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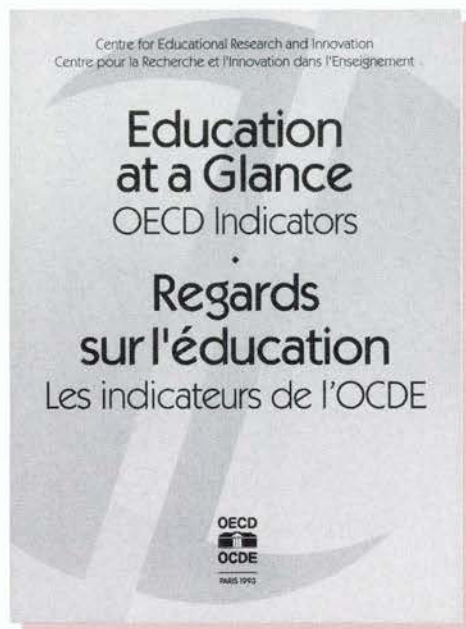
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Stittler/R.E.A.


# 186

February/March 1994

Cover

What is the state of female employment today? One major trend is a concentration in the service sector, often coupled with part-time work.





*What is the employment picture for women today? The OECD has taken a fresh look at the lie of the land in this period of economic restructuring, widespread joblessness and new forms of employment.<sup>1</sup>*



# Women and the Restructuring of Employment

In 1992 there were around 169.4 million women in the labour force in the OECD area – 33 million more than in 1980. The ranks of economically active women – on the rise everywhere – averaged 2% annual growth over the past decade, twice the pace of their male counterparts, whose numbers are on the wane in the majority of countries. At this rate, the sexes will have reached numerical parity in several national labour markets by the dawn of the 21st century.

Statistical equality will be obtained in some countries but not all – patterns vary extensively from one OECD country to the next (Figure 1). At one extreme are Sweden and Finland: in both countries, women's employment rates are very similar to men's, but in Sweden, unlike Finland, women frequently work part-time. At the opposite extreme is Ireland, where economic activity among women is low and offers little sign of change, and Spain, where, from an identical starting point, the participation of women has made clear gains among the younger generations. In a third, intermediate group of countries, including Australia and Japan, women's employment rates are still dropping sharply for the 25–34 age group.

## Segregation in Employment

Today women can be found in every occupation, yet gender-based job segregation remains solidly anchored in all

*Françoise Coré*



*In a couple it is the woman who – even if she has a formal occupation – has to perform the bulk of domestic and family chores.*

own sex outnumbers the other by more than nine to one.

Listing the ten occupations that respectively employ the largest numbers of women and men (Table 1) prompts three observations: there is virtually no common ground between the two lists; the most common occupations for both sexes have a particularly pronounced 'unisex' tendency; and on each list the same occupations appear again and again, whatever the country.

Such segregation occurs by industry as well as by occupation. Focusing on the three major sectors of activity in the aggregate, one finds that the breakdown of employment between men and women is extremely uneven (Figure 2). Although 90% of jobs in most OECD countries are non-agricultural for women and men alike, this 90% is much more evenly split between industrial and service employment for men than for women, whose jobs are very heavily concentrated in the service sector. And the more women there are in the labour force, the bigger the sectoral inequality.

## Received Ideas, New Facts

Does the fact that women are taking over an increasing share of the labour

countries. One statistic from the Nordic area is particularly striking: less than 10% of women (and men) hold jobs for which there is approximate numerical equality between the sexes, and half of all women (and men) occupy posts for which their

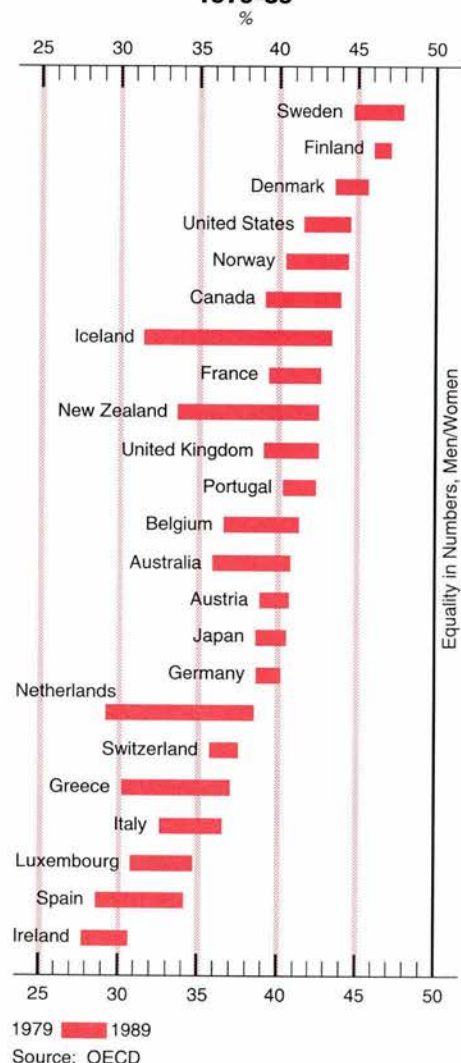
*Françoise Coré specialises in the role of women in the economy in the OECD Directorate for Education, Employment, Labour-Market and Social Affairs.*

1. *Women and Employment Restructuring: New Perspectives*, OECD Publications, Paris, forthcoming 1994.

*Collective, social and personal services will provide by far the largest number of jobs for women.*



Figure 1  
**GROWTH OF FEMALE REPRESENTATION  
IN THE LABOUR FORCE,  
1979-89**



force have any effect on the quality of their employment?

It is argued that women constitute a different kind of labour force because of their reproductive function and because they have maintained their traditional role within the family and the home. How much truth is there to this assertion?

Repeated pregnancies have become a rare phenomenon in the OECD

countries, where (with the exception of Turkey) fertility rates range between 1.3 and 2.2 children per woman. Matters are more complex when it comes to women's traditional role. First, an increasing percentage of women are either single, separated or divorced, and for them the issue is not the same as for married women. With couples, the way they budget their time makes it undeniable that it always falls to the woman – even if she has a formal occupation – to perform the bulk of domestic and family chores (Table 2).

The presence of young children always entails a considerable overall workload for mothers, who bear a double, if not a triple, burden. Nevertheless, fewer and fewer women are putting their careers on hold while their children are young, even if in certain countries they find

themselves having to work part-time, at least for a while. In any event, at any given time mothers with young children make up only a small percentage of women in the labour market.

Although still highly prevalent among employers, the idea that women workers are less readily available, less motivated and less productive on account of their reproductive function and the maintaining of their traditional role seems ready for the scrap-heap of misconceptions. Not only do such notions prevent women's productive capacities from being used to the full; they also impede the search for genuine solutions to the problem of reconciling family responsibilities and professional obligations.

Workers who can rely on a full-time home-maker to relieve them of all household and family concerns are a

Table 1  
**PRINCIPAL OCCUPATIONS OF WOMEN AND MEN IN CANADA, 1991**

Occupation	Number (thousands)	% of total in the labour force
<b>Women</b>		
Secretaries and short-hand typists	430	7.7
Sales-workers, commodities <sup>1</sup>	347	6.2
Tellers and cashiers	257	4.6
Nurses	220	3.9
Waiters and caterers	205	3.7
Book-keepers and accounting clerks	193	3.5
Elementary and kindergarten teachers	148	2.6
Child-care	147	2.5
General office clerks	142	2.5
Accountants, auditors, other financial officers	141	2.5
<b>Total of top ten occupations</b>	<b>2,230</b>	<b>39.9</b>
<b>Total women in the labour force</b>	<b>5,589</b>	<b>100.0</b>
<b>Men</b>		
Truck drivers	222	3.3
Sales-workers, commodities <sup>1</sup>	218	3.2
Sales and advertising management	193	2.9
Accountants, auditors, other financial officers	148	2.2
Janitors and cleaners	138	2.0
Industrial, farm, and construction machinery mechanics and repairers	128	1.9
Motor-vehicle mechanics and repairers	118	1.7
General managers and other senior staff	109	1.6
Systems analysts, computer programmers and related	106	1.5
Carpenters and related	104	1.5
<b>Total of top ten occupations</b>	<b>1,484</b>	<b>22.0</b>
<b>Total men in the labour force</b>	<b>6,751</b>	<b>100.0</b>

1. Includes occupations not classified elsewhere.

Source: adapted from Statistics Canada



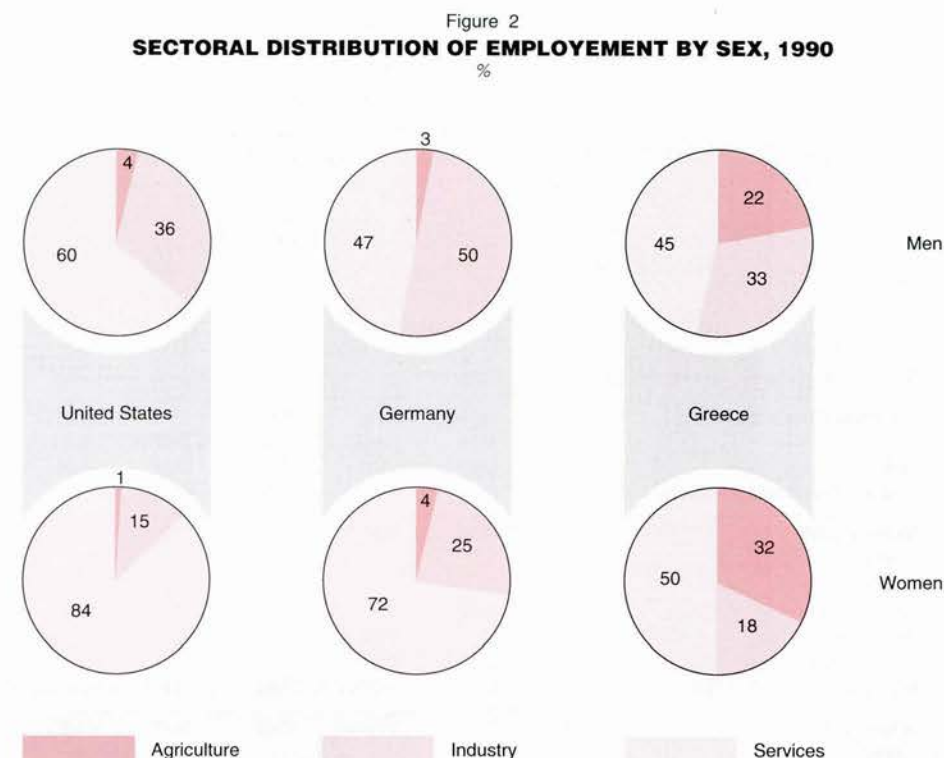
dying breed. Today, every day, the vast majority of workers must confront the problem of organising their personal and family lives in the light of the constraints put upon them by professional responsibilities and an ill-suited environment; cities, for example, have to be re-examined and redesigned (box, p. 9).

A second assertion is that women bring a lower degree of skills to the job market. Although the tendency for girls to stay in school longer than boys is in evidence in many countries, both subject-matter and career paths are still heavily differentiated by gender, with a large majority of girls gravitating towards general education, the humanities and social sciences. Until now, training of this sort was not considered particularly marketable. But in post-industrial society the skills and aptitudes that women acquire through their participation in the educational system (abstract reasoning, oral communication and so on) and the qualities that are often referred to as 'typically feminine' (organisational and interpersonal skills) will be increasingly in demand. As a result, the 'difference' with female labour stems not so much from a lack of skills as from a lack of acknowledgement and of proper use of these skills in the workplace.

## Trends in Services

Employment opportunities for women in the OECD area are increasingly limited to services. This sector, which currently accounts for 50–70% of all jobs, depending on the country, currently comprises a wide spectrum of activities that differ with respect to required skills, working conditions, work organisation, professional status, and so on.

Of the activities that make up the service sector, each has its own pattern of development. In the 1980s, employment growth was led by services to businesses as well as by social and personal services. Banking and insurance companies, along with public services, which had driven expansion in past decades, seem to have exhausted – at



Source: OECD

least temporarily – their ability to absorb additional labour. The same can be said for retailing.

Many service jobs held by women are to be found in branches of activity that are undergoing extensive restructuring because of changing patterns of competition or, in the case of the public sector, the necessity of reigning-in spending and reducing the deficit.

The development of financial services initially prompted a surge in the number of office jobs. In Japan, for example, where financial services have grown spectacularly, such jobs rose from 17.5 to 26.6% of all non-farm employment between 1960 and 1980. More recently, both the computerisation of a large portion of office work and administrative streamlining have considerably slowed the growth of office jobs. Unskilled positions, where women are in a majority, have been the hardest hit. At the same

time, financial-market deregulation in the 1980s, along with higher mobility of capital, triggered a substantial expansion of financial services, along with a demand for highly skilled labour. By and large, it was met mostly by men, although in some countries (the United States in particular), women with the requisite qualifications were also able to benefit from the demand.

The same two trends – the rationalisation of low-skilled jobs, which will keep disappearing, and a rise in the demand for more highly skilled workers – can also be seen in other service activities and are likely to persist. Services to businesses provide highly skilled jobs (in advertising, marketing, accounting, legal services, and so on) as well as very low-skilled and insecure jobs in activities where women predominate (cleaning and corporate catering, for example). That puts women doing unskilled jobs



Table 2  
**CHANGE IN DAILY USE OF TIME, 1974–85**  
*French adults living in urban areas<sup>1</sup>*

	18–64							
	Women				Men			
	Employed		Unemployed		Employed		Unemployed	
	1975	1985	1975	1985	1975	1985	1975	1985
<b>Personal care</b>	<b>11h20</b>	<b>11h15</b>	<b>12h08</b>	<b>12h06</b>	<b>11h40</b>	<b>11h17</b>	<b>13h04</b>	<b>12h23</b>
of which:								
Meals at home	1h28	1h18	1h54	1h37	1h33	1h23	1h47	1h37
Meals outside home	0h26	0h33	0h15	0h21	0h42	0h40	0h40	0h31
<b>Paid work, study and training<sup>2</sup></b>	<b>5h36</b>	<b>5h16</b>	<b>0h38</b>	<b>0h57</b>	<b>6h49</b>	<b>6h21</b>	<b>2h06</b>	<b>1h59</b>
Paid work	4h58	4h38	0h05	0h08	6h05	5h36	0h20	0h15
Study and training	0h06	0h04	0h28	0h41	0h04	0h05	1h35	1h31
Travel because of work or training	0h32	0h34	0h05	0h08	0h40	0h40	0h11	0h13
<b>Domestic work</b>	<b>4h42</b>	<b>4h38</b>	<b>7h47</b>	<b>6h53</b>	<b>2h20</b>	<b>2h41</b>	<b>3h34</b>	<b>4h05</b>
of which:								
Cooking, washing-up, house-keeping, washing, etc.	3h15	3h09	5h14	4h17	0h54	1h05	1h31	1h38
Sewing, mending	0h13	0h11	0h30	0h23	0h21	0h24	0h21	0h36
Domestic travel	0h39	0h41	0h51	0h54	0h41	0h43	1h02	1h07
Child care, care of elderly, etc.	0h28	0h28	1h02	0h55	0h12	0h12	0h10	0h11
<b>Leisure time</b>	<b>2h22</b>	<b>2h51</b>	<b>3h27</b>	<b>4h04</b>	<b>3h11</b>	<b>3h41</b>	<b>5h16</b>	<b>5h33</b>
of which:								
Television	0h59	1h10	1h25	1h51	1h20	1h38	1h43	2h18
Sport	0h02	0h05	0h02	0h05	0h05	0h11	0h09	0h17
Going out (theatre, etc.)	0h05	0h09	0h03	0h08	0h08	0h09	0h09	0h15
Games (cards, crosswords, etc.)	0h05	0h06	0h04	0h08	0h09	0h10	0h13	0h21

1. Activities showing the most marked change.

2. Taking Saturdays and Sundays into account in the calculation of these averages produces a surprising figure for the time spent daily in working or studying; when multiplied by seven they appear closer to the figure one might expect.

Source: INSEE

extraordinary expansion of the welfare state in the 1970s. But the rise in public-sector employment<sup>2</sup> was not uniform in all countries, with the ratio of such jobs to total employment varying widely from country to country: from less than 10% in Japan to nearly a third in Sweden at the end of the '80s. In general, the percentage of women is higher than in the private sector and increases with the relative size of the public sector. In the Nordic countries, for example, more than half of all working women are employed in general government, and two-thirds of these are staffed by women.

Does the public sector offer advantages that have a particular appeal for women? Offhand, as far as equal opportunity is concerned, the

answer would seem to be 'no'. Horizontal segregation and the concentration of women in a small number of occupations can be observed in the public as in the private sectors. In the federal government in Canada, for example, three-quarters of the women are employed in four of the 72 sub-categories: as office workers, secretaries, administrators and programme managers; one group alone – office workers – employs 44% of the women. There is also strong vertical segregation (with women concentrated at the lower echelons), especially in the central administration. As in the private sector, this dual segregation by gender

2. Understood here as general government.

in a very vulnerable position, at the same time as more opportunities are opening up for highly qualified women.

Nevertheless, trends in collective, social and personal services (health, education, household services, and so on) are the most important ones for women's future job prospects, since this sector is by far the biggest provider of jobs for women. In most post-agricultural countries, it alone employs about half of all working women, in a host of traditionally – and to a large extent exclusively – female occupations, such as child-care, teaching, nursing, and so forth. In Sweden, for example, women represent 73% of the sector's total labour force.

This type of service is doubly important for women's employment. Not only is it the area with the largest, and as yet largely untapped, potential for new jobs (demand for training services and services for old people and families is expected to swell), but as more of these services become available, women will be freed from some household and family constraints and thus be more fully available to work.

### Developments in the Public Sector

In a fairly large number of countries, the growth of collective, social and personal services took place amidst the

Continued on p. 10



## ACCOMMODATING WOMEN IN THE CITY

Lindsay McFarlane

Modern cities and suburbs have been influenced by many factors: the introduction of the private car; commuter-oriented public transport; zoning regulations (separating industrial activities from residential areas); the quest for cheaper and more spacious housing in the suburbs; and, more recently, economic restructuring and the pursuit of economies of scale.

But many of the basic assumptions upon which nineteenth- and twentieth-century urban planning was founded are now being called into question. There are several reasons: the emergence of different household structures, with a decrease in the number of 'standard' households with two parents and children and an increase in single-parent households and people, often elderly, living alone; the increased participation of women in the labour force; higher unemployment; and a concern for the environment. There is now an increased demand for more 'people-centred' urban policies which bring the home, work and recreational facilities closer and which allow city-dwellers access to employment, to bring up their children and enjoy their leisure under better and less stressful conditions.

Women are often economically disadvantaged because the urban environment imposes higher costs of access to employment and services, disadvantages that are compounded for lone mothers. If women are to obtain work and accommodate both job and domestic responsibilities, they must overcome innumerable hurdles: difficulty in moving between home, job and shops; limited public transport, particularly in the suburbs; transport schedules designed primarily for the trip to and from work; services (such as medical facilities, housing-authority offices, social security) the schedules of which are based on the assumption that consumers and clients will be available during the working day; and limited availability of, and access to, child care. The geographical separation of home and workplace thus acts together with restricted choice in transport to limit accessibility to jobs.<sup>1</sup>

Many planners and sociologists alike have forgotten that the neighbourhood community is particularly important for people at certain periods of their life – pre-school children, full-time parents (mostly women) and retired and elderly people. To their number can be added the increasing numbers of (particularly long-term) unemployed. Urban environments should help households, whether traditional or lone-parent, to provide a stable home for their children. There are alarming indications (increasing crime and violence, drug addiction, low educational achievement, and so) that it does not.<sup>2</sup> Similarly, the increasing number of elderly people living alone (mainly women) require better access to assistance and care, through measures that also allow members of their own family to assist them.

In many OECD countries there is growing awareness that women should be better integrated into the life of the city. In July 1993, for example, the Federal Department of Housing, Local Government and Community Services of the Australian government organised the first National 'Women in Planning' Conference in Melbourne. In the Netherlands work is going on to raise awareness and formulate innovative ideas – including a national research programme for Emancipation Studies and experimental urban projects which highlight the viewpoints of women. These include a housing project in Zwolle, the Netherlands, where women architects and planners were involved in the development of a neighbourhood of 230 new dwellings. The plan stresses maximum social and road safety and allocates equal importance to all modes of travel connecting both locations within the neighbourhood and employment and services. The Foundation of Women, Building and Living is organising women's networks throughout the Netherlands for women who are, professionally or otherwise, interested in housing and office buildings.

Lindsay McFarlane is Secretary of the OECD Group on Urban Affairs, a project manager in the Urban Affairs Division of the OECD Environment Directorate, and is organising the OECD conference on 'Women in the City'.



J. K. Magnum

A first Swedish congress on 'Housing and Building on Women's Terms' was held in Kungsälv, initiating a dialogue between the women's movement in housing and planning and a Scandinavian interdisciplinary women's research group that resulted in the creation of a project, 'New Everyday Life', financed by the Nordic Council of Ministers. The project aims to encourage models of neighbourhoods which pay more attention to the viewpoints and requirements of women.

In Finland, the concepts developed in the course of the 'New Everyday Life' project have been applied in a number of housing experiments and in the development of service systems for the elderly and for long-term patients. A research project on 'Healthy Environments for Children and Youth' is also underway in three Finnish neighbourhoods in conjunction with the WHO 'Healthy Cities' project.

Meetings of female urban professionals are now a regular feature in the Nordic countries. The various initiatives emerging from them are helping to shed light on the specific interests of women – and their own special requirements, ideas and view of the world – which are not necessarily those of men. This in turn should help guide policy-makers in developing communities which cater for women and children.

The role of research in shaping policy is crucial. In the past it has largely been men who have made decisions on the subject of research. This means that there is a good deal of information on heads of households (who in most cases are men) but little about their wives. Traffic between work and home has been researched, but virtually nothing is known about the destinations and criss-cross routes that women take each day. Again, an 'ideal' of family re-creation is automatically assumed, with little investigation of the way women spend their free time. And this lack of research data makes it difficult for women to support their proposals for changes to their immediate environment.

Evolution towards a pluriform, emancipated society will require that every man and woman has the possibility of acquiring an independent life-style, if so desired, of benefitting from the opportunities available to the maximum of his or her abilities.

