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**The European Union preliminary views  
on  
“Mobilizing domestic financial resources for  
development”**

New York, 14 February 2008

The **mobilization of domestic resources** is a key component of the global partnership on financing for development. Effective domestic resource mobilisation in and by developing countries, is the most sustainable way and essential to provide important development resources for the purpose of sustainable pro-poor growth.

The Monterrey Consensus states that each country is **primarily responsible** for its own economic and social development. The importance of a **favorable and constructive domestic environment** can not be overemphasized and is a prerequisite to effectively mobilize domestic financial resources as well as international private flows, including foreign direct investment. The role of good governance and sound national development strategies, that are gender responsive and pro-poor growth oriented, cannot be overemphasized. This **might require improving economic and financial governance, sustaining stability-oriented macroeconomic policies and better exploiting natural and human resources.**

1. Six years after the Monterrey Consensus was agreed progress has been recorded in this regard, although unevenly across countries and sectors. While external resource flows have an important supporting role to play in financing for development, **long-term development processes can only be sustained through domestic resources, mobilized in compliance with the principles of good financial governance.**
2. **Governance**<sup>1</sup> at national and local levels, especially good economic and financial governance, based on the rule of law and respect for human rights, with particular attention to people belonging to vulnerable groups and gender equality and democratic processes, is a precondition to sustainable and equitable development.

Corruption and its pernicious effects on resource mobilisation and allocation is an example of the damage caused by poor governance. **Fighting corruption** needs a two-pronged strategy that addresses both individual instances of corruption and the underlying factors. The UN Convention against Corruption (UNCAC), as of now ratified by 107 states, offers a holistic framework for combating corruption at all levels and for providing technical assistance to states wishing to implement the Convention. While there is a clear priority to prevent corruption, there is also the responsibility to return stolen assets to the victim states in order to make them available for development again.

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<sup>1</sup> The EU approach to governance is holistic and entails mainstreaming of human rights and fundamental freedoms, good governance and rule of law to all policy sectors, while respecting national ownership and dialogue.

3. The leading actions identified in the Consensus to spur the mobilisation of domestic resources and their efficient intermediation remains appropriate. Still required is the establishment of **good economic and financial governance**, that is to say a practice of economic management and a regulatory and institutional environment that foster economic decisions leading to sustainable pro-poor growth. Good economic and financial governance rests on the pillars of **transparency, accountability, rule of law and participation**.

Among the various elements of good economic governance identified in the Monterrey Consensus, it is worth recalling that:

- The exceptionally **good growth performance** of developing countries in recent years was supported by a **favourable global economy** but would not have been possible without the fairly widespread implementation of **stability-oriented macroeconomic policies** that maintained internal and external stability. Partners' commitment to such policies buttressed by international surveillance and financial support need to be maintained. In many low-income countries, debt relief provided the fiscal space to shift expenditure from debt service to poverty reduction without deterioration in the fiscal position; governments should aim at avoiding a renewed accumulation of public debt that would put at risk the regained fiscal space in the medium term.
- The importance of an **enabling business environment** that provides women and men with opportunities to unleash their economic potentials and promotes private investment at manageable levels of risk has been increasingly recognised by policy-makers across the world. Non-discriminatory, transparent and predictable investment rules should trigger and facilitate the re-investment of domestic capital in the national development processes. Adequate infrastructure, an educated and well-trained workforce, an efficient regulatory framework and well-functioning administrations and judicial systems are increasingly seen as crucial components of a successful development strategy fostering sustainable and inclusive growth. While progress has been significant, it has also been uneven across countries and continents, and thus still requires a major effort in the future, notably in Africa.
- Some progress in **financial sector development** has been achieved thanks to an improved business environment, better financial sector regulation, innovative approaches (e.g. mobile banking) and the wider availability and use of microfinance. In this context, the EU underlines the critical need for reinforcing national efforts in building capacity for social and gender budget policies as

stated in the Monterrey Consensus<sup>2</sup>. There has been considerable progress since 2002 in this regard, but we still need to move firmly from analysis to implementation, targeting i.a., the revenue side of budgets. Efforts must continue in all dimensions of financial sector development (depth, outreach, efficiency, access etc.) as the mobilisation of domestic resources can only succeed with a well-developed and demand-oriented financial sector which intermediates savings into investment and allows a smoother adjustment to economic shocks.

