



Business and Industry Advisory Committee to the **OECD**

Comité Consultatif Economique et Industriel Auprès de l' **OCDE**

BIAC Statement to the OECD Council Meeting at Ministerial Level

Paris, 3 May 2005

- I. Investment Challenges in the Energy Sector**

- II. Meeting the Challenges of Globalisation and
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BIAC STATEMENT TO THE OECD COUNCIL MEETING AT MINISTERIAL LEVEL

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EXECUTIVE SUMMARY

I. Investment Challenges in the Energy Sector

Energy is an essential motor of growth and development for an ever increasing world population. Social and economic development can be attained only if a secure, reliable and affordable supply of energy is ensured. Achieving development goals in the poorest countries will require greater access to energy and improved energy services as a means to provide education, health, clean water and other societal needs.

In its 2003 World Energy Investment Outlook, the International Energy Agency (IEA) estimated that the total investment requirement for energy supply infrastructure worldwide over the period of 2001-2030 is \$16 trillion. Mobilising the required investment will be a challenge for the coming decades and underlines the importance of a competitive energy sector that can attract the much-needed investment. Financing energy investment cannot be taken for granted, and the key question will be whether conditions in the energy sector are right to attract the necessary investment with adequate incentives for investors.

Taking into account long-term investment cycles

Investment in energy projects is a long-term proposition and in that context, investors face considerable risks and challenges, which vary by region and the stage of the energy chain. Overall, investment conditions must be appealing and returns high enough if they are to trigger the necessary investment. Energy investment requires a long-term view. Many options involve considerable time and expense to alter energy and raw material inputs and to develop and introduce technological changes. Business therefore encourages policy makers to commit themselves to a consistent policy framework taking into account long-term investment cycles.

Keeping all energy options open

Long-term energy security calls for the utilisation of a variety of energy sources. National circumstances will best determine the mix of fuels which is necessary for energy security and sustainable growth in a given country. BIAC encourages governments to keep all energy options open, to avoid trying to choose “winners” and “losers” among technologies and to consider investment requirements for a range of options in the energy mix. The diversification of energy supplies and distribution, both by energy type and by source, is an important measure to help improve energy security.

A competitive, free and open market

The macro-economic environment is a key driver of energy demand and energy investment. Economic prosperity and efficiency depend upon free and open markets as well as predictable and transparent regulatory frameworks that reduce competitive distortions. Governments play a major role in ensuring that adequate financing for energy infrastructure can be mobilised in a timely fashion, notably by establishing enabling policy frameworks for the energy sector. Free and open markets operating within a clear, stable and well-designed legal, fiscal and regulatory framework are the foundation to avoid market distortion. Market-

based prices, market solutions, cost-benefit analysis and a non-discriminatory and consistent legal enforcement are all attributes of these frameworks.

Improving public governance

Energy investors often face high risks of political uncertainties in a number of developing countries. In addition to free and open markets, other factors such as political and legal stability, transparency of regulation and rule of law, as well as the elimination of bribery, corruption and bribe solicitation emerge as crucial issues for the investment environment. Political stability promotes consistent policy frameworks to improve public governance, which in turn affects the planning basis for business development, investment decisions and cost-recovery in the longer term. This highlights the importance of increasingly involving non-member countries in discussions on energy investment and cooperation, and we encourage both OECD and IEA to reinforce their successful outreach work in this respect.

II. Meeting the Challenges of Globalisation and Structural Adjustment

For developed and developing countries alike, implementing policy frameworks that provide for successful and fruitful structural adjustment are key to competitiveness, job creation, and sustainable economic growth. Across sectors and across policy areas, comprehensive integrated policy approaches are needed to ensure that as we go forward, our globalised economy is a growing economy – the necessary basis for investment, trade and development, raising standards of living and eliminating poverty.

Business recognises the challenges for individual employees, companies, even for entire sectors brought on by the opportunities afforded by open markets. In this context, BIAC welcomes the completion of the OECD Project on Trade and Structural Adjustment as well as its complementary project on enhancing services sector performance. OECD fact-based analysis in general and through projects underway such as the reassessment of the OECD Jobs Strategy and OECD recommendations on regulatory quality and reform are critical in addressing misperceptions related to globalisation and pre-empting protectionist policies.

In our Statement to the 2005 OECD Council Ministerial, BIAC identifies the following policy priorities that enable business to positively respond to necessary structural adjustment:

Enabling Policy Framework Conditions for Sustainable Growth

Good public governance, appropriate macro-economic policies and regulatory frameworks that promote competition and innovation are essential to stimulate entrepreneurial activity, economic growth and job creation in all economies. Trade and investment liberalisation complement good macroeconomic policies. They are instrumental in fostering competition and economic growth through a more effective international division of labour. With the appropriate enabling frameworks, liberal trade and investment regimes help in facilitating and accelerating countries' adjustment processes. The WTO Doha Round offers an excellent opportunity for further trade liberalization. BIAC urges OECD countries to stay committed to negotiating meaningful results.

Stimulation of Entrepreneurship and Innovation

Entrepreneurship and innovation are key to creating more jobs, and are at the heart of business creation and transformation in today's global economy. The following general

conditions stimulate and maximise entrepreneurial and innovative opportunities: a regulatory and legal environment that clearly promotes open market competition and business creation; incentives to encourage skill acquisition and necessary changes in the organisation of the workforce; strengthening standards world-wide for intellectual property rights protection; closer relations between industry and academia to raise standards of excellence, ensure effective knowledge and technology transfer and achieve mutually beneficial personal exchanges and awareness; encouragement of SME and entrepreneurship development.

