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22580

# Reforming the UN System

## UNIDO's Need-Driven Model

by

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**UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION**



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## REFORMING THE UN SYSTEM

# NIJHOFF LAW SPECIALS

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## Abbreviations

3 Es	Economy, employment and environment
ACABQ	Advisory Committee on Administration and Budgetary Questions
ACC	Administrative Committee on Coordination
CCAs	Common country assessments
CCPOQ	Consultative Committee on Programme and Operational Questions
CDP	Committee for Development Planning
CEE	Central and Eastern Europe
CPC	Committee for Programme and Coordination
CSAE	Centre for the Study of African Economies
CSOs	Civil Society Organizations
CTC	UN Centre for Transnational Corporations
DAC	Development Assistance Committee
DANIDA	Danish development agency
DDSMS	Department for Development Support and Management Services
DESA	Department of Economic and Social Affairs
DESIPA	Department for Economic and Social Information Policy Analysis
DPCSD	Department for Policy Coordination and Sustainable Development
ECOSOC	Economic and Social Council
EPTA	Expanded Programme for Technical Assistance
EU	European Union
FAO	Food and Agriculture Organization of the United Nations
FDI	Foreign direct investment
FSU	Former Soviet Union
GATT	General Agreement on Tariffs and Trade
GNP	Gross national product
HABITAT	United Nations Centre for Human Settlements
IAEA	International Atomic Energy Agency
IBRD	International Bank for Reconstruction and Development
ICAO	International Civil Aviation Organization
IDA	International Development Agency
IDA	International Development Agenda
IDA	International Development Association
IDB	Industrial Development Board
IDDA	Industrial Development Decade for Africa
IFAD	International Food and Agriculture Development
IFC	International Finance Corporation
ILO	International Labour Organization
IMF	International Monetary Fund
IMO	International Maritime Organization
INSEAD	The European Institute of Business Administration
IPF	Indicative Planning Figure
IPU	International Postal Union

ISO	International Organization for Standardization
ITC	International Trade Centre
ITU	International Telecommunications Union
JITAP	Joint Integrated Programme of Technical Assistance for Selected Least Developed and other African Countries
JIU	Joint Inspection Unit
JPOs	Junior Professional Officers
LAC	Latin America and the Caribbean
LDCs	Least developed countries
MENA	Middle East and North Africa
MSTQ	Metrology, standards, testing and quality
MVA	Manufacturing value added
NGOs	Non-governmental organizations
NIEO	New International Economic Order
NIEs	Newly Industrializing Economies
NIS	Newly Independent States
NSF	US National Science Foundation
ODA	Official Development Assistance
OECD	Organization for Economic Cooperation and Development
OPEC	Organization of the Petroleum-Exporting Countries
PROBE	Productivity On-Line Benchmarking
QA	Quality assurance
R&D	Research and development
RB	Resource based
SF	United Nations Special Fund
SNFED	Special UN Fund for Economic Development
SSA	Sub-Saharan Africa
TBS	Tanzania Bureau of Standards
TC	Technical cooperation
TNCs	Transnational Corporations
TRIMS	Trade-Related Investment Measures
TRIPS	Trade-Related Intellectual Property Rights
UK	United Kingdom
UN	United Nations
UNCED	United Nations Conference on Environment and Development
UNCTAD	United Nations Conference on Trade and Development
UNDA	United Nations Development Agency
UNDAF	United Nations Development Assistance Frameworks
UNDCP	United Nations International Drug Control Programme
UNDG	United Nations Development Group
UNDP	United Nations Development Programme
UNEP	United Nations Environment Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNFIP	United Nations Fund for International Partnerships
UNFPA	United Nations Population Fund
UNHCR	Office of the United Nations High Commissioner for Refugees
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organization

UNIFEM	United Nations Development Fund for Women
UNOID	United Nations Organization for Industrial Development
UNU	United Nations University
UNWRA	United Nations Relief and Works Agency for Palestine Refugees in the Near East
URT	United Republic of Tanzania
USA	United States of America
USG	Under-Secretary-General
WFC	World Food Council
WFP	World Food Programme
WHO	World Health Organization
WIPO	World Intellectual Property Organization
WMO	World Meteorological Organization
WTO	World Tourism Organization
WTO	World Trade Organization

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*Carlos A. Magariños*

# Foreword

CLARE SHORT

*Secretary of State for International Development  
United Kingdom of Great Britain and Northern Ireland*

I believe that in a world confronting globalization, we need a stronger and more effective UN. The challenge for our age is to manage globalization equitably and sustainably. The UN, as the world's only genuinely global institution, with a special moral authority on the world stage, should play a leading role in ensuring that the world's poor benefit from the wealth being generated by globalization.

The great UN conferences of the 1990s were the source of the international development targets for poverty eradication, which have been endorsed by the Development Assistance Committee of the OECD, the G8, the IMF and the World Bank. I believe that the UN should use its authority and influence to mobilize the international system to meet these international development targets.

There is an enormous potential in the expertise, commitment and energy of the 30,000 UN staff involved in development work and the \$10 billion a year they have to spend. But the UN's development impact is well below its potential. I believe that all UN development agencies should focus their efforts around the international development targets, concentrating on their own areas of comparative advantage where they can add most value to the achievement of these targets. It is vital that UN agencies work more collaboratively together in order to improve their effectiveness. UN Common Country Assessments and UN Development Assistance Frameworks and the World Bank's Comprehensive Development Framework and Poverty Reduction Strategies provide important opportunities for all donors to work more closely together behind developing country leadership in pursuit of the international development targets.

The British Government is strongly committed to providing increasing support to those agencies which modernize their management and organization to increase their effectiveness in helping meet the international development targets.

UNIDO has set an example. It has sought to focus its efforts on its own areas of comparative advantage and is working to strengthen the industrial capacities of developing countries through environmentally friendly and sustainable industrial development.

The Director-General of UNIDO, Carlos Magariños, and his staff continue to implement significant reforms. UNIDO has made important changes to its management, organization and personnel. It is re-focusing its programmes. It has managed a 20 per cent budget reduction. It has given greater emphasis to performance measurement and



transparency and has moved towards results-based budgeting. UNIDO is investing in staff training and in strengthening its field representation. It continues to look for ways to develop deeper contacts with industry and academia, encourages linkages with other UN bodies and with the World Bank, and supports the UN Development Assistance Framework.

The modernization of policy and organization, which has done much to restore the credibility of UNIDO, needs to be carried through in all the UN funds, programmes and agencies.

I hope this book will help to reinforce the case for UN reform and that other UN agencies will be able to learn lessons from the experience of reform in UNIDO.

# Preface

CARLOS A. MAGARIÑOS

*Director-General of UNIDO*

I always count it a blessing that my professional life has been so frequently associated with change. From my youth I have had the opportunity to participate in the implementation not of mere marginal changes but of major economic turnarounds.

The first occasion was in Argentina, at the beginning of the 1990s, when the country was struggling to end a 40-year process of inflation—which at that moment had reached its peak and become hyperinflation—by introducing a new economic policy based on market-oriented reforms. As National Director, Undersecretary and Secretary of State responsible for the portfolios of foreign trade, industry and mining, I had the opportunity to help shape the process of change of Argentina's economic fundamentals.

The second occasion was in the mid-1990s, when I was in Washington D.C. selling the initial success of the Argentine reform process as Economic and Trade Representative. I was then encouraged to run for the position of Director-General of UNIDO, the UN agency specialized in the field of industry, which was struggling to reform itself. After winning a difficult international election in 1997 I took over the task at the beginning of 1998.

By January 2001 the reform process of UNIDO had won worldwide recognition, with the accession of new member States to the organization, complete stability in the areas of personnel and finance, and a growing number of countries contributing to its technical cooperation activities. Furthermore, the Secretary-General invited me to Chair the High-level Committee on Programmes of the United Nations System (Administrative Committee on Coordination, ACC).

That is why I am generally identified or introduced as a “reformer”. I have accepted that label gladly since it is being used in a positive sense. Obviously to be a reformer in an era of change can be seen as a positive thing.

However the label carries a risk: to be seen as considering change or reform good in itself. I certainly disagree with that notion, and that is why I have always considered it essential to analyse and evaluate the process of change and its direction. Maybe that is why my first book was about the economic reform process in Argentina in the areas of industry and trade. And it is certainly why I feel compelled to share some reflections about the UN reform process and the particular case of UNIDO, to help understand how to do more or better to improve the opportunities provided by the multilateral system.

Change, reform or transformations are not good in themselves. They can only be judged from the perspective of their purpose.

To improve the economic management of a country or the managerial performance of a multilateral organization is certainly a good thing. But in my view, what makes the effort relevant is the potential outcome of these improvements in terms, for example, of the reduction of poverty and the restoration of the capabilities denied to people by poor economic performance, or of other development goals such as the promotion of human rights and the maintenance of peace.

Otherwise we can fall into a common trap of our times: to believe that good macro-economic indicators are the final aim of a given economic reform process, or that enhanced managerial performance will suffice to improve the impact and relevance of an agency.

To avoid this trap we have to place at the centre of our efforts the will and the needs of the stakeholders, the ultimate recipients of the fruits of reform.

As we intend to discuss in the first part of this book, reform is necessary to improve coordination and efficiency of the system but is also, and mainly, unavoidable if we are to respond adequately to the needs posed by the changes that have taken place in the world's political and economic scene.

In the second part we try to show how the case of UNIDO virtually forced member States to find and develop new mechanisms of interaction to ensure the direction they wanted to impress upon the reform process of the agency, re-defining its usefulness and relevance.

Another and more recent example is the negotiation and approval of the Millennium Declaration adopted at the United Nations Summit held in September 2000 in New York. In it, as Secretary-General Kofi Annan explains in his foreword to the recent publication of the Declaration,

“the world leaders have given clear directions for adapting this Organization to the new century. They are concerned, rightly, with the effectiveness of the United Nations. They want action and, above all, results.”

Improved economic and administrative management is necessary and could solve many problems, but to ensure that the process of change and its direction is right, the continuous feedback of the stakeholders is necessary.

Good managerial practices are important but have their limits. The direction and the purpose of any reform process should be evaluated and monitored in terms of the results that can be achieved on behalf of the stakeholders. And stakeholders are responsible for giving guidance and providing the necessary means that any reform process requires to succeed.

This concept may sound too business-oriented, but it is also applicable to multi-lateral institutions.

I always recall a dialogue at the end of the film “The Mission” where a bishop was talking with the Spanish commander while his troops were attacking a group of natives, both looking at the scene through a window. “Life is like this,” the commander said. “No, we make it like this,” answered the bishop.

For that reason I felt that it might be useful to share some of the lessons learnt in the process of reforming UNIDO; to explore the role and the limitations of good managerial practices and the need to gather a “group” of stakeholders very much committed to the reform process, not for the reform process itself, but to ensure its results.

This “group of reformers” should be formed with countries from different regions, with different levels of economic and institutional development. The more diversified the better. A diverse membership will ensure that the reform process will not attend the interest of the few but address the problems of a wide range of actors.

However, since the identity of the group will not rely on its homogeneity or that of the problems they are confronting, the unity of the reformers should arise from their common values and interest in fighting poverty and marginalization in a very effective and serious manner.

Only then we will have true, lasting and meaningful reform.

# Introduction

More than half a century has passed since the United Nations (UN) was established in 1945. In this time, the Organization can claim major achievements in a rapidly changing world—particularly in the areas of economic and social development. Yet the UN system has yet to fulfil the hopes and aspirations of its founders. It comes as no great surprise that calls for reform of the Organization have been raised with increasing stridency over the years as the UN has struggled with continuously increasing demands, a radically different geo-political context from 1945, and unsecured political support and resources.

The UN as a system—and the United Nations Industrial Development Organization (UNIDO) as a specialized agency—have recently undergone the most intense scrutiny in their history. Fundamental questions are being asked about the role of multilateral cooperation—and, indeed, of the UN itself. Its principles have been challenged. Its relevance has been doubted.

The Bretton Woods institutions—the World Bank, the International Monetary Fund (IMF)—and the World Trade Organization (WTO) have not escaped this scrutiny; and there have been loud calls to reform these organizations as well, most audibly in the form of open protests at meetings of the Bretton Woods organizations in Washington, Seattle and Prague.

In the case of UNIDO, questions have even been raised as to whether there is any longer a need for a publicly funded international body devoted to promoting industrial development. The implication is that the private sector and the spur of market forces can best handle industrial development today.

At the same time, the UN system is being asked to do more with less, and to be responsive to a new set of demands from its clients. UN agencies are increasingly being judged not only in terms of their own performance, but also in terms of the performance of the UN system as a whole. Donors now want clear evidence of unity of purpose, coordination and coherence, and harmony of actions, as well as a significant development impact as a result of individual and collective UN efforts.

## Changes in the global landscape

Calls for reform, and reform itself, within the UN system and the Bretton Woods institutions, are driven by profound political, economic and social changes which in recent years have fundamentally altered the international context of multilateral cooperation and development.

The end of the Cold War, which came with the collapse of the former Soviet Union and the demise of the command economic system, has radically altered international political and economic relations.

It has also brought about significant changes in the relationships between individual countries and the multilateral system—changes which are yet to be fully worked out. The transition from command to competitive market economies in Central and Eastern Europe (CEE), the former Soviet Union (FSU) and Asia, the re-integration of these countries into the world economic system, and their membership, or application for membership, in international organizations such as the World Bank, the IMF and the WTO, present special problems and opportunities for the international community and for multilateral cooperation.

As the confrontational politics of the Cold War gives way to more cooperative relations between East and West, new considerations are coming to prominence. Donor countries and international institutions are more concerned with promoting peace, democracy, human rights, environmental sustainability and good governance. These concerns constitute a new dimension of the development agenda and present new responsibilities and challenges for the UN system.

The end of the Cold War has brought additional economic difficulties for some developing countries in the shape of sharp reductions or cessation of economic aid from the former Soviet Union. On a more positive note, the end of the Cold War has meant reduced military expenditures in developed and developing countries as well as in economies in transition—although expenditures are still high. Unfortunately, only a small proportion of this peace dividend has gone into aid to the transition countries and poor countries elsewhere.

Conflict has increased as transition economies and developing countries attempt to establish independent nations or identities: Bosnia and Herzegovina and Kosovo in the former Yugoslavia; Chechnya and Tajikistan in the former Soviet Union; Burundi, the Democratic Republic of Congo and Rwanda in Africa. These often brutal hostilities have created a huge need for post-conflict assistance. Furthermore, a spate of natural disasters—such as floods in Mozambique and drought in Ethiopia—has further increased the need for emergency assistance. Of course, hostilities and natural disasters are not new, but their extent is growing. So, fortunately, is the will to confront these problems and the capability to do so.

These emergencies make tough demands on the UN system: greater speed and scale of response, better coordination and collaboration, and additional funding. Coordinated responses are required, for emergency humanitarian assistance, rehabilitation and reconstruction, and to address the problems caused by mass migration and the influx of refugees. A further challenge has arisen: to ensure that emergency and long-term assistance are linked to achieve sustainable development.

The interlinkage between poverty alleviation and conflict prevention needs to be emphasized. The Secretary-General of the UN has said, 'Without peace, development is not possible; without development, peace is not durable.'<sup>1</sup>

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<sup>1</sup>Speech delivered to the Security Council, 25 September 1997.

The resurgence of growth in the industrialized countries, with substantial reduction in unemployment in the European Union (EU) countries, if sustained, sets the stage for a timely reappraisal of their approach to the plight of the most laggard countries. This is already taking place by enlarging the number of highly indebted nations being granted debt forgiveness and by lifting barriers to their exports.

Over and above the profound political and economic changes that have taken place in the last decade or more, recent years have seen a rethinking of economic policies and the role of the State, with emphasis shifting towards a far greater reliance on market forces and the private sector as the engines of development. This rethinking has gathered momentum particularly since the collapse of the former Soviet Union and the command economic system. Greater reliance on market forces and the private sector has forced a reconsideration of the basic tenets of multilateral cooperation—including bilateral cooperation—and of the role of the UN system and civil society.

More importantly, the UN system, and particularly those agencies that deal with development, have had to reorient their assistance to include a much greater focus on and cooperation with the private sector and, increasingly, with civil society.

The biggest change in the world economic and political environment in recent years has been the extraordinary diversity of the development experience of developing countries. Yet what still shows through this diversity is the evidence that increasing inequality of incomes, poverty and environmental degradation remain formidable challenges for the UN system—and that a new challenge has emerged in the form of increasing volatility.

Current data confirm the unbalanced growth of the world economy, and show especially that the benefits of global growth have not spread sufficiently to the poorest countries of the world.

There is now a strong argument that growing inequality of incomes and wealth among and within countries seriously threatens future global economic growth, prosperity and peace. Recent economic research argues that there are good theoretical and empirical grounds to believe that inequality is harmful to growth and poverty reduction. Failure to reduce disparities among and within countries may affect the fabric of our societies, fuel economic and civil unrest, and cause international migration. At the very least, it may force the adoption of harmful or costly quick-fix remedies to ward off such disruptions.

Since much of the inequality is in terms of income, particularly earned income, paid employment is particularly important in combating inequality and poverty. The private sector has a central role to play in providing employment as a gateway to opportunity and to the reduction of poverty in the long term. However, the private sector cannot do everything. It is essential for developing and transition countries that the UN and, particularly organizations such as UNIDO, address the problems attendant upon globalization. In her Foreword, Clare Short strikingly describes the management of globalization equitably and sustainably as 'the challenge of our age'.

## **Dealing with globalization**

The process of economic globalization has accelerated greatly over the last decade. The liberalization of international and domestic trading environments, the growth in foreign

direct investment (FDI), rapid technological change and the geographic dispersion of production have all contributed to an increasingly integrated international system of production and trade. For all this, it must be noted that, in developed and developing countries alike, industrial investments are still financed predominantly from local savings, and most jobs still depend on demand in local markets.

Globalization has brought to developing and transition countries tremendous opportunities for trade, much larger inflows of FDI with its associated new technologies and skills, and improved market access. The industrialized countries—particularly the private sector—also benefit enormously from trade with developing and transition countries. The private sector undoubtedly plays a vital role in this process.

However, globalization also poses formidable challenges for most developing countries and economies in transition. It has highlighted the importance of a knowledge-based economy. Many developing countries are at a disadvantage when it comes to meeting competitive pressures. The uneven distribution of the economic benefits of globalization has also fostered a growing fear among low-income economies, particularly the least developed countries (LDCs), that instead of being integrated into the world economy, they may be marginalized.

Since the globalization process entails the integration of international markets for finance, trade and production, industry is an essential part of globalization. African countries and LDCs, in particular, because of various policy and structural weaknesses, have so far been unable to integrate fully—if at all, in many cases—into the global economy and enjoy its benefits. Indeed, evidence is growing that the global economic and industrial integration process, so vital for joining the mainstream of economic progress, is bypassing them. For these countries, because of market and government failures, industrial development is still far from being self-sustaining; continued support is critical to enable them to participate in and benefit from global competition.

These are the fundamental changes that have taken place in the global political and economic landscape. It is against this background that questions have been asked about the role and relevance of the UN system.

## **The role of the UN**

Globalization cannot and must not divide the world even further into the rich and the poor, those moving ahead and those left behind. Unless this powerful process is made to benefit all countries, it will not be sustainable. In that case we might soon be haunted by the spectres of the past—such as protectionism and trade wars—when we should be developing the promise of a prosperous future. The private sector has much to do with this future. The UN system has much to do with ensuring that developmental capabilities are built up to allow *all* countries to participate fully in the globalization process and enjoy its benefits. But it cannot do it alone. It needs to join hands with other players.

The UN system has an important role to play in reducing inequality within and between countries, and especially in devising policies to respond to the worst impacts of globalization and to meet ever increasing competitive pressures. The need for the UN is



hence greater today than ever before. Increasing globalization and the new, post-Cold War world landscape have indeed altered the development agenda, raised questions about the basis for multilateral cooperation and therefore posed serious challenges for the UN system.

These fundamental changes have also been behind recent calls for reform of the UN. There is no doubt that the UN system needs reform to reduce duplication, inefficiency and overlap and to ensure system-wide coherence and effectiveness.

However, reform of the UN is not only about cost cutting but also about making the Organization more responsive to new global realities. It is about UN agencies identifying and concentrating on their core competencies. It is, at the same time, about strengthening joint and collaborative action and partnerships to deal with the interrelated and multifaceted nature of development. It is about clearer delineation of mandate and of responsibilities, and for greater collaboration and coordination, particularly in the field. It is about being more responsive to its clients. But, most of all, it is about making a difference to the lives of so many who have so little.

In order to succeed, the arguments for reform of the UN system must be articulated around a clear and agreed definition of the stakeholders' needs, and become part of a single undertaking for world development. Such a process may be driven by a group of reforming Member States that coalesce beyond the boundaries of conventional regional or political groupings in bringing about effective and efficient reform. In this, Member States have an important role to play; expressing clear priorities, limiting political influence, ensuring substantive discussions at UN forums and ensuring that mandates are compatible and not infringed. This is not mere wishful thinking: UNIDO's experience with the development of its Business Plan—examined in Chapter 5—gives a flavour of the rewards that can be drawn from an approach of this kind.

The development debate should not be addressed in terms of polarities, such as peacekeeping *or* development, Bretton Woods institutions *or* the UN system, normative *or* operational activities, government *or* private sector. To better address development issues in general and poverty alleviation in particular a more constructive approach is needed, recognizing the synergies that exist between peacekeeping and development, between the Bretton Woods institutions and the UN system, between normative and operational activities, between the government and the private sector. In today's competitive world it is more than ever necessary to acknowledge that the world's inequalities will only be overcome through partnerships based on cooperation and mutual respect.

But there are still some who believe that international agencies such as the UN should have no role in development. Their argument has two basic strands. First, that development is primarily a private matter and should be left to the private sector and market forces. Thus, there is no effective role for public intervention. Second, that if there is a case for public intervention, it is only for national Governments acting alone or in concert on a voluntary basis, not for international agencies. This line of argument implies that international agencies cannot effectively address national development problems.

There is certainly a strong case for recognizing the vital role in development of market forces and the private sector on the one hand, and action by national Governments on the other. But important areas of development still require multilateral action

in the form of the UN. Globalization, and its manifestations of growing poverty, inequality and environmental degradation increase, rather than reduce, the need for the provision of 'global public goods'. By 'global public goods' we mean: 'global commons' such as a sustainable environment, peace and safety; the basic infrastructure of international economic relations; the furtherance of human rights, democratization, poverty reduction and humanitarian assistance; and the creation, adaptation and diffusion of knowledge. Equally important, the provision of global public goods means correcting market failures, as well as government and institutional failures.

These are some of the basics of the rationale for the role of the UN in development.

But to say that there is a need for the UN system is also to say that there is a need for its services to be provided efficiently, and with development impact and social equity. It is this line of reasoning that is the driving force behind UN reform.

This book examines the issue of UN reform from the perspective of development, particularly its economic and social aspects. It is not yet another recitation of the history of the UN and its various difficulties; it is intended as a thought-provoking contribution to the development debate, a challenge to the UN reform agenda and an invitation, through tight analytical and factual argument, to broader reform of the multilateral system. We offer the acknowledged success of UNIDO's transformation to show what can be done more widely and to share the lessons learned from it with those contemplating or undertaking similar reform efforts. We hope also that UNIDO's experience may provide some measure of inspiration and encouragement to others.

One theme permeates the whole of this book and provides its main thrust. In the words of the Swedish Minister for Foreign Affairs, Anna Lindh:<sup>2</sup>

We have a tendency to blame the United Nations for our own failures and shortcomings. In fact, when the UN fails, we fail. If the UN loses its relevance, we lose. There is no real alternative to global cooperation with increasingly global problems. For this, we need the UN—but a strengthened and reformed UN.

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<sup>2</sup>Speech delivered in the General Debate of the 54th session of the General Assembly of the UN, New York, 21 September 1999.

## Chapter 1

# The cases for reform

As the United Nations moves into the 21st century, it faces formidable challenges in adjusting to new political, social and economic realities. These are very different from those that prevailed when the UN was founded in 1945. True, many ideas and proposals for reforms, and for reforming the reforms, have been formulated, and actions initiated. But much remains on the agenda to be done. Indeed, reform is a continuous process of adjusting to changing realities for preventing war, protecting fundamental human rights, establishing conditions for justice and respect for international law, and promoting social progress with sustainable standards of living, as stated in the preamble of the UN Charter. Reform is a complex process, too, since actors in the international community have different political perceptions of the role of the United Nations.

Since the late 1960s more than fifty proposals for UN reforms, originating from both within and outside the UN system, have been put forward (see annex). Some of these have played a part in changing the system, while others have stimulated dialogue and influenced international public opinion without being formally adopted and implemented.

Most cases for reform have targeted the developmental role of the UN system, its proliferation of bodies, inadequate coordination between the UN proper and the specialized agencies, a lack of focus and inadequate impact. The system has been perceived to be supply-driven, and recipient countries have lacked the sense of 'ownership' that would have enabled them to identify with the assistance provided. Moreover, the system had become over-politicized, with diplomats and politicians, rather than professionals, in high-level positions. It has been alleged that UN programmes suffer from inter-agency turf battles. The consequent limited impact has led to dwindling support and funding. The cases for reform have often focused on incremental changes rather than radical reform.

Discussions on UN reform have often been passionate since they relate to much hope and expectation about peoples' life, security and welfare. They have been significantly influenced by the political, economic and social priorities among Member States — and these have changed over time. As we shall see, the bids to reform the UN have gone through five phases:<sup>3</sup>

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<sup>3</sup>For an in-depth analysis of the UN Reform Process, see: Joachim Müller, ed. *Reforming the United Nations, New Initiatives and Past Efforts*, vols. I-III, published in cooperation with the United Nations, Kluwer Law International, 1997.

- Initial reform efforts in the framework of the Cold War in the early 1960s focused primarily on organizational, financial and budgetary matters and were driven by concerns in the East about what was perceived to be a UN Secretariat dominated by the West.
- A new focus on development in the late 1960s and 1970s, with many newly independent States joining the UN, followed by growing North-South strains and the establishment of the Group of 77. Efforts were aimed at creating new bodies, increasing the efficiency of the system for implementing technical cooperation and the emergence of the UN as a forum for global negotiations on development, trade, industry and natural resources (Jackson Report, Gardener Report, Brandt Commission).
- New visions and criticisms accentuated the North-South differences during the 1980s, including changing United States policies (Heritage Foundation); calls for financial reform (Maurice Bertrand, Brundtland Commission); and emphasis on improving efficiency, streamlining and budget reductions (Group of 18).
- The end of the Cold War was accompanied by a rediscovery and even renaissance of the UN in the late 1980s and early 1990s. This new wave of enthusiasm for the UN led to further reform proposals (The Nordic Project, proposals by Brian Urquhart and Erskine Childers, Boutros Boutros-Ghali's Agenda).
- Following the emphasis placed on peace and security matters in the context of developments in Central and Eastern Europe and the demise of the former Soviet Union, in the early 1990s the South demanded a reassessment of the role and purpose of the UN. Reform proposals by the South Centre and negotiations for an Agenda for Development reveal a lack of common ground among Member States regarding the future role of the UN. Initial expectations in the security area proved unrealistic and there was a strong need for the UN to focus and prioritize its activities (Independent Working Group: Commission on Global Governance).
- The current reform agenda comprising, *inter alia*, a new proposal of the South Centre and a proposal by the industrialized countries through the Group of Seven (Nordic Project II and the European Union Proposals). This is followed by a 1997 by a proposal of the Secretary-General Kofi Annan for a structured and comprehensive reform effort.

All these reform proposals have one thing in common—the quest for cohesiveness and a clear sense of direction in a highly diverse system. The concern voiced by the stakeholders of the UN system focused on three main elements: (a) the balance between the normative and the operational role of the UN; (b) the alleged proliferation of the UN bodies and lack of coordination; and (c) the cost efficiency and effectiveness of the UN development functions.

A distinction needs to be made between the functional cases for reform and those based on the needs of the stakeholders. The former focus on improved functioning at an

organizational level in the context of the changing political environment. The latter are about adapting to the needs of developing countries and economies in transition in a changing world economic environment. While the former involve a debate among the stakeholders for improving the performance and functioning of the UN system, the need-driven approach involves mobilizing the support required by the recipient countries to meet their challenges and opportunities in the field of economic and social development.

It is essential for shaping the future of the United Nations to reflect on past UN reform efforts and to draw the lessons they offer. A proper assessment of the need for future reforms demands a clear understanding of the intentions of different groups of interests in this process.

### **The changing international political environment**

Since the United Nations was founded, five political and economic developments have had a particularly significant impact on the geopolitical structure and the role of the multilateral system:

- *The emergence of a bipolar world*, and Cold War between the West and the East, which had different views of the roles of the market and the state, and on how to foster the development of developing countries; aid flows from both the West and the East were motivated by a drive to gain and retain influence in the South.
- *The decolonization process*, mainly in the 1950s and 1960s, which altered the world political landscape by weakening the traditional European powers, and led to almost tripling the number of sovereign States and the emergence of political and economic powers in developing countries, as well as expanding and diversifying the need for multilateral development assistance to these countries.
- *The oil crises of 1973/74 and 1979 and the debt crisis of the 1980s*, which highlighted both the aspirations of the South for a greater share of world income and the difficulties they faced in financing their development, and which had important effects on the multilateral system, exposing its weaknesses and heightening calls for reform of the UN system.
- *The end of the Cold War in 1989/90* and the demise of the centrally planned political system in Eastern Europe and the former Soviet Union, which resulted in a drastic shift from a bipolar to a unipolar world, dominated mainly by the United States and to a lesser extent by other Western powers including the European Union and Japan.
- *The growing impact of globalization*. Already a factor in the security field—the UN was established because of the existence of nuclear weapons—globalization became predominant in the economic field in the 1970s with the emergence of transnational corporations (TNCs), the oil crisis, the rapid growth and

volatility of international financial flows, and the expansion of international trade following trade liberalization and technological breakthroughs, especially in information and telecommunications technologies.

## Uneasy consensus

An uneasy political consensus prevailed from the establishment of the UN in 1945 to the mid-1970s. It was based on an uncertain balance between the Soviet centrally planned economy approach, European social democracy, Third-World economic nationalism and Rooseveltian 'New Deal' policy.<sup>4</sup> This consensus granted an important role in economic development to Governments, emphasized minimum social and economic preconditions, and entailed national economic planning and regulations, as well as national self-reliance. The consensus permitted the UN system to build up considerable influence—without major competition from the Bretton Woods institutions—and to establish activities both in social fields and in economic development areas such as trade and industrial development.

In the 1950s and 1960s, many newly independent States concentrated on nation-building and gained increasing influence in the UN system and in global economic matters. Greater attention was placed on international economic cooperation, and the UN gradually emerged as a global political forum for North–South dialogue on the economic and social issues of the South. The first such initiative was the establishment of the United Nations Conference on Trade and Development (UNCTAD) in 1964. Subsequently, new development issues were taken up in such areas as industrialization, environment, energy and transfer of technology. UN development activities shifted towards these new development issues, but the impact on the economic progress of developing countries remained limited.

This prompted demands for more radical changes in the world economic system, such as fairer terms of trade and more liberal terms for financing development, in the context of UNCTAD negotiations between the developing countries—represented by the Non-Aligned Movement and the Group of 77—and the developed countries. The developed countries hesitated to support such reforms as the debate shifted towards the General Assembly and the specialized agencies where the South had gained greater influence.

The Non-Aligned Movement of developing countries argued for a declaration of principles for a *New International Economic Order*. This called for global redistribution of wealth and was adopted by the General Assembly in 1974. It was followed by:

- The adoption of the International Development Strategy for the Second United Nations Development Decade.
- The 'Lima Declaration' in which the developing countries aspired to attain 25 per cent of world industrial production by 2000.

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<sup>4</sup>James Paul, *The United Nations and Global, Social-Economic Policy, United Nations and Global Social-Economic Policy: Analysis* (<http://www.globalpolicy.org/Soceon/UN/analysis.htm> (1/17/00)).

- A new UN Centre for Transnational Corporations (CTC) which endeavoured to establish a 'code of conduct' for TNCs.

At the same time, the petroleum-producing developing countries had nationalized production and, through the Organization of the Petroleum-Exporting Countries (OPEC), succeeded in raising prices for oil. This led to a series of oil shocks for consumers in developed countries, followed by recession in Organization for Economic Cooperation and Development (OECD) countries. Similar aspirations became visible in discussions on raw materials and development. The developed countries expressed reservations but avoided open opposition, arguing that the proper forum for economic changes was the Bretton Woods institutions, where they held the balance of power.

### Shift in policy priorities

In the meantime, by the early 1980s, national policies in developing countries had increasingly shifted from inward-oriented towards outward-oriented policies, mainly because the viability of the former was limited, but also because of the growing forces of globalization. The consensus on the so-called global Keynesianism that had prevailed from 1945 started to ebb around 1980. The new governments in the United Kingdom and the United States, under Prime Minister Margaret Thatcher (1979–1990) and President Ronald Reagan (1981–1988), proclaimed new policies towards a reduced role of the State in the economy, and emphasized policies towards market-oriented private sector development within the framework of privatization, deregulation of markets and fewer government services. Many other Governments, first in the North and later in the South, changed their policy priorities in the same direction. A new era of refocusing the role of the State had begun.

These policy changes had implications for the UN system. The United Nations had had considerable success in a number of areas, such as decolonization. It also provided a world forum where conflicts could be resolved, or at least disagreements aired, and countries be held accountable for their conduct in international affairs.

There was, however, increasing criticism of the UN System. The South was disenchanted by the lack of progress towards global economic cooperation and greater social and economic equity. While developing countries deplored the 'ignorance of the minority', the developed countries ignored the 'tyranny of the majority'.<sup>5</sup> Disenchantment with the UN and criticism of multilateral development were quickened by the change of government in the United States; the Reagan administration emphasized unilateral rather than multilateral action.

The end of the Cold War in 1989/90 created hopes for a new beginning. The demise of the Soviet Union and the centrally planned economy approach in the wake of the collapse of the Berlin Wall in November 1989 marked a turning-point in geopolitics. The bipolar world became a unipolar one, dominated militarily by the USA, economically by

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<sup>5</sup>Joachim Müller, ed., *Reforming the UN*, vol. 1, p. 32.

a triad of the USA, Japan and the EU. These political developments were accompanied by a parallel shift in the UN, from crisis to opportunity, rediscovery and renaissance of the system. This enthusiasm stimulated further reform. Proposals had already been made by Mikhail Gorbachev (1987)—in the wake of *glasnost* and *perestroika*—towards addressing common problems of peace and security. Further, a certain euphoria emerged when President George H.W. Bush spoke of a 'New World Order' while preparing the coalition against Iraq in 1990. However, by 1993 it had become clear that the international community did not have a common understanding of the role of the UN in the post-Cold War period. The developing countries were deeply concerned about the low priority given to development cooperation issues. The low priority was partly because of the importance of peace operations and assistance to the new countries with economies in transition, and partly due to a parallel shift from 'aid' to 'relief'. The renaissance of the United Nations after 1989/1990 was almost exclusively based on its limited successes in the area of peacekeeping, and its resolution of a large number of regional conflicts.

Only limited results had been achieved in restructuring the UN in the economic and social fields. Indeed, development cooperation and human rights were given less and less importance. This turn of events stimulated renewed efforts towards designing a new vision for the UN.

### **Emergence of new partners**

Meanwhile, during the past decades new partners in development had been emerging. The weakening role of the State, policy changes towards privatization and private sector development, the increasing importance of TNCs, and the accelerated pace of globalization of industry, trade, finance and services gradually created new actors in the international development scene. To be effective in the economic and social fields, the UN system increasingly needed to work with *the private sector*, both as clients and advisers.

A related change occurred with regard to the rapid growth of a multitude of *civil society organizations*, institutions and informal movements outside the sphere of Governments—chambers of commerce, industry associations, cooperatives, industry branch organizations, women's groups, universities, and groups representing the interests of different sections of society in the social, developmental, humanitarian and other fields.

Such organizations had originally emerged in developed countries, but had become increasingly important in developing countries and also in transition economies, partly because of reduced confidence in national decision making. These organizations have gained increasing legitimacy and significant influence in many areas of development. They form a reservoir of human knowledge, skills and enthusiasm from which economic and social development can draw. They are increasingly viewed as an important forum for popular participation in decision-making and as a complement to the resources of Governments and official agencies, including the UN system. They are also seen as contributors to empowerment, decentralization, grass-roots development and new forms of participatory development, and as embodying the principle of subsidiarity—the lowest



and most decentralized level possible of institutional representation and action—and as increasingly important partners in the public–private sector dialogue on development. In short, they have added a new voice and fresh impetus to the development debate.

The UN system has increasingly involved these new partners of development in regional and global forums and in technical cooperation at the national level. While this has increased the degree of participation in international and national development efforts, it has also made the process of decision-making more complex. To some extent, these partners have also emerged as competitors to some of the activities of the UN system.

### **The role of the UN: normative vs operational**

Many reform proposals have raised debate on the *normative* versus the *operational* development functions of the multilateral system. The *normative functions* are intended to influence the perception and norms of actors in the international community within a specified set of international issues, while the implementation is left to these actors. Normative functions include being a forum of ideas, agendas and debate on issues of economic and political significance, setting targets and monitoring the performance of Member States. The *operational functions*, on the other hand, involve the implementation in recipient countries of decisions made by participating Governments.<sup>6</sup> In practice, any combination of the two functions is possible.

Policy advice and governance can be both a normative and an operational function, in the sense that it can be the last in a series of normative functions and the first in a sequence of operational functions. The two functions can then be mutually supportive.

Of importance to the UN reform process here is the fact that normative and operational functions place entirely different demands on the governing structure of an international organization. The fulfilment of normative functions requires universal participation and formal equality among all participants. In the course of time, the organization should adjust to a greater number and a greater diversity of actors, in order to ensure support for new normative functions.

Organizations with operational functions, on the other hand, require a structure and a management culture which promotes decision-making capabilities, as they will be judged on their effectiveness in achieving objectives with the resources at their disposal. The degree of participation must be made compatible with the demands of a decision-making system aiming for efficiency and effectiveness. Moreover, there must be a formal organizational hierarchy, with clear division of authority from political bodies to professional managers, and clearly defined criteria of success.

There are thus fundamental differences between the governing structures required for normative and for operational functions—what may be an organizational strength for normative functions can become a liability for operational functions. The functions of an international organization must, therefore, be compatible with its governing structure

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<sup>6</sup>Helge Ole Bergesen and Leiv Lunde, *Dinosaurs or Dynamos? The United Nations and the World Bank at the Turn of the Century*, London: Earthscan Publications, 1999, p. 3.

and, at the same time, its governing structure must be supportive of the functions of the organization. If a mismatch develops, the organization will run the risk of malfunction, in either its normative or operational role, or both.

As long as an international organization remains either normative or operational, organization problems are easily rectified. However, when an organization endeavours to perform both normative and operational functions at the same time, problems related to the governing structure may emerge. Such a mixture is quite common in the UN system. With a blending of the two functions, in the course of time the required reorganization may become frustrated, with governing structures that may become untenable.

While the comparative advantage of the UN system originated in a structure devised for normative functions, the organization has increasingly moved towards operational functions, where such structures can be more a liability than an asset. The more diversified the system becomes, in the sense of having more organizational entities and assuming more operational functions, the more complicated the implementation of general decisions becomes. This can be compensated, to some extent, by managerial efficiency. Most reform proposals have attempted to solve this problem by introducing coordination centres with the appropriate authority. However, these moves have largely failed, because such an approach contradicts the political and bureaucratic forces of the system—the insistence of Member States on the principle of equality, the absence of intergovernmental agreement and coordination, and the vested interest of bureaucracies.<sup>7</sup>

## **How the UN's normative functions evolved**

From a very early stage in the UN's history it was obvious that the United States and the major European countries did not intend to create a global supranational organization. National issues that required international cooperation and coordination would be dealt with through institutions which were controlled by the superpowers and which reflected the prevailing political power structures. The most normative institutions—the IMF and, to a certain extent, the World Bank—were not part of the UN proper.

The West never seriously considered providing the UN with a major normative function such as determining the development agenda, nor even a regulatory function in the field of international trade. The formal requirement of universal participation and equality—one nation, one vote—as the primary decision-making principle in the UN (in the General Assembly and in the Economic and Social Council (ECOSOC), for example), reduced from the very beginning the scope for the UN to assume the major normative function for which it was presumably best equipped. However, there were exceptions in such fields as decolonization and human rights.

The developing countries increasingly used the UN as a global platform for voicing their concerns about socio-economic development. They had secured a majority in all the main UN bodies for economic and social development, and thereby achieved a common identity. Independently of the UN, they had become organized into a Non-Aligned

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<sup>7</sup>Bergesen and Lunde, *op. cit.*, pp. 91–92.

Movement and the G-77. Ever more frequently, they used the UN, first, as a means of obtaining greater financial transfers from the developed countries, and second, in new UN institutions such as UNCTAD, to vote in a more concerted, and gradually also a more confrontational, way. In contrast, their influence in the Bretton Woods institutions—which had a major normative role, especially the IMF—was rather limited.

The reaction of the developed countries to the increasingly confrontational demands for redistribution of global wealth was a hesitant and passive resistance. Led by the United States they adopted a defensive attitude in UN fora, and deliberately transferred any issue that was strategically important and required international coordination to the Bretton Woods institutions, where they enjoyed the balance of power because of the way the voting system was weighted.

The developed countries pursued two strategies. First, they initially resisted demands for the establishment of potentially important UN agencies dominated by developing countries; for example, in 1960 they established the International Development Agency (IDA) under the World Bank umbrella instead of a Special UN Fund for Economic Development (SNFED) sponsored by developing countries. Second, they accommodated the rising demands of the developing countries for increased development assistance principally in order to gain political influence in those countries.

In spite of rising aid budgets for operational functions throughout the 1960s, the dispute over the normative functions, especially in the field of development cooperation, remained on the agenda of the UN. Meanwhile, the UN increasingly found itself looking at a tripolar world made up by the West, the East and the South. However, well-established specialized agencies, such as the International Labour Organization (ILO), the World Health Organization (WHO) and the United Nations Educational, Scientific and Cultural Organization (UNESCO), were still seen as quite successful in the area of norm-creating functions. Other parts of the UN normative institutional machinery were not. Furthermore, the expenditures of the normative-functional agencies of the UN and the norm-creating parts of WHO and UNESCO accounted for less than 7 per cent of the UN system's total expenditure of the UN system.<sup>8</sup>

## Quest for a new economic order

The efforts of developing countries to extend the normative functions of the UN were reinforced by the drive of the G-77 and China for a *new development paradigm*, as expressed in the New International Economic Order (NIEO) of the 1970s, in a range of UN forums: the Annual Session of the General Assembly and ECOSOC, where the G-77 and China enjoyed a majority; UNCTAD, which had emerged as an effective platform for the developing countries and as a catalyst of the NIEO; and the governing bodies of UN funds, programmes and specialized agencies, where the South endeavoured to add substantive arguments for the NIEO. Among the specialized agencies was UNIDO,

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<sup>8</sup>Maurice Bertrand, Some Reflections on the Reform of the United Nations, Joint Inspection Unit, Geneva (JIU/REP/95/9), 1985

where the G-77 and China succeeded in getting a resolution adopted—against the votes of the developed countries—calling for a \$300-million fund for industrial development to be managed by developing countries. The atmosphere in UN forums in the 1970s became one of polarized confrontation over global economic issues.

Yet the quest for an NIEO by the G-77 and China eventually failed, in spite of increased aid flows and developing countries' growing share of world industrial production. Most of the demands of the NIEO remained unfulfilled—global decision-making structures, stabilization of commodity prices, system-wide improvements in market access and other, more specific, demands. Conversely, the attempts to obtain a NIEO led to a decline in support for the UN from the developed countries, particularly the United States—which rendered the UN less able to perform global normative functions.

The confrontation culminating in the NIEO decade ended in a stand-off between North and South, with the North losing confidence in the UN system's ability to handle economic and social issues on its behalf.

### Backlash against multilateralism

Political decision-makers in the United States went even further, questioning the very concept of multilateralism and its translation into government policies, largely on the basis of a study published by the *Heritage Foundation* (1984).<sup>9</sup> The thrust of the report was that the politicization of the UN increasingly prevented the Organization from achieving, even partially, the goals stipulated in the Charter.

The report addressed two important issues: economic development and the environment.

- *Economic Development.* It suggested that the NIEO had replaced the original development mandate of the UN. Nationalization had taken place and property rights over patents, trademarks and technology had been questioned. It also contended that many projects encouraged planning and government policy intervention, rather than private market-oriented activities, and that 'eliminating the United Nations development activities would make very little aggregate difference to economic development in the developing countries.'
- *Environment.* It suggested that international decision-making was inappropriate, that national concerns should be dealt with by each country individually, and that 'regional compacts or conventions, no doubt, would develop to meet larger geographic, transboundary concerns.'

In other areas the report recommended that the technical agencies of the UN should focus exclusively on technical matters and not on the NIEO; the function of the General Assembly should be reduced and 'not be allowed to pose as a legitimate and impartial global forum.' It went on to say that if these recommendations were not adopted the United States Government should consider withdrawing from the UN. This would, in the

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<sup>9</sup>*The World without a United Nations: What would happen if the United Nations shut down?*, Heritage Foundation, Washington, DC, 1984.

authors' view, create an opportunity to design a new system of international cooperation. The report concluded 'that a world without the United Nations would be a better world'.

This stance contrasted sharply with that of the *Marc Nerfin Report* (1985)<sup>10</sup> which, after evaluating the UN and its specialized agencies, including UNIDO, argued that 'the world as we know it would not have been possible without the UN.'

The recommendations of the Heritage Foundation Report were largely adopted by the Reagan administration, and found echoes elsewhere:

- The United States withdrew from UNESCO in 1984; the United Kingdom followed. This was partly because of allegations of mismanagement in that organization, and partly because of a proposal for a New World Information and Communications Order, which was seen as an attempt to control the free press.
- The Food and Agriculture Organization of the United Nations (FAO) was also criticized for alleged politicization and mismanagement.
- Criticism of the UN intensified over its efforts to establish a code of conduct for TNCs, and codes for infant food formula, pesticides and toxic chemicals, and transfer of technology.
- The United States administration also refused to sign the Law of the Sea Convention which had been agreed earlier.
- With regard to the management of the UN, the United States Government criticized a lack of transparency and accountability in budget matters, excessive documentation, technically deficient and biased management, duplication and questionable financial management practices.

Other areas of concern were the North–South dialogue, under the aegis of UNCTAD, and global negotiations, beneath the umbrella of the UN. Because of the confrontational attitude it had adopted, the United States often found itself on the defensive and being outvoted even though other developed countries had some of the same concerns. However, the United States was prepared not only to voice concern, but also to push for action.

