

# Peer review in the context of regional integration

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Peer review of economic policies by countries comprises peer learning, peer support and peer pressure. Durable peer review processes focus on mutual peer learning and support as peer pressure rarely works unless countries can be convinced that a policy is in their national interest. It requires a high degree of trust and respect, sharing of information, analytical and administrative capacity and legitimacy.

Proximity may lead to greater trust and openness, but it may also be associated with long-standing historical differences and grievances. In principle peer review could be a useful adjunct to other aspects of a regional integration strategy designed to bring mutual benefit to the participating countries. In the Asian context there appears ample scope for well designed peer review to contribute to domestic policy development.

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## Introduction

It is a great pleasure to be here today. In thinking about this topic it occurred to me that a useful question to address would be the following: 'what, if anything, is different about peer review in the context of regional integration?' In answering this question I will do three things. First, I will outline three aspects of peer review. These are peer reviews as peer learning, peer preview as support for domestic stakeholders, and peer review as peer pressure. In outlining these elements I will argue that peer learning is the core of peer review and that attempts to pursue peer pressure more aggressively will almost certainly undermine the process. Second, I will outline the preconditions necessary for peer review to work well. Third, I will comment on whether undertaking peer review in the context of regional integration helps or hinders constructive peer review. Naturally this last aspect will be heavily influenced by the specific regional integration project, but I think that some general observations can be made.

My discussion is focused on peer review between countries with respect to economic policy matters rather than peer review in the academic context or regarding other policies. In this context mutual discussions between countries about their economic policies often lead to recommendations for action agreed among the peers.

However, before exploring the detail, I think it is worth stating a key premise on which I believe peer review is based. This premise is that it is in our own interests for everyone else to be successful. This is true in the economic sphere. It is also true with respect to having successful, sound and stable institutions. To economists this is an obvious point that is implicitly rejected by many mercantilists. Put another way, the objective of peer review is to help each other to be successful in our own enlightened self-interest.

## Three aspects of peer review

The term 'peer review' is often used to describe a wide variety of processes. However, I would argue that practical peer review combines three main elements. The three elements are:

- peer review as peer learning (or alternatively peer exchange);
- peer review to provide support for a policy that a country would already like to undertake; and
- peer review where the reviewers would like the country to do something that they do not want to do.

Peer review can usually be considered as involving the 'reviewers' (perhaps a few countries designated to lead questioning and discussion of the country under review); that country's 'counterparties' (the officials representing their government); and the 'other parties' to the review, countries which join the discussion led by the reviewers. In addition, where a permanent secretariat exists, they can play quite an important role. Whether this role is merely one that facilitates the process or leads to a fundamentally different outcome depends on the responsiveness of the secretariat to member countries and to the formal process of clearance for review documents.<sup>2</sup>

### Peer review as peer learning

Arguably the most important aspect of peer review is genuine peer learning. This may sound a little counter-intuitive as the phrase peer review often invokes a more inquisitorial process, but I am convinced it is true. The nature of peer review is that it is a process whereby 'soft powers' are exercised, and those 'soft powers' are the power to convince people that there is a policy prescription worth following and to encourage all countries to think analytically about the lessons for their own national case of the country under review. Importantly, the directions in which the information flows are often from the reviewed country to the reviewer and to the other countries in the dialogue. In this respect the attitude of the reviewers is vital. Peer review works best when an atmosphere of constructive dialogue is created. Peer reviewers and other countries should be motivated by the question 'what can I learn from this process?' as much as 'what can I impart?'

Learning from peer review is multidirectional, and 'what you get out is proportionate to what you put in'. While the reviewers and the counterparties may be focused on the country experience under examination, the other parties may be wondering (and debating with their domestic authorities) 'what do country A's lessons and country B's lessons have in common?'; or 'why does this policy work in country A, but not in country B?'