1. The OECD Group on Urban Affairs is organising a conference on 'Women in the City: Housing and Urban Services' in the autumn of 1994 to focus on the special housing and service demands of women in cities.
2. See also pp. 20–22.



brings about a wage-gap between women and men.

Newly created employment opportunities were therefore the main reason that women entered the public sector. But government jobs do offer certain advantages, particularly for civil servants: until recent years, pay for women was often higher than in the private sector; vacations are longer and there is more job security. Furthermore, in several countries women are becoming better represented in skilled occupations and at middle echelons. And affirmative-action programmes have now been introduced for their benefit in the civil-service systems of most countries (box, p. 11).

## New Kinds of Employment

One of the most significant structural changes in the labour markets of the OECD countries is the rising number of jobs that depart from full-time, permanent employment. Part-time work is one such atypical formula, and it applies mainly to women. Self-employment is another option which is expanding rapidly in certain countries, but one in which women are relatively under-represented. Interpreting how these two forms of employment affect equal opportunity for women is not without ambiguity.

### Part-time Work

The frequency of part-time work varies substantially within the OECD countries – from less than 5% of total employment in Mediterranean countries to over 30% in the Netherlands. In all countries, women account for more than two-thirds of all part-time workers; in a significant number, nearly half of all women work part-time (Table 3). Fur-

Table 3  
**PART-TIME EMPLOYMENT IN 21 OECD COUNTRIES**  
%

	Share of part-time in total employment				Female participation in part-time employment	
	Women		Men		1979	1991
	1979	1991	1979	1991		
Australia	35.2	40.9	5.2	9.2	78.7	76.3
Austria	18.0	20.1	1.5	1.5	87.8	89.7
Belgium	16.5	27.4	1.0	2.1	88.9	89.3
Canada	23.3	25.5	5.7	8.8	72.1	70.5
Denmark	46.3	37.8	5.2	10.5	86.9	75.5
Finland	10.6	10.2	3.2	5.1	74.7	65.2
France	16.9	23.5	2.4	3.4	82.2	84.0
Germany	27.6	34.3	1.5	2.7	91.6	89.6
Greece	..	7.2	..	2.2	..	62.9
Ireland	13.1	17.8	2.1	3.6	71.2	71.6
Italy	10.6	10.4	3.0	2.9	61.4	65.4
Japan	27.8	34.3	7.5	10.1	70.1	69.9
Luxembourg	17.1	17.9	1.0	1.9	87.5	83.3
Netherlands <sup>1</sup>	44.0	62.2	5.5	16.7	76.4	70.1
New Zealand	29.1	35.7	4.9	9.7	77.7	74.2
Norway	50.9	47.6	7.3	9.1	83.0	81.4
Portugal	16.5	10.5	2.5	4.0	80.4	66.7
Spain	..	11.2	..	1.5	..	78.0
Sweden <sup>2</sup>	46.0	41.0	5.4	7.6	87.5	83.4
United Kingdom	39.0	43.7	1.9	5.5	92.8	86.1
United States	26.7	25.6	9.0	10.5	68.0	67.2

.. not available.

1. Break in series after 1985.

2. Break in series after 1986.

Source: OECD

thermore, it can be noted that in some cases the rise in female employment in the 1980s stemmed exclusively from an increase in part-time work.

Has the spread of part-time work come about to meet the requirements of certain employers (that is, is it supply-led?) or to suit new categories of workers (demand-led)? It is extremely difficult to say; what is certain is that the phenomenon exists mainly in activities and occupations that are dominated by women, and hardly anywhere else. In some countries, part-time work has become the norm in retailing, catering and the hotel industry, as well as in social and personal services. It results most frequently from a re-organisation of tasks

that limits such arrangements to unskilled job categories. To make things worse, part-time workers frequently have a separate status, below that of full-timers, especially for social-security regulations.

More and more women are working part-time against their will, since those are the only jobs available that fit their profile. Women who have a full-time job and decide at some point to work part-time – generally for family reasons and for the want of adequate day-care for their young children – cannot always do so without changing jobs, even sectors. As a result, their career advancement is halted – perhaps irreversibly – and they frequently have to settle for a job that is below what their skills and quali-

fications would merit.

Although it is indisputable that part-time work now makes a major contribution to the employment of women in very many countries, it is not without drawbacks. Because it overwhelmingly concerns women, and because the job categories involved are both separate and inferior, part-time work adds another dimension to gender-based employment segregation.

If part-time work is to contribute more to equal opportunities for women, it will have to be developed across all sectors and positions. The Nordic countries offer an example: all workers there have the right to reduce their hours under certain circumstances and for a specified period

Continued on p. 12



## EQUAL-EMPLOYMENT OPPORTUNITIES IN THE PUBLIC SECTOR

Sally Washington

Employment opportunities and conditions experienced by women working in the public sector have a significant impact on the status of women in employment in general. Government employers have become front runners in promoting equal opportunities, often acting as role models for their private-sector counterparts.

Direct discrimination in public-sector recruitment, pay, promotion and dismissal is prohibited in all OECD countries. And in many, measures to compensate for lingering systemic discrimination against women (and minority groups) also exist. They include setting targets to increase the representation of women in senior positions; positive action in recruitment; and career-development strategies. The United Kingdom, for example, has set a benchmark of 15% for women in top civil-service jobs by the year 2000; amongst equally qualified applicants in Norway, women are designated the preferred candidate for positions where there is a sizable imbalance of the sexes (that is, where women make up less than 40% of the staff); in New Zealand there are career-development courses designed especially for women, as well as women's networks, wherein senior women coach and support up-and-coming female staff.

In spite of progress towards equal opportunity – although uneven across OECD countries – women remain relatively disadvantaged in public-sector employment. Occupational segregation persists, and women are still severely under-represented in senior posts. It is estimated that at current pace it would take at least 25 years for women to achieve numerical equality in senior public service positions in the OECD area.<sup>1</sup>

### Management Reform and Equal Opportunity

The public-sector environment is also changing.<sup>2</sup> Government employment is being affected as the public sector is reduced in size and as some services are contracted to the private sector, as well as by policies to reform the management of human resources (HRM). HRM reforms vary across OECD countries, but common developments include devolution of HRM to individual organisations and individual managers; the use of management techniques including performance contracts and sometimes performance-related pay; more flexible systems for hiring, deploying, rewarding and laying off staff, and a focus on raising productivity and cutting labour costs.

How much women's employment opportunities and working conditions have been affected by these changes is difficult to determine without systematic assessment and monitoring. Very little of that occurs in OECD countries. Nevertheless, there are pertinent questions to be asked which may offer some insights and suggest areas for further inquiry.

For example, are women's jobs being disproportionately affected by changes in the size and shape of the state sector? Does managerial discretion open doors to the advancement of women or create new scope for discrimination? Are centrally determined equal-opportunity programmes or rules actually at odds with the new spirit of public management and the managerial freedoms it prescribes?

It is hard to judge whether occupations that are traditionally held by women have been hardest hit by privatisation and contracting-out. Some female-dominated jobs, such as cleaning services, have been contracted out to the private sector in several countries – but so have services like refuse collection, which employ more men. The transfer of blue-collar jobs to the private



Sittler/Jerrican

sector may result in some loss of conditions and security for the people affected, especially in categories important for women's employment, such as parental leave or permanent part-time work, where there has tended to be most divergence between public and private sectors.

It is equally difficult to say whether increased flexibility in promotion and reward systems has reduced or increased the barriers to advancement for women. For example, have management strategies such as performance-related pay<sup>3</sup> reduced or exacerbated the gender-based pay gap?

Initial inquiry<sup>4</sup> suggests that in most OECD countries, at least for the moment, equal-opportunity policies are still determined centrally and administered in individual public agencies. But some changes are occurring as a result of wider management reforms. In Finland and New Zealand, for example, individual public-sector organisations now assume primary responsibility for designing their own equal-opportunity programmes. In New Zealand, responsibility rests with the chief executives of government departments. Progress in equal opportunities forms part of the performance appraisal on which the renewal of their contracts is based.

Monitoring is required to identify the effects of changes in the public sector on equality and fairness in employment. Governments have to ask what sort of a public service they want in the future, as well as what 'good employer' signals they wish to give to the private sector. They have also to ensure that managerial discretion does not lead to discrimination.

New or adjusted equal opportunities measures that are compatible with, support, and are supported by the new managerialism may be required. The benefits accruing through effective equal-opportunity measures are compelling. Improved recruitment and retention of skilled staff, enhanced flexibility and occupational mobility, and a public service that is more representative of the wider society and potentially more responsive, are all consistent with the underlying objectives of public-management reform.

1. **Women and Structural Change: New Perspectives**, OECD Publications, Paris, 1994.

2. Derry Ormond, 'Improving Government Performance', *The OECD Observer*, No. 186, October/November 1993.

3. **Private Pay for Public Work: Performance Related Pay for Public Sector Managers**, OECD Publications, Paris, 1993; see also Maria Maguire and Robert Wood, 'Private Pay for Public Work?', *The OECD Observer*, No. 175, April/May 1992.

4. The OECD Public Management Service is reviewing reforms in human resource management systems in OECD countries.

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Fabricius-Taylor/Jerrican



*Although the demand for highly skilled labour in financial services was largely met by men, women have also benefited.*

of time. Another positive trend is that, more and more frequently now, employers are offering their skilled workers a chance to work part-time.

### **Self-employment**

Self-employment, or setting up a business, can be one solution for women seeking access to work and social advancement. At present, it is a path chosen by relatively few women in the OECD countries, or at any rate by far fewer women than men. And yet it can

be a particularly attractive option, especially in rural areas, where local job-markets are extremely thin.

Self-employment can satisfy two entirely different types of aspiration for women. For highly skilled women looking for professional success, it can be an alternative to corporate jobs where entrenched training and promotion systems thwart their advancement. It is mainly women in the professions who take this route. For others, self-employment is a means of juggling family tasks and gainful employment; these women generally go into personal services and other female-dominated activities such as health care or retailing.

Women who decide to start a business still have to cope with problems and discrimination. In the event, many attempts fail, either in the planning stages or after a firm has been created. To help women create their own businesses, many schemes and programmes have been established in recent years. The goals have been to inform, train and advise women all along the way, from initial planning through to company launch and subsequently expansion and consolidation.<sup>3</sup>

■ ■

As women carve out a larger and larger place for themselves in the labour market, it is increasingly unrealistic to marginalise them as a minority. It is chiefly through measures of a general nature and applied in companies themselves that equal opportunity for women must be pursued. It also has to be recognised that coping with both professional and family responsibilities is a problem for all workers – not merely for women – and that across-the-board solutions must be found.

The female labour force is not a uniform population – far from it. Although many women are perfectly able to cope and to benefit from employment restructuring, some are finding it very hard to adapt to the new demands of employment. The groups that currently give most cause for concern are single mothers and unskilled older workers, for whom special measures are still urgently required. ■



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# Why Governments Must Work Together



Scott H. Jacobs

***Globalisation, increasing international co-operation, economic and monetary unions, social conventions and a variety of other formal and informal relations have meant growing interdependence between countries, and particularly between members of the OECD. That has a substantial impact on how governments exercise regulatory powers, with less freedom of action – and new responsibilities.<sup>1</sup>***

**A** vast array of agreements and treaties influence the regulatory systems of national governments. They range from the supra-national (the European Community, for example, has adopted no fewer than 22,000 regulations), through international multilateral agreements (the North American Free Trade Agreement, the GATT (not least its Technical Barriers to Trade agreement), Decisions of the OECD Council), bilateral treaties and co-operative agreements (such as the Australia-New Zealand Closer Economic Relations Agreement), national-local arrangements to share responsibility for making and implementing rules (in most OECD countries, both federal and unitary), to regulatory agreements between sub-national governments (negotiations among Canadian provinces to reduce provincial trade barriers).

The rapidity and scope of the move toward regulatory interdependence is opening new opportunities for government action and closing others, reshaping institutional roles and relationships, and transferring power from national

political institutions and traditional bureaucracies to emerging intergovernmental networks. Effects on the roles of government, the legislatures and the judiciary in setting and overseeing laws and policy are only beginning to be perceived.

Intergovernmental co-operation – though often described as reducing discrepancies through the harmonising of regulation – has usually amplified regulatory complexity by introducing new forms of decision-making and involving a range of individuals, institutions and processes that are outside the traditional scope of government, yet whose actions must nonetheless be dependable, consistent and co-ordinated.

Interdependence affects governments not only at all levels of national government, but also locally, regionally, and supra-nationally. An accurate view of regulatory interdependence has to see it as an intricate web of vertical and horizontal links between all these levels,

often stretching from the lowest to the highest. Tasks are scattered throughout this web. Implementation of regulations, for instance, may be carried out by parts of government far removed from where decisions were made, as when environmental-health inspectors employed by local authorities in the United Kingdom advise refrigerator repairmen how to handle ozone-depleting chemicals under the terms of the Montreal Protocol. 'Regulatory diversification' is a better term for these developments than such popular terms as 'internationalisation' or 'decentralisation'.

Regulatory co-operation, too, tends substantially to increase the amount and detail of regulation. As member states of the EC often note with dismay, issues that seem simple at home expand to pages of text as negotiators strive to eliminate ambiguities and ensure consistency. At times, the effect of governmental co-operation seems to be multiplication of regulation rather than solving of problems.

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1. Regulatory Co-operation for an Interdependent World, OECD Publications, Paris, forthcoming 1994.



### MAKING IT WORK: HARMONISATION, MUTUAL RECOGNITION, CO-ORDINATION

Regulatory co-operation does little good, and perhaps much harm, if governments choose the wrong strategy. Three approaches to co-operation – harmonisation, mutual recognition and co-ordination – are proliferating in the OECD area. Because they each have the effect of eliminating differences in regulations, they offer forms of regulatory *rapprochement*.

These regulatory strategies are not simple in practice; on the contrary, their success seems to depend on sophisticated management strategies that are carefully designed to match the specific regulatory environment, expected consumer and business responses, and the roles of government institutions, including the judiciary. The European Court of Justice, for example, has played a central role in establishing and sustaining mutual recognition in the EC.

What general lessons are suggested by experiences to date?<sup>1</sup>

First, these strategies may be best used in combination. Harmonisation – with its often under-rated administrative and political difficulties and its risk of ‘freezing’ multiple governments into the wrong decision – seems most effective when it is limited to a few ‘essential’ issues, such as, in the EC, health and safety. Even in those cases, harmonised rules should state the desired performance rather than list technical specifications. On all other issues, regulatory diversity should be permitted through mutual recognition. This is, of course, the ‘new approach’ adopted by the EC in 1985, although the subsidiarity debate reveals substantial uncertainty about which part of government should act on specific issues.

Second, the regulatory strategy should be suited to the specific type of ‘market failure’ that governments are attempting to correct. Mutual recognition is likely to be appropriate when consumers have insufficient information on the quality of goods and services (because

producers will compete by providing more information) but harmonisation may be required when the problem is a ‘negative externality’, such as trans-boundary pollution.

Third, disciplined mutual recognition can establish the basis for beneficial regulatory competition. Regulatory competition allows businesses and consumers to choose between alternative regulatory regimes, as when a consumer picks a television made to either German or French standards. Theoretically, regulatory competition is desirable because it expands consumer choice, increases efficiency and rewards cost-effective regulatory approaches. Governments tend not to trust it because they fear that weaker standards will vitiate stronger ones. But it is not clear that this always happens. As seems to be the case in car-safety and securities markets, many consumers prefer tighter standards. Regulatory competition can thus strengthen regulatory protections. More understanding is required of how regulatory competition works, the role of information, and the general rules by which regulatory competition can be disciplined so that – as consumers ‘discover’ which regulatory regimes offer the most value – it generates knowledge.

Fourth, much can be accomplished through informal processes instead of formal and legalistic systems of mutual recognition and harmonisation. The Basel Supervisors’ Committee, for example, has accomplished through its discussions a gradual convergence of bank supervisory practices. And the market tends to drive a ‘bottom-up’ process of convergence, as in the case of technical standards for bolts, light-bulbs and telecommunications systems.

1. Giandomenico Majone, *Comparing Strategies of Regulatory Rapprochement*, Paris, 1993, available free of charge from the OECD Public Management Service.

This complexity is made even less manageable by relentless pressure for change as economic, environmental and social issues become increasingly intertwined. Markets have led interdependence with the growth of global trade and capital movements; unless governments resort to protectionist measures, they have no choice but to follow. There is also a growing recognition of environmental and social externalities, exemplified recently by charges of ‘social dumping’. Linkages among policies means that governments are not con-

trolling change; rather, they are attempting to cope with it.

Making this sprawling, multi-governmental regulatory system work is a management challenge of the first magnitude. As in any interdependent system, the likelihood of failure increases with complexity: policy success will be constrained by the weakest link in this web of relationships.

But is this new regulatory environment, as some public-sector managers believe, so uncertain, involving so many different individuals and institutions, and

changing so rapidly that it defies any kind of strategic planning? Indeed, are governments losing control of regulation? This perception would be quite dangerous politically if it triggered a retreat from the economic necessity of interdependence and led to a reduced capacity to deal with the urgent common issues in the OECD area.

Governments do not have to lose control, but deep-seated reform is necessary if they are to use these intergovernmental processes profitably and within the constraints of their political legitimacy and public acceptance. The old style of government in OECD countries – hierarchical, vertical, standardised, lodged firmly in the structure of the national state – is suited for stable conditions and well-defined problems, but it is not appropriate for a multi-layered regulatory system characterised by complexity, diversity and innovation.

### Networks and Partnerships

One of the most profound changes in the making of regulation is the emergence of decentralised networks among bodies that formulate and implement regulation. One example is the group of national regulators from 144 countries who gather in Rome to make recommendations on food standards under the auspices of the FAO-WHO Codex Alimentarius Commission. Similarly, in areas ranging from capital movements and training of pilots to chemical testing and workplace standards, thousands of intergovernmental networks of organisations, administrators and experts analyse, discuss, negotiate, or even make regulatory policies.

Such intergovernmental networks provide flexible and specialised frameworks within which multiple governments can interact as partners.<sup>2</sup> But national administrators find them very difficult to

2. Les Metcalfe, *The Weakest Links: Building Organisational Networks for Multilevel Regulation*, Paris, 1993, available free of charge from the OECD Public Management Service.



manage, since they are often informal, responsibilities are diffuse and shared among governments, issues can be technical, and information on what they are doing is not consistent or easily available. Frequently, it is not even clear who is involved in a network. Networks can thus escape existing national mechanisms for policy oversight and co-ordination, quality control, and consultation.

Yet government effectiveness in OECD countries today depends less on how well single organisations function, and more on how well these networks of people and organisations function. Styles of government are changing – slowly – in response. Networks are being institutionalised, as in the EC Standing Committee for Administrative Co-operation which has created

co-operative bodies between national authorities in areas such as abolition of tax frontiers in the European internal market. Partnerships between governments – such as an agreement between Sweden, Canada, and Australia to share the burdens of testing of new drugs – are supplementing decision-making in national administrations.

Co-ordination among decision-makers has emerged as a major issue for managers: 'top-down' central coordinators and lengthy co-ordination processes may have to be replaced by 'bottom-up' networks that are more tightly knit. The current efforts of pharmaceutical regulators and industries from the United States, Japan and the EC to arrive at consensus on requirements

for drug testing and registration is a case in point. This informal and open process has made more progress toward improving drug standards and reducing testing costs than has been achieved by the unwieldy national negotiating forum in the WHO.

Perhaps the biggest obstacle to co-operation is lack of trust. In spite of increasing interdependence, governments find it difficult to trust one another to carry out their respective duties in regulatory agreements. To some extent, this suspicion is realistic: many international agreements have simply not been respected. But it is also inherent in the intergovernmental process. Differences in administrative cultures, legal traditions (such as treatment of liability),

capacities, values and policy priorities undermine co-operative relationships.

Trust is required not only in administrations, but also among politicians and the general public. Public acceptance of regulatory interdependence rests ultimately on perceptions of the reliability and compatibility of the 'other' governments involved.

Trust between governments must be built horizontally and vertically, using tools such as common professional norms, clear agreements on duties and roles, communication and growing familiarity. Improved transparency is essential. Governments and intergovernmental organisations must actively generate and disseminate information. Information technologies have not, in general, been used very effectively in informing

governments about one another, but they do show considerable promise. Trust can also be buttressed by more effective procedures for resolving disputes. Much can be done to help governments gain experience in making such procedures work better.

Governments may therefore have to devote more time to familiarising themselves with one another's administrative styles, to better communication and public openness, and processes that control the quality of administration. A step-by-step approach, in the co-ordination of rule-making, may be preferable to immediate harmonisation. The OECD itself offers many examples – such as its 'Guidelines for the Testing of Chemicals' Programme – of how trust

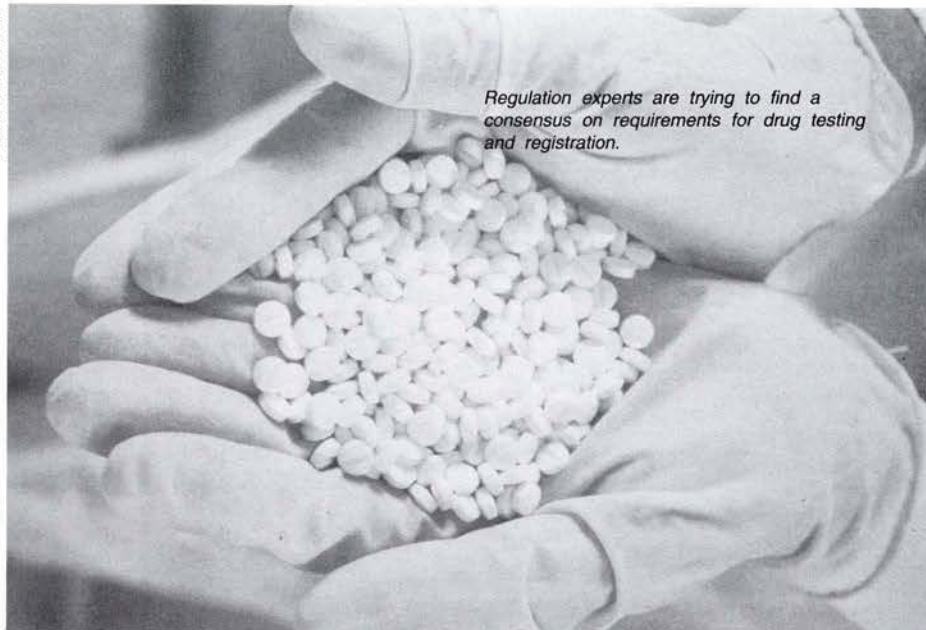
Sittler/R.E.A.