The major donor countries saw the North–South confrontation as an exercise in futility, and the South could no longer oppose the efforts of the developed countries to reform the UN—even though developing countries considered these efforts to be against their own interest. In the post-NIEO vacuum, a search was initiated for new normative functions of the UN which would be attractive to the developed countries, such as sustainable development.

## **The Brundtland Commission: sustainable development**

These developments prompted new approaches to reform through the World Commission on Environment and Development, the so-called Brundtland Commission

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<sup>10</sup>Marc Nerfin, *The Future of the United Nations System: Some Questions on the Occasion of an Anniversary*, November 1985.

(1987).<sup>11</sup> It addressed issues 'on our common future', and underlined the need to ensure that new approaches to sustainable development had a chance of succeeding.

The Commission argued that environmental and development issues should be considered together on a global scale. Sustainable development, to be achieved in both the North and the South, meant 'ensuring that development meets the needs of the present without compromising the ability of future generations to meet their own needs.' First, population growth should be in harmony with the changing productive potential of the ecosystem (giving economic and environmental sustainability). Second, the poor should be guaranteed a reasonable share of resources, and new economic growth patterns should be promoted to alleviate poverty (giving social sustainability). The Commission specifically recommended that international bodies and agencies should ensure that their operational activities encouraged sustainable development.

Altogether, the Brundtland Commission report was timely and contributed to an increase in the attention given to environmental issues in international forums. Many Governments, particularly in the developed countries, had already introduced environmental programmes and policies. The ensuing international interest in environmental issues led to the United Nations Conference on Environment and Development (UNCED) in Rio de Janeiro in 1992. This Conference approved Agenda 21 and three conventions, on climate change, bio-diversity and desertification. Of overwhelming importance was the fact that the concept of sustainable development was now accepted and assumed a central role in the activities of the United Nations. This entailed new alliances within the UN system—of UNIDO, the United Nations Development Programme (UNDP) and the United Nations Environment Programme (UNEP)—and a new momentum for environmental issues, which led to important new normative functions, in the shape of the Montreal and Kyoto protocols.

The normative functions of the UN system, which were envisaged in the early stages of its existence—such as providing global forums on economic and social issues—had been suppressed during the Cold War because of lack of political consensus and the growth of operational activities for development. The end of the Cold War, therefore, raised hopes for a new beginning of the UN normative functions.

## **The South Commission: poverty and human needs**

The developing countries recognized that they shared many problems and experiences, but also that there was a lack of initiative from the South itself to examine these issues, draw lessons and take action.<sup>12</sup> The *South Commission* (1990)<sup>13</sup> stressed that the

<sup>11</sup>*Our Common Future*, World Commission on Environment and Development (Brundtland Commission), 20 March 1987.

<sup>12</sup>The lack of initiative from the South should be viewed in the context of the summit meetings of the non-aligned countries after 1961 where there were repeated proposals for UN reform. The Non-Aligned Movement, however, has always spoken in favour of a reinforcement of the UN and has therefore agreed to forgo an institutionalisation of the movement: the UN should be and remain the field of activity and platform of the non-aligned countries.

<sup>13</sup>*The Challenge to the South*, South Commission, May 1990.

aspirations of developing countries to advance their development efforts had not materialized. Widening disparities between North and South were compounded by intensified globalization, while the easing of East–West tensions had led to fears that resources would be shifted from the North to the East and that the South would be further marginalized. The vision of the Commission emphasized an undivided world, economically and politically, in which the primary concerns were overcoming poverty and satisfying basic human needs. The Commission underlined that prospects for the development of the South hinged on its improving its relationship with the North—while noting that international economic relations were unfavourable to the South in view of the existing world distribution of wealth.

These problems were compounded by the North's new demand to attach priority to environmental protection in relation to development objectives. This issue was complicated by two facts. First, that poverty itself was a major cause of environmental damage in the South—a problem that could only be overcome by economic development. Second, that environmental effects were transmitted from the North to the South through trade in raw materials intended for the affluent consumer lifestyle of the North. The South Commission therefore called for a renewal of the North–South dialogue and negotiations on restructuring world economic relations. Priority, it said, should be given to reform of the international financial and trade system, based on multilateralism and non-discrimination and with the object of promoting sustainable development in the Third World. A programme was formulated to revive economic growth in the South and to move towards a restructuring of the international system in the fields of science and technology, the environment, global commons, development and the United Nations.

Among the South Commission's key recommendations were the following:

- A link should be established between total international aid and aid for science and technology.
- A regime should be established to provide for the transfer of relevant technology from the North on terms consistent with the development interests of the South.
- UNIDO, UNESCO, the International Atomic Energy Agency (IAEA) and the United Nations University (UNU) should build up a scientific infrastructure with a view to contributing to scientific and technological progress in the South.
- International regimes for the exploitation of global commons such as Antarctica and outer space should be established.
- An international regime for energy should be established, minimizing disruptive fluctuation in supply and prices, and providing for a fair allocation to developing countries of exhaustible energy resources.
- The South should be assisted to develop substitutes for fossil fuels and to adopt techniques for conserving energy.

In the post-Cold War period, the Commission visualized the emergence of a new system which would entail the 'radical transformation of the existing arrangements

consistent with the goals of democracy, equality and equity in international relations'. In the absence of such a transformation, the South feared that the existing multilateral system would be adapted to new requirements of the North with limited or no significance for the South. However, in spite of all these efforts the hopes and aspirations of the South, so forcefully advocated in the South Commission's report, were not heeded. Development issues of the South were accorded low priority in the North because of the importance attached to security and reconstruction efforts in the economies in transition as a result of the new spirit of cooperation in the Security Council.

During the 1990s a number of global conferences organized by the UN and representing the essence of its normative function brought the development dialogue back on the international agenda. These conferences were focused on key issues of common interest to the developed and developing countries such as sustainable development, children, human rights, social development and the role of women. Undoubtedly the dialogue associated with these global conferences has created not only stronger awareness and common understanding of key social, economic and humanitarian issues among key stakeholders but also established detailed plans of actions and commitments to be implemented by the major actors in developed and developing countries. As such they have formed an important part of the UN's global norm-setting role especially in the economic, human and social areas. At the same time these conferences and their related activities have contributed to the central advocacy function of the UN in the above-mentioned areas.

## **Evolution of the UN's operational functions**

The suppression of the UN's normative functions during the Cold War gave increasing scope for operational activities in support of development. The post-colonial movement accelerated the proliferation of new development actors. Many new UN organizations and bodies in the field of development assistance were established, especially from the mid-1960s, in line with the rapid growth in aid transfer to developing countries. Operational development functions had been assumed by a wide range of UN bodies—specialized agencies, regional commissions, functional commissions, secretariat bodies and financing schemes.

In 1965, the General Assembly decided to merge the Expanded Programme of Technical Assistance (EPTA) and the Special Fund (SF) into the *UNDP*, which was expected to become the main coordinating body for financing UN operational functions. Many different UN bodies created institutional capacities for their operational functions, by means of funds made available through UNDP (and its predecessors) and other sources. The big four specialized agencies—the FAO, UNESCO, the ILO and WHO—expanded their development activities significantly. UNIDO was created in 1967.

Even in this early phase of development cooperation, problems of coordination and the politicization of the legislative bodies of the specialized agencies tended to influence their performance and even threatened the legitimacy of some of these agencies. In response, a number of coordinating bodies were established:



- The Committee for Programme and Coordination (CPC) in 1962 as a subsidiary organ of ECOSOC and the General Assembly for planning, programming, evaluation and coordination.
- The Committee for Development Planning (CDP) in 1964, comprising experts appointed to consider and evaluate the programmes and activities of the UN organs in the field of economic planning and projections.
- The Joint Inspection Unit (JIU) in 1968, entrusted with powers of investigation in all matters related to efficiency and the proper use of funds and with ensuring better coordination between organizations.

The period from 1970 to around 1990 saw a further rapid growth of development aid, in terms of Official Development Assistance (ODA) flows to developing countries. This happened in spite of the growing confrontation between North and South, criticism of the UN, and the lack of progress towards reforming the UN system. The growth in resources for development channelled through the UN system did not reflect political convergence between donors and recipients. Rather, it was the result of careful lobbying by the developing countries, the Cold War, whose protagonists were motivated by the desire to secure political influence in the South, and more genuine aid motives, mainly from the Nordic countries. The main features of ODA flows to the South can be summarized as follows:<sup>14</sup>

- The period 1955–1992 saw a strong and growing support for total development aid (ODA) through the UN system. After this it stagnated and then declined, primarily because of aid fatigue.
- In spite of the rapid growth in UN development assistance, the total remained modest compared with other development assistance channels. In 1995, the total net flows of financial resources through the UN amounted to \$4.2 billion, considerably less than those of the EU (\$5.3 billion—in grants), Japan (\$10.4 billion), and Germany (\$4.8 billion).
- Net ODA, as a percentage of the gross national product (GNP), in 1998 exceeded the 0.7 per cent target set for individual countries by the General Assembly in 1970 only for Denmark (0.99 per cent), Norway (0.91 per cent), the Netherlands (0.80 per cent) and Sweden (0.72 per cent). These countries were all among the top twelve donors in absolute contributions. The corresponding average for all DAC countries was only 0.24 per cent.

The UN's operational development functions expanded correspondingly:

- The number of staff in the UN proper rose from 31,000 in 1974 to 47,000 in 1994, operational activities in the field accounting for most of the increase.
- From the 1970s, an increasing number of UN funds and programmes, such as UNDP, the World Food Programme (WFP), the United Nations Population Fund (UNFPA), the United Nations Children's Fund (UNICEF) and the Office

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<sup>14</sup>OECD, Development Assistance Committee (DAC) Annual Report, various issues.

of the United Nations High Commissioner for Refugees (UNHCR), expanded their institutional cooperation machinery, which was spreading worldwide, inevitably leading to overlap. By 1995, the number of field offices worldwide had reached 1,125.

- From 1980, much of the growth in assistance channelled via the UN was in the form of contributions earmarked for specific purposes, as donors wished to increase their control of UN funding and activities.
- The importance of non-UN multilateral donors increased, primarily because of the growth of the resources of the EU and the multilateral development banks.

Despite fundamental disagreement between North and South on development issues, a convergence of interests took place in the area of multilateral development assistance, which may be explained by the Cold War-dominated aid motives mentioned above. This resulted in the growth of organizational layers in the UN system. After five decades of growth, the UN development system<sup>15</sup> today comprises the following main institutional categories in the areas of economic, social and human rights:<sup>16</sup>

- Nine main Committees and treaty bodies reporting to the General Assembly.
- Seventy-three functional commissions, standing and expert bodies and regional commissions under ECOSOC.
- Twenty-one programmes, subprogramme, organs and funds.
- Eighteen specialized agencies, subsidiary agencies or autonomous bodies affiliated to the UN system.

Thus the UN development system came to comprise as many as 125 legally independent entities. The more institutions were created, the more bodies were needed to coordinate them. The fragmentation of the UN development system commenced very soon after its establishment and, in spite of stated intentions of coordination from the very beginning, the UN system has never had an effective and sufficiently powerful coordinating body.

## Early reform proposals

### *THE JACKSON STUDY*

The first major reform effort in this area was proposed in a study on *Capacity of the UN Development System* (1969) by Sir Robert Jackson.<sup>17</sup> It contained a set of recommendations to rationalize the UN development system, in particular UNDP, ECOSOC, and

<sup>15</sup>Broadly defined here as those parts falling outside the sphere of the Security Council and the International Court of Justice. For the full structure of the UN, see Annex.

<sup>16</sup>Partly based on *An Agenda for Development: 1995*, Boutros Boutros-Ghali, United Nations, New York, 1995.

<sup>17</sup>Sir Robert Jackson, *Capacity of the United Nations development system*, 1969.

coordination between agencies. UNDP was to act as the coordinating body of development assistance, while ECOSOC would become a policy centre for development and coordinate the activities of the specialized agencies.

The plan to establish UNDP as the central financing institution for technical assistance of the UN system had limited success, and its role as the centre for funding and coordination declined. Nor was the recommendation to transform ECOSOC into a policy centre taken up. The specialized agencies showed little enthusiasm for reduced independence. Member States also showed limited interest, and their own delegations in various UN governing bodies suffered from a lack of coordinated positions on key issues.

### *THE GARDNER REPORT*

A new reform effort was made in 1975 when the developed countries agreed to establish a group of 25 experts which was to make recommendations as to how the UN system could be adapted to meet the development needs and aspirations of the developing countries. These issues were addressed by the Gardner Report (1975),<sup>18</sup> which expressed concern about the fragmentation, proliferation and multiplicity of UN organizations, the need for consensus through new consultative procedures, revision of voting rights in the Bretton Woods institutions to reflect the interests of developing countries, improving working methods, decentralization, coordination, and efficiency. The report called for structural changes in the UN related to the General Assembly and ECOSOC, for the establishment of a United Nations Development Agency (UNDA), and for new consultative procedures to help Governments to implement agreed solutions. It also contained suggestions for the replacement of UNCTAD by an international trade organization.

The General Assembly, in 1975, merely took note of the recommendations of the Gardner Report, but subsequently the report was considered by a newly created Ad hoc Committee on the Restructuring of the Economic and Social Sectors of the United Nations. During the period in which this Committee was active, significant differences existed among member States. The proposed reforms of the administrative system revealed a conflict of interest between developed and developing countries.

Unlike in earlier discussions of the Jackson Report, the developed countries, particularly the United States, were concerned about the prospect of a strong, consolidated UN development system, and felt that a more fragmented UN development system would increase their influence.<sup>19</sup> As a result, the recommendation of the Gardner Report to establish a UNDA was not adopted. The General Assembly, after consultation and debate, adopted the recommendations of the Ad hoc Committee in 1977. Yet by then the recommendations of the Gardner Report had been substantially diluted in the political process of the Ad hoc Committee of the General Assembly. Overall, the political compromise reached in 1977 represented a vivid example of a half-hearted attempt at UN reform.

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<sup>18</sup>A *United Nations structure for global economic cooperation*, Gardner Report, 1975.

<sup>19</sup>Joachim Müller, ed., *Reforming the UN*, vol. 1, p. 32.

## THE BERTRAND REPORT

In the mid-1980s a report by Maurice Bertrand (1985)<sup>20</sup> for the JIU reiterated many of the recommendations of the Jackson and Gardner Reports. This report was even more critical with regard to waste, overlapping functions, inefficiency and lack of impact in the field. It suggested that coordination efforts since the late 1970s towards joint planning, country programmes, field coordination and an integrated approach to development had produced no results. The report further recommended that ECOSOC—enlarged from 27 to 54 members in 1973—should be replaced by an Economic Security Council comprising no more than 23 members from the larger developed countries and with limited geographical representation.

With regard to the coordination of operational functions, the report recommended the establishment of a single, interdisciplinary development agency responsible for agriculture, industry, health and education, and, further, that this agency should have integrated operations and offices in various regions and subregions. This recommendation was significant in that it implied a restructuring of all the operational activities of existing bodies such as UNDP. The report received extensive publicity and widespread attention both within and outside the UN system, but the official response was lukewarm. While the main recommendations were considered rather utopian within the UN system, the report served as an important input into the work of the Group of 18 (see below).

## BOUTROS-GHALI'S AGENDA

In 1992, the Secretary-General, Boutros Boutros-Ghali,<sup>21</sup> emphasized the lack of coordination between the specialized agencies and the UN and also stressed the link between peace and development. In this connection, he argued that growing peace-keeping activities should not be accommodated at the expense of development. He further suggested that the ACC should act more definitely to guide the work of specialized agencies and that ECOSOC should be strengthened. The enthusiasm for a stronger UN system, however, was ambiguous and there was little room for implementing drastic proposals.

In response to the concern that had been expressed at the downgrading of development issues in favour of peace and security concerns, and as a complement to the UN Agenda for Peace, an Agenda for Development was prepared and issued by the Secretary-General in May 1994.<sup>22</sup> The Agenda considered five dimensions of development: peace as the precondition for development; the economy as an engine of progress; the environment as the basis for sustainability; justice as a foundation of society; and democracy as good governance. It assigned an indispensable role to the UN in implementing a new collective development vision which gave cause for optimism that the main actors for development would be integrated.

<sup>20</sup>Maurice Bertrand, op. cit.

<sup>21</sup>*Empowering the United Nations*, Boutros Boutros-Ghali, Secretary-General of the United Nations, December 1992.

<sup>22</sup>*An Agenda for Development*, Secretary-General, United Nations, New York, 6 May 1994.

In essence, the agenda, which was normative in character, provided an example of reform efforts going on inside the UN. However, in contrast to the very concrete proposals contained in the Agenda for Peace, the Agenda for Development focused narrowly on principles and contained little resembling a practical implementation strategy.

In discussions at ECOSOC in 1994, the developing countries expressed disenchantment at the absence of an action-oriented blueprint in the Agenda. In their view, focus on economic growth, and commitment on the part of developed countries to provide resources for development were both missing. The developed countries, on the other hand, emphasized the role of market orientation, human rights, environmental sustainability and democratic systems for development. While it was acknowledged that the UN controlled only a fraction of the resources available for development, it was also stressed that the Organization had a unique advantage in normative global consensus-building.

### **The UN Charter: hindrance and asset**

One of the main reasons for the lack of successful reforms can be traced back to the Charter—first, because of its vagueness and second, because it had not been implemented. The original agreements between the UN and the specialized agencies contained provisions (in Article 58) for coordinating the promotion of the economic, social and cultural objectives of the Charter, including administrative coordination and coherence. Yet large parts of these agreements have never been put into practice. Radical reforms were perceived as politically unfeasible, since UN reform debates revealed a lack of political consensus to make changes to the Charter and related constitutions, which would have required a two-thirds majority, and which could have been vetoed by any of the permanent members of the Security Council.

The vagueness of the Charter, however, had a positive aspect: the flexibility of its regulations enabled the Organization to adapt itself to international changes and to take on new areas of responsibility without altering the Charter.

As a result of divergent political attitudes, most reform proposals were made within the existing Charter, and hence were piecemeal and incremental rather than radical. However, even without constitutional change reforms could have been more effective in terms of coordination, cooperation and functional consolidation, if all the provisions of the Charter had been implemented and if government policies in the UN system as a whole had been harmonized. This did not happen; instead many countries spoke with different voices in different legislative bodies of the UN system because of lack of coordination within their own Governments. As a result, the aspirations of the South were diluted.

### **Financial crisis**

Most observers identified the lack of development impact in the developing countries as an important element of the case for reform. Attempts had been made to strengthen the coordination of the UN development function in the field through country programmes,

integrated programming and coordination at the country level, but little progress had been made. Also, recipient countries felt a lack of ownership in development cooperation.

These developments led to a series of financial crises in the UN system during the 1980s. Apart from political disagreement, the main cause was the United States' criticism of the UN, which led Congress' call for the reduction of the United States' contribution from 25 per cent to 20 per cent of the annual budget of the UN or of any specialized agency which did not adopt a voting system on budgetary matters weighted according to the contribution of each Member State.

However, the introduction of a system of weighted voting would require an amendment to the Charter and could only be adopted if the smaller member countries forfeited their influence on the budget. Such a change would also have reduced the influence of larger countries, such as the Soviet Union and China. The so-called Kassenbaum legislation led to part of the United States contribution to the UN budget being withheld, and to other countries withholding their assessed contributions for peacekeeping, thus precipitating a financial crisis. As the UN was not permitted to borrow from the commercial market, the Organization endeavoured to cope through organizational reforms, administrative economy measures, staff reductions and programme and budget reforms. The developing countries criticized the withholding of funds by the United States—which became strategically stronger through accumulated arrears—and argued against weighted voting, which they considered to be against the very principles of the Charter, which was based on the sovereign equality of all Member States. While the United States defended the withholding as a policy practised by other countries, the Soviet Union and European countries joined in the criticism, but supported the budgetary cuts, emphasizing the need for improvements in cost efficiency.

### **Tackling the budget: the Group of 18**

The financial crisis and the widespread quest for change resulted in the establishment of the Group of 18; the task of this group was to take a long-term view of economy measures and new decision-making mechanisms for budgetary matters that would satisfy both the few large-scale contributors and the majority of Member States.

The report of the Group of 18 in 1986<sup>23</sup> made a number of recommendations related to the intergovernmental machinery, the structure of the Secretariat, personnel policies, monitoring and evaluation, and budgetary procedures. Emphasis was placed on a leaner Secretariat, less top-heavy, less complex and less fragmented, more productive and more efficient. The main breakthrough was a new budget process which gave more influence to the CPC in budgetary issues and broadened its representation; this did not imply weighted voting but it did give *de facto* veto rights to each member of the CPC. Other recommendations of the Report were, to a large extent, restatements of previous proposals for administrative reform. The report was approved by the General Assembly

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<sup>23</sup>'Emphasis on improving efficiency', Group of 18 1986.

in 1986 by consensus, which was seen as a major achievement. The negotiations on reform towards improved efficiency, through a reduced budget, revealed a striking convergence of interest between East and West in many areas.

However, the developing countries considered the new budget process a threat to the principles of the Charter that related to the adoption of General Assembly resolutions, the principles of sovereign equality and majority decision making. While the consensus was seen by many developing countries as unconstitutional and as granting *de facto* veto rights in budgetary matters to major contributors, the South finally agreed on the proposal in the expectation that the United States would pay its assessed contributions in full. The reforms had been implemented swiftly and were largely complete by the end of 1989. The United States resumed payment of part of its assessed contributions, and paid part of its arrears. The reform process had reduced the amount of confrontation, especially between East and West, and led to a greater convergence of views on administrative matters. The United States' Representative characterized the 1989 General Assembly as 'one of the most constructive and realistic within memory', and even went as far as to describe the UN as 'a useful place'.

### **Pragmatic adjustment: the Childers-Urquhart proposals**

The renewal of the United Nations system was increasingly being viewed within the context of the economic and social functions of the UN and their relationship to the root causes of instability and conflict. In response to a request by a representative group of ambassadors to the United Nations and in preparation for discussions envisaged for the 50th anniversary of the UN in 1995, two former senior staff members of the UN—Erskine Childers and Brian Urquhart—prepared a study on renewing the UN system.<sup>24</sup> Rather than proposing radical reforms, they adopted a pragmatic approach, concentrating on transformation which could be introduced within the framework of the Charter and within the constitutions of the specialized agencies. Their study drew attention to limitations of past reforms which were due to such factors as the appointment of government nominees with inadequate skills to top positions, reshuffling of the organizational chart without greater coordination, lack of guidance from legislative bodies and the absence of programmes for staff training. Moreover, it emphasized that earlier efforts at reorganization had not adequately discharged responsibility for the right organizational unit to the right post. The report recommended a consolidated budget for the United Nations, which should be adopted by the General Assembly.

The authors had endeavoured to prepare a practical proposal for gradual reforms which were politically feasible, but their recommendations were largely ignored by the governing bodies, though their concerns remained valid.

Overall, administrative reforms succeeded in reducing staff and introducing economy measures in various parts of the organization. However, progress in a number of important areas was limited:

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<sup>24</sup>Erskine Childers with Brian Urquhart, *Renewing the United Nations System*, 1994.

- Organizational reforms were undertaken primarily by reshuffling boxes in the organizational chart, which was a zero-sum game and did not lead to greater coordination or effectiveness.<sup>25</sup> A conceptual framework for organizational restructuring of a multilateral organization appeared to be lacking.
- The programmes and budgets of various organizations were originally presented separately, but later combined in consolidated programmes and budgets for each organizational body. However, the combined programme budget lacked transparency and accountability. Recommendations for a consolidated programme budget for the whole UN Development System in the mid-1990s were not approved.
- In its early decades, the Organization had succeeded in mobilizing and associating world-renowned intellectuals in the economics and social fields. Later, however, it became evident that many Member States viewed the UN Secretariat as an area where they could gain political influence and control activities by installing their own nationals in senior positions. This reduced the effectiveness of the system and the organizational capability of various units in the system. The absence of programmes for staff training only compounded the problem.

### **Major recent reform proposals**

The case for reform was incomplete. As concerns about the insufficient coordination and impact of the UN system grew, the issue of its governance came to the fore. In the early 1990s, proposals for reforming the system multiplied and related political negotiations—above all within the General Assembly—intensified. As mentioned earlier, the debate, which still goes on, has been driven by a complex set of determinants and objectives, including:

- The desire of some of the major donor countries (led by the United States of America) to improve the UN system's effectiveness and efficiency by streamlining its operations — which, in turn, would reduce their financial contributions to multilateral development.
- Countervailing attempts by the developing countries (expressed through the Group of 77 and China) to safeguard a strong UN system with sufficient capacity to support economic and social development in the South amidst the challenges of globalization.
- Efforts to improve the coherence, complementarities and coordination of the UN system's development activities, particularly at the country level, and to define the balance between the normative and operational activities of UN organizations (primarily a concern of the Nordic countries).

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<sup>25</sup>Erskine Childers and Brian Urquhart, *op. cit.*



The following are some of the more noteworthy current proposals for UN reform<sup>26</sup> which, in various ways, dominated the intellectual and policy debates in the 1990s and are likely to influence the UN reform agenda in the years to come. Only their most important action-oriented recommendations are summarized here.

### THE NORDIC PROJECT

Launched at the end of the 1980s, the Nordic UN Reform Project (referred to henceforth as the Nordic Project) published its conclusions and recommendations in 1991.<sup>27</sup> Presented jointly by the Governments of Denmark, Finland, Norway and Sweden, it provided the foundation for a series of reform initiatives by the Nordic countries (both collectively and individually).<sup>28</sup>

One of its key conclusions was that 'a stronger sense of partnership and willingness to reform needs to be fostered among the UN's members'. The report focused on issues of governance of UN system operations on the one hand, and on improved system-wide coordination on the other. The ultimate goals were to reduce duplication of effort and to enhance transparency and accountability within the UN system.

In another document<sup>29</sup> it was pointed out that 'the Charter of the United Nations did not foresee an operational role for the United Nations in the economic and social fields, and it provides little guidance on distribution of powers and responsibilities.'

In the area of *governance*, the report recommended:

- Creating an *International Development Council* as a high-level forum to provide policy guidance and discuss system-wide development issues in the broader context of a rationalized and more effective ECOSOC.
- Putting *one senior official in charge* of economic and social matters in the UN Secretariat.
- *Limiting membership* in the governing bodies of operational UN funds and programmes to around twenty countries (elected by different regions) in order to improve decision-making.
- *Extending the UNDP's analytical capacities* beyond its core mandate to act as a central funding mechanism. The object was not to enlarge the role of the UNDP in project execution but to improve the conceptual underpinning of key development issues (for example through the Human Development Report).

As regards better coordination of *operational activities*, the proposals advanced by the Nordic Project set the agenda for many years to come, particularly where they

<sup>26</sup>Excluding Childers and Urquhart (1994), which has been analysed earlier, for substantive reasons.

<sup>27</sup>*UN Reform Issues in the Economic and Social Fields. A Nordic Perspective*, 1991.

<sup>28</sup>The Project was taken up again in 1996 in the context of General Assembly negotiations on strengthening the UN system; see further below.

<sup>29</sup>Nordic Memorandum of Reform of United Nations Governance and Finance, 22 June 1992.

concerned the UN's specialized agencies.<sup>30</sup> Their traditional analytical and normative roles were seen as having been eroded by an unfocused expansion of their operational activities—driven primarily by the availability of project funding. The specialized agencies were thus called upon to strengthen their analytical and normative roles, define their core competencies and areas of focus, and place more emphasis on 'upstream' activities such as policy advice and sectoral analyses. The specialized agencies were identified as being best placed to deal with the emerging environmental agenda in terms of negotiating, monitoring and supporting the implementation of international conventions and treaties. In a nutshell, the most appropriate role of the UN specialized agencies was that of centres of excellence rather than merely as executors of projects.

The Nordic Project also strongly argued for the establishment of a unified structure for UN system operations at the field level. As we shall see, this issue resurfaced in the mid-1990s and led to the streamlining and harmonizing of the UN system's operational activities.

### *THE COMMISSION ON GLOBAL GOVERNANCE (1994)*

The Commission was established to contribute towards improving global governance in an emerging 'global neighbourhood'.<sup>31</sup> Governance was seen as going beyond purely governmental actors to encompass interaction among the institutions, processes and people which together constitute society and through which public and private bodies and individuals manage their common affairs. The Commission's point of departure was an increasingly complex world in which the private sector and civil society were becoming more and more powerful as agents of development within the context of economic globalization.

Adopting the common values of democratic principles, the rule of law, human rights, liberty and integrity, the Commission endeavoured to reconcile global institutions with a more inclusive and democratic framework for global governance. Its recommendations included an integrated framework for governance functions based on the principle of subsidiarity at the global, regional, national and local levels; that is, action is to be taken always at the lowest and most decentralized level possible.

A summary of the Commission's report was submitted to the 50th session of the General Assembly, but its main recommendations were not translated into action. The most far-reaching ones, such as the reform of the Security Council and the creation of an Economic Security Council, did not immediately command a consensus and would have required lengthy negotiations.

Others, such as the convening of an annual Civil Society Forum, were found too cumbersome and have anyway been rendered irrelevant by a progressive integration of

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<sup>30</sup>The Agencies at a Crossroads. The Role of the United Nations Specialized Agencies' (a study commissioned by the Nordic UN project, Report No. 15:1990).

<sup>31</sup>The Report of the Commission on Global Governance was published under the title 'Our Global Neighbourhood'. The summary of action proposals was also issued in 1995 as a General Assembly document under the symbol A/50/79. The Commission was co-chaired by Ingvar Carlsson and Shridath Ramphal.

Civil Society Organizations (CSOs) into the work of individual UN organizations. Finally, the call to review the case for dismantling a number of UN organizations and bodies (such as ECOSOC, the Regional Commissions, UNCTAD and UNIDO) was not based on a solid analysis of their functions and was therefore considered unacceptable by most countries. It did help, however, to trigger reform efforts in the UN organizations affected. In UNIDO, early reform efforts gathered momentum around 1995 and led in 1997-1999 to the transformation of the organization, which will be analysed in detail further on.

### *THE INDEPENDENT WORKING GROUP*

As the Commission on Global Governance had done earlier, the Independent Working Group on the Future of the United Nations<sup>32</sup> focused on issues of political and global governance, and on the complex interplay of economic, social, cultural and political factors in conflict prevention and peace building. The Group saw national sovereignty being weakened by the globalization process and attributed to the UN an important role in supporting developing countries in their efforts to adapt to this process.

In the field of economic development, it recommended the establishment of an *Economic Council* as a principal organ of the UN system. This Economic Council—as a counterpart to an expanded Security Council and a proposed Social Council—was to integrate the work of all UN agencies and international institutions engaged in economic issues and, supported by an Advisory Committee drawn from academia and the private sector, was to promote the global harmonization of macro-economic policies.

Ultimately, the Group's report, which was submitted to the General Assembly in 1995, received little attention and has not had any significant impact on the UN reform debate.

### *THE SOUTH CENTRE*

While acknowledging the imperative of increasing the UN system's efficiency and effectiveness, the South Centre's report of 1996<sup>33</sup> expressed concern over the erosion of the UN system's pluralist and democratic character. It also asserted that underfunding and understaffing were progressively weakening key functions of the UN system. In particular, the report identified a diminution of the UN organizations' role in supporting economic development. Large industrialized countries were seen as aiming to divest the UN

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<sup>32</sup>The Independent Working Group on the Future of the United Nations was co-chaired by Moeen Qureshi and Richard von Weizsäcker, former Presidents of Pakistan and Germany, respectively. The project was sponsored by the Ford Foundation with the Secretariat located at Yale University. The Working Group's report was issued in 1995 under the title 'The United Nations and its Second Half-Century'.

<sup>33</sup>The South Centre, which in 1995 became a permanent intergovernmental organisation of developing countries, prepared a contribution to the economic agenda of the Non-Aligned Movement (NAM) which was submitted to the 11th NAM Summit in Cartagena, Columbia, October 1995. The final report was issued in 1996 under the title 'For a Strong and Democratic United Nations. A South Perspective on UN Reform'.

of its policy and research capacities in the economic sphere—an integral element of a strategy to strengthen the Bretton Woods institutions and the WTO as the lead agencies in matters of economic development. The report criticized the shift of UN resources towards humanitarian and peacekeeping activities as undermining the capacity to contribute towards economic development. It perceived the danger that the UN system would turn away from long-term development issues towards short-term issues of political instability and humanitarian crises.

Among the main recommendations of the South Centre Report are:

- Strengthening the financing of the UN through a revised system of assessed contributions (with a 12.5 per cent ceiling for country contributions), a gradual reduction of voluntary contributions, and the introduction of international levies and taxation.
- A more representative Security Council without veto rights and with no permanent seats.
- Enhancing the research and policy-making roles of the UN, allowing better policy coordination at the global level.
- Democratizing the governance and improving the transparency of the Bretton Woods institutions.

### *NORDIC PROJECT II AND THE EUROPEAN UNION PROPOSALS*

The first phase of the Nordic Project (reviewed above) was followed up in 1996. This second phase culminated in a report on *The United Nations in Development*.<sup>34</sup> In parallel, the EU reform proposals were formulated at the beginning of 1997 as an input to the debates of the General Assembly Working Group on the Strengthening of the UN System. The EU proposals reflected many of the concerns of the Nordic countries and, taken together, the two sets of proposals greatly influenced those put forward later by the Secretary-General (see below).

The EU reform proposals<sup>35</sup> explicitly recognized that the UN remains the central framework for multilateral cooperation aimed at credibly addressing global issues. The key challenge they identified was that of ensuring sustainable development and poverty reduction amidst an increasingly competitive global economy, with special emphasis on the needs of the least developed countries. It was explicitly stated that ‘reform of the United Nations is not about cost-cutting: it is about strengthening and revitalizing the organization to effectively meet the challenges of the future.’

<sup>34</sup>The Nordic UN Reform Project 1996 in the Economic and Social Fields. *The United Nations in Development, strengthening the UN through Change: Fulfilling its Economic and Social Mandate*. The report was also issued as a UN General Assembly document under the symbol A/51/785 of 27 January 1997.

<sup>35</sup>‘Proposals of the European Union for Reform of the United Nations System in the Economic and Social Areas’ (submitted to the UNGA Working Group on the Strengthening of the UN System), January 1997.

The double role of the UN system was considered to require first, agenda setting and the establishment of globally agreeable norms (which demanded strengthening inter-governmental processes) and second, operational activities in the field (which called for more coherence among the activities of UN funds and programmes).

The following reforms were proposed:

- Appointment of an Under-Secretary-General (USG) for economic and social cooperation and development issues.
- Merger and reorganization of three UN Departments: Department for Economic and Social Information Policy Analysis (DESIPA), Department for Policy Coordination and Sustainable Development (DPCSD) and Department for Development Support and Management Services (DDSMS).
- Unified representation of the UN at the country level, with clear authority given to the UN Resident Coordinator; stronger emphasis on joint priority-setting, programming and implementation of activities; and the establishment of common UN premises.
- ECOSOC to fully exercise its envisaged role as the coordinating body of all UN funds and programmes, and to be convened in a more flexible manner.
- Better cooperation between the UN agencies, the Bretton Woods institutions and the WTO.
- New and innovative sources of funding to be identified, and the savings made as a result of UN reform to be reallocated to strengthening UN development activities.
- UN specialized agencies to concentrate on their normative and guideline roles, with operational activities to rest on comparative advantage criteria.

While fully supporting these reform proposals, the Nordic Group, in its own recommendations, put a stronger accent on integration within the UN system. This related, first of all, to the country level, where it not only urged the definition of a common policy framework and the identification of a limited number of joint priorities but also advocated in the long term a 'unified UN development system'. This was to be backed up by 'functional consolidation' at the level of UN funds and programmes.<sup>36</sup> The UN specialized agencies should cooperate closely with the funds and programmes and, again, should serve as centres of excellence focusing primarily on their normative tasks.

### *THE ANNAN PROPOSALS*

In July 1997, UN Secretary-General Kofi Annan presented his own reform proposals to the General Assembly. They acknowledge the persisting gap between the huge action agenda in front of the UN system on the one hand, and the limited resources available

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<sup>36</sup>An 'eventual consolidated structure' of all operational funds and programmes is considered the ultimate goal.

on the other. They also underscore the need for a political consensus among Member States if the UN is to be effective and to make a difference. In his words:

The fundamental objective of this reform is to narrow the gap between aspiration and accomplishment. It seeks to do so by establishing a new leadership culture and management structure at the United Nations that will lead to greater unity of purpose, coherence of efforts and agility in responding to the pressing needs of the international community. Reforming the machinery of the United Nations is no substitute for the willingness of Governments to use the Organization, nor can it, by itself, bridge the very real differences in interests and power that exist among Member States.

Reiterating the concerns of many earlier reform proposals, the Secretary-General identified rigid, fragmented and sometimes duplicative organizational structures as sources of institutional weakness and ineffectiveness. His reform proposals were broken down into two types of measures (often referred to as two 'tracks'):

- Those under the direct jurisdiction and authority of the Secretary-General.
- Those within the jurisdiction of Member States and thus requiring their approval (e.g. the structure and functioning of intergovernmental bodies).

The most salient reform proposals directly related to the UN system's developmental activities in economic and social fields are selectively summarized below.

In areas within his direct authority, the Secretary-General, *inter alia*, proposed the following changes, which have since been implemented:

- Reconfiguration of the UN Secretariat's management structure into four main clusters with an executive committee for each: peace and security; humanitarian affairs; economic and social affairs; and development operations. These are complemented by a cross cutting theme: human rights. The executive committee on development operations is convened by the UNDP Administrator and has come to be known as the *UN Development Group* (UNDG). Its membership comprises 15 UN entities. The Heads of the four main UN entities — UNDP, UNFPA, UNICEF and WFP—constitute the Executive Committee.

Consolidation of three economic and social departments of the UN Secretariat itself (DPCSD, DESIPA and DDSMS) into a single *Department of Economic and Social Affairs* (DESA).

- At country level, a gradual move toward *single UN offices* under the Resident Coordinator with a view to facilitating greater cooperation and coherence (the 'UN House' approach, as piloted in South Africa).
- Establishment of *UN Development Assistance Frameworks* (UNDAF), in close consultation with Governments, with common objectives and priorities for development support from UN organizations. UNDAF is intended to make the UN more coherent at the country level through a participatory approach focusing on a limited number of issues and representing a balance between national priorities and international development goals where the UN has a comparative advantage. UNDAF has thus become a vehicle for the integration of the

work of the UN specialized agencies and for better coordination with the Bretton Woods Institutions.

Action taken by the Secretary-General in these areas was endorsed by the General Assembly in a resolution passed on 12 November 1997. The current reform of the Secretary-General has been able to build on and strengthen this momentum. Its achievements will be reviewed in 2001 by the Triennial Comprehensive Policy Review of Operational Activities to ascertain the political support of Member States for the UN reform.

The following more far-reaching proposals were put forward for the approval of Member States:

- Creation of a post of *Deputy Secretary-General* with the primary responsibility of overseeing the *coordination of multi-sector activities and programmes*. The Deputy Secretary-General has also become responsible for coordinating UN reform efforts.
- Strengthening the role of the *General Assembly* by giving it the task of providing more focused *strategic guidance* to the work of the UN.
- Consolidating and streamlining ECOSOC's subsidiary machinery, and strengthening ECOSOC's capacity to engage in discussion of macro-economic coordination issues.
- Improving the *governance of UN funds and programmes* through joint committees and through joint meetings of their governing bodies.
- Creation of a *Development Account* to be funded from administrative savings.
- Review of the Regional Commissions' role within a reformed UN.
- Launch of a Special Commission, at ministerial level, to examine the possibility of changes in the UN Charter and in the treaties from which the specialized agencies derive their mandates.

While the last proposal in particular—to instigate a fundamental review of the role of the specialized agencies—remains a controversial and unresolved issue, other more specific proposals—such as the new Deputy Secretary-General post and the Development Account—were approved by the General Assembly in a resolution passed on 19 December 1997.

## The main themes of reform

As we have seen, the many proposals for UN reform vary greatly in their aims and scope. What emerges quite clearly from our overview, though, is that—apart from grand political designs such as those relating to reform of the Security Council or the possible launch of a new Economic Council—the debate has centred on *the strongly perceived need to improve coherence, coordination and cooperation within the UN system*. This has been one of the main themes sounding through reform proposals addressing the UN's support programmes for developing countries—what is customarily referred to as 'operational

activities for development'. The discussion has gravitated from issues of structural reorganization to issues of functional harmonization.

Within this area of the discussion, the country or field level has attracted most attention. In the second half of the 1990s more changes were made to the operational modalities of UN development support than in the preceding several decades. The notion of organizing and harmonizing UN system development programmes around jointly identified objectives and priorities (the so-called programme approach) received a strong boost from the establishment of UNDG, the strengthened Resident Coordinator system, and UNDAF as a new instrument.

- With regard to the specialized agencies, the debate has come to be about their positioning within a spectrum ranging from norm setting on one side to technical cooperation (TC) project implementation on the other. Should they be more an adviser or more a service provider, more normative or more operational, more upstream or more downstream? To put it in a nutshell, should they be political or action organizations? The answer given to these questions obviously has a number of implications, including for the structure and functioning of governing bodies: the more action-oriented and operational an organization's mandate is, the more also its governing bodies must be geared towards taking 'actable' decisions and adjusting to changing conditions. Many of these issues will be taken up again in chapter 4.

The analysis in this chapter has emphasized the political nature of most cases for UN reform, and the diverging political motivations for reforming the multilateral system—which, unresolved, delivered a less than wholehearted effort to adjust the system, without actually reforming it.

There had been two original perspectives on reform.

The view of the North was incremental, focusing on restructuring, streamlining and reactivating the organizations of the UN to make them more cost-efficient, effective and accountable to member States. The North had earlier suppressed normative functions of the UN, rejected negotiations for far-reaching changes in connection with the NIEO, and opposed radical restructuring of the world economic system. Regulatory policies and the establishment of international norms were considered counterproductive. Moreover, the North, especially the United States, was in favour of private-sector development and increasingly against a dominant role for government in economic development. These attitudes gained support through the budgetary reduction which followed the election of a Republican majority in the United States Congress, and through declining ODA flows from developed countries in the 1990s.

- The more revolutionary aim of the South was to make the UN more responsive to the aspirations of the developing countries for economic and social development and to improve the institutional mechanism for assistance through operational activities. The South favoured a dialogue on new development issues in the fields of trade, industry, finance, technology and social development, and felt that progress could be achieved only through stronger global cooperation and a new collective vision of development.



While the concept of sustainable development came to be recognized, and indeed assumed a central role in the activities of the UN, the aspirations of the South have clearly not been fulfilled and success in restructuring the economic and social activities of the UN system has been limited. On the eve of the end of the Cold War the South feared that the North's new priorities, such as energy and the environment, while essential, would have little impact on their development prospects. In the period immediately after the Cold War, the South argued that the increased priority of the reconstruction of the new countries with economies in transition should not be at the expense of UN development assistance to the South. During the remaining part of the 1990s, the UN exhibited positive achievements, particularly due to the holding and follow-up of major UN global for a and conferences and related advocacy functions on such diverse issues as promoting the human and sustainable dimension of development, ensuring gender equality, protecting human rights, advocating the right to development, fighting poverty and improving governance. Moreover, the convergence among most, if not all, key stakeholders on key issues and themes, promoted mainly by the UN, represents a major achievement for the organization.

A third and more nuanced view, inspired by the Nordic countries and adopted by the EU, recognized real *needs* for reform and the incompleteness of most cases for reform.

Divergent political views constrained efforts to establish an effective coordination mechanism for the UN system which would have led to increased efficiency, effectiveness and relevance. Closer cooperation between the Bretton Woods institutions and the other parts of the UN system was frustrated by the preference of the North, particularly the United States, for working through the former because of their system of weighted voting, and the preference of the South for dealing through the latter. The UN reform process was further complicated by the apparent lack of a conceptual framework for organizational restructuring of the normative and operational functions of a multilateral organization.

A consensual approach has been, and is, prevalent, in the UN negotiating process. The upshot is only those proposals that meet the least resistance tend to be accepted. This has inhibited the more radical reforms, which would require adjusting the Charter and achieving agreement among a heterogeneous range of UN members.

As a result of limited real reform, the UN system has not been in a position to play its full role in the economic and social development of developing countries as envisaged in the Charter. Coherence within the system and effectiveness at the field level remain insufficient. This, in turn, has resulted in missed opportunities for mobilizing the full development potential of the South, which has become much more heterogeneous because of impressive economic development in a few countries, particularly in East Asia and Latin America.

There has been no lack of ideas on reform; what has been missing is political consensus and a concerted will, between East and West, North and South, and donors and recipients. Some proposals have led to reform in some areas of the UN; others have stimulated dialogue and influenced the opinion of the majority against the policy priorities of the few, yet failed to be formally adopted and implemented. New reform proposals often

restated old ideas which had not been implemented, but were still valid. Undoubtedly the numerous reform efforts reflected the growing number of complicating factors in international development cooperation—globalization, private-sector development, the emergence of new partners in development, declining ODA flows due to aid fatigue (though not universally), and also to the expanded and more diversified needs of developing countries and economies in transition for multilateral assistance.

Eventually, under these constraints, an element of ‘reform fatigue’ crept in. Most of the reform proposals that were adopted were piecemeal, incremental and limited, in spite of a wealth of ideas and a series of concrete proposals for reforms and for reforming the reforms. The reform agenda for the UN at its 55th Anniversary was, therefore, larger than ever before. There is a need to review critically that agenda and to identify successful reform processes within the UN system in order to use them as models for other agencies to emulate.

### *Annex*

#### **The UN reform dossier**

##### *Summary of major proposals, 1969-1996<sup>37</sup>*

- Failed attempt by Nikita Khrushchev (1961) to replace the position of Secretary-General with a troika representing the major power blocs.
- Early reform blueprints, such as Sir Robert Jackson’s Capacity Study (1969), on which the United Nations development system is founded, and the famous Gardner Report (1975).
- Eight reports by renowned personalities or international commissions headed by them: Lester Pearson (1969), Willy Brandt (1979), Olof Palme (1982), Gro Harlem Brundtland (1987), Julius Nyerere (1990), Shijuro Ogata and Paul Volcker (1993), Shridath Ramphal and Ingvar Carlsson (1994), and Moeen Qureshi and Richard von Weizsäcker (1995).
- Position papers of the United States Government, including the Carter Administration (1978) and the Clinton administration (1996 and 1993), and of the G-7 summit meeting (1996).
- Proposals from the conservative Heritage Foundation of the United States (1984, 1985) contrasted with those of third-world organizations such as the South Centre (1992, 1996).
- Proposals from government officials, diplomats and experts, including the following: Maurice Bertrand (1985), member of the Joint Inspection Unit of the United Nations; Marc Nerfin (1985), former staff member of the United Nations; Peter Wilenski (1991), Ambassador of Australia to the United Nations; and Gareth Evans (1993), Foreign Minister of Australia.

<sup>37</sup>Joachim Müller, ed., op. cit.