This observation is not surprising when one pauses to think about the nature of the peer review processes. It is only natural that the reviewed country knows more about

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2 In the context of the OECD's Economic and Development Review Committee (EDRC) the role of examiners (lead countries) has diminished over time. In practice the examiners act as lead discussants with the Committee as a whole performing the role of reviewers. This evolution may reflect the longstanding nature of the EDRC (it has held over 1,000 meetings), the frequency of the meetings (around 25 per year) and the continuity of delegates to the meetings. Less well established processes may need to rely more heavily on a subset of countries in initiating discussions. Also in the EDRC context, the Secretariat is very responsive to the collective view of the Committee, partly reflecting the fact that review documents are released under the auspices of the Committee itself as adopting reports under a consensus rule.

their country than the reviewers. Indeed, while there may be cases where reviewers are better informed, these are likely to be the exception to the norm. It is natural that authorities representing a country will have a much better appreciation of the specific circumstances of their country than the reviewers.

This last point has become increasingly true given the shift in focus of macroeconomic peer review and surveillance. There is now a much greater understanding that macroeconomic analysis is not very useful without strong links to structural policy which drive the supply potential growth of the economy. The OECD's EDRC process prides itself on undertaking macro-structural analysis. This reflects the clear understanding that the interaction of macroeconomic and structural policies is the key to understanding an economy. Two examples illustrate this point well.

- First, the European Central Bank (ECB) is sometimes criticised for not behaving more like the United States Federal Reserve. Much of this criticism is unfounded as it fails to take account that the Fed faces a very different set of product and labour markets than the ECB. A central bank dealing with some areas with implicit wage indexation and influential unions cannot behave the same way as a central bank operating in an economy with very weak employment protection legislation and substantial inter-regional labour mobility.
- Second, external observers often compare favourably the resilience of the Australian economy to Europe. It is true that sound macroeconomic policies and a flexible exchange rate play an important role in delivering resilience. But it is also true that highly competitive product markets, with the implied discipline to factor markets, play a very significant part in allowing the smooth absorption of economic shocks – both negative (such as the global slowdown of the start of this decade) and positive (such as the commodity-price driven improvement in Australia's terms of trade).

It is not true that macroeconomic policy lends itself to simplistic one-size-fits-all solutions. But it probably is true that macroeconomic experts can readily discuss the appropriate macroeconomic settings in a country with recourse to a relatively small set of data. I have certainly observed this in the context of the EDRC. Members can easily debate the merits of inflation targeting, flexible exchange rates and centralised versus decentralised wage bargaining. It takes a lot more homework to debate the merits of the regulatory arrangements around infrastructure or network industries. In practice this homework will rely a lot on information provided by the reviewed country.

Furthermore, the scope for peer learning with respect to structural policies is large, particularly where countries face common problems, but there is no consensus around solutions. For example, many OECD countries face a common problem of growing numbers of people receiving sickness, disability or incapacity benefits. Many OECD

countries acknowledge the problem and are keen to learn from countries that seem to be making progress on the issue. Accordingly, the new approaches that have been introduced in Denmark and the Netherlands excite a lot of interest – when these countries are reviewed the reviewers are not looking to criticise, they are looking to learn.

When trying to benefit from peer learning, peer reviewers often have in mind the following question ‘when I see a policy that looks successful, is there some country specific factor that means it would not be applicable to my country?’ This is a critical question, and is at the heart of both the inquiring and respectful nature of peer review. It recognises that policies often evolve in countries in response to the specific cultural, institutional and historical context. Policies rarely come into being for no reason. The flipside of this is that the good peer reviewer does not jump to the conclusion that a particular policy is bad and should be changed without carefully considering the country-specific context. The question that should come into the mind of a good peer reviewer when they see a policy that does not make sense to them is ‘what am I missing; what factor might exist that I do not understand?’ Of course the benefit of peer review is that the reviewer can actually ask this question, and in giving the answer the reviewee may reflect on whether the current policy is the best policy that can be pursued.