*When it comes to safety many consumers will opt for higher standards – especially where children are concerned.*



Patrick Allard/R.É.A.



Regulation experts are trying to find a consensus on requirements for drug testing and registration.

can be built and sustained between countries as a foundation for regulatory co-operation.

## Accountability and Sovereignty

Concerns about accountability and national sovereignty lie behind many criticisms of the multi-layered regulatory system. How can governments work effectively together while maintaining the controls on law-making necessary for a democratic system? How can agreements between governments be held accountable to citizens? This is made more difficult by such traditions of intergovernmental processes as closed negotiations, limited participation and lack of public information on consequences and options.

Public concerns about sovereignty tend to out-pace government response, and will continue to heighten. Even so, there may not be complete realisation of the extent to which governments have already effectively surrendered legal authority to intergovernmental regulatory processes – that is, they have become

'regulation-takers' rather than 'regulation-makers'.<sup>3</sup>

Information can be used to strengthen accountability. Pertinent analysis, for example, can be used to open up intergovernmental decisions and improve the quality of public debate on important issues. The EC and the GATT are using benefit-cost analysis to clarify to interested groups the consequences of regulatory decisions. But communication is complicated because perceptions of the problem to be solved by regulation can vary widely between tiers of government. This is particularly true when the benefits and costs of regulatory actions are distributed asymmetrically, as is often the case in trade agreements on specific products. In these cases, the benefits of sustaining the broader co-operative system must also be presented to the public.

Public consultation and participation are not well-developed in processes of regulatory co-operation, but demands from non-governmental parties for access are intensifying. Environmental, labour and consumer groups are making appearances in fora such as the GATT, NAFTA, FAO-WHO, and the OECD.

National governments can do much to strengthen and diversify the partici-

pation of interested groups; regional and local governments, for example, may be under-represented in international regulatory fora, given the importance of their roles in implementation. Yet care must be taken to ensure that a multitude of new voices do not lead to chaos and, equally, to ensure that participation is not captured by narrow interests who may be tempted to use intergovernmental fora to suppress competition and injure wider public interests.

Careful thinking is required on the relationship between intergovernmental co-operation and the sovereignty of citizens in a democracy. A loss of democratic control in a national context may be inevitable as the monopoly on law-making held by national legislatures and administrations weakens, but compensating increases in accountability may be achieved through the design of networks, markets and international institutions. As the GATT process shows, international agreements can, in fact, stimulate useful national debates on fundamental issues of public policy. Moreover, regulatory competition allows consumers to choose between alternative regulatory regimes, and hence can supplement 'national sovereignty' with 'consumer sovereignty'.

■ ■

An interdependent world requires new forms of governance. Indeed, the transition to co-operative government is already well-advanced. Sharing regulatory authority with other governments does not have to be a threat to national authorities or to the democratic values they preserve. On the contrary, the current search by national governments for new and more effective forms of regulatory co-operation to solve urgent common problems is fuelled by a reliable propellant – self-interest. ■



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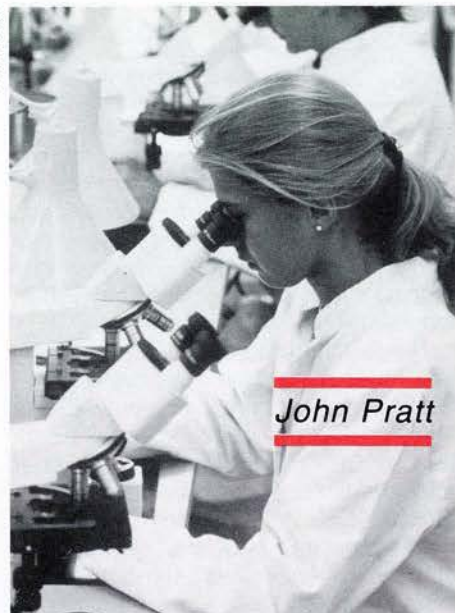
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3. John Braithwaite, *Prospects for Win-Win International Rapprochement of Regulation*, 1993, available free of charge from the OECD Public Management Service.



# Expanding Choice in Austrian Education

ZEFA-Voigt



John Pratt

Last May Austria adopted a law which may well be the first step towards the overall reform of the higher-education system; its purpose is the development of an entire new non-university sector. It marks an important departure from the policy of higher education to date and a rethinking of the regulated, centralised system of policy-making in Austria in general.

Several external and internal factors explain such a decisive move. The first is Austria's proposed membership of the European Union (EU), and the move to the market in Austria's neighbours in central and eastern Europe. Both developments will stimulate demand for Austrian goods – but will also expose them to increased competition. So there will be implications for the formation of skills in the education and training system. Even if the much-debated principle of 'subsidiarity' governs European policy in education as elsewhere, the growing integration of trade in goods and services calls for increased mobility of qualified manpower and more transparency – and, perhaps later on, more homogeneity – in qualifications.

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***Austria is proposing to create an entire new sector of non-university higher education. What problems will have to be resolved if this ambitious project is to succeed?***

EU membership will have other implications for education. Recent EC directives on the harmonisation of qualifications have acted as a catalyst for reform, particularly in higher education, triggering renewed discussion on creating a non-university sector, alongside the state-owned universities. Unlike the majority of OECD countries, Austria does not offer a real alternative to university education. In 1990/91, less than 14,000 students were enrolled in non-university post-secondary institutions, as against 170,000 enrolments in universities. And the students who currently graduate from this small post-secondary sector rarely benefit from the kind of mobility enjoyed by graduates whose diplomas are recognised in other European countries.

Although it is always difficult to assess accurately the demand for an emerging middle-level qualification, it is clear that Austrian employers are ready to hire specialists in technology and business from vocationally oriented courses of higher education. As in several other OECD countries, the initial demand is from big and medium-sized firms which specialise in high-technology products and export a large part of their output. Until now the flow of graduates from the highest stream of technical education in engineering and business has generally met local demand, from a variety of different firms, both in quality and quantity. The holders of such diplomas easily found jobs even in neighbouring countries (chiefly Switzerland and Germany). But, as in the most advanced industrialised countries, changes in technology and work organisation now call for a more advanced and broader general and technological education. The corresponding lengthening and revised content of the curriculum implies that it should take place in post-secondary institutions.

The resulting pressure for reform is calling many aspects of the current university system into question. Again as in numerous other OECD countries,

the coalition government's commitment to reducing the Austrian budget deficit and improving the effectiveness and efficiency of public services has led to a consensus that it is no longer possible to justify such returns on the 'investment' that Austrian taxpayers make in the universities, which are marked by a high drop-out rate and excessively long duration of study. Although it is generally considered that graduates have a high standard of academic education, in 1992 only 9,000 students graduated.<sup>2</sup> Hence the recurrent idea – it was first raised in the 1970s – that the universities might be relieved of the burden of the mass extension of higher education.

Another factor contributing to reform, again common to most other OECD countries, is the question of financing higher education. Many countries have now accepted that it is no longer possible to sustain a mass system of higher education solely through central public funding. In Austria, by contrast, since higher education has always been free to students, the political parties are reluctant to see a change, since they regard fees as a barrier to the poorer student.

## Features of Austrian Education

These factors should be viewed against specific national features. First, major changes at any level in the Austrian education system are difficult, because they require a two-thirds majority in parliament and thus a broad political consensus.

Second, decision-making is concentrated at the top of the system, either in provincial or federal government. Institutions, schools and universities have little autonomy. The universities themselves suffer from the complexity

1. *Reviews of National Policies for Education: Higher Education in Austria*, OECD Publications, Paris, forthcoming 1994.

2. *Statistisches Taschenbuch*, Bundesministerium für Wissenschaft und Forschung, Vienna.



and difficulty that stem from central control of curricula, which are regulated by two Acts of Parliament that prescribe not only the duration of studies, but also the names of degrees, sub-divisions in speciality subjects, types and details of examinations, and so on. Any change involves a four-stage process, which also includes consideration of the academic programmes by the 200 members of parliament. Previous attempts at reform have run foul of the Austrian regard for social consensus.

Third, Austria, like other industrialised countries, has seen an impressive expansion of educational provision since the Second World War. It was previously reserved for a small elite. Today only 2% of students leave the educational system at the end of compulsory schooling, and the number of students completing higher secondary education up to the age of 18 or 19 has more than doubled in the past two decades, to reach 31% of the age-group. These are impressive achievements, but unlike most industrialised countries, Austria did not match this increase in student numbers by structural reform. There was no diversification of the post-secondary sector, nor was a comprehensive system introduced at the lower secondary level, where streaming begins at the early age of ten.

Fourth, secondary schooling in Austria is still selective and compartmentalised. The majority of Austrian school children start vocational training at a relatively early age. Fourteen-year-olds who intend to continue in full-time education enter either four years of general education (in a Higher Secondary General school, or AHS) or vocational education, where they take four-year courses (in a Full-time Vocational School, or BMS) or five-year courses (in a Higher Secondary Vocational/Technical School, or BHS). Students completing the AHS and the BHS obtain the 'Matura' qualification and are entitled to enter university. But nearly half of all 14-year-olds enter the 'dual' system of apprenticeship, where they receive one year of pre-vocational education, and then go into employment

and receive only part-time (although still compulsory) education. The majority of the students who follow the dual system do not go on to a higher level of education. There is also a gap between the age of graduates from higher vocational education (19) and those from university (generally 25–30).

## Proposals for Reforms

To resolve some of these issues, the Austrian government has offered two main proposals. First, since the government is conscious of the consensus within Austria on the desirability for a new form of post-secondary education, it has placed considerable emphasis on the creation of an alternative sector of higher education in 'Fachhochschulen', or vocationally oriented colleges and programmes. Second, it is taking initial steps in reforming the management of universities.

The objective of the Fachhochschule programme – which has already received wide support from employers and others outside the educational system and from the universities themselves – is to enable a large variety of institutions, mainly already in existence (top-level secondary vocational schools, adult education institutions established by business and/or unions, some university faculties or departments, private schools, and so on), to offer courses, while at the same time ensuring unified standards. This use of a diverse range of existing institutions and agencies has been questioned, but the government believes that the benefits of this innovation will outweigh the drawbacks.

A law to establish an accrediting body, or Fachhochschulrat, to supervise the academic development of this sector was passed in May 1993. An autonomous board appointed by the Federal Ministers of Science and Research and of Education and Arts, the Fachhochschulrat will examine proposals for courses, the adequacy of regulations on access, staff qualifications, existing infrastructure, cost estimates and a plan for evaluating and

developing the curriculum. It will accredit satisfactory proposals (for a limited period) and monitor and evaluate progress and outcomes. The limited-period accreditation, together with a continuous assessment of the outcomes, are aimed to guarantee that the courses and curricula are still matching demand in the labour market.

The existing institutions, and possibly new ones, that wish to provide Fachhochschule courses can apply to the Ministry for designation as a Fachhochschule, provided they meet a number of academic and organisational requirements. One of the merits of the Fachhochschule system is that, although complying with strict standards, the institutions will be allowed to take a variety of curricular initiatives. Increased organisational flexibility will be matched with concomitant freedom in financial decisions.

To this end, academic and organisational regulations are separated from decisions on finance. The Fachhochschulrat will make no funding decisions, and will thus impose no financial obligations on the federal authorities. It is up to the Fachhochschule itself to provide funds from its own resources or through subsidies from federal, provincial or local authorities. The extent of federal-government funding for the Fachhochschule sector has not yet been specified; to date, the government has merely stated that 'The federal government should not be released from its primary responsibility for tertiary education'.

The original proposal was that the Fachhochschulen should be able to charge fees for tuition, but because universities do not charge for teaching and the government is reluctant to change this situation, the proposal has been delayed and the parties in the coalition government agree that the same regulations should be applied to the entire higher-education sector. It is therefore likely that fees will be a major policy issue in years to come. It means that in the first years of their existence the Fachhochschulen would have to rely



on more limited funding than was initially expected, with the risk that it might be more difficult later for the responsible authorities to introduce tuition fees on a significant scale.

If the Fachhochschulen are to enjoy acceptance and success, several conditions have to be met. First, the type of institution that the government intends to bring into the Fachhochschule sector must be defined. Is it, for example, to include colleges that provide training for teachers and social workers? Should small colleges offering a handful of Fachhochschule courses be encouraged to become fully fledged Fachhochschulen?

Early consideration also has to be given to the feasibility of combining related disciplines, such as technology and management, within one institution, and to potential development along 'polytechnic' lines. This question raises a host of political and financial issues. In non-university teacher-training, no political decision has yet been taken about the university or Fachhochschule status for the institutions concerned. The Austrian authorities do not seem to be ready to up-grade socio-cultural and para-medical studies to the level of Fachhochschulen because of salary implications for new graduates and, later, for the whole profession. But it is clear that fully fledged polytechnical institutions provide opportunities to redress current geographical imbalances in the provision of tertiary education throughout Austria by developing them in regions where there is no university.

## Whither Research?

For research, the role of the Fachhochschulen requires careful definition, since this issue has created conflict with the universities, which insist on a monopoly on pure research and reject the idea of allowing graduates from the Fachhochschulen direct access to doctoral studies. But if, as is intended, the Fachhochschulen are to provide an advisory and consultancy service to

industry, their staff will require both theoretical and practical experience and an understanding of current developments.

The government must decide whether the Fachhochschulen should be 'equal but different' to the universities – as was originally intended with British polytechnics (a goal reinforced in some instances, abandoned in others, with the recent transformation of many of them into fully fledged universities) – or stay subordinate to them at the highest level of studies. If, as in many cases (Belgium, France, Germany, the Netherlands and Norway among them) such an alternative to university should become an arm in national and regional development of technology, especially in its transfer to small and medium-sized firms, the experts are generally of the opinion that the Austrian Fachhochschulen will not be able to avoid taking part in R&D and applied research and should therefore have the resources for that purpose. This raises the question of the extent to which the universities and Fachhochschulen should be mutually exclusive – at what point could the benefits of competition between them be realised?

The Fachhochschulen will also have implications for secondary education. Until now, the quasi-monopoly of universities in higher education has meant a rather rigid division of upper secondary education (if not before) between streams leading to university and those culminating with a secondary vocational diploma. But if secondary education is to offer a pool of good candidates for the Fachhochschulen, it will prove necessary to avoid over-early, over-rigid selection. That would require the rethinking of the relationship between vocational and technical education and access to higher education, not least for adult learning, on both a full-time and a part-time basis.

But it will be important also to ensure that the Fachhochschulen do not encroach on the five-year BHS route – if there continues to be a demand for it. Until now, such vocational/technical training has been much praised by

employers, not only in Austria but also in its neighbouring countries. It will take several years before the new graduates of the Fachhochschulen are unquestioningly accepted at a higher level of qualification on the labour market. Until then, it is likely that the five-year BHS route will continue to deliver its highly appreciated diplomas.

The opportunities for innovation that the Fachhochschulen offer, stimulated by recent progress in information technology, could also be extended to distance education, which may thus be able to help answer questions raised by mass higher education by allowing a new public access to higher education.

■ ■

Broad consensus on the importance of reform is evident on the surface but its significance is hard to judge; it has not produced a coherent picture of the future of the higher education system, even in the short-term. Inevitably, reform will be carried out step by step, since tradition and parliamentary procedure in Austria do not encourage proposals for radical change. There are, moreover, many unresolved issues, not least the relationship between the Fachhochschulen and the universities. Such an approach risks a lack of co-ordination because of the number of organisations involved (two federal Ministries, local authorities, business, unions, and so on). The government might therefore usefully launch a broad public debate in order to achieve the necessary consensus on, and closer understanding of, the functions of the whole higher-education system, and the roles of the different institutions it should encompass. ■



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# Tackling Educational Disadvantage

Peter Evans

Martine Franck/Magnum



***Some 15–30% of children in many OECD countries may be identified as being at risk of failing at school and thus of jeopardising their successful transition to work and adult life. What are the educational and social indications that a child may be at risk? How can they best be understood in a way that provides an agenda for action? And what strategies and innovations have been adopted by OECD countries in trying to tackle the problem?***

**D**eclines in birth rates, increasing numbers of elderly retired citizens and high unemployment rates mean that today many fewer working people are supporting more and more 'pensioners'. That adds an economic imperative to the individual desirability that as many children as possible acquire the skills imparted by formal education in order to maintain the economic growth that will be necessary to support the growing burden.

There is substantial agreement on the operational definition of what being 'at risk' of school failure means for children and what it can lead to: low attainment, low satisfaction and self-esteem, dwindling participation in school activities, growing truancy and school refusal, drop-out, behavioural problems and delinquency. These patterns, to which there are of course individual exceptions, in turn can lead to broader difficulties of integrating into society and obtaining work, often producing unemployment, poor health (sometimes psychosomatic), drug abuse, crime, early pregnancy and poverty.

A number of factors can help predict some or all of these outcomes and,

indeed, are used to guide policy decisions. There are six main elements:

- poverty
- ethnic-minority status
- family factors, such as single-parent-hood, standard of family education, housing, a breakdown in relations between home and school, and child abuse
- poor knowledge of the language of instruction
- the type of school attended and its location
- community factors, such as lack of support, poor accommodation, lack of leisure facilities and political voice.

These individual factors may act in combination. Any one of them – say, coming from a single-parent family – may present no risk at all. But two – perhaps a combination of having a single parent and poverty – may increase the chances of failure four-fold, and four factors suggest a ten-fold increase. It is recognised in some countries that resources should be provided to schools to reflect potential disadvantage. In the Netherlands, for instance, additional teaching staff are allocated by weighting pupils according to certain social and cultural background factors. Using 1.0 as a baseline, Dutch families from low socio-economic backgrounds are given

a weighting of 1.25, families who drive barges for a living one of 1.40, travellers, gypsies, circus families and other nomadic families 1.70 and ethnic minorities 1.90.

## The Importance of Background

What should be changed in order to improve the chances of success for young people at risk? To this end the processes which allow children to feel part of the community have to be identified and encouraged.

The majority of children are brought up in healthy, supportive homes, by parents who esteem education and whose values are broadly those of the mainstream of society. Career paths can be set quite early (from 14 onwards) in the light of knowledgeable discussion with family and friends. But breakdowns in the relationships between child and family, or family and community, which all help to fashion the child's own attitudes, values and knowledge-base, can help to create a gap between desired and actual experiences, which then affect the ability to benefit fully from education.

These concerns and problems have, of course, always existed, but in the past

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a lack of 'school learning' was not as crucial as it is today. A wide diversity of skills and abilities was required in such activities as agriculture, building and mining – and this kind of work often had strong family traditions which could offset lack of academic success in school.

It may not be surprising that earlier analyses of why children from disadvantaged backgrounds seemed to fail were made in terms of either environmental variables – membership of a particular social class, for example, or constitutional factors such as inherited intelligence. But in retrospect, these views seem rather naive; it now seems clear that the factors which influence the child's development, education and socialisation, must be looked at in terms of a complex interaction, unfolding over time from conception to adulthood and beyond, between children themselves and the experiences received within the family and the community, in the school and the workplace and with their peer groups.

It is in the harmonisation of these experiences that successful development is found. Increasing degrees of disharmony increase the likelihood of failing at school and its associated difficulties. Since many aspects of the child's character and personality, such as learning potential and attitudes and values which enable him/her to benefit from education will be formed from these experiences, it is of deep importance that they be carefully directed.

An analysis couched in terms of background and socialisation has the further important advantage that it focuses the search for causes on to a set of factors that are open to change. It is possible, for instance, to improve the relationships between family, school and community. Schools can be changed to meet the heterogeneity of demands and expectations presented by multi-cultural and pluralistic communities. And it follows that it is possible to prevent,

certainly to reduce, the number of children leaving schools with inadequate academic and social skills to make their way in the world. But achieving all this will be no mean feat; it requires confidence that the theoretical analysis is correct, courage to make the necessary changes, and a commitment of policy to ensure that resources are directed to where they are most required.

## Prevention, not Remedy

The emphasis on prevention focuses attention on the development of the child throughout its life – beginning as early as the womb. When fetuses and parents are healthy, babies are born at full-term and full weight; the educational interest is that low weight at birth (commonly associated with, for example, excessive consumption of alcohol and cigarettes by pregnant women) is associated with slower cognitive development. It is becoming increasingly acknowledged that the child's cognitive and linguistic development must be stimulated during the pre-school years, and that adequate maternity leave, pre-school education and access to health care and other social services are beneficial for educational progress, as evaluations such as those of the 'Headstart' programmes in the United States demonstrate.<sup>1</sup>

In addition, there is growing evidence that these preventative programmes are cost-effective as well as educationally beneficial, reducing the extent of drop-outs as well as demand for expensive special education facilities and custodial care at a later age. The development of appropriate child-care policies – access to private care or a good national system, such as the *écoles maternelles* and the *crèches/garderies* in France – can also respond to women's growing expectations that they will be able to continue to develop their careers

after giving birth. Policies and practices that encourage parental involvement in education also have to be devised – in, say,

pre-school classrooms, caring for children with learning disorders, or helping with extra-mural activities: visits to art galleries, theme parks, swimming pools, and the like.

Many children at risk enter school poorly prepared, cognitively and socially, for learning in a classroom with perhaps 35–40 other children and one adult. Those whose parents do not speak the school's language of instruction at home will have other challenges to respond to which will be exacerbated if the parents themselves are poorly educated and have little personal understanding of the demands on their child and the ways in which schools function.

In response, education systems are beginning to show the necessary flexibility through analysis of school organisation, curriculum content and teaching methods. France, for example, is abandoning 'redoublement' (repeating a year) in favour of educational cycles spread over two or three years. Other countries, not least Italy, the Netherlands, the United Kingdom and the United States are variously introducing other changes: mixed-ability teaching, postponing or eliminating streaming, incorporating ethnic issues and inter-cultural teaching, and so on. One of the main goals of such reforms is to make these essential elements of schooling more sensitive to the educational requirements of the individual child. But the individualisation of the teaching process does not mean providing one-to-one teaching; it emphasises instead the importance of moving away from the idea of teaching to the 'average' child in the class by developing content and method from which all children can benefit – abandoning centralised texts, avoiding illustrations that have a cultural bias and emphasising cultural diversity. That challenge, inci-

Daniel Giry/R.É.A.



Uninspiring schools will not encourage learning.