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- Proposals of the Group of 18 (1986) covering budget, finance and administration.
  - Historic article by Mikhail Gorbachev (1987) redefining the relationship between the Soviet Union and the United Nations—a prelude to the end of the Cold War.
  - Reports from non-governmental organizations, including the United Nations Association of the United States of America (1988), the Stanley Foundation (1991), the North-South Roundtable (1991) and the Canadian Committee for the 50th Anniversary of the United Nations (1995).
  - Three famous studies by Sir Brian Urquhart and Erskine Childers: the Leadership study (1990), *Reorganization and Strengthening of the United Nations* (1991), and *Renewing the United Nations* (1994).
  - Government-sponsored initiatives, including the Nordic Project (1991) supported by four Nordic countries, and the Stockholm Initiative on Global Security and Governance (1991).
  - Records of the summit meeting of the Security Council on international peace and security (1992), held after the end of the Cold War for the first time at the level of heads of state.
  - Important reports issued by the Secretary-General of the United Nations, including *An Agenda for Peace* (1992) and *An Agenda for Development* (1994), which provide the foundation for recently implemented reforms.
  - Recent proposals emanating from intergovernmental committees of the United Nations on Security Council reform (1996) and the strengthening of the United Nations (1996).

## Chapter 2

### The need for reform

The case for reforming the UN is a strong one. It has been argued that the system is uncoordinated, with a proliferation of bodies and weak articulation between it and its specialized agencies. This has led to overlap, duplication and waste. In the field, programmes have suffered from lack of coordination, coherence and focus. Much of its work has often been driven by the staff rather than by the countries. Accountability has been weak, and member countries have not generally felt ownership of their programmes. Donors have cut the (already meagre) resources they allot to the UN, as its weaknesses have become more apparent. Some fifty proposals have been made for UN reform since 1945, but few of them have been implemented.

Some argue that it is not worth pursuing the reform agenda further, because the UN and the international community generally have no role to play in the emerging economic environment. Three arguments might be used to support this view:

- First, there is no need for any international agency in development: bilateral aid, technology flows, globalization and liberalization provide for all development needs.
- Second, there may be a need for international agencies, but it can be fully met by agencies such as the World Bank or regional development banks.
- Third, there may be a need for the UN, but its agencies are unable to respond efficiently because of their inability to reform. The UN should therefore return to its original 'normative' role and leave development to other institutions.

The arguments against a role for international agencies in development fall essentially into two categories. The first say that development is a purely private matter, with no role at all for public intervention. The second say that it does require public intervention, but this is best done by national Governments, acting singly or jointly, but on a voluntary basis (as in bilateral aid).

The first category eschews any influence by government apart from that of providing security, legal structures and the minimum public goods that private markets cannot

supply. The second is based on the view that multilateral organizations are essentially incapable of helping with national development problems. This may be because there are no 'global public goods' that call for such organizations or, if there are, multilateral institutions as constituted cannot provide them.<sup>38</sup>

Both approaches are mistaken. Economic development is not, and cannot be, a purely private matter that is best left to untrammelled market forces: there are too many imperfections in free markets and institutions for this to be so. There are many global public goods that must be provided, and their provision is best undertaken multilaterally. Certainly there is a strong, perhaps growing, role for market forces, national Governments and bilateral action, but there remain some critical elements of development that call for international action. In other words, there *is* a need for the UN system and so also a need for its reform. Current technical change, globalization and liberalization increase rather than reduce the need for global public goods. In essence, there is a very real need for international institutions in development.

Current technological developments are indeed enormously promising: they can raise productivity in all activities, including traditional ones that provide the main sources of livelihood in developing countries. New technologies also diffuse across countries rapidly, and the process that embodies the diffusion—what has come to be known as 'globalization'—has immense dynamism and a long reach. Countries that have been able to utilize these developments have managed to leap from low, stagnant incomes to modernity and high standards of living.

If globalization could spread the benefits of new technologies universally with no need for public policy apart from removing barriers to free trade and investment, there would be but a small economic role for international institutions like the United Nations. But this is not the case. Recent economic trends show large stresses in the international political economy, with growing inequalities and divergences. Many poor countries, and poor groups within countries, are becoming marginal players, facing low rates of growth, and are unable to reap the benefits of new technology.

These trends are unacceptable. Evidence on the enablers of economic progress—skills, investment and technological effort—does not suggest that inequalities will reverse themselves automatically. On the contrary, there appear to be cumulative forces at work that may perpetuate inequities unless coherent and purposive action is taken. There is, in other words, a critical role for the providers of 'global public goods', the international community, to help those at risk of exclusion. This means going beyond poverty alleviation programmes into building the ingredients of growth—the skills, capabilities and institutions needed to use new technologies and compete in world markets. The UN system, with other institutions, has to help developing countries to do this. The next section outlines the new context for economic and industrial development and leads to the case for 'global public goods'.

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<sup>38</sup>The general argument applies not just to the UN system but to all international organizations, including the Bretton Woods institutions and many others (Frei, 1998).

## The key role of technical progress

The changes sweeping the world economy are prompted by rapid technical progress. Technical progress leads to shrinking economic space, growing trade and the increasing globalization of information, finance, technology and production. It is facilitated by—and in turn raises pressures for—policy liberalization and institutional change.<sup>39</sup> The actors that increasingly dominate economic life, led by large transnational corporations, increasingly demand transparency, predictability and level playing fields to deploy their resources. Production location is being determined less by natural resources, cheap labour and protected markets and more by the skills, capabilities and modern infrastructure needed for using new technologies.

While the international economy is more closely knit together by trade and investment, the impact is, however, very uneven. Most economic activity (production and research) still centres on the 'Triad' of North America, Europe and Japan. Apart from these, there are some dynamic newcomers, but they are few; the rest of the world remains largely excluded from the dynamic vortex of technology-based growth and internationalization.

Technology is also a key force behind competitive advantage. New technologies affect all manufacturing and service industries, making it imperative for every country to raise its abilities to access and deploy such technologies. So broad and far-reaching are the developments that analysts highlight the role of new pervasive 'general purpose technologies' (David, 1989, Bresnahan and Trajtenberg, 1989) or see the emergence of a new technological 'paradigm' (Freeman and Perez, 1988). This involves a myriad of minor innovations around a few major breakthroughs that originate new trajectories and gradually pervade the whole economy. It also entails not just new production technologies in the traditional sense but also new management forms, different enterprise linkages, closer relations between industry and science, and the intensification of information flows between economic agents. These technological changes are transforming international economic relations: patterns of trade and comparative advantage, flows of capital, technology and people, generation and ownership of information and property rights.

While the main locus of technological dynamism is the industrialized world, developing countries are not insulated from technical change. All activities, even traditional ones, must use new technologies if they are to compete. For instance, a low-tech activity like clothing manufacture for export now has to cope with demanding quality requirements, along with frequent changes in design, rapid turnaround and timely delivery. To meet these needs, developing country firms have to invest in sophisticated design, sewing, cutting and pattern-making equipment and skills, as well as in advanced logistics and communications. This applies not just to export activity but also, increasingly, to production for the domestic market: with import liberalization, reaching world levels of 'best practice' in technology becomes vital for survival here.

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<sup>39</sup>That globalization, investment flows and rising trade also owe much to purely political factors, in particular the end of the Cold War, should also be borne in mind, though this aspect is not analysed here.

This is not the only challenge. The structure of activities also has to shift from traditional activities to those based on more advanced technologies to sustain high growth driven by constant technical progress. The US National Science Foundation (NSF, 1998) shows that technology-intensive manufacturing activities such as electronics, advanced machinery or pharmaceuticals are consistently growing faster than other activities. This is as true of developing countries with large industrial sectors as of advanced OECD countries. The recent performance of the USA also shows that the 'new economy'—technology-intensive manufacturing and services—is becoming a powerful engine of growth. Despite the hyperbole surrounding parts of the new economy, and the instability in the market prices of many high technology firms, there is little doubt that the current technology revolution, in the broader sense, is real and pervasive.

While all countries need to use more advanced technologies, innovation remains centralized in developed countries. However, technology diffuses internationally more rapidly than before, and development requires that other countries must build their capabilities to absorb and adapt new technologies. These capabilities are very unequally distributed, and the skills and Research and Development (R&D) that underlie them are growing more concentrated over time. At the advanced end the transmission of technology is concentrated in a small number of the TNCs that dominate R&D in industrial countries. This makes it increasingly important for developing countries to attract FDI. In fact, many valuable new technologies are simply not available for sale without direct equity investment by the TNCs that own those technologies.

Partly as a result of the growing technology-intensity of trade and production, TNCs are increasing their role in the world economy. As UNCTAD (1999) shows, they account for growing shares of global production and trade. With falling transport and communication costs and more liberal FDI policies, TNCs are also integrating their production systems and rationalizing their distribution across national boundaries. Countries that are able to participate in such global systems, such as Mexico or Malaysia, are able to raise output and exports rapidly in complex manufacturing activities. However, much of the developing world is outside these integrated networks. FDI is highly concentrated and export-oriented FDI even more so. As a result, TNC-based activity is accentuating national disparities rather than reducing them.

### **The rise of market-based capital flows**

FDI and other market-based financial flows increasingly dominate external resource flows to developing countries. The role of concessional aid (ODA) has diminished steadily, from 50 per cent in 1990 to 15 per cent by 1997. This has been partly because of growth in market-driven commercial loans, portfolio investments and FDI, and partly because of falls in the real value of ODA. Market-driven flows are as concentrated as FDI, benefiting a few countries much more than others. The short-term component of such flows can be highly volatile, and, as the Asian financial crisis shows, can be very destructive even to strong and well-managed economies.

In the five most affected economies (Malaysia, Indonesia, Thailand, the Republic of Korea and the Philippines), net private capital flows from abroad went from plus \$97 billion in 1996 to minus \$12 billion in 1997 (World Bank, 1998). While FDI stayed relatively stable, portfolio investments fell by \$17 billion and bank loans by \$83 billion. Thus, the globalization of financial markets showed a hard and dangerous edge, with lessons that were widely discussed at the time but are now in danger of being forgotten.

Policy-setting in developing countries has changed greatly in recent years, from widespread government intervention and participation in economic life to a greater orientation towards free markets and the private sector. While a significant part of this shift is due to disillusionment with import-substitution strategies on the part of national Governments, external pressures have played an important part. The most powerful agencies promoting policy liberalization have been the World Bank and the IMF, through their stabilization and structural adjustment programmes, operations and general policy advice. Many bilateral aid agencies and regional development banks have supported them.

At the level of international agreements, a series of regional trade agreements and, most importantly, the Uruguay Round of the General Agreement on Tariffs and Trade (GATT) (now the WTO), have set the scene for freer trade and investment flows. The confluence of these various agreements and pressures form the new 'rules of the game' for international trade, investment and technology transfer, all tending towards free-market-determined resource allocation and a 'rules-based' trading system. The setting for economic development has thus changed dramatically in recent years. How has it affected development prospects? Has its enormous productive potential worked for the benefit of the poor countries and levelled the playing field?

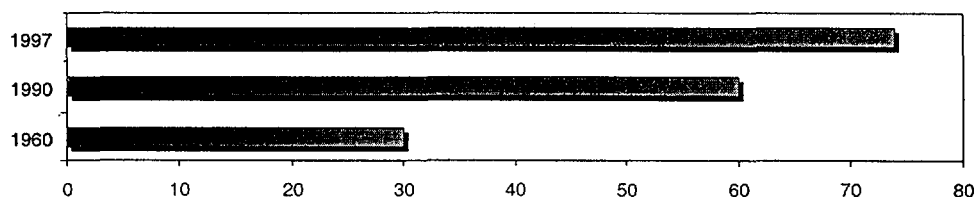
## **Growing disparities**

The emerging world order is accentuating disparities between countries and within them (by income levels, wages, skills and gender). Three billion people have no access to sanitation, 2 billion no access to power, and 1.3 billion no access to clean water. Women and children are the worst affected by the lack of sanitation and safe water. The World Bank admits that 15 per cent more people live in poverty in the developing world than ten years ago. In 2000, some 1.6 billion people are estimated to be living on less than \$1 per day, the yardstick of absolute poverty, and 3 billion on less than \$2 per day. Some regions, like Asia, have done better than others in reducing absolute poverty, but the numbers involved are still unacceptably large. Poverty has risen significantly in parts of Africa and Latin America, while the financial crisis has partly reversed the gains in Asia.

Income inequalities between countries are rising. The richest and poorest countries have grown further apart, even when incomes are adjusted for purchasing power differences (see figure 1). It is only been between the richest countries and some of the middle-income ones that some income convergence has taken place. Per capita incomes in the G7 countries was 20 times that of the poorest countries in 1965; in 1997 it was 39 times as high.



**Figure 1. Per capita incomes: how they compare**  
*Ratio of richest 5% of countries to poorest 5%*



Inequality is also increasing *within* many countries. The share of the poorest 50 per cent in Brazil has fallen from 18 per cent of national income in 1960 to less than 12 per cent in 1995; there are similar trends in many other Latin American economies. Central and Eastern Europe and the former Soviet Union also had sharply rising inequality, rising from relatively low levels to equivalence with the most unequal economies of Latin America. In the USA, the average income of the bottom fifth of families fell by 21 per cent over the past two decades, while that of the top fifth rose by 30 per cent.<sup>40</sup> Income inequality rose too in most European countries, but at different rates. It grew more sharply in the United Kingdom (UK) than in the USA or in European countries with more advanced social welfare systems, such as Scandinavia, Germany and Benelux.

However, inequality was not a universal trend, nor was it sustained even within countries where it existed. Its causes were not always technological or external; much depended also on domestic social policies. In other words, inequality was not inevitable: its causes were complex and variable, and Governments had a significant role to play in deciding income distribution.<sup>41</sup>

Wages are diverging by skill, gender and occupation in both rich and poor countries. Labour-market deregulation is accentuating wage differences. In the OECD, skilled workers are increasing their lead over unskilled ones, with unemployment concentrated among the latter. In the UK, for instance, the wage differential between high- and low-skill male workers rose from 2.5 to 1 in 1980 to 3.3 to 1 in 1995. Technological change and globalization are shifting labour demand towards higher skill levels, not only to use advanced technologies but also to comply with new forms of work organization.

## Manufacturing as a driving force

The growth of primary products in world trade has in recent times been much slower than that of manufactured products: over 1980–1997, the former expanded at about 2 per cent per annum and the latter at 8 per cent. Surprisingly, the primary exports of devel-

<sup>40</sup>At the same time, real wages in the USA at the bottom of the distribution increased in relation to the median. In other words, inequality increased, but because of what was happening at the top (Atkinson, 1999).

<sup>41</sup>As Atkinson (1999) argues for the UK, rising inequality was not due just to external forces but also to domestic policies. The rise was not a sustained trend, however; it was the result of a series of episodes that increased inequality in the 1980s but not in the 1990s. This is also true of the USA.

oped countries grew faster than those of developing ones, presumably because of faster technical change and trade barriers in the developing world. As a consequence, the developing world lost significant market share in its traditional export markets.

Within manufactured exports, growth was driven by technology. Let us consider manufactures classified by technological category (see table 1). High-tech exports were the fastest-growing group and resource-based products the slowest.<sup>42</sup> Low-tech products grew slightly faster than medium-tech products, because of the widespread relocation of production from high- to low-wage areas, not because of expanding markets. This growth will slow over time as the relocation process matures. By contrast, technology-based products will continue to grow fast because innovation creates new demand and substitutes for older products (NSF, 1998). The electronics part of high-tech exports also grew rapidly because final assembly can be relocated, just like garments, to low-wage areas; this process is still continuing vigorously. Countries like the Philippines and Mexico are the latest beneficiaries of this growth.

**Table 1. Growth rates and shares of exports by technological categories, 1980-1997 (%)**

	Growth rates (% p.a.)				Developing country shares (%)		
	World	Industrialized countries	Developing countries	Developing less industrialized	1980	1997	Change in share
Primary products	2.3	3.1	1.6	-1.5	52.5	46.3	-6.2
Manufactures	7.9	6.8	13.5	6.7	10.1	24.0	13.9
<i>Technical breakdown of manufactured exports</i>							
Resource-based	5.7	5.1	8.1	3.0	16.9	24.7	7.8
Low-technology	7.8	6.2	12.4	6.2	17.0	35.1	18.1
Medium-technology	7.4	6.6	16.4	9.8	4.1	15.9	11.8
High-technology	11.4	9.8	21.2	11.4	6.7	27.8	21.1
All exports	7.0	6.5	8.5	2.0	20.7	26.3	5.6

Source: Calculated by Sanjaya Lall from UN Comtrade database.

Developing countries grew faster than developed ones in all categories, doing particularly well in technologically complex products. While their share was largest in low-technology products, their growth was fastest in high-tech products, as was their

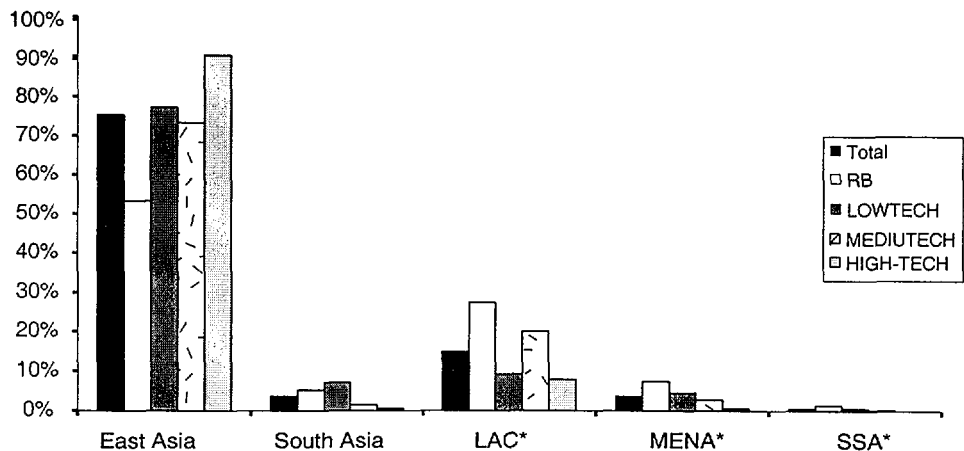
<sup>42</sup>See Lall (1998). The classification is done at the 3-digit SITC level. *Resource-based* products like processed foods or beverages tend to be simple and labour-intensive, but there are segments using capital-, scale- and skill-intensive technologies (e.g. petroleum refining). *Low-technology* products (garments, textiles, footwear, travel goods, simple metal and plastic products) have stable and well-diffused technologies, with low technological expenditures and simple skill requirements. *Medium-technology* products (standard machinery, automobiles, chemicals and basic metals) tend to have complex technologies, moderately high levels of R&D and advanced skill needs. *High-technology* products (advanced electronics, precision instruments, aircraft and pharmaceuticals) have fast-changing technologies with particular emphasis on product innovation. They are driven by high R&D expenditures, specialized technical manpower and developed technology institutions; however, high-tech electronics (in contrast to other high-tech products) have labour-intensive assembly processes that can be economically relocated in low-wage areas.

relative lead over developed countries (both concentrated in East and South-East Asia). By 1997, the value of their high-technology exports (\$287 billion) exceeded that of low-technology exports (\$256 billion). Much of their high-tech exports consisted of final assembly of imported components, but some countries and areas (particularly the mature Asian Tigers, the Hong Kong Special Administrative Region of China, Singapore, the Republic of Korea and Taiwan Province of China) had built up considerable local technological capabilities. Even in the so-called 'new Tigers' (Malaysia, Indonesia, Thailand and the Philippines), which have relatively low local technological capabilities, local content and technological activity by TNCs grew over time.

### Concentration of benefits

However, this does not mean that developing countries as a whole are benefiting from technical change and globalization: quite the opposite. Very few regions and countries show competitive dynamism in manufactured trade. Within these even fewer do well in high-technology products. In 1995, East Asia alone accounted for three-quarters of the total manufactured exports of the developing world, and for 90 per cent of high-tech, 73 per cent of medium-tech and 53 per cent of low-tech exports (see figure 2). Sub-Saharan Africa (excluding South Africa) accounted for only 0.5 per cent of all manufactured exports, 1.4 per cent of resource-based, 0.6 per cent of low-tech and virtually 0 per cent for high- and medium-tech exports. The inclusion of South Africa raises Sub-Saharan African shares to 2.2 per cent for total manufactured exports, 6.1 per cent for resource-based, 1.5 per cent for low-tech, 2.1 per cent for medium-tech and 0.3 per cent for high-tech products. Regional concentration has increased rather than diminished since 1980.

Figure 2. Developing country manufactured exports by technological category, 1995 (%)



\*See list of abbreviations

Concentration is also high at the country level. Only 15 countries account for 92 per cent of total manufactured exports from the developing world in 1997, and their share has risen from 80 per cent in 1985. These are the four mature Asian Tigers, the four new Asian Tigers (Indonesia, Malaysia, the Philippines and Thailand), China, India, Turkey, South Africa and, in Latin America, Argentina, Brazil and Mexico.

The level of concentration rises with technological sophistication. The leading five exporters in the developing world, with 62 per cent of total manufactured exports in 1995, accounted for 46 per cent in resource-based, 63 per cent in low-tech, 69 per cent in medium-tech and 78 per cent in high-tech products.<sup>43</sup> Within high-technology products, concentration rose faster than in other categories. The technological drivers of export competitiveness were clearly very unevenly spread, and highly concentrated, in the developing world.

Unevenness in manufacturing production is also high and its geographical distribution is similar to that of exports. However, the level of concentration is lower because domestic-oriented activity is more widespread. Consider 1995 manufacturing value added (MVA) in low- and middle-income countries or areas.<sup>44</sup> East Asia and the Pacific accounted for 40 per cent of the total, Latin America and the Caribbean for 23 per cent, South Asia for 5 per cent and Sub-Saharan Africa for 1 per cent (3 per cent if South Africa is included). The Middle East, South Europe and countries with economies in transition accounted for the remaining 29 per cent.<sup>45</sup> While the developing world raised its share of global MVA over time, the increase came largely from the rapid growth of the Newly Industrializing Economies (NIEs). The share of the least developed countries stagnated at 0.3 per cent from 1980 onwards (Assaf, 1999).

What do these trends suggest for the spread of manufacturing production and competitiveness? Given the pace of technical change and the spread of liberalization, unevenness is likely to increase rather than decrease. As countries expose sheltered activities to trade and shrinking economic distance intensifies competition, activity will concentrate further in a few centres with the necessary skills, capabilities, supply links and infrastructure.

## Concentration of FDI inflows

Inward FDI is one of the most effective ways for countries to access foreign resources—not just savings but also technology, managerial expertise, brand names, skills and markets. TNCs now account for between two-thirds and three-quarters of world trade; of

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<sup>43</sup>Mani (2000) develops a more detailed classification of high-technology exports and finds that the top five developing country exporters accounted for over 90 per cent in 1997.

<sup>44</sup>Including the countries and areas with economies in transition of Central and Eastern Europe and Hong Kong (as of 1 July 1997, the Hong Kong Special Administrative Region of China), Singapore and the Republic of Korea. Taiwan Province of China is omitted for lack of data.

<sup>45</sup>Calculated from World Bank, *World Development Indicators 1998*. If developing countries were defined conventionally to exclude economies with countries in transition, the share of East Asia would rise significantly; it would rise further if Taiwan Province of China were included.

this about a third takes place within TNCs (between parents and affiliates). The higher the technology and skill intensity of the activity, the greater the export role of TNCs (UNCTAD, 1999). Entry into the most dynamic segments of economic activity increasingly requires direct participation by TNCs.

International investment activity is very concentrated, both by source and destination. A few giant firms from a few rich countries dominate investment flows and the innovative activity underlying them. In the USA, for instance, just 50 firms (out of a total of more than 41,000) account for nearly half of industry-funded R&D.<sup>46</sup> In smaller developed countries, concentration is much higher. In Switzerland just three firms accounted for 81 per cent of national R&D in the early 1980s, in the Netherlands four firms for nearly 70 per cent. All these are the leading TNCs. Innovators (particularly from smaller countries) are spreading their R&D activities overseas, but mainly to other advanced countries. Apart from a few NIEs, the developing world does not participate in the advanced value-added activities of the TNCs that invest in them.

FDI in the developing world has grown rapidly since the mid-1980s (see table 2), rising from an annual average of \$29 billion in 1986–1991 to \$149 billion in 1997. Of this, South and East Asia and Latin America account for 93 per cent; at the other end, the 43 least developed countries received only 0.5 per cent. The ten leading host countries raised their shares over 1986–1997 from 64 to 76 per cent. The extent of concentration is increasing with policy liberalization. TNCs are rationalizing their production systems, concentrating in fewer sites to take advantage of economies of scale and scope. This means that fewer countries are benefiting from the resulting larger scales of production, and even fewer from the growing R&D that supports TNC production.<sup>47</sup>

Needless to say, little FDI goes into vital social sectors like health and education, or into rural activities: these are not generally activities that yield the returns needed by private investors, and many are closed to such investors. In the least developed countries, the bulk of FDI goes into extractive activities with low linkages to domestic enterprises. A large and rising share of FDI is attracted into the acquisition of privatized utilities. This may raise overall economic efficiency but does not provide a sustainable basis for industrial growth or for attracting further FDI.

Most development countries are moving towards fairly similar FDI policies, partly to attract investors and partly as a result of pressures for 'level playing fields'. With economic liberalization and technical progress, protected domestic markets and low wages for unskilled labour become less important for attracting TNCs. The main determinants of FDI location, apart from sound economic management and stable and welcoming policies, are large markets, good growth prospects and the ability to provide the factors that facilitate efficient production. These factors are labour skills, technological capabilities, modern infrastructure and low transaction (entry, exit, operation and trading) costs. These basic ingredients of growth are as unequally distributed as FDI or exports.

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<sup>46</sup>National Science Foundation (1998). The *identity* of the R&D leaders has changed over time: nearly 40 per cent of the leading R&D performers in 1994 were not in the list a decade earlier.

<sup>47</sup>For instance, major pharmaceutical TNCs are now using just two production sites (Egypt and South Africa) to serve North Africa and East and South Africa, closing down formulation facilities in a large number of African countries.

Table 2. Inward FDI flows, 1986-1997

	Inflows by year (\$ m)					Inflows (shares)			
	1986-1991 average	1990	1992	1994	1996	1997	1986-1991	1997	
<i>World</i>	159,331	183,835	175,841	242,999	337,550	400,486	100.0%	100.0%	
<i>Developed countries</i>	129,583	151,970	120,294	141,503	195,393	233,115	81.3%	58.2%	
West Europe	66,470	98,941	85,837	78,417	99,954	114,857	41.7%	28.7%	
North America	54,674	43,133	23,662	53,571	82,851	98,994	34.3%	24.7%	
Other	8,439	9,896	10,796	9,515	12,588	19,263	5.3%	4.8%	
<i>Developing countries</i>	29,090	31,766	51,108	95,582	129,813	148,944	18.3%	37.2%	
North Africa	1,196	1,341	1,582	2,364	1,313	1,811	0.8%	0.5%	
Sub-Saharan Africa	1,673	855	1,589	3,329	3,515	2,899	1.1%	0.7%	
Latin America, Caribbean	9,460	10,055	17,611	28,687	43,755	56,138	5.9%	14.0%	
Developing Europe	88	114	214	405	1,029	796	0.1%	0.2%	
West Asia	1,329	1,004	1,827	1,518	303	1,886	0.8%	0.5%	
Central Asia	4		142	896	2,084	2,627	0.0%	0.7%	
South and East Asia	15,135	18,328	27,683	58,265	77,624	82,411	9.5%	20.6%	
<i>Central and Eastern Europe</i>	658	300	4,439	5,914	12,344	18,424	0.4%	4.6%	
			<i>Memo item</i>						
Least developed (43)	781	603	1,463	844	1,965	1,813	0.5%	0.5%	

Source: UNCTAD, *World Investment Report 1998*.

## Human resources: a core factor

As the industrial sector grows more complex and sophisticated, the challenge of providing better and more appropriate human resources becomes more important. As the pace of technical change accelerates, and competition becomes more open, specialized state-of-the-art skills become even more critical to competitive success. Traditional methods of education and training are often inadequate. New institutions need to develop and firms must become more conscious of the importance of employee training. In the traditional setting, industrial development required simply improving the quantity and quality of primary schooling and basic technical education, and encouraging all forms of in-firm training. In the future, there has to be greater emphasis on high-level, specialized training, with close interaction between education and industry to assess and communicate evolving needs.

This is much more difficult. Many countries are failing to keep pace with the need. The pattern of educational enrolments in the developing world shows this clearly. Admittedly, this is not the best way to measure skill creation, since it ignores quality differences and informal learning and enterprise training. Nevertheless, these are the only skill-formation data available on a comparable basis, and the rates do show the formal base for skill acquisition.

Table 3 shows, region by region, the total numbers enrolled in tertiary education and in the three main technical subjects (science, mathematics/computing and engineering) in 1995 (weighted by population). The mature Asian Tigers enrol more than 33 times the proportion of their population in technical subjects than Sub-Saharan Africa (including South Africa). Among these, the Republic of Korea is the clear leader, not just in the developing world but in the world as a whole. The ratio for the four Tigers is twice that of industrial countries, nearly five times that of Latin America and the new Tigers, and over ten times that of South Asia and China. The leading three countries in terms of total technical enrolments—China (18 per cent), India (16 per cent) and the Republic of Korea (11 per cent)—account for 44 per cent of the developing world's technical enrolments, the top ten for 76 per cent and the top 20 for 93 per cent (Lall, 1999).

Since skill creation is so unevenly distributed, future growth will also be highly uneven. Globalization and liberalization will not solve this problem. On the contrary, they may make it worse by reducing investible surpluses and job prospects in the lagging countries.

**Table 3. Tertiary-level enrolments, total and in technical subjects (1995; numbers and percentage of population)**

	Tertiary enrolment				Technical tertiary enrolments					
	Total No. of students	Total % pop	Natural science		Mathematics, Computing		Engineering		All technical subjects	
			Numbers	%	Numbers	%	Numbers	%	Numbers	%
<i>Developing countries</i>	35,345,800	0.82	2,046,566	0.05	780,930	0.02	4,194,433	0.10	7,021,929	0.16
Sub-Saharan Africa	1,542,700	0.28	111,500	0.02	39,330	0.01	69,830	0.01	220,660	0.04
MENA	4,571,900	1.26	209,065	0.06	114,200	0.03	489,302	0.14	812,567	0.22
Latin America	7,677,800	1.64	212,901	0.05	188,800	0.04	1,002,701	0.21	1,404,402	0.30
Asia	21,553,400	0.72	1,513,100	0.05	438,600	0.01	2,632,600	0.09	4,584,300	0.15
4 Tigers	3,031,400	4.00	195,200	0.26	34,200	0.05	786,100	1.04	1,015,500	1.34
4 new Tigers	5,547,900	1.61	83,600	0.02	280,700	0.08	591,000	0.17	955,300	0.28
S. Asia	6,545,800	0.54	996,200	0.08	7,800	0.00	272,600	0.02	1,276,600	0.10
China	5,826,600	0.60	167,700	0.02	99,400	0.01	971,000	0.10	1,238,100	0.13
Others	601,700	0.46	70,400	0.05	16,500	0.01	11,900	0.01	98,800	0.08
<i>Transition economies</i>	2,025,800	1.95	55,500	0.05	30,600	0.03	354,700	0.34	440,800	0.42
<i>Developed economies</i>	33,774,800	4.06	1,509,334	0.18	1,053,913	0.13	3,191,172	0.38	5,754,419	0.69
Europe	12,297,400	3.17	876,734	0.23	448,113	0.12	1,363,772	0.35	2,688,619	0.69
N. America	16,430,800	5.54	543,600	0.18	577,900	0.19	904,600	0.31	2,026,100	0.68
Japan	3,917,700	0.49					805,800	0.10	805,800	0.10
Australia and NZ	1,128,900	5.27	89,000	0.42	27,900	0.13	117,000	0.55	233,900	1.09

Source: Calculated from UNESCO (1997) and national sources

## **Acquiring the technology: imports and domestic effort**

All developing countries rely on imported technology and access it in many ways. One major form, apart from FDI, is licensing. Because of lack of data, this is difficult to compare across countries. However, the patchy data available suggest that only a few industrializing economies account for most technology purchases (measured by royalties and technical fees). In 1997, the developing world paid \$5.8 billion (14 per cent of the world total of \$41 billion), up from \$757.5 million in 1980 (8.4 per cent).

The largest single purchaser of foreign technology was the Republic of Korea (\$2.4 billion), accounting for 42 per cent of purchases by developing countries (up from 8 per cent in 1980). It was followed by Thailand (\$804 million), China (\$543 million), Mexico (\$501 million), Argentina (\$241 million), the Philippines (\$158 million) and India (\$151 million).<sup>48</sup> Sub-Saharan Africa as a whole spent \$84 million, 1.4 per cent of the total for the developing world. The least developed countries together paid \$9 million.

Technology imports may become progressively more expensive for developing countries as stricter intellectual property rights are enforced by the WTO under Trade-Related Intellectual Property Rights (TRIPS). A significant part of technological learning in the NIEs took place under lax enforcement of patent and copyright laws, allowing local enterprises to copy or 'reverse-engineer' foreign technologies. The spread of globalization and the rising costs of innovation have led TNCs and their home Governments to press strongly against these strategies, and the NIEs have given in to their pressures. However, their technological bases are now well established; they can afford higher prices and have the ability to develop their own technologies. It is the later arrivals that may have to suffer more costly technologies, with greater enforced reliance on TNCs for access.

Domestic technological effort is essential to the efficient use of technologies. Much effort is informal—learning, incremental improvements, adaptations and copying—rather than formal R&D. Over time, however, R&D becomes more important as countries use complex technologies and have to conduct formal effort to understand, absorb and adapt such technologies, increase local content, and access technologies not easily available on licence. The R&D data show the same unevenness as other variables (see table 4). Perhaps the most relevant measure of industrial technology is productive enterprise-financed R&D. As a percentage of GNP, this is nearly 400 times as high in the mature Asian Tigers as in Sub-Saharan Africa, and around 10 times as high as in the new NIEs and Latin America.

These averages conceal large differences among countries. The leader in the developing world is the Republic of Korea, which runs neck to neck with Japan (and, surprisingly, leads all OECD countries). Taiwan Province of China comes next, spending the same proportion as the UK, higher than the Netherlands or Italy. Singapore follows, with TNC affiliates conducting the bulk of industrial R&D. These three Tigers are in a different class from the rest of the developing world. Some successful exporters (such as

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<sup>48</sup>Data are not available on major technology importers such as Taiwan Province of China, Singapore, Brazil and Malaysia.



**Table 4. R&D propensities and manpower in major country groups**  
(simple averages, latest year available)

Countries and regions <sup>a</sup>	Scientists/engineers in R&D		Total R&D (% of GNP)	Sector of performance (%)		Source of financing (% distribution)		Source of financing (% of GNP)	
	Per million population	Numbers (000)		Productive sector	Higher education	Productive enterprises	Govt	Productive enterprises	Productive sector
<b>Industrialized market economies<sup>b</sup></b>	<b>1,102</b>	<b>2,704.2</b>	<b>1.94</b>	<b>53.7</b>	<b>22.9</b>	<b>53.5</b>	<b>38.0</b>	<b>1.037</b>	<b>1.043</b>
<b>Developing economies<sup>c</sup></b>	<b>514</b>	<b>1,034.3</b>	<b>0.39</b>	<b>13.7</b>	<b>22.2</b>	<b>10.5</b>	<b>55.0</b>	<b>0.041</b>	<b>0.054</b>
Sub-Saharan Africa (exc. South Africa)	83	3.2	0.28	0.0	38.7	0.6	60.9	0.002	0.000
North Africa	423	29.7	0.40	N/A	N/A	N/A	N/A	N/A	N/A
Latin America and the Caribbean	339	107.5	0.45	18.2	23.4	9.0	78.0	0.041	0.082
<b>Asia</b>									
(excluding Japan)	<b>783</b>	<b>894.0</b>	<b>0.72</b>	<b>32.1</b>	<b>25.8</b>	<b>33.9</b>	<b>57.9</b>	<b>0.244</b>	<b>0.231</b>
NIEs <sup>d</sup>	2,121	189.2	1.50	50.1	36.6	51.2	45.8	0.768	0.751
New NIEs <sup>e</sup>	121	18.5	0.20	27.7	15.0	38.7	46.5	0.077	0.055
S, Asia <sup>f</sup>	125	145.9	0.85	13.3	10.5	7.7	91.8	0.065	0.113
Middle East	296	50.5	0.47	9.7	45.9	11.0	51.0	0.051	0.045
China	350	422.7	0.50	31.9	13.7	N/A	N/A	N/A	0.160
<b>European transition economies<sup>g</sup></b>	<b>1,857</b>	<b>946.2</b>	<b>0.77</b>	<b>35.7</b>	<b>21.4</b>	<b>37.3</b>	<b>47.8</b>	<b>0.288</b>	<b>0.275</b>
<b>World (79-84 countries)</b>	<b>1,304</b>	<b>4,684.7</b>	<b>0.92</b>	<b>36.6</b>	<b>24.7</b>	<b>34.5</b>	<b>53.2</b>	<b>0.318</b>	<b>0.337</b>

Source: Calculated by Lall from UNESCO, *Statistical Yearbook 1997*.

Notes: <sup>a</sup>Only including countries with data, and with over 1 million inhabitants in 1995.

<sup>b</sup>USA, Canada, West Europe, Japan, Australia and New Zealand.

<sup>c</sup>Including Middle East oil States, Turkey, Israel, South Africa, and formerly socialist economies in Asia.

<sup>d</sup>The Hong Kong Special Administrative Region of China, the Republic of Korea, Singapore, Taiwan Province of China.

<sup>e</sup>Indonesia, Malaysia, Thailand, the Philippines.

<sup>f</sup>India, Pakistan, Bangladesh, Nepal.

<sup>g</sup>Including Russian Federation.

Mexico, Thailand, the Philippines or Indonesia) depend heavily on TNCs to provide all innovative inputs and conduct very little local R&D; this is viable in the short term but perhaps not in the long term. Some, like India, have rising industrial R&D but their manufacturing lags technologically because of trade strategy or infrastructure problems. Most others, with small or weak industrial sectors, make little or no technological effort. They risk being caught in a vicious spiral of industrial backwardness, low skills, low FDI inflows and little domestic ability to absorb or improve on modern technologies.

## Strategy options

Growing disparities are an unfortunate, but perhaps intrinsic feature, of the new technology-driven economy. Skill development, industrial specialization, enterprise learning and institutional change create cumulative and self-reinforcing processes that promote or retard further learning.<sup>49</sup> Countries set on a pattern with low technology, low skills and low learning specialization find it difficult to change course without a concerted shift comprising interacting markets and institutions. Economic liberalization may help them realize advantages based on inherited endowments like natural resources and cheap unskilled labour. However, it may not lead them to develop the more dynamic (skill- and technology-based) advantages they need to sustain growth and structural change. Thus, they may become outsiders in a world of rapid and accelerating technological change, new skill needs and integrated production systems. They may suffer from having to export larger amounts of products facing static or declining prices in order to import given amounts of foreign services and products.

The insiders are the relatively few developing countries that have been able to launch themselves on a sustainable high-growth path. The insiders also differ, depending on the strategies adopted. We may distinguish two general strategies: domestic enterprise-centred and FDI-centred. Domestic enterprise-centred strategies, as demonstrated by the Republic of Korea and Taiwan Province of China, entail a great deal of policy interventions in factor (e.g. labour) markets and institutions. They lead to a massive development and deepening of indigenous skills and technological capabilities in order to keep abreast of new technologies and for domestic enterprises to become significant global players in their own right.

*FDI-centred strategies* comprise two sub-strategies: targeted and passive. Targeted strategies, as in Singapore, also entail considerable policy interventions, but the intensity of such interventions is lower than with domestic enterprise-centred strategies. The sources of technical change remain largely outside, in the hands of TNCs; there is hence less need to intervene to promote learning in infant industries. However, policy interventions are needed to ensure the development of the skills, capabilities and institutions as well as the physical infrastructure required to ensure that TNCs keep transferring new

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<sup>49</sup>On cumulative causation as related to development and specialization see Redding (1999) and Venables (1996). On evolutionary theories of change see Nelson and Winter (1982) and Nelson (1995), and on national systems of innovation and technology development see Lundvall (1992), Nelson (1993) and Lall and Teubal (1998).

technologies and higher-value functions. Passive strategies involve less reliance on policy in export-oriented activities to start with (though there may be intervention in domestic-oriented activity). TNCs are often attracted by low wages for unskilled or semi-skilled labour and good infrastructure, given a conducive macro environment and welcoming policies to FDI.

Subsequent dynamism and upgrading depend on whether TNCs are induced from simple assembly activities into more advanced, value-added activities with stronger local 'roots'. This involves deepening the local skill and supplier base and targeting FDI itself (as in Malaysia and Thailand). Without such capability development, the initial spurt of growth may well peter out: rising wages will erode the competitive base. This is the danger facing a number of developing countries (such as Bangladesh, Mauritius or Morocco) which have done well out of the relocation of the clothing industry in building simple manufactured exports, but have not been able so far to upgrade into more complex or technology-intensive activities.

### **Beyond liberalization**

Simply opening up to free trade and investment flows does not seem to be an adequate strategy for countries at the low end of the technology ladder. Stabilization and liberalization can remove the constraints to growth caused by poor macro management, inefficient public enterprises, high entry costs for private enterprises, and restrictions on FDI. However, they cannot by themselves allow the economy to build more advanced capabilities, to escape a 'low-level equilibrium trap'. Evidence on liberalizing countries like Kenya, the United Republic of Tanzania, Zimbabwe and Ghana shows that after an initial spurt of growth, economies with static capabilities slow down as their inherited advantages are exhausted (Lall (ed.), 1999).

The initial spurt comes from using formerly idle capacity as imported inputs and spares become available. As import competition in the final-product market increases, however, enterprises find it difficult to cope, and close down or withdraw into non-traded activities. Without enabling support from the Government, they find it difficult to bridge the gap between their skills, technologies and capabilities and those needed for international competitiveness. New enterprises find it even more difficult to enter complex activities with even more stringent skill and technology requirements.

There is a danger, therefore, that industrial structures in low-income countries may regress into simple activities that do not provide a basis for rapid growth. This is one important reason why liberalization has had such poor results in Sub-Saharan Africa. Liberalization has also led to discontinuities in technological learning in many countries of Latin America, which affect growth and competitive performance. These countries often have a large base of capabilities in such industries as food processing and automobile manufacture, but find it difficult to move into dynamic high-tech activities (Benavente *et al.*, 1997).

The rule-setting part of the international system that deals most directly with development (the Bretton Woods institutions and increasingly the WTO) has so far been more

concerned with facilitating globalization than with helping countries cope with its demands. This approach, broadly labelled the 'Washington Consensus', has been based on the implicit premise that free markets and rules to promote market forces will accomplish both objectives: liberalization is the best policy response for all countries. This approach has been extremely influential.

The WTO is enforcing trade liberalization throughout the world (though the least developed countries have been given a longer grace period, now fast coming to an end). It is also enforcing related measures such as TRIPS (noted above) and Trade-Related Investment Measures (TRIMS) that disallow policies, such as copying, local-content rules and performance requirements, which were extensively relied upon by the NIEs.

There has been considerable liberalization in developing countries and countries with economies in transition. Governments are withdrawing from direct ownership of productive resources and also from the provision of a number of infrastructure services. They play a steadily diminishing role in the allocation of productive resources. The ultimate objective of the current phase of reforms is a liberal production, trading and investment framework in which the driving force is private enterprise responding to market signals.

There is much to welcome in these trends. Many government interventions to promote development have a poor record and have constrained rather than helped growth and welfare. Giving greater play to market forces will contain many of the inefficiencies and rent seeking inherent in government intervention. However, as noted, simply opening up to market forces does not deal with many structural problems of development. The most successful developing countries in recent economic history (the Asian NIEs) intervened intensively in markets, with many different strategies to build up their competitive capabilities (Lall, 1996). Their experience suggests that there is a significant and positive role for government in providing the 'collective goods' needed for sustained development. The real issue is not *whether* Governments should intervene, but *how*.

It is not just experience that supports careful policy intervention: economic theory also provides a sound case for intervention (see below). The World Bank admits that Governments have a larger and more positive role to play than the Washington Consensus allowed for, and that liberalization *per se* will not alleviate poverty. Nor will it counter the growing divergence in development performance and the marginalization of large parts of the developing world. There is a need for more nuanced strategies than the old Consensus, with greater support from the international community.

This discussion of trends, by showing the threats to the developing world in the new global economy, sets the scene for analysing the UN system as a provider of international public goods. It makes clear that the challenge is not simply to promote liberalization or to alleviate poverty. It goes much deeper and into more difficult areas—the enabling forces behind industrial and technological development. Without an understanding of these, it would not be possible to explain properly the task facing the international development community. However, before we come to these, it is necessary to explore briefly the concept of public goods and how they determine the role of government.

## The role of government and public goods

The role of government can be considered at many different levels. While much of the discussion has focused on national Governments, the same reasoning applies at lower (state or local) as well as at higher (multilateral and international) levels. Let us consider the economic role of Governments and international institutions before coming to the UN's role in the development context. What does economics say about the role of government (or, as some put it, 'collective action')?

All accept that Governments have to provide security, law and order, legal recourse and good macro management. In addition, neoclassical economic theory argues that Governments may intervene in economic life only to remedy *market failures*. Market failures are departures from a competitive equilibrium.<sup>50</sup> Such 'failures' occur if there are conditions that lead free markets to give the wrong signals to private agents and so lead to inefficient responses. The most commonly mentioned causes of market failure are public goods, externalities and monopolistic elements.

*Public goods* exist when consumption by one person does not reduce their availability to another and where it is difficult to limit access; a good example is police protection. Private agents will not provide these goods to everybody because they cannot reap sufficient profit. *Externalities* exist when one agent's activity affects another but cannot be properly charged for, like pollution created by a factory or training provided to employees who later leave the firm for a competitor. *Monopolistic markets* allow firms to restrict production and so earn higher profits than they would in a competitive situation.

Market failure can also arise when *information* is not freely and fully available and is costly to collect; in this case, the best solution may be unattainable because it may be inefficient to devote the (possibly enormous) resources needed to have full information. With imperfect information, it is possible for enterprises to generate rents that are not (as in perfect markets) competed away.