The process of information exchange described above relies on a high degree of openness. If a country chooses not to disclose key information, then the opportunity for peer learning is significantly diminished. Accordingly, the conduct of the participants is vital. Many have commented that peer review is a fragile process. This may partly reflect the fact that if one participant acts in bad faith, then it can undermine the spirit of trust that allows free exchange of information and genuine learning. Accordingly, good peer review processes need to be nurtured as an appropriately constructive approach often needs time to develop.<sup>3</sup>

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3 This is analogous to negotiation contexts. Some negotiation theorists distinguish between distributive and integrative negotiation. Distributive negotiation seeks to divide a given set of resources. Integrative negotiation seeks to expand the set of resources for mutual gain. That said, integrative negotiation can only be achieved if the parties agree to exchange information with a view to finding mutually advantageous exchange. If parties fear that the other party will behave in a narrow distributive sense, then it will hamper the chances of achieving mutually beneficial gains. Peer review is similar. Parties must be prepared to share information in order to achieve mutual gains. However, if parties fear that others will behave distributively (for example by using information to their advantage in a parallel negotiating context), then the benefits of the process can be eroded (see Bazerman and Neale 1992).

## Peer review as peer support

The second aspect of peer review is peer review that facilitates domestic reform. Reviewed authorities may already wish to implement a particular policy, but may need additional support due to political economy considerations.

Peer review may be most helpful where a particular policy is in the national interest, but powerful vested interests stand in the way of its introduction. Peer review can assist by providing an independent analysis of the facts of the situation, one that may carry more weight in shifting public opinion than an assessment made from within the country as internal assessments may be perceived to be driven by their own vested interests.

The relevance of this leg of peer review is critically linked to the credibility and weight given to the particular peer review mechanism. For example, it has often been argued that the influence of OECD reviews is inversely related to the size of the reviewed country (partly related to the vibrancy and competitiveness of its domestic marketplace for policy ideas, and the depth of its domestic analytical processes). In the US political context peer review by an international organisation appears to have little weight – indeed it may actually be counterproductive to positively influencing public opinion. Similarly, some countries may view outside advice as inappropriate and unhelpful.

In this respect it is important to highlight the role of the counterparty in the peer review process. Internationally, the counterpart generally represents the government of the reviewed country. That said, in practice the counterpart may be a subset of that government that may consult and coordinate in varying degrees with other parts of government. Practice in this area varies considerably.

There may be different country-specific dimensions to this counterparty variation. These variations are as numerous as the different forms of government. However, some of the most notable variations in counterparties are:

- Instances where there is a separation of the executive branch of government and the legislative branch. The executive typically is the counterparty in international peer review and may have interests that are not aligned perfectly with those of the legislature.
- Variations within the executive branch of government. For example, in some processes the Ministry of Economics may be the counterparty with the responsibility of representing the government of the reviewed country.

- Variations between levels of government in non-unitary systems. In federal systems this may involve differences between the interests of the national, provincial and local government levels.

Implicit in this is the fact that the results of the peer review are published. Other channels of peer review do not necessarily require the results to be transparently available. But, as the OECD (2003) notes,

... the government of the reviewed country can also come under pressure from the press and the public to accept the recommendations [but] ... officials of the country under review may welcome advice from outside that supports unpopular policy changes ... which they themselves feel are necessary for the longer term good of the country.

### Peer review as peer pressure

The third aspect of peer review is where the peer review process seeks to make a country do something that it does not want to do. I would argue that this rarely if ever works, unless the policy is actually in the interests of the reviewed country. This then begs the question 'if it is really in the interests of the reviewed country, then why do they not do it in the first place?' It also raises the question 'why would the peer reviewer be better placed to know what is in the best interests of the reviewed country?'

