Developing countries **must lead the way**

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Roundtable on UN Development in Response to Financial Crisis

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While the outcome document of the recent United Nations conference is a strong statement of commitment by all UN member states to address some of the critical issues facing developing countries, the realisation of real solutions to these problems will very much depend on how developing countries lead the process for change.

For the developing countries, the objective of the UN's economic crisis conference was threefold:

- to reaffirm their need for adequate policy space in order to respond to the fallout from the crisis

- to discuss and reach an agreement on immediate policy actions to be taken by the international community in support of developing countries
- to identify shortcomings in the global financial architecture with a view to addressing them in a follow-up process in the UN.

Whether or not this agenda was initially shared by the governments from advanced economies, the outcome document, agreed by consensus, addresses all three, albeit with varying degrees of satisfaction.

On policy space, the document unambiguously recognises the right of developing countries facing severe shortage of foreign reserves because of the fallout from the crisis to use legitimate trade measures in accordance with relevant World Trade Organisation provisions. This presumably includes the right not only to raise tariffs within WTO-bound rates, but also to make recourse to balance-of-payments safeguard provisions. Perhaps more significantly, it recognises the right to impose temporary restrictions over capital outflows – something that is fully consistent with the International Monetary Fund (IMF) Articles of Agreement.

Regarding debt servicing, the document recommends negotiations with creditors for voluntary standstills. It does not go far enough in this respect; even the IMF board had recognised in 2000 that "in extreme circumstances, if it is not possible to reach agreement on a voluntary standstill, members may find it necessary, as a last resort, to impose one unilaterally".

INTERNATIONAL MEASURES

On international support measures, agreement could not be reached on the specific proposals made by the G-77, which had sought unconditional and adequate liquidity provision. These included a $100 billion no-cost special drawing rights (SDR) allocation (that is, international money-printing) for low-income countries (LICs) and a moratorium on their official debt, including deferral of principal and interest payments with no additional cost. For other developing countries, the G-77 had proposed a reversible SDR allocation of $800 billion, to be repurchased when the crisis is over.

> For the low-income countries, such an allocation would provide $70 per head. This compares with the $8 000 per head that the US has so far spent to deal with the crisis at home.

UN Photo/ Sophie Paris

These were sensible proposals, based on the most recent estimates of the Bretton Woods institutions of the likely foreign exchange shortfalls in developing countries. They would constitute "quantitative easing" at the global level, reinforcing similar actions already undertaken by some advanced countries at the national level. For the LICs, such an allocation would provide $70 per head. This compares with the $8 000 per head that the Unites States has so far spent to deal with the crisis at home. A moratorium on official debt is a part of the existing debt framework and has been used in the past, for example after the Asian tsunami. The SDR allocation to other developing countries draws some concern over possible inflationary impacts. However, this would not be the case now, or in the future, because reversibility means a built-in exit from liquidity expansion – a feature missing in recent intervention packages in the US and the European Union.

It is therefore quite disappointing that the conference could not reach agreement on these sensible proposals. This is not, however, the end of the issue. Since there is a follow-up process, these matters can be taken up and decided upon in coming months, perhaps as the first item on the agenda of the working group, particularly if it turns out that there are many more yellow weeds than green shoots in the global economy.

SYSTEMIC REFORM?

On systemic issues, the document is quite comprehensive. It recognises that the international economic system and financial architecture suffer from serious shortcomings. It identifies problems but, rightly, does not attempt to provide blueprints for solutions. This is left to the follow-up process.

It recognises the incoherence of the global economic system and the role of the UN as a co-ordinating body, even though the exact form such co-ordination could take is a contentious issue that is likely to give rise to heated debate over coming months. It further recognises that the mandates, policies and governance of international financial institutions, notably the International Monetary Fund, require an urgent reform. In fact, it puts a specific deadline for governance reform – something quite unprecedented. There is also a clear recognition that IMF surveillance needs to be even-handed and effective.

However, reference here is to surveillance over "major financial centres, international capital flow and financial markets", but not over the policies of systemically important countries. This is an area in which the IMF has constantly failed. The G-20 summit expressed its support for "candid, even-handed, and independent IMF surveillance", but without making specific recommendations as to how this could be achieved.

The document points to calls for reform of the existing international reserve system and recommends exploring the scope for a greater role for the SDR. Cognisant of the fact that countries enjoying reserve-currency status, notably the US, are unlikely to give it up voluntarily, it calls for consensus over methods and parameters of such an exploration. But it also points to regional arrangements which many developing countries have started to view as an alternative option in the event of failure to reform the global system.

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Several references made to debt sustainability in developing countries, including the threat that the current crisis poses, constitute a recognition that the initiatives pursued since the launching of the heavily indebted poor countries (HIPC) debt relief initiative in the mid-1990s have amounted to no more than a muddling-through process, unable to find a lasting solution. Although the document talks about seeking solutions "based on existing frameworks and principles", it is certainly cognisant of the fact that these may need to be significantly reformed to address the debt overhang – through what it calls "a more structured framework" which should, presumably, include orderly international debt workout mechanisms. Even though the document shies away from mentioning it explicitly, it has all the elements that could open the door to negotiations over such a mechanism in the follow-up process.

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AVERSION TO REGULATION

The document puts much less emphasis on global regulation of financial markets and institutions than is found in the debate in the civil society and academic communities. While the need for effective regulation and supervision is clearly recognised and recommended, the document expresses an unambiguous preference for national over international regulations. This is not just a reflection of a strong US aversion to multilateral disciplines in such areas. Many developing countries are concerned that a process designed to broaden the scope of global governance over finance may end up extending the global reach of financial markets, leading to a one-size-fits-all approach and considerable loss of policy autonomy for them, particularly when governance-related problems that pervade the multilateral system continue unresolved.

Briefly, the document is a strong statement of commitment, by all members of the UN, to actively engage in a common process of finding solutions to these three immediate concerns of developing countries, as well as other related issues. Whether it will lead to a structured negotiation over the international monetary and financial architecture or simply degenerate into the kind of hapless exercise typified by the UN Financing for Development (FFD) process remains to be seen. This very much depends on the extent to which developing countries own and lead this process. Perhaps there are reasons for optimism since, for the first time after recurrent crises and hardships, developing countries have begun to fashion a common vision of what kind of international monetary and financial architecture they should be seeking in support of development, rather than simply reacting to positions and proposals coming from governments of advanced economies.