Linking Structural Adjustment Approaches to Labour Market and Social Policies

Removing disincentives to work is a critical element of a policy framework that provides the necessary environment for job creation. Widespread misconceptions regarding the benefits and perceived costs of trade liberalisation and investment and their impact on jobs, can lead policy makers to implement protectionist measures that are harmful to the world economy as a whole. BIAC supports the OECD view that often it is the relationship between labour market conditions and the trade regime that determines whether or not adjustment is successful. From the business perspective, this view clearly emphasises the need for labour market and social policies that provide for: flexibility to manage human resources; active and inclusive labour market and employment policies; and the reform of benefits systems.

Encouraging Investment in Human Capital Formation and the Promotion of Lifelong Learning

Education and a culture of life long learning instilled at an early age are perhaps the most effective mechanisms to improve employment prospects for all groups. They are also fundamental in aiding workers to positively respond to structural adjustment. Companies depend upon a labour pool that is flexible, technologically literate and work-ready and have a vital interest in schools turning out young people equipped to take on the ever more technologically sophisticated and knowledge-intensive jobs. In our view, Government has the primary responsibility for initial education. Employers and companies contribute by working with Government and educational institutions to provide clear goals for education and training according to the needs of the market. Employers can also provide development opportunities at the workplace as well as firm and job-specific training.

Business is a key actor in generating growth in both developed and developing countries. Trade and foreign direct investment in the context of good governance, sound macroeconomic frameworks, open competitive markets, and labour and social policies that promote job creation, are important tools for reaching this goal.

BIAC welcomes future OECD work on globalisation and structural adjustment, and stresses the value of fact-based analysis in putting forth a positive political message on the benefits afforded by the global economy.

I. Investment Challenges in the Energy Sector

1. The importance of energy for economic growth and development

Energy and economic growth

Energy is an essential motor of social and economic development for an ever-increasing world population. Growth and development can be attained only if a secure, reliable and affordable supply of energy is ensured. Energy remains a strategic commodity, and ensuring its availability remains a key objective for national security and economic growth. An important consideration is that oil and gas resources are unevenly dispersed geographically. Furthermore, according to a recent study by the International Institute for Economics (IIE), approximately 77 percent of world crude oil reserves are controlled by national oil companies. New energy supplies to meet rising demands will increasingly lead to requirements from countries with large reserves.

Overall, energy prices remain an important determinant of global economic performance. As illustrated, for example, by the International Energy Agency (IEA) analysis of the impact of high oil prices on the global economy in 2004, oil prices matter to the health of the world economy. According to a quantitative exercise carried out by the IEA in collaboration with the OECD Economics Department and with the assistance of the International Monetary Fund Research Department, a sustained \$10 per barrel increase in oil prices would result in the OECD as a whole losing 0.4% of GDP in the first and second years of higher prices.

While the vulnerability of countries varies depending on the degree to which they are net importers, high oil prices have a negative net effect on the global economy by affecting economic activity, consumer costs, corporate earnings and inflation in importing countries. This illustrates the importance of taking due account of the energy dimension in discussions on economic growth, development and investment. It also underlines the importance of giving consideration to the possible impacts of tax policies affecting energy supply and use in a global context.

Suppliers' interests for attracting investment need to be taken into account along with the needs of small and large energy consumers. While governments have a crucial role to play in setting predictable policies and adequate framework conditions for investment in the energy sector, business is indispensable in helping ensure a secure and reliable energy system for all.

Keeping all energy options open

Energy security is a broad concept, which significantly depends on the diversification of energy sources. A variety of options will be necessary to meet the needs of social and economic development. While new energy technologies may have a role to play in the future, fossil fuels, hydro and nuclear energy will remain predominant in the near to mid-term energy mixes. While new energy options can be expected at some point to affect the balance of the existing energy mix, it would not be realistic to anticipate a sudden and immediate changeover from existing major energy systems to new ones.

Long-term energy security therefore calls for the utilisation of a variety of energy sources in order to reduce exposure to sudden disruptions. National circumstances will best determine the mix of fuels – oil, gas, coal, nuclear or renewable energy – which is necessary to contribute to energy security and sustainable economic growth in a given country. BIAC encourages governments to keep all energy options open, to avoid choosing “winners” and

“losers” among technologies and to consider investment requirements for an appropriate range of options in the energy mix. The diversification of energy supplies and distribution, both by energy type and by source, is an important measure to help improve energy security.

Improving developing countries’ access to energy

Achieving development goals in the poorest countries will require greater access and improved energy services as a means to provide education, health, clean water and other societal needs. Making energy available to the almost 1.6 billion people who still lack access to electricity is a prerequisite to overcoming poverty, and presents a considerable challenge for governments and the energy industry in the approaching decades. The growing requirements of OECD non-member countries will undoubtedly create major challenges for global supply security. Current energy supplies will require commensurate development to support economic growth throughout the world.

Innovative energy technologies and major investments in energy infrastructure in developing countries are therefore of crucial importance. While governments continue to have an important role to play in fostering technology that can help address these challenges on a global level and in offering a framework of well-functioning and competitive markets, the engagement of the private sector for global dissemination of the necessary technologies is essential. The ability of energy project participants to secure local acceptance and build social trust is important to determine the extent to which new energy technology is successful in developing countries. Business is central to innovating and deploying advanced technologies that utilise energy resources more efficiently, improve product quality and enhance both environmental and end-use performance. One constructive step in this regard would be the liberalization of energy services in the WTO Doha negotiations.