While such textbook market failures are common (and information failures are probably universal), it is reasonable to expect that failures run deeper in developing countries. There may, for instance, be widespread failures due to strong linkages between markets or investment decisions, even when information flows in markets are not imperfect. These linkages may lead firms to collectively invest too little or in the wrong activities, because they cannot correctly anticipate the consequences of their own actions on other firms (raising demand for their products, or lowering their costs as they learn to become more efficient). The 'equilibrium' reached may be at a low level of income,

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<sup>50</sup>A competitive equilibrium is in turn is defined by market efficiency. 'Market efficiency' in this sense is based upon strong assumptions: perfect competition, perfect knowledge, no externalities or scale economies, and a complete set of markets, including all future markets covering all risks. In this setting, if markets are fully efficient, they can achieve a 'Pareto optimum' without intervention. A 'Pareto optimum' exists when it is not possible to make anyone better off without making someone else worse off. Any number of such equilibria is possible, depending on the distribution of income: the theory itself says nothing about the desirability of any given distribution.

or lead to low rates of growth. Coordination of investment decisions by the Government may lead to a more dynamic outcome.<sup>51</sup>

The role of government, then, can be conceived as broader and less well defined. It may intervene to *coordinate activities and markets* in order to move the economy from one equilibrium (low-income, low-growth or low-skill) to another. It may need to *provide a 'vision' of economic structure and growth* to define which particular market interventions are required. For instance, moving from a low-skill to a high-skill growth path may require promoting technological development along with the creation of the necessary skills, attraction of particular types of FDI and so on (Lall, 1996, Lall and Teubal, 1998). In the absence of interventions, free but badly functioning markets may lead to stagnation or slow growth.

Another set of 'failures' is important here—those of *Governments*. Government failure is widespread (and may be as much a feature of underdevelopment as is market failure), and coping with it is a necessary part of any policy discussion. Public intervention may or may not improve matters, depending on such things as foresight, impartiality and skills. The provision of information to Governments on policy needs, assistance in designing and implementing 'best practice' policies, and strengthening government capabilities and accountability, become an essential part of collective action, particularly at the international level.

The recent literature on the role of international institutions focuses on *the provision of public goods as the primary function of government*. As noted, free markets cannot provide such goods since they cannot be priced correctly or yield sufficient private profit.<sup>52</sup> We noted that the proper development role of Governments goes beyond the provision of public goods in the narrow sense. Governments have to remedy all sorts of market failure, not just those arising from pure public goods. Where necessary, Governments have to provide a development 'vision' to enable a shift from low- to high-growth paths. They have to furnish socially acceptable income distribution and take care of deprived sections of society. They have to protect the environment and promote the creation and diffusion of productive knowledge. Technology foresight, as applied in developed countries, is an example of a useful tool for this purpose.

However, for the sake of convenience we can call all these functions the provision of public goods in the broad sense. This broad understanding of public goods is relevant to the analysis of the role of international agencies like the UN and the Bretton Woods institutions.

<sup>51</sup>On multiple equilibria and the role of government see, for example, Redding (1999) and Rodrik (1996). On diffuse market failures in information and the role of government see Stiglitz (1996). In the absence of perfect futures markets (for all goods over all time), there are inevitable allocation issues that free markets cannot resolve. There is then a role for Governments in deciding how much resources to devote to current as opposed to future generations.

<sup>52</sup>For an analysis of the concept and its various forms, see Kaul *et al.* (1999a). Public goods can be 'pure' or 'impure'. Pure public goods are wholly non-rival and non-excludable, like peace, security, or the rule of law. Impure public goods are those which are partly rivalrous or excludable (like common property) or which are not consumed in the normal economic sense (like art, culture or biodiversity). In the traditional literature, public goods are narrow in scope, covering such 'pure' goods as defence, security, and rule of law or common standards that provide the essential framework of economic life in market economies.

## Global public goods and international institutions

International bodies, such as the UN and its agencies, the Bretton Woods institutions, regional agencies and development banks, manifest the desire of individual nations to undertake collective action. This has to do with the provision of global or international public goods in the broadest sense. What do these public goods comprise in the sphere of economic development? The main items to consider are:

- *Providing global commons*, such as the environment, peace and safety, that affect all nations. All analysts agree that these are pure global public goods.
- *Providing the basic infrastructure of international economic relations*: the system and rules for trade, payments, financial flows and competition policy. Most agree that these too are global public goods, though they may differ on the definition and content of such goods. Some tend to identify them with the enforcement of free trade and capital movements—a ‘level playing-field’ regardless of income, size and development. Others argue that in view of market failures, caused by learning, externalities and cumulative effects, a truly fair system would give preference to weaker players (for instance by means of infant industry protection or preferences for domestic enterprises). Some consider coordination of economic activity between nations or assistance to countries with economies in transition the subject of collective action. In general, optimal economic rules are not ‘given’ by theory; much depends on the analyst’s reading of market efficiency and government capabilities.
- *Furthering humanitarian and legal objectives* such as universal human rights, democratization, poverty reduction, justice and humanitarian assistance. These are not economic public goods in the strict sense but most people would regard them as legitimate concerns for both national government and international agencies.
- *Promoting international solidarity and stability*: like humanitarian objectives, these are not economic public goods in the strict sense. However, fostering development in poor countries can be regarded as essential to international solidarity and stability, and so included as a global public good.
- *Creation and diffusion of knowledge*: as a global public good, it can take different forms, including production of scientific and technological knowledge to offset underinvestment, particularly in basic research; fostering the flow of technology and other productive knowledge to developing countries and helping developing countries to develop skills and technological capabilities directly by providing training and expertise, or indirectly by allowing them to promote learning processes or by subsidizing activities with strong technical spillovers.
- *Good governance*. Developing countries often find it difficult to identify which strategies to adopt or how best to implement them, and find it difficult to analyse correctly the experience of other, more successful, countries.

Moreover, evidence is subject to different interpretations, depending on the perspective of the analyst. The real international public good would be to provide Governments with alternative views of good policy and the analytical tools to interpret alternative views as well as knowledge on ways to ensure participation, equity, transparency and accountability throughout the process of policy design, implementation and monitoring.

The provision of all these international public goods needs collective action by Governments. Note, however, that some public goods like humanitarian or solidarity concerns do not imply market failures in the normal sense. All markets may function efficiently but still not yield the income distribution, stability or solidarity that is considered desirable. Global public goods clearly have an ethical as well as an economic rationale, but the line between them is difficult to draw in practice. There is no need here, however, to draw such a line; we work with a broad definition of global public goods and consider the role international institutions can play.



## Chapter 3

# Sustainable industrialization and development: the role of UNIDO

There is broad agreement that the current Development Agenda is appropriate. Still, if it is to meet its objectives fully, it will be necessary to address the imbalances in the multilateral trade and financial regimes, and to remove the obstacles still preventing the private sector from playing a leading role in mobilizing the skills and capabilities needed to ensure the successful outcome of reform programmes under way.

### Missing links in the Development Agenda

The consensus already reached around the need for macroeconomic stability, open trade and investment regimes and institutional reform needs to be consolidated. But this can only be accomplished by addressing some missing links in reform programmes. The existence of such missing links explains why, despite macroeconomic stabilization, trade and investment liberalization and improved institutions and governance, the connecting tissue linking institutions, economic agents and capabilities still remains extremely weak, fragmented and often unworkable in a large number of development countries. This leads to failure in ensuring sustained productivity growth in private sector-led, innovation-driven developing economies and, with it, to elicit the necessary public support and trust.<sup>53</sup>

The Development Agenda has undergone important changes over the last few decades. In the process of adjusting the agenda in line with the evolving economic and social ideas, international organizations have made important changes to the policy prescriptions given to developing countries. Many of such prescriptions, and other factors, such as planning ideologies in developing countries, actually hindered economic and social development.

The international community of nations has gradually been converging towards a common view on the basic set of policies that are necessary for creating the conditions

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<sup>53</sup>For further elaboration on this see: C.A. Magariños "Reflections on the Development Agenda", report submitted to the High Level UNIDO Meeting on Marginalization versus Prosperity-Improving the Creation and Distribution of Gains Brought by the Process of Globalization, Venice, 28-29 September, 2000.

for economic and social take-off. These include those addressing macroeconomic stability, ensuring balanced public accounts, and trade and capital account openness. These basic policy prescriptions are complemented with an added emphasis on appropriate institutions and good governance and a private sector driven mobilization of resources for economic growth. This high degree of concurrence among international organizations is quite unique in historical perspective. The opportunity to build on this consensus should not be wasted.

The development challenges remain huge and continue to grow. Many developing countries have embraced the basic policy prescriptions just outlined, but not all have been equally successful. The lack of connectedness between large segments of developing countries' populations and the global economy is a major source of popular dissatisfaction or indifference towards the basic economic and institutional reform prescriptions of the Development Agenda. This is observed in countries, which, in spite of having opened their economies, have for the most part been excluded from capital and trade flows. It also happens in other countries where reform programmes met initial success in delivering productivity gains but where the growth momentum was subsequently lost. As a consequence, the per capita income gap between most developing countries and the industrialized ones continues to widen.

This widening gap is a matter of growing concern to developing countries' Governments and international organizations. The reasons why this is so should be at the top of the Development Agenda today in a concerted effort by the international community to make globalization become a win-win proposal for all countries and not just for a few rich ones.

The multilateral trade rules and market access opportunities are biased against developing countries, particularly because of remaining restriction of developing country exports in developed country markets. In addition, some regulations of the international financial system entail implicit barriers to the development of small- and medium-sized companies.<sup>54</sup> The gains to industrialized countries from liberalization policies in trade and services have been substantial. In contrast, many developing countries are still waiting for similar opportunities. In some goods, like textiles and clothing, industrialized countries have promised to lift some trade barriers in the future while in others, including agricultural products, such a promise has not even been made. In many products of this sector, the markets of these countries are even less opened than what they were before the Uruguay Round. Doubtless, the lifting of trade barriers would provide important growth opportunities for developing countries in the years ahead. This is not a matter of development assistance but simply of levelling the playing. The longer it takes for this action to be implemented, the longer underdevelopment and poverty will linger.

The biggest promises of public policy lie in strengthening the capacity of the private sector of developing countries to mobilize resources—skills, capital and knowledge. This requires, first and foremost, liberalizing trade where it remains protected against the interests of developing countries. This will help these countries to increase their exports and benefit from the learning that comes with operating in the international marketplace.

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<sup>54</sup>For further details see, C.A. Magariños, *op. cit.*, chapter 4, section b.

Second, international organizations need to continue finding the best means of assisting Governments and the private sector to cooperate in fostering the mobilization of resources for growth.

This approach is likely to provide many of the key answers sought by developing countries to the question of how to address current development challenges, particularly those of poverty, volatility and the environment, in a sustainable and effective manner.

To draw fully on world trade and investment flows and thus enter the high road to development, developing countries need to ensure sustained productivity growth and the equitable distribution of its benefits. This way they will also be able to connect their populations to the global economy. Facilitating the unfolding of a dynamic and innovative private sector-driven economy is key to the success of macroeconomic and institutional reforms.

While many countries have made notable strides towards stabilization and getting prices right, several have failed to benefit from global trade and investment flows. The next step revolves precisely around the need to develop the broader set of institutions and capabilities needed to respond to freer markets and emerging technologies. Simply putting the right incentive framework in place does not ensure an adequate response on the supply side. On the contrary, it may accentuate unevenness of opportunity and disadvantage the weak. It may even erode the social, political and institutional base to provide the new capabilities needed.

A healthy interaction between markets and institutions can largely be taken for granted in the developed economies (although most also feel the need to mount competitiveness strategies at the national or local level). These economies generally rely on a critical mass of skills, information flows, business networks and facilitating institutions to allow private firms to tackle competitive challenges. Such challenges today essentially concern technology, broadly defined to include not just technical know-how, largely embodied in people, but also managerial and organizational methods. A myriad companies are engaged in the process of generating and using innovation and coping with intensifying competition and the unprecedented growth of information and communication technologies. This flow stems from the entrepreneurial mobilization of the key ingredients of innovation, technical change and productivity growth. The endless (and intensifying) processes of technical creation and destruction that drive growth and efficiency gains have become embedded in advanced economies' normal "flow of business". This has been the result of gradual and cumulative economic, social and institutional evolution, led in almost all cases by manufacturing industry.

In the developing world, there are certainly countries that have achieved rapid growth and structural transformation drawing on industrialization. The leading examples are the original Asian Tigers (Hong Kong Special Administrative Region of China, Singapore, the Republic of Korea and Taiwan Province of China). These countries have rapidly progressed in closing the gap with advanced industrialized countries in less than forty years; in some ways, they surpass many mature economies in competitiveness and technical prowess. While their experience has greatly influenced our understanding of development policy, the precise nature of the factors that propelled their industrial success is still under debate.

Some recent growth accounting exercises have been used to suggest that it has been the result simply of massive accumulation (of physical and human capital), openness and good macro management, with very little role assigned to technological effort. There are problems with this interpretation. The measurement of primary factors of production, particularly capital, is laden with difficulties. The assumption that these factors are separable is questionable. The specific form in which the residual is measured (that is, the specification of the production function) matters, and different specifications give very different results.

These technical difficulties apart, there is an analytical problem, which is important to the understanding of development strategy. The growth accounting methodology assumes that technology is easily transferred and adopted by new users: that, for instance, maintaining a high rate of investment in advanced industrial sectors at competitive levels involves no technological effort. Only on this basis can it be argued that the Tigers were able to rapidly diversify into export-oriented production of highly complex industrial products without technological effort. This is, of course, a gross oversimplification. Technology is more than what one finds embodied in capital goods, blueprints or instructions. For this reason, absorbing and using new technology is a difficult process. It involves investment in building new technical information, experimentation, new skills and new organizational routines. In more neoclassical terms, the Tigers could only prevent the marginal returns to capital from declining, despite massive investments, by undertaking significant technological effort and innovation.<sup>55</sup>

This is not to say that accumulation and macro stability did not play an important role. Clearly they did. Without these basic framework conditions, technological effort could not have taken place or been embodied in physical facilities. However, the Tigers had to go beyond creating these conditions to foster learning, help enterprises bear its costs, set up support institutions, and overcome externalities and coordination problems. Note that each Tiger adopted a different strategy, in line with its own vision of industrial development, and built different levels and kinds of capabilities. The accumulation of human and physical capital was a necessary part—but it was not sufficient. There are many important lessons for other countries, from both their common elements as well as their differences.

Unfortunately, such cases of rapid catch-up are relatively rare. Most other developing countries, faced with the challenge of globalization and liberalization, have not managed the process well. At best, they enjoyed a spurt of growth when they realized existing competitive advantages by improving macro management and 'letting in' the market. After that, most tended to relapse or stagnate. Such economic improvements as took place failed to reach the majority of the population, which, in a world of rapid change and shrinking economic space detracts legitimacy to the reform programmes.

The Asian experience shows that the basis for sustainable growth lies ultimately in the capacity of the private sector to manage effectively new technology and organizational practices. This requires constant learning, experimentation and innovation. The

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<sup>55</sup>R. Nelson and H. Pack, "The Asian miracle and modern growth theory", *Economic Journal*, vol. 109, No. 457, July 1999.

capabilities to do all this arise from the creation of new skills, information on technology, markets and management practices, focused technological effort, finance for risky activity, and the fostering of cooperation between agents that learn collectively.

If it is accepted that such factors are at the core of innovation for productivity growth, what is the role of policy? Most of these factors are not provided adequately by markets. In fact, many of them lack 'markets' altogether in a meaningful sense, certainly in most developing countries. They have strong 'public goods' elements and face a high degree of risk and uncertainty as well as enormous coordination problems. Only coherent government policy—supported by international action to provide the international public goods required—could start to overcome the vicious circles that trap economies in poverty and marginalize them. The need for efficient physical infrastructure to provide logistic, communications and supply chain management hardly needs to be emphasized. For efficient, demand-driven education and training, technological support, technology-based investment and cluster promotion is equally important. The efforts made in the OECD countries (and the EU at the regional level) illustrate how important Governments of the most advanced countries consider it. Poor countries, with far weaker capabilities and institutions, need such efforts all the more.

What developing countries need is a set of liberalization cum public goods supply policies to mobilize information, knowledge, skills and technology to support the private sector. Only by improving the interaction between markets and agents does it become possible to attain a fair social distribution of the fruits of productivity growth and hopefully gather popular support for the reform programmes.

## Industrialization and development

Industrial enterprises have an important role to play in facilitating a working interaction between markets and institutions through the mobilization of information, knowledge, skills and technology.

Most developing countries, and most now considered developed, accorded industrialization a special role in economic development. They regarded it as the engine of structural transformation, moving a low-income economy with traditional agriculture and simple processing to one with high incomes based on new technologies, economies of scale,<sup>56</sup> new skills and new knowledge. This perception was not based just on the simple association between national wealth and large and developed industrial sectors. It reflected a feeling that the process of industrialization offered special benefits, raising productivity not just directly but also indirectly: it provided the necessary basis of creating a 'modern' economy. A modern economy has the ability to use and create new

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<sup>56</sup>Scale economies arise when larger scale of production leads to lower unit costs. For instance, it is much cheaper to make petrochemicals or automobiles in large facilities than in small ones, because the fixed cost of equipment and plant can be spread over a larger volume of output. Economies of scale tend to be low or absent in simple-technology activities such as clothing manufacture, and here a small plant can compete effectively with a large one. While some new high-technology activities and services can be efficient on relatively small scales, in general industrial development has meant a structural shift from scale-neutral to scale-intensive activities.

technologies, to offer steadily rising living standards and to respond flexibly to changing market conditions. A traditional economy in the developing world lacks all these attributes.

The historical evidence on the role of industrialization is overwhelming: 'all countries that escaped poverty did it by industrializing. Inversely, with the exception of few very small countries—tourism or finance paradise islands, service city-states or oil kingdoms—countries that did not industrialize remained poor' (UNIDO, 1999, p. 1). The statistical work of Chenery *et al.* (1986) confirms earlier findings by Kuznets that the shift of resources from agriculture to industry is a central feature of all structural transformation.

However, in textbook neoclassical economics there is no reason for industrialization to play a special role in growth. In its idealized world of perfect competition, without scale economies, uncertainty or externalities,<sup>57</sup> and with universal access to information and knowledge (created outside the economic system), returns to factors equalized across all activities, no activity yields greater benefits than another. This is a world without institutions or history, where atomistic agents reach allocative equilibrium only by interacting in anonymous markets. When these strong simplifying assumptions are dropped and we consider something approximating the real world, the value of industrial activity emerges more clearly. If we accept that there are economies of scale, that technical change is costly and uncertain, and that innovation is conducted by enterprises rather than coming like manna from heaven from outside, that information is imperfect and there are widespread linkages, the picture changes. It becomes evident that some activities have much larger effects on growth, incomes, learning and innovation than others. Manufacturing industry takes pride of place in this.

Manufacturing offers special economic benefits in many forms:

(a) Manufacturing industry is the main vehicle for *technological progress*—the application of science to production and for the use of technology in productive activity. Governments and economists have long considered this to be the main benefit of industrialization. While agriculture enjoys technical progress, the pace of technical change there has been low—historically much lower than in manufacturing. Agriculture is intrinsically constrained by the presence of one fixed factor, land, while manufacturing can apply a limitless variety of inputs and equipment. Thus, the application of science to production has focused overwhelmingly on manufacturing, and the shift from low- to high-productivity activities has almost inevitably been identical with the shift from agriculture and traditional services to industry. In recent years, modern information- and communication-based services have also attracted significant innovative activity; however, this has been possible only because of technological advances in the hardware of information processing and telecommunications.

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<sup>57</sup>Externalities exist when market prices cannot capture all the costs and benefits to parties in a transaction. For example, a classic negative externality occurs when a factory pollutes the atmosphere for neighbouring residents but is not obliged to pay for the nuisance; a positive externality occurs when an enterprise trains workers who then leave with their new skills and find better-paid jobs elsewhere, without compensating their original employer for its investment. Where externalities exist, market prices by definition cannot give the right signals for resource allocation: in the second example, the original firm may soon stop investing in training because it does not recoup most of its investments.

(b) Not only does manufacturing allow enormous scope for the application of science to production, it is itself the *major source of innovation*. R&D by private industrial enterprises has grown in importance since the nineteenth century, and now accounts for the bulk of innovative investments. Such enterprises also finance significant amounts of research in other laboratories and in universities. However, formal R&D is only part of the technology development process. A significant part of productivity-raising effort, often the most significant part, takes place in engineering, production, procurement, quality management and other activities. The scope for such incremental innovation is enormous in manufacturing, and recent organizational changes have made it an integral part of many activities. We should note again that there are enormous differences *between* manufacturing activities. As noted above, technology-based activities are growing much faster in production and trade than are other activities. Leading NIEs are growing much faster, but often from a smaller base, than mature developed countries, but the trend is universal. Internal technological effort is becoming essential to competitiveness and survival in all activities. Moreover, the fact that some activities offer better growth prospects than others because of greater technological potential means that technological effort should focus more on these. Growth and dynamic comparative advantage (that is, export competitiveness that changes with technology and rising incomes) depend on these technology-based activities; most are in manufacturing or closely related to it.

(c) Manufacturing is a *vital source of new skills and work attitudes*, particularly in the process of transforming the structures of traditional rural societies. There are several elements to this contribution:

- The creation of an industrial tradition and work ethic, with the spreading of discipline and organization required in modern societies.
- The fostering of entrepreneurial capabilities, with small and medium-sized manufacturing enterprises providing the seedbed of the skills needed today.
- The development of managerial and technological capabilities, the core of modernization and competitiveness. These capabilities are created mainly by on-the-job experience and problem solving. Manufacturing provides the widest and most relevant ground for such capability development.
- The creation of skills by enterprise training. Enterprises invest increasingly in enhancing the skills of their employees, by both in-house training and external courses. In countries like Japan, investments in enterprise training are even larger than the expenditures of the higher-education sector.
- Interaction between industrial enterprises and educational institutions. As skill needs change more rapidly, and become more specialized, there is closer interaction between the users and providers of formal education, creating beneficial synergies for the economy.

- Transfer of foreign skills. This is a growing feature of globalized production (also very important in modern services). Manufacturing enterprises with international operations move highly skilled manpower around the globe as needed, in the process filling specific gaps in different locations and providing beneficial training and spillover effects.

(d) Both the technological and skill benefits of manufacturing have *large beneficial externalities*. Technical change and skill creation by industry stimulate productivity growth in other activities: agriculture gains by having better equipment and inputs, improved storage, transport, distribution and processing facilities, and richer consumers; services gain from better equipment and skills. While agriculture and services can be improved without local manufacturing of inputs, the presence of an efficient industrial sector capable of providing equipment and intermediate goods is likely to promote more rapid technical change and adaptation. More broadly, however, it is the general 'modernizing' effect of industrial growth that helps all other activities in a developing economy to upgrade.

(e) Even more important is the fact that the manufacturing sector provides the *direct demand stimulus for the growth of many modern (increasingly high-technology) services*. It is often the largest customer for banking, transport, insurance, communications, advertising, utilities and other activities. It creates markets for new services and skills, which are particularly important for finance, education and logistics. It is also the source of new service enterprises: many services that were traditionally part of manufacturing, have been hived off as enterprises concentrating on their 'core competencies'. For example, many large manufacturers now out-source design, logistics, maintenance, training and other services, often setting up affiliates to specialize in these activities for themselves and other firms.

(f) The *internationalization of services* (facilitated by new information technologies, which allow functions to be separated and relocated abroad more easily) often follows the spread of manufacturing TNCs. Banks, transport-providers, advertisers and so on are setting up across the world to serve customers with whom they have long-standing relations. The original lead in globalization, however, came from manufacturing firms (earlier resource-extraction TNCs never really became 'globalized' in the sense of integrating operations at all levels across countries). Historically, manufactured trade has been the largest stimulus for FDI, which then built the international linkages that led to the spread of other activities.

(g) Manufacturing is the main source of *dynamic change in comparative advantages*. Chenery *et al.* (1986) call this 'transformation of comparative advantage as factor proportions change'. Early analysts like Prebisch and Singer saw industrialization as the way to overcome constraints caused by declining terms of trade for primary exports. As shown earlier on, sustained and dynamic growth in exports necessitates a shift from primary to manufactured products (and within manufacturing from low- to high-technology products). Manufacturing accounts for around 90 per cent of global visible trade, and most developing countries consider the development of export-oriented industry



vital to their future growth. While modern service exports are also growing, much of this growth comes from relatively advanced countries that have built modern skills and capabilities by manufacturing. It is difficult to find countries selling high-value services (excluding such activities as tourism that depend heavily on natural resource endowments) that have not first undergone sustained industrial development: the institutions and skills now involved in service exports were developed in conjunction with manufacturing.<sup>58</sup>

(h) Manufacturing led the *evolution of modern corporate forms of capitalist enterprise* (like joint stock companies) without which economic development would not have taken place. This applies also to the related legal instruments, practices and conventions.

(i) Manufacturing development can also *help develop rural industry via backward linkages*, and so feed into the technological development of agriculture. It can help the development of female entrepreneurs, small enterprises and backward classes. In general, it can make a valuable contribution to social development by promoting mobility, skill formation and new opportunities for self-advancement.

(j) Successful industrial development can provide a *sound base for sustainable growth in incomes and employment* and so promote national stability and security.

In sum, industry has been the main source, user and diffuser of technical progress and associated skills and attitudes. No other productive activity comes near it. Its special role can only be understood in a world of dynamic learning and technical change, where large firms strive to increase their size and capabilities and realize economies of scale, and societies constantly transform their structures and habits. In this world, manufacturing industry is not only important for development—it is an essential ingredient.

The role of industrialization in development has to be viewed in historical perspective. Only highly advanced economies, after having reached high levels of productivity and standards of living, can afford not to regard manufacturing as key to their economic growth, although in fact it continues performing as key engine of productivity growth and assisted by means such as the setting of priorities in the allocation of resources to science, technology and education.

## The need for policies to promote industrialization

Given that industrialization plays a vital role in development, does it need policy support? Or can its progress be left to free-market forces? As argued before, there are strong policy needs for development in general because of pervasive and diffuse market failures.

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<sup>58</sup>Consider the example of Singapore. In the 1960s Singapore launched its industrial drive by exporting simple manufactures such as clothing and services such as ship repair. In the 1970s it moved into low-level electronics assembly and petrochemicals manufacture. In the 1980s it moved into sophisticated electronics and complex services like airlines, aircraft servicing, shipping, containerization and finance. In the 1990s it pushed further into high-technology electronics manufacturing and design, high value-added services such as regional headquarters for TNCs, more advanced financial services and R&D. Its upgrading of economic structure was driven by manufacturing but closely coordinated with services.

Market failures apply with particular force to industry. The essence of industrial development is what Schumpeter, in describing the productive forces released by capitalist entrepreneurs applying new technology to industry, termed 'creative destruction'. It destroys older, less productive, modes of production and organization. It replaces less creative and dynamic activities and enterprises with new ones. It applies the productive powers of science in unforeseen ways. It is a creature of market imperfections, uncertainty, externalities and disequilibrium. Of the three basic forms of economic activity (agriculture, industry and services), industry is the one that enjoys the greatest application of new knowledge and skills.

Bearing in mind the deficiencies of the market-failure approach to the analysis of policy needs, let us consider why Governments need to support industrial development. The case can be made at two levels, macro and micro.

At the macro level, the main case for policy rests on the externalities that industrialization generates. The main externality noted in the early literature is 'pecuniary': the growth of one industrial activity creates demand for other industrial products or for complementary services. This enables other activities to set up economically and achieve scale economies. Later literature notes the significance of other externalities, created by strong technological linkages between activities that rely on each other for technical knowledge or inputs. Where such linkages are strong, firms may underinvest because they cannot anticipate correctly how other firms in the production chain will invest or raise productivity over time when they do invest. In other words, free markets cannot provide the coordination needed because current prices are not a good guide to future prices. Where there are a few firms and they can exchange information with each other on investment and technology, they will be able to coordinate their investment plans: this generally happens in developed countries where intra-industry linkages are strong.

However, in developing countries these linkages are lacking and many activities are completely new to the economy. There is then no way for firms to 'discover' these future prices. A coordinated effort may be needed if the economy is to enter into these new activities. If the new activities are desirable from the perspective of technological development and skill creation, the Government may encourage investment. Such strategic interventions have been used by many economies, like the Republic of Korea and Taiwan Province of China, to move into dynamic activities. More generally, where an economy starts from a static industrial structure, such interventions may be needed to take it from a low-growth trap to a high-growth path.<sup>59</sup>

At the micro level, the case for interventions rests on market failures in the technological processes inherent in industrialization. But why 'technological processes' in developing countries, when all they are doing is applying technologies in existence elsewhere? The efficient use of technologies by enterprises is not a simple or costless process. It involves building new capabilities: selecting the right technology, buying it, mastering its use, building institutional skills, adapting technology to the enterprises' own needs and improving it as changes occur (Lall, 2000). Technology is not sold like physical products,

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<sup>59</sup>See Murphy, Shliefer and Vishny (1989) for a modern exposition of the traditional 'big push' thesis. Rodrik (1996) uses a similar argument to advise Governments to move from one equilibrium position to another: free markets yield multiple equilibria because of linkages between different activities.

in fully embodied forms; nor does it transfer by osmosis when agents are exposed to more advanced systems of knowledge. It has important *tacit elements* that can only be mastered by effort.<sup>60</sup> The process of mastery is generally slow, incremental and path-dependent. It takes place in an uncertain environment where skills, information, networks and credit are deficient. Industry may not be able to get either the quantity or the quality it needs in such areas as new skills, technological information, standards and suppliers.

Many enterprises in developing countries may not even know how to go about learning, and have to 'learn to learn'. Given this uncertainty and unpredictability, they cannot raise capital from conventional sources. They often interact intensively with other agents in the learning process. In this process they can lose the skills and knowledge they have accumulated. Externalities are sometimes so extensive that learning is more collective than individual. This raises another coordination problem. Firms cannot invest the right amounts since they cannot predict how learning will proceed in their input suppliers. Thus, they cannot know how much their inputs will cost in the future, how reliable they will be and how technologically up to date. If exposed to competition from enterprises abroad that have already undergone the learning process, firms may underinvest in difficult technologies with costly learning processes. This is the classic case for infant industry protection, and it remains valid.

Mastering new technology is not a once-for-all task. Technology requires continuous upgrading and deepening of technologies and of human capital, as well as of supporting networks and institutions. Without this, countries can remain at the bottom of the technology ladder, where their competitive edge lies in simple assembly or processing based on cheap labour; once wages rise they lose this edge. Thus, as they master the simpler elements of technology, they have to move into more advanced technological functions. As technologies improve, they have to upgrade their own capabilities to remain competitive. As they gain competence in simple activities, they have to move into more advanced ones. At each stage, learning needs new knowledge, skills and organization. It also needs support from institutions that provide such collective goods as training, information, standards, technical support, design services or finance. At every stage, learning becomes more challenging. In the new technological context, the challenges themselves become greater.

Typical features of learning in developing countries are: poor understanding of learning by firms; lack of information on sources of technology and information; risks, uncertainty and unpredictability in learning; spillovers and externalities; weak financial and skill markets; poor or absent coordination between firms; weak or absent institutional support. Moreover, learning processes are cumulative and path-dependent; once launched, they are difficult to change. All these factors make capability development and its deepening over time dependent on government policies which, in turn, may need support from international organizations.

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<sup>60</sup>'Tacit' elements of technology cannot be fully explained or embodied in physical goods such as manuals, machines, blueprints, patents and so on. They require the recipient of the technology to invest time, effort and possibly additional resources in learning the technology. A good example is learning a new language: the physical elements of a dictionary and grammar book are necessary and useful, but becoming proficient necessarily takes time and involves practice, interaction and making mistakes.

## A varied record

Country leaders have long understood the value of industrialization and its policy needs. The early history of industrial development shows this clearly (see Reinert, 1995).

The strategies adopted by Governments varied considerably over time and among regions, reflecting differences in economic conditions as well as in ideology and history. In recent development, the most interesting differences are between (apparently similar) countries or areas—the mature Asian Tigers (the Hong Kong Special Administrative Region of China, Singapore, the Republic of Korea and Taiwan Province of China). While each pursued strongly export-oriented and private-sector-based strategies, each also had a different *vision* of desirable industrial development. These visions led them to mount different strategic responses: ‘market failures’ were, in other words, given by their national objectives. They made some mistakes, but overall the results were extremely impressive.

At one end was the Hong Kong Special Administrative Region of China, with a Government that provided good infrastructure, cheap land and low taxes, and left resource allocation to market forces. At the other was the Republic of Korea, where the government intervened extensively in the industrial structure, technology development, firm size, FDI inflows, skill creation and institution building. The resulting depth and capabilities of industry reflect their strategies: the Hong Kong Special Administrative Region of China is highly specialized and its industry lacks technological depth, while the Republic of Korea’s development of innovative capabilities approach those of mature industrial countries.

While industrialization does raise policy needs, and policies can promote its growth and deepening, history shows that most developing countries have not managed policies efficiently. This does not mean that government has no role in industrial development. Recent experience shows that the opposite strategy, of a minimal role for the state, also has substantial flaws because it tends to place too much weight on free markets that also suffer from deficiencies. There is a clear need to reintroduce a more positive role for government, but one that is very different in scope and objectives from earlier forms of industrial policy. It is here that an agency like UNIDO can provide some of the international public goods that developing countries need if they are to be more effective.

## The role of UNIDO

Given the critical role of industry in development, and the need for government policy to support industrialization, there is also a need for a publicly funded, intergovernmental body like UNIDO to provide international public goods that promote industrial development. Let us return to the earlier discussion of global public goods. There is no other international institution that specializes in the provision of such goods for industry.

Before coming to these public goods, it is important to mention that following its reform, UNIDO has developed a unique approach: service modules. These address particular industrial development problems and tackle their policy needs directly.

What are the public goods that UNIDO can provide in its area of specialization?<sup>61</sup> Let us return to our earlier discussion of 'global public goods'. The first three categories—global commons, basic infrastructure of international economic relations, and provision of humanitarian assistance and redistribution—seem too general for a specialized agency like UNIDO. However, there are particular issues here that concern industry, noted below. The main role of UNIDO revolves around the fourth category: the creation and diffusion of knowledge, including the knowledge of good governance. This role assumes particular significance in the context of growing inequities in industrial development and competitiveness consequent upon globalization and liberalization. Let us take the categories in turn.

### *ENVIRONMENT*

As a 'pure' public good, the preservation of the environment is the direct concern of all agencies dealing with potentially polluting activities. Industry is an important area for environmental concern and UNIDO has a number of activities in the environment field. At the international level, it has two service modules in this area, the Montreal Protocol and Kyoto Protocol modules. At the national level, its other environment policy service modules deal with building policy capabilities at the national and local levels. It helps Governments to formulate desirable environmental policies—setting standards, ensuring compliance and monitoring. Its cleaner production module deals with production techniques, while the pollution control module deals with the control of pollutants and management of waste. The energy efficiency module helps countries to improve their energy use and thereby reduce the damage caused by the use of fossil fuels.

### *EQUITY AND REDISTRIBUTION*

While UNIDO is not an aid agency concerned directly with promoting international equity, it can effectively address equity issues through other means. For instance, it can focus its assistance for industrial development on the least developed countries that need most help and are least able to access private sources of advice and skills. It can persuade developed countries to grant tax relief for FDI, and provide experts willing to provide technical assistance, or technology transfer, to least developed countries. Within developing countries, UNIDO can promote the least advantaged groups by helping rural enterprises or micro, small and medium-sized enterprises. The justification for providing international assistance is that Governments find it difficult to devise appropriate policies in areas that are far removed from market-based sources of help and often also from existing institutions. International investment flows do not reach these areas. The purchase of foreign advice and private consultancy services is very expensive, and it is difficult to cover the very extensive needs of rural areas and small and medium-sized enterprises (SMEs).

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<sup>61</sup>Forstner (2000) has a more detailed discussion of these issues with reference to UNIDO's current activities. Also see Martinussen (1999).

Again, UNIDO has several service modules in this area. The SME module provides help to Governments in designing and implementing strategies for SMEs and monitoring their progress. The rural energy module promotes the supply of energy to villages, mainly by the use of renewable energy sources. The agro-industries module promotes activities that provide considerable employment by helping them upgrade technology. The women entrepreneurship module addresses this very important issue by building awareness and providing information and policy advice.

## Creation and diffusion of knowledge

UNIDO is not in a position to support basic science or research activities globally. However, it can and does help developing countries in the other sub-categories: transfer of technology, building skills and capabilities, synthesising theory and experience to provide good policy advice, and helping Governments to implement good governance on industry. Under this heading, the following areas are significant.

Regarding the *transfer of industrial technology*, the need for international public goods stems from the fragmented and imperfect nature of technology markets. While market-driven flows of technology have grown greatly in recent years (via licensing, equipment, subcontracting and FDI), it remains difficult and costly for typical developing-country enterprises to access the market efficiently. Information on suppliers, prices and quality is difficult and costly to obtain. There are databases on technology suppliers and there are intermediaries that bring prospective partners together, but these are not easily accessible to smaller enterprises outside the main urban centres. Information about local supply or subcontracting capabilities is also imperfect, and difficult for investors to acquire. In addition to economic handicaps such as small and fragmented markets, poor infrastructure, instability and insecurity, low skill levels and poor governance, country 'image' is also a problem, particularly in Africa. Investment promotion agencies in many developing countries are passive and relatively ineffective, and need to be improved and streamlined. There are thus many things international agencies like UNIDO can do to promote technology transfer.

UNIDO can also help countries *strengthen the technology infrastructure*. The so-called MSTQ institutions (metrology, standards, testing and quality) are the backbone of technical activity in any country. In addition, there are institutions for technical extension to SMEs, technology finance, R&D and marketing assistance, and policies and institutions for stimulating R&D within private enterprises. While most countries have these institutions, their effectiveness varies greatly. A weak technology infrastructure can be a drag on competitiveness and upgrading. Knowledge of how it can be improved and made more relevant to industrial needs is a valuable global public good. Europe and the developing world now have considerable experience of technology institution reform. UNIDO can help synthesize and transfer the experience to other developing countries as well as upgrading their technology infrastructure. Particular needs are the encouragement of ISO 9000 and 14000 standards, strengthening of testing and calibration services (with

greater accreditation of private providers) and strengthening of links between research laboratories and industry.

The *collection and analysis of industrial information* are vital global public goods that UNIDO must, and is best placed to, provide. The first comprises the compilation of statistical information on aspects of industrial performance and competitiveness on a comparable basis across countries. The second comprises the analysis of these data and of industrial trends and issues more generally. There is no other international agency that studies industrial development and policy across countries on a sustained basis (see, for example, UNIDO, 1998 and Sercovich et al., 1999). Countries have to turn to private consultants if they want to learn about 'best practice' from other, more successful, countries (although the World Bank has carried out some analysis on industrial policy in the past).

Although disparities in industrial performance have grown in recent years, little is known about their dimensions or causes; yet without this knowledge it is impossible to devise meaningful policy responses. In addition, industry in developing countries is constantly faced with new issues that need research and analysis. Consider, for example, the impact of the abolition of the Multi-Fibre Agreement on the exports of manufactures of a large number of development countries. Which technologies and skills will be most relevant? Which countries may be well placed, given their labour costs, to retain or increase market shares in the face of free competition from large countries like China and India? What do countries need to do to enhance their competitive position? Other emerging issues include: the impact of WTO measures such as requirements on removal of trade barriers and Trade-Related Investment Measures; the effect of the Internet on international or domestic trade; new skill and organizational needs for competitiveness; issues in biotechnology; and the stimulation of local R&D by TNCs. A sound analysis of these and numerous other issues would be extremely valuable.

One growing need in developing countries is *information for benchmarking industrial performance*. Large industrial firms in developed countries constantly benchmark technical performance against major competitors, while Governments assist benchmarking efforts by sectors and by SMEs.<sup>62</sup> Developed country Governments increasingly benchmark national competitive performance in various areas (skill creation, technology, institutional performance, business costs and so on). Some standard benchmarks are available from published data, but others have to be developed and are often costly. Many Governments in developing countries are not able even to collect available data, and are even less able to build other benchmarks. UNIDO can provide a very useful policy tool by disseminating or building competitive benchmarks (see Sercovich et al, 1999).

We also noted the vital need for *analysis to provide alternative perspectives on economic phenomena and on policy*. Different perspectives on the complex area of industrial development policy remain essential. UNIDO is uniquely endowed to develop

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<sup>62</sup>In the UK, for instance, large companies use the Productivity On-Line Benchmarking (PROBE) database to evaluate themselves against several thousand European leaders. This benchmark is produced by the Confederation of British Industry. A developing-country Government could encourage the private sector to launch a similar effort with UNIDO assistance. The UK Government offers subsidized benchmarking services to SMEs to help raise their productivity and technological levels (for further information).

strong and *independent* analytical capabilities on industrial development policies and strategies at the service of its member countries.

The *building of skills and capabilities* in the industrial arena can be an important global public good, particularly in the least developed countries that lack the internal resources and information to do it well. This is a wide mandate. It applies to helping skill formation within industry, for specific functions (standards, quality management, sub-contracting), activities (resource processing or fostering emerging technologies), or institutions (training, technology and so on).<sup>63</sup> It also applies to capability building in policy formulation, implementation and monitoring. Apart from the provision of information and analysis, international assistance is uniquely placed to help Governments understand which policies and instruments have worked elsewhere, and which have not, in both similar and more advanced economies.

The organization of government departments and procedures may also need to be improved, as may private sector associations and their links with the Government. The accretion of policies and regulations in developing countries often imposes heavy transaction costs on industrial enterprises without accomplishing basic policy objectives efficiently. Many regulations breed corruption and delay. They generally weigh more heavily on smaller enterprises that lack the resources and connections to 'work the system'. Business costs are now an important factor in international competitiveness, and global investors weigh them carefully when choosing sites for non-resource based investments. Advising Governments on the removal of such unnecessary and inefficient regulations can be an important public good, while providing international best practice can be a global public good.

UNIDO can act as an independent adviser when Governments use private sources of advice and information. A multitude of consultants now offer studies and advice on all aspects of industrialization, and it is difficult for Governments to evaluate their real capabilities. Private consultants can also face conflicts of interest as they serve a number of clients. UNIDO can help Governments evaluate their advice.

UNIDO has an important *global forum role*, involving fostering and participating in international meetings, conventions, norms and standards. This normative role is supported by its unique base of data on industrial performance, and UNIDO is striving to improve and accelerate the collection of data by member countries. It is building its research capabilities and re-launching its publications.

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<sup>63</sup>Everyone recognizes the significance of enterprise training in industrial competitiveness, yet firms generally underinvest in such training. They are often unaware of the productivity and technological benefits of raising the skills of the workforce, or do not know how to go about providing effective training. Most fear that employees will leave for competitors after the training. A study undertaken by the World Bank (Tan and Batra, 1995) suggests that a sizeable proportion of enterprises in developing economies provide no worker training at all, either informal on-the-job or structured formal training. This problem is especially pronounced in small and medium-sized enterprises, where more than half the firms give no formal structured training, and over a third do not provide any informal training. This suggests that several constraints on training may be at work – poor information about the benefits of training, high training costs, the inability to exploit scale economies in training, weak managerial capabilities, absence of competitive pressures, or market imperfections. There is much that UNIDO can do, perhaps in collaboration with the ILO, to help Governments formulate better training strategies geared to industrial competitiveness.



UNIDO can work with the private sector in *promoting public-private partnerships and facilitating private-sector development*. Its role in fostering SMEs and entrepreneurship can be particularly valuable. UNIDO can also work with civil society (universities, research institutes, non-governmental organizations (NGOs) and so on) to provide the global public goods they need to help and guide industrial development.

Finally, it is important to remember that the various functions of UNIDO complement and feed into each other, providing economies of scale and scope. Thus, it is vital that it undertakes both normative and operational activities, to allow for greater learning, better policy advice and data collection, and closer interaction with Governments. This argument has been made cogently for the World Bank (Krueger, 1998; Gilbert *et al.*, 1999), and it applies with equal strength to UNIDO.

In essence, the role of UNIDO in the emerging competitive environment for industry derives from the inefficiencies and inequities globalization is creating. Freer market can yield efficiency benefits to developing countries, but they also impose costs and exacerbates inequality and marginalization within and across countries. These problems arise from market and institutional failures and the lack of ability of many countries to cope without careful preparation for the competitive world. There is now much greater acceptance of a positive role for government in development. International institutions are also accepted more positively. They support national Governments in the economic field, by furnishing the global public goods that national Governments cannot provide and helping them to fulfil their own functions more effectively. In the industrial sector, while liberalization has helped market forces to provide many of the necessary conditions and inputs required, it is not sufficient to achieve the kind of development needed for global welfare. Much remains to be done in the policy sphere, and in the international arena UNIDO is the only organization capable of doing this.

## Chapter 4

# The evolution of UNIDO

UNIDO presents an interesting case study in UN reform for a number of reasons. First, in the recent past it has been charged with many of the failures alleged to have affected the UN as a system, particularly lack of administrative and operational efficiency, ineffectiveness and lack of responsiveness to client needs and of relevance.<sup>64</sup> Second, it has recently been the subject of intensive scrutiny by both donor and recipient countries. Third, its reform programmes since 1993 have been extensive and far-reaching. Fourth, its transformation since 1997 is acknowledged to have been one of the most comprehensive and successful in the UN system.

For all these reasons, the story of UNIDO's reform process—and particularly the lessons to be learned from this—may be especially relevant and useful to others facing similar challenges of reform and to their development partners. Along the way, mistakes have been made and rectified in UNIDO's reform process; many approaches have been tried—some successful and some not. But the end result is that the organization has been put on a new dynamic path with increasing efficiency and impact.

### The beginnings

The focus of the work of the United Nations in the years after its establishment was on reconstruction and decolonization in the context of the Cold War. In 1948, the Secretary-General was authorized to carry out TC through some specialized agencies, initially with an annual budget of less than \$300,000. Funding for this activity increased considerably with the establishment in 1950 of the *Expanded Programme for Technical Assistance* (EPTA), which was financed by voluntary contributions outside the regular budget of the UN. The first-year budget for EPTA was some \$20 million.

In the early 1950s, at the request of ECOSOC, the UN Secretariat prepared a number of studies on industrial development. In 1956, the Secretariat created an *Industry Section*. In 1957, a more systematic programme of studies was approved. These addressed such topics as small-scale industry promotion, environment planning, industrial

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<sup>64</sup>See UNIDO (1996a, 1996b) and *Assessment of UNIDO* (1997).

management in developing countries, capital intensity in industry, and capital investment and productivity.

In the late 1950s and early 1960s, rapid decolonization considerably increased the number of developing countries in the UN. By 1965, the number of founding members had doubled to 118. The scope and orientation of the UN changed; more attention was now being paid to economic development issues, including industrial development.

In 1960, ECOSOC established a *Standing Committee for Industrial Development*. During its first meeting the committee recommended the establishment of a *Centre for Industrial Development*. In 1961, through General Assembly Resolution 1712, the Centre was established within the Department of Economic and Social Affairs of the United Nations. Its objective was to record, analyse and disseminate the experience gained in technical assistance programmes in support of industrialization. The Centre also aimed to provide the means for better coordinating all the activities in the industrial field carried out by the United Nations, the regional economic commissions and the specialized agencies.

