Joint Government/NGOs Roundtable on Multilateral Development Banks

JUBILEE AUSTRALIA
drop the debt

AGENDA PAPER, 3 April 2009

Reform of IMF Macroeconomic policies

No new money should flow to or through the IMF without the achievement of significant, verifiable changes in Fund policy.

In response to the following clauses in the *G20 London Summit Leaders' Statement, 2 April 2009*:

Clause 17: Emerging markets and developing countries, which have been the engine of recent world growth, are also now facing challenges which are adding to the current downturn in the global economy. It is imperative for global confidence and economic recovery that capital continues to flow to them. This will require a substantial strengthening of the international financial institutions, particularly the IMF. We have therefore agreed to make available an additional $850 billion of resources through the global financial institutions to support growth in emerging markets and developing countries by helping to finance counter-cyclical spending, bank recapitalisation, infrastructure, trade finance, balance of payments support, debt rollover, and social support. To this end:

- We have agreed to increase the resources available to the IMF through immediate financing from members of $250 billion, subsequently incorporated into an expanded and more flexible New Arrangements to Borrow, increased by up to $500 billion, and to consider market borrowing if necessary; and
- We support a substantial increase in lending of at least $100 billion by the Multilateral Development Banks (MDBs), including to low income countries, and ensure that all MDBs have the appropriate capital.

Clause 18: It is essential that these resources can be used effectively and flexibly to support growth. We welcome in this respect the progress made by the IMF with its new Flexible Credit Line (FCL) and its reformed lending and conditionality framework which will enable the IMF to ensure that its facilities address effectively the underlying causes of countries' balance of payments financing needs, particularly the withdrawal of external capital flows to the banking and corporate sectors.

The extraordinarily serious global economic crisis has its origins in the developed countries. Developing countries are not responsible, but they are severely affected, and in ways that are worse than the developed countries, as they also lack the means to counter the effects.

In the past, developing countries have not been given policy space to pursue the kind of expansionary policies they need to pursue at such a juncture of crisis. Thirty years ago, a much less severe global economic downturn began a debt crisis that has thwarted and even rolled back development in many countries of Africa, Latin America and Asia for two decades, with an extremely high social cost. The IMF was at the centre of this market driven policy disaster. It would be tragic to repeat history.

Infusing the IMF and MDBs with an additional $850 billion of resources will not achieve the necessary development and anti-poverty impacts unless it is accompanied by substantive reforms to the practices of the international financial institutions (IFIs).

Although the G20 communiqué states that the resources will be made available to support "growth in emerging markets and developing countries by helping to finance counter-cyclical spending, bank recapitalisation, infrastructure, trade finance, balance of payments support, debt rollover, and social support", there is no decisive break with the economic policy conditionality that has partly caused this crisis and which seriously aggravated the social impact of previous financial crises

Analysis of the nine most recent IMF loans to countries affected by the crisis clearly demonstrates that the Fund is still prescribing pro-cyclical policies of fiscal and monetary policy tightening. The IMF's crisis loans still contain the old policy conditions of reducing public sector expenditure, reducing fiscal deficits and increasing interest rates – which is in stark contrast to the expansionary, stimulus policies being supported in the G20 countries.

Recommendations:

The IMF macroeconomic policies in low-income countries must be substantially reformed, and aligned to support efforts to scale up education and health sectors in the world's poorest places.

I) No new money should flow to or through the IMF without the achievement of significant, verifiable changes in Fund policy including:

- more macroeconomic flexibility, regarding both fiscal and monetary policy for developing countries
- a guarantee that countries will have flexibility to expand healthcare and education spending, irrespective of budget caps;
- a prohibition on financial deregulation as an IMF conditionality or policy recommendation.

II) The IMF should separate the provision of grants and loans from technical assistance and policy advice.

Notes:

UNITED NATIONS PROPOSALS: Commission of Experts of the President of the General Assembly on reforms of the international monetary and financial system, Recommendations, 19 March 2009

<u>Developing Countries need more policy space</u>

Clause 36: There are asymmetries in global economic policies—countercyclical policies are pursued by developed countries, while most developing countries are encouraged or induced to pursue pro-cyclical policies. While this is partly due to the lack of resources to pursue countercyclical policies, it is also due to misguided policy recommendations from international financial institutions. Conditionality attached to official lending and support for international financial institutions has often required developing countries to adopt the kinds of monetary and regulatory policies which contributed to the current crisis. In addition, these conditionalities contribute to global asymmetries, disadvantage developing countries relative to the developed, and undermine incentives for developing countries to seek support funding, contributing to global economic weakness. While the IMF initiatives to reduce conditionalities are to be commended, they might be insufficient, while in many cases countries are still required to introduce pro-cyclical policies.

<u>Lack of coherence between policies governing trade and finance must be rectified</u>

Clause 37: Policy space is circumscribed not only by a lack of resources, but also by international agreements and by the conditionalities that often accompany assistance. Many bilateral and multilateral trade agreements contain commitments that circumscribe the ability of countries to respond to the current crisis with appropriate regulatory, structural, and macro-economic reforms and rescue packages, and may have exposed them unnecessarily to the contagion from the failures elsewhere in the global economic system. Developing countries especially need policy frameworks that can help protect them from regulatory and macro-economic failures in systemically significant countries. Developing countries have had imposed on them not only deregulation policies akin to those that are now recognized as having played a role in the onset of the crisis, but also have faced restrictions on their ability to manage their capital account and financial systems (e.g. as a result of financial and capital market liberalization policies); these policies are now exacting a heavy toll on many developing countries.