Energy in a sustainable development context

The World Summit on Sustainable Development highlighted the need to dramatically increase access to affordable energy as a crucial enabling condition for achieving sustainable development. Predictable, accessible and affordable energy is not only crucial for economic activity, but it also contributes to social development and improves living standards in developing countries.

At the same time, energy can pose environmental and social challenges, including issues surrounding land use, global climate change, water and urban air quality. Actions to address climate change will have a significant impact and implications for energy policies, which in turn will have economic implications. Continuing research on climate science as well as technology to improve energy efficiency and development of energy supplies with lower levels of emissions should figure prominently in climate policy priorities. As energy demand increases around the world, it will remain essential to consider the trade-offs between the economic, social and environmental considerations to decide on the role that the various energy options should play in a country’s energy mix. Climate and energy policies should be integrated, long-term, market oriented, cost effective, and harmonious, fostering innovation and commercialisation of technologies.

Sustainable energy pathways will require broad societal consensus around integrated policies to advance economic, environmental and social development. According to their state of development, priorities, and available resource mix, countries will pursue different paths towards sustainable development. They involve different policy mixes incorporating fiscal, regulatory and research & development efforts. The best energy option will emerge when geographical borders have the least impact on reaching the most economic and sustainable solutions.

2. Investment challenges in the long-term

Investment requirements by 2030

In its 2003 World Energy Investment Outlook (WEIO), the IEA estimated that total investment requirements for energy supply infrastructure worldwide over the period 2001-2030 are \$16 trillion. This investment would be needed to expand supply capacity and replace existing and future supply facilities that will be exhausted during the projection period. This figure illustrates the magnitude of the task that lies before us, and it is BIAC's hope that it will trigger governments to adopt policies that will help encourage the necessary investment flows.

While the world's energy resources are sufficient to meet projected demand, mobilising the required investments in the neediest regions will be a challenge for the coming decades and underlines the importance of a competitive energy sector that can attract the necessary investment. Financing energy investment cannot be taken for granted, and the key question will be whether conditions in the energy sector are right to attract the necessary investment with adequate incentives for investors. OECD countries will face considerable challenges to ensure the security of supply as well as transmission and distribution reliability. However, financing the necessary investment in developing countries with favourable investment requirements will remain the most daunting challenge. Governments can assist in this process by encouraging their official export credit agencies to support the financing of key energy infrastructure projects on appropriate credit terms, and by insuring private sector investments in such projects. Increased private sector investment will be required and governments will have a key role to play in promoting competitive energy markets and setting the right framework conditions for investment.

From a business perspective, access to secure and affordable energy involves a range of business actors in addition to the traditional sectors of power generation, utilities and natural resource extraction. Transport, grid maintainers, automotive and energy intensive sectors are essential parts of the energy supply and use chain. Their needs and operating realities have to be taken into account as decision-makers consider how to attract and retain the investment that will be necessary to meet the challenges of the WEIO's forecasted needs in developing countries.

Taking into account long term investment cycles

Investment in energy projects is a long-term proposition and in that context, investors face considerable risks and challenges, which vary by region and the stage of the energy chain. Overall, investment conditions must be appealing and returns high enough to trigger the necessary investment. Many options involve considerable time and expense to alter energy and raw material inputs, operations and products and to develop and introduce technological innovations.

For energy producing and large energy-intensive industries, equipment lifetimes often range from 30 to 50 years. With regular maintenance and newly available technology, capital stock can often last decades longer than its initial expected/proposed lifetime. New process technology, i.e., technology that improves the efficiency and cost effectiveness of a factory or power plant, requires performance improvements of an exceptional magnitude to induce a firm to retire equipment where capital costs have already been paid.

Furthermore, the planning basis for business development, investment decisions, and cost-recovery may be profoundly affected by governmental commitments and changes in the international framework in the longer term. Uncertainty regarding longer-term time frames has already introduced concerns and delays in decision making, especially regarding international investments for energy production and distribution projects to develop long-lived infrastructure.

Business encourages policy makers to commit themselves to a consistent policy framework over an appropriate period of investments, which in the energy sector can amount to several decades.

3. Key business messages in energy governance and investment

A competitive, free and open market

Governments will continue to play a major role in ensuring adequate financing for energy infrastructure and in encouraging private investment by establishing an enabling policy framework for the energy sector. The macroeconomic environment is a key driver of energy demand and energy investment as it affects not only the amount of investment needed, but also the energy sector's access to capital.

Economic prosperity and efficiency depend upon free and open markets and predictable and transparent regulatory frameworks which reduce competitive distortions. Free and open markets operating within a clear, stable and well-designed legal, fiscal and regulatory framework are likeliest to avoid market distortion and best serve the interests of business and society. Open markets across national borders have been a reality for decades in the oil and coal sectors, whereas integrated regional markets are a more recent experience for electricity and gas. Market-based prices, market solutions, cost-benefit analysis, non-discriminatory and consistent legal enforcement, risk assessment and sound science are all attributes of these frameworks. The use of market-distorting policies adds unnecessary costs to society, hampers efficiency and should be avoided.

Differences in taxation and in environmental and other regulations between different energy sources and jurisdictions can distort competition significantly and influence the investment climate. Therefore, policies should be carefully assessed for their economic burdens and cost-effectiveness before they are finalised and implemented. The possible impacts of tax policies in a global context, such as competitive distortions, need to be given due consideration. The OECD work on Regulatory Reform can be an important instrument to promote such policies.