It is clear that the role originally envisaged for the Centre involved only *normative* activities. However, even as early as this, the question was raised whether the UN should establish a specialized agency for industrial development which would probably have a wider set of tasks. The ECOSOC Standing Committee was asked to prepare a report on the matter. In 1963, it recommended that such an organization should be set up; it would report to the General Assembly. The matter was taken up by the General Assembly in 1966 on the back of rapid developments concerning UNCTAD and UNDP.

As explained earlier, the tension between the different perceptions and priorities of the developed and the developing countries came to a head at the first UN Conference on Trade and Development (UNCTAD) in 1964. The Conference clarified the demands of the developing countries. Recognizing the need to industrialize developing countries, it also set clear objectives, including the extension of industrial production in developing countries, in part through the managed transfer of production from the North to the South, higher and stable raw material prices, and mechanisms to achieve this. Another objective was an increase in the technical cooperation activities of the UN.

## UNDP and UNIDO

In 1965, in response to the demands of the developing countries, EPTA and the United Nations Special Fund—established in 1958 to deal with larger and more comprehensive technical assistance projects, and for investment preparation—were combined to form UNDP, which was charged with providing a *framework for coordinating the technical cooperation of the whole UN system*. Soon after UNDP came into existence, it was decided, through Resolution 20/89 of the General Assembly, to establish UNIDO as a special organ of the United Nations. This was a compromise solution: the developing countries (the Group of 77) wanted a specialized agency with its own political decision-making governing body (and eventually normative activities), while the industrialized countries preferred a lower-profile organization under the direct control of the General Assembly.

In November 1966, through Resolution 21/52 of the 21st Session of the General Assembly, this compromise resulted in the creation of the United Nations Industrial Development Organization<sup>65</sup> as the organization responsible for *coordinating the industrial development activities of the United Nations*. Resolution 21/52 is generally regarded as UNIDO's founding document, and in January 1967 UNIDO was formally established in Vienna, Austria.

Initially a large part of UNIDO's activities were a continuation of the work of the Centre for Industrial Development, as a global forum and for normative or analytical functions and information dissemination. This was because technical cooperation activities had still to be developed. Donor member States, however, considered that any such activities carried out by UNIDO should largely be funded outside the budget, mainly by UNDP.

It is interesting to note the small budget that was originally envisaged when UNIDO began life as the Centre for International Development. Mr. Ibrahim Helmi Abdel-Rahman, the first Executive Director of UNIDO (1967–1974), recounts that during his first visit to Washington to attend the World Bank/IMF Annual Meetings in September 1963, he met the then President of the World Bank, Mr. George Woods, who said to him, 'Welcome to the man who will industrialize the world with four million dollars.' Mr. Abdel-Rahman replied that his job compared well with George Woods' task which was to develop the whole world with four billion dollars.<sup>66</sup>

UNIDO was originally organized into three major divisions—Policy and Analysis, Technology, and Manpower, Research and Services—and an Operations Division. Staff in the three major divisions undertook studies and held seminars, and helped to design and manage projects which were the primary responsibility of the Operations Division supported by field advisers.

In 1969 Sir Robert Jackson prepared his famous Capacity Study for UNDP.<sup>67</sup> Its main recommendations were largely welcomed by member States; their aim was to strengthen and centralize the planning and coordination of all UN technical cooperation in UNDP which, as a central funding organization, would also channel most of the funds to the specialized agencies.

However, the main specialized agencies, whose mandates all combined global forum and normative responsibilities with operational activities, did not welcome this limitation of their autonomy. In particular, they were unhappy with the study's implied separation of global forum and normative activities on the one hand—which were evidently the full responsibility of these agencies—and operational activities on the other.

In response to the Capacity Study recommendations, in 1970 UNDP started a new system of country planning and five-year rolling funding for the country programmes, in the form of the Indicative Planning Figure (IPF). IPFs were to be the main mechanisms for coordination of UN technical cooperation. However, the funding channelled through

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<sup>65</sup>Originally it was called UNOID, the United Nations Organization for Industrial Development.

<sup>66</sup>Abdel-Rahman, 1995, p. 50.

<sup>67</sup>For details see, R. Jackson, *op. cit.*, chapter 1, page 26.

UNDP did not grow as anticipated. And, as other funding directly available to the specialized agencies remained outside the country programming process, the central funding role of UNDP and the coordinating role of the country programme gradually deteriorated.

At first, UNIDO was served well by this system. The volume of its technical cooperation increased from \$12.7 million in 1970 to \$40.0 million in 1976. Some 80 per cent of this was funded by UNDP. This was a reflection of the high and growing demand for industry-related technical cooperation from the developing countries, which had a direct influence on the allocation of UNDP funds available to them.

At the same time as this growth in the volume of UNIDO's operational activities, the political dimension of the development debate between developing and developed countries led to an important milestone for the organization.

In the context of General Assembly discussions related to the establishment of a New International Economic Order,<sup>68</sup> the Second General Conference of UNIDO, held in 1975 in Lima, Peru, adopted the *Lima Declaration and Plan of Action on Industrial Development and Cooperation*. In the Declaration, for the first time, quantified targets were agreed for the industrial development of developing countries (they were to have 25 per cent of world industrial production by the year 2000; the share in 1974 was only 7 per cent). The 'Plan of Action' drawn up to implement the Declaration included a detailed list of general and specific measures aimed at achieving the target.<sup>69</sup>

As part of the 'institutional arrangements' in the Plan, it was recommended to the General Assembly that UNIDO should be converted into a specialized agency. It was also recommended that an *Industrial Development Fund* be established to channel voluntary contributions to the technical cooperation activities of UNIDO so that the organization could contribute to the achievement of the objectives of the Declaration.

The Declaration specified that UNIDO should have both global forum/normative and operational responsibilities:

UNIDO should not only intensify and expand its present operational activities and action-oriented studies and research programme in the field of industrial development but should include among its activities a system of continuing consultations at global, regional and sectoral levels for the purposes set forth in paragraph 61 (d) above. UNIDO should be prepared to serve as a forum for negotiation of agreements in the field of industry between developed and developing countries and among developing countries themselves at the request of the countries concerned. Paragraph 61 (d) specified that these consultations would be in respect of demand and supply, availability of production factors and their costs, the possibilities and conditions of investment and the availability of appropriate equipment and technologies, with a view to facilitating ... the redeployment of certain productive capacities existing in developed countries and the creation of new industrial facilities in developing countries.<sup>70</sup>

To help meet the target that developing countries should achieve 25 per cent of world industrial production by the year 2000, UNIDO created a new instrument, the

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<sup>68</sup>The New International Economic Order is explained in more detail in chapter 3.

<sup>69</sup>Lima Declaration and Plan of Action on Industrial Development and Cooperation, 1975.

<sup>70</sup>Op. cit., paragraph 66.

*System of Industrial Consultations*.<sup>71</sup> To this end, there was also restructuring of the organization to substantially increase traditional activities, but especially to develop investment promotion. A new Research Centre was created to serve a new System of Consultations Division and support technical assistance initiatives.

More controversial was the System of Consultations, whose aim was to focus 'international cooperation to follow more enlightened paths [...] and work towards greater equity in the sharing of the general wealth'.<sup>72</sup> Not surprisingly, this was not particularly welcomed by the developed countries.

These countries did welcome, however, the expansion of UNIDO's investment promotion programme to include investment promotion offices funded by host countries in Brussels, Zurich, Cologne, Tokyo, New York, Paris, Vienna and Warsaw. There were some objections by developed countries to UNIDO's Warsaw office, which was seen as a dangerous way 'to promote capitalistic influence in the third world'.<sup>73</sup>

It was not until 1979 that a compromise was reached on the exact nature and responsibilities of UNIDO as a specialized agency. A major bone of contention was the idea that UNIDO should also be a financial organization, promoted by the Group of 77. This was not acceptable to the developed countries and was left out of the Constitution, adopted on 8 April 1979 in Vienna at the second session of the United Nations Conference on the Establishment of UNIDO as a specialized agency. The Constitution did include, however, both the global forum/normative and the operational tasks described above.<sup>74</sup> The Constitution stated that the principal objective of the organization was to promote and accelerate industrial development in developing countries with a view to assisting in the establishment of a new international economic order. A subsidiary goal was to promote industrial development and cooperation at the global, regional and national levels. (Countries with economies in transition were added later as targets for UNIDO's assistance through a re-interpretation of UNIDO's Constitution.<sup>75</sup>)

Even with this compromise, the developed countries were not convinced that a UN specialized agency for industrial development was necessary. Another separate organization would mean another separate assessed contribution, as well as increased demand for voluntary contributions. Other issues weighed too. Some countries had lingering doubts about the desirability of helping to create competitors, especially to the private sector. There was also concern about duplication and coordination within the system, and the loss of control to a majority which consisted of developing countries. The objections and doubts of developed countries contributed to the delay in the ratification of UNIDO as a specialized agency. They also influenced the degree to which these countries were willing to fund the organization, particularly in the form of voluntary contributions.

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<sup>71</sup>Rahman Khane, 1995, pp. 57–59.

<sup>72</sup>Rahman Khane, 1995, pp. 57–58.

<sup>73</sup>Rahman Khane, *op. cit.*

<sup>74</sup>UNIDO's normative function was added to in 1985 with the establishment of its annual Industry and Development Global Report.

<sup>75</sup>*Assessment of UNIDO*, 1997, p. 7.

## **UNIDO as a specialized agency**

On 1 January 1986 UNIDO formally became the 16th specialized agency of the United Nations, able to start operations with its own programme and budget and assessed (non-voluntary) contributions from its member States. However, the newly independent organization immediately had to deal with a financial crisis—an effective shortfall in the first biennium of some 30 per cent of the regular budget. There were two causes. The budget was prepared on the basis of the US dollar, while most of the costs of the organization were linked to the Austrian schilling; at the same time the value of the US dollar underwent a rapid decline. In addition, several major (developed) member States paid their assessed contributions late or not at all. In consequence the organization suffered a serious loss.

When the new Director-General, Domingo L. Siazon Jr., took office in 1986, he planned changes in the orientation of the organization to adjust to changes in demand from developing countries and to increase responsiveness, effectiveness and transparency—efforts which were seriously hampered by this financial crisis. His intentions were to focus more on industrial cooperation with private companies, human resource development, small and medium-sized enterprises, industrial rehabilitation and enterprise-to-enterprise cooperation, and to foster a more integrated approach to industrial development; these intentions could only partially be realized. Important activities under approved programmes and work plans could not be carried out. This situation continued through the next biennium.

A further problem was that although member States cried out for increased effectiveness and the restructuring of the organization, the same member States continued to push 'candidates for high-level posts without very much consideration of the candidates' actual capability'.<sup>76</sup> UNIDO was also forced to continue with a system of as many as five Deputy Director-Generals.

On the other hand, voluntary contributions (additional to the regular budget) to UNIDO's technical cooperation activities grew and grew. The annual volume of technical cooperation increased from \$40 million in 1976 to \$92 million in 1982. Before 1982, it had remained at the same level for four years because of a funding crisis at UNDP and large variations in the value of the US dollar. From 1987, UNIDO's technical cooperation work began to grow again as UNDP's funding recovered.

Supporting funds increased to \$120 million in 1988, and \$159.6 million in 1990. This rapid growth in technical cooperation, in combination with the funding crisis in the regular budget, changed the balance between the organization's global forum/normative and operational function. Slowly, the volume of studies and analytical work, and of information dissemination, decreased—including work related to technology transfer. As most of UNIDO's extra-budgetary funding was for 'special purposes'—the donor decides which activities they fund—UNIDO's influence on the direction of these activities was limited.

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<sup>76</sup>Siazon, 1995, p. 67.

After 1990, UNIDO also had to meet the new challenge of assisting the countries of Central and Eastern Europe and the former Soviet Union to make the difficult transition to competitive market economies. At the same time, Africa's increasingly desperate economic plight could not be ignored. In response, UNIDO tried to use its regular budget to support Africa's development under the Industrial Development Decade for Africa (IDDA) programme and from its IDF.

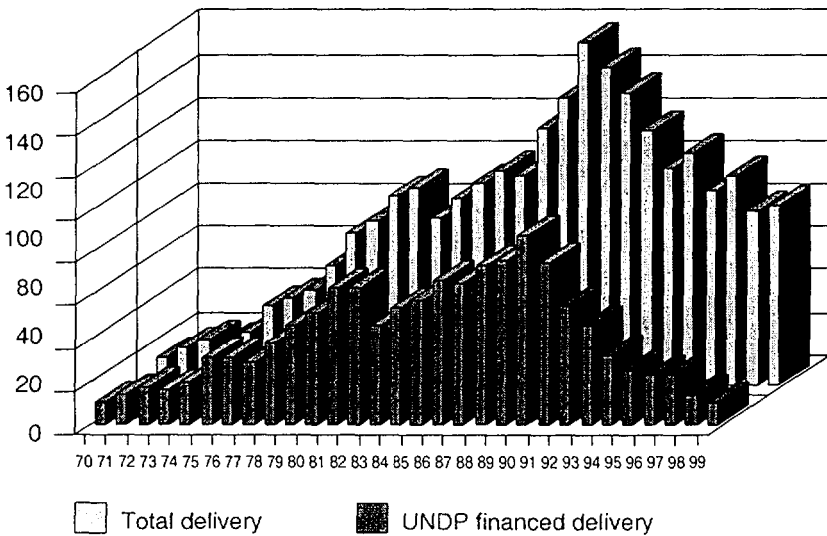
1990 was also the year in which funds for UNIDO's technical cooperation peaked at \$159.6 million. After 1990, the volume of technical cooperation fell rapidly to \$118 million in 1993 and to \$91 million in 1996. Since then it has stabilized between \$80 million and \$90 million. Virtually the whole decline was caused by the sharp decrease in UNDP-financed activities, which have now dwindled to about \$10 million for reasons explained below.

As the world changed and donors became less inclined to support public-sector projects, UNIDO received less UNDP funding and had to rely more on funds from other sources.

From 1994, projects financed by the Multilateral Fund for the Montreal Protocol, a highly specialized fund, have become an important component of funding, having some 40 per cent of the total. A similar share is contributed by governmental donors, mainly through the IDF. The development of UNIDO's annual volume of technical cooperation is shown figure 3.

Figure 3 shows that until 1991-1992 UNIDO's technical cooperation activities were highly dependent on UNDP funding, and that the decline in total volume after 1991 is almost the same as the decline in UNDP funding. The dependence on UNDP funding

**Figure 3. Funding for UNIDO Technical Cooperation**  
*UNDP and total UNIDO TC. funding (in millions of US dollars)*





was helpful as long as UNDP played its original role as a central funding organization which programmed available funds in a sectorally unbiased manner in close consultation with recipient Governments and the specialized agencies.

Activities related to industrial development were clearly among the top priorities of developing countries. However, with the start of UNDP's fifth programming cycle in 1992, the funding situation changed. UNDP funding for UNIDO programmes and projects declined rapidly for three reasons: a substantive refocusing of UNDP, in part away from the industry sector; an increasing preference for national execution of projects (in which a UNDP-funded project is carried out by the national authorities), which unfortunately was interpreted by UNDP as largely excluding the specialized agencies; and a gradual but consistent decline in member States' contributions to UNDP's core resources.<sup>77</sup>

Direct funding to UNIDO from a variety of other sources increased gradually until 1990, and stabilized thereafter at around \$70–75 million. The IDF, agreed in 1979 with a target annual funding of \$50 million, never received more than \$30 million. In spite of the agreement, several donors actually considered that UNIDO should obtain most of its funding for technical cooperation from UNDP. As a result, UNIDO never received the financial means to set its own course and be more responsive to the needs of developing countries. In fact, even a part of these direct contributions to UNIDO by donor Governments, although extra-budgetary, is in support of global forum related activities, for example funding related to the organization's investment promotion network.

## Beginning of reforms and looming crisis

The Fifth General Conference of UNIDO, held in December 1993 in Yaoundé, Cameroon, with Mauricio de Maria y Campos as the new Director-General (1993–1997), was another milestone in UNIDO's history. It was the first attempt at major reform of the organization. It tried to address the changes in the world situation, particularly rapidly increasing globalization with its 'strong trends towards deregulation and restructuring which require appropriate responses in the field of industrial development'.<sup>78</sup> It did this through a unanimously approved far-reaching reform programme intended to improve the organization's realization of its objectives and to strengthen its role as the central coordinating agency in the UN system for the promotion of the industrialization of developing countries and countries with economies in transition.

The General Conference also recognized a need to better direct UNIDO's work in industrial development to achieve the socio-economic objectives of increased employment and income in less developed regions—particularly Africa—and for vulnerable sections of the population. Importantly, it was felt that UNIDO's technical cooperation had to refocus, away from its previous concentration on support to governmental institutions and

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<sup>77</sup>By 'core resources' is meant voluntary contributions programmable by UNDP, which are largely allocated to individual countries and available for the UNDP programmes there.

<sup>78</sup>De Maria y Campos, 1995, pp. 74–78.

state-owned enterprises towards providing policy advisory services for the private sector—particularly SMEs. UNIDO also needed to cut down the fields of assistance and industrial sectors it covered, to better reflect its core capabilities, technical expertise, and resources. It needed to prioritize amongst activities, regions and sectors.<sup>79</sup>

The *Yaoundé Declaration* did not specifically address the issue of UNIDO's operational activities versus its global forum function. The declaration reiterated that

'the major means of achieving UNIDO's objectives of environmentally sustainable and equitable industrial development remain investment promotion, technology transfer, development of human resources and the creation of an enabling environment, both nationally and internationally, for industrial growth and competitiveness'.

These objectives clearly included elements of both operational and global forum activities. The regular budget for 1994–1995 retained all the global forum activities that UNIDO had been performing. Only the System of Consultations, the most politically oriented activity, became less visible. However, when the reform—which was unanimously approved—was implemented in 1995, the USA, the largest contributor, announced its intention of withdrawing from the organization. The result was a 25 per cent cut in UNIDO's regular budget. It was against this background that UNIDO set out its first major attempt at reform in January 1994.

During 1994–1997, UNIDO carried out a far-reaching process of reform which aimed to refine its relevance in a changed global economic and political environment by focusing its services and improving managerial and administrative efficiency.<sup>80</sup> In this period, UNIDO:

- Abolished 101 posts, including five Deputy Director-General (ODG) posts out of eight.
- Saved funds and increased efficiency by contracting out computer support, language services, documentation and conference facilities management.
- Reduced support costs to 14.5 per cent of the total costs of delivery, from 18.8 per cent in 1992–1993 and 22 per cent in 1994–1995.
- Cut staff from 1,373 at the end of 1992 to 755 at the end of June 1997—a 42 per cent reduction.
- Improved internal procedures, and reduced the number of steps and signatures required to finalize tasks.
- Introduced electronic mail and drastically cut paper communications.
- Delegated authority and control to staff in the areas of travel approval, programme development and expert recruitment.
- Introduced a new evaluation and quality assurance system based on seven quality management principles of accountability and client focus.
- Decentralized certain activities to the field to better serve the needs of clients.

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<sup>79</sup>De Maria y Campos, 1995, pp. 75–76.

<sup>80</sup>*Assessment of UNIDO*, 1997.

A dual role was envisaged for the organization which combined the provision of technical cooperation services and acting as a global forum for industrial development issues. In its role as a global forum, UNIDO was to give more emphasis to upstream policy advice and institutional development. The organization also adopted a more focused sectoral, thematic and geographical approach. It focused its sectoral activities on:

- Agro-based industries (food processing, leather, textiles and wood processing).
- Chemical industries (biotechnology, water management, medicinal plants, building materials and organic chemicals).
- Engineering industries (electronics, metalworking and machine tools, particularly agricultural machinery).

Seven themes provided a focus for the organization:

- Strategies, policies and institution building for global economic integration.
- Environment and energy.
- Small and medium-sized industrial enterprises.
- Innovation, productivity and quality for international competitiveness.
- Industrial information, investment and technology promotion.
- Rural industrial development.
- Africa and the least developed countries: linking industry with agriculture.

Africa and LDCs became the geographical focus, but UNIDO's work was to cover all developing regions and economies in transition.

Two organizational restructurings in 1994 and 1996 led to drastically reduced costs in some areas and to better coordination. The organization now had a flatter structure with fewer divisions and a lower ratio of general service to professional staff—over 90 per cent of staff reductions were made in non-substantive divisions (administration and support services). The consolidation of critical planning and oversight functions in a new Policy Coordination Office, and the merger of UNIDO's programming and funds mobilization functions, in particular, were significant improvements.

Other improvements were made. In the area of personnel policies and management, a revised recruitment scheme, and a new system for staff performance evaluation, placement and promotion was introduced. Improvements in financial management led to reductions in expenditures on administration and operational support, more efficient usage of financial resources, more transparent and effective monitoring and reporting, and the incorporation of UNIDO's thematic priorities into its budgeting methodology.<sup>81</sup>

Guidelines issued in April 1996 for the management of UNIDO's services further streamlined and focused services in line with the new thematic priorities.

As a result of these restructurings, costs decreased, efficiency improved, and the demand for UNIDO's services increased significantly.

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<sup>81</sup>*Assessment of UNIDO*, 1997, p. vii.

From a high point in 1990 of \$159.6 million, the level of annual project delivery had fallen until 1995 when the restructuring began to take effect. In 1995, delivery rose above the 1994 level by \$7.5 million. Although delivery fell in 1996 (largely because of the discontinuation of the International Centre for Genetic Engineering and Technology, which became an independent entity), in 1997 delivery surpassed the 1996 level by more than \$6.5 million.

But, as we shall see, these reforms were still not enough to convince UNIDO's major donors and some recipient countries of its continued relevance and effectiveness. Gradually, but surely, dissatisfaction gathered momentum. The results were a crisis of confidence in 1997, financial problems brought about by a build-up of arrears and non-payment of assessed contributions, a severe fall in UNDP funding, and a series of drastic budget cuts.

In summary, UNIDO was created largely at the instigation of the developing countries. They perceived industrial development as an important component of their long-term balanced development strategy, and anticipated significant support for this objective from the new organization. However, the organization never received the financial support from the developed countries that it needed to develop and deliver the support demanded. This was despite the fact that the financial requirements had been agreed by all member States through either the regular budget or the IDF target set in 1979. UNIDO has always had to adjust its programmes, both in volume and in content, to the wishes and limitations of individual donors.

The regular budget, through which the organization, in agreement with all its members in the forum of the General Conference, defines its priority programme and activities, has invariably been insufficient for the mandate and tasks set for the organization and the expectations of its members. Furthermore, even this low budget has been consistently underfunded. UNIDO's financial problems have constantly undermined its quest for relevance and for effectiveness and impact.

UNIDO was created on the basis of an uneasy compromise between developed and developing countries. The tension continued throughout its earlier history. Indeed, many of the organization's past problems had their origins in this compromise, which finally broke down and led to open dissatisfaction in 1997.

## Chapter 5

# From crisis to the Danish Assessment and the Business Plan

Despite having undertaken significant reforms in 1993–1997, UNIDO's difficulties reached crisis point in 1997. Why did this occur at this point, and why did it threaten the very survival of the organization? A full answer requires going back to what had happened at UNIDO since the watershed Yaoundé General Conference in 1993.

Since Yaoundé, when all member States had enthusiastically endorsed the reform of UNIDO, the organization had forged ahead with a series of extensive changes. These changes were largely prompted by the findings of a 1992 study commissioned by the Danish Ministry of Foreign Affairs which examined UNIDO's comparative advantages, areas of concentration, organization and resources.<sup>82</sup> In quite a short time, UNIDO had tried to adjust to new global realities. It had tried to cater for a new set of clients—the now independent countries of CEE and the FSU. It had tried to focus its substantive programmes on priorities that better reflected the new demands of recipient countries. It had done this by elaborating development objectives, by developing thematic and sectoral priorities, and by a geographic priority on LDCs, especially Africa.

With this new focus it had tried to streamline its management and administration, and had achieved a flatter organizational structure with less bureaucracy. In short, it had tried to make itself a very different organization from the one that existed before 1993: better at meeting the new support needs of developing countries and countries with economies in transition, more effective in delivering high-quality services, and more efficient in the utilization of increasingly scarce budgetary resources.

### United States withdrawal

Many member States recognized these achievements, particularly after 1995, but felt that they did not go far enough. As a result, confidence in the organization was still lacking, and its relevance was still questioned.<sup>83</sup> This was the atmosphere in which the United

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<sup>82</sup>*A Future UNIDO. A Study on UNIDO's comparative advantages, areas of concentration, organization, and resources*, 1992.

<sup>83</sup>*Assessment of UNIDO*, 1997, p. vi.

States—the biggest contributor to the organization—decided not to pay its contribution in 1994, and announced its withdrawal in December 1995. The move was much regretted by many member States, including major donor countries. The US decision was seen as premature as it was taken before the reforms had been given a chance to succeed. Ostensibly, the US withdrawal was for ‘budgetary reasons’.

The US withdrawal was a body blow to the organization; its repercussions are felt to this day. It put the organization in the perilous position of having to manage without 25 per cent of its regular budget. Worse, the organization was diminished by the absence of the world’s major economic and political power.

A common view within the organization, and amongst influential commentators outside it, was that the US withdrawal had placed the organization in check, forced it to sacrifice the dividends of reform in order to survive and to maintain its relevance, and weakened the very logic and objective of reform. This view was supported by an increase in the effective demand for UNIDO’s services as measured by what its clients were willing to pay for its services. Between 1993 and 1996, the organization not only maintained its technical cooperation delivery levels; the value of projects approved for funding rose by 40 per cent.

The disaffection of other leading donor countries compounded the problems caused by the US withdrawal. From 1995, when fundamental aspects of the reform had been completed, UNIDO again had to confront doubts about its continued relevance. Two influential development commentators—Ingvar Carlsson, former Prime Minister of Sweden, and Shridath Ramphal, former Secretary-General of the Commonwealth—published in 1995 a damning report, entitled ‘The Global Neighborhood’, which proposed that serious consideration be given to closing UNIDO down. UNCTAD was also slated for closure.<sup>84</sup>

Denmark (in November 1994 at the meeting of UNIDO’s Industrial Development Board) and the United Kingdom threatened to withdraw from the organization unless significant progress was made before the General Conference in 1995. After this General Conference, reform work gathered pace, spurred by the Carlsson–Ramphal report. Both Denmark and the UK, while maintaining their threat of withdrawal, announced that they would reconsider their position in the course of 1996 if progress was made in reform.

Other countries—Australia, Canada—did indeed withdraw from the organization, largely on the grounds that they were not getting value for money.<sup>85</sup> Discontent was also expressed by New Zealand. All the major English-speaking countries—the USA, the UK, Canada, Australia and New Zealand—seemed to have lost faith or to be rapidly losing faith in the organization, many for reasons that reflected their own domestic political agendas and priorities.<sup>86</sup>

<sup>84</sup>Commission on Global Governance, *Our Global Neighborhood: The Report of the Commission on Global Governance*, Oxford: 1995.

<sup>85</sup>Report of the Joint Standing Committee on Treaties: *Australia’s withdrawal from UNIDO*, 1996; Canada left UNIDO on 1 January 1994.

<sup>86</sup>Australia—and to a lesser extent New Zealand—wanted to concentrate resources on institutions in the region where they had greater interest and responsibilities. Like the US and the UK they both questioned the continued relevance in the changed global context of a publicly funded body devoted to promoting industrial development. The US position was alleged to reflect a ‘strong, anti-internationalist ideological trend in the United States Congress’. See Urquhart, ‘Blaming the Storm on the Ship’, 1996

At the same time Germany, the largest contributor to UNIDO's 'voluntary funds', expressed strong dissatisfaction and suspended its voluntary contributions, including the provision of Junior Professional Officers (JPOs) and Associate Experts, key staff— young and often extremely capable—who serviced UNIDO's field offices.

UNIDO also faced renewed calls for merger with other UN organizations under threat, principally UNCTAD and UNDP. Discontent and calls for merger were coupled with a very unsatisfactory financial situation. UNDP funds were dwindling rapidly due to UNDP's own difficulties and its move towards national execution of projects.

This was to the particular detriment of specialized agencies like UNIDO which were very dependent on UNDP funds. Arrears caused by late or non-payment of assessed contributions amounted to \$98.7 million for the period 1986–1996, with an additional \$44 million for 1997. Almost half of these arrears—\$61.3 million—was owed by the United States, which was no longer a member of the organization.

All these events culminated in a crisis for the organization. It is important to explore in a little more detail why matters came to a head in 1997, in particular, why member States were dissatisfied with UNIDO, and the steps more enlightened member States took to rectify the situation in the form of the Business Plan and the 'Danish Assessment' of the organization.

### **The motives behind the 1997 crisis**

Many reasons underlay the dissatisfaction of member States, especially major donor countries, with UNIDO, which reached a boiling point in 1997.

These reasons fall into two groups: emerging trends in the external environment affecting wider multilateral cooperation, which conditioned the general attitude of member States towards UNIDO; and aspects of UNIDO itself which gave rise to questions about its relevance and the effectiveness of its performance. Many of these questions are not unfamiliar; they reared their heads in the general case for reform of the UN made in earlier chapters. Some, however, are new, at least in emphasis, especially those that concerned the responsiveness of UNIDO to the needs of its clients.

Let us begin with the first group: the factors conditioning multilateral assistance in general which also affected donor countries' support of UNIDO.

During this critical period, the economies of the more advanced, richer industrialized countries unexpectedly slowed down. This undoubtedly posed a major challenge to multilateral cooperation. Industrialized countries, particularly in Europe, beset by high and rising unemployment, especially amongst the young and unskilled, and under severe pressure to cut fiscal deficits, slashed spending, even in such important areas of social domestic need as health, education and social security. As a result, many of these countries gave less priority to funding international cooperation, and ODA fell, particularly aid channelled through multilateral agencies. Such aid as was given was frequently 'tied aid'.

This cut in aid through multilateral channels was surprising; given the difficulties brought about by globalization—increasing inequality among and between countries and social income groups, poverty and its manifestations in social problems, immigration and

mass migration, environmental problems and severe dislocations caused by rapid reversals in capital flows—more, not less, enthusiasm for multilateral problem solving might have been expected.

Many major donors, convinced of the need for overall UN reform, sought out particular specialized agencies to build their case for, or start the process of, reform. UNCTAD and UNIDO were singled out. It will be recalled that the Commission for Global Governance had recommended the closure of both UNIDO and UNCTAD; other influential commentators urged, if not their closure, then their merger.

In their announcements of withdrawal or threatened withdrawal from UNIDO, the US and the UK Governments raised fundamental questions about the rationale for multilateral cooperation, particularly in promoting industrial development.

Specifically, some questioned the appropriateness of industry as a motor for development, especially in poorer countries. Others, while conceding the importance of industrial development, doubted whether it needed special support. The question was asked repeatedly: could not industrial development be more efficiently and effectively supported by markets and the private sector? Was a publicly funded body still needed to support industrial development in the new global economy, characterized by widespread liberalization, the primacy of market forces, and the lead role of the private sector in development? After all, did not capitalism triumph conclusively over the ill-fated command economic system when the Berlin Wall fell and the Cold War ceased?

These arguments, though popular, were fundamentally incorrect. None the less, important donors to UNIDO believed them, and they informed the criticism of the organization and conditioned the generally negative attitude towards it.

As we have seen, UNIDO was founded essentially on the initiative of developing countries. It was 'their organization'.<sup>87</sup> It was also seen as having an 'original aim to reinforce the efforts of developing countries in achieving industrial development based on a centrally planned economy, and the influence of the Communist countries within the Secretariat was considerable.'<sup>88</sup>

This lingering, but incorrect, view lay behind the Commission of Global Governance's recommendation to close down the organization. Their report seemed to be based on a dubious, and certainly outdated, misconception, and ignored UNIDO's potential as a development organization.

UNIDO was undoubtedly seen as 'the specialized agency with one of the worse reputations.'<sup>89</sup> But the 'slow and sometimes incorrect or nervous responses of the management continued to increase criticism and reduce [the] confidence of a number of member States.'<sup>90</sup>

Many in top management had been appointed on political grounds, with scant attention paid to the candidates' technical or professional competence. Most importantly, the organization had spread its limited resources too thinly and thereby reduced its

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<sup>87</sup>Danish Government's *Plan of Action for Active Multilateralism*, 1996.

<sup>88</sup>*Plan of Action for Active Multilateralism*, 1996, p. 44.

<sup>89</sup>*Plan of Action for Active Multilateralism*, 1996.

<sup>90</sup>Posta, 2000, p. 1.



impact. Despite major reform attempts from 1993, the organization's activities lacked focus and integration. There had been some geographical focusing on Africa, where most of the LDCs were, but it was felt that the organization still needed to cater for the needs of other developing countries and of countries in transition.<sup>91</sup> It was also felt that the geographical focus was vague and did not provide sufficient operational guidance for programming or for selecting among the many requests for UNIDO's services.

The organization's sectoral coverage had been narrowed to focus on 32 high-priority and 30 medium-priority sectors, eliminating coverage of 15 sectors. But this focusing had not taken the reductions in resources sufficiently into account or ensured that there was sufficient critical mass to provide effective coverage.

The thematic focusing of the organization was also felt not to give sufficiently clear guidelines on which activities should be pursued. 'Each of the seven themes identified are very broad in coverage; they overlap; they are conceptually different; some imply global coverage while others embody a geographical focus. Thus, in logical terms there is considerable scope for improvement. Decisions on thematic focusing have too much scope for interpretation.'<sup>92</sup>

## **The response**

The crisis of 1997 threatened the very survival of UNIDO. Urgent action was needed if the organization was to be saved and the confidence of member States restored. A special session of the organization's Industrial Development Board (IDB) was convened to find a way out of the difficulties.

It was obvious that, if UNIDO was to be saved, member States had to play a more active part, particularly through their Permanent Missions based in Vienna, Austria. Their involvement is an interesting phenomenon in itself. It was not based on any ambitious initiative or even on a conscious decision. The involvement of the Missions grew gradually until, 'one day, Missions discovered to their surprise that they had a lead role in the reform process'.<sup>93</sup>

Prominent roles were played by the EU, particularly the Netherlands which held its presidency, the United Kingdom, Denmark, Japan and India. The latter was critical in persuading the developing countries that UNIDO could not survive without the active involvement and cooperation of donor countries.

Denmark had always been an active and strong supporter of UNIDO, but did not hesitate to criticize the organization's performance and lack of focus when it felt that criticism was required. It had already commissioned a study in 1992, to determine UNIDO's advantages.<sup>94</sup> Before the IDB of December 1996 it announced it would carry

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<sup>91</sup>*Assessment of UNIDO*, 1997, p. vi.

<sup>92</sup>*Assessment of UNIDO*, 1997,

<sup>93</sup>Förster, *op. cit.*, p. 1.

<sup>94</sup>*A Future UNIDO. A Study of UNIDO's Comparative Advantages, Areas of Concentration, Organization, and Resources*, 1992.

out an in-depth assessment of the relevance of UNIDO for development. The Danish 'Assessment of UNIDO' is treated fully below; here, suffice it to say that the Danish study of UNIDO was very influential and played an important role in the development of UNIDO's Business Plan. It independently arrived at similar conclusions to an EU Missions' 'Assessment' of UNIDO and became available at a strategic moment in May 1997.

Unlike other countries, Denmark backed its constructive criticism with additional financial support to UNIDO when it was satisfied with the progress that had been made. Every year since 1998, it has given 15 million Danish krone (\$1.8 million) in voluntary contributions to the organization.

The Danish Assessment, none the less, contained serious criticisms of UNIDO's objectives and priorities—they did not provide adequate programmatic and operational guidance—and of its activities and structure, in particular that they lacked focus and integration. But it was the conclusion of the Assessment that was instrumental.

The Assessment's definitive conclusion was that UNIDO *was* relevant; its services were needed and were in high demand. It was an organization with a future, an organization to which at present no viable alternative was available. The Danish Assessment was very well received not only on account of its thorough, unbiased analysis but also because of its professionalism. The respect accorded to the study helped EU and other donor countries to lend their support to the Business Plan. It also prompted the Danish Government to make a generous voluntary contribution to UNIDO.<sup>95</sup>

Denmark played an important role in reconciling differences among EU partners concerning the EU's position on what percentage cut in UNIDO's budget was appropriate.

## Developing the Business Plan

In addition to the financial difficulties caused by the withdrawal of the United States, by the late or non-payment of assessed contributions and by the significantly reduced funding from UNDP for its projects, UNIDO faced the threat of severe budget cuts demanded by some prominent donor countries, notably Germany and Japan. Budget cuts as high as 40 per cent were discussed.

In response, the Director-General presented a contingency plan to cope with the threatened budgetary situation and to mobilize member States in support of the organization. He wanted to secure their public, political and financial commitment to the future of UNIDO. Unfortunately, their reaction to the Director-General's proposals was restrained. They felt that the proposals were 'too late and too little'. The major donors were not willing to give him *carte blanche*.

The special session of the IDB produced a 'Common Ground' paper. This contained a very general formulation of the desired future concentration of UNIDO's activities. It outlined the need to continue the reform of the organization and the key functions it

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<sup>95</sup>Förster, *op. cit.*

should exercise, and formulated the main programme priorities for its future activities. It urged measures to improve efficiency, and new managerial and organizational structures.

Despite the repeated appeals of developing countries, the major donor countries were not ready to announce an open political and financial commitment to ensure the organization's future. It was made clear to developing countries, informally, that the support of donor countries depended on reform of the UN as a system. Support was also conditional on UNIDO proposing concrete programmes that reflected the new global realities and the needs of developing countries.

Member States increasingly lacked confidence in UNIDO's senior management. They did not want the direction of UNIDO's future activities to be left entirely in the hands of the Secretariat. They proposed instead to establish an *Inter-Sessional Working Group*<sup>96</sup> of member States which could draw on the Secretariat as resource persons.

The debate that ensued during the Special Session of the IDB underscored the urgent need for a document that outlined clearly and definitively the future of UNIDO. Signals were coming thick and fast that decision makers in donor capitals expected as a precondition for future support of the organization an expeditious and meaningful formulation of UNIDO's future priorities and activities, a significant budget cut and a reconfigured management and organizational structure. Without such reassurances the number of withdrawals from the organization would increase, and UNIDO would be marginalized.

Fortunately, many developing countries realized how serious the situation was. They accepted, albeit somewhat reluctantly, that the organization could only be saved if it reduced and focused its activities, and that the 'usual confrontation' with donor countries seen so often in the past was not an option.

The representatives of Algeria, Egypt, India, and Tunisia played a particularly cooperative and constructive role in bringing developing countries to this conclusion.

Against this background, the Inter-Sessional Working Group, under the able chairmanship of Ambassador Posta of Hungary, met frequently to develop a paper on the 'Future Role and Functions of UNIDO', which became known as the 'Business Plan'. The Working Group had to work under enormous pressure. In less than two months they held five meetings of the Group, five meetings of 'Friends of the Chair' at ambassadorial level, several other meetings of experts, and many consultations with the Secretariat. At the same time, members of the Group frequently consulted their own regional groupings, such as the EU and G-77.

The working method of the Group was very simple. Once parts of the future Business Plan were identified, preliminary notes were sent to the 'Friends of the Chair'. These were followed by one to two drafting meetings at the expert level. The text was then discussed and agreed with the 'Friends of the Chair' at ambassadorial level. In between, various regional groups had their own meetings to discuss proposals or agree

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<sup>96</sup>This section is drawn from Posta, *op. cit.*, pp. 2-3. In addition to their formal deliberations during sessions of the policy-making organs, representatives of member States meet in Inter-Sessional Working Groups to examine specific matters as directed by the governing bodies. Since UNIDO became a specialized agency, its policy-making organs have established a number of working groups with mandates that cover a wide range of issues.

positions. The text was then circulated to all members of the Inter-Sessional Working Group and discussed at its informal meetings. Comments from the capitals of donor and recipient countries were also discussed at these meetings. The end result was that the work of the Inter-Sessional Working Group was presented, in the form of the Business Plan, to the Seventeenth Session of the IDB, and adopted with very few changes.

### **The Business Plan: objectives, structure and priorities**

The challenge for the drafters of the Business Plan<sup>97</sup> was to pin down clear comparative advantages for UNIDO, while avoiding overlap and duplication with other multilateral institutions and bilateral technical assistance.<sup>98</sup>

The drafters' objective was to develop:

- A clear description of UNIDO's future priorities and activities which would provide unambiguous guidance to the Secretariat for the elaboration of programme and budget proposals. The priorities could also help to restructure the organization.
- A set of guidelines and measures which would send a clear and convincing message to the capitals of member States that UNIDO was a very different organization from what it had been, reflecting new political and economic realities and development paradigms.

Another objective of the Business Plan, which is still to be achieved, was that it should guarantee political and financial support from member States, and thereby ensure the predictable and stable conditions essential for the future success of the organization.

The Business Plan had four major clusters:

- Activities to be carried out by UNIDO in the future.
- Activities to be discontinued.
- Guidance on the future programme and budget, particularly for the next biennium.
- A new organizational set-up for the organization, including field representation.

The Plan established a new framework to promote and integrate UNIDO's programmes and activities. It adopted a 'dual-track approach' to UNIDO's future activities, identifying which the organization should be engaged in, and which should be discontinued.

It clustered the organization's activities into two main areas: 'strengthening of industrial capacities' and 'cleaner and sustainable industrial development'. It proposed a

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<sup>97</sup>This section is based on Posta, *op. cit.* and Förster, *op. cit.*

<sup>98</sup>Ikeda, *op. cit.*

concentration in LDCs, especially in Africa, on agro-based industries, and support of small and medium-sized enterprises as the principal means of achieving equitable and sustainable industrial development. It emphasized that UNIDO should provide packages of services and support for the integration of women in industrial development. It also suggested a new, streamlined organizational structure that reflected the new areas of concentration.

Cooperation with other United Nations agencies, particularly in the field, was emphasized, to encourage a unified field presence and integrated activities. Decentralization to the field was necessary to make the organization more demand-oriented, bring its services closer to its clients, ensure effective programming of technical cooperation at the country level, and deliver technical cooperation services in a timely fashion with greater impact. Strengthening of UNIDO's field presence would mean substantive redeployment of qualified staff from Headquarters in Vienna. It also implied that the field presence would have greater administrative and financial autonomy, but that a critical number of staff would remain at Headquarters, the two groups interacting extensively.

The elaboration of the Business Plan was not without its problems.<sup>99</sup> One was the lack of any precedent: in no other UN organization had member States worked out their own schedule for reform. Valid legal questions could be raised: should the aim be a resolution, an amendment to the Constitution?

A second procedural problem was to decide in which forum the embryonic Business Plan was to be discussed. Clearly, in view of the keen interest shown by so many parties, all member States should have the opportunity to express their views. After intensive consultations with the regional groups and others the Inter-Sessional Working Group was established. A special Industrial Development Board was to be held in June to approve the Business Plan.

At this juncture, UNIDO's management presented a reform project of their own, more in line with UNIDO's earlier reforms. However, a clear majority of member States believed that the momentum created during the preceding months should not be lost. They felt that the draft Business Plan recognized the wishes of developing countries while taking account of the spending limits some of the developed member States had imposed upon themselves, and decided to conduct discussions on the basis of the draft alone.

The discussions were far from easy. There were three fundamental problems.

One was *the scope and focus of activities*. All member States agreed that the old-style UNIDO had catered too much to the often diverging wishes of too many member States. Choices had to be made, and activities limited to those fields in which UNIDO disposed of real added value in comparison with its 'competitor' international organizations. Elaborate discussions took place before a clustering of activities in two main

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<sup>99</sup>Förster, op. cit., pp. 2-3; Posta, op. cit., p. 4. For details see UNIDO, *Business Plan on the Future Role and Functions of UNIDO*, IDB.17/Dec.2. The Business Plan was formally adopted by UNIDO's Industrial Development Board on 27 June 1997 and by General Conference on 4 December 1997 through Resolution GC.7/Res.1.

areas was decided: 'strengthening of industrial capacities' and 'cleaner and sustainable industrial development'. Probably the most controversial subject was whether 'energy' should be included. Finally it was decided to exclude it. Some member States greatly regretted this, but the prevailing view was that other, better-qualified, organizations and institutions were dealing with the subject. It was also felt that it was difficult to reconcile the question of energy with the large-scale investments of countries like Japan (an active participant in the reform process), which sought to reposition UNIDO further 'upstream'.

UNIDO had to focus its activities without losing its universal character in industrial development. While it was obvious that smaller, more focused activities would mean the discontinuation of some activities, many member States were worried that the organization might lose its critical mass of knowledge if activities were too narrowly defined. Identifying activities to be discontinued was difficult and painful, and was only done after long and painstaking debate.

Since each member State inevitably had different interests in particular programmes, it was agreed that ongoing programmes should not be affected. The geographical, sectoral and thematic concentration of UNIDO's activities was formulated so as to leave room for a wider interpretation of UNIDO's future activities.

A second problem was *the future structure of the organization*. Member States had to tread carefully here as personnel management was within the competence of the Director-General. The new organizational structure attracted less debate. Member States opted for a structure consisting of two divisions, then called 'investment promotion and institutional capacity building' and 'sectoral support and environmental sustainability'. It soon became clear to member States that the unavoidable consequence of this structural reform, combined with the announced budgetary restrictions, would be some personnel lay-offs. In the intersessional meetings, and even more so in smaller groups, this unfortunate development was much discussed and alternatives were sought, but none was found.

A third problem, closely related to the second, was *the budget*. From the outset it was obvious that it would not be possible to maintain the budget at its current level: if the most important donor in the EU, Germany, was to be kept on board, and another important European donor, the UK, which had already announced its withdrawal, to be lured back, a budget cut was unavoidable.

The size of the cut was the subject of much discussion. Germany wanted a 40 per cent reduction, which many believed would mean the end of UNIDO. Japan followed Germany closely in asking for a 30 per cent cut. In the end, it was decided that the Director-General would be invited, in a special June Board, to present three budget scenarios based on 10 per cent, 20 per cent and 30 per cent cuts. After long and exhausting negotiations, within the EU and between the EU and its partners, the General Conference of December 1997 accepted a budget reduction of just over 20 per cent—a considerable cut indeed, but the only way out of a discussion which many felt was putting the cart before the horse.<sup>100</sup>

<sup>100</sup>Förster, *op. cit.*

## Lessons of the Business Plan

The Business Plan was the product of an intensive process of cooperative, common thinking. Most commentators agreed that it was a success for UNIDO. It achieved a difficult political compromise and an agreed framework and set of priorities for re-launching the organization. It was a kind of common denominator on the future role and functions of UNIDO among donor and recipient countries.

The lessons UNIDO learned from the development of the Business Plan may be of value to others undertaking or supporting similar reforms.

First and foremost, the Business Plan was only successful because it was *conceived in a cooperative, consensual process involving the key donor and recipient countries*. It was a kind of common denominator of the future role and functions of UNIDO. It would not have succeeded without the political will of all parties to come to a common position and to do so quickly. This is not to say that debate was not difficult on certain issues, particularly on what activities UNIDO should discontinue. Some countries lost their hobby-horses, and are still aggrieved. But, ultimately, the priorities and future direction of the organization were agreed by all.

