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## The Foreign Investors Council In Latvia Position On National Economy Competitiveness Institution

### 1. Executive Summary

The Foreign Investors Council in Latvia (FICIL) position is that the Government should improve coordination and concentrate available resources for economic research and in a medium term facilitate establishment of an independent economic research institution - *National Economy Competitiveness Institution (NECI)*. The institution should work in sphere of macroeconomic analysis including long term economic planning, labour market research and assessment of tax policies. *NECI* would be a central coordinator of all economic related research in the country, and would ensure quality control, more efficient use of existing resources and undertake the task of making results publicly available and communicating them via seminars and discussions. Improved research quality, long term projects, effectiveness, direct applicability of research results, and attraction of foreign research colleagues with necessary scientific and experience background should be primary aims of the organization. The new institution should also be more integrated into the European and American research networks. FICIL position is such that qualitative, independent and appropriate ex ante and ex post research could be helpful in evaluating the Government policies and their effect on national economy and forecasting models could be a good tool for knowledgeable decision making and qualitative alternative to the policy makers.

### 2. Recommendation/Suggestions

1. To centralize research process in Latvia via introducing main coordinating institution, to enhance effectiveness in both - research activities and communication of the results obtained.
2. To promote and ensure with necessary funding long term research projects and consolidate the current funding with the aim of improving research depth, quality, applicability and actuality in the economic sphere.
3. To impose four main objectives for the research - namely to be objective, credible, effective, actual and provide necessary support for the fulfilment of these criteria.
4. To develop a system of knowledge sharing via publicly available means: research databases, internet, scientific journals and magazines.
5. To increase competence of Government side representatives in order to ensure fruitful dialogue between researchers and policy-makers.
6. To promote international cooperation by attracting foreign specialists.
7. To create competitive base financing and project financing system to keep establishment attractive to the scientists (both local and foreign) and prevent "brain drain" and allow them to concentrate on the research process.
8. To use as a guide foreign experience in the research area, the best and the most similar by the conditions being example of the Economic and Social Research Institute (ESRI) in Ireland.

### 3. Rationale

The situation in Latvia during last years demonstrates a clear need for an authoritative independent institution which would participate in the evaluation and discussion of economic policy-making. The necessity to strengthen economic research capacity has become especially important as Latvia candidates to adopt the euro in 2012 and has become vulnerable in times of economic downturn. There is an important need to evaluate consequences of any proposition from the Government side to ensure stabilization of the situation and successful inclusion into Europe.

The FICIL suggests creating the *National Economy Competitiveness Institution* to promote qualitative, independent research work with publicly accessible results. Previous experience shows that due to the incoherence of the research institutions, cooperation among them remained low. Moreover, due to insufficient financial means these institutions were usually created as supplementary services where primary job of researchers remained teaching or even working in business which considerably impacted the quality of the previous research.

Another aspect is that the research performed was mostly short term (6-8 month or 1 year max) and on irregular basis. This is due to the fact that research financing was distributed by the program *Valsts Pārvaldes Institūciju Pasūtītie Pētījumi* and was tailor-made according to the needs of yearly budget balance requirements. The projects were case-based and suited for the needs of an organization which ordered them, and were rarely distributed across other organizations/political institutions, thus making enlargement of common knowledge field impossible. The evaluation of performed research by the institution ordering them was also around average or satisfactory grade being commented by low quality/applicability and lateness of the research results.

The areas studied mostly were financial policy, education, regional development and demographic questions. The governmental institutions expressed strong agreement on the need of research in macroeconomics sphere, entrepreneurship development, labour market, and fiscal policy evaluation and recommendations. Importantly, the low current level of research used in policy planning was emphasized. Not only dissatisfaction with the current state in research activities was mentioned but also the fact that the communication between researchers and policy-makers is not equally competent from both sides. This implied a need for additional education and cooperation between government representatives and the research world to achieve full agreement and efficient implementation of the research results.