Improving public governance

Outdated regulations contribute to a bureaucratic, less efficient environment, often inhibiting the potential of private sector or foreign direct investment. Regulatory reform that encourages open markets and competition will have to overcome entrenched interests and this will require international dialogue, incentives and cooperation. Sound data and analysis are indispensable to this effort, particularly in order to identify patterns of regulatory reform that have been successful and sustainable in one or more member countries. A main focus should be on promoting the adoption of these approaches and on finding ways to bring these messages to the attention of relevant non-member countries.

Giving attention to the following concepts helps facilitate the promotion of efficient policies and well-directed investments:

- **Free market** - An economic system promoting individual business/property rights and freedom of entry, with market prices and profit-and-loss incentives used to allocate scarce resources to competing uses.
- **Open market** - Markets where barriers to entry are few, defined by an enterprise's competitive/financial capabilities and its profit-and-loss incentives and enabling an impartial, non-discriminatory environment for competing alternatives.

- **Market solutions** - A free market approach to determine solutions and prices to consumer, supplier, investor or government objectives. This is a more efficient alternative to government "command and control" regulatory approaches that set mandates and restrict potential options.
- **Cost/benefit analysis** – A quantifiable approach to account for and determine how the expected tangible costs (including foregone opportunities) of a policy, project or action compare with the expected tangible benefits. Regulatory Impact Analysis (RIA) is another useful tool to assess and seek areas in which to improve rule making.
- **Rule of law** - A system of government whereby a reliable and transparent framework of laws provides a common and stable foundation to promote law and order, protection of investors rights and protection of intellectual property, standards for personal and business conduct, and justice via due process.

Business should participate in policy discussions to help governments take a global and long-term view, pursue market-based solutions and support open competition. As predictability is best achieved through a consistent political framework, BIAC encourages governments to set long-term policy frameworks for energy investment.

Transparency of regulation and policy instruments

Business needs transparency of regulation and policy instruments. Non-transparent regulatory systems serve as a significant barrier to private investment. Transparency reduces risks and uncertainty while promoting consistency and predictability. It also minimizes corruption and discrimination, promotes competition, and strengthens accountability of governments.

The unique long-term and capital-intensive nature of the energy industry's investment and commercial activities, its price and revenue flows fluctuations, and its economic significance and impacts in the producer countries and world markets all depend on transparency. As energy sector investors face a particularly high risk of policy reversals and policy uncertainties in a number of developing countries, it is essential to enhance transparency, not only through national laws and regulations but also through international cooperation.

Political and legal stability and strong institutions

Political stability promotes consistent policy frameworks to improve public governance, which in turn profoundly affects the planning basis for business development, investment decisions, and cost-recovery in the longer term. Hence, political stability is a crucial requirement to encourage international investments for energy production, infrastructure and distribution projects.

A reliable regulatory and legal redress process can help reduce 'regulatory risks', which tend to be prevalent in developing countries. Business understands that full regulatory certainty can never be guaranteed. In fact, new information may require new approaches, for example, environmental or safety risks or unforeseen consequences of regulations that may emerge.

Eliminating solicitation, bribery and corruption

To promote investment in the energy sector, the business community sees a strong need to eliminate acts of bribery and corruption, which is a shared responsibility. BIAC believes that governments and inter-governmental actions have an important role to play in assisting companies in the prevention of bribe solicitation as well as in prosecuting offenders.

The OECD represents the majority of world investment activities and is well suited to assist governments in reducing bribe solicitation, based on experience and oversight of the OECD Anti-Bribery Convention. Convention-related outreach activities with non-member countries and initiatives on better governance and regulatory reform are very useful. The fight against bribe solicitation must be an integral part of the OECD's anti-corruption and regulatory reform activities with non-member countries.

Infrastructure requirements

Energy companies frequently require infrastructure that developing countries lack. In those instances, energy companies are expected or obliged to actually provide the lacking infrastructure (building roads, providing health care, etc.). In areas where there is a lucrative source of energy to be extracted, this is part of the business equation. In other areas where the economics do not allow this potential, the dynamic will be very different.

The availability of capital resources, including both up-front costs borne by project partners and basic infrastructure requirements, remains a challenge facing many energy proposals. Financial mechanisms to stimulate markets to make the necessary capital available are often in short supply in developing countries where they are most needed. This, of course, affects the risk portion of the equation. In addition, technical capabilities, human resources and cultural aspects strongly affect the viability of projects, and capacity building should be part of any project planning.

4. The importance of international cooperation

For BIAC, which represents the broader business community, including both energy producers and consumers, the challenge is how economies can provide and use energy more efficiently with reduced environmental impacts, while maintaining economic growth and prosperity. In this context, how can necessary investment levels be reached? International co-operation is especially relevant in this respect and contributes to enhancing the overall efficiency of national efforts. Societies will benefit when governments and industry work together cooperatively and effectively.

The IEA plays a crucial role in addressing emergency preparedness, promoting rational energy policies in a global context through co-operative relations with its members, non-member countries, industry and international organisations and in contributing to discussions to improve the world's energy supply and demand structure. The OECD has the potential to bring these messages and policy recommendations to the attention of decision-makers in governments beyond the energy departments and raise the profile of the energy dimension in discussions on economic policy, investment, regulatory reform, innovation and its work with non-member countries.

The growing importance of non-OECD countries in global energy consumption has major implications for global supply issues as well as environmental consequences. Non-member countries should be engaged as essential partners in discussions on energy investment and co-operation, and we encourage both OECD and IEA to continue and reinforce their successful outreach work in this respect.