The ownership felt by all member States, the cooperative spirit in which negotiations took place, and the responsibility assumed by all parties to reach a solution by consensus together ensured the success of the Business Plan.

The Business Plan defined for the first time a focus and a set of priorities for the organization. Without clarity of focus and integration of activities, a reform programme is unlikely to be effective. The emphasis on teamwork gave a much-needed new dimension to UNIDO.

*Leadership* was important in the success of the Business Plan. The Inter-Sessional Working Group, the able leadership of its chairman, the initiative and the stewardship of difficult negotiations undertaken by the Permanent Mission of the Netherlands, which held the presidency of the EU, and the chairs of the various regional groupings and the G-77 group of developing countries and China, were major contributors to the successful development of the Business Plan. An important lesson is that member States must go beyond mistrust and misunderstanding among themselves on the one hand, and of the secretariat of a UN Agency on the other.<sup>101</sup>

Without the will to get things started and the leadership to ensure the participation of all the major developed and developing countries and countries in transition, as well as of their respective regional groupings—or at least to ensure consultations between these parties—a difficult consensual solution like the Business Plan would not have been possible.

The Business Plan was drawn up by the member States themselves, but key members of the Secretariat were important as resource persons when needed. The confidence placed in these individuals by member States was instrumental in the achievement of a successful conclusion of its development process.

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<sup>101</sup>Tiwari, *op. cit.*

The vision, receptiveness and energy of UNIDO's new Director-General and his management team and the resulting restored confidence of member States, was critically important for the successful implementation of the Business Plan.

Even in the best of times, a UN agency undertaking drastic reforms cannot deliver its objectives unless it has *adequate resources*. The onus is on member States who call for the reform of UN agencies to realize that they must follow through with financial and other resources to ensure success.

A Business Plan should not be seen as set in stone. It is a new focus and set of priorities for particular circumstances and a particular time. It must be re-assessed when these circumstances change or are superseded by other events or priorities. A Business Plan, if it is to stay relevant, cannot be considered unchangeable.

This said, any change in the scope of activities envisaged in a Business Plan must satisfy two conditions:

- The new management must have demonstrated visible success in the implementation of a current Business Plan. Such a demonstration strengthens the confidence of donor countries and of member States at large that changing the Business Plan would add to success.
- New priorities must respond to changed political or economic circumstances in recipient countries, and have the support of major donor countries.

Both these conditions imply that changes to a Business Plan in the short term may be counterproductive. However, re-assessment of a Business Plan in the medium to long term may be not only advisable but essential to ensure its continued usefulness in guiding effective developmental support.

## **The importance of the Danish Assessment**

We cannot conclude this chapter without a final word on the importance of the Danish Assessment. The frequent references to it are a testament to its importance in UNIDO's transformation process.

We have already seen that the Danish Assessment's positive conclusions about UNIDO in May 1997 were critical in persuading major donors, such as the EU, and other member States, of UNIDO's relevance and viability. It also gave initial, but important, momentum to the development of the Business Plan. However, the Danish Assessment is not only important for its association with the Business Plan. The conclusions reached in the Danish Assessment also had a positive influence on the German and Japanese attitudes towards UNIDO and on the UK's decision to remain in the organization.

When the Danish team initiated their research they had been inundated with negative news about UNIDO. Indeed, in the preface to their report they admitted that they did not expect to reach positive conclusions. The team leader, Professor John D.-Martinussen, wrote:



Our general impressions of the effectiveness and efficiency at headquarters level in Vienna, when we started the Assessment exercise, were not particularly positive. Basically, we shared the views of several donor member States that the UNIDO Secretariat's performance was unacceptably poor.<sup>102</sup> However, after an extensive examination of the organization he was led to the conclusion that '... at least some of the criticism levelled against the Secretariat by Member States must be based on either selective perception or knowledge about the Organization which has not been successfully updated or both.'<sup>103</sup>

The Danish Assessment powerfully demonstrated that only a careful examination of facts and analyses would lead to proper conclusions about UNIDO's progress in reform. Its conclusion was that 'it is difficult to find justification for abolishing UNIDO on the grounds that its services are not needed'.

The Assessment also argued that it would be probably not be cost-effective to merge UNIDO with other organizations, unless 'a priori [this] would result in increased effectiveness, efficiency and responsiveness to client countries' needs'. And the organization was undoubtedly needed, since industrial development remains a precondition for sustainable economic growth and social advancement. Although UNIDO did not have the capability to meet all industrial development needs,

[n]o other international organization has the same comprehensive experience, technical knowledge and multi-disciplinary expertise for continuing and linking industrial technical cooperation services targeted at both the policy and strategy level, the institutional framework level and the enterprise level.

The Assessment recommended the continuation of UNIDO as a specialized agency, but suggested further cuts in administration and support costs, and better focusing and integrating of activities, and that special attention be paid to UNIDO's normative functions and global forum role.

Important as these conclusions of the Danish Assessment undoubtedly are, arguably what was most important for UNIDO's current transformation process were its findings that UNIDO has a comparative advantage in providing 'integrated packages of services', and that it must emphasize cross-organizational coordination and teamwork.

As we shall see when reviewing UNIDO's transformation, these observations have been the driving force behind the reorientation of the organization and the development of its new service modules and integrated programmes based on organization-wide teamwork.

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<sup>102</sup> *Assessment of UNIDO*, 1997, p. ii.

<sup>103</sup> *Assessment of UNIDO*, 1997.

## Annex

### The Business Plan as key players saw it

The following are extracts of personal reflections from five ambassadors who were intimately involved in the development of the Business Plan: Istvan Posta of Hungary, Hans Förster of the Netherlands, John Freeman of the United Kingdom, Yuji Ikeda of Japan and Yogesh Tiwari of India.<sup>104</sup>

#### ISTVAN POSTA

As I recall, the initiators of the proposal did not have a clear vision about how to carry out this work but their intention was to secure the continuous control of the member States between the two sessions of the IDB over the steps to define the organizational structure, aiming at furthering the Common Ground Paper. In decision IDB/S.7/Dec.3., I was requested to establish and chair an Inter-sessional Working Group to further advance the process of definition of the future role and functions of UNIDO. The adopted mandate was clear but flexible: the Board decided 'to establish an Inter-sessional Working Group with equitable geographical representation', 'invited member States to continue to contribute to the formulation of basic parameters to guide the work in adapting the organization to new economic realities', and finally requested the Chairman 'to establish a timetable for negotiations and to submit a progress report to the Board not later than its seventeenth session'.

On the very first informal gathering of the diplomats in charge of UNIDO's activity, we agreed not to continue working on the Common Ground Paper which would involve us in a political or linguistic type of drafting exercise. Rather, we agreed to elaborate a paper giving very practical answers to define the mutually acceptable future role and functions of UNIDO. As an aside let me mention—if I am not misled by my memory—that our Dutch colleague Neline Koornneef proposed the name 'Business Plan' as a temporary title of the document to be elaborated. We all understood what kind of paper it might be, although we thought we would later find a better title. Then during our meetings we concentrated more on substantial issues and finally we got used to this title. At the end of the exercise nobody proposed to change it. The other important agreement was to try to draft one single document with the participation of a limited, but geographically balanced group of countries. Though it might seem very obvious today, I should mention that earlier the usual way of elaboration of any document in UNIDO was to have a draft from the G-77 and a draft from the donor countries, followed by the merging of the two documents through various political compromises. Using the prevailing recognition of the urgency of the situation and the strong determination to find a solution in a short time frame, I encouraged a common drafting procedure, with the participation of all parties concerned. I do believe that our agreement on these two basic starting points played an essential role in the success of this exercise.

A very difficult period in the life of UNIDO was over with the adoption of the Business Plan. The Business Plan was a response to a concrete crisis situation when the very existence of the organization was at stake. The response was successful; the member States could elaborate a

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<sup>104</sup>Istvan Posta, *Reflections on the importance and role of the consensual solution of the Business Plan to the successful transformation of UNIDO*, 2000; Hans A. Förster, *Personal thoughts on UNIDO's reform process as a contribution to UNIDO's study on its reform*, 2000; John Freeman, *A UK perception of UNIDO's Situation*; Yuji Ikeda, *In Search of Comparative Advantage*, 2000; Yogesh Tiwari, *Solving a Crisis through Consensus and Partnerships*, 2000. All five Ambassadors have written in their personal capacities. The views expressed in this chapter do not necessarily represent the policies of their Governments.

programme acceptable as a minimum compromise for the developing countries as well as for the donor community to continue the activity of UNIDO through providing services in accordance with the changed economic and political environment. I consider the Business Plan as a political response to the challenges posed by a given political economic situation. It is a compromise the developing countries were ready to accept and the major donor countries were willing to go along with. Obviously, as any compromise, the Business Plan also contains questionable formulations, it is not free from internal contradictions and certainly some of its concrete proposals were not proven by the practice. However, it was not the intention of the authors to elaborate a perfect document but to provide the possibility for UNIDO to continue its activity for the benefit of the member States. And in that sense the Business Plan was a successful and useful tool.

Two and a half years later in December 1999, I was invited to attend the General Conference of UNIDO where the Director-General reported on the results and experiences of the implementation of the Business Plan. I could see that while the new management put UNIDO on a new track outlined in the Business Plan, the organization was not free from difficulties either. However, the problems raised are of different nature and in no way connected with the question of survival of the organization. The elaboration and adoption of the Business Plan contributed to this qualitatively new situation.

#### HANS FÖRSTER

Having gone through a considerable amount of reform efforts and reorganizations in the preceding years, UNIDO faced the worst crisis of its existence in late 1996. At the December session of the Industrial Development Board (IDB), the United Kingdom announced its intention to withdraw from the organization and Germany indicated that, unless very drastic budgetary cuts would be effectuated, it would take Britain's (and Australia's and the US's) example and follow suit. Both countries left their European Union partners feeling uncomfortable, as little previous consultation had taken place. Matters such as adherence to international organizations are—and were already then—considered to be subjects on which EU member States should preferably speak with one voice.

It was with no other ambition than to harmonize apparently diverging views within the European Union that the incoming EU presidency, the Netherlands, took the initiative of organizing a number of meetings as from January 1997. It soon became clear, however, that these divergences were based on very different appreciations of the work UNIDO had delivered so far. Thus it was decided, after consultation of the EU working group on UN matters, the 'Conun', to try and draft a common 'preliminary assessment' of UNIDO's relevance for past and future development efforts.

EU Permanent Missions rapidly discovered that such an assessment was no easy task and additional expertise was needed. So it was decided to hear the Director General, then Mr. Mauricio Maria y Campos, his staff members, representatives of the Staff Council, and, particularly, other Permanent Representatives. Thirty to forty interviews later—it is difficult to select just a small number of representatives, the Presidency decided to rather hear as many as possible—we thought we had a fairly clear idea of what the organization meant to the countries directly concerned, what its shortcomings were, what its future could be. Although some EU partners remained more critical than others, all of them helped without reservation in the drafting of the 'assessment' asked by Conun, and the Presidency was indeed able to produce a common paper within the—incidentally, very short—deadline set by the working group. The Assessment opened the way for further support to UNIDO, provided the organization would be able to transform itself.

It took some time to convince UNIDO member States of the necessity of reform considered by the EU to be a condition for continued support. Several Missions voiced concern that this was yet another example of 'donor fatigue' and served no other purpose than the reduction of developed countries' contributions. Fortunately, in the process leading to the conclusion of the 'assessment', Missions had been able to create a climate of mutual trust, overcoming traditional and political cleavages. Ambassadors of important countries, such as Brazil, India, Pakistan, Sudan, Tunisia and many others, helped persuade their colleagues that a revitalization of UNIDO would be in the interest of all, not in the last place of developing countries themselves.

Now, more than two years later, the organization has changed beyond recognition. Having borne for so many years the stigma of a 'difficult' organization within the UN family, it has now become one of its most dynamic and rejuvenated members. Shock therapy seems to have worked. All the same, some problems remain, the most important of which is finances. Its budget shrunk, UNIDO depends more than ever on voluntary contributions which are still slow to come. Developed countries should realize that their commitment to reform must be matched by adequate funding without which the life span of UNIDO will just have been prolonged for a mere couple of years. After all the efforts invested in the revitalization of the organization this would represent a true catastrophe: much of the confidence so painstakingly created would be lost. Moreover, the failure of this example of autonomous reform of a UN specialized organization would no doubt have its repercussions on the reform process of the UN as a whole. UNIDO faces a vicious circle: it needs financial resources to create success stories, but it needs success stories to mobilize financial resources. Donor countries should show more audacity and more confidence in the organization, and give it the chance it deserves.

Looking back at the process as it took place in 1997 and 1998, two factors seem to have been of crucial importance.

First, the role of the European Union. Although the Union was divided internally, with Denmark on one side, and Germany on the other side of the spectrum, the others being somewhere in between, it has on the whole been able to speak with one voice, all through the crucial years 1997 and 1998. Perhaps that voice did not always carry a totally transparent message for everyone. But the fact that the subsequent Presidencies (Netherlands, Luxembourg, UK and Austria) were always able to speak for 15 member States made it one of the key players during this exercise. Without it, no 'rescue operation' of UNIDO would have succeeded. Without the Union, both Germany and the UK would almost certainly, and many others most likely, have left the organization, thus almost certainly condemning it to irrelevance, or even death.

Second, the unprecedented efforts of all Permanent Missions in Vienna. No doubt it was rare and fortunate coincidence that at this critical juncture in UNIDO's existence so many constructive, patient and dedicated Representatives served in Vienna. They showed that true reform of an international organization need not always come from its management or from New York: it can just as well be 'bottom up' once traditional dividing lines are crossed. In this sense the UNIDO experience is no doubt an interesting case in point for many other international organizations, and in particular those which are in difficulty themselves.

JOHN FREEMAN

UN reform matters. If the multilateral system is to respond to the challenges of the new century, it needs to continue to modernize. And for modernization to succeed, member States need to work in new ways, focused on specific outcomes best achieved through the multilateral system. The modernization of UNIDO is an example of what can be achieved by member States working together.

In 1996/97 UNIDO had to face up to an uncertain future. If the organization had failed to reform itself, it is doubtful if it could have survived as a separate UN body. The process by which it was reformed is also instructive, not least the ways in which member States in Vienna have worked together with the Secretariat to determine UNIDO's future.

The UNIDO Business Plan grew out of an extended process of consensus building. It was a time-consuming and demanding process based on the realization that UNIDO could not survive without change. But there was a more positive aspect also: there was a chance together to focus UNIDO on the objectives and specific geographies of the greatest importance to donors and recipients alike. Sterile debates, reiterating regional group positions, were largely avoided. There was a focus and a seriousness to the discussions among member States.

Exchanges often cut across customary groupings and positions. There was a common effort to produce practical outcomes and to define the areas in which UNIDO could make a distinctive contribution, reflecting its comparative advantages as a multilateral organization, to sustainable industrial development.

The process of change in UNIDO did not come to an end, however, once the Business Plan had been approved and an associated 20 per cent budget cut achieved. Member States have a continuing role to ensure that the organization adheres to the Business Plan prescription in both programmatic and managerial terms, including appropriate decentralization to the field.

UNIDO is a small organization that needs to be aware of its limitations and cut its cloth accordingly. It cannot do everything; it cannot operate everywhere. In the next stage of its evolution UNIDO needs to clarify further its new integrated programmes, limit their number (because if there are too many the Secretariat will not be able to implement them) and ensure they work effectively. That is the real test of reform: is UNIDO contributing to the international development targets, is it making a difference? If it is, the process of change on which member States have been engaged with the Secretariat will have been worthwhile and may have lessons for other parts of the multilateral family. For reform needs champions and UNIDO can be one such.

The result of these discussions in the form of the Business Plan is well known. But there is an ongoing lesson also: member States are capable of working together on key common objectives which cut across divisions between the North and the South in ways that are beneficial to developing countries.

YUJI IKEDA

In January 1997, a bilateral meeting between the EU and Japan was held at the Netherlands Mission where an exchange of views on the reform of UNIDO took place and where I presented the Japanese view of the Business Plan. In retrospect, the meeting turned out to be pivotal as almost all the key elements of the Business Plan emerged from the participating donor country ambassadors. The ensuing consultation that the EU and Japan conducted respectively with developing countries, such as the African group in the case of Japan, was characterized by constructive spirit. This same spirit was maintained throughout the period leading to the final substantive agreement on the Business Plan at the IDB in June of that year. This amicable and productive spirit among the players, created throughout the UNIDO process, seemed to have an infectious effect at the meetings of other organs in Vienna, such as IAEA.

Given this situation, the donor and recipient countries working together did, in my view, produce a reasonable and respectable set of working programmes, something more than a *modus vivendi*. At the same time, however, we should not be too complacent about what we have produced. For the continued success of UNIDO, it will be crucial for the Secretariat and member States to implement the Business Plan in a flexible manner so that UNIDO be attuned to the needs of the time.

Additionally, I would like to emphasize the importance of the political will of member States, both donors and recipients, to make the Business Plan meaningful by working together with the Secretariat. We look forward to witnessing UNIDO's success stories, which in turn will broaden the basis of support for UNIDO from the Governments and business circles of member States.

#### YOGESH TIWARI

My basic conviction was to save UNIDO even though I was not clear on how it could be done. As I got involved, I realized that for UNIDO to survive it was imperative that confidence be re-established between the donor countries and the recipient countries. At the same time, UNIDO would have to be restructured and would have to operate with funding at a lower level than previously. I therefore interacted with all major donor countries and gradually convinced the most sceptical among them to look from the perspective of the acutely necessary industrial development of the developing countries. Without the cooperation of the major donors it was not possible. At the same time, the alternative of clear-cut polarization and conflict with the developing countries was not in their own interest, as indeed evidenced by the fact that most donor countries were actually giving aid bilaterally. Therefore, any attempt by the major donors to weaken international cooperation would be understood by developing countries as something against their own interest. Two colleagues who played a role in acceptance of this thinking were the Permanent Representatives of Holland and of Denmark, and later also the Permanent Representative of the United Kingdom. They also helped to persuade major donors like Germany and Japan to take a more moderate approach.

We all agreed that reforming and restructuring UNIDO was necessary to respond to the changing global environment dominated by globalization, privatization and the need for competitiveness. With the developing countries, my first task was to persuade them to accept that UNIDO could not survive without the donor countries' active and willing cooperation. Secondly, there were many developing countries which had benefited from the services of UNIDO, some of which were not paying their contributions and therefore were not in any moral position to demand earlier levels of contributions from developed countries and the maintenance of the status quo. Over the next months these trends converged and with the exception of a few countries in either camp, the majority of countries were willing and ready to have a consensus solution through a cooperative approach.

I think the lesson of UNIDO's case for other UN organizations is to realize that bureaucratic structures can be made leaner and at the same time can become more efficient. All this can be achieved in a relatively short period of time if all partners, developing and developed countries, work in concert along with a strong leadership within the secretariat.

## Chapter 6

# The transformation of UNIDO

Before the development of the Business Plan in 1997, UNIDO was in dire straits. The Business Plan was critical in establishing new priorities and the future direction of the organization. It also re-established the legitimacy of and political support for the organization, particularly from major donor countries. But it only laid the foundation for UNIDO's renaissance. Much work was still needed to implement it, refine priorities, streamline the organizational structure, improve management and simplify procedures, refocus and integrate UNIDO's services, and inculcate a new ethos of teamwork to be more responsive to the needs of UNIDO's clients. In short, UNIDO had still to be transformed. There were those who still had to be convinced that UNIDO 'made a difference.'

The Business Plan reflected a difficult political compromise. It grew out of a period of intense debate, consultation and consensus building. It was premised on the stark realization that without such a consensus UNIDO could not survive. It therefore represented the sustained efforts of member States of UNIDO, recipient and donor countries alike, to identify appropriate priorities and organizational structures, as well as to find the direction the organization should take.

The Business Plan had to send a clear message to UNIDO's member States. The message was a simple one: the new UNIDO would be a revitalized organization worthy of their support, a very different UNIDO from before. It would reflect the political and economic realities that had changed the nature of development cooperation.

But, as member States recognized when the Business Plan was adopted, it provided only general guidance. Further refinement and clearer prioritization, with supporting organizational and programmatic focus, were required. The first task of Carlos A. Magariños, the new Director-General, when he took office in December 1997 was to put the Business Plan into action.

Following the guidance given in the Secretary-General's reform proposals for improving UN system-wide coherence and effectiveness and building on the Business Plan, the Director-General set out five principles for UNIDO's transformation.<sup>105</sup>

- *A clear sense of where industrial development needs to go in the 21st century and UNIDO's role in this process.* This requires that UNIDO's future direction

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<sup>105</sup>The Secretary-General, 'Renewing the United Nations', A/51/950, 1997.

is defined not by what it did in the past, but by the needs of developing countries and countries with economies in transition which will matter in the future. It would require a more precise definition of UNIDO's services, transformed through continuous review, improvement and innovation, and with a premium on staff creativity and empowerment, and on transparency.

- *A systemic approach, not a piecemeal one.* Wholesale rather than incremental change would ensure systemic transformation, not piecemeal reform.
- *A new culture of teamwork.* The new way of working should emphasize multi-disciplinary and multinational, cross-organizational teams. This new working culture should be based on an increase in cross-organizational cooperation, simplified procedures, decentralization and delegation of authority.
- *Elimination of internal and external overlaps and duplication of activities.* This would foremost imply a streamlined and decentralized organizational structure. Given the resource crisis and the need to re-establish relevance, UNIDO would need to be more productive and only undertake activities in areas in which it has a comparative advantage. UNIDO should therefore strive to become a centre of excellence in only a few selected areas, and withdraw from other areas. It should seek alliances with other development partners to maximize synergies, and hence developmental impact—UN agencies and other multilateral, international and bilateral agencies. It should cooperate more with the private sector and with civil society—particularly NGOs, industry associations, and research institutions and universities. In short, UNIDO should identify what it does best, what it should not do at all, and what it can only do with others.
- *Adoption of the Business Plan as the anchor and beacon to guide all actions.* The Business Plan should be the basis of UNIDO's structure and focus. First and foremost, attention should be given to the challenges of industrialization facing Africa and LDCs, but without prejudice to UNIDO's universal mandate.

UNIDO's basic mission is to help countries pursue sustainable industrial development. This is its specialist role in the UN system. But sustainable development is never achieved easily. It means balancing concerns for:

- *Competitive economy:* making industry efficient.
- *Productive employment:* promoting employment in industry.
- *Sound environment:* environmentally friendly industry.

These '3 Es'—economy, employment and environment—were essential in the vision of the organization. They became the overarching development goals that focused and guided UNIDO's activities, especially in the light of international concerns about the social and environmental consequences of industrialization. A competitive industrial economy is the long-term driving force of economic and social development. Productive employment is a vital means of generating income and accomplishing social goals such as



the reduction of income inequality and poverty. A sound environment is required to ensure an adequate supply of renewable and non-renewable resources and to safeguard human health and the quality of life.

Focus on the 3 *Es* aligned the organization with its long-term goal of sustainable industrial development and achieved a closer identity with system-wide objectives.

UNIDO's transformation process had two conceptually distinct phases:

- Phase I: financial, personnel, administrative and structural changes.
- Phase II: programmatic changes.

In practice the two phases were not entirely distinct; some complementary changes belonging to different phases were made simultaneously to ensure the success of transformation.<sup>106</sup>

## **Phase I**

### *FINANCIAL, PERSONNEL, ADMINISTRATIVE AND STRUCTURAL CHANGES*

At the very beginning of the transformation process, a number of emergency measures were needed. The organization faced severe difficulties:

- The new demands and priorities for UNIDO's future work given in the Business Plan and the limited resources given to programmes in its budget (Programme and Budgets, 1998–1999).
- Financial constraints resulting from the approved Programme and Budgets, 1998–1999, and a precarious cash-flow projection for 1998.
- More staff than were budgeted for.
- An organizational structure that did not correspond to the Business Plan and therefore had to be adjusted.
- Fragmentation of UNIDO's activities into a large number of small projects without sufficient integration or focus.
- Uncertainty resulting in low morale amongst staff.
- Arrears and late payment of assessed contributions by member States.

Priorities had to be set immediately to address a number of interrelated problems. It was decided to concentrate first on UNIDO's immediate financial, managerial and personnel issues.

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<sup>106</sup> To support implementation of the programmatic transformation, UNIDO designed specific training workshops and seminars, as well as a new management framework and service management cycle, a new staff career development system, and other support mechanisms mentioned in later sections. In addition, a number of country missions to selected donor and recipient countries were arranged to test markets and implement the new services; see UNIDO, *Annual Report 1998*, pp. 14–18.

New purchases, procurement and consultancy contracts, except those related to technical cooperation, were banned. For a 60-day period official travel was severely restricted. Through these temporary measures, which were not sustainable in the long run and caused some initial discontent and dislocation, the organization saved some half-million US dollars.

Next, a staff reduction programme was implemented.

At the end of 1997, UNIDO had 760 professional staff. By the end of 1999, there were 630, a net reduction of 130. Of those who left, 92 went voluntarily under 'agreed separations'. Other staff who found themselves in posts that were abolished were placed in existing or new vacancies.

This approach meant that UNIDO did not need to dismiss staff and thereby incur high financial costs and adversely affect staff morale. Staff concerns were alleviated and staff-management relations improved. Compared to an initial cost estimate of \$15.9 million, the staff reduction programme cost less than \$10 million, saving the organization nearly \$6 million.

As no provision for redundancies had been made by member States in the organization's Programme and Budgets for 1998–1999, the reduction had to be carried out within the prevailing financial constraints. The separation programme was therefore budget-driven and resulted in the retention of a number of staff whose skills were not fully in line with UNIDO's new programmatic focus. Some were retrained; others were subsequently separated from the organization.

### *CHANGES IN MANAGEMENT STRUCTURE AND STYLE WITHIN THE SECRETARIAT*

Weakness in managerial structure and style impeded UNIDO's effectiveness for a long time. An early task of the transformation process, therefore, was to install a new management structure and style within the Secretariat.

To this end, the following changes were made immediately:

- In line with the Business Plan three divisions were created in UNIDO—and within these divisions branches specifically dealing with environmental issues—and the Office of the Director-General was significantly reduced.
- An effective management team was established by the appointment of all staff required at managing director (heading a division) and director (heading a branch of a division) level.
- All staff were assigned to new organizational units, with only a few units left dealing with programme support services.
- Terms of reference for new organizational units emphasized clear lines of responsibility and accountability and well-defined performance targets.
- The Office of Internal Oversight was established.

The number of committees and administrative 'bulletins' and 'instructions' was rationalized to increase administrative and operational clarity. In 1998, for example, the number of bulletins and instructions was cut from 250 to just five and the number of committees from 110 to five. This led to a much simpler, quicker and smoother administrative system. It also brought about greatly simplified operational procedures for the organization, resulting in a marked increase in efficiency.

The consolidation of the Director-General's Office and the establishment of the Office of Internal Oversight ensured greater focus, coordination and oversight in the management of the organization and its relations with member States and other development actors.

### *TRANSPARENCY MEASURES*

An important part of the organization's new management philosophy was to ensure transparency and openness. To this end, a number of measures were enacted:

- *A policy of public access to documents.* In an unprecedented move, all major internal documents and correspondence were placed in a designated room to which staff and representatives of member States had full access.
- *Management by personal contact.* The Director-General visited staff for informal discussions. He explained his policies to staff on an individual basis and obtained their views and advice. Staff greatly appreciated these informal visits by the Director-General.
- *Direct communication with the Director-General by electronic mail.* This communication, actively encouraged by the Director-General, improved corporate spirit. It also changed the hierarchical culture of the organization, which had imposed a strictly vertical line of command in the exchange of information. In particular, the Director-General was able to hear directly from staff of the difficulties and progress of the transformation process.
- *Open office.* An 'open access' or 'open office' policy, in which staff could freely discuss matters of concern with the Director-General, was instituted. This initiative has enhanced mutual trust and understanding and appreciation by staff of the transformation process.
- *Early disclosure of policies to member States.* Without waiting for formal requests for information, the Director-General proactively disclosed important policy initiatives, such as the new staff career development policy described below, to member States in order to facilitate understanding and feedback and to give a better basis for decision making. The active use of informal meetings before formal sessions of the policy-making organs, such as the Industrial Development Board and Programme and Budget Committee of UNIDO, has also facilitated communication between the secretariat and governing bodies, and thereby reduced the time required for these sessions and hence costs.

- *Workshops and meetings with staff.* These were important in keeping staff informed and exchanging views about the future direction of the organization and its services. This approach increased staff's understanding and ownership of the transformation process.

### CHANGES IN UNIDO'S DECISION-MAKING SYSTEM

To improve the cohesiveness and effectiveness of UNIDO's decision-making system, a *new Executive Board and Board of Directors* were created.

The Executive Board is the organization's highest-level managerial mechanism. It consists of the Director-General as chair, the three Managing Directors responsible for the divisions of UNIDO, and the Director of the Executive Office of the Director-General. It is the authority for policy direction and for final approval of all UNIDO programmes and projects. It has a special role of ensuring the proper functioning of the organization's service management cycle and the implementation of its new integrated services.<sup>107</sup>

The Board of Directors provides the organization with guidance at branch level. It consists of all the managers of the organization, that is, in addition to the Executive Board members, all branch and Regional Bureaux directors.<sup>108</sup>

Together, these two bodies provide essential support and advice to the Director-General to ensure the smoother running, appropriate direction, management and monitoring of the organization's activities.

A *new financial authorization system* was introduced, based on simplification of procedures, delegation of authority to middle-management levels as required by the Business Plan, empowerment of staff and strong accountability mechanisms. In particular, it made steps towards the delegation of authority for transactions authorized in UNIDO's budget.

UNIDO created a new management framework, with a regional dimension, represented by the *Regional Bureaux*, and a functional dimension, represented by the *technical branches*. Representatives from both work in teams to develop and monitor the programme of services UNIDO offers at the regional and country level.

A further innovation was *retreats for senior managers* to discuss key technical and policy issues and workshops of professional staff, to redesign UNIDO's services and advise on the reorientation of the organization; these have been very useful.

<sup>107</sup>UNIDO's integrated services are discussed in detail below. UNIDO's new management cycle is designed as a further stage in the implementation of the Business Plan and the programmatic transformation. It translates the new management framework into operating procedures. It aims to ensure that services are delivered so as to have the greatest impact and thereby make the most effective contribution to sustainable industrial development. See UNIDO, *Annual Report 1998*, pp. 15–16.

<sup>108</sup>Regional Bureaux are branches of the organization which focus on technical cooperation programmes for specific regions (Africa, Asia, Latin America and the Caribbean, Arab, and Europe and the Newly Independent States (NIS)). They act as the marketing arm of UNIDO and as the focal point in processing demands for UNIDO's services and designing and coordinating responses.

Retreats have been used to achieve clarity on UNIDO's basic mission, to develop a new corporate image and strategy, and to establish budget priorities. They helped to answer the basic question: what does UNIDO stand for? Most importantly, they have enabled frank dialogue between the Director-General and his senior managers in an open and relaxed atmosphere. They have discussed and developed consensual solutions for: problems with the transformation process—substantive, administrative and personnel issues; the principal trends and challenges in industrial development and how UNIDO can address these challenges; the reorientation of UNIDO's services to achieve a clear and distinct identity with services tailored to the development needs of specific regions and individual client countries—in short, the key issues requiring policy decisions and direction to ensure the success of the transformation process.

The retreats were not just one-off events where senior management went away for relaxed discussions in pleasant surroundings; they were steps towards dialogue about where the organization was going or should be going. On the basis of these frank discussions adjustments were made to help keep the transformation process on track.

They were also important for self-discovery, consensus building, and bonding for the organization, its management in particular. They threw the difficulties in the transformation process into relief, but also showed that many of the deficiencies in the organization could be rectified by the organization itself, and that the real challenge was to manage these difficulties in a spirit of shared purpose and collective responsibility.

*Workshops and other forums*, for UNIDO professional headquarters staff, staff brought in from the field (UNIDO Representatives), high-level representation from member States, eminent outside experts and development practitioners, also provided a new dynamic framework for decision making and played a major part in clarifying UNIDO's role in industrial development. Specifically, they provided conceptual and practical guidance in the programmatic refocusing of UNIDO, and in the redesign of its services and field presence. They were pivotal in optimizing in-house integration of activities and acting as an organization-wide forum to refocus policy advice and services and maximize synergies, while avoiding internal duplication and duplication with other organizations and development actors. They also provided the organizational framework to maximize development impact.

### *CHANGES IN PERSONNEL POLICY: CAREER DEVELOPMENT AND SUPPORT*

A proper human-resource and skill base was vital to UNIDO's transformation, particularly the programmatic transformation. A new career development system and other support mechanisms were introduced; they became fully operational in January 1999. These introduced fundamental changes in the way the organization operated. The system included:

- *New job descriptions* for all staff, based on the specific services the organization offers.

- A *comprehensive training programme*, based on the skill gaps revealed by a comparison of existing staff skills with the competencies and skills required to implement the new services.
- A *rotation policy* between Headquarters and field offices and among Headquarters posts.
- An updated roster of consultants.
- A new staff performance appraisal system focusing on teamwork.
- A new *staff incentive scheme*, including training abroad, merit awards and publication of achievements.
- *Planning to renew UNIDO's human-resource base* in response to expected retirements in years up to 2003.

It is believed that these measures will enhance efficiency, reduce staff stress and increase morale. Retirements in the years up to 2003 will offer an opportunity to refresh the organization's human-resource base, ensure career stability and provide longer-term job opportunities.

Enhanced information systems have been developed and are being continuously improved to support programmatic decision making, particularly to monitor programmes, integrate and strengthen financial reporting and improve communication with field offices and Investment and Technology Promotion Offices.

### *DECENTRALIZATION*

Decentralization to the field was an important goal of the transformation process. In response to the Business Plan, UNIDO began at an early stage to decentralize responsibilities and delegate activity to the field offices, taking action to empower them.<sup>109</sup>

Although UNIDO has always maintained an active corps of field staff, throughout its history it has been seen primarily as a headquarters organization. In 1998, the organization introduced a number of measures to assign greater responsibility to field staff as part of its transformation. In 1999, UNIDO began its progression from being a predominantly headquarters organization with a field component to being a *field organization with its Headquarters in Vienna*. In testimony to the importance UNIDO attaches to activities in the field the organization increased by 44 per cent the resources allocated to its field programme in the biennium 2000–2001.

By the end of 1999, 23 country offices were headed by UNIDO Representatives, the vast majority of which had been deployed from Headquarters. Five Regional Offices were established at the end of 1999 (Egypt, Ethiopia, Thailand, Uruguay and Zimbabwe) and four country offices converted into Regional Offices in 2000 (Austria, Colombia, India, and Lebanon). In a number of countries without a UNIDO Representative, the organization established national focal points. In a few countries where there is no UNIDO presence, a UNIDO officer was placed in the local UNDP office.

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<sup>109</sup>This section is drawn from UNIDO, *Annual Report 1999*.

The field network aims to keep people in the field in touch with UNIDO's clients, in both the government and the non-governmental sectors. It also helps the increasing decentralization of decision-making by donors to their field offices. Field staff are well placed to assess their host countries' requirements for industrial development. The main purpose of the field offices is to promote and support technical assistance in order to encourage national capacity building for industrial development at the level of government, public sector, industrial associations and enterprises. This in turn facilitates local ownership of the organization's integrated programmes.

The field offices also have a function in advocacy and funds mobilization, promoting a better awareness of UNIDO's programmes and activities, and providing on-the-spot evaluations of UNIDO's programmes. Their job is to describe UNIDO's services to a client country, to suggest the services that would be most appropriate for its needs and to relay this information back to Headquarters, so that work can begin on the preparation of a tailor-made programme.

A criticism levelled against UNIDO in the past was that its services tended to reflect the expertise and interests of the staff member preparing projects and programmes rather than the requirements of its client countries. This has changed; the primary purpose in strengthening UNIDO's field activities has been to *ensure that its services are demand-rather than supply-driven*.<sup>110</sup>

UNIDO's field officers now have much closer contact with other United Nations agencies present in the field. They often serve as country-level focal points for the UNDAF exercise and as members of the United Nations country teams. They participate in programming meetings for representatives of different organizations and play a critical role in the preparation of common country assessments (CCAs).

## Phase II

### *CHANGES IN PROGRAMMING METHODS*<sup>111</sup>

Administrative, operational and structural reforms provided the framework and procedural mechanisms to facilitate UNIDO's transformation. But a concomitant and complementary set of programmatic reforms was required to ensure that the organization had the right focus. There was therefore a conscious decision at the beginning of the transformation process to initiate an overhaul of programming along with the administrative, structural, personnel and financial reforms. This was required because it was found that the uncoordinated way in which technical cooperation was designed, processed and implemented hindered the potential synergy of UNIDO's activities to achieve optimal impact at the country level.

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<sup>110</sup>UNIDO, *Annual Report 1999*, p. 11; see also UNIDO, *Annual Report 1998* and below.

<sup>111</sup>UNIDO, *Indicators and Impact in the Context of Integrated Programmes*, Conference Room Paper, IDB.22, 2000.

Formerly, in UNIDO as in other UN specialized agencies, a response to a request for assistance from a country was prepared by one staff member isolated from staff working in other parts of the organization. This staff member would, after analysing the request, decide which activities should be performed. In general, the staff member would, to the best of his or her ability, suggest which technical action would lead to the required results, in most cases suggesting combinations of different specializations without necessarily being an expert in all of them. This process was inefficient, ineffective and time-consuming. Staff members would often need to make an educated guess about how to combine the many different technical fields which would be required. In many instances these staff drew largely on external consultants not conversant with UNIDO methodologies available elsewhere in the organization.

Since the assistance was frequently designed by a single person, it was usually limited to a few outputs. Not surprisingly, technical assistance projects had low budgets and were too limited to produce significant impact. In many cases, these limitations meant that the technical assistance designed to assist countries would foster overlap among staff, lack standardization, and produce highly varied results. This approach prevented UNIDO from giving its clients the range of expertise needed to ensure a sustained improvement in their development situation.

As a result, when the new Director-General took office in December 1997, UNIDO had a total of 1,700 projects, with an average size of \$100,000 and activities originating from 48 components and 205 sub-components, with considerable duplication of activities among branches. To remedy the situation, UNIDO completely overhauled its programming approach and methodology. It developed a number of criteria to guide its programmatic transformation:

- Technical cooperation should be *demand-driven*.
- *No overlap* should exist within the organization or, wherever possible, with other agencies of the UN system.
- *Competition* with private-sector consulting companies should be *avoided*.
- The programmatic *changes should not result in staff lay-offs*. Staff changes would be effected through retirements and training.
- UNIDO should *specialize in a limited number of fields of expertise*. Nevertheless, these should be delivered in an integrated fashion to comprehensively address identified problems. The transformation was undertaken in five—not always sequential—steps:
  - Revise the concept of UNIDO's *product*.
  - Design a new and improved *process* for preparing products.
  - Establish a new *production* mechanism based on teamwork.
  - Develop appropriate *procedures* for design and implementation of technical cooperation.



- Develop *performance* indicators to measure the efficiency of product delivery, internally and with respect to external impact at the institutional (client) and target group (enterprise) level.<sup>112</sup>

## PRODUCT REDESIGN

The starting-point for redesigning UNIDO's products was to analyse the existing activities performed by each branch of the organization, and group them into 'components' and 'services'.<sup>113</sup> For example, for the component 'industrial standards', the services could be 'establishment of a standardization body', 'harmonization of standards', 'development of standards', and so on.

The components of on-going projects were identified by listing all the services offered by each technical branch of the organization. This procedure led to a detailed analysis of the services that UNIDO could offer, based on the available expertise. It also identified which services should be discontinued or transferred to another UNIDO branch or even another UN agency better able to provide them. The main finding was that most staff were designing their own projects, mainly from the perspective of their own areas of competence. Most important of all, the exercise found a high level of duplication of activities throughout the organization. Projects were often supplier-driven, and usually originated in a proposal from a staff member to a counterpart in a recipient country. Invariably, this person was not responsible for, or did not have an overview of, the overall development strategy of the country, so that the project was too narrowly conceived.

The next stage was then to filter or combine services or both, using the following criteria:

- That activities should be in line with the Business Plan.
- That specialized technical staff were available to carry them out.
- That developing countries needed the proposed activities.
- That UNIDO had experience of implementing them in the field.

The services that passed these criteria were regrouped according to the fields of knowledge required to carry them out. As a result, 16 types of specialized services, called '*service modules*', were declared to be available from UNIDO.<sup>114</sup>

Each service module represents the final stage of UNIDO's first systematic attempt to refine and streamline its body of knowledge specific to a major concern in industrial development. Decisions to retain modules are also the result of intensive analysis of the demand for UNIDO's services on the one hand and of an assessment of the organization's core competencies on the other.

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<sup>112</sup>These steps were known internally as the '5 Ps'.

<sup>113</sup>A 'component' is a set of actions by UNIDO to address one critical problem that constrains the achievement of a development objective that a country has selected.

<sup>114</sup>As of early 2001, the services modules will be streamlined and reduced in number with a view to maximize synergy amongst them.

Sixteen service modules have been developed:

- Industrial Strategies and Policies
- Statistics and Information Networks
- Metrology, Standardization, Certification and Accreditation
- Continuous Improvement and Quality Management
- Investment and Technology Promotion
- Environmental Policy Framework
- United Nations' Framework Convention of Climate Change and Kyoto Protocol
- Energy Efficiency
- Renewable Energy Development
- Cleaner Production
- Pollution Control and Waste Management
- Montreal Protocol on Substances that Deplete the Ozone Layer
- Policy Framework for Small and Medium-sized Enterprises
- Women's Entrepreneurship Development
- Industrial Business Development Services
- Upgrading Agro-Industries and Related Technical Skills.<sup>115</sup>

The service modules refocused UNIDO's activities into a limited number of areas. They provide a clear idea of what it can deliver. It also helped the organization to decide what it can do alone and must be done together with others. To ensure that the refocusing of UNIDO's services was practical and not theoretical, between one and three service modules were assigned to each branch of the organization as part of its distinct core identity.

The new service modules have included an innovative managerial tool, which uses *the concept of 'buy and sell'*. This is a mechanism to exchange services among branches, and to 'buy' services from other agencies, which UNIDO does not or cannot provide itself. This mechanism has introduced routine cooperation between the branches of UNIDO, and with other agencies—particularly within the UN system—and other development actors. It thus facilitates teamwork across the organization and between agencies. Most importantly, it avoids duplication and overlap. The organization now has a framework to maximize synergies throughout the UN system by means of inter-agency agreements, for example the Memorandum of Understanding signed by UNIDO with UNCTAD, UNDP and UNEP, covering services that each organizations provides.

The 16 service modules were also grouped into *three 'baskets'* according to how each service contributed to UNIDO's long-term goals of sustainable development, the *3 Es* (competitive Economy, productive Employment and sound Environment).

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<sup>115</sup>UNIDO, *Service Modules*, 1999.

Clients can now 'pick and mix' services from the three baskets according to their specific requirements. They thus have ownership of the services provided and can tailor the services to their own development goals and their preferred means of achieving them.

In sum, the service modules are comprised of a set of interrelated services which facilitates their combination with other services modules as required. The combination of services ensure a significant contribution to the achievement of development objectives. They are client-based and client-driven; they link the interests of recipient and donor countries in a practical development approach. They have allowed UNIDO to focus more sharply, avoid duplication and integrate internally and externally. Most importantly, they have allowed a closer identification with broader UN objectives and international development targets.

### *PROCESS IMPROVEMENT*

The service modules were so designed that there was no duplication between them. The next step was to redistribute services to the individual branches of the organization, taking into consideration the skills of the staff and past activities.

At least one service module was assigned to each Branch of UNIDO as its core competency. But the requirements of an individual country would in most cases need to be covered by more than one service module. It became clear that UNIDO would have to refine the way in which offered its services. It introduced the concept of 'integrated packages of services', which the Danish Assessment had identified as UNIDO's comparative advantage.

In the terms of the Business Plan, *these packages became 'integrated programmes'*. Integrated programmes are packages of mutually supportive services which combine the collective experience of UNIDO to help overcome the critical industrial development problems of countries, or of particular geographic areas within a country.

Nevertheless, the characteristics and needs of developing countries are extremely varied, and there are cases in which assistance is required mainly from one service module; here 'stand-alone' service modules are offered. In particular, they are important for countries which do not as yet have an integrated programme, or large developing countries such as India and China where an integrated programme for the whole country is not feasible. For these countries '*service frameworks*' are developed which combine geographically focused integrated programmes and stand-alone projects required to comprehensively solve local development problems and at same time address specific constraints in a particular field elsewhere in the country.

Teamwork is the key to the design of services offered as integrated programmes. This means that UNIDO had to change the process by which it drew up its offers of services so that it was based not on the efforts of one or a few individuals but on cross-organizational teamwork.

The concept of integrated programmes also stems from the programme approach that was agreed by all UN agencies in 1993. It is based on the view that it is best to tackle only one development objective at a time, but to address it in all its dimensions. What

is new in the UNIDO concept is the emphasis given to integration and coordination of efforts at three different levels:

- Integration with country efforts.
- Integration with external aid.
- Integration within UNIDO.

Instead of as a number of isolated, small projects, UNIDO support is now *packaged as a programme*. The programme has well-defined linkages among its different components, a greater sense of ownership at the country level and increased synergy with external aid. Ideally, an integrated programme should:

- Focus on the critical problems that constrain the achievement of a country's industrial objectives.
- Seek out areas where UNIDO assistance could have a catalytic or multiplier effect.
- Look for synergy with United Nations and other external aid programmes.
- Aim at a reasonable balance among economic, social and environmental considerations.

UNIDO's integrated programme approach represents the successful implementation of the Business Plan's call for UNIDO to support the industrial development efforts of recipient countries primarily through comprehensive packages of integrated services provided by multi-disciplinary teamwork.

UNIDO's philosophy in developing integrated programmes is to base them squarely on consultation and collaboration with Governments, the main stakeholders in recipient countries, and with potential donors. As a result of this consultation, UNIDO implements its programmes only in those areas where it can really make a difference.

By channelling UNIDO's limited resources to where they are most needed, the integrated approach increases the efficiency of the assistance provided by the organization, produces a multiplier effect and leads to greater impact.

In summary, UNIDO's integrated programmes embody the organization's comparative advantage, they are comprehensive yet focussed since they are based on the view that it is preferable to tackle only one development objective at a time but uniquely address it in all of its dimensions. UNIDO's concept gives emphasis to integration and coordination of efforts at three levels:

- with the strategies and action of the partner country
- with the initiatives of the development agencies and donors
- within UNIDO itself.

### *PRODUCTION MECHANISM: CROSS-ORGANIZATIONAL TEAMS*

Once the concept of integrated programmes was refined, the next challenge was to tailor UNIDO's services to requests for assistance by countries in an integrated fashion. More

often than not this would mean combining different service modules, which would require combining the expertise of staff with different specializations and cooperation between branches of UNIDO. Hitherto, cross-organizational cooperation had been much talked about, seldom practised and, when practised, rarely successfully. Staff had often worked in splendid isolation, as if separated by fire-walls. The solution was to form teams composed of staff representing all the specializations required to address the development problems identified in the request for assistance.