1. Mary Ann McGovern, 'Education and Care in Early Childhood', *The OECD Observer*, No. 184, October/November 1993.





Truancy can lead to broader difficulties of integrating into society.

Howard Barlow/The Independent

dentially, will also have to be met as more and more handicapped children are integrated in mainstream schools.

## The Pursuit of Flexible Curricula

For many countries, especially those with centralised curricula, stimulating flexibility has meant giving schools more freedom to adapt teaching content and to adopt approaches which are sensitive to the interests of the child and the family and the community, including the workforce. In France, for example, the development of 'Zones d'Éducation Prioritaires' (ZEPs) is a way of supporting local initiatives from central funding while maintaining the general framework of the national curriculum. But the development of flexibility and individualisation should not give carte blanche either to the school or to the child to go their own way; they are procedures intended to raise both personal and average standards by helping children to be successful in school and realise the benefits of education within the mainstream of society.

The transition from school to work is especially important for students likely to fail in school, since it is they who run more risk than others of failing to find work. It is also a period where in some countries ethnic-minority groups experience particular problems. Yet most schools have not yet realised the full implications of the changes that have taken place in the labour market and they do not give adequate attention to the transition to work. Indeed, many schools keep follow-up records only of those students who go on to colleges or universities – which presumably indicates the goals schools aspire to – and perhaps, as a consequence, access by students to potential sources of good information and advice is unnecessarily restricted.

As a way of tackling these problems many OECD countries have developed

schemes to improve the links between industry/business and schools as well as with the wider community.<sup>2</sup> Schools can learn more about the realities facing employers, who in turn learn more about the ways schools are currently developing. In practice, it can mean, for instance, 'de-academicising' the school curriculum and increasing flexibility in the way qualifications are earned. Individualising the curriculum is also a necessary component of this process.

## Three Desiderata

Three important common themes for change can be identified which run across the periods of pre-school, school age and the transition to work. First, children at risk, whose active involvement in society is an essential aspect of future growth, should have their social and personal, as well as their educational, requirements catered for in schools, with more consideration being given to the role of the family and the community. This means improving the social environment in which many children live. The fact that some children succeed in spite of harsh surroundings does not mean that there is no requirement to improve the general conditions in which many of them are raised. That in turn calls for a holistic, not a fragmented, approach to be taken, with the implication that government ministries and departments and other agencies offering, among other things, health care, education and social services should co-operate to establish common goals.

Second, education systems must learn to become more flexible and willing to meet the educational demands of their pupils, instead of imposing unnecessary structural difficulties on them, by insisting, for example, that they repeat a year.

Third, schools and their local communities have to be able to influence education systems so as to develop the necessary flexibility and an individualised approach. Occasionally, that may require a change in the law; it certainly involves changes in school organisation,

the training of teachers and pedagogical approaches. The involvement of the community, particularly that of other professionals and local business leaders, should be a high priority.

Achieving these goals will not be easy and will certainly be dependent on developments in the training of all the professionals involved, as well as on improving methods of evaluating the effectiveness of the system. Some OECD countries have taken these challenges on board. In Australia, for example, the allocation of additional funds from central government is contingent on schools' meeting criteria related to, for example, training, evaluation and community involvement. And in the ZEPs in France government funds are contingent on school-based plans and are evaluated on a three-year cycle.

■ ■

Tackling the problems of children and other young people at risk requires a broad approach that has an impact even as late as their first 25 years of life, since the policies involved also have to tackle the re-integration of young people into the workforce. They must both prevent and improve. The heterogeneity of the populations that make up the societies of the OECD countries means that education systems built on earlier assumptions of homogeneity and on teaching aimed at the average child can no longer provide the education that will be required in the next millennium. ■



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# From Stick to Carrot in the Environment

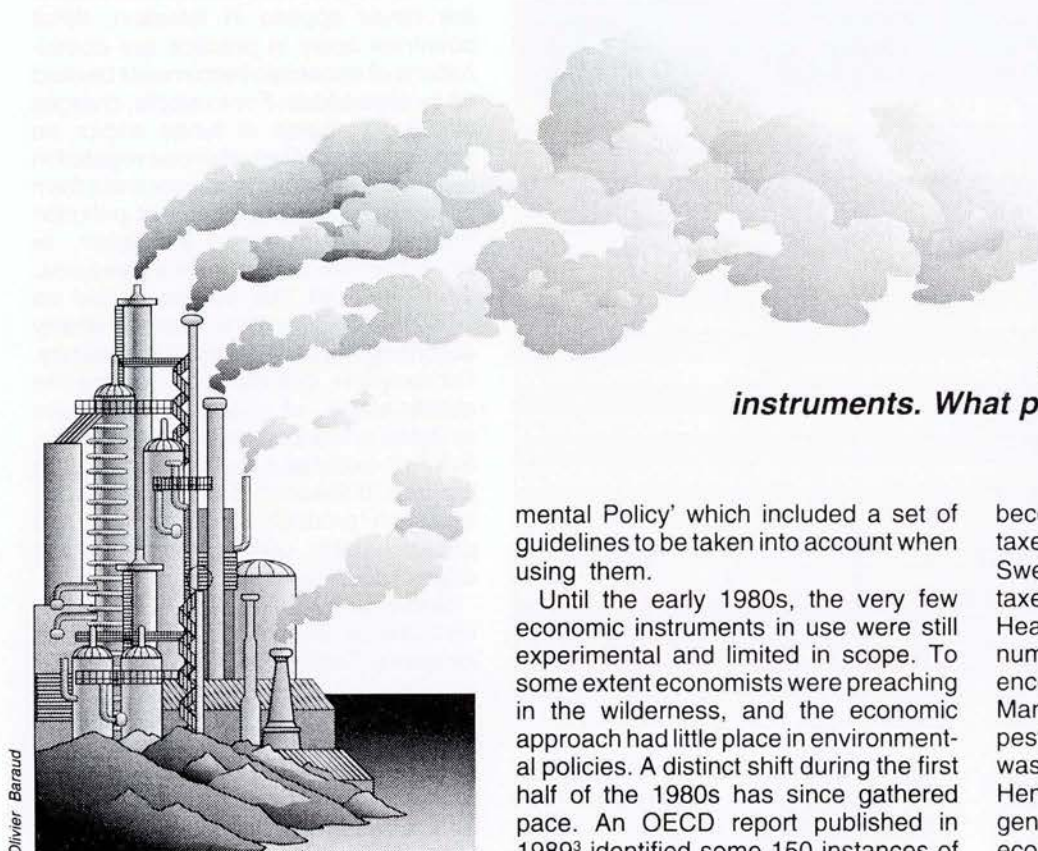
Jean-Philippe Barde  
and Johanes Baptist Opschoor

*With the growth of environmental policies in the early 1970s, two approaches emerged, sometimes in conflict.*

*The first was for government to step in and regulate directly. The*

*alternative, 'economic' approach, based on the neo-classical theory of externalities, brings market mechanisms*

*to bear through economic instruments. What progress have they made?'*



Oliver Baraud

**T**he most usual approach in environmental policy is regulation – a 'command and control' strategy, involving licences, standards and bans. But over the last decade or so economic instruments – taxes, charges, tradable emission rights – have considerably grown in importance (box, p. 25), meeting the call for environmental policies that are both more efficient economically and also fit as best they can into economic and sectoral policies. Both are indispensable prerequisites for a process of sustainable development.

The OECD has long recommended the economic-instruments approach.<sup>2</sup> In January 1991, environment ministers adopted a 'Recommendation on the Use of Economic Instruments in Environ-

mental Policy' which included a set of guidelines to be taken into account when using them.

Until the early 1980s, the very few economic instruments in use were still experimental and limited in scope. To some extent economists were preaching in the wilderness, and the economic approach had little place in environmental policies. A distinct shift during the first half of the 1980s has since gathered pace. An OECD report published in 1989<sup>3</sup> identified some 150 instances of various economic instruments in 14 countries, of which 80 were pollution charges and taxes. Things have moved on considerably since then, and numerous countries, especially in Scandinavia, have introduced new economic instruments.

Between 1987 and early 1993, the number of economic instruments has increased by 25–50% according to country (Table 1).<sup>4</sup> The most significant growth has been in product taxes, especially energy taxes which are

becoming increasingly 'green': carbon taxes in Denmark, Finland, Norway, Sweden and the Netherlands, sulphur taxes in France, Norway and Sweden. Heavier taxation on leaded petrol in numerous countries has done much to encourage wider use of lead-free fuels. Many other polluting products, such as pesticides, fertilisers, packaging, oil wastes and so on, have been taxed. Hence the emergence, still tentative but genuine, of a pattern of 'green' or ecological taxes which, if taken to its logical conclusion, implies real tax-reform, as in Sweden during 1991.<sup>5</sup>

Deposit-refund systems have also grown strongly, up by 35–100% according to country, especially in response to the serious problem posed by constantly rising volumes of packaging materials (140 million tonnes a year in

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Table  
ECONOMIC INSTRUMENTS PER COUNTRY, 1 JANUARY 1992

	Charges on emissions (of which user charges)	Charges on products (of which tax differentiations)	Deposit refunds	Tradable permits	Enforcement incentives
Australia	5 (2)	1 (0)	3	1	2
Austria	3 (1)	4 (2)	3		
Belgium	7 (2)	2 (2)	1		
Canada	3 (2)	7 (3)	1	2	2
Denmark	3 (2)	10 (2)	2		
Finland	3 (2)	10 (2)	2		
France	5 (2)	2 (1)			
Germany	5 (2)	3 (3)	2	1	
Greece	2 (1)	1			
Iceland	1 (1)	1 (1)	2		
Ireland	2 (2)	1 (1)			
Italy	3 (2)	2 (0)			
Japan	3 (1)	1 (1)			
Netherlands	5 (2)	4 (2)	2		
New Zealand	1 (1)				
Norway	4 (2)	8 (2)	3		
Portugal	2 (0)	1 (1)	1		
Spain	3 (2)				
Sweden	3 (2)	11 (2)	4	2	
Switzerland	3 (2)	2 (2)	1		
Turkey	1				
United Kingdom	1 (1)	1 (1)			
United States	5 (2)	6 (1)	4	8	2

Source: OECD

the OECD area). Deposit-refund systems are also being applied for bulky items such as car hulks. Such systems are generally proving highly effective, producing an average return of 80%, and as much as 100% in some cases, for packaging materials and containers (mainly plastic/glass bottles).

There has been little further growth in emission taxes and charges, perhaps because those constituted the first range of economic instruments applied during the 1970s and '80s (many water pollution charges, for instance, were introduced then). Such charges tend to be mainly financial, because their yield is designed to fund pollution-control measures, such as communal water-treatment facilities.

Some countries, such as Australia, Canada and Germany, have introduced marketable pollution permits, but applications are few and of limited scope. Pollution permits are applied on any large scale only by the United States, espe-

cially for air pollution. The US tradable permits programme received a fresh boost from the 1990 Clean Air Act, under which it is to expand significantly. The US programme has clearly yielded some substantial cost reductions, but apparently not to the extent anticipated (40-50%). No estimates are available yet for the country as a whole, but the pollution-permits system will certainly continue to develop.

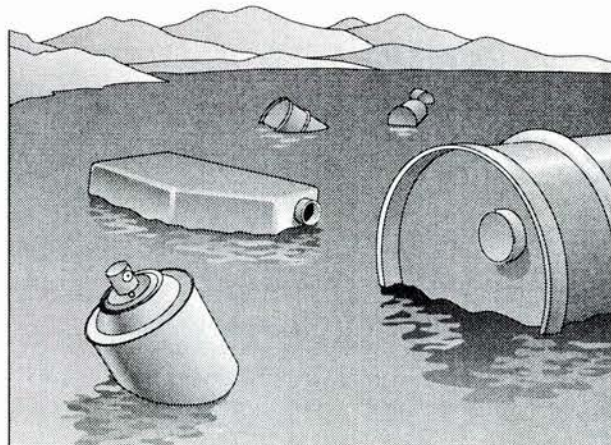
### Six Features

This substantial rise in the number of economic instruments only partly reflects their actual position in environmental policy. The picture at present, more subtly

shaded, can be described in terms of six features.

In the first place, economic instruments are never applied in isolation. What countries apply in practice are combinations of economic instruments backed up by regulations. For example, charges can be a source of funds and/or an additional incentive, whereas regulation provides a general framework and a form of protection against kinds of pollution that are best banned altogether, or limited by means of restrictive standards. That being so, the emphasis laid on individual instruments varies widely according to type of pollution and country. For example, pollution charges are the corner-stone of water-management systems in France and the Netherlands. Sulphur oxide and carbon taxes are to the fore in Sweden. Conversely, many taxes on products like fertilisers and pesticides are only a rather modest adjunct to regulations.

Second, the main goal of economic instruments should be to act as an incentive. That means, for example, that eco-taxes should be levied at rates high enough to prompt polluters to reduce their emissions to the desired volumes. Experience shows, though, that this does not always happen. Admittedly, taxes and charges are incentives in themselves, since everyone wants to pay less



Olivier Baraud



tax, but they tend to be set too low to achieve pollution-control objectives on their own. That is why economic instruments and regulation co-exist.

Yet a trend is now emerging, although still tentatively, towards systems with more 'bite', especially through higher taxes. Certain eco-taxes recently introduced in Sweden, for example, have already produced convincing results: the nitrogen-oxide charge levied on thermal power stations since 1992 (4,500 ecus per tonne of NO<sub>2</sub>) has resulted in an average emission cut of 35%; taxing diesel fuel according to its pollution potential (especially its sulphur content) yielded, within eighteen months, a tenfold rise in the share of 'clean' diesel fuels in total diesel consumption.

Third, many of the taxes and charges retain an essentially financial purpose. It is the search for money to fund environmental protection measures that has led to their being introduced. The funds raised are earmarked for a variety of purposes: financial aids of all kinds to the private sector and local authorities (water basins in France and the Netherlands); funding the rehabilitation of polluted areas ('Super Fund' in the United States); funding R&D projects in pollution control, covering the administrative costs of implementing pollution control policies and measuring emissions; and so on. It is perhaps this 'milk-cow' aspect which explains why finance and budget ministers are now showing so much interest in 'green taxation', even though taxes that have genuine incentives should produce smaller or decreasing yields over time (the less you pollute, the less you pay). It is noteworthy that an eco-tax is more acceptable politically the more its yield is earmarked for environmental protection: the tax seems justifiable and fiscal transparency is ensured.

Fourth, tax reform is on the agenda. If eco-taxes are to play a growing part, how should they be built into present and future tax structures? Taxation will have to be arranged in such a way that non-environmental levies (on, for example, energy, transport, agriculture) do

## WHAT ARE ECONOMIC INSTRUMENTS?

Economic instruments can be defined as proxies for market signals in the form of change to relative prices (through, for example, taxation of certain products) and/or a financial transfer (for instance, a tax or a charge to be paid). One important feature is that an economic instrument leaves economic agents freedom to choose and to adapt their activities, enabling them to maximise profit through whatever solution is the most economically efficient for them (for a pollution tax, simply paying the tax or, alternatively, taking measures to reduce their emissions). Economic instruments fall into one of four main classes.

- Marketable permits are pollution quotas, permits or ceilings (or more broadly, rights to use the environment), marketed by the competent authorities (by allocating them free of charge or offering them for sale). Permits can be traded, bought and sold, within the bounds of rules laid down by the authorities. This approach is applied mainly in the United States to control air pollution (sulphur oxides, lead, CFCs).
- Emission charges and taxes are applied to emissions of air, water and land pollutants, also to noise pollution. France, for example, levies water pollution charges and taxes on sulphur oxides; Sweden taxes nitrous oxides.
- Product taxes are designed to alter the relative prices of polluting products such as fuels, fertilisers, pesticides, batteries, packaging materials, etc.
- Deposit-refund systems have long been applied to beverage containers: a deposit, a kind of tax, is paid on the packaging or container and reimbursed when the packaging or container is returned to an approved agent to be re-used, recycled or destroyed.

Countries are applying financial assistance fairly widely in the forms of grants, accelerated depreciation and soft loans, although in macro-economic terms they are of minor significance (a few tenths of a percent of GDP, varying from one country to another). These too are economic instruments but they have many disadvantages, not least because they conflict with the OECD's 'Polluter Pays' Principle.

not have unfavourable environmental consequences, while at the same time new eco-taxes are effectively incorporated in tax systems. A recent OECD study of taxation and the environment<sup>6</sup> concludes that tax policy and environmental policy must not only be compatible but be made mutually reinforcing.

Fifth, one new feature of the present situation is the growing international dimension of economic instruments. The UN Conference on Environment and Development at Rio de Janeiro in June 1992 forcefully brought home the importance of international action to conserve the biosphere, control climatic change, curb transfrontier pollution and preserve biological diversity.

How can countries implement policies that are effective in all these aspects? The potential international, even global, role for economic instruments is under serious consideration, especially the possibility of taxes to cut emissions of greenhouse-gases (mainly carbon dioxide). The European Commission has proposed to apply a mixed carbon/energy tax across the Community, but the proposal remains blocked at present by the 'conditionality clause' under which no such tax can be applied unless the Community's main trading partners, essentially the United States and Japan, adopt similar measures. Several countries have already opened the way by introducing carbon taxes (Figure, p. 26).

The OECD has produced several feasibility studies for such taxes and their economic consequences. The 'Green' model shows that, to be effective, a carbon tax has to be very high (\$250 per tonne of CO<sub>2</sub> on average for the OECD area, up to \$450 in certain other countries<sup>7</sup>) and to be applied across the world or at least covering, in addition to OECD countries, China and the former Soviet Union, which account for 28% of total world CO<sub>2</sub> emissions. The OECD is also investigating the scope for using

6. **Taxation and the Environment: Complementary Policies**, OECD Publications, Paris, 1993.

7. Tom Jones, 'The Economics of Climate Change', *The OECD Observer*, No. 179, December 1992/January 1993.



economic instruments to conserve common resources and biological diversity (through international transfers, for example), under the Rio de Janeiro Convention on Biological Diversity.<sup>8</sup>

One final feature of the present situation is that it is no longer only the advanced industrialised countries that are applying economic instruments. The transition countries of central and eastern Europe are already applying (Poland in particular) or considering them.

In the dynamic economies of Asia and developing countries examples are fewer (South Korea, Hong Kong, Singapore, Thailand). In the context of structural-adjustment programmes designed to institute true-cost pricing, the economic instruments of environmental policies are definitely going to loom all the larger, since protecting the natural resources of those countries will be an essential prerequisite for sustainable development.

## Constraints and Obstacles

Countries trying to implement economic instruments are encountering various technical, economic and political constraints and obstacles. Technically, a tax may not always be readily applicable to certain forms of pollution, or taxes may be inappropriate for toxic or hazardous pollutants which should best be banned altogether or strictly controlled. Moreover, economic partners are not unanimous. Industry, for example, looks askance at the prospect of new taxes. Two points among many others are particularly sensitive: international trade and distributive effects.

### Trade

Environmental protection tends to have a cost, which may affect the competitive positions of particular firms or industries.<sup>9</sup> But economic instruments, like taxes,

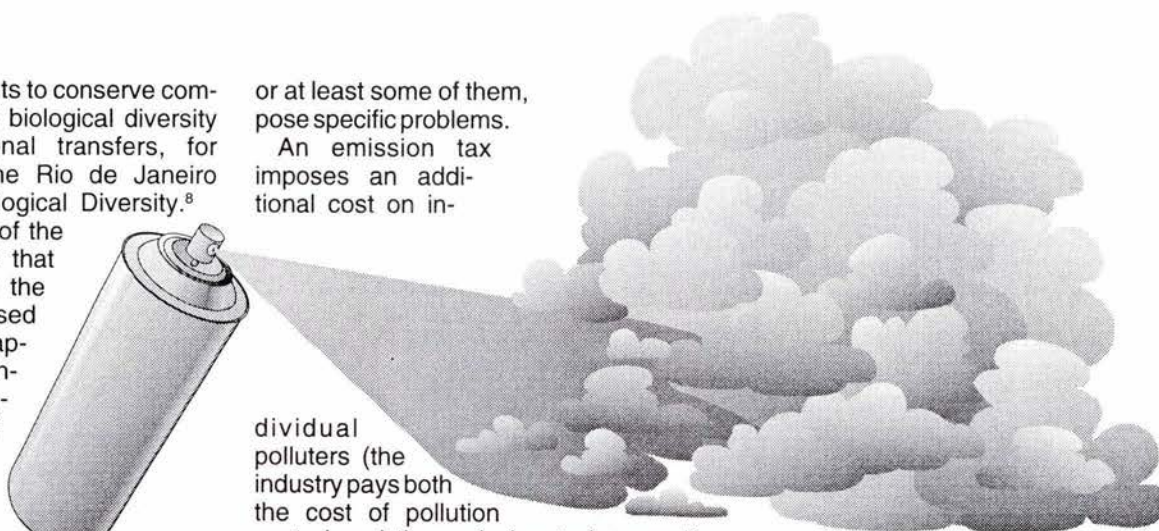
or at least some of them, pose specific problems.

An emission tax imposes an additional cost on in-

dividual polluters (the industry pays both the cost of pollution control and the emission tax), even if efficiency gains which the tax may yield are expected, ultimately, to offset such possible losses of competitiveness. Industry is particularly watchful on this matter, and experience shows that the problem can be a genuine obstacle in discussions on carbon taxes (the conditionality clause).

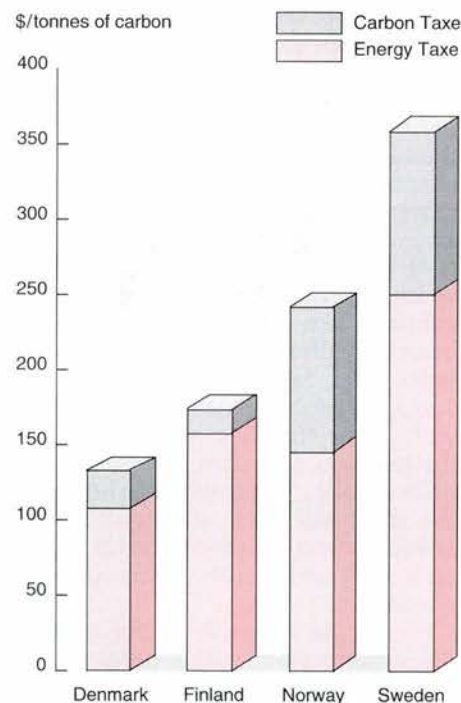
Product taxes should not introduce distortion so long as the 'destination principle' prevails, under which the tax applies at the point of consumption to all products regardless of source. The GATT broadly sanctions the levying of taxes on imports and tax relief on exports, when the same taxes are also applied to products of domestic origin. Tax adjustments at frontiers reflect the 'destination country' principle customary in tax treatment: in order to avoid double taxation, the tax adjustment should be applied in the country consuming the product (the destination country) rather than the source country.