BIAC congratulates the OECD for initiating a dialogue with Energy Ministers on the topic on energy and investment during the 2005 OECD Council Ministerial. We encourage the Organisation to work towards increased policy integration and dialogue among ministries on this important issue and give due consideration to the energy dimension across a wide range of its ongoing activities.

II. Meeting the Challenges of Globalisation and Structural Adjustment

1. Introduction

In this era of globalisation and demographic change, the benefits that can be gained by seizing the opportunities created by open markets have never been greater. At the same time, the challenges and costs of adjusting to changes accompanying these opportunities and realising their benefits are also great.

For developed and developing countries alike, implementing policy frameworks that provide for successful and fruitful structural adjustment are key to competitiveness, job creation, and sustainable economic growth. Across sectors and across policy areas, comprehensive integrated policy approaches are needed to ensure that as we go forward, our globalised economy is a growing economy – the necessary basis for investment, trade and development, raising standards of living and eliminating poverty.

The issue of how companies and sectors can adjust to restructuring pressures stemming from international trade liberalisation and new patterns of industrial production and services is not at all a new one for the OECD business community. What is new is that challenges that once were predominately confined to the manufacturing sector now confront the service sector and higher-value activities on a global basis in a phenomenon that is commonly described as “outsourcing”.

In this context, sustainable economic growth and job creation are common to all necessary policy approaches to structural adjustment, whether they be in response to new sources of competition, technological change or shifting consumer preferences.

BIAC welcomes the completion of the OECD Project on Trade and Structural Adjustment as well as the complementary project on enhancing services sector performance. We appreciate the opportunity to provide business views on structural adjustment to the 2005 OECD Council Ministerial. OECD fact-based analysis, including other projects underway such as the reassessment of the OECD Jobs Strategy are critical to address misperceptions related to globalisation and to pre-empt protectionist policies.

Ever-Changing Environment for Business

As we noted to Ministers in 2004, the old and simplified model of a multinational enterprise setting up a plant in a host country no longer corresponds to the reality of much of international investment as it exists today. Thanks to technological developments, continued rounds of trade liberalisation and a world-wide opening up of sectors for investment, companies have had a growing number of alternatives in international production.

FDI in the OECD area soared before the recent downturn in 2001, and continued to fall through 2003. However, Global FDI total outflows have multiplied 17-fold since 1985 to 1.3 trillion US dollars in 2000¹. As a result, the production and consumption of goods and services has been internationalised. Today, 60 000 parent companies have established more than 500 000 foreign affiliates worldwide. National firms, even quite small ones, have become multinational by increasingly localising their production facilities outside their home countries to benefit internationally from local competitive advantages. Companies transcend

¹ OECD, “Foreign Direct Investment for Development”, 2003..

national borders by establishing a network of subsidiaries and linkages with local enterprises to relay outsourcing and offshore activities on a global scale.

This new pattern of international production has major implications for business, including the following:

- Changes in production processes and technologies;
- Increasing competition and new sources of competition;
- Constant pressures to reduce costs and improve productivity;
- Mismatches between job requirements and labour skills;
- Mounting labour compensation costs including payroll taxes and benefits;
- Shorter product cycles and need for agility and flexibility;
- Importance of efficient international supply chains for reducing costs and reliable, fast delivery of components;
- Increased cost generated by enhanced supply chain security requirements;
- Proliferation of conflicting and overly rigid, e.g. not performance based, regulations.

2. Policy Priorities for Business

Business recognises the challenges for individual employees, companies, even for an entire sector brought on by the opportunities afforded by open markets. The approach to structural adjustment must be a comprehensive integrated policy strategy, as is also emphasised in the OECD Project on Trade and Structural Adjustment.

We also stress that adjustment to trade-related impacts addresses only a fraction of the dislocations caused by competition and innovation in domestic markets. Therefore, any adjustment programs directed at trade impacts should be integrated with larger efforts to address on-going, non trade-related structural adjustment needs within national economies.

Longer term adjustment responses will necessarily involve a broader range of policies, including macroeconomics, competitiveness initiatives, regulatory policies as well as labour market adjustment policies. Education and training also play a critical role in successful approaches to structural adjustment.

With this in mind, in this Statement, BIAC identifies the following policy priorities that enable business to positively respond to necessary structural adjustment:

- A. Enabling Policy Framework Conditions for Sustainable Growth**
- B. Stimulating Entrepreneurship and Innovation**
- C. Linking Structural Adjustment Approaches to Labour Market and Social Policies**
- D. Encouraging Investment in Human Capital Formation and the Promotion of Lifelong Learning**

We note that the “Recommendations for Good Practices” in the Final OECD Report on Trade and Structural Adjustment emphasise all of these areas. In the following sections, BIAC outlines more specifically elements of each of these priorities.

A. Enabling Policy Framework Conditions for Sustainable Growth

Good public governance, the implementation of appropriate macro-economic policy and regulatory frameworks that promote competition, innovation and entrepreneurial activity are essential to stimulate economic growth and in turn reduce unemployment in all economies. Such enabling framework conditions are the necessary foundations for successful structural adjustment.

Macroeconomic policies that promote economic growth on a sustainable basis are an important prerequisite for countries' ability to swiftly adjust to structural changes. Avoiding high inflation rates, excessively high unemployment rates, and excessive public deficits are key elements of sound macroeconomic policies.

Trade and investment liberalisation complement good macroeconomic policies. They are instrumental in fostering competition, innovation and economic growth through a more effective division of labour between countries based on comparative advantages. Through this, liberal trade and investment regimes help in facilitating and accelerating countries' adjustment processes.