An initially slow and sometimes painful process of team building and a new culture of cross-organizational teamwork were begun.

For each country, a team is put together that comprises five to ten members who between them have in-depth knowledge of the main areas of the proposed approach to the development problems presented in the request for assistance. The team includes staff in UNIDO's field offices. After consultations among senior and middle management, a team leader is nominated and presented to the Executive Board for approval. In terms of line authority, the team leader reports to the Executive Board. Individual team members are also cleared by the Executive Board on the basis of the proposed approach and the recommendations of managing directors and branch directors. The composition of the team is nevertheless flexible and additional members can be changed when the need arises.

The selection of the team leader<sup>116</sup> is of critical importance for the successful outcome of the programming exercise. A good team leader should

- be able to get along with staff at all levels
- motivate and coach team members
- be objective and be a good facilitator
- have a good grasp of all UNIDO service modules
- be respected in his or her own right
- have good management skills.

In addition to these general qualities, specific competencies may be required depending on the complexity and scope of the formulation exercise. For a programme that would include a wide range of services, good coordination skills may be essential; for a more focused programme, a strong thematic or sectoral background may be important; for a programme which proposes to omit some of the services requested, negotiating skills may be crucial to arrive at a common understanding with the Government.

The successful production of integrated programmes has been extremely difficult for UNIDO,<sup>117</sup> as it would be for other organizations. It is difficult and time-consuming to put together multi-disciplinary approaches and teams. They are a necessary but complex response to complex problems. After a team is composed, extensive analysis must be done to identify the needs of a country as a basis for subsequent discussions with local authorities and programme stakeholders. This needs assessment is essential to ensure that

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<sup>116</sup>UNIDO, *Guidelines for the Formulation of Integrated Programmes*.

<sup>117</sup>UNIDO, *Indicators and Impact in the Context of Integrated Programmes*, Conference Room Paper, IDB.22, 2000.

a programme is properly focused and ultimately has impact. But the process is frequently lengthy, entailing many exchanges between UNIDO and the recipient to refine the needs analysis. Regional specialists in the Regional Bureaux play an important role here. They dialogue with Governments to identify the response strategy, in the light of the country's development objectives and other current or future assistance, and help to identify the service modules which will form the basis of an integrated programme.

## *PROCEDURES FOR DESIGN AND IMPLEMENTATION*

Successful implementation is the major challenge of any technical cooperation and careful preparation is often the key to success. This has been particularly true for UNIDO's integrated programmes, which are a complicated undertaking. They require a common understanding of the issues to be confronted and the steps to be taken, selectivity in the identification of the country objective to be supported, committed counterparts, mechanisms for coordination, and sufficient human and financial resources.

UNIDO has guided the implementation of its integrated programmes by means of a detailed manual called 'Guidelines for the Formulation of Integrated Programmes', issued in May 1999. It is based on careful analysis of best UNIDO and international practice.

The Guidelines have helped teams to prepare viable, fundable integrated programmes that demonstrably meet expressed needs. They indicate the steps to be followed, by whom and when. The objective is to ensure a systematic and analytical approach which consistently produces programmes of high quality.<sup>118</sup>

## *PROGRAMMES TO DATE*

The first integrated programmes were launched by UNIDO in 1998; in line with the priorities set in the Business Plan, half were for African LDCs: Burkina Faso, Guinea, Rwanda, Uganda and the United Republic of Tanzania. Algeria and India were also included in the first programming round. Nevertheless, UNIDO is a universal organization and its industrialization support services need to be provided to developed countries and economies in transition to maintain the organization's relevance for them.

With 33 programmes in progress at the end of April 2000, eight more approved by the Executive Board and five being finalized or under development, integrated programmes are now the main instrument for the delivery of UNIDO's technical cooperation activities. Coverage has been extended to all regions, but the focus is still on Africa and LDCs, which accounts for 22 of the programmes. The distribution of the programmes by region is shown in table 5. The total budget of the 41 on-going and approved programmes amounts to some \$290,000,000.

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<sup>118</sup>The Guidelines are organized in four blocks: Screening, Preliminary assessment, Fieldwork and Programme finalization. Each block is divided into steps that outline actions to be taken, responsibilities, and documentation to be completed. Annexes provide formats for the documentation and tools for collecting and analysing the information and defining the UNIDO approach. See, UNIDO, *Guidelines for the Formulation of Integrated Programmes*, Appendix to DGAI No. 11, 1999 and subsequent Addenda.

**Table 5. UNIDO's integrated programmes**  
*Status of development and implementation (at 4 May 2000)*

<i>Region</i>	<i>In progress</i>	<i>Approved</i>	<i>In preparation</i>
<b>Africa</b>	Burkina Faso Côte d'Ivoire Eritrea Ethiopia Ghana Guinea Mali Mozambique Rwanda Senegal Uganda United Republic of Tanzania		Lesotho Namibia Nigeria
<b>Arab</b>	Algeria Morocco Palestinian Authority Sudan Tunisia Yemen	Egypt Jordan Saudi Arabia	Lebanon
<b>Asia and the Pacific</b>	India (Partnership— preparatory phase) Pakistan Sri Lanka Thailand	Islamic Republic of Iran Lao People's Democratic Republic Nepal	
<b>Europe and NIS</b>	Armenia Russian Federation (Bashkortostan) Russian Federation (Federal) Russian Federation (Moscow) Russian Federation (St Petersburg) Russian Federation (Komi)	Tajikistan Uzbekistan	
<b>Latin America and the Caribbean</b>	Bolivia Colombia Cuba Guatemala Honduras		Nicaragua

*Source:* Integrated Programmes database.

## **PERFORMANCE MEASUREMENT**

Increasingly, donors and recipients insist on visible impact from programmes. The measurement of performance is therefore essential to assess the impact of UNIDO's services—whether their intended results are being achieved. It is also important to measure changes brought about by a technical cooperation programme in order to show donors and recipients the validity of the approach used to deal with development problems, as well as its impact.

UNIDO has identified three levels of indicators: *milestones*, which are the results or products delivered by UNIDO; *success indicators*, which measure the changes at the level of the direct beneficiaries—UNIDO's counterparts—usually at the institutional level, but sometimes at the level of pilot enterprises; *impact*, or changes, at the level of the target beneficiaries—the universe of enterprises in a particular sector or geographic location—in accordance with a country's objectives.

UNIDO is continuously improving its programme performance measurement system. Work is underway to systematically measure economic impact by establishing better programme baselines. Other agencies are also struggling with the need to provide better measures of programme achievements. UNIDO is actively seeking to cooperate with them to collectively resolve this long standing problem.

Some of the preliminary achievements of UNIDO's earliest integrated programmes are presented in table 6.

However, many achievements cannot be captured by indicators. For example, daily optimization of resources, sharing of experience and coordination among stakeholders have been cited as side-effects of some programmes; these aspects are hard to quantify.

**Table 6. Achievements of some integrated programmes**

<i>Outputs</i>	<i>Milestones</i>	<i>Success indicators</i>	<i>Impact (country-level)</i>
<b>Burkina Faso</b>			
Artisans processing of horns and bones introduced in pilot workshop	Nine artisans trained	Pilot workshop set up	Completely new business created
	Machinery for common use installed	Cluster of artisans created and operational	Example set for other countries
	Each artisan provided with tool kit for production	New range of products manufactured from previously useless raw material (horns)	
		New income opportunities generated	
		Inputs provided to leather artisans	
<b>United Republic of Tanzania (URT)</b>			
Improved fish processing capacity	15 inspectors, 23 QA staff, 73 managers, 293 vessel staff and 1158 workers trained	Fishery Authority regularly tests fish quality	Fish products meet international safety requirements
	Code of conduct prepared	40 fish-processing plants apply quality procedures	EU ban on fish imports from URT lifted (\$150 m)
	Fish inspection manual prepared	50 per cent of vessels' crews apply quality procedures	Example set for other countries in the region
	Laboratory equipped and tools provided to Tanzania Bureau of Standards (TBS)		



## **UNIDO's global forum function**

UNIDO has a dual role, as a provider of integrated technical cooperation services and as a global forum for industry in which UNIDO acquires and disseminates knowledge of the industrial development process.

The transformation of UNIDO's programming methods has refocused the organization in both its roles. The changes in programming as well as in the administrative, structural and financial areas also affected the organization's global forum function. First, the initial concentration on technical cooperation reduced the resources and staff available for global forum activities, particularly research (though the integrated programmes did include global forum components, for example with respect to industrial policy). Secondly, the inter-linkages between global forum activities and technical cooperation had to be strengthened. This became a priority in the later stages of the transformation process.

The Business Plan attached special importance to UNIDO's global forum function. It saw it as an integral part of UNIDO's mandate to strengthen industrial capacities in developing countries and countries with economies in transition. It called upon UNIDO to implement programmes related to:

- Industry policy advice based on action-oriented research.
- Institutional capacity building at the country and sectoral levels.
- Quality, standardization and metrology.
- Industrial information through networking, including information on the transfer of technology.
- Industrial statistics.

On the basis of these programmes, UNIDO has been able to undertake a wide range of activities, beyond the confines of specific technical cooperation projects, to support and promote industrial development. These activities have included initiatives to understand the dynamics of the industrial development process and disseminate through specialized meetings and publications the lessons learned about a diversity of industry-related issues. In the course of these activities, UNIDO has promoted partnerships and supported global industrial cooperation, both between developed and developing countries and among developing countries. In doing so, it has facilitated the spread of industrial information, knowledge, technology and investment.

The reorientation of UNIDO's global activities has included the development of major meetings, fora, partnerships and publications.<sup>119</sup> These instruments have presented to the international community the major issues of industrial development, particularly the relevance of industrial development to broader economic and social development, and identified areas for developing countries to focus on in the pursuit of economic reforms.

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<sup>119</sup>UNIDO, *Annual Report 1999*, pp. 12–18.

The importance of UNIDO's global forum function is beyond doubt. Global forum activities confirm the organization's agenda-setting, knowledge-sharing, partnership-promoting role. Done well, they can build UNIDO's image and make it more visible. But before the transformation UNIDO's global forum activities suffered from inadequate financial and staff resources, and their messages were insufficiently clear. Not surprisingly, their impact was weak.

UNIDO's *Research Programme*, in particular, had undergone significant structural and organizational changes and cuts in staff and financial resources in previous reforms of the organization, beginning in 1994. UNIDO's research activities required urgent re-examination as part of the transformation process, if UNIDO was to achieve its potential as a global forum for industry. A cross-organizational team was set up which recommended that UNIDO's Research Programme should *concentrate on selected areas*. The recommendations emphasized action-oriented research, including better linkage of research with technical cooperation activities, the use of technical cooperation evaluation results, the dissemination of best practices and policies, and the development of networks of researchers to maximize the capacity of UNIDO's limited but still important research capabilities. Emphasis, as required in the Business Plan, was still to be placed on Africa and LDCs.

A special focus in UNIDO's reorientation of its global forum activities has been to forge *partnerships with universities, research institutions and other civil society organizations*. The objective is to help UNIDO acquire a stronger analytical base and at the same time to encourage greater international cooperation in the area of sustainable industrial development in developing countries. This approach also enhanced the normative capabilities of UNIDO—an imperative in the context of both United Nations reform and today's global economy.

One such partnership has been with the *University of Oxford* in the United Kingdom. On 6 October 1999, a two-year agreement was signed for research on African economic performance under a joint programme to be funded by UNIDO, the first agreement of its kind between UNIDO and a university in the United Kingdom. It includes funding for a two-year UNIDO research fellowship at the University's Centre for the Study of African Economies (CSAE) within the Department of Economics. Under the terms of the agreement, UNIDO and the University will

'enter into a programme of cooperative research [...] with the aim of enhancing and disseminating knowledge and skills which foster Africa's improved economic performance, particularly through the promotion of sustainable industrial development'.<sup>120</sup>

The research programme is a direct response to the mandate given to UNIDO in its Business Plan to focus its activities on LDCs, particularly in Africa. A *training programme for African civil servants* aims to build capacity among African policy-makers, especially in countries where UNIDO has initiated, or will initiate, an integrated programme.

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<sup>120</sup>UNIDO, *Annual Report 1999*, p. 14.

The Oxford experience, a concrete example of UNIDO reaching out to link up with civil society, adds a new string to UNIDO's bow and is being replicated with leading universities in other countries.

As part of the refocusing of its global forum activities, UNIDO developed a partnership of a different kind. This partnership programme seeks to develop a new approach towards capacity building for small and medium-sized enterprises, and to do so with major players in the business world who have an interest in strengthening their supply chain.

One of the most difficult hurdles facing developing countries which are trying to increase exports is raising product quality to meet international standards. The gap in standards is the reason for the extensive use of non-tariff barriers that frequently prevents the developing world from gaining access to markets. *Fiat SpA*, through Magneti Marelli, a subsidiary with car production plants in India, has entered a *partnership programme* with UNIDO which aims to improve the quality of car parts produced by suppliers in south-east India. The partnership also includes the Government of India, INSEAD—a prestigious French business school—the Prince of Wales Leader Forum and two local car component producer associations.

This unique private/public-sector undertaking has, in less than a year, produced striking results: increased productivity, cleaner production methods, better use of technology and greater awareness of the need for continuous improvement.

UNIDO has also been in contact with other transnational corporations seeking to replicate the Fiat success in other sectors of industry. Ultimately, the Fiat-UNIDO partnership programme will help small and medium-sized Indian car parts' manufacturers not only to expand their production to meet local demand, but also to be ready to meet the demands of a global market.

These are but a few of the initiatives taken to revitalize UNIDO's global forum functions. Much has been achieved, but further refinement is required, first to encourage greater cross-fertilization with operational activities, and secondly to better reorient the Research Programme to applied research. Basic research is no longer undertaken, but focal areas for applied research are only just emerging. A revitalizing focus on research by small teams drawing inputs from across the organization would be useful.

The key to focusing UNIDO's global forum activities has been the development of a umbrella theme to ensure a clear and consistent message, enhance the organization's image, ensure greater visibility, and economize on resources. This work is not complete, but the right path has been found.

## **System-wide cooperation**

In the reform and refocusing of the multilateral system, a pillar of UNIDO's transformation, has been *cooperation with other organizations, particularly within the United Nations system*.

It has also given UNIDO a clear purpose and identity in the United Nations system. Before, UNIDO suffered from isolation from the rest of the system and a lack of focus. Overlap with other agencies was also a problem. In addition to agreements with

UNCTAD, UNDP, and UNEP, UNIDO has initiated cooperation with WTO, the International Trade Centre (ITC), the World Bank and IMF in the implementation of the WTO Integrated Framework of Assistance to LDCs, aimed at improving their trade sectors and trade-related activities. A basic implementation agreement was signed with the United Nations Fund for International Partnerships (UNFIP), and a joint programme is being developed with the United Nations Centre for Human Settlements (Habitat). UNIDO also cooperates with other organizations.<sup>121</sup>

Part of the implementation of UNIDO's transformation process has been its new decentralized and empowered network of field offices. The current challenge is to integrate UNIDO into coherent United Nations approaches and institutional set-ups at the country level—particularly the new United Nations Development Assistance Framework (UNDAF) and 'UN houses' where UN agencies are housed together to encourage cooperation and synergies—and to ensure a consistent system-wide approach to development. UNIDO is helping to lay the groundwork for this further integration at the country level by participating in UNDAF pilot countries. It has worked closely with United Nations Resident Coordinators to undertake integrated programming in a number of African countries, including Côte d'Ivoire (environment and private-sector development), Ghana (environment), and Guinea (private-sector development), and in countries in other regions.

UNIDO's integrated programmes and field-level emphasis have endowed the organization with appropriate means to contribute to the UNDAF process, which is a direct response to the Secretary-General's reform programme and a key mechanism in developing a common system framework. UNIDO Representatives serve as country-level focal points for the UNDAF exercise and as members of United Nations country teams. They also participate through United Nations country-level meetings in the development of system-wide approaches. UNIDO has provided substantial inputs into CCAs and the UNDAF guidelines. During the development of its integrated programmes, UNIDO ensures integration with UNDAF and the United Nations Special Initiative for Africa exercises. In 1999, UNIDO was engaged in the UNDAF process at the country level in places where no integrated programmes had yet been developed.

While the organization has over time accrued significant experience in collaboration, it encountered a number of constraints in achieving cooperation with other organizations, despite the supportive spirit that generally prevails. One reason is the far-reaching agenda implied by some agreements. Another is the insufficiency of financial resources.

However, UNIDO is firmly committed to systemic approaches and to the Secretary-General's reform proposals. The reforms launched by the Secretary-General have given a welcome new momentum to the United Nations agenda. To support them, UNIDO seconded a senior staff member to the United Nations Development Group Office in New York. The purpose of UNIDO's transformation is to contribute to the renewal and revitalization of the UN system as a whole.

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<sup>121</sup>UNIDO, *Annual Report 1999*, pp. 28–29.

## The lessons of UNIDO's transformation process<sup>122</sup>

Many lessons can be learned from UNIDO's transformation process. These can be divided into general lessons and those specific to the integrated programmes, the key instrument through which the transformation was carried out.

The general lessons can be divided into the following—not always mutually exclusive—categories:

- Cross-cutting issues
- Leadership
- Structure and personnel
- Budgets and programmes
- Governance
- Coordination and cooperation with other UN agencies, multilateral organizations, and civil society
- Public image and public relations

### CROSS-CUTTING ISSUES

A number of factors are critical for successful transformation:

(a) Transformation needs to be driven and owned by the organization's stakeholders (principally the member States, with the Secretariat playing a supportive role). This is the main lesson of UNIDO's Business Plan. Priorities have to be developed and agreed by member States in consensus if there is to be real ownership of the role and functions of an organization.

(b) Transformation is not a one-off event, but a process. Priorities must not be set in stone, but adapted to changing circumstances.

(c) Recipient countries must be involved from the very beginning in the design and implementation of a transformation process, particularly in the identification, formulation and implementation of an organization's new programmes, such as UNIDO's integrated programmes.

(d) Tacit values, the intangibles of an organization, need to be considered; these include culture, values, leadership, current and past practices and incentives. UNIDO's previous incentive structure was biased against teamwork; rewards structures did not encourage cooperation and cross-organizational teamwork.

(e) Transformation requires a long-term commitment and sustained political and financial support from all stakeholders—donor and recipient countries alike. The Business Plan staked out this initial commitment, but sustained support in the form of predictable funding, for operational activities in particular, is still a problem. There are no quick fixes for successful transformation.

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<sup>122</sup>This section draws on comments made at a presentation of UNIDO's transformation process at the Wilton Park conference on 'The United Nations: Prospects for Renewal', 9–13 November 1998.

(f) Transformation requires a spirit of shared responsibility and common purpose, a complete re-thinking of old priorities, approaches and procedures. It must focus on the positive. It must preserve what was good about an organization and abandon what was bad. A new culture of learning and teamwork has to be inculcated so that all staff and, on occasions, member States and their technical experts as well, fully understand and share the objectives, and thereby accept ownership, of the transformation process. Senior management retreats, seminars, workshops and training programmes can help to do this. They can also help to develop the focus and major services of an organization and to constantly adjust a transformation process to keep it on track. Staff at all levels need to understand their role and function in a transformation process.

(g) An organization needs to address traditional functional and power structures at an early stage and be imaginative in replacing them. In UNIDO's case, multi-disciplinary, cross-organizational teams and team leaders were the instruments. Teams and team leaders drawn from individual branches under the line of authority of a Branch Director were successful because they were appointed by and reported to the senior managers of the organization, the Executive Board, comprising the Director-General and the Managing Directors of divisions; because team leaders had organization-wide responsibilities, they also had the authority to draw on inputs across the organization to ensure an integrated response to requests for technical cooperation. With the empowerment of teams, and team leaders in particular, by the highest management in the organization, cooperation and coordination was assured.

UNIDO's experience has emphasized transformation designed and implemented by the management and staff themselves. Earlier reform efforts which engaged external consultants achieved only partial success. However, the work of these external consultants, particularly with respect to administrative structures and procedures, did lay the foundation in these areas for the organization's eventual transformation.

Finally, it is important to stress that transformation is not about cutting budgets or staff. It is essentially about *making an organization more responsive to the needs of its clients*.

## LEADERSHIP

High-quality leadership is critical for successful transformation. The new leadership provided by the United Nations Secretary-General and heads of specialized agencies shows what good leadership can contribute to successful transformation.

As well as strong and effective leadership, transformation requires clear policy and strategic direction. The leadership must emphasize partnership with staff, with donor and recipient countries, with other UN, multilateral and bilateral agencies, and the private sector and civil society, the so-called 'friends' of an organization. Partnership, not autocracy, provides the sustained momentum, support and effort required for successful transformation. An obvious and closely related lesson is that teamwork—as in UNIDO's integrated programme approach—is the hallmark of success in transformation.

Heads of agencies need to provide a clear vision and strategy in the form of a mission statement and a corporate identity. Priorities and broad direction can, and must, be undertaken by member States, but the organizations themselves, particularly their leaders, must add a strong and easily communicable policy and strategic vision to refine these priorities. This lesson is clearly shown in the experience of the Business Plan, which could not have been implemented without the further refinement given by the Director-General's personal stamp, or his vision of how he wanted the organization to develop.

Leaders need to have at least an appreciation, and will preferably have some experience, of 'change management'; if they do not have such experience themselves, then their senior management must. A capable and complementary senior management team is therefore vital.

Agency heads should provide leadership and vision and high-level external advocacy. But they should be supported by a deputy or deputies, a competent senior management team. At UN Headquarters the Secretary-General has a Deputy who deals, among other things, with the everyday management of the organization; at UNIDO the Director-General has a Deputy and an Executive Board and a change-management support team in his office; similar relationships between agency heads and top management exist at other specialized agencies.

There can be no dispute that as leadership skills have been a major factor in successful transformation in specialized agencies, so they must be for UN system-wide transformation.

## *STRUCTURE AND PERSONNEL*

UNIDO's experience shows the necessity of fitting organizational structures to its programmes. The new organizational structure of UNIDO is fully aligned with its programmatic priorities as given in the Business Plan. Responsibilities are clearly delineated by terms of reference for organizational units. A new career development system and staff appraisal system is in place. Teamwork is recognized and rewarded. Promotion is based on objective assessment, and first and foremost on merit.

A more effective system is still needed to identify successors to those retiring or otherwise leaving the organization, to avoid affecting the organization's critical mass in key areas. Staff, teams especially, need to be given clear and feasible targets to ensure a shared vision and strategy and effective implementation.

Finally, recruitment is still subject to political pressures and outside interference. UNIDO has a policy to recruit staff to fill clearly identified vacancies, to develop clear terms of reference for vacant posts, and to advertise these posts widely to increase transparency and competition.

## *PROGRAMMES AND BUDGET*

If Programme and Budget documents are to be effective, they must be clearly written and easy to understand, and avoid jargon. UNIDO has made tremendous progress in this area.

Its Programme and Budget documents are concise and clear, and its programme documents pay special attention to presentation, format and readability. Member States cannot be expected to support budget priorities and requests for programme funding if they are not clearly communicated.

UNIDO's budget is presented in a programmatic format to better articulate the organization's priorities, objectives, services and costs. In the presentation of UNIDO's budget, programmes are equated with service modules as opposed to organizational units, greatly improving the transparency of the budget.

UNIDO's experience shows that agencies need strict criteria to select programmes and to reject proposals that do not meet these criteria. For example, once UNIDO had adopted its integrated programme approach for technical cooperation, in general it rejected proposals that could not be accommodated within this framework. This was also the approach UNIDO used to whittle down its services to 16 service modules.

The objective of any programme is client satisfaction. Programmes should therefore be demand- and not supply-driven, closely tied to an organization's, and preferably to the UN's, system-wide objectives of avoiding internal and external duplication; they should avoid the constant revision of objectives which tends to over-extend or blow up the original programmes. UNIDO's 'pick and mix' approach, whereby clients can choose from three baskets of its services, the *3 Es*, and its innovative mechanism in the form of 'buy and sell' tables to avoid internal and external duplication while encouraging cooperation, may be of interest to others.

Programmes should have definite time limits or 'sunset' provisions so that they remain focused on clearly defined but limited objectives, and do not go on for ever. In the past, in other agencies as well as in UNIDO, projects have sometimes gone on for as long as ten years despite questionable validity. This often resulted in inefficiencies and difficulties in assessing impact.

## GOVERNANCE

UNIDO showed that transformation can be achieved quickly and effectively, given clear guidance from member States and direction from policy-making organs or 'boards of management' (comprised of high-level representatives of member States). This is also the experience at other agencies. But a more pressing problem remains: that is, the optimal duration and focus of 'boards of management' meetings. UNIDO has tried, with the agreement of member States, to reduce the duration, and hence the cost, of meetings, and to keep the focus of meetings on substantive, rather than political and procedural, issues. These objectives have yet to be fully achieved, despite the good-will of a growing number of member States. Consideration should be given to so-called 'expert boards of management', in which more technical experts attend meetings. UNIDO's approach of calling in external experts to help guide its policies and strategic direction may also be of interest.

What UNIDO's experience shows, in particular, is that all member States must have a common interest in improving the effectiveness of UN agencies, if transformation is to take place.



On an operational level, UNIDO's experience demonstrates conclusively the need for widespread changes in an organization's strategic and internal management structure and style. Hierarchies must be flattened, transparency increased and effective rules of the game introduced quickly for successful transformation. This is especially required for decentralization and delegation at Headquarters and in the field, but also in relations with member States. Openness and transparency, re-adjustment and improvements—especially by agency Heads and senior management—based on real and continuous consultation are the hallmarks of successful transformation.

However, transformation cannot be done in a mechanistic way. It must take into account the characteristics and idiosyncrasies of a particular organization's staff, policies and structures. Each transformation process must therefore be tailor-made.

### *COORDINATION AND COOPERATION WITH OTHER AGENCIES*

Inter-agency agreements have proved useful, particularly at the political and senior management levels. But if they are to be more effective there are still many obstacles to be removed and turf battles to be overcome. It is not yet clear how this is to be done, but with good-will and commitment on the part of the agencies concerned, real partnership can be achieved. Merely signing declarations of intent and Memoranda of Understanding is not enough; programmes of cooperation at the working level based on clear delineation of areas of focus are needed. UNIDO's approach was to redesign its services into a few core areas and withdraw from other areas. Practical cooperation between agencies would be helped if each agency knew clearly what its comparative advantages were.

UNIDO's increasing reliance on networking with the private sector—for example its Public-Private Partnership programme, which includes the Fiat programme—and with research institutes and universities has maximized the value of resources and improved impact. NGOs should not be forgotten; and innovative strategies and cooperative mechanisms could better integrate NGOs into the work of UN agencies. Recognizing the role of civil society in the current global context should be a priority in any transformation. There is room for improvement here at both UNIDO and other UN agencies.

### *PUBLIC IMAGE AND PUBLIC RELATIONS*

UNIDO needs to make more effort to improve its image and reputation. This requires a clear and well-targeted communications strategy to disseminate best practices and success stories, particularly the impact of its programmes. UNIDO is redoubling its efforts in this area.

The difficulty is that development is a long-term phenomenon. It is often hard to demonstrate enough short-term impact to satisfy the demands of some donor and, less often, recipient countries.

A strategy of improving public relations would build on success, strengthen the resolve behind an organization and its mandate priorities and programmes, build up a critical mass of external support, and set an example for others.

## *THE LESSONS OF INTEGRATED PROGRAMMES*

UNIDO's integrated programmes teach that in selecting the industrial objectives to be supported, there is a need to focus. Such an approach is more likely to result in measurable impact within a reasonable time. Given its limited resources, UNIDO can only expect to comprehensively support a few out of the many development objectives that a country may have. The same is true of many other agencies, particularly UN organizations.

UNDP carried out an evaluation of the programme approach in October 1998. It classified a number of variations in the design of programmes and projects being implemented under this approach. At one end of the range were uncoordinated or scattered projects and unfocused programmes, at the other umbrella programmes and focused sectoral and multisectoral programmes. UNIDO has aimed for the top of the range—focused sectoral and multisectoral programmes. But programme teams have faced pressures to broaden the focus of programmes during the formulation phase to meet the requirements of all the counterparts. As a consequence, many programmes have fallen into the category of 'umbrella programmes'. At the country level, there has been a concern that when an integrated programme is in place, no further requests for technical assistance will be entertained. This is a largely unnecessary concern, since there are regular opportunities for review and revision of the programme in the light of achievements, constraints and changing needs. An integrated programme is a living instrument.

The three levels of integration mentioned earlier—with respect to country efforts and to external aid and within UNIDO—were designed to increase the efficiency of assistance, produce a multiplier effect, and lead to greater impact. When the Guidelines were first introduced programme teams made conscious efforts to identify complementarities with external aid, building linkages and synergies into their programmes. However, they have found themselves under pressure to disaggregate the programmes during implementation to meet the requirements and priorities of donors as preconditions for funding. Focus, linkages and synergies built into the programmes may then be diluted, particularly when available funds are channelled to 'peripheral' activities. This realization has encouraged later programme teams to ensure from the outset that their programmes can be easily split into components suitable for individual donors. However, without more flexible funding, it is difficult to ensure that integrated programmes achieve their full potential.

While individual components and outputs of a programme may be perfectly viable on their own, it is their integration that is expected to provide much of the value added and the catalytic effect. Disintegration of a programme not only negates the effort invested in its preparation but, most importantly, reduces its potential impact.

Working in teams producing integrated programmes has provided both an opportunity to develop comprehensive solutions to identified problems and a challenge to established methods of work at UNIDO. Although teams work towards a common purpose under the guidance of a team leader, cross-organizational teamwork also places demands on the Directors of technical branches who have to ensure a balanced distribu-

tion of work. During implementation these same Directors are responsible for ensuring that the work undertaken by team members is in line with the service modules, approaches and methodologies—in short, the core competencies—of their branches.

All this illustrates the complexity of teamwork in a predominantly hierarchical organization. Nevertheless, much has been achieved within a short time since the integrated approach was introduced. Cross-divisional teamwork is now the working culture of UNIDO—a major change from before. It is reflected in the main thrust and content of all integrated programmes.

### **A final comment**

It would be wrong to leave the impression that UNIDO's transformation was a smooth, painless exercise. That it was not. At the beginning there was considerable 'text book' resistance from some management, staff and organizational units. Morale was low and went even lower in the early stages of the transformation process when emergency measures curtailing expenditures and travel were enacted. Staff, not unreasonably, wondered why official travel should be restricted when this was the main way of building up business. They could not easily see from their individual perspectives that expenditures had to be curtailed to send a clear signal that there was a new way of doing business, and that unjustified expenditures would not be tolerated.

There was resistance to working in teams or with other specializations. Generalists had initial difficulties in appreciating the concerns of specialists, and vice versa. Branch directors felt their importance and authority compromised by integrated programme teams and team leaders. Technical branches felt their critical mass seriously threatened when their lead specialists were continually called upon to take part in integrated programmes which necessitated frequent field trips. UNIDO's personnel services felt challenged by the requirement to evaluate and reward teamwork and to overhaul procedures. The continual work in retreats, working groups, seminars and other fora in the context of meetings of UNIDO's Board of Management also stretched resources; some claimed they were an obstacle to fast and effective programme implementation.

The emphasis on integrated programmes meant many smaller projects were discontinued, many of them 'pet projects' of individual branches and staff members. It also caused resentment from those whose projects could not fit into this new framework, and intensified competition to get into integrated programmes.

The priority given in the early stages of the transformation process to technical cooperation activities, and cuts in resource allocation to global forum activities such as research, also caused disquiet and dislocations. UNIDO is still struggling to find the optimal mix of technical cooperation and global forum activities and also to provide the appropriate focus for its overhauled research programme. 'Management was in continuous flux through trying to understand and respond to the new challenges of transformation.

Despite these difficulties, UNIDO, with clear direction and sustained commitment, came through its transformation process successfully. This is the major lesson for others: transformation can be achieved through effort and long-term commitment.

## Annex I

### A parallel case: the evolving role of UNCTAD

By Rubens Ricupero  
Secretary-General of UNCTAD

UNCTAD was established in 1964 as an organ of the General Assembly with a view to contributing to the economic growth of developing countries through international trade. To respond to this broad objective, the organization has constantly been required to adjust to new circumstances. Institutional reform and adaptation have thus been intrinsic to its evolution. The end of the Cold War, the fundamental changes in the global economy, and the rapid shifts in technology are all new challenges which call for further institutional adaptation.

UNCTAD was created in order to provide an alternative to the conventional wisdom—a wisdom which, at that time, was moulded largely by an international environment of which the Bretton Woods institutions and the GATT were the institutional pillars. Its inspiration was rooted in the development synergies that justice and efficiency can create: the conviction that only a radically changed system could open the way to development for all mankind. Development was deemed to be indispensable if the world was to succeed in closing the ever-widening gap between the contented affluent few and the miserable and destitute many, and in ensuring sustained growth throughout the world.

Change did indeed come about, although not at all in the manner originally envisaged. The change observed has escaped, to a large extent, from the control of Governments. Production and distribution today are the result of profound globalizing forces and are organized not according to a predetermined pattern to be outlined by Governments, but by the interplay of market forces at the planetary level.

### The ‘Aggiornamento’

UNCTAD has always tried to adapt to new circumstances and to give them a missing development flavour. UNCTAD purports to assist developing countries to adopt more efficient development policies by using international trade as a tool for integration, growth and development. The organization was itself one of the early examples of *aggiornamento* when, at UNCTAD VIII in Cartagena in 1992, it redesigned its role and machinery in order to improve its response to the requirements of the age.

Setting aside what had come to be regarded as a too rigid and, at times, confrontational group system of negotiation, UNCTAD shifted the accent to the need for partnership and cooperation for development. Partnership is advocated not so much on the basis of a conceptual platform—some blueprint or programme of action adopted by Governments to restructure economic relations—but rather in response to the exigencies imposed by a complex and emerging reality. At the same time, UNCTAD has not failed to stress that the persistence of extreme poverty and growing inequality, together with the proliferating risks of marginalization and environmental destruction, poses a threat to international economic stability and renders multilateral cooperation a *sine qua non* for meeting the challenge of globalization.

From Cartagena onwards, a shared perception of the nature of prevailing economic conditions has begun to assert itself. Several features of this perception are discernible:

- It attempts to grasp all the elements and complexities of development and to interweave them in a balanced and comprehensive tapestry.
- It recognizes the market and private initiative as dynamic agents of an expanding economy, without losing sight of the determining influence of good governance and an efficient State.
- It rightly lays stress on the ultimate responsibility of each country, and of each Government, to create the political and macroeconomic conditions for stability and progress.
- It attempts to enhance consensus among international partners.

The new approach has also continued to stress that the success or failure of domestic efforts often depends on the external economic environment. To succeed, such efforts require an international system capable of facilitating growth in a stable and sustainable way across the world. The external environment must thus provide countries with open and competitive access to the basic elements of sustainable development, i.e. markets, financing, investment, technology and technical assistance. These elements constitute the fundamental priorities of UNCTAD's work.

In response to these shifting realities, far-reaching institutional reforms, initiated by the secretariat, were agreed upon at UNCTAD IX, held in 1996 in Midrand, South Africa. Their implementation had the following practical consequences: 25 separate work programmes and sub-programmes were replaced by one programme consisting of five subprogrammes; the number of intergovernmental bodies was halved; the number of meetings was cut to a third of what it had been in 1992; the number of divisions in the secretariat was reduced from nine to five. The end result was a refined and more focused work programme, a streamlined intergovernmental machinery, a comprehensive restructuring of the secretariat, a leaner administrative and management structure, a lighter financial burden for the organization and an improved coordination with other organizations.

## **The new role**

The central objective of UNCTAD must be to help developing countries grasp fully the policy implications of the dynamic interplay of issues in the areas of money and finance, trade, investment and technological innovation. UNCTAD must also strive, in view of the interdependence of national economies, to redress the imbalances in global systems and to counter inappropriate development and economic policies.

By so doing, UNCTAD expects to help to ensure the overall coherence of the global system and to making it more conducive to the moral goals of fighting poverty, reducing inequality within and among nations, protecting the right of present and future generations to the preservation of the environment, integrating women on an equal basis and bringing the marginalized fully into the market economy.

At UNCTAD X, held in Bangkok in February 2000, I stressed that UNCTAD is an institution devoted to the generation and dissemination of action-oriented knowledge with the goal of steering processes of global change towards maximizing sustainable and equitable development. It does so through research and policy analysis, consensus building through intergovernmental deliberations and the provision of policy advice, and technical assistance aimed primarily at capacity building in areas such as commercial and investment diplomacy. In other words, UNCTAD's mission involves

producing ideas, fostering agreements and contributing to the implementation of those agreements and ideas in its three main core areas of work: the dynamics of globalization and interdependence, trade and investment.

Above all, however, UNCTAD will need to focus its work in the areas in which it can have most impact. UNCTAD does best what it was created for: to promote development through the right kind of integration of developing countries into the world economy and the trading system. Two qualifications are needed. The first is that the quality of integration is more important than its degree. The contemporary world provides examples of countries that suffer from too much dependence on external financial flows, or on a few commodities, or on too much foreign direct investment concentrated in an 'enclave'. What is needed, therefore, is an integration which would help countries to grow in a sustainable and equitable manner. The second qualification is that, although UNCTAD should concentrate more on the global systems than on their individual components, it should never lose sight of their intimate interrelationships. UNCTAD's focus should grasp the dynamic interplay between the external environment and national strategies, and how they are endlessly influencing and changing each other.

The main point is that the Manichean controversy about the relative importance of the external environment and of domestic strategies has been overtaken by events. In effect, one of the neatest definitions of globalization is that everything that is global has become relevant to the national or local level and, conversely, that everything local or national has relevance for the global system.

It is clear, therefore, that UNCTAD's task is not to tell developing countries that they should integrate themselves into the world economic system as fast as possible, regardless of the price or the consequences. They should instead, with UNCTAD's assistance, negotiate their entry into the system, trying, as far as realistically possible, but to the very extreme of that possibility, to make the system more responsive to their needs.

## **Creating synergies**

What is described above is certainly a very tall order for any single institution, let alone for one that is not exactly suffering from an embarrassment of riches. To succeed, UNCTAD will need to engage civil society and to draw on expertise to be found in non-governmental organizations, academia and the private business sector. It will also need to work closely with other organizations and entities within the United Nations system, and with regional organizations.

It is clear that UNCTAD cannot fully perform its developmental role in isolation. To begin with, its work takes place in the context of a constellation of development-oriented intergovernmental organizations and agencies, within and outside the United Nations system, whose activities touch on areas of concern to UNCTAD. Collaborating and complementing efforts, dividing up labour in the most efficient manner and avoiding unnecessary duplication are prerequisites for the effective delivery of UNCTAD's development work.

The UNCTAD secretariat has developed a large number of links with development-oriented international organizations. In terms of format, they range from working-level operational links to memorandums of understanding and other formal agreements; in terms of substance, from simple exchanges of information and documentation to joint projects.

UNCTAD cannot duplicate the work of organizations that, like UNDP, have a strong field presence and are oriented towards countries, not the global system. This is why, with UNDP, in 1998 we started a project on globalization, liberalization and sustainable human development to test on the ground the links between policy advice and global analysis and research.

The Joint Integrated Programme of Technical Assistance for Selected Least Developed and other African Countries (JITAP) is a good example of innovative partnerships. JITAP is a technical assistance programme linking the three major Geneva-based organizations concerned with international trade: UNCTAD, ITC and the WTO. It initially embraced eight African countries, namely four LDCs—Benin, Burkina Faso, Uganda and the United Republic of Tanzania—and Côte d'Ivoire, Ghana, Kenya and Tunisia. Based on country-level needs assessment and extensive consultations, the programme aims to: build national capacity to understand the WTO agreements and their implications for the country; help ensure that the policy and regulatory framework conforms with the agreements; and enhance the country's ability to take advantage of the agreements through improved export readiness.

A critical issue is to define relationships with other organizations, both intergovernmental and non-governmental, that take full account of comparative advantages, maximize synergies, and avoid unnecessary duplication. Relevant in this respect is the memorandum of understanding signed with UNIDO, which focuses on the competencies of the two organizations in the field of investment and enterprise development and on how to put these competencies to the benefit of developing countries. These and similar efforts will be pursued further on the basis of the priorities and core areas defined at UNCTAD X.

The joining of efforts, however, must go further. Experience has shown that non-governmental groups can enrich public discussion, as they did at UNCTAD X. Non-governmental groups bring forward voices that might not otherwise be heard, and improve on the effectiveness and relevance of development activities in the field. The importance of the private business sector in international development cooperation is self-evident in a context of globalization. The development of creative and innovative partnerships with these non-governmental actors is a new challenge before us which will not fail to have new and salutary implications for the manner in which international organizations carry out and deliver their mandates.

## *Annex II*

### **UNIDO after the transformation: relevance and challenges**

*By Professor J. D.-Martinussen*

Since UNIDO was established, conditions for industrial development have changed considerably in at least three respects. First, diversity has increased among recipient countries. Some countries have achieved a high level of internationally competitive industrialization; others have managed to achieve some industrial development mainly based on import substitution; while the large majority of poor and small countries have seen only very limited progress. Countries with economies in transition have added to the diversity with their special problems.

Second, the role of the State has changed in most countries. The changes have been particularly significant in the countries with economies in transition from centrally planned to market-led development. But the role of the State has also been reduced in the large majority of developing countries—partly based on recognition of the poor results achieved with state-led development in the past, partly in response to pressure from the IMF, the World Bank and leading donor Governments.

Third, cross-border economic transactions have increased in scope and intensity in such areas as trade, investment and financial flows. The same applies to services, technology transfer, and exchange of information and ideas. These tendencies are often referred to as globalization, but the patterns emerging should rather be characterized as a complex combination of globalization, regionalization and marginalization.

The changes in global and regional conditions for industrial development have added to diversification rather than reduced it. The 'rules of the game' have become more global and uniform, particularly with the application of common strategies among international financial institutions and major donors (the Washington consensus in its original and revised forms), the establishment of the WTO, and the increasing transnationalization of private capital. In terms of outcome, however, benefits from increasing flows of capital and technology have accrued to only a small number of countries. The same applies to the benefits from increasing international trade. The so-called globalization of industrial and technological development has resulted in little or no progress for the overwhelming majority of both developing and transition economies. Rather, they have experienced the changes as marginalization both in the sense that they have been bypassed, because they are unattractive to private capital, and in the sense that their weakly developed industries are facing fiercer competition in foreign as well as domestic markets.

### **UNIDO's reassessed role**

As a reaction to the changes outlined some of the major donors in the mid-1990s came to the conclusion that a specialized UN agency in the field of industrial development was no longer required. UNIDO had become redundant. This was not the conclusion we arrived at in the assessment of UNIDO, commissioned by the Danish development agency (Danida) in 1997. Instead, we found that both the needs and the articulated demands for UNIDO's services had increased in the 1990s, and they have continued to increase since then.



In this context it should be borne in mind that industrial development remains a precondition for long-term sustainable economic growth and social advancement. Industry plays a pivotal role in encouraging technological development; increasing productivity; promoting entrepreneurship; generating employment and income; and in creating sectoral linkages, including linkages with agriculture and the service sector. In relation to the global economy, manufacturing activity and a continuing rise in manufacturing productivity play critical roles by ensuring export earnings. It should be acknowledged that the needs and demands for UNIDO's services have decreased in some recipient countries. But few countries with developing or transition economies have attained a level and pattern of industrial development where they can manage without having access to international assistance, including the types of services and forum facilities offered by UNIDO.

The needs have changed considerably over the last decade. The increased reliance, worldwide, on the private sector—and the associated deregulation and liberalization of trade and investment—all imply needs for services and assistance different from those prevailing where and when industrial development was led by the State. But the point is that the needs for technical cooperation and services on a non-commercial basis, although altered, have not decreased in the large majority of UNIDO's member countries. The role of the State may have changed from that of a regulator to that of a promoter and facilitator, but industrial growth and efficient functioning of the market still require policies and institutional frameworks that only the State can provide. Consequently, there continues to be great need for international assistance to strengthening the governmental system, partly with a further view to building up an enabling institutional and organizational framework for private sector growth, but also more generally with a view to enhancing national capacities for shaping industrial development. International pressure for industrial and technological restructuring in accordance with emerging standards for environment protection and pollution control add to the needs for international cooperation and services. The growing significance of quality as a determinant of international competitiveness further reinforces these needs, particularly in areas such as international standard setting and institutional capacity building for quality control.

UNIDO does not have the capability—and is not likely to develop the capability—to become the international lead agency in providing technical assistance. But the organization can contribute in several areas, where supply of services are too expensive or falls far too short of needs and demand. Besides, UNIDO is widely recognized as a neutral and impartial provider of advice and services and as an organization with no commercial or specific interests of its own. Further, UNIDO continues to have a comparative strength as a global forum for documenting industrial development and setting standards.

## **The transformation**

Meanwhile, considering the major changes referred to above, and also considering the shrinking support for the organization from many donors, UNIDO has had to transform itself to become more relevant and more effective. This is exactly what UNIDO has done in recent years. The services offered by the organization have been more clearly defined and focused, based on an assessment of its comparative strengths. Services are now categorized into 16 modules which can be combined in integrated programmes adapted to the diversity of needs and requirements of the recipient countries. The administrative structure and the procedures have been streamlined. A

particularly important change is the use of teams to prepare the integrated programmes. These teams are composed of members from the relevant branches of UNIDO, even sometimes cutting across the two technical divisions of the organization.

In response to the increasing emphasis on the private sector, UNIDO has adjusted its strategies and search for partners. In this context, however, a strong focus has been retained on industrial policies and the institutional prerequisites for industrial development. This is fully justified as argued above. There is little doubt that the vast majority of developing and transition countries can improve their economic performance by relying more on market mechanisms, but there is also little doubt that the best results are achieved where appropriate policies and institutions are developed to complement the market. This is important for industrial growth in general. It is important for promoting entrepreneurship, technological development, international competitiveness, and employment. It is particularly important for promoting cleaner production and introducing other environmental concerns and social considerations into the shaping of industrial development. Acknowledgement of the role of Governments and various public and mediating institutions is properly reflected in UNIDO's present priorities and service modules.

## The challenges ahead

It follows by implication from the above observations that UNIDO has managed to transform itself to become more relevant and more effective. At the same time, however, the organization faces several serious challenges and dilemmas which need to be resolved before UNIDO can play a more important role.

The 'Business Plan on the Future Role and Functions of UNIDO', adopted in 1997, stipulated a concentration of activities on African and other least industrialized countries. This was to some extent justifiable on the basis of a needs assessment and considering the limited resources at UNIDO's disposal. But it raises some difficult questions. How can UNIDO retain its universal mandate with a concentration on selected member countries? How can the organization retain its relevance to other member countries? These issues have not been resolved at the policy level, but it seems that UNIDO is coping with the inherent contradictions by taking a proactive role in some of the least industrialized countries and at the same time responding to specific requests from other member countries. The act of balancing, however, is difficult because there are no operational criteria for selecting and de-selecting among the several requests received as long as they fall under the areas covered by the 16 service modules. In practice, the process of prioritization is heavily influenced by the availability of funding, whether from donors or—in the form of cost sharing or full payment of services—from middle-income recipient countries.

