio-economic instruments to better serve the citizens of the E & CIS region.

Ultimately, PS/PAR success will be measured how best we have created an environment where all citizens contribute their fullest potential on the development journey, creating a new paradigm of human development.