The world trading system and the open markets that it promotes are essential to sustainable economic growth, to supporting and diffusing innovation, and to reducing poverty by creating wealth. Multilateral free trade policy has an important role in helping countries absorb and capitalise on the growth and development potential of a rapidly changing global marketplace. The economic growth and improved living standards around the world we have seen over the past 50 years would not have been possible without the disciplines and achievements of the GATT/WTO system. The WTO Doha Round offers an excellent opportunity for further welfare-increasing trade liberalization that must not be missed. BIAC is concerned, however, about the fact that many trade negotiators around the world are paring down expectations for the outcome of the Round. The OECD business community remains strongly committed to a successful Doha Round and it urges governments to negotiate meaningful results.

As outlined in the recent BIAC position paper on the WTO Doha Round², market access for goods and services remains among the most critical issues for achieving a successful negotiation. Negotiators need to focus on these areas in order to ensure that they do not lag behind the work on the also much-needed substantial liberalization of agriculture.

In order to improve market access for non-agricultural products OECD countries should cut their industrial tariffs ambitiously. In addition, non-tariff barriers also need to be reduced substantially. Emerging markets and developing countries should participate in the exercises to improve market access for industrial goods in a meaningful way.

Trade in services offers a tremendous growth potential for most economies. In order to unleash this potential, developed and developing countries should vastly improve and expand their market access commitments for all services sectors and modes of supply. Governments need to begin serious negotiations on services without delay.

An additional crucial element of trade liberalization is trade facilitation. Increasing the efficiency of customs and logistic procedures will generate a win-win situation for all countries involved. Developing countries benefit in particular from trade facilitation, as recent OECD and World Bank studies show.

The WTO is a rules-based system and some of the global trade rules need to be improved. Priority should be given to the Doha Declaration mandate for clarification and improvement of anti-dumping and countervailing duty laws as well as to the enhancement of disciplines on Regional Trade Agreements.

² BIAC Priorities for the WTO Doha Negotiations and Recommendations to the OECD. February 2005.

BIAC believes that it is to the clear benefit of all countries to adhere to common trade disciplines. Special and differential treatment should be in the form of different time periods wherever possible coupled with capacity building commitments where truly needed.

The OECD has a key role to play in building confidence in and support for the global trading system. Its analytical work is an important base for the negotiations outlined in the WTO Doha Declaration. In addition, the OECD's outreach programmes provide skilled resources for improving the technical capacities of developing countries in the field of trade policy. Encouraging and participating in this process is fundamental for the OECD.

Foreign direct investment (FDI) is closely linked to trade. Both are complementary activities vital to modern international business operations. FDI generates not just capital, but also increased knowledge and skills in an economy. It promotes a focus on productivity improvement, management skills and facilitates integrated links to markets. Through this, foreign direct investment enables countries to adapt to structural changes. Because of the beneficial effects of FDI, countries compete with each other in order to attract as much FDI as they can.

Attracting foreign investment requires creating an attractive environment for investment. This includes ensuring government accountability and transparency, capital mobility, labour market flexibility, human resource development and infrastructure. Markets need to be open for foreign investors and a level playing field between domestic and foreign investors has to be guaranteed. Furthermore, many countries need to reduce risks that may discourage foreign investment. Such risks for investment include unstable macroeconomic developments, unstable financial markets, lack of enforcement of intellectual property rights, corruption and bribe solicitation.

BIAC believes that the OECD can and must play an important role in supporting OECD and non-OECD countries in improving their economic and policy environments for FDI. Thus, we support the OECD initiative for a 'Policy Framework for Investment' aimed at promoting shared views among OECD governments, non-OECD governments and business on what constitutes "good policies" for attracting foreign direct investment. The Framework could become a useful tool for countries that want to increase their attractiveness to foreign investment.³

Foreign investors enhance the social good by investing as such. In addition, companies decide to engage on further voluntary activities related to corporate social responsibility (CSR). Many businesses are investing significant resources in policies such as fostering an atmosphere of trust between management and workers, protecting the environment, supporting national science and technology policies and engaging in community relations. Such CSR activities do additionally increase the beneficial effects of FDI and may help facilitating structural changes within companies, communities and societies.

The OECD Guidelines for Multinational Enterprises provide an important reference point for foreign investors who are seeking recommendations on good corporate conduct. As part of the wider OECD Declaration on International Investment and Multinational Enterprises the Guidelines are the only comprehensive set of recommendations for foreign investors that are multilaterally endorsed by governments. BIAC members encourage companies to put the principles for good business conduct outlined in the Guidelines into practise when investing abroad.

It needs to be pointed out though that there is a close relationship between what a company can achieve through corporate governance and the commitment of host governments to improve regulation and its enforcement. In this relationship, the governance environment

³ See BIAC Comments on the proposed OECD Policy Framework for Investment, April 2005.

provided by governments is the precursor to good corporate governance and not the other way round.

Governments have the responsibility to take the lead on reforms and to commit themselves to reform processes on a sustained basis. They must establish the necessary legal and economic infrastructure in which businesses can operate. We urge OECD countries to continue encouraging countries in transition and developing countries to improve their public governance. Capacity building for governments where needed, in particular in weak governance zones, would be an important element that could contribute to significant improvements of the situations in these regions.⁴

BIAC welcomes the OECD 2005 Recommendations for Regulatory Quality and Performance and the APEC-OECD Integrated Checklist for Regulatory Reform, and sees these as important tools for leadership to provide a whole of government approach to achieving greater regulatory quality. They provide important guidance to OECD and non-OECD Member countries alike for good public governance, and the development of enabling policy frameworks that are absolutely essential to create competitive business environments.