Economic instruments may also raise non-tariff barriers to trade. They can arise for deposit-refund systems, which may affect the kind of packaging used, and how the product is marketed, shipped and distributed. Foreign producers may have difficulty in accessing storage and return facilities for recycling, or in acquiring



Olivier Baraud

Figure  
**AVERAGE TAXES ON ENERGY AND CARBON IN FOUR OECD COUNTRIES**



Source: OECD

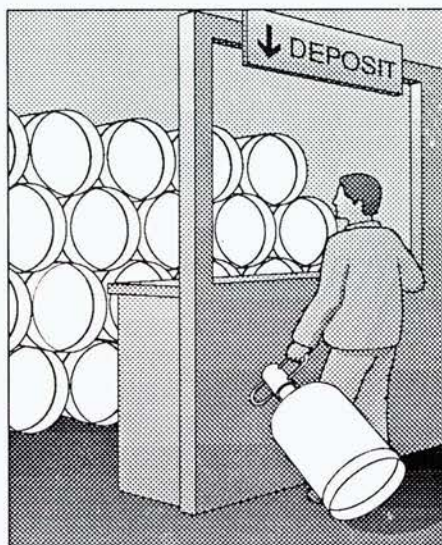
9. Jacques de Miramon and Candice Stevens, 'The Trade/Environment Policy Balance', *The OECD Observer*, No. 176, June/July 1992; *Environmental Policies and Industrial Competitiveness*, OECD Publications, Paris, 1993.



recycling facilities on foreign markets. Producers who are remote from markets applying deposit-refund systems may be handicapped, as may smaller-scale producers.

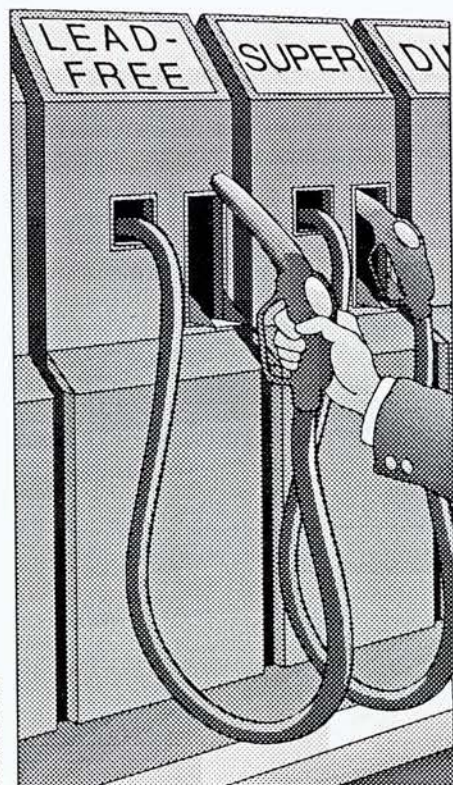
### Distributive Effects

Environmental policies may have implications for the distribution of wealth and well-being. For example, an environmental regulation or tax may have unequal impacts on different categories of income. Eco-taxes are liable to have regressive effects by directly affecting the prices of certain products, such as energy, fertilisers, pesticides and so on. Surveys in the United Kingdom and the United States have highlighted the regressive effects of energy taxes, even though, because most current eco-taxes are still modest, the effects remain very limited. The matter is no less sensitive in the discussion of economic instruments. But it should not be allowed to



Olivier Baraud

various regulatory and economic instruments be better co-ordinated so as to avoid a proliferation of rather ineffectual 'mini-taxes'? How can countries achieve the necessary degree of international harmonisation and co-ordination, both in trade and in protecting the world environment? What methods and procedures can they develop to assess the effectiveness of these instruments? ■



Olivier Baraud

eclipse the discussion, either by undermining the introduction of eco-taxes or by resulting in rebates or any other kinds of exemption, which would erode the effects of the tax and might call its whole validity into question. How environmentally effective a tax is depends to a large extent on the rate at which it is set. If the rate is reduced for distributive reasons, its effectiveness will be jeopardised. That is not to say that the distributive implications should be ignored, but the problems have to be dealt with separately, as part of social policy, not environmental policy.<sup>10</sup>

■ ■

Economic instruments are, of course, not the only tools used in environmental policy. Although a more widespread application of economic instruments is an essential prerequisite for sustainable development, many questions remain outstanding. Should existing instruments be reinforced, especially by setting eco-taxes at higher levels and so making them more effective? Should countries introduce economic instruments in the context of tax reforms? How can the

10. David Harrison, 'Who Wins and Who Loses from Economic Instruments?', *The OECD Observer*, No. 180, February/March 1993.



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# Investing in Eastern

Rolf Alter

*Investment by foreign companies can play a vital role in helping the former Communist countries move to a market economy. What pitfalls and progress can be reported?*<sup>1</sup>

Policies intended to develop the private sector in the countries of central and eastern Europe (CEECs) and New Independent States of the ex-Soviet Union (NIS) must aim at enhancing opportunities and reducing uncertainties for investment. In particular, they include: sound macro-economic policies; a stable political framework; a legal and institutional framework for private business, including tax policies; efficient mechanisms for privatisation; a sound financial sector; and the promotion of foreign direct investment (FDI).

Investment by foreign companies is particularly important in the transition from a centrally planned to a liberal, market economy, since FDI can act as a powerful catalyst for economic change. It offers not only financial resources for host countries; it also brings technology, management, a 'business culture' and access to foreign markets – each of which factors can help overcome obstacles to the development of the private sector.<sup>2</sup>

The performance of flows of FDI to the CEECs and NIS has been mixed. Thousands of foreign companies have invested in the region, the number of projects with foreign participation is expanding rapidly, and the value of FDI flows is increasing. The overall volume of FDI in the region nonetheless falls dramatically short of the external capital required for a rapid increase in the standard of living (Figure). Since early 1993, moreover, FDI flows seem to be levelling off, even in the more advanced of these economies.

This weak performance is disappointing in view of the attractive opportunities for large-scale FDI that many of these countries offer: relatively large, sometimes even vast, internal markets that urgently require an efficient consumer-goods industry, and in some cases



enormous natural resources. But many of the home countries for FDI are in recession and have reduced their outward investment, while potential hosts have to face competition as a location for investment from other regions of the world – and their domestic economic performance is often still very weak.

## Political Stability

Sound macro-economic policies and a political commitment to democracy and the market mechanism are not enough to assure foreign investors. To induce companies from abroad to bolt down their capital in a growth-starved country, policy-makers there must be able to muster a high degree of credibility, and be prepared to support clear, simple and market-oriented policies. Even then it

1. *Investment Patterns in Eastern Europe. Proceedings of the Second AGI Meeting*, OECD Publications, Paris, forthcoming 1994; *FDI in 14 Eastern European Countries in Transition*, OECD Publications, Paris, forthcoming 1994; *Establishing a Reporting System for FDI Statistics: Proceedings of a Technical Meeting*, 1993, available free of charge from the OECD Centre for Co-operation with the Economies in Transition.

2. The non-financial benefits of FDI (in technology, market access, and so on), though difficult to quantify, are of considerable importance in economic development, but are often also the source of major concerns in the host countries because they touch upon sovereignty, foreign domination, and like questions; see Rolf Alter, 'The New Challenge in Eastern Europe: Investment and Restructuring', *Intereconomics*, Vol. 27, January/February 1992.

3. Guillermo A. Calvo, Leonardo Leidermann and Carmen Reinhart, *The Capital Inflows Problem – Concepts and Issues*, International Monetary Fund, Washington DC, 1993.

may be a while before substantive direct investment takes place: building credibility takes time – and in most of these countries the process of reform was implemented only relatively recently.<sup>3</sup>

Obviously, investors will seek protection against erratic changes and risks from political upheavals in countries that are still undergoing far-reaching institutional change. Contracts between states and investors (for large-scale projects) containing stability clauses and guarantees against retro-active changes in laws and policies could offer a degree of security. Expanding the network of Bilateral Investment Treaties (BITs) that many countries – Hungary, Poland and Bulgaria, for example – have initiated will also help provide protection and improve confidence among foreign investors. Legally binding on both parties, BITs spell out rights, obligations and rules of behaviour on essential issues for both foreign investors and host governments. BITs are often a prerequisite for financial support of investors by their home countries. Combined with treaties to avoid double taxation, they can be a stimulant to investment.

## Laws and Institutions

Typically, foreign investors are able to choose between the creation of

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# Europe

## Catalyst for Transition

joint-ventures, establishing companies they own entirely, or holding a minority stake in the equity of an indigenous firm. There are often only a few restrictions on the legal form of the investment, as long as it is legally incorporated in the host country. Basic legal rules for business activities – such as corporate organisation, codes defining and regulating commercial activities, and entrepreneurship and bankruptcy laws – are frequently already in place.<sup>4</sup>

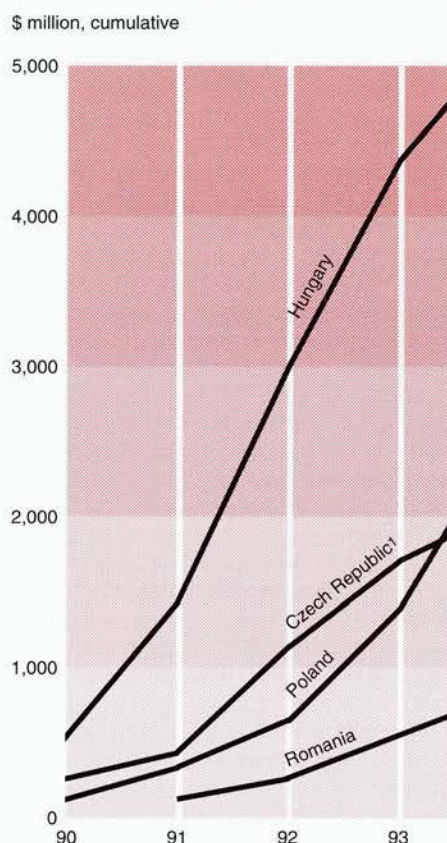
Free repatriation of profits, of the salaries of expatriate workers, and of capital gains is usually granted, although intellectual property rights are not yet fully protected. Domestic legislation and a network of BITs usually provide for compensation in cases of expropriation, and procedures for settling disputes.

Most transition economies follow broadly the principle of national treatment, by which the host country undertakes to treat foreign-controlled enterprises operating on its territory no less favourably than domestic enterprises. Some, like Hungary, include the principle in their domestic laws. There are, of course, still exceptions that limit the freedom of foreign investors in comparison with nationals – in, for example, the financial sector, real estate, and arms production, and restrictions on the ownership of land and fixed property exist in many transition economies. (Here medium- or long-term leasing offers a temporary alternative.) But although these exceptions may be related to domestic policy considerations, they frequently have adverse effects on the perception of the investment climate in a given country.

In spite of the progress already made, there is room for improvement. The most important tasks in the short term are the effective implementation of FDI policies, and ensuring their coherence, predictability and institutional co-ordination.

New laws frequently require new administrative structures that often take time to recruit the qualified staff required to make sure that legislation is effective; and confusion can reign in the interim.

Figure  
**FOREIGN DIRECT INVESTMENT  
FLOW IN CEECs,  
1990-93**



1. Czech and Slovak Federal Republic from 1990 to 1992.

Sources: national statistics, OECD estimates, Economic Commission for Europe

The establishment of 'one-stop-agencies' would seem to be an appropriate response. By uniting all an investor's governmental interlocutors on a single site, it would help reduce the administrative hurdles many investors discover to be an unnecessary headache.

The political process frequently aggravates the problem of competing and contradictory pieces of legislation, since FDI policies are influenced by various interests and may differ at national and sub-national level. With different kinds of legislative acts, such as laws and decrees, it remains sometimes unclear what exactly is the legal basis for a

particular decision (for example, the refusal of an authorisation to invest), and how and where it could be appealed against. A review of first-generation reform laws could help improve consistency. A clear hierarchy of legal and regulatory acts introduced at various tiers of government still has to be established.

### Taxation and Incentives

When these economies were centrally planned, taxes on enterprises were basically transfers of profits from state-owned enterprises to government. The move towards a modern corporation tax requires a definition of the tax base in accordance with the accountancy standards accepted in western countries. The effectiveness of tax audit and collection procedures is an important complement to a sound tax system, while international treaties for the avoidance of double taxation facilitate cross-border investment and contribute to stability and confidence.

Most central and eastern European countries use financial incentives for foreign investment, mainly through tax policies. Experience in OECD countries of the costs and benefits of schemes that offer such financial promotion is mixed indeed. Although it is not clear whether incentives really influence investors' decisions or whether they offer 'windfall profits' for the foreign investor, many OECD countries think that they cannot do without incentives in view of the offers made elsewhere – which could, of course, also be an argument for economies in transition to make use of them.

In that case, they should be based on clear and objective criteria. The budgetary consequences of tax incentives have to be taken into account from the outset: limiting tax exemptions to some percentage of taxable profits may be one way of constraining revenue

4. See R. Alter and F. Wehrle, 'Investissements Directs Etrangers (IDE) dans les Six Pays d'Europe de l'Est aux Economies en Transition (Pologne, CSFR, Hongrie, Roumanie, Bulgarie et Albanie)', *Revue De Droit des Affaires Internationales*, No. 5, 1992.



### THE OECD ADVISORY GROUP ON INVESTMENT

The OECD Advisory Group on Investment (AGI) was established in 1992 to provide a forum for:

- an exchange of experience in FDI policies among senior policy-makers from Western governments, transition economies and representatives from the private sector and labour
- monitoring progress in FDI legislation and policy – policy-makers from the transition economies have the opportunity to report regularly on recent legislative and institutional changes; quantitative developments in FDI are also addressed
- discussion of economic policy issues that put FDI in the broader context of the transition process.

The AGI, which includes not only the CEECs, but also the Baltic States and many of the NIS, is unique in many ways. The active role of the private sector ensures that both policy issues and practical problems and challenges of investors are recognised and discussed in a mutually beneficial perspective. Substantial flexibility in the format of the AGI allows for the *ad hoc* participation of experts, academics and so on. Emphasis has been put on the close co-operation with other international institutions for gathering maximum expertise.

The substantive work of the AGI started with a meeting in Paris in January 1993 that produced a detailed catalogue of measures that create a favourable business climate. The second meeting, in Warsaw in July 1993, focused on the investment patterns of western-based foreign investors; it was based on a comparative study of the investment processes, and examined case studies of the experiences of individual western investors in the CEECs and the NIS. The third meeting of the AGI, in Budapest in February 1994, will discuss the role of financing and guarantee schemes for the promotion of FDI; commercial and official sources of investment capital will also be explored and bilateral and multilateral investment guarantee schemes will be examined.

losses, and 'sunset clauses' that determine an expiry date for incentive provisions are also useful in this context.

But some east European countries have abandoned the policy of generous tax incentives, mainly because of the exponential growth of revenue foregone.

5. See Hans J. Blommestein, 'Banks in the East: Paths to Privatisation', *The OECD Observer*, No. 185, December 1993/January 1994.

So is there an alternative? A few countries have introduced direct, targeted subsidies to investment – in infrastructure, for example. One temptation would be to offer high and selective customs duties and quotas to protect foreign production in the country. Some major investors seem to have bargained successfully to obtain such advantages. But giving in to this kind of request does three things. It weighs on the liberalisation of the external regime that many transition economies had implemented so courageously at the outset of reform. It creates substantial economic costs because it distorts the structure of production and trade. And it makes it hard to remove the special treatment, as experience with any kind of subsidies demonstrates everywhere.

The accumulation of non-performing assets and highly inefficient clearing and payment settlement systems distort proprietary relationships between banks and large domestic enterprises. That calls for a rapid and massive bank restructuring.<sup>5</sup> The creation of a sound banking system is a priority of financial reform. First, the bulk of domestic savings is likely to be channelled through the banking system rather than capital markets, at least at the early stage of transition. Second, an efficient banking system is necessary for the effectiveness of discount rates and other indirect monetary-policy instruments and for the development of capital markets. And third, although foreign investors are likely to resort to external capital to finance new large investment projects, an efficient local credit market is required for normal working-capital operations and to finance local partners in joint ventures.

Although retained earnings and bank loans are likely to be major sources of

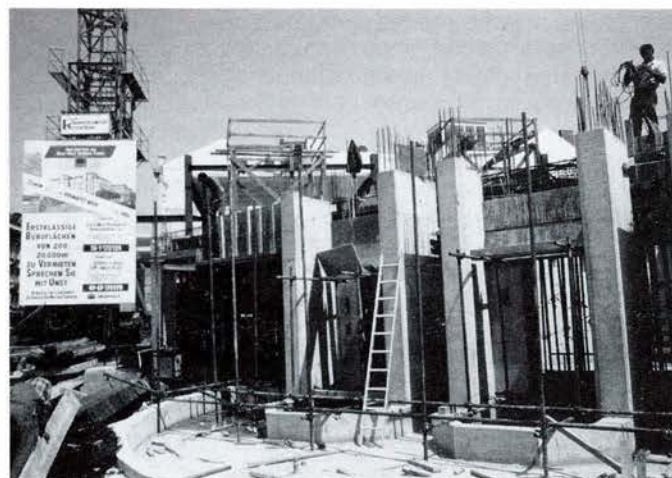
finance for local enterprises for some time, the development of markets for equities and other securities is of increasing importance, especially to foster privatisation and thereby increase foreign participation in existing enterprises.

Emerging financial markets typically are vulnerable to malpractice, fraud and excessive exposure to risk, which undermine the confidence both of domestic savers and of foreign investors. The strengthening of supervisory structure and prudential regulations is therefore an immediate priority for a successful financial reform.

### Promoting FDI

National programmes intended to promote investment usually consist of three main elements: building or changing the 'investment image' of a country; generating investment directly; and servicing existing and prospective investors.

Foreign investment agencies (FIAs) play an important role in preparing and distributing information about the country as an investment location. There is no uniform model for such an agency. It should at least be autonomous and have sufficient resources and policy flexibility to carry out its promotional activities effectively and recruit qualified staff. Experience shows that FIAs operate



Craig/Expo



more efficiently when registration and approval functions for FDI projects are clearly separated. FIAs could also provide 'one-stop' services for investors and act as mediators with the regulatory authorities. FIAs should also encourage the establishment of business councils and associations of domestic and foreign investors to promote dialogue between government officials and the private sector and to develop recommendations for improving the investment climate.

An important feature in support of outward FDI by home countries are 'open market policies' that help exploit the links between trade and investment, particu-

institutions could help in identifying suitable investment projects. There should also be room for the expansion of investment guarantee schemes. It remains to be seen whether multilateral agreements are adequate for the specific requirements of eastern Europe and the NIS because, for example, of frequent changes in legislation.

Training has been identified as a vital ingredient in the transition. Western governments could provide an exchange of civil servants, and private companies could assist in offering training to local employees in the East, which will have a substantial impact on the social and economic culture of the CEECs and NIS. Finally, international organisations could step up their efforts to provide training in areas related to private-sector devel-

opment, such as privatisation, taxation and the like.

■ ■

The contribution of foreign investment in transition economies goes beyond the entrepreneurial and financial engagements of the investor. Representing the market system, foreign investors contribute to the emergence of the corporate business culture and help shape the attitudes of a population that, until recently, was not confronted with a substantial foreign presence. That role brings with it responsibilities, and multinational enterprises ought therefore to commit themselves to principles of good corporate behaviour. The OECD's Guidelines for Multinational Enterprises,

which address a wide range of issues, including respect for the host country's general policy objectives, industrial relations, competition and environmental protection, have contributed to an open climate for FDI in OECD countries. They could do good work also in the CEECs and NIS.

Foreign investors could also make their experience available to policy-makers in the host country, through, for example, a consultation mechanism between the host government and the private sector – where business associations with a fair representation of domestic and foreign investors would discuss policy problems of investment with the government. Setting up or promoting these private business associations could also be a major contribution to the building of institutions in transition economies. ■



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East News/Sipa Press



Craig/Expo

larly where central and eastern Europe and the NIS provide a sound basis for export production. Market access is a powerful incentive for export-oriented FDI.

In addition, investor-country governments and multilateral institutions have designed instruments targeting the investment process directly, such as financing feasibility studies and providing start-up loans in hard currency repayable in local currencies. They have also offered close co-operation between FIAs in the East and their own agencies.

To give small and medium-sized enterprises more chance of investing in transition economies, special programmes have been designed in the EC, and more are desirable. Western governments and/or international financial



# Hungarian Agriculture at the Crossroads

Matthew Harley

*The move from collectivism to market is proving difficult for Hungary's agricultural sector, as it has for all the other economies in transition. Progress in the reform of farming and the food industry has been patchy but is undeniable. It should not be compromised by the mistaken adoption of the kind of support policies that have produced large-scale inefficiencies in OECD countries.<sup>1</sup>*



Ph. Juliette/Sipa Press

**A**lthough in many respects less centralised than other countries in central and eastern Europe (CEECs),<sup>2</sup> Hungary, like them, suffered severe macro-economic imbalances after 1989. But by 1993 there were signs of a turn-around. Hungarian economic growth may have been close to zero for 1993 in contrast to the sharp falls of earlier years. Inflation, which never became hyper-inflation, has declined and should have stayed around 20% for the year as a whole. In mid-1993 the rate of unemployment was about 13%, and interest rates remain high.

Like many other sectors, agriculture has contracted, a fall exacerbated in 1992 by drought. As in the other CEECs, Hungarian agriculture has been squeezed between soaring costs and prices that are rising more slowly. Demand has been depressed by the loss of CMEA<sup>3</sup> markets for exports and by falling domestic purchasing power with the removal of consumer subsidies and reductions in household incomes. These conditions, coupled with lower producer subsidies, have brought about many bankruptcies

in agriculture. The accompanying loss of jobs, an inevitable feature of adjustment, has been marked.