Moreover, there is a very low cooperation between Latvian and foreign researchers. Latvian research is rarely publicized into the international research databases. Foreign researchers with experience are not attracted to work in Latvia due to uncompetitive financial support and communicate with representatives of a local research force on a case-by-case basis.

Following from the facts above, the FICIL strongly advises creation of the research institute similar to the Economic and Social Research Institute (ESRI) in Ireland. This institution was developed in a similar to Latvia situation and was initially based on substantial governmental financing and aimed to attract foreign qualified research force. Further on, it had developed strategy by gradual replacement of internationally recognized researchers by educated local specialists.

To employ the resources more efficiently, the research institution would undertake the function of coordination of all economic research. When specific research topics or requests arise, the institution would announce a tender and research institutes would compete for the right to perform the particular project, thus increased competition among research institutes would improve quality of their work. On the other hand, some extensive projects could be performed by cooperation of two or more institutes. The coordinating institution would supervise and ensure no overlapping in the research process. Besides by undertaking functions of research coordination it will resolve the

current problem of incoherence. As some projects will be carried out jointly, research institutes will benefit from knowledge spillovers, cooperative work will create synergies.

A duty of the *NECI* would include a constant development of forecasting models useful for policy-makers to better see the cost-benefit tradeoff of different policies.

Independent analysis of key political planning documents and legal acts and their evaluation would considerably contribute to the performance of the public sector.

*The NECI* would maintain ongoing research (systemic modules) in strategically important areas: tax policy, government spending, and labour market.

Another crucial aspect is communication of the research results. Task of the central research institution would be to ensure availability of the research and introducing public to results via different events like presentations, seminars and discussions.

The growth of research capacity will be ensured through various channels: consolidating resources countrywide, attracting researchers from abroad and new local researcher base.

As attracting and maintaining highly qualified professionals can be difficult until the economic research institute has earned international recognition, it might be advised to establish it on a base of an existing institute with experience of international cooperation and research or by means of consolidating some of the existing institutes.

Important is independence of the *NECI* from the governmental apparatus. Two-tiered system of financing, via base financing and additional project and grants based support would keep the brightest minds and enhance the quality of work on projects provided by the Government and the Central Bank. Such an institution will also attract private and international funding via performing orders and generate revenues from research itself. For a large central institution it is easier to gain recognition. If an institution is a brand itself, credible and recognized, more opportunities to get grants from international organizations will be available. The pooling of existing funding and appropriate allocation between different research projects will strengthen the analytical capacity and will help avoid overspending on overlapping research and underfunding of large and important projects. The variability of financing sources will enhance the objectivity and independence of the research made.

From experience of other countries it can be noted that specific personnel is needed as a mediator to present the ideas formulated by researchers in a language understandable and useful for policy-makers.

The FICIL sees three main action spheres for the *NECI*:

Firstly, modelling of fiscal policy: this would provide capacity to explain and evaluate quickly the economic impact of budget changes. Ex ante and ex post research on the economic policy would allow for prudent decision making and situation control. Additionally political decision papers should be studied for the policy approval.

Secondly, introducing a research programme on development of long term economic models for Latvia, for example, on understanding the drivers of productivity and innovation. This would provide a basis for evidence-based policy-making in this area.

Thirdly, coordination and centralization of existing research process being the initial duty of proposed organization.

Currently the situation is such that many important political decisions are intuition-based. Such are increase in minimal wage, changes in tax regimes, unemployment programmes. The

consequences of these decisions should be assessed to avoid possible flaws in the future. To understand and study all the issues an increased capacity in the research field is needed. Without it the analysis of Latvian economy never will become sufficient enough to be guide for a prudent decision-making.

The central research institution could be an efficient way of solving current situation as it allows for high long term cooperation, consulting and knowledge sharing between science and academic circles. It also prevents overlapping of work and induces stability and development path into local research area. Moreover, this institution will foster distribution of knowledge to local and foreign public policy-making, and scientific circles, implying the immediate usability of the research results.