B. Stimulating Entrepreneurship and Innovation

Entrepreneurship and innovation are key to creating more jobs, and are at the heart of business creation and transformation in today's global economy.

Regulatory frameworks that are transparent, understandable, un-bureaucratic and pro-competitive are essential to stimulate business creation that may otherwise be discouraged by excessive administrative burdens and costs. Creation of new businesses also relies on access to technology and a skilled labour pool that results from quality education and the accessibility of lifelong learning. Taxation and fiscal policies that support entrepreneurship are also essential.

Opportunities for self-employment and improving the conditions for the creation and growth of micro-businesses and SMEs, also play a crucial role in job creation. Likewise, instilling the value of entrepreneurship in young people can contribute to their successful and early integration into the labour force. These entrepreneurial skills can be developed with business in coordination with educational institutions.

OECD research has shown that while information and communication technology is a significant source and force multiplier for economic performance, an even more fundamental source of growth is innovation. The development of new products, processes and services drives improvements in productivity. It also facilitates the fulfilment of numerous societal needs, such as improved health and environmental protection.

As has been elaborated by the OECD, innovation often involves organisational as well as technological change and requires sizeable complementary investments in worker training, manufacturing and marketing, in addition to investment in R&D. Governments need to foster investment and innovation through government funding and sponsoring, including offering tax incentives for R&D.

There is a continuous need for better understanding of how innovation impacts economic prospects and what other factors must be in place to generate a sustained, economy-wide improvement in productivity and output. In fact, innovation appears to be playing an increasingly important role in driving economic growth.

⁴ See BIAC position paper commenting on the OECD draft "Conducting Business With Integrity In Weak Governance Zones – Lessons Learned" DAF/INV/WP(2005)1, April 2005.

The following general conditions must be in place in order for entrepreneurial and innovative opportunities to spread quickly in the context of economic activity:

- A regulatory and legal environment that is strongly in favour of open market competition and business creation;
- Incentives to encourage skill acquisition and necessary changes in the organisation of the workforce;
- Continuation of strengthening standards world-wide for intellectual property rights protection;
- Closer relations between industry and academia to raise standards of excellence, ensure effective knowledge and technology transfer and achieve mutually beneficial personal exchanges and awareness;
- Encouragement of SME and entrepreneurship development.

C. Linking Structural Adjustment Approaches to Labour Market and Social Policies

Removing disincentives to work is a critical element of a policy framework that provides the necessary environment for job creation. Widespread misconceptions regarding the benefits and perceived costs of trade liberalisation and investment, and their impact on jobs, can lead policy makers to implement protectionist measures that are harmful to the world economy as a whole.

We support the OECD view that often it is the relationship between labour market conditions and the trade regime that determine whether or not adjustment is successful. From the business perspective, this view clearly emphasises the need for labour market and social policies that provide for:

- Flexibility to manage human resources;
- Active and inclusive labour market and employment policies;
- Reform of benefits systems.

To this end, we believe that the OECD Jobs Strategy must continue to target increasing *labour market participation* and increasing awareness about the effects of *over-regulation* and *lack of flexibility* in labour markets across OECD economies. Developing countries will also benefit from this approach. The analysis being undertaken as part of the Reassessment is critical in support of these objectives, and helps to pre-empt protectionist policies.⁵

Flexibility to manage human resources

Companies require heightened flexibility in the labour market in order to respond to market shifts, customer needs and competitive pressures, as these changes take place at an increasing pace. Obstacles to the creation of new jobs are often in the form of rigidities in labour legislation, high non-wage labour costs, overly strict job protection, minimum wages,

⁵ See BIAAC Statement to the OECD Liaison Committee « Managing Competitiveness in a Changing World », November 2005. Found at www.biac.org.

income taxes, excessively generous benefits systems, and undue administrative barriers, all of which are disincentives for companies to hire.

Labour laws and employment policies need to be modernised to allow for more flexibility and reduce regulatory and administrative burdens. As such, existing protective measures should be reviewed and reforms implemented.

The growth of non-standard forms of employment should be seen as a positive advancement toward achieving greater employment opportunities and better work/life balance. For example, such flexible approaches can include part-time or flexible working hours, variations in working time, innovative leave arrangements, telecommuting, and part-time retirement. These measures can also facilitate the reconciliation of work and family life, and careers across various ages and groups, for example, women, older workers, and the disabled.

Mobility of personnel within an organisation also contributes to its competitiveness. Policies to support mobility can contribute to skill enhancement, and support diffusion of technologies within and between organisations. Mobility also contributes to the transfer of skills and technologies to developing countries. High job turnover and restructuring firms in today's economy has also made mobility critical for both employers and employees in a domestic or international context.

Active and inclusive labour and employment policies

Policies to increase employment rates of all groups, and in particular those under-represented in the workplace, such as older workers, youth, women, and immigrants are crucial in view of today's global business environment and the demographic changes we face as a result of ageing populations.

“Making work pay”, that is, implementing strategies that provide the necessary incentives for all individuals to seek and accept employment, is essential. Those receiving income support should be encouraged to resume work. The modernisation of social security systems and the implementation of tax policies that activate the unemployed to seek new employment are vital to achieving this objective.

Governments, in particular, have a role to play in stimulating labour demand and in activating the supply side by reforming tax and benefit systems. There is a need for continued reform of taxation and fiscal policies that impact both employers and those seeking work. Excessive income taxation can be a real barrier to employment, in particular with regard to unskilled or low skilled workers. Reforms should also aim to reduce regulatory and administrative burdens related to employment and social benefits.