- **The principle of country ownership** should be respected and therefore it is clear that supporting and strengthening host governments' own governance efforts is a core objective.
4. The management of a country's endowment has a direct impact on the availability of domestic financial resources and their efficient mobilisation. This focuses attention on the challenges and progress affecting:
- The **management of natural resources** which has a tremendously important role to play if the paradox of "resource curse" is to disappear. Resource use taxes and fees can promote sustainable extraction and consumption of scarce natural resources and can be used to recover costs to improve the quality of the environment. While there are positive signs suggesting better macroeconomic management of the current boom in commodities markets, weak governance and poor institutions are still a source of concern in many resource-rich countries. International initiatives such as the Kimberley Process, the Extractive Industries Transparency Initiative (EITI) and the Forest Law Enforcement, Governance and Trade (FLEGT) Action Plan to fight illegal logging are examples of worthwhile innovations that deserve to be deepened and broadened.
  - **The progressive realization of decent work for all, including investment in human capital** through non-discriminatory and better designed and better funded health and education policies, coupled with better social protection and active labour market policies, have begun to show results but require increased efforts. The promotion of gender equality and the empowerment of women as a fundamental human right and a catalyst for human and sustainable development play a crucial role with regard to the mobilization and effective utilization of a country's human capital and thus its domestic resources. Migration policies should aim at maximizing the positive spillovers for source countries (in terms of

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<sup>2</sup> See para 19 and 64

remittances but also brain gain) while minimizing the potentially negative effects (brain drain).

- By limiting access to services and markets, the lack of infrastructure is a serious constraint to the exploitation of economic opportunities and the establishment of pro-poor growth. Partnership efforts towards **infrastructure development** therefore play an important complementary role in the mobilization of resources.

5. The **State** – be it at the central government or sub-national level - **has a particularly important role** to play in the mobilisation of domestic resources for three reasons: because it designs and implements the relevant laws, regulations and policies; because taxpayers' willingness to pay depends on citizen's trust in government and their acceptance that enforcement of tax collection is a legitimate exercise of state power; and because the state directly raises taxes and re-allocates these resources through its budgetary system. In this regard: not only because it designs and implements laws, regulations and policies but also because it directly raises public savings through taxation and re-allocates resources through its budgetary system. In this regard:

- To support an enabling fiscal policy, **reform of tax policies and tax administrations** (i.e. to enhance progressivity, diversity and stability of tax revenues) play a crucial role and can potentially improve several dimensions of economic, financial and political governance at the same time and might also be suitable to address income equalities. Developing countries' efforts need to be sustained and deserve the type of increased support from the international community as identified in the G8 Action Plan for Good Financial Governance in Africa.
- The strengthening of partner countries' **public financial management (PFM) systems** is an on-going and lengthy process which has seen progress as evidenced by the HIPC Assessment and Action Plans and the Public Expenditure and Financial Accountability (PEFA) monitoring framework. Past and future progress depends upon the genuine commitment of partner countries' authorities, a strengthened role for local external accountability bodies like Supreme Auditing Institutions and National Parliaments, a greater use of country systems by donors, and better harmonisation and alignment around a national reform programme and a coordinated programme of support as proposed by the PEFA Strengthened Approach to PFM.

- There is growing evidence and consensus on the fact that gender equality contributes to and boosts economic growth rates and sustainable development<sup>3</sup>. Thus, **gender aspects need to be broadened** beyond the social sectors so as to encompass other policy areas (economic growth, trade, migration, infrastructure, the environment and climate change, fragile states, peacebuilding and reconstruction). Specific actions for the empowerment of women constitute core components of domestic resource mobilization and need to be integrated into national development strategies and budgets (see also above)
  - The State has a further potential role in mobilizing and encouraging domestic savings. Many poor countries' growth rates are constrained by low domestic savings rates.
6. The **private sector**, including both its domestic and foreign components, also has an important role to play and strengthening national and international initiatives around corporate social responsibility constitutes a novel element that deserves to be further developed.
7. While the effective mobilisation of domestic resources for development is primarily a national responsibility, it can be greatly supported by parallel **complementary efforts at the international level**. Examples include the need to ratify and, above all, implement the UN convention against corruption (UNCAC), the shared responsibilities among suppliers and consumers of natural resources and the emerging international initiatives in this regard. The G8 Action Plan for Good Financial Governance in Africa outlines a framework for both national activities and international support in the field of promoting competent, transparent and accountable public financial management.
8. The **potential of remittances** as an important source of financing for development **complementing domestic savings** should also be considered.

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<sup>3</sup> Source: MDG Progress in Asia and the Pacific, ESCAP 2007, see also World Bank Gender Action Plan "Women's Economic Empowerment as Smart Economics" and the latest MDG Global Monitoring Report of the World Bank.

## **The European Union initiatives**

9. The EU will continue to encourage and support partner countries' efforts in building and developing their capacity for domestic resource mobilisation. As an example, the promotion of governance, including all aspects of economic governance, constitutes a central feature of the Joint Africa-EU Strategy and Action Plan launched in Lisbon on 8-9 December 2007. Through their Strategic Partnership on Democratic Governance and Human Rights, Africa and the EU will enhance their continent to continent dialogue on governance and the progressive realization of human rights including the realization of gender equality. This dialogue should help both parties to define the issues at stake, agree on common positions on issues of common concern and jointly undertake specific initiatives and actions. Support to the consolidation of the Pan-African Governance Architecture will also be an integral component of this Strategic Partnership. It includes in particular implementation of the African Charter on democracy, elections and governance, where AU member states formulate key commitments in the area of economic governance.