The structure of agricultural production in Hungary, as in most other centrally planned economies, was based on the *sovkhoz*, the 'state farm', held in state ownership, and the *kolkhoz*, a 'co-operative' or collective farm in which farmers had notionally agreed to pool their land to be farmed collectively – though any 'voluntary' behaviour in the early days of collectivisation was rapidly replaced by various forms of coercion. In Hungary's case private ownership persisted throughout the Communist period, and much of the land remained the individual property of members of the collective farm. A substantial degree of private farming was also permitted on plots assigned to individuals on collective farms and on state farms. This symbiosis of private and collective farming accounted for much of the relative prosperity of Hungarian agriculture.

## Reviving Property Rights

Restructuring has involved the break-up of collective farms or their transformation

into free co-operatives. And state farms are being privatised, in a process that the government hopes may both encourage the development of private farming and avoid the problem of farm fragmentation that has occurred in other CEECs.

As elsewhere, of course, the restoration of former property rights has been contentious. In 1992, Hungary opted for a process of partial compensation rather than a restitution of expropriated property. Compensation vouchers were paid, on a sliding scale of loss, to successful claimants. These vouchers are bonds that can be used by the bearer to acquire shares in state-owned industries being privatised or to acquire housing owned by local authorities; they can also be traded for cash through brokers and on the Budapest stock exchange or used to claim a life annuity. The first bearer

1. *Review of Agricultural Policies: Hungary*, OECD Publications, Paris, 1994.

2. The CEECs include Hungary, Poland, the Czech Republic and the Slovak Republic as well as Albania, Bulgaria, Romania, and the Baltic States: Estonia, Latvia and Lithuania.

3. The Council for Mutual Economic Assistance, also known as Comecon, was established in January 1949 by centrally planned economies in response to the creation of GATT in 1947. Its aim was to co-ordinate the economic development of members through centralised arrangements for trade. It collapsed in 1990.

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of a voucher can use it to acquire farm land in a series of auctions from 'funds' of land held by collective and state farms.

This settlement of property rights has much to commend it. By allowing compensation for lost land to take various forms, including land of equivalent value if the claimant so wished, it helped to separate questions of justice from those of land privatisation and farm restructuring.

The results so far have nonetheless been disappointing, mostly because validating claims is so complicated. Disputes over boundaries and rights of access have delayed the resolution of claims and the subsequent issue of vouchers. That in turn has retarded the auction of land and the resolution of property rights. And delays in settling land issues have potentially serious consequences for the development of agriculture. They hinder the emergence of the efficient market in land that is necessary if new banking and financial institutions are to facilitate investment in agriculture. Restrictions on the use of any land, acquired as compensation, for any use other than farming may also be hindering the development of a land market.

The basic aim of the legislation reforming the collectives to force them to transform themselves into new business organisations, such as private or public companies, or, if they so wished, into new, free co-operatives. Although the deadline has technically passed for this transformation – it was supposedly the

end of 1992 – many issues remain unresolved.

Few members of the former collectives who had re-established as new co-operatives opted to take their land and other assets out in order to farm independently. This low rate of conversion to private farming can be ascribed to many factors. There was undoubtedly a reluctance to give up what had generally been a relatively prosperous and secure environment in favour of higher-risk private endeavour. State and

obliged to provide jobs for members. The resulting power of management to share out the remaining jobs may have been used to put pressure on people to stay and to vote for the new co-operative structure.

Such farming co-operatives have not developed and thrived in market economies, and indeed the new co-operatives may not survive in Hungary. Yet the hybrid business organisation that is emerging – a mixture of co-operative and other private or public structures – could

facilitate their survival or their evolution into other forms.

The privatisation of state farms is a different process to that of the transformation or reform of collective farms.

Apart from a small number of specialised state farms, one hundred or so state farms are to be wholly privatised in the same manner as any other state-owned industry. The aim is to create viable individual farms with between 1,000 and 2,000 hectares of land each. In addition, the industries attached to state farms can be transformed and sold as units without any farm land attached.

The privatisation of the state farms has

been slowed by a number of difficulties. Prominent among these is the delay in compensation. Like collective farms, the state farms were obliged to put land in compensation funds against any potential claims. And until the claims are resolved, the vouchers issued and all necessary land auctions take place, all state farm-land remains in the hands of a state agency. Only the non-land

*Hungarian exporters have difficulty competing with heavily subsidised products on third markets.*



*István Csérei/Interphoto MTI*

local authorities have not replaced the social safety-net function formerly provided by the collective farms. Few co-operative members or workers as yet have the knowledge and skills necessary to survive as private farmers. Capital is scarce and expensive, and market conditions have not been attractive.

Since the transformation, by contrast, the new co-operatives are no longer



assets of the farms can be offered for sale; land for farming can only be rented. Inevitably, there is now uncertainty and confusion as to the true amount of land that will be available with the other assets being offered for sale.

Moreover, the state farms are saddled with so much debt that they are unattractive at the prices being asked. Foreign interest may also have been dampened by restrictions on land acquisition by non-residents. More recently, some debt has been consolidated and firm commitments made as to the minimum area of land that will be available for sale or rent from the state with each unit to be privatised. Government experts now expect about one-third of the state farms to have been privatised by the end of 1993, helped by subsidised credit being made available to finance buy-outs by management, at around half the rate of 30% or so normally charged for agricultural loans.

## Privatising the Food Industry

The degree of privatisation achieved in the food industry has been mixed. The most successful group consists of companies producing consumer goods such as vegetable oils, sugar, alcohols, confectionery and tobacco. These firms were more amenable to privatisation, for a number of reasons, not least their more modern technological base, better location and closer ties with western businesses. Less successful are the more traditional industries – canning, meats, dairy and cereals, whose lower value-added products were traded largely with the Soviet Union. Their severe financial condition after the loss of eastern markets has undoubtedly played its part; but the poorer prospects, poor location and sometimes low state of technology and quality are major factors in delaying their transformation and discouraging interest in acquiring them.

Foreign interest has been strongest in the less traditional industries. Like the tobacco industry, the vegetable oil in-

dustry is now completely foreign-owned. It was sold as a single entity, effectively converting a state monopoly in vegetable oil into a *de facto* private, foreign monopoly, though the final product is still open to some competition, as vegetable oil is not subject to quantitative import restrictions.

The small number of former state-owned monopolies in foreign trade – trade in all cereals and vegetable oils, all meats and all fruits and vegetables used to be under three state monopolies – have been effectively privatised, although their new owners still include state companies, state farms and co-operatives, themselves still undergoing privatisation. In 1993 the former monopolies still retained a very large share of foreign trade although that share is declining and competition is growing.

Competition policy, too, has a vital role in the transition to a market-based agricultural sector and ensuring the success of privatisation. In some areas it is difficult for competition to emerge because of high entry costs and border protection. The job of the state in ensuring competition in agricultural products, during and after privatisation, should be emphasised. In addition, to take advantage of emerging trade opportunities and to compete with imports, Hungarian business has to enhance the quality of its agricultural and food products and

increase the effectiveness of its marketing, at home and abroad.

## Restoring Markets

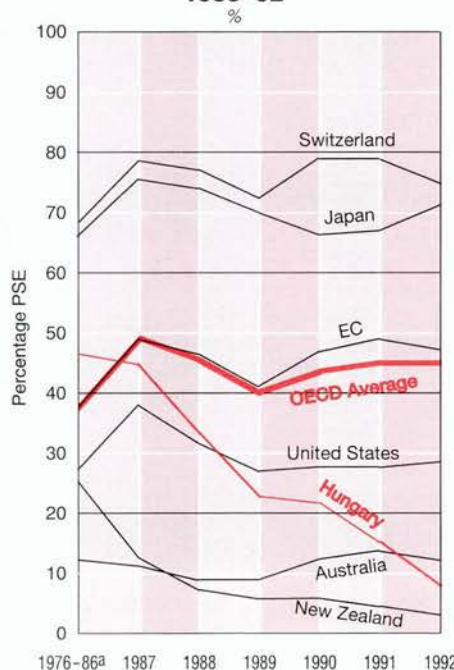
Before the transition, agricultural markets were regulated essentially by the state procurement system under which input and output prices were strictly controlled. Subsidies to the food industry to meet losses on domestic sales (consumer subsidies), as well as to cover losses on export sales (export subsidies), were used extensively to sustain these industries and maintain regulated farm prices. Other trade measures, including quantitative controls on imports and exports, were also used.

In most of the CEECs, including Hungary, the reform of the supply side of agriculture through the break-up of collectivised agriculture has been accompanied by the dismantling of the compulsory state procurement system.

Price liberalisation has been the principle instrument of reform here. The difficult market conditions resulting from these changes have led naturally, but unfortunately, to pressure for relief in the form of support mechanisms modelled on those of the Common Agricultural Policy (CAP) of the EC and other western European neighbours. The tendency in the CEECs to provide such structures has also been

encouraged by the apparent desirability of aligning their policies with the CAP

Figure  
PSEs IN HUNGARY  
AND THE OECD COUNTRIES,  
1986-92



a. 1986 for Hungary  
Source: OECD



Horvát/SABA-R.É.A.



The privatisation of the agro-food industry has had mixed results.

with a view to eventual membership of the EC.

This offers the danger of putting in place a mechanism to guarantee minimum prices that in future years, and under pressure from interest groups, could be used to increase support and further distort agriculture (even if the danger seems slight now, given how low Hungarian prices now appear). Many similar systems that were introduced in OECD countries – with the same good intentions – have proved difficult to remove.

## Support to Agriculture

For some years now the OECD has been calculating the total support to agriculture in an indicator known as the Producer Subsidy Equivalent (PSE).<sup>4</sup> Simply put, the PSE measures the money value of the transfers made in favour of primary agriculture from the range of government policies that affects farmers' interests. It is especially effective in identifying the transfers to producers that result from the higher prices consumers are obliged to pay as a result of market regulation. These 'market price support' transfers are often much higher for OECD countries than the more visible direct transfers that are made from government budgets.

The percentage PSE, broadly speaking, measures the share of producers'

farm receipts accounted for by transfers. The Figure shows that Hungary has done better than any OECD country in reducing support to agriculture since 1987.<sup>5</sup>

This sharp drop in support can be explained by a number of policy-related and other factors. Among the policy factors has been the reduction in protection of the domestic market because of cuts in the rate of export subsidy and in tariff rates. Another factor has been the very sharp cuts in many of the subsidies paid to agriculture directly from government budgets, often paid to the food industry to cover losses. Another has been the rise in costs after the product leaves the farm gate, not least because of the persistent inefficiency of monopolistic industries down-stream.

Among the non-policy factors is the price-cost squeeze. Producer prices have not kept pace with rising costs and the general rate of inflation. World prices, rising more in line with domestic inflation as the exchange rate adjusted,<sup>6</sup> have narrowed the price gap between the farm and border prices in forint terms;<sup>7</sup> market price support has therefore declined over the period 1986–92. The reduction in export subsidies is in part both a cause and a result of this evolution.

Hungary has to sustain this achievement if it is to be competitive and, in particular, has to be alert to the danger that the new system of market regulation

could become an instrument of higher market-distorting support. Calls for more support are stimulated, quite understandably, by concerns about the penetration of the Hungarian market by the subsidised exports of OECD countries and the difficulties Hungarian exporters have in competing with such heavily subsidised products on third markets.

■ ■

Increased import protection for domestic markets and fighting export-subsidy wars on third markets are not answers for Hungary. Instead, Hungary has to try to maintain and improve the competitiveness of its products on domestic and export markets by a restructuring of its industry. The establishment of strengthened and more operationally effective GATT rules and disciplines together with a multilateral reduction in support and protection would help maintain such a policy orientation.

Hungary is a Cairns Group member and thus advocates freer trade. Hungary requires freer access to OECD markets and less disruption of her own and third markets by the export subsidies of big exporters. But it must also resist protectionist pressures at home and reduce its own use of non-tariff barriers. ■



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6. For the PSE calculations, the official forint exchange rate against the US dollar was adjusted to reflect changes in the domestic price level relative to those in the United States. This adjustment had the effect of increasing the rate of decline in the percentage PSE compared to the results without the adjustment.

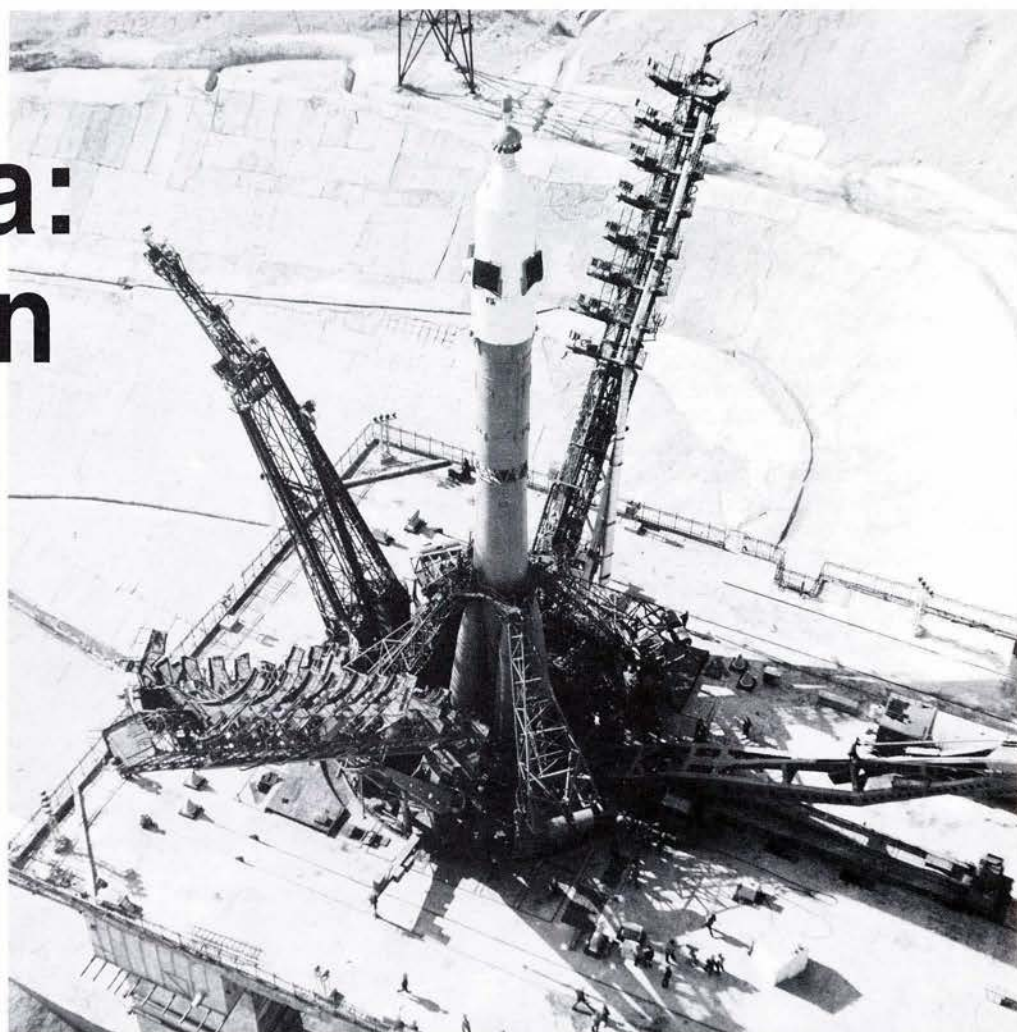
7. In November 1993 the US dollar was worth about 100 Hungarian forints.



# Science in Russia: Implosion and Rebirth?

*Jean-Eric Aubert*

Fototronics TASS



***Russia has inherited most of the science and technology complex of the former Soviet Union. But with the crisis in the economy and the political uncertainties connected with transition towards a free market, this huge system is rapidly falling apart. Where does research and development stand in Russia today? How are the scientists and engineers coping? How is the military establishment moving to civilian activity? What is the government doing? What part is being played by international co-operation? The Russian authorities have asked the OECD to provide an outside opinion on these questions.<sup>1</sup>***

In its day, the Soviet Union regarded science and technology (S&T) as one of the pillars of development and a key to its power in the world. The S&T complex took on gigantic proportions under the aspirations of both the military and the bureaucrats. In the late 1980s there were as many as 1.5 million researchers and technicians engaged in research and development (R&D) – nearly a quarter of the world total and almost as many as in the United States, but in an economy the real size of which was considerably smaller.<sup>2</sup> The military are reckoned to have accounted for over 70% of R&D spending.

There were more than 5,000 R&D institutes. Over 70% of the S&T workforce was employed in branch research in-

stitutes. Basic research was for the most part the concern of the USSR Academy of Sciences; roughly 12% of all science personnel worked in Academy institutes. University research was underdeveloped, employing only 6% of science personnel – a result of the Soviet principle of keeping research separate from higher education. Research carried out within industry itself involved no more than 10% of the total.

The innovation system resembled a pyramid divided vertically into well-defined layers. In most branches of activity, research, design, testing and production were kept clearly apart. Innovation – as

it is understood in a market-based economy, that is, as not only the development but also the dissemination of new products and techniques – barely existed. Only one or two enterprises would handle questions of application –

1. **Science, Technology, and Innovation Policies: Federation of Russia**, Part I: Evaluation Report, CCET/OECD Publications, Paris, forthcoming 1994; Part II: Background Report, CCET/OECD Publications, Paris, forthcoming 1994. The two Reports will also be published in Russian. They were drafted in 1993 on the same lines as other OECD S&T country studies. In each case, a background report is prepared by specialists in the country concerned and an evaluation report is drawn up by experts from OECD countries working in co-operation with the OECD Secretariat.

2. US GDP in the late 1980s was estimated, according to a recent International Monetary Fund study, at about 22.4% of world wealth, whereas the figure for the Soviet Union was 8.3% (*World Economic Outlook*, Annex IV, IMF, Washington DC, May 1993).

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hardly surprisingly, since monopolies were the rule in every sector.

Another feature of the Soviet system was the existence of more than 70 science cities (*naukograds*), each with its speciality: aeronautics, electronics, telecommunications, nuclear science (over 15 sites), and so on. Located in large part close to Moscow, most of the science cities were off limits to foreigners.<sup>3</sup>

Management of the S&T system was controlled to a large degree by the Military-Industrial Commission (VPK), representing the complex of the same name. It worked through the Ministry of Defence and a dozen other Ministries, including the Ministry for Nuclear Energy (Minatom), whose budget was bigger than that of the Academy of Sciences. The system was also infiltrated by the Communist Party, whose cells were present in every laboratory and factory and which acted as a communications thoroughfare, regionally and locally, for the central government. Lastly, the State Committee for Science and Technology (GKNT), headed by an official with the status of Minister or on occasion Deputy Prime Minister, took charge of national planning and international co-operation.

This elaborate organisation began to crumble and fragment when the Soviet Union burst and the economy ran into crisis.

## The Collapse of the Apparatus

With dismemberment of the Soviet Union the research and innovation apparatus fell apart. Although Russia controlled the lion's share – 70% of R&D plant and personnel – the system was

relatively well integrated across the USSR. There were many sectors, the least militarised ones in particular, in which R&D establishments suddenly found themselves cut off from their science correspondents and their industrial design bureaux and experimental stations located in other Republics.

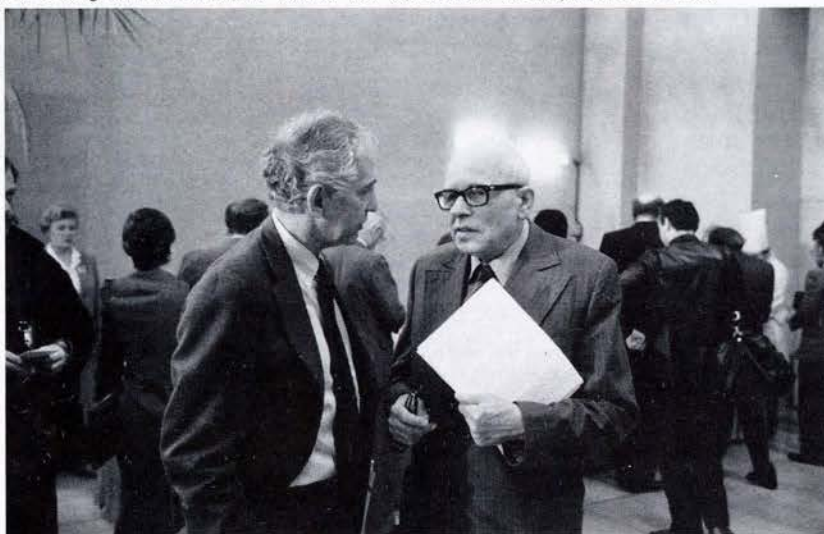
But the worst blows have been inflicted by the economic crisis. From 1991 to 1993, the budget for research tumbled by two-thirds in real terms. Funds are today distributed on a quarterly or even

and establishment directors, have nevertheless suffered severe damage in terms of quality.

Institutes have done everything within their power to stay afloat. Many have sold or let part of their premises, taking advantage of the budding market-based economy to give a roof to a new business. Some have set up their own firms or accommodated firms organised by their staff to merchandise their services and technology, such as their data-processing facilities. Others have sought contacts

abroad in an attempt to sell their expertise in exchange for hard currency. Russian science is being 'dollarised' as western companies and foundations enter into contracts with institutes and researchers. It is helping to save, but is also somewhat disorganising, the best elements in the system. With the dollar buying 1,000 roubles in autumn 1993, and the average Russian monthly wage today standing at 90,000 roubles, a tremendous divide has been created between scientists who are receiving foreign

*For a long time now Russian science has commanded the respect of the West.*



Inge Morath/Magnum

monthly basis. In a context of 30% inflation a month, that poses insoluble problems. External sources of funding – among them, enterprises that had been obliged under the old rules to order a certain amount's worth of research from R&D institutes – have dried up.

The immediate result of these hard times was a rapid outflow of scientists and technicians.<sup>4</sup> An estimated 300,000 researchers and engineers have abandoned the R&D sector in Russia, most going to other parts of the economy. The brain drain abroad has been limited: about 20–30,000 researchers, counting both those who leave for good and those who take up long-term contracts in another country. Some activities, deserted by many of their best researchers

money and the rest.

As to industry, the sudden opening-up of the market has resulted in an invasion of foreign products with which Russian manufacturers cannot compete. A good example is the micro-computer market, where local makers were wiped out in the space of a few months.

Most of the forbidden cities have opened their gates to make their technology, services and equipment – some of it without equal elsewhere in the world – available, and not only to for-

3. Tim Kelly and Martin Salamon, 'Swords into Ploughshares, Tanks into Telephones', *The OECD Observer*, No. 177, August/September 1992.