With increased longevity has also come the need for people to stay in the workforce longer and thus “active ageing” should be encouraged. Continued education and lifelong learning, cultivated from an early age, is key to the continued employability of workers and in particular to helping older workers cope with structural adjustment. Increasing the effective age of retirement; diversifying working times and work organisation; increasing emphasis on lifelong learning; analysing the effects of employment protection measures; encouraging more wage flexibility; and promoting effective job placement are important measures towards continued employment of older workers.

Support for job search and provisions for additional training that is necessary to enter the labour market are also important and should be accessible to all groups. It is crucial to focus on active and rapid job search assistance, in addition to improving the quality of the general job brokerage systems. Such services should take into account the needs of both the unemployed and companies. Matching between companies' needs and job seekers' skills must be improved, which could be facilitated by closer liaison of employment services and educational institutions with the private sector.

Reform of benefits systems

Benefits systems need continued analysis in order to target those in greatest need, and also to address the needs of those who are in transition between jobs.⁶

Appropriate schemes need to be designed to ensure that people have the incentives to enter and re-enter the labour market and can accept new jobs where their skills are most applicable. In many countries, a dependency culture has been created due to unemployment benefits that are so high that they discourage active job-seeking. The difference between remuneration for work and benefits should always be high enough to stimulate increased individual motivation for active job-seeking.

The burden imposed both on companies and employees by taxes and social security contributions must be reduced. The distribution of cost-sharing varies from country to country, but is extremely striking in some Member states. In some countries, the limited effectiveness of social security services causes contributions to be viewed as an additional tax by employers and employees. The situation is particularly difficult for small and medium-sized enterprises, which play an essential role in any well-balanced economy. Modernising tax and benefit systems, including addressing eligibility for and taxation of benefits and pensions in a cross border context, is vitally important in order that workers can adapt to changing business environments.

By increasing the overall cost of hiring workers, the growth in social transfer expenditures worsens the labour market situation, in particular for low-skilled workers. A broad reduction in non-wage labour costs is therefore essential and should be accompanied by a reduction in administrative burdens, which impose additional "indirect" costs on companies. The savings from such reforms would give companies better opportunities to invest in continuing education and re-training programmes for employees, especially important in the context of structural adjustment.

D. Encouraging Investment in Human Capital Formation and the Promotion of Lifelong Learning

Education is perhaps the most effective mechanism to improve employment prospects for all groups. The increasingly dynamic labour market brought on by globalisation has necessitated an important shift in thinking about goals of education. Rapidly evolving job profiles responding to market needs require employees to have an education that equips them with the ability to respond and adapt to market changes and new technologies. This need becomes even greater as a result of changing demographics. Likewise, management of companies is increasingly horizontal, requiring teamwork to complete complex tasks, and emphasising entrepreneurship in exploring new business opportunities.

Education and training need to be managed and equipped to respond to these new market realities. This entails school objectives shifting from only or mostly pure cognitive goals and "ready for use" vocational qualifications, towards emphasising basic knowledge and skills, including practical and ICT-skills, complemented by social and personal skills, interdisciplinary approaches, diversified working methods and the ability to learn throughout life.

Initial education is essential to a healthy economy. The quality of human capital is a key contributor to competitiveness, enhanced productivity, and the capacity for innovation. Companies depend upon a labour pool that is flexible, technologically literate and work-ready, and have a vital interest in schools turning out young people equipped to take on the

⁶ See BIAC Statement to OECD March 2005 Social Policy Ministerial "Extending Opportunities: How Social Policy Can Benefit us All", March 2005. Found at www.biac.org.

ever more technologically sophisticated and knowledge-intensive jobs. Likewise, an awareness of career possibilities and understanding of the labour market should start with initial education.

In developing countries, public expenditure on education can be quite restricted. Thus innovative ways need to be found to use often scant resources to good effect in the provision of education.

In our view, Government has the primary responsibility for initial education. Employers and companies contribute by working with Government and educational institutions to provide clear goals for education according to the needs of the market. At the local level, companies provide opportunities for students to learn about developments in industry, services and technology. Many companies are deeply involved in helping education institutions with the assessment of attributes that employers will be looking for in their recruits in the coming years. They consider the skills that will be in demand; the breadth of education required for different areas of work; and the timing of opportunities and the number that are likely to become available.

Both employers and employees have a major responsibility with regard to further training and life long learning. Employees need to take initiative to develop transferable skills and be receptive to learning that is not exclusively job-or firm-specific. Employers can provide development opportunities at the workplace as well as firm- and job-specific training.

3. Conclusion

Governments play a critical role in sustaining public support for open markets, via positive messages that underpin the benefits of globalisation. Business also relies on governments to set policy frameworks that enable trade and investment, and for the necessary flexibility to manage human resources in the midst of change brought about by competitive pressures, technological change and evolving consumer preferences.

Moreover, governments must assure their citizens that implementation of policies in favour of open markets will allow for a smooth transfer of resources from declining to expanding activities, and provide adequate assistance to those who experience adjustment costs as a result of structural change. The OECD's Report on Trade and Structural Adjustment has quite fully outlined policy approaches that together can work to achieve such a balance.

Business is a key actor in generating growth in both developed and developing countries. Trade and foreign direct investment in the context of good governance, sound macroeconomic frameworks, open competitive markets, and labour and social policies that promote job creation, are important tools for reaching this goal.

BIAC welcomes future OECD work on globalisation and structural adjustment, and stresses the value of fact based analysis in putting forth a positive political message on the benefits afforded by the global economy.