There are many ways to think about this question. However, a useful way to think about this may be to reflect on Yew Kwang Ng's (1983) taxonomy as to why people disagree. Ng argues that there are three reasons why people disagree. First, people can differ in their basic value judgments. Second, people can differ regarding statements of fact. Third, people can make errors of logic. My belief is that the third category is rarely the reason for prolonged differences of opinion, at least at the level of policy. Accordingly, differences are likely to arise over the first two elements.

Turning to the first element, it is possible that different countries may genuinely seek different objectives. I believe that if this is the case, then peer review should respectfully note the different objectives and limit any comments or suggestions to how these objectives can be met in the most effective manner. In this area, one does need to be very careful. It is not uncommon that objectives are stated that are not ultimate objectives. Once these objectives are appropriately clarified, generalised and reformulated, then there is often scope for constructive policy dialogue.

For example, OECD (2004) has a very good discussion of policies to promote recycling. Many countries have quantitative targets for the volume of recycling. If these targets were interpreted as the objectives of policy, then there would be little scope to discuss

the merits of the policy. However, if the objective is really to promote environmental amenity, then there is scope for constructive dialogue of whether quantitative recycling targets are the best instrument for pursuing this broader goal. Indeed, the OECD concluded, and by a process of consensus the countries accepted, that there were better ways to achieve the broader environmental goal.<sup>4</sup>

Ng's taxonomy relates to why individuals disagree. However nations are not individuals. Accordingly, an additional related source of difference may be that different countries place different weights on the importance of furthering different groups, or that political rules may advantage one group over others. Again, if this is genuinely the case, then peer review should restrict itself to suggesting policies that may better achieve the given objective or improving transparency to empower domestic stakeholders with information about the effects of current arrangements.

The second element lends itself to exchange of information. In particular, certain country specific factors may mean that critical facts differ, leading to quite different policy conclusions. For example, I would argue that the extent of product market reform in Australia has meant that labour markets operate more efficiently than might be guessed from the state of labour market regulation. Product market reform has squeezed economic rents out of the system, requiring labour market actors to behave in a manner that is consistent with a highly resilient and growing economy. However, I should be wary in applying this lesson of Australian economic reform to other countries. Some other countries may believe that labour markets should be reformed first as the interaction of liberal product markets with unreformed labour market institutions may lead to even more restrictive measures being sought by labour market actors.

Perhaps more concretely, a Scandinavian may be relatively relaxed about high marginal tax rates on labour income, judging the international mobility and hence the labour supply elasticity of high income earners to be low. An Australian or New Zealander may take a different view based on a concern that the English-speaking labour market provides a powerful pull factor that cannot be ignored.

With respect to this last point, it becomes clear that peer review as peer pressure may really be just another form of peer review as peer learning. The process of peer review may convince a country that what they thought was in their interest is not. But it must be stressed that the country must be convinced on the merits of the case unless there are possible sanctions outside the peer review process. For the moment I will not pursue this, but merely note that introducing sanctions in my view takes us out of the

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4 Comley (2007) provides a fuller discussion of these issues in the context of reform of environmentally harmful subsidies.



realm of pure peer review. Indeed sanctions may significantly hamper peer review by inhibiting the free flow of information that is integral to genuine peer review and support.

### Conditions under which peer review works well<sup>5</sup>

The foregoing discussion implies a number of conditions that are required for peer review to work well:

- first, there must be a high degree of trust and respect between the parties to the peer review;
- second, parties must be prepared to share information freely and openly;
- third, the peers must have at their disposal sufficient analytical and administrative capacity to conduct the peer reviews;
- fourth, the peers must be seen to have legitimacy in the eyes of domestic constituents; and
- fifth, the reviewed country counterparty must be seen as legitimate in the eyes of the domestic constituents.

### Peer review in the context of regional integration

The premise that I asserted at the start was that peer review is based on the idea that it is in all countries' interests for another country to be economically successful. This is true in general, but is an even stronger proposition in the context of regional economies where economic geography suggests that interests are more intertwined.