The focusing on least industrialized countries poses another challenge: How can UNIDO achieve stronger and more visible impact, as demanded by major donors, when dealing mainly with 'most difficult cases'? As with other types of aid, impact is easier to bring about where the basic preconditions for development are in place. When this is not the case, the difficulties should be openly acknowledged and, moreover, the required funding for comprehensive programmes of assistance should be made available by the donors, especially by those who demand stronger and more visible impact.

Availability of funding interferes with UNIDO's actual priorities in other ways. According to the Business Plan, UNIDO must give emphasis to delivering integrated packages of services. In keeping with this stipulation more than 30 integrated programmes have been prepared. The major difficulty here is that the donors, with very few exceptions, have refused to fund programmes as

a whole. Instead, they have selected for funding only particular components in keeping with their own priorities. This has left UNIDO with several programmes where the composition of the components do not reflect the composite needs for support in the recipient countries, and where the complementarity aimed at in the original integrated programmes may be lost. This has prompted some donors to argue that UNIDO is preparing too many programmes. While this may be true from other perspectives, the core issue here is really why so few donors have adapted their financial support to the new modes of operating which they themselves have demanded from UNIDO.

In a longer term perspective, what is required is a different approach in donor funding. Rather than earmarking their funding for particular components, donors should allow UNIDO to pool resources to finance the integrated programmes as a whole in conjunction with recipient Governments. Moreover, donors should commit funding for the whole duration of the integrated programmes.

In a short term perspective, recipient countries may benefit from the programming undertaken by UNIDO even when funding is not made available for all components and when the organization is not the implementing agency for the whole programme. This can be achieved if the integrated programmes are prepared with a view also to providing a basis for future fund raising by the recipient Governments themselves as has happened in some cases. The basic idea is that UNIDO should not only include components that are anticipated to attract funding immediately but rather try to cover all the areas deemed necessary to deal with based on a technical assessment of needs. Such programmes may provide a framework for attracting and integrating assistance from other multilateral as well as bilateral donors. This may be helpful particularly for the least industrialized countries who face obstacles for industrial development at both the policy level, the institutional level, and the sectoral level. But the integrated programmes may also, more generally, place UNIDO in a better position within the UNDAF mechanisms and help in creating more attention to industrial development within the Comprehensive Development Framework proposed by the World Bank. Essentially, what is proposed is that UNIDO more systematically explore the possibilities for playing two roles: that of preparing and implementing programmes, and that of preparing programmes to assist recipient Governments in their efforts to mobilize funds and coordinate and integrate support for industrial development provided by other agencies.

Yet another area where availability of funding, rather than policies and needs, shape UNIDO's mode of functioning relates to the global forum role and normative functions. Several donors, particularly the Nordic countries, have requested UNIDO to give more emphasis to these areas. They comprise UNIDO's involvement in producing industrial statistics; in exchanging experience from promoting sustainable industrialization through innovative approaches; in provision of services in relation to international conventions, norms and standards; and in establishing international networks and partnerships that can stimulate economic cooperation among developing countries at different levels of industrialization. With the very considerable budget cuts in the 1990s UNIDO's roles in these 'upstream' activities and in combining the (fragmented) operational activities with the normative and global forum functions have been endangered. Although the Business Plan re-emphasized these roles, lack of funding has actually forced the organization to reduce its activities in some of the areas referred to, especially in research and evaluation. It is important that UNIDO's capacity is enhanced for providing global public goods such as those referred to above. No other organization has a specific mandate for doing so in relation to sustainable industrial development in the non-OECD countries. At the same time, there is a need for strengthening the organization's capacity for combining the experience from technical cooperation at country and regional levels with global forum and normative activities such as disseminating knowledge about and setting standards for best practices. No other (non-commercial) organization has the same potential for extracting and documenting lessons learnt from industry-related operational activities in developing and transition countries.

In order for UNIDO to better address the diversified needs and demands at regional and country levels the Business Plan called for a more decentralized approach. It is not quite clear, however, how this can be achieved with the present level of funding and staffing. The number of specialists available in most areas is far too limited to permit deployment of technical staff to regional, let alone national level. Some of the highly specialized technical skills are not tied to specific conditions in various regions and countries, and therefore the experts concerned should continue to be recruited from headquarters. But with the increasing emphasis on policy advice and institutional strengthening, effective programming and service delivery depend critically on regional and country-level knowledge. External consultants can play a major role here, but there is little doubt that strengthened field offices can add to the relevance and quality of UNIDO's services and help making these services more complementary to those provided by other agencies. Again the main obstacle is lack of funding due to budget cuts and late or non-payment of assessed contributions. That is the major reason why the organization has been unable to move much forward with decentralization since 1997.

UNIDO plays important roles by providing global public goods and by directly supporting sustainable industrial development in many countries. The organization can continue to play a role with the present level of funding and staffing. It can enhance impact by working more together with other agencies and by building on its expertise and particular strengths. But the organization cannot play the role envisaged by its member organizations in the Business Plan with the resources presently available, as argued in the previous paragraphs. This implies opportunities foregone. More important, perhaps, is the danger of UNIDO losing credibility and legitimacy among recipient countries who expected more benefits from the donor-driven transformation of the organization.

In broad terms, the leading donors demanded that UNIDO become more relevant, more focused and more effective. The organization was transformed accordingly in close cooperation with both donors and recipients. A compromise was reached at the policy level with the Business Plan. The 'new' UNIDO, under the present leadership, has come far in adapting its structure and mode of operating to the priorities embodied in the Plan. But very few donors have responded by increasing their voluntary contributions or adjusted their mode of financing to the new set-up and procedures for service delivery at country, regional and global levels. Several member countries have continued with the bad habit of delaying their payment of assessed contributions and some have build up considerable arrears. These are not the most appropriate signals for donors or recipient countries to send to a UN organization that has seriously tried to come to terms with both donor demands and changing conditions for industrial development. They are also not the best signals to send to the UN system as whole. What is called for, in particular, is more consistency in donors' policy-making and funding that can more effectively promote UN reform by rewarding reform initiatives where the commitment is strong and where progress is achieved.

## Chapter 7

# Conclusions

We have come to the end of a journey that took us from a review and assessment of the many proposals for reform of the UN system as they relate to the changing international setting, to UNIDO's unique need-driven reform and transformation process.

Successful reform within the multilateral system is made difficult by the wide range of political, managerial and financial conditions that have to be met, in addition to the necessary correspondence with changes in the global economic, social and institutional scenario.

With the case of UNIDO, we have intended to provide a well-documented illustration of what it takes for reform to succeed, and hope that this will assist in the efforts underway for broader reform within the UN system. In fact, we see UNIDO's transformation as a milestone for the renewal and revitalization of the UN system as a whole.

In the foreword to this book, Secretary Short calls the UN "the only genuinely global institution". The UN can only justify its special moral authority as such if it addresses the need of the destitute effectively, efficiently and sustainably.

To be able to perform as required, with economy of means, responsiveness and discernible impact, the UN system and its agencies need, first, to muster state-of-the-art skills, capabilities and organizational competencies to serve urgent social priorities by means of well-defined, opportunely rendered and competently performed specialized services. They also need to work within a consistent framework, a Development Agenda, which soundly articulates the role of the various specialized institutions concerned with development, and addresses the challenges and opportunities facing developing and transition economies in a world economy hallmarked by rapid technological change, fading barriers to cross-border economic integration and new global institutions. The UN Secretary-General's Millennium Declaration is a landmark on this path.

### **Limits to reform**

We have learnt from the experience of reform in the UN and in UNIDO that, over time, tensions tend to develop when governing structures focus on steering normative functions, while, at the same time, operational functions tend to grow beyond those originally

envisaged. In the last resort, such tensions arise because the universality, equity and transparency requirements of norm-making are somehow at odds with the principles guiding efficient execution. More specifically, government structures apt for guiding and managing normative functions have attributes that differ from those required to lead and conduct implementation functions.

Improvements in management efficiency can only partially address gaps between the purview of governing bodies and the requirements for implementation. A different, although closely related kind of gap arises when the actual evolution of operational functions driven by the needs of member States clashes with the limits defined by the scope of governing bodies and management.

These gaps can only be partially addressed by improvements in management efficiency. At some point, the onset of a transformation process aimed at redressing the balance becomes inescapable.

The experience of reform in the UN suggests that addressing the mismatch between original design and evolving performance by means of incremental changes aimed at improved efficiency and focus is relevant, necessary and important. But it is not enough. Adaptation to a changing setting is at least as, and perhaps even more, important as internal restructuring; concentrating on the latter yields decreasing returns.

Reform, in and of itself, neither necessarily addresses the problem of lack of relevance nor confers legitimacy. How can a genuine transformation, that is, one that addresses both the need for adaptation to a changed environment as well as that for management efficiency, be triggered? Our experience suggests that this can hardly be accomplished when change is sought within the confines of governing bodies along the lines of traditional political and geographical divides. It needs to be driven by a coalition of reforming member States that cuts across such divides while representing the views of both donor and recipient countries and proceeding by consensus.

## **Changing setting for development**

In a world where the pursuit of social equity and equality of opportunity is to continue being sought, the need for global public goods is enhanced, rather than diminished, by the global spread of technological change, economic globalization and trade liberalization. Market forces, along with national Governments and bilateral assistance, play a key role. But this does not suffice.

The emerging rule-based international system has been designed with a view to smoothing globalization rather than enabling developing countries to draw on it. This confronts the international community with the fundamental need to properly address the implications of the current international system for development, including those relating to regulating the 'global negatives' as G. H. Brundtland, WHO's Director-General, has called the social and environmental ills of the age of globalization.

It is not clear at all, and can by no means be taken for granted, that the drastic changes experienced by the world in recent years, with increasingly market-driven international trade, investment and technology flows, guarantee development and address the

hindrances of globalization. On the contrary, there are enough reasons for concern that, without international action, increasing inequality of incomes, poverty and environmental degradation may continue growing at an alarming rate, let alone being checked.

Market forces alone are unlikely to reverse inequities. Concerted action is needed to assist those threatened with exclusion, not just by means of poverty-alleviation programmes but, particularly, by helping them to master the ingredients of wealth creation and productivity growth, that is, the skills, capabilities and institutions that enable putting new technologies at the service of development.

We examine various national strategies to address these issues in historical context. But circumstances are changing and conditions are becoming increasingly harder, particularly for the least developed countries.

### **Learning from UNIDO's trajectory**

The historical review of UNIDO's origin and initial stages of development bring us back to the previous discussion on normative versus operational functions. The relationships between both informed the debate on UNIDO from its early start, when it was recognized that the industrialization of developing countries had to be addressed by the multilateral system.

UNIDO faced from its very inception the constraints stemming from an uneasy balance of forces in the multilateral system between North and South. An example is the fact that technical cooperation activities had to be financed outside the budget, mainly by UNDP. As the central funding role of UNDP gradually deteriorated, UNIDO, faced with growing demand for its services, had to rely increasingly on voluntary contributions.

When UNIDO became a specialized agency in 1986, it did so with the principal objective of promoting and accelerating industrial development in developing countries. This was the result of a compromise, which did away with the idea of making UNIDO a financial organization. Indeed, even so, some developed countries remained unconvinced of the rationale of committing resources to fund a specialized agency for industrial development, which might compete with, rather than assist, the private sector.

UNIDO thus had to fight financial crises from its very inception. Its increasing reliance on voluntary contributions led to a decline in the importance of its global forum/normative work. These conditions led to the first attempt at major reform at the Fifth General Conference (1993). The conclusion was reached that the technical cooperation programme had to be refocused, away from support to governmental institutions and state-owned enterprises towards rendering advisory services to the private sector (SMEs in particular). The range of fields of assistance had to be narrowed down, focusing on core capabilities and on environmentally sustainable and equitable industrial development through investment promotion, technology transfer, human resource development and creation of an enabling environment. Major steps were taken to save resources, increase operational efficiency, gain focus and increase relevance. These steps were followed by two further restructurings, in 1994 and 1996, for additional cost-cutting and improved coordination.

And yet, all this did not suffice to get out of trouble. The spectre of the uneasy original compromise that gave rise to the creation of UNIDO returned with a vengeance, leading to a major crisis in 1997. A great deal of the quest for achieving change and turning concepts into practice while breaking bureaucratic inertia, allaying paralysis and demonstrating efficiency both at headquarters and in the field, still lay ahead.

## **Onset of the Business Plan**

Member States remained unconvinced that the reforms had gone far enough. The withdrawal of the US in 1995 'for budgetary reasons' was a further, critical blow and clearly threatened the survival of the organization, particularly since other countries threatened to follow suit. All this in an international environment that had become adverse to the cause of international cooperation, particularly in promoting industrial development.

However, this major challenge, rather than leading to discouragement, prompted a renewed search for a positive outcome driven by a select group of member States. This gave rise to the birth of the so-called 'Business Plan', which recognized the 1997 Danish *Assessment of UNIDO* as its most immediate precedent.

In a thorough evaluation, the Danish report arrived at the conclusion that UNIDO was indeed relevant and its services were in high demand, although it did need to be streamlined further. The Danish Assessment, backed by a generous voluntary contribution to UNIDO, led other donor countries to seriously assess their own perspective and thus created the conditions for the onset of the Business Plan as a way to make the organization truly responsive to the new global realities and the needs of the developing countries.

As mentioned at the very beginning of this concluding chapter, the Business Plan came out of a very unique set of circumstances, whereby a group of reforming countries, cutting across conventional political and regional boundaries, led a process of reassessment of the role of the organization in light of the new international setting.

The key contribution of the Business Plan was that it provided unambiguous guidance by identifying clear comparative advantages for UNIDO while avoiding duplication with other multilateral and bilateral technical assistance institutions. Other key attributes of the Business Plan include its emphasis on the commitment, geographical balance and consensus orientation of the reforming member States involved as well as the flexibility, need-orientation, competence and outcome specificity and time-boundness of the reform process. Still, the key actors themselves recognized that the guidelines of the Business Plan were not cast in stone, and that its follow-up was not exempted of downside risks, such as the lack of adequate funding.

## **Transforming UNIDO**

Although the Business Plan laid the foundations for the recovery of UNIDO's legitimacy and political support, particularly from major donor countries, the agency could only be genuinely revitalized only through a true transformation which, in turn, would lead to the



expansion and consolidation of such support. The Business Plan provided only general guidance. It had to be translated into action.

Such translation emphasized the need for a clear sense of the future of industry, a systemic approach, a new culture of teamwork and doing away with internal and external overlaps and duplication of activities. This took place in two highly interdependent phases: financial, personnel, administrative and structural changes, on the one hand, and programming changes, on the other, in the context of an unwavering concern for the social, economic and environmental facets of industrial development.

*Internal management transformation entailed the adoption of openness to dialogue, transparency of information, access across hierarchies, simplicity of procedures, delegation of authority, shared purpose, collective responsibility and continuous improvement and skill-building as guiding principles in Headquarters, and those of decentralization of functions, customer-driven and system coordination in field operations.*

Programming transformation entailed fully reaping the advantages of cross-disciplinary synergies, specialization, need- and impact-orientation and efficiency gains. In order to ensure such results, changes included major innovations in the areas of product design, process improvement, production retooling, design and implementation of procedures and performance measurement. The establishment of service modules and integrated programmes as organizational devices are two key examples of such innovations.

## **Litmus test**

Successful reform entails meeting two essential preconditions. The first is having leading countries from North and South coalesce to catalyse concrete new initiatives. The current efforts at breaking the longstanding deadlock over the US contribution to the UN are a good example. Which leads us to the second precondition, i.e., the need to back intentions with financially enabling deeds.

For the first time in history, humankind possesses the financial and technical means required to defeat poverty on a global scale. But global prosperity does not suffice. Although a good deal of the developing world displays pockets of development that may eventually pull forward the rest of society, this is not the case when we look at Sub-Saharan Africa and least developed countries elsewhere.

In the last instance, the litmus test for reform of the UN system and its specialized agencies consists in fulfilling the hopes brought about by the end of the Cold War for a new beginning with regard to its normative functions, and for effectively addressing the UN's developmental role in light of new realities such as the aggravation of poverty and marginalization, the emerging digital divide and the skewed playing field in trade negotiations. The implementation of the Secretary-General's Millennium Declaration is a decisive step in the right direction.

## *Annex*

# **The structure of the UN system**

*'I would we were all of one mind, and one mind good.'*

Shakespeare, *Cymbeline* v. iv. 205

The founders of the United Nations showed great foresight in their determination to establish an international organization for shaping a new and better world. The United Nations was conceived in the wake of the turmoil and tragedy of the Second World War and was born out of the determination to create a new world in an endeavour 'to save succeeding generations from the scourge of war'. It came into existence on 24 October 1945 when the United Nations Charter had been ratified by China, France, the Soviet Union, the United Kingdom, the United States and a majority of other signatories, comprising altogether 51 States.

The United Nations originally consisted of the United Nations Organization (UNO) and a number of legally autonomous special bodies, all of which—the signatories hoped—would work in harmony and cooperation. More than half a century later, the UN system remains the principal global institutional mechanism for international peace and security. It is also the principal global institution for mobilizing global cooperation in pursuit of economic and social development, human rights, and justice.

The constitutional set-up of the UN system provides for a coordinated system based on a holistic approach. This approach encompasses both specialized functions, such as sectoral specialization, and overarching functions, such as poverty alleviation, carried out by organizational bodies within the system.

This annex examines the institutions and coordinating mechanisms that serve the UN's economic and social development functions, both normative and operational, and how they fit into the UN system as a whole. The annex provides the background essential to an understanding of the UN reform agenda in the area of development.

## **The UN Charter**

The Charter—the constitution of the Organization—stipulates the rights and obligations of Member States and establishes the organs and procedures of the Organization. The

Charter is in itself an international treaty, which codifies the major principles of international relations. The preamble to the Charter states,

'WE THE PEOPLES OF THE UNITED NATIONS DETERMINED [...] to promote social progress and better standards of life in larger freedom, [...] AND FOR THESE ENDS [...] to employ international machinery for the promotion of the economic and social advancement of all peoples, HAVE RESOLVED TO COMBINE OUR EFFORTS TO ACCOMPLISH THESE AIMS'.

The Charter declares that the purposes of the United Nations are: to maintain international peace and security; to develop friendly relations among nations based on respect for the principle of equal rights and self-determination of peoples; to achieve international cooperation in solving international problems of an economic, social, cultural or humanitarian character and in promoting human rights and fundamental freedom; and to be a centre for harmonizing the action of nations in the attainment of these common ends.

Initially, the United Nations was generally perceived to be better equipped for normative than for operational activities for development because of the universal and equal participation among Member States.<sup>123</sup> However, it should be emphasized that in 1945 many of the current areas of activity were not yet part of the international agenda, for example environmental problems, questions related to population, anti-drugs campaigns and the fight against international crime. Even the development functions are only briefly mentioned in the Charter.

Membership in the United Nations is open to all peace-loving States which accept the obligations contained in the Charter. The admission of new members is effected by a decision of the General Assembly—the main deliberative organ of the UN composed of all Members, each with one vote—upon the recommendation of the Security Council.

Since the UN was founded, the number of Member States has almost quadrupled from the original 51 members to some 188 in 2000. The rapid increase in membership is a consequence of the decolonization process of the 1950s and 1960s and the emergence in the 1990s following the end of the Cold War of new countries with economies in transition. As a result, there has been an increase of the representation of the world's people in the United Nations from 70 per cent in 1945 to almost 100 per cent in 2000. At the same time, it is fair to say, wider and more diverse membership has led to more difficult and protracted negotiations on difficult issues and slowed and complicated decision making in the face of new and often strident political and development agendas.

Amendments to the Charter, which are important for the UN reform process, are binding on all Members. They have to be agreed by two-thirds of the members of the

<sup>123</sup>Normative functions are defined as: (i) **agenda setting** for the attention of policy-making organs based on the demands of various development actors; (ii) **promoting understanding** through international and national fora and providing analytical foundations for related debate; (iii) **norm setting** through international fora of negotiations, providing analytical inputs for such negotiations and serving as an honest broker; (iv) **monitoring** of implementation of agreed norms by national Governments; (v) **policy advice** in the form of elaborating normative principles for translation into action at the national level. Policy advice is considered to be both a normative and an operational function, and as the last in a series of the former and the first of a sequence of the latter. For a more detailed elaboration of the UN's normative functions see Bergesen and Lunde (1999), pp. 3–9.

General Assembly, and ratified in accordance with the constitutional processes of Member States, again by two-thirds of the Members of the United Nations. These must include the five permanent members of the Security Council (Article 108), each of whom thus has the power to veto amendments. Therefore a change in the Charter of the UN is politically a difficult process which, unsurprisingly, has seldom occurred. Indeed, it has only been modified once to increase the number of non-permanent members of the Security Council and twice to increase the number of members of ECOSOC. (These institutions are described below.) The difficulties in amending the charter have been seen as an obstacle to more radical and widespread reform of the UN.

The Charter established six principal organs of the United Nations System: the General Assembly, the Security Council, the Economic and Social Council (ECOSOC), the Trusteeship Council, the International Court of Justice and the Secretariat. Because of the linkages between security, conflict, poverty and development, a close relationship was envisaged among the first four of these organs in the constitutional set-up of the UN system.

## **The General Assembly**

The General Assembly is the main deliberative organ of the UN. It comprises all Member States, each having one vote, unlike the Bretton Woods Institutions with their weighted voting system. Decisions on major issues, such as peace, security and admission of new Members, and on budgetary matters, require a two-thirds majority, while decisions on other issues are made by simple majority. Thus the few countries that contribute substantially to the budget have no more influence over its use than the many that contribute less, some as little as 0.01 per cent. Before 1989, the large contributors were often outvoted on budgetary issues. In that year, the budget procedures were modified so that large contributors could no longer be outvoted.

Under the Charter, the major functions and powers of the General Assembly (of relevance to this book) are:

- To initiate studies and make recommendations for the purpose of promoting international cooperation in the economic, social, cultural, educational and health fields.
- To receive and consider reports from other organs of the United Nations.
- To consider and approve the budget of the Organization.
- To consider and approve any financial and budgetary arrangements with the specialized agencies referred to in Article 57, and to examine the administrative budgets of such specialized agencies with a view to making recommendations to the agencies concerned.

The Charter formally established an institutional mechanism for the coordination of the budget within the UN system, including all specialized agencies 'brought into agreement with' the United Nations. Despite this, there is no consolidated budget for the UN system as a whole. Some believe that this lack has hindered attempts to improve coherence in the system.

## **THE SIX MAIN COMMITTEES OF THE GENERAL ASSEMBLY**

The deliberations of the Assembly are concentrated in six main committees, of which the following are relevant to our subject: the Economic and Financial Committee (Second Committee); the Social, Humanitarian and Cultural Committee (Third Committee) and the Administrative and Budgetary Committee (Sixth Committee). See appendix II.

While the decisions of the General Assembly are not legally binding for Governments, they do exert a moral authority and influence public opinion on international issues.

### **The Security Council**

Under the Charter, the Security Council has primary responsibility for the maintenance of international peace and security. It also has the function of recommending the admission of new Members and, more importantly, recommending to the General Assembly the appointment of the Secretary-General. The Council comprises 15 members, of which five—China, France, the Russian Federation,<sup>124</sup> the United Kingdom and the United States—are permanent, and ten are elected by the General Assembly for a period of two years.

Each member of the Council has one vote, and decisions on procedural matters are made by an affirmative vote of nine members, including the concurrent votes of all five permanent members. This means that any of the five can veto a decision by voting against it. Abstention by a permanent member, or non-participation in a vote, no longer reduces the UN's ability to pass resolutions.

Under the Charter, members of the United Nations agree to carry out the decisions of the Security Council. The Council is thus the only organ of the United Nations that has the power to take decisions which Member States are obliged to carry out. However, a lack of enforcement mechanisms has weakened the implementation of its decisions.

### **The Economic and Social Council (ECOSOC)**

The ECOSOC acts under the 'authority' of the General Assembly (Article 60) and is, in accordance with the Charter, the principal organ responsible for the coordination of the economic and social activities of the United Nations and the specialized agencies and institutions of the UN family as a whole. ECOSOC originally consisted of 18 members, but was subsequently expanded to 27 and then 54 members, who are elected for a three-year term. The optimal size of ECOSOC is one of the main issues of contention in the UN reform process. The issue is closely related to the effectiveness of the decision-making process, which requires a simple majority with each member having one vote.

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<sup>124</sup>A successor of the Soviet Union.

The major functions of ECOSOC are:

- To serve as a central forum for discussion of international economic and social issues of a global or inter-disciplinary nature, and for the formulation of policy recommendations on these issues addressed to Member States and to the United Nations system.
- To initiate studies and reports, with respect to international economic, social, cultural, educational, health and related matters, and to make recommendations on these matters to the General Assembly and to Members of the United Nations.
- To call international conferences and prepare draft conventions on matters falling within its competence.
- To enter into agreement with specialized agencies (see Article 57 on page 156) defining their relationship with the United Nations.
- To coordinate the activities of the specialized agencies through consultations with and recommendations to such agencies, and through recommendations to the General Assembly and Members of the United Nations.
- To obtain reports from the specialized agencies on the measures they have taken to effect its own recommendations on matters falling within its competence.
- To perform services, with the approval of the General Assembly, for Members of the United Nations and, on request, for the specialized agencies.
- To make suitable arrangements for consultation with non-governmental organizations on matters falling within its competence.

These functions may be interpreted as formally defining a major normative role for ECOSOC and, through relations with the specialized agencies, for the UN system as a whole.

ECOSOC holds one substantive five-week session each year, which includes a special meeting attended by Ministers and other high-level officials to discuss major economic and social issues. ECOSOC may make arrangements for representatives of specialized agencies to participate, without vote, in its deliberations and in those of its commissions, and for its own representatives to participate in the deliberations of the specialized agencies.

In the course of time the number of subsidiary and related bodies of ECOSOC has increased and now comprises nine functional commissions, five regional commissions, a number of sessional and standing committees as well as expert and related bodies reporting to these commissions, fourteen specialized agencies, including the World Bank Group comprising four additional organizations, nine programmes and funds with three additional subsidiary programmes under UNCTAD and UNDP, five research and training institutes and four other UN entities (see appendix II). Yet, almost every UN reform proposal has recommended changing or strengthening the coordinating functions of ECOSOC. Indeed, some critics have alleged that ECOSOC has duplicated or overlapped

with some of the other main committees of the General Assembly, particularly the Second Committee which deals with economic and financial issues. It has also been alleged that ECOSOC's task of 'initiating studies and reports with respect to international economic, social, cultural, educational, health and related matters' overlaps with the work of the United Nations Conference on Trade and Development (UNCTAD).<sup>125</sup>

## **The United Nations System**

The founding fathers of the United Nations expressly created a decentralized system rather than a pyramid system with a command headquarters able to issue guidelines for the other organizations. The individual organizations of the UN are all international organizations, and are thus subject to international law. They are intergovernmental organizations which are represented by their Governments. There is thus no federation of States, no unification of States ('We the peoples ...' in the preamble to the UN Charter is misleading, to say the least). International organizations are not players who can act autonomously. Their actions are limited to what accords with the political wishes of the Member States (in reality the Governments of the States with the most influence and power) and to what is approved of by these States. In view of the considerable differences in political power between the Member States, the United Nations is a democratic body only in a very limited sense. Even membership in the UN for a particular country depends on that country having a democratic regime.

The work of the United Nations system, which derives mainly from majority decisions (Resolutions) of member countries made in the General Assembly, is carried out by:

- The Secretariat and subsidiary organs.
- Committees and bodies established by the General Assembly to examine and report on specific issues.
- International conferences, called for by the General Assembly.

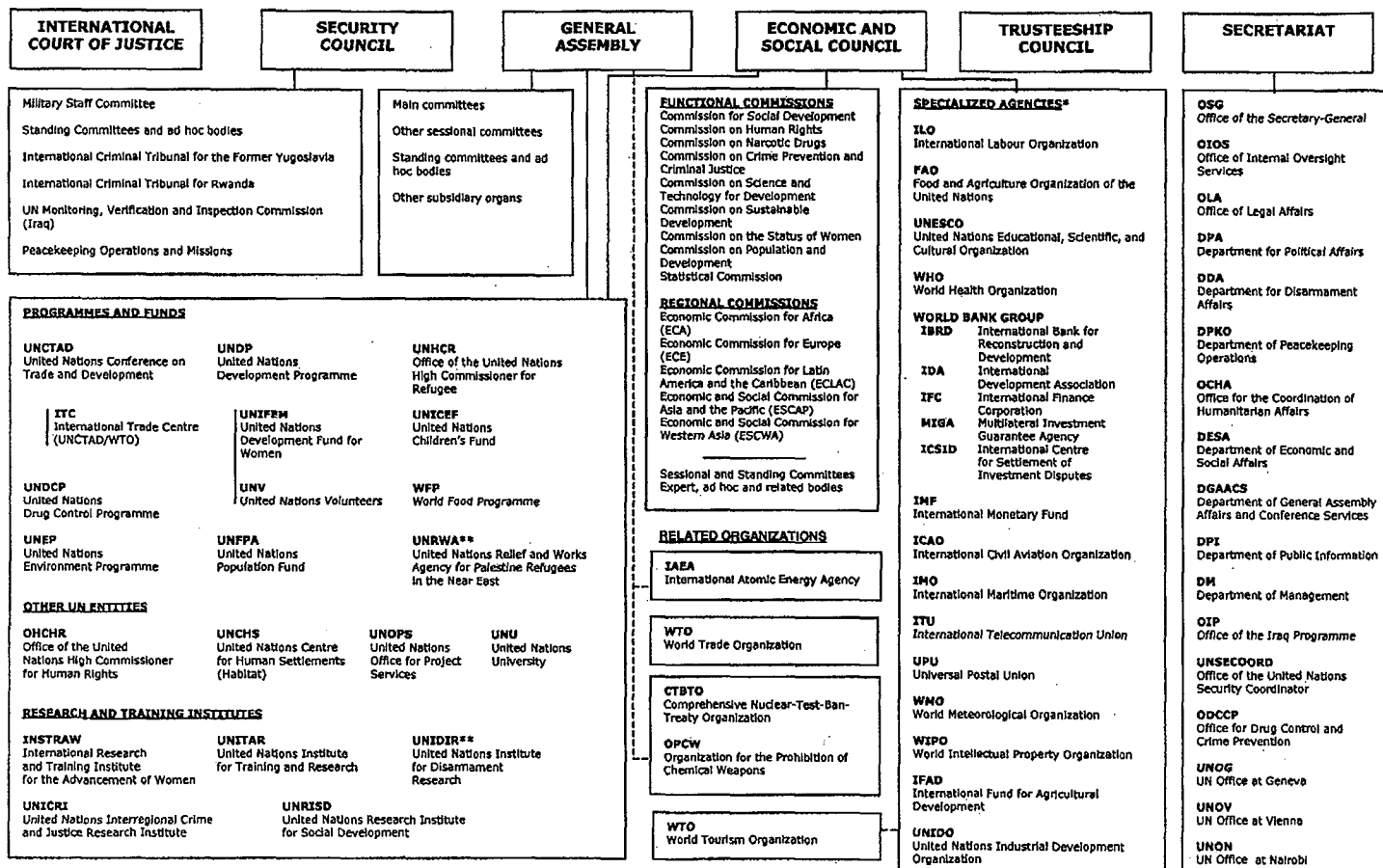
The UN comprises, in addition to the Secretariat, units, programmes and funds which are financed wholly or partly by voluntary contributions—extra-budgetary resources. They include inter-alia UNDP, UNCTAD, UNICEF, UNEP, WFP, UNFPA and UNHCR. Each of these entities has its own governing body which is responsible to the Secretary-General and ultimately to the General Assembly.

Further there are sixteen specialized and technical agencies established by Governments which have their own constitutions, memberships, governing bodies, secretariats and executive heads, and their own policies, budgets and programmes approved by their legislative bodies. The regular budgets of most specialized agencies are mobilized through assessed contributions of their member States, though separated from the UN budget. The first five agencies listed in figure IV are recognized as specialized agencies 'brought into agreement' with the United Nations.

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<sup>125</sup>Following the refocusing that has recently occurred in both these institutions it is doubtful that this criticism now contains much substance. See Maurice Bertrand, 1997.

Figure IV. The United Nations System: principal organs of the UN



\* Autonomous organizations working with the United Nations and each other through the coordinating machinery of the Economic and Social Council.  
 \*\* Report only to the General Assembly



The UN system thus comprises all organizations that have been 'brought into relationship' with the United Nations as specialized agencies, through the signing of legal agreements with it under Articles 57 and 63 of the Charter on page 164 (see appendix I). As stated in Article 58, a key purpose of these special agreements, which also contain commitments in various degrees to administrative coordination and coherence, was to ensure coordination in activities related to the promotion of economic, social and cultural objectives set out in the Charter. While some functions of the UN system can, undoubtedly, be performed separately in highly specialized fields, because of the UN's holistic approach, they do need to be coordinated. This is especially important for overarching functions or issues, such as poverty alleviation, to ensure policy coherence and operational effectiveness. There is no intergovernmental assembly or council of the UN organs as a whole. The main linkages in inter-secretariat relations are, therefore, maintained through the ACC (see below).

### *THE BRETTON WOODS INSTITUTIONS*

The second tier of specialized agencies, in the context of the United Nations Charter, is the Bretton Woods institutions, comprising the World Bank Group and the IMF, both established in 1944. The Bretton Woods institutions are governed by a voting system weighted according to shares held by member States; wealthier, more developed countries have a greater influence. The system has therefore significantly influenced the agenda for UN reform (see chapter 2). The budgets of these institutions are raised by different procedures of underwriting and capital market issues.

The original purposes of the International Bank for Reconstruction and Development (IBRD) were: to assist in the reconstruction and development of territories of its members by facilitating capital investment for productive purposes; to promote private foreign investment and, when it was lacking, to supplement it by providing finance for productive purposes; and to promote long-term balanced growth of international trade and maintain balance-of-payments equilibrium by stimulating international investment for the development of productive resources of members. The IBRD was supplemented by the International Finance Corporation (IFC) in 1956, and the International Development Agency (IDA) in 1960.<sup>126</sup>

The IMF was established in 1944 to: promote international cooperation on international monetary issues; facilitate a balanced growth of international trade by contributing to high levels of employment, real incomes and productive capacity; promote exchange-rate stability and avoid competitive exchange-rate depreciation; foster a multilateral system of payments, transfers for current transactions and the elimination of foreign exchange restrictions which hamper world trade; make resources of the Fund temporarily

<sup>126</sup>IFC plays a significant role in mobilizing private capital for enterprises in developing countries, through co-financing, loan syndications, and underwriting of securities and guarantees. IFC also renders technical assistance and advisory services to Governments in such areas as development of capital markets and privatization. The IFC provides credits to developing countries with a per capita income between \$800 on much more favourable terms than the IBRD – that is, for periods of 30–40 years without interest, except for small administrative charges, and with a grace period of 10 years for repayment of capital.

available to members to facilitate adjustment in their balance of payments without deterring national or international prosperity; and shorten the duration and magnitude of payments imbalances.

The WTO, like its predecessor the GATT, is not formally part of the United Nations system, but works very closely with the UN system. The WTO was established on 1 January 1995 as an intergovernmental organization to promote a rules-based global trading system, and to oversee and rule on international trade disputes. Cooperative arrangements with the United Nations are currently under discussion.

The key actors within the UN system concerned with the economic and social development functions comprise first, the UN proper, second, the Bretton Woods institutions (the IMF and the World Bank Group), and third, the group of specialized agencies as shown in figure IV.

## Coordination of the UN system

### *THE ROLE OF THE ACC AND THE SPECIALIZED AGENCIES*

A number of bodies are responsible for coordination within the UN system. In addition to ECOSOC, a particularly important role is assigned to the ACC. The Advisory Committee on Administration and Budgetary Questions (ACABQ), a 16-member standing committee of the General Assembly, also reviews the regular budget of the UN as submitted to the Secretary-General. The Consultative Committee on Programme and Operational Questions (CCPOQ) is a subsidiary body of the ACC. The programmatic aspects of the budget are reviewed by the 34-member Committee for Programme and Coordination (CPC), a standing committee of ECOSOC.

One of the main bodies entrusted with the coordination of the UN system is the ACC. This committee was established with a view to providing a civil service mechanism for assisting Governments in discharging their responsibilities under the Charter and for coordinating the UN system in both the General Assembly and ECOSOC. It meets twice a year. There is an unwritten but long-standing tradition of avoiding serious disagreement among its members, with the result that proposals for the ACC, assembled in advance by preparatory sub-groups, tend to be watered down until no one can disagree with them.<sup>127</sup>

The ACC is composed of the Secretary-General (Chair) and the heads of UN bodies. It supervises the implementation of agreements between the United Nations and the specialized agencies, and endeavours to ensure that their activities are coordinated. But executive heads are not obliged to attend ACC meetings, to implement agreements reached in these meetings or to heed any exhortations made there by the Secretary-General. This is because the executive heads of specialized agencies have been appointed by different governing bodies and so have the right to claim the 'sovereign' status of the policies of their agencies.<sup>128</sup>

<sup>127</sup>Childers and Urquhart, 1994, p. 31

<sup>128</sup>Childers and Urquhart, 1994.

Thus the ACC bears little resemblance to the conventional perception of a coordinator of a 'system'. The role of the chair of the ACC—the Secretary-General—is limited, since he is appointed by the General Assembly. The heads of the specialized agencies on the other hand are appointed by their legislative bodies.

The constitutional set-up of the UN system, which gives different specialized agencies their own autonomous governing bodies, reduces the possibility of a strong, coordinated UN system and therefore makes implementation of the mandated Charter for promoting economic and social development difficult. Each agency adopts its own policies and budgets, and member Governments of the UN system have never adopted a mandatory, overall strategy or consolidated budget for the UN system as a whole.

Because of these difficulties, the ACC has not achieved its potential in coordinating the economic and social activities of the UN system. There has been no significant progress in clarifying mandates or in avoiding duplication, overlap and proliferation in the UN system. The proliferation has arisen out of new requirements in different specialized fields, such as trade, drugs and the role of women, with the active support of various member Governments.

## **The UN development system**

### *RESOURCES DEVOTED TO NORMATIVE AND OPERATIONAL ACTIVITIES*

A broad estimate of resources in the UN development system devoted to normative and operational activities is given in table 7, which shows the number of staff employed from 1974 to 1994, in both headquarters and the field. In total, the headquarters staff of the development system of the UN grew from 32,000 in 1974 to 48,000 in 1994. The expansion of staff in the UN proper—for example in UNCTAD, UNEP and Habitat—from 1974 to 1983 would appear at first glance to be related to the growing importance of the normative functions of the Organization—agenda setting, promoting understanding and establishing norms. However, the largest increase—almost three-quarters—occurred outside headquarters, suggesting an increasing focus on operational as opposed to normative activities in the UN. The expansion has been concentrated especially in funds and programmes, such as UNDP, UNFPA, UNICEF and WPF, and in other field-oriented organizations, such as UNHCR.

With the exception of UNIDO, the large specialized agencies, which were already well established by 1974, did not expand. The optimal mix of normative and operational activities—or, as some influential commentators would allege, which one the UN should focus on—is still a major issue in the debate on UN reform.

The concept of UN development assistance began in 1947 when the Secretary-General was asked by the General Assembly to establish the institutional machinery for providing development assistance to Governments of Member States in addition to those provided by some of the specialized agencies. Initially, the modest provisions in the UN regular budget were supplemented by the Expanded Programme of Technical Assistance

(EPTA) for developing countries. In 1958, the United Nations Special Fund (SF) was established to manage the larger and more comprehensive projects. The EPTA and SF were amalgamated in 1965 into a new organization, the United Nations Development Programme (UNDP). By 1960, around half of the total UN budget of \$226 million was earmarked for economic and social activities primarily financed by extra-budgetary resources from voluntary sources.

In the early years, much of the development assistance was provided by bilateral donors, especially the United States, which was followed by other donors. Over the years, bilateral assistance was increasingly channelled through the UN development system, and numerous bodies and agencies within the system were created. For example, the International Finance Corporation (IFC) was created in 1956, the International Development Association (IDA) in 1960, UNDP in 1965 and the United Nations Capital Development Trust in 1966; the Centre for Industrial Development in the UN Secretariat was converted to the United Nations Industrial Development Organization (UNIDO) in 1967, and became a specialized agency in 1985; the WTO was created in 1995.

**Table 7. Trends in UN staffing**  
1974, 1983 and 1994<sup>a</sup>

	1974		1983		1994	
	Headquarters	(Field)	Headquarters	(Field)	Headquarters	(Field)
UN: UNCTAD, UNDCP, UNEP, etc. <sup>b</sup>	11,436	(7,017)	16,205	(11,171)	14,710	( 9,056)
Funding organizations:						
UNDP, UNFPA, UNICEF	2,151	(1,313)	7,941	( 6,513)	11,287	( 9,059)
UNCHR, UNWRA, WFP	705	(175)	2,673	( 2,980)	5,028	( 3,647)
Large specialized agencies:						
FAO, ILO, UNESCO, WHO, UNIDO	17,273	(8,705)	17,133	( 8,526)	16,551	( 7,619)
<b>Total</b>	<b>31,565</b>	<b>(17,210)</b>	<b>43,952</b>	<b>(29,190)</b>	<b>47,576</b>	<b>(29,381)</b>

<sup>a</sup>Non-headquarters staff in parentheses.

<sup>b</sup>Not comparable with other field categories because of the inclusion of UNEP, Habitat, etc. as non-headquarters stations.

Source: Joint Inspection Unit: *Strengthening Field Representation of the United Nations System*, Geneva, 1997, JIU.REP/97/1.

**Appendix I. International Economic and Social Cooperation  
in the UN Charter (Chapter IX)**

**ARTICLE 55**

With a view to the creation of conditions of stability and well-being which are necessary for peaceful and friendly relations among nations based on respect for the principle of equal rights and self-determination of peoples, the United Nations shall promote:

- a. Higher standards of living, full employment, and conditions of economic and social progress and development;
- b. Solutions of international economic, social, health and related problems; and international cultural and educational cooperation; and
- c. Universal respect for, and observance of, human rights and fundamental freedoms for all without distinction as to race, sex, language, or religion.

**ARTICLE 56**

All Members pledge themselves to take joint and separate action in cooperation with the Organization for the achievement of the purposes set forth in Article 55.

**ARTICLE 57**

1. The various specialized agencies, established by intergovernmental agreement and having wide international responsibilities, as defined in their basic instruments, in economic, social, cultural, educational, health, and related fields, shall be brought into relationship with the United Nations in accordance with the provisions of Article 63.<sup>a</sup>
2. Such agencies thus brought into relationship with the United Nations are hereinafter referred to as specialized agencies.

**ARTICLE 58**

The Organization shall make recommendations for the coordination of the policies and activities of the specialized agencies.

**ARTICLE 59**

The Organization shall, where appropriate, initiate negotiations among the states concerned for the creation of any new specialized agencies required for the accomplishment of the purposes set forth in Article 55.

**ARTICLE 60**

Responsibility for the discharge of the functions of the Organization set forth in this Chapter shall be vested in the General Assembly and, under the authority of the General Assembly, in the Economic and Social Council, which shall have for this purpose the powers set forth in Chapter X.

ARTICLE 63

1. The Economic and Social Council may enter into agreements with any of the agencies referred to in Article 57, defining the terms on which the agency concerned shall be brought into relationship with the United Nations. Such agreements shall be subject to approval by the General Assembly.
2. It may coordinate the activities of the specialized agencies through consultation with and recommendations to such agencies and through recommendations to the General Assembly and to the Members of the United Nations.

## **Appendix II. Main UN intergovernmental and expert bodies in the economic, social and human rights fields**

### **I. General Assembly and treaty bodies reporting to the assembly**

Main committees	Second—Economic and Financial; Third—Social, Humanitarian and Cultural
Treaty bodies	Elimination of Racial Discrimination/ Human Rights—International Covenant on Civil and Political Rights; Economic, Social and Cultural Rights/ Elimination of Discrimination against Women; Torture; Rights of the Child
	<b>Total 9<sup>a</sup></b>

### **II. Economic and Social Council and its subsidiary bodies**

Functional commissions	Statistics; Population; Social Development; Human Rights, including the Subcommission on Prevention of Discrimination and Protection of Minorities; Status of Women; Narcotic Drugs; Science and Technology for Development; Sustainable Development; Crime Prevention and Criminal Justice
Standing and expert bodies	Transnational Corporations; Human Settlements; New and Renewable Sources of Energy for Development; Non-Governmental Organizations; Programme and Coordination; Natural Resources; Development Planning; Transport of Dangerous Goods; International Cooperation in Tax Matters; Public Administration and Finance; International Standards of Accounting and Reporting; Geographical Names
Regional commissions	Economic Commission for Africa; Economic and Social Commission for Asia and the Pacific; Economic Commission for Europe; Economic Commission for Latin America and the Caribbean; Economic and Social Commission for Western Asia
	<b>Total 73<sup>b</sup></b>

### **III. Other United Nations Secretariat units, bodies, programmes, organs and funds, and their governing bodies**

United Nations Conference on Trade and Development (UNCTAD)	Conference Trade and Development Board, other UNCTAD Standing Committees and Ad Hoc working Groups (11)
United Nations International Narcotic Drug Control Programme (UNDCP)	International Control Board

United Nations Development Programme (UNDP)	Executive Board
United Nations Environment Programme (UNEP)	Governing Council
United Nations Population Fund (UNFPA)	(same board as UNDP)
United Nations High Commissioner for Refugees (UNHCR)	Executive Committee
United Nations Children's Fund (UNICEF)	Executive Board
United Nations Development Fund for Women (UNIFEM)	Consultative Committee
United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA)	Advisory Commission
World Food Council (WFC)	
World Food Programme (WFP)	Committee on Food Aid Policies and Programmes
	<b>Total 23</b>
	<b>Grand total 105</b>

<sup>a</sup>In addition there are at present preparatory bodies for the World Summit for Social Development, the Fiftieth Anniversary of the United Nations, the International Conference on Population and Development, the Global Conference on the Sustainable Development of Small Island Development States and the United Nations Conference on Human Settlements (Habitat II); there are also Intergovernmental Negotiating Committees for a Framework Convention on Climate Change and for the Elaboration of an International Convention to Combat Desertification, and a United Nations Conference on Straddling Fish Stocks and Highly Migratory Fish Stocks.

<sup>b</sup>This total includes 45 subsidiary bodies reporting to the regional commissions.

Source: Partly based on *An Agenda for Development 1995*, Boutros Boutros-Ghali, United Nations, New York, 1995.



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