4. Anne de Tinguy and Catherine de Wenden, 'Eastern Europe: What Benefits from the Brain Drain?', *The OECD Observer*, No. 184, October/November 1993.



eigners.<sup>5</sup> But these places are mono-technological by nature and are having enormous difficulty in diversifying. Their institutes and industries are further handicapped in their efforts to adjust by having to pay for their staff's housing and social services.

## Government Action

As soon as the first Gaidar government was set up after the attempted putsch in August 1991, a Ministry for Science and Technological Policy was created on the foundations, and with many of the powers, of the old GKNT. It was given responsibility for the whole civilian R&D budget (an important point), and the various industry-sector Ministries were abolished. The Ministry of Defence retained control over the R&D appropriations in its field. The Academy of Sciences, which has always enjoyed high prestige and a certain amount of freedom, continued to manage its institutes and to receive its own share of the national R&D budget. Friction rapidly developed with the new Ministry for Science as a result of conflicts of interest and power-struggles in many different activities.

A Russian Fundamental Science Foundation was created by presidential decree in late 1992 and funded with 3% of the civilian R&D budget. Its purpose is to aid research projects controlled by western-style peer review. During the first four months of 1993 it distributed funds with a will, 80% of the money going to Academy of Sciences researchers.

The Ministry has launched a programme of assistance that benefits thirty or so specialised institutes, renowned nationally, even world-wide, for the quality of their personnel and facilities, to help them survive through the current crisis. These newly dubbed 'Federal Research Centres' are granted 40% of their staffing costs by the Ministry, on the condition that they raise the rest of their funds in Russia or abroad. Some university institutes have joined the

## TEN KEY RECOMMENDATIONS

The OECD Evaluation Report lists almost thirty recommendations on the subject of institutions, adjustment of R&D to economic capacity, promotion and protection of innovation, development of civil technology, international co-operation, and improvement of statistics and accounting practices. The ten which follow seem particularly important for the transformation of Russian science and technology with a minimum of expense.

- the establishment of a reasonably sized R&D budget within the state budget (as a percentage of government spending), making it available annually to designated recipients
- the drawing-up and implementation of rational personnel reduction and re-organisation schemes within the different R&D institutional structures (Academy of Sciences, university and branch institutes)
- the development of extensive peer-review evaluation mechanisms for attributing funds to R&D projects requiring support, choosing institutes for preservation, nominating researchers eligible for aid
- the familiarisation of all institutes and firms with accounting procedures capable of measuring the real costs (including indirect subsidies) of research and innovation
- the constitution of an effective judicial system for protecting inventors and entrepreneurs against fraudulent practices, monopolies, and the like
- the introduction of a system of quality norms and certification which will eventually bring Russian merchandise up to OECD market standards
- the elimination of institutional and financial obstacles to the transfer of foreign funds intended for S&T co-operation
- the design and carrying-out, in conjunction with the OECD countries, of large-scale programmes to help young researchers and teachers
- the modernisation, with outside help, of telecommunications services
- the avoidance, through negotiated 'co-operative equilibria' agreements, of destabilisation of certain world markets.

programme but the Academy institutes have so far declined the offer.

Intellectual property laws providing for a system much like the European one

5. Hans-Peter Gassmann, 'Krasnoyarsk-26', *The OECD Observer*, No. 177, August/September 1992.

were passed in autumn 1992. They are largely ineffectual for lack of enforcement structures (inspection, penalties for fraud or infringement). Other vital factors in improving the climate for innovation – norms, standards, quality promotion – are stultified by the absence of resources and, above all, of a guiding strategy.

Parliament, represented by its Commission for Science and Education, on the whole co-operated actively with the Ministry in implementing policy – until it was dissolved last September. The biggest obstacle to reforming the S&T system has been, and continues to be, not so much disputes between the executive and legislative branches, as in other sectors, but the lack of the third leg of the tripod in functioning democracies, the judiciary. Entrepreneurs and innovators trying to gain a footing in the nascent market economy are seriously hindered by the absence of arrangements for monitoring compliance, enforcing laws and decrees, or seeking redress.

## International Co-operation

Russian science for a long time past has commanded the respect of the West for its achievements in theoretical (mathematics, say) and applied (space) activities alike. When the barriers around it suddenly came down in the early 1990s, international co-operation went into high gear, especially as it was feared that top-flight teams might make their way, taking sensitive technology with them, to developing countries eager to arm themselves quickly, powerfully and cheaply.

The governments of many OECD countries, the G7 in particular, stepped up the budgets of their bilateral programmes and launched new initiatives such as joint ventures and institute twinning. Multilateral projects were also initiated. The best-known of them is probably the creation in Moscow of the International Centre for Science and Technology funded by the United States, Japan and the European Community.

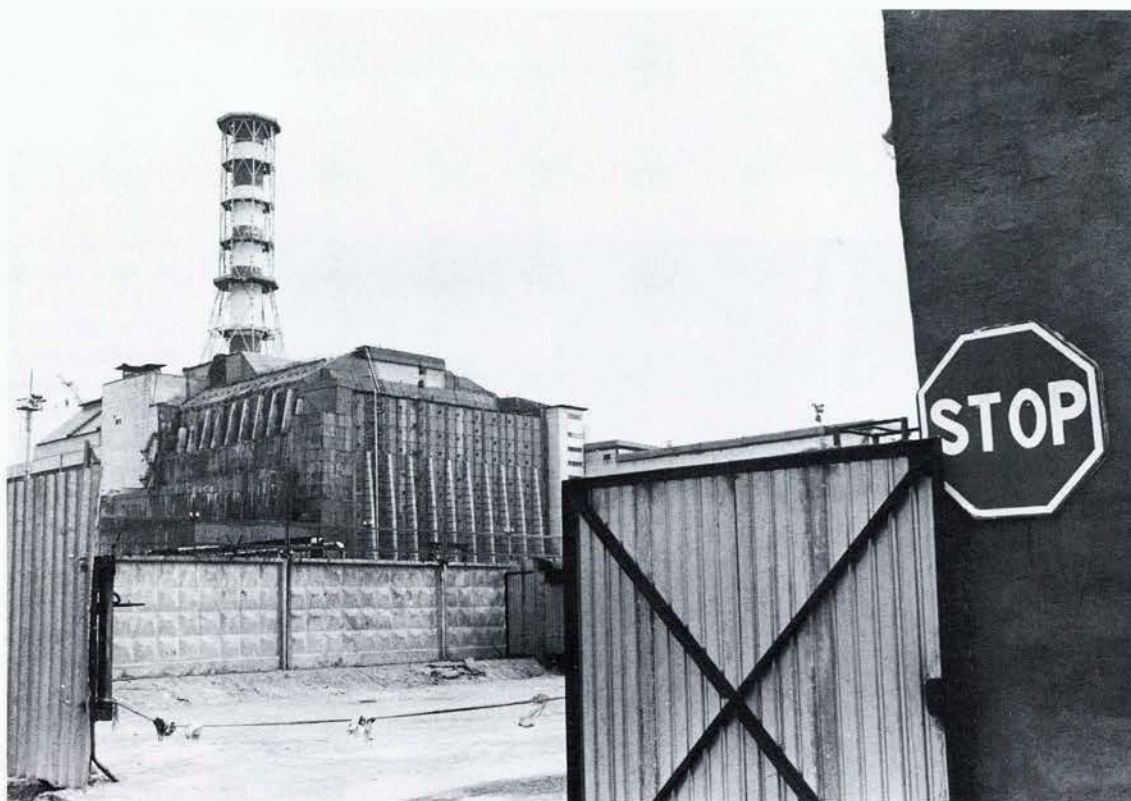


Its purpose is to 'tether' researchers and engineers working in sensitive areas like nuclear and chemical weapons. In autumn 1993, the project had still not been approved by the Russian Parliament, and so it is not yet really off the ground.

The total amount set aside by OECD governments for bilateral and multilateral co-operation with Russia (nuclear safety excluded) is \$300-400 million, of which very nearly half is provided by the United States.

In truth, quite a large portion of this amount will never be spent, for lack of suitable partners in Russia. Another part of it will be used in the OECD countries themselves to host Russian researchers or finance joint research projects. The result is that no more than a quarter of the amount is being spent in Russia.

In addition to such official funding, a good deal of aid is promised by national and international learned associations (in astronomy, mathematics, and so on) and private foundations. The most diligent has been the International Science Foundation, created by the financier George Soros; it plans to spend \$100 million over three years and has already aided several tens of thousands of Russian researchers with its individual grants (\$500). Lastly, one should mention the private firms which have 'gone shopping' in Russian R&D institutes and occasionally picked up outstanding



*The risk of a techno-industrial incident of the Chernobyl kind is not negligible.*

talents, especially in establishments working for the military. In 1993, private-sector R&D spending in Russia probably topped \$100 million.<sup>6</sup>

In overall terms, funding from abroad may today be estimated at 10% of total R&D expenditure in Russia (military included). This is a large figure, higher than in most OECD countries. Yet there is much disgruntlement, both in Russia and outside it. Foreigners complain of the fearsome difficulty they have in transferring funds, owing to the shortage of proper bank facilities, to bureaucratic red-tape and, more than anything else, to a 60% tax levied on incoming capital. So many barriers can only encourage the illegal importing of money and favour corruption. The Russian authorities for their part are unhappy that most of the co-operative arrangements are concluded directly with the scientists and do not, as they formerly did, transit through the central co-ordinating apparatus (Ministries, Academies and so on). They are also convinced that the financial inflow from outside countries amounts to tens and not hundreds of millions of dollars (perhaps because a large proportion of the money is paid straight to the interested parties in circumstances that are not entirely transparent).

Big changes have also occurred in technology transfers. CoCom regulations used to discourage transfers, subjecting them to heavy controls. The rules were eased first for the countries of central Europe and have now been relaxed for Russia itself to the point where most obstacles have been lifted. Industrial co-operation with Russia raises unusual problems for the equilibrium of a number of world markets owing to Russia's propensity for dumping.<sup>7</sup> Yet the Russians depend on foreign participation to develop the sectors in question. It is the case with space, but also with non-ferrous metals and certain energy products. What is required is a system of 'co-operative balances' that can satisfy the demands of partners on both sides and, more generally, serve their common interests.

### What Does the Future Hold?

Given the background of economic, political and geostrategic uncertainty besetting Russia today, forecasts on the future of Russian science and technology are not easy to make, the more so in that everything depends on financial, institutional, legal and other 'frame-

6. The figures come from a survey carried out especially for the Evaluation Report in the main OECD countries: *International Co-operation in Science and Technology with the Federation of Russia: Experiences and Programmes of Selected OECD Countries*, OECD Publications, Paris, forthcoming 1994.

7. The inclination towards dumping may be partly explained by the Russians' ignorance of their true production costs, there being no appropriate accounting machinery in a planned economy system.



Fotochronika TASS



Space – one of the activities where Russian technology had its most marked success.

work conditions' that are not likely to exist until the reigning doubts and difficulties have been cleared up. An attempt may nonetheless be made to sketch in the most likely forecasts.

First, in the medium run – in three to five years – the R&D system will shrink considerably (possibly by half in terms of personnel) compared to its size in the late 1980s. It was then far too large. While its cost to the country will never be known, the former system would clearly be out of key with the real capacity of the economy once it forms part of the world market and has to start obeying normal cost/price rules.

Second, for a long time to come, the R&D system will continue to be largely dependent on government funds, just as the proportion of R&D performed in the public and academic sectors will continue to be substantial. The present outlook for setting up industrial research within industry itself is dim, and will remain so until the legal and financial structures enabling production methods

to fit in with principles of the market economy are in operation.

Third, S&T will probably remain a fairly low priority for the Russian people and government. The military will go on playing a pivotal role; they will hence be a major employer in both research and industry. The regions will almost certainly be asked to play a bigger part in funding research and innovation and in framing institutional and legal rules.

Lastly, the system will go on becoming more internationalised since foreign money is vital to its survival. Foreign involvement will, by its very existence, provide standards of comparison of use to the players on the Russian scene.

■ ■

The long-term outlook is not necessarily bleak. In the short and medium term, adjustment is likely to be arduous. Nor can serious 'accidents' with world-wide consequences be ruled out. The chance of a techno-industrial incident of the

Chernobyl kind is not negligible. There is also the possibility that 'sensitive' technology might fall into the hands of unfriendly powers or organised crime. Specialists consider that bacteriological weapons present the biggest danger of proliferation.

On the other hand, the opening-up of Russian science and its acceptance into the international community will almost certainly benefit the planet in many ways. That science is, after all, the product of seventy years' colossal investment in scientific and technological exploration by a superpower which has shaped the history of the world. ■



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(41 93 15 3) ISBN 92-64-03899-X, 364pp.  
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#### **EXTERNAL DEBT STATISTICS** **Annual Report**

**The Debt and Other External Liabilities of Developing, Central and Eastern European and Certain Other Countries and Territories at end-December 1992 and end-December 1991**  
November 1993

This annual report provides detailed information on the amount and composition of the external debt of each of 151 countries and territories (in effect, worldwide coverage of non-OECD countries) at the end of 1992, with corresponding revised figures for the previous year. In addition, estimates are provided of the amortisation payments due by each country on long-term debt in 1993. These data are reported to OECD by member countries' governments and credit institutions, and the main international organisations. As a result of the use of common reporting rules and timely reporting, this volume gives a comprehensive, consistent and up-to-date account of external debt, making it invaluable for international comparisons and country risk analysis.

**Special feature:** this publication also includes a table on claims arising from export credits extended to the individual New Independent States of the former Soviet Union and the Republics of the former Yugoslavia after they emerged as separate political entities.

(43 93 05 1) ISBN 92-64-14001-8, 31pp.  
France: FF95  
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## Education

#### **EDUCATION AT A GLANCE: OECD INDICATORS**

November 1993, bilingual

This second publication of *Education at a Glance* (first published in 1992) covers the 1990/91 school year and includes a set of 38 indicators. These make it possible to examine different aspects of education policy; the volume of investment that is supported; how the education system is financed and staffed; where important decisions are taken; what level of participation is reached; how student differentiation operates; what results are achieved in key subjects; and student graduation rates.



These indicators also help identify the levels and types of education that lower the risk of unemployment, one of the major problems now affecting the OECD countries.

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##### Proceedings of a Technical Workshop, Cadarache, France, 11-13 May 1993

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The near-field of a high-level nuclear waste repository consists principally of the waste itself and of the man-made barriers engineered around it. Over time, its behaviour determines the amount of potentially harmful substances that can be released to the geological barrier and it is therefore important for long-term safety. This technical workshop addressed the issue of modelling near-field performance. The discussion focused on the conceptual and mathematical models for source-term calculations and reviewed the state of the art in the field. These proceedings include the conclusions of the workshop and an updated version of a discussion document prepared by consultants.

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### *Series: Nuclear Energy and Information*

#### PUBLIC PARTICIPATION IN NUCLEAR DECISION-MAKING Proceedings of the International Workshop, 4-6 March 1992

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However, the successful application of this principle, in particular with regard to the siting and operation of nuclear installations, requires that certain conditions be met in order to ensure meaningful participation of the public concerned.

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December 1993

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December 1993, bilingual

Recent restructuring or retirement of several suppliers in the nuclear field has made qualified equipment more scarce. Not only is equipment scarcity raising concerns, but the potential shortage of qualified manpower and loss of know-how are also generating worry.

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See Nicholas Zarimpas, 'Qualified Manpower for the Nuclear Industry', *The OECD Observer*, No. 181, April/May 1993.

(66 93 16 3) ISBN 92-64-03973-2, 267pp.

France: FF260

Other countries: FF325 US\$56 DM97

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November 1993

This report is part of the new OECD Environmental Performance Review Programme which conducts peer reviews of environmental conditions and progress in each Member country.

It scrutinises efforts to meet both domestic objectives and international commitments. Progress in reducing the pollution burden, improving natural resource management, integrating environmental and economic policies, and strengthening international co-operation are also central to these reviews. The analyses presented are supported by a broad range of economic and environmental data.



Environmental performance reviews on Germany and Iceland have already been published.

97 93 07 1) ISBN 92-64-14003-4, 108pp.  
France: FF130  
Other countries: FF170 US\$29 DM49

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This report scrutinises efforts to meet both domestic objectives and international commitments. Progress in reducing the pollution burden, improving natural resource management, integrating environmental and economic policies, and strengthening international co-operation are also central to these reviews. The analyses presented are supported by a broad range of economic and environmental data.

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See Jean-Pierre Pellegrin, 'The Hidden Sources of Employment', *The OECD Observer*, No. 185, December 1993-January 1994.

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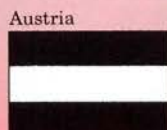
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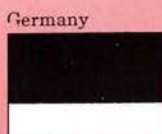
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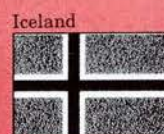
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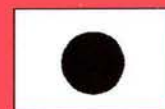
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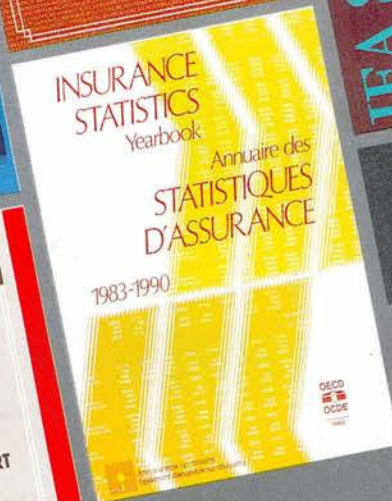
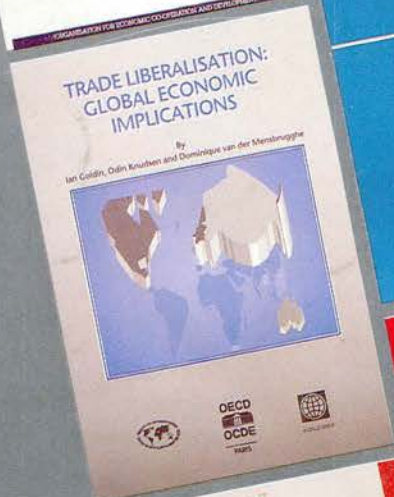
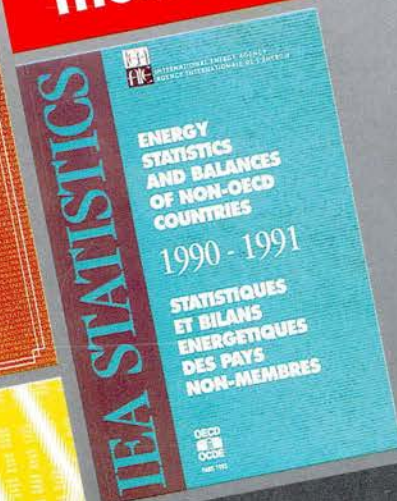
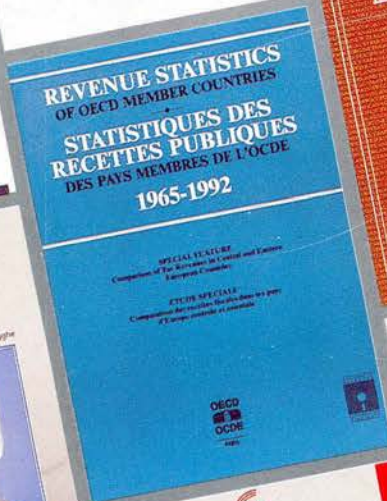
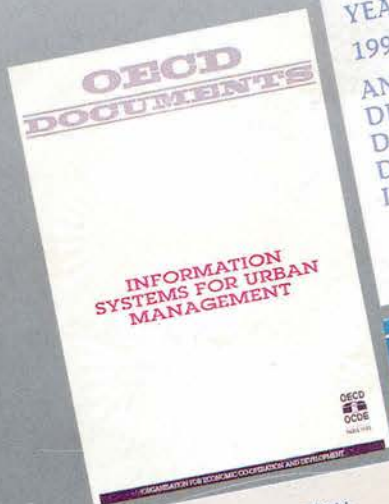
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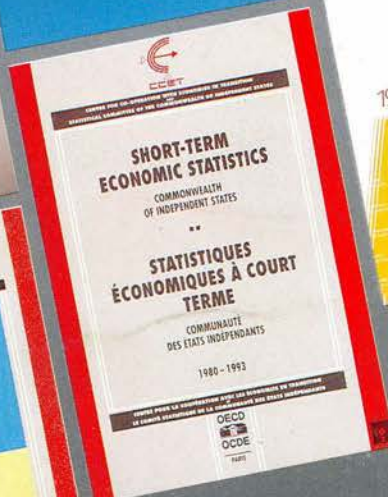


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# OECD Economic Outlook

## Highlights

An increasingly solid expansion is under way in North America, and moderate, if unspectacular, recoveries are continuing in the United Kingdom, Australia, New Zealand and some smaller European countries. For the remainder of the OECD area taken together, activity continues to be disappointingly weak, and household and business confidence are typically depressed. In most of continental Europe the recovery that was projected last spring is not yet apparent, although there are some indications that, with the possible exception of Germany, the trough has been reached. In Japan economic activity has renewed its decline.<sup>1</sup>

The forces that have underpinned recovery in the English-speaking countries, in particular significant falls in interest rates, should have an increasingly positive impact in continental Europe during 1994. In Japan, however, where the depressive effects of yen appreciation are being felt strongly and the negative effects of balance-sheet adjustment are easing slowly, recovery may be more gradual. Overall, output growth in the area may rise slowly, from about 1% in 1993 (the third year in which it has been well below potential) to perhaps just over 2% in 1994 and close to 3% in 1995 (Table 1). Global activity has been – and will continue to be – supported by buoyant growth in a number of non-OECD countries, particularly in Asia.

Inflation has fallen to low levels and is likely to come down somewhat further during the coming two years (Table 2). By 1995, it is projected to be 3% or less in 20 OECD countries, an inflation performance throughout the area which compares favourably with that of the early 1960s, often remembered as a period of reasonable price stability. The emerging very favourable price situation, if sustained, will help to establish an economic environment more conducive to sustainable increases in productive investment, output, and employment than has existed since the early 1960s.

Unemployment is high and, during the recent downturn, it has increased in most countries, especially in continental Europe (Table 3). Unemployment is likely to fall somewhat in North America, but it could approach 35 million people in the OECD area as a whole during 1994 and may fall only marginally thereafter. This has put policy-makers under considerable political pressure to act on jobs. The challenge they face is to find policy responses that yield results quickly but that also promise durable gains.