In principle peer review in the context of regional integration is no different to peer review elsewhere. However, depending on the nature of the regional integration project peer review may be more or less difficult to conduct successfully.

I do not want to go through the conditions for successful peer review in an exhaustive manner. Readers will have in mind their own examples of regional integration projects. Proximity may lead to greater trust and openness, but it may also mean that long-standing historical differences and grievances may exist. Near neighbours may be

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5 Kanbur (2004) outlines three broad criteria for successful peer review: competence; independence; and competition. OECD (2003) outlines four elements: value sharing; commitment; mutual trust; and credibility.

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seen as informed and legitimate reviewers, or to be too coloured by their own national interests to constructively enter into a dialogue.

There is one issue that I would like to focus on – the role of potential sanctions in peer review. It is worth looking at the list of conditions for successful peer review and asking ‘how would the existence of potential sanctions affect the peer review process?’

My answer to this would be that it would almost certainly diminish the usefulness of peer review. As the OECD (2003) has noted,

... peer review is a discussion among equals, not a hearing by a superior body that will hand down a binding judgment or punishment. A state may be more willing to accept criticism, and its neighbours to give it, if both sides know it does not commit them to a rigid position or obligatory course of action.

Perhaps more importantly, a peer is much less likely to share information if they believe that the information may be used against them now or in the future. In terms of the taxonomy of peer review, sanctions may cripple peer review as peer learning and peer review as peer support and leave only the weak limb of peer review as peer pressure. Further, once the voluntary flow of information from the reviewed country dries up, then peers would have to ramp up the resources used to conduct the review. This could leave to a vicious cycle of limited disclosure, intrusive questioning and even weaker trust. Kanbur (2004) makes a similar point when he states that,

... IMF reviews work like OECD reviews in rich countries not using IMF resources, but not so in poor countries dependent on them. When a review is, or is perceived to be, the ‘only game in town’, or ‘too big a game in town’, the high stakes set up dynamic pressures that can undermine trust.

The same lesson flows from the experience of the World Bank, where analysis of desirable policy reform and recommendations are usually bundled with International Development Association or International Bank for Reconstruction and Development lending programmes at more or less attractive interest rates. The experience of recent decades is that there have been few development successes from trying to ‘buy’ reforms through concessional lending and policy conditionality; the key ingredient of success is ‘country ownership’ of the need to make the reform in question (World Bank 2005).

One could argue that attempts to ingrain peer review in the European Union have been hampered by exactly this issue. Peer review within the European Union cannot escape the fact that the legal structure of the Union constrains the actions of the member states. Countries must always be wary that information disclosed in one context may be used elsewhere. The open disclosure of information is not encouraged.

If a country is not prepared to air its faults, then even well intentioned observers are unlikely to be able to help.

Naturally, the European Union is a special case of regional integration. It is a model that has moved well beyond information exchange and cooperation given its myriad common policies and well-developed institutional architecture. Accordingly, other experiments in looser integration projects with the absence of sanctions have less to fear.

In contrast the prospects for peer review in the Asian context do not appear to be hampered by the formal structures of legalistic integration. Accordingly, there appears ample scope for well designed peer review, focusing on respectful peer exchange to contribute to domestic policy development.

## Conclusion

Peer review can be thought of as having three aspects – peer learning, peer support and peer pressure. Durable peer review processes focus on peer learning and support. Peer pressure rarely works unless countries can be convinced that a policy is in their national interest. Viewed through this lens, successful peer pressure should best be thought of as another form of peer learning – a peer learning where the country may initially be unconvinced of the merits of the case.

Peer review may be more or less difficult in the context of regional integration. In principle peer review could be a useful adjunct to other aspects of a regional integration strategy designed to bring mutual benefit to the participating countries. However, where regional integration projects involve deepening legal and economic commitments it is important to disentangle sanction regimes from peer review to ensure that the free disclosure of information is incentive compatible.

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