### Macro-economic Policy Requirements

The background to the setting of fiscal policy in the current situation is the need to contain and reverse the steady build-up of public debt in most countries, which has severely circum-

scribed the scope for any fiscal support to activity. Between 1979 and 1992 average OECD gross public debt rose from 41% of GDP to around 63%. In the face of recession, the issues facing policy-makers have been: whether plans for fiscal consolidation should be temporarily deferred; the extent to which a cyclical widening of the budget deficit (sometimes described as the working of the 'automatic stabilisers') should be accepted; and the risk that such actions would weaken confidence and thereby lead to increases in long-term interest rates or pressure on exchange rates. In a slightly longer-term context, however, the need for fiscal consolidation does not necessarily preclude increased expenditure on projects assessed to have a high rate of return. Between 1979 and 1992, transfers increased by 3½ to 4% of GDP on average in OECD countries and interest payments by 2½ to 3% of GDP.<sup>2</sup> Reversal of these trends would help to provide scope to both reduce deficits and shift expenditure to more fruitful uses.

In practice, countries have reacted differently to the tendency for deficits to widen during the downturn. Many have allowed automatic stabilisers to work as far as has been consistent with maintaining some degree of control over the increase in public debt. Some have gone further and taken modest expansionary measures. And Japan has taken significant expansionary action. But now OECD countries have largely exhausted the scope for allowing public deficits to widen. Indeed, in a number of countries where priority was given to fiscal consolidation in the face of rising public debt, policy-makers have reaped the reward of a fall in long-term interest rates. On the other hand, where discretionary fiscal measures have been taken to support demand, the effects on activity appear to have been disappointing.

With little scope for expansionary macro-economic action on the fiscal side, support for recovery in current circumstances must rely largely, if not solely, on monetary policy. Here a number of countries do have room for man-

Table 1

#### GROWTH OF REAL GDP IN THE OECD AREA

seasonally adjusted at annual rates (%)

	Share in total OECD 1991	change from previous year			
		1992	1993	1994	1995
United States	37.68	2.6	2.8	3.1	2.7
Japan	15.47	1.3	-0.5	0.5	2.3
Germany	8.80	2.1	-1.5	0.8	2.2
France	6.82	1.4	-0.9	1.1	2.7
Italy	6.42	0.9	-0.1	1.7	2.3
United Kingdom	5.94	-0.6	2.0	2.9	2.9
Canada	3.46	0.7	2.5	3.7	4.1
Total of above 7 countries	84.58	1.8	1.2	2.1	2.6
Austria	0.89	1.5	-0.5	1.0	2.3
Belgium	1.16	0.8	-1.2	0.9	2.0
Denmark	0.60	1.0	0.2	2.5	2.8
Finland	0.51	-4.0	-2.0	-0.3	2.4
Greece	0.52	0.9	0.5	0.9	2.1
Iceland	0.03	-3.7	0.4	-2.0	1.1
Ireland	0.27	4.9	2.7	3.1	3.2
Luxembourg	0.05	1.8	1.0	1.5	2.3
Netherlands	1.64	1.4	-0.2	0.6	2.2
Norway	0.47	3.3	1.6	3.2	3.8
Portugal	0.59	1.6	-0.4	2.0	3.1
Spain	3.27	0.8	-1.0	0.8	2.6
Sweden	0.95	-1.7	-2.7	1.5	2.2
Switzerland	0.98	-0.1	-0.8	0.8	2.0
Turkey <sup>1</sup>	1.33	5.9	7.0	5.0	4.7
Total of above 15 countries	13.27	1.2	0.1	1.5	2.7
Australia	1.84	2.0	2.5	3.1	3.4
New Zealand	0.31	0.5	3.0	3.3	3.1
Total of above 17 countries	15.42	1.3	0.4	1.7	2.8
Total OECD	100.00	1.7	1.1	2.1	2.7
OECD Europe		1.1	-0.2	1.5	2.6
EC		1.1	-0.3	1.4	2.5
Total OECD less the United States		1.2	0	1.4	2.6

1. GNP.

œuvre, although there may be a question of how most effectively to exploit this room, in terms of the size and timing of cuts in officially controlled interest rates. While the specific requirements of monetary policy differ across countries, there are nevertheless some common threads. One is the need for monetary policy, in supporting activity, not to compromise the control of inflation over the medium term. A second is the importance of financial market expectations in the determination of long-term interest rates, which have significant consequences on business investment, output and employment over the longer

1. OECD Economic Outlook, No. 54, OECD Publications, Paris, December 1993.

2. OECD Economic Outlook, No. 52, OECD Publications, Paris, December 1992.



Table 2

**PRIVATE CONSUMPTION DEFLATORS IN THE OECD AREA**

seasonally adjusted at annual rates (%)

	change from previous year			
	1992	1993	1994	1995
United States	3.3	2.7	2.7	3.0
Japan	2.0	0.9	0.3	0.4
Germany	4.7	4.1	3.2	1.9
France	2.4	2.3	1.9	1.5
Italy	5.4	4.5	4.1	3.0
United Kingdom	5.0	3.5	3.4	3.3
Canada	1.1	1.7	1.9	1.8
<i>Total of above 7 countries</i>	3.4	2.6	2.4	2.3
Austria	4.2	3.7	2.8	2.5
Belgium	2.4	2.7	2.4	2.1
Denmark	1.9	1.1	2.5	2.3
Finland	3.9	3.0	2.0	2.0
Greece	14.6	14.1	10.8	8.5
Iceland <sup>1</sup>	4.9	4.1	2.4	1.5
Ireland	2.6	2.2	3.5	3.6
Luxembourg	2.8	3.5	3.0	2.5
Netherlands	3.0	2.0	2.2	2.0
Norway	2.6	2.3	1.9	2.2
Portugal	9.4	6.3	5.3	4.8
Spain	6.5	4.8	4.1	2.9
Sweden	2.5	5.2	3.5	3.0
Switzerland	4.1	3.3	1.8	2.0
Turkey	70.0	71.0	75.0	70.0
<i>Total of above 15 countries</i>	11.3	10.8	10.5	9.5
Australia	1.7	2.1	3.1	2.7
New Zealand	1.0	1.4	1.5	1.7
<i>Total of above 17 countries</i>	10.0	9.5	9.5	8.6
Total OECD	4.4	3.7	3.5	3.2
OECD Europe	6.6	5.9	5.5	4.7
EC	4.6	3.8	3.3	2.5
<i>Total OECD less United States</i>	5.0	4.3	3.9	3.4

1. Consumer price index.

run. Market expectations in turn are heavily influenced by the credibility of policy. It is only if policy is credible and consistent across countries that governments are in a position to support activity without deleterious consequences for interest rates and exchange rates.

## Policy Priorities in Major Countries

The strengthening recovery in the United States suggests that this is one major country where additional support to activity is not an immediate concern. A necessary tightening of fiscal policy has been embodied in the Administration's medium-term deficit-reduction package. And this welcome step towards eliminating the budget deficit has contributed to the significant

decline in long-term interest rates through much of the last year. Given prospects for demand growth, concerns on the fiscal side are now related more to the contribution of the public-sector financial position to increasing national saving and investment over the longer term. Further measures to reduce the structural deficit, beyond those in the medium-term deficit-reduction package, will be needed over the coming years. Success will depend importantly on achieving a satisfactory reform of the health care system that does not weigh on budget deficits. Should the economy recover somewhat more rapidly than projected, it will be important that the resulting improvement in the deficit be recognised as cyclical and not taken as a substitute for further fiscal consolidation. (This consideration also applies to, *inter alia*, Italy, the United Kingdom and Canada.)

On the monetary side, the stance of policy in the United States, which has appropriately remained expansionary for the past few years, will have to be adjusted at some stage so as to lock in low inflation and ensure satisfactory growth over the medium term. This adjustment will need to take due account of the projected narrowing of slack in the economy and of the long lags with which monetary policy affects the economy.

Japan stands in strong contrast. It is uncertain how far the main forces behind the current recession there – adjustment to sharp falls in asset prices and the appreciation of the yen – are still depressing activity. It is therefore necessary to re-assess whether the easing to date – the three fiscal packages over the last eighteen months and the reduction in the official discount rate to the historical low of 1.75% – is sufficient to ensure a recovery. On the monetary side, although both money-market rates and long-term yields on government securities have come down to levels that are very low in nominal terms, a number of indicators suggest that monetary conditions are tighter than the levels of nominal interest rates might imply. Because the scope for further declines in interest rates is limited by their already being very low, effective monetary easing may require action which facilitates more balanced behaviour toward risk taking by banks in their lending activities.

On the fiscal side, some indicators suggest Japan may be the only major OECD country

in a position to envisage significant fiscal expansion. However, the relatively high level of gross debt, future demands on public finances and the impact of the three packages already adopted on underlying budget positions restrict the scope for such action. Furthermore, the limited results of action taken so far raise questions about its effectiveness. This suggests that any expansionary fiscal-policy moves, if undertaken, should be temporary and designed so as to achieve other ends that are desirable in their own right. In this regard, a direct tax reduction now, fully offset in due course by a phased introduction of indirect tax increases as the economy recovers, would provide positive short-run support for the economy while having the durable effect of improving the structure of government revenues. Furthermore, comprehensive structural reforms going further than those contained in the recent package could also have some favourable impact on activity.

In Europe, the budgetary position of nearly all countries has deteriorated significantly in recent years and gives virtually no room for any fiscal stimulus. For most countries the central issue to be addressed is how rapidly to consolidate budget positions despite direct negative demand effects. Many (including Germany, France, Italy, and the United Kingdom) have already taken, or have indicated their intention to take, action which promises to improve underlying, or structural, budget positions over the next two years. Provided these actions are implemented as planned, significant fiscal consolidation should become apparent over the medium term as cyclical conditions improve. However, in some (including Italy, Belgium and Greece), where public indebtedness is particularly high and budget deficits are large, there is a strong case for taking further measures in order to move more rapidly. The risks in these countries of not doing so in terms of future tax burdens and loss of financial market confidence very likely outweigh the risks to activity of taking decisive action in cyclically weak conditions.

A central question in continental Europe is whether, or how, the negative direct demand effects of fiscal consolidation can be more than offset by cuts in officially controlled interest rates as well as declines in market rates induced by fiscal consolidation. Unlike other OECD regions, officially controlled interest rates in continental Europe have until recently been rather high. These high interest rates were necessary to deal with inflation pressures in Germany following unification, but they were not always appropriate to domestic conditions in countries whose exchange rates were linked, whether officially or *de facto*, to the Deutschmark or the ecu. This tension was at the root of the turmoil in European currency markets which led ultimately to the adoption of 15% fluctuation bands by most of the remaining participants in the European Exchange Rate



Mechanism (ERM) in August. While both short- and long-term interest rates in Germany have come down since September 1992, in many countries short-term rates are still high relative to inflation, and inverted yield curves indicate that monetary conditions remain relatively tight. Continued economic weakness and declining inflation make further cuts in short-term rates likely. The main question is how rapidly this should happen.

In Germany, given the fiscal deterioration that has occurred since unification, the stubbornness of inflation pressures, and the overriding need to ensure that confidence in the Deutschmark is maintained, the Bundesbank has so far proceeded cautiously in allowing money-market conditions to ease. The continuing inverse yield curve and a low absolute level of long-term interest rates appear to reflect the favourable prospects for a decline in overall inflation as well as weak economic activity. Those indicators appear to suggest that the monetary authorities can continue to follow the announced strategy of relaxing monetary conditions steadily without undermining the credibility of their policy.

In Germany's ERM partners, where activity is weak and inflation is low, further interest-rate reductions will be required to underpin recovery. In spite of the scope for flexibility provided by wider fluctuation bands, these countries have so far been cautious about bringing money-market rates below those in Germany in order to limit further movements of exchange rates away from central parities. The case for proceeding in this way rests on the important contribution it makes to sustaining the credibility of commitments both to continued non-inflation policies as well as to the Maastricht process for achieving monetary union. However, if German inflation remains unsatisfactorily brisk and German interest rates continue to decline only slowly, these countries will face an increasingly difficult situation. The extent to which monetary autonomy can be achieved, and interest rates – particularly at the longer end of the market – can be reduced below German levels without disruptive exchange rate movements will depend at least in part on the credibility of anti-inflation policy by most of the remaining in Germany's partner countries.

In countries which suspended their participation in the ERM or cut informal links with the Deutschmark or the ecu in 1992, interest rates were lowered and currencies have depreciated, in most cases significantly. Many of these countries had been suffering from severe balance-sheet adjustment problems following the asset price cycle of the late 1980s and early 1990s or, in Italy, from a major fiscal problem in which debt servicing played a large role. Lower interest rates contributed to easing the stresses which various sectors faced in these countries, while competitive exchange rates led to strong export demand. In most of these countries (with

the exception of Finland, where the balance-sheet adjustment problem has been particularly severe) moderate recoveries are either already apparent or in prospect. Most of these countries would benefit from further lowering of interest rates, in particular in the context of widespread falls in European interest rates which would not generate downward pressure on exchange rates within Europe and upward pressure on inflation.

## Structural Reform

For the past decade or more, OECD governments – and indeed many others outside the OECD area – have sought to pursue economic reforms based on the proposition that open and efficient markets for goods and services, exposed to domestic and international competition, provide the crucial underpinnings for dynamic, high-income economies. The agenda for reform that emerges from this proposition is a many-faceted one, ranging over such areas as freeing-up international trade in goods and services as well as capital flows; introducing competition into previously sheltered sectors – not least those dominated directly by governments; making labour markets more responsive and flexible in the face of changing technologies and trade patterns; liberalising financial markets, both domestically and internationally; reducing distortions to incentives to work, save and invest by broadening tax bases while reducing marginal rates; improving the efficiency of government itself; and developing effective means for integrating environmental concerns into economic decision-making in both the public and the private sectors.

A review of government actions over the past three years in relation to this reform agenda, lessons from this experience, and priorities for the future will be published by the OECD early

Table 3

### UNEMPLOYMENT IN THE OECD AREA<sup>1</sup>

	thousands	% of labour force			
	1991	1992	1993	1994	1995
United States	8,446	7.4	6.9	6.5	6.2
Japan	1,366	2.2	2.5	2.9	2.8
Germany	2,602	7.7	8.9	10.1	10.3
France	2,362	10.4	11.7	12.4	12.3
Italy <sup>2</sup>	2,654	11.6	10.2	11.1	11.6
United Kingdom	2,346	10.0	10.3	10.0	9.5
Canada	1,417	11.3	11.2	11.0	10.5
Total of above 7 countries	21,192	7.3	7.3	7.5	7.3
Austria	125	3.6	4.8	5.3	5.3
Belgium	391	10.3	12.1	13.0	13.2
Denmark	296	11.1	12.1	11.9	11.3
Finland	193	13.1	18.2	19.9	20.3
Greece	301	9.2	10.0	10.7	11.2
Iceland	2	3.0	4.4	5.1	5.1
Ireland	209	16.7	17.6	17.8	17.8
Luxembourg	2	1.4	2.2	2.7	2.8
Netherlands	493	6.8	8.3	9.3	9.7
Norway	117	5.9	6.0	5.9	5.7
Portugal	198	4.2	5.1	6.0	6.1
Spain	2,464	18.4	22.7	23.8	23.5
Sweden	122	5.3	8.2	8.8	8.4
Switzerland	40	2.5	4.5	5.0	4.5
Turkey <sup>3</sup>	1,547	7.9	8.6	9.5	10.7
Total of above 15 countries <sup>3</sup>	6,499	9.6	11.5	12.4	12.6
Australia	817	10.7	10.9	10.4	10.1
New Zealand	167	10.3	9.8	9.3	9.0
Total of above 17 countries <sup>3</sup>	7,482	9.7	11.4	12.1	12.3
Total OECD <sup>3</sup>	28,674	7.8	8.2	8.5	8.4
OECD Europe <sup>3</sup>	16,462	9.6	10.7	11.4	11.5
EC	14,316	10.3	11.3	12.0	12.0
Total OECD less the United States <sup>3</sup>	20,228	8.0	8.8	9.3	9.4

1. Commonly used definition.

2. After 1992, data are based on new definitions and are therefore not comparable with earlier figures.

3. The figures incorporate important revisions to Turkish data.

in 1994.<sup>3</sup> The assessment is mixed. Constructive reforms have been undertaken in most countries in many of the areas listed above, though in most cases much remains to be done. The review identifies trade policy as an area of particular concern: there have been signs of vacillation on carrying through with global trade liberalisation; unilateral protectionist measures have become more prevalent; and there has been a drift towards 'managed trade'; forward momentum has occurred primarily in the extension of regional trading

3. **Assessing Structural Reform: Lessons for the Future**, OECD Publications, Paris, forthcoming.



arrangements to include a larger number of countries and more aspects of activity.

Structural reforms bring benefits, but also entail costs. There is much scope for further work to assess costs and benefits in terms of the direct effects in the sectors concerned, but especially in terms of broader impacts on longer-term social and economic evolution. Even so, there is empirical evidence across a range of areas that the benefits substantially exceed the costs. The economic gains from trade liberalisation, for instance, are substantial and well documented. Many studies also identify large potential economic gains from privatisation and/or reform of regulation in a range of services presently provided by the public sector. Countries with less regulated, more flexible labour-markets not only experience higher rates of employment growth but also face substantially smaller problems of long-term unemployment. Liberalised financial markets yield important benefits to savers and investors by allowing for increasingly tailor-made management of risk. Finally, significant cost-savings can be achieved by shifting from direct regulation to the use of economic instruments in the achievement of environmental goals.

Perhaps even more tellingly, in many cases the failure to correct inappropriate policies can create growing problems as economic agents adjust to the perverse incentives generated by them. In the end, these policies become unsustainable, but the costs of correcting the situation will in the meantime have risen substantially. This has been evident in the case of delayed financial reform in some countries. It is also clear in the case of agricultural-support policies, whose costs continue to rise. Likewise the evidence is that protectionist policies cannot, in the long run, prevent adjustments in employment and production patterns that are driven by increasing international integration. In the meantime, they increase the eventual costs of making these adjustments.

In spite of the gains that structural reform can generate, it has in many cases proved difficult to implement. In part this reflects the fact that reforms require political support, which is often lacking for two reasons in particular:

- the gains from structural reform tend to be widely distributed among consumers and taxpayers in the country as a whole; at the same time the losers may be a relatively small group but in a position to complain loudly at reforms which undermine their vested interests
- reaping the benefits of reform can take time while the costs are borne straight away; this increases the need to deal with the legitimate

Table 4

## CURRENT BALANCES IN THE OECD AREA

% of GDP

	1992	1993	1994	1995
United States	-1.1	-1.7	-2.0	-2.1
Japan	3.2	3.3	3.1	3.0
Germany	-1.3	-1.1	-0.8	-0.7
France	0.3	0.8	1.1	1.4
Italy	-2.2	0.4	1.0	1.4
United Kingdom	-1.4	-1.8	-1.9	-1.5
Canada	-4.0	-3.6	-3.1	-2.7
Total of above 7 countries	-0.2	-0.1	-0.1	-0.1
Austria	-0.2	0.1	0.1	0.2
Belgium-Luxembourg	2.4	2.1	1.8	2.0
Denmark	3.3	2.6	1.8	1.4
Finland	-4.9	-1.5	2.7	5.5
Greece	-2.8	-1.9	-2.0	-2.0
Iceland	-3.2	-1.5	-1.0	-0.8
Ireland	5.2	5.6	5.9	6.1
Netherlands	2.1	2.0	2.7	3.1
Norway	2.5	3.1	3.9	5.2
Portugal	-0.2	-0.5	-0.2	0.1
Spain	-3.3	-2.3	-2.0	-2.0
Sweden	-2.1	-0.2	1.3	2.7
Switzerland	6.2	7.8	7.9	8.1
Turkey <sup>1</sup>	-0.8	-5.2	-4.8	-3.5
Total of above 15 countries	0.2	0.8	1.2	1.6
Australia	-3.7	-4.2	-4.4	-4.4
New Zealand	-1.9	-1.7	-1.5	-0.4
Total of above 17 countries	-0.3	0.2	0.6	0.9
Total OECD	-0.2	0.0	-0.1	0.0
OECD Europe	-0.7	-0.1	0.2	0.6
EC	-0.9	-0.3	0.0	0.2
Total OECD less the United States	0.2	0.8	1.0	1.1

1. % of GDP.

concerns about transition hardships of those affected.

These difficulties do not call into question the need for continued reform, but rather highlight the importance of overcoming resistance to it by effective leadership and management of the reform process. The experience of recent years suggests a number of lessons in this respect, beyond those identified above:

- failure to take account of incentive effects can lead to large costs over time as economic agents adapt to the perverse incentive effects of inappropriate policies
- changed circumstances can turn reasonable policies into very costly ones – for example, energy price controls after the large oil shocks; or agricultural-support policies in the

face of sharp increases in agricultural productivity

- the appropriate nature and scope of government intervention can be changed or reduced over time as a result of technological progress that diminishes the extent of natural monopoly
- the service sector, which has traditionally been sheltered from international competition and has often been heavily regulated, will increasingly be a focus for future reform
- binding budget constraints often can play a major role in advancing structural reform.

Looking ahead, the following reform issues would seem to deserve the highest priority:

- erosion of the open multilateral trading system needs to be reversed, and drift into managed trade avoided; a new impetus towards liberalisation, transparency and fairness is urgently required
- a few tentative steps towards reforming agricultural policies in a more market-oriented direction have been taken; but there is much more to do.
- labour-market reforms – generally involving actions on a number of fronts, and in ways that reflect each country's situation – are necessary if high rates of unemployment are to be brought down; macro-economic policies that promote economic recovery will help, but the largest part of most countries' unemployment problems are structural in nature and require structural remedies
- reforms directed at bringing more competition to bear in sectors that have previously been largely sheltered need to be carried through; marketisation within the public sector, privatisation, deregulation and/or redefinition of regulatory regimes are all approaches that can yield substantial efficiency gains and take advantage of rapidly expanding technological possibilities in many of these sectors
- substantial reforms in health and welfare systems are needed in a number of countries in order to cope with exploding budget costs in these areas, to improve service delivery and to help deal with inappropriate incentives that affect other areas of the economy
- as regards environmental protection, there is a strong case for making more use of economic instruments rather than regulation.

This list is not exhaustive; depending to some extent on the country, other areas – including tax policy and financial market reform – remain areas where further reform efforts can be expected to yield important benefits.