

Statement by José Antonio Ocampo, Professor, Columbia University and former Under-Secretary-General of the United Nations for Economic and Social Affairs, in the UN Hearings with Civil Society on Financing for Development, representing the New Rules for Global Finance Coalition and the Initiative for Policy Dialogue of Columbia University

Let me express my great satisfaction for participating in these hearings leading to the Doha follow-up of the Financing for Development Conference, and to be back at the United Nations, now representing civil society.

The systemic agenda that is addressed in chapter VI of the Monterrey Consensus covers two broad set of issues: the functions of the international monetary and financial architecture, and its governance structure. With respect to the first of these issues, we can broadly define four functions: (1) guaranteeing that national macroeconomic policies are consistent with the stability of the global economic system, and avoiding the adverse effects that macroeconomic policies of individual countries could have on other nations; (2) designing appropriate transparency and regulation of international banks and capital markets, and adequate regulation of domestic and international financial systems, including cross-border capital account flows; (3) providing sufficient international official liquidity in crisis conditions; and (4) designing standstills and orderly debt workouts mechanisms at the international level for managing problems of over-indebtedness. With respect to the governance structure, I will focus here only on the fair representation of developing countries in international economic decision making and the role of regional arrangements.

The Asian crisis and its spread throughout the world unleashed a high level of attention to many of these issues. Indeed, the Monterrey Consensus is part of that process, and its great virtue is that it provided for the first time an agreed framework for the reform of the international financial system and its development implications. A decade later, however, we face the worst macroeconomic imbalances of the post-war period, large turbulence in developed countries' financial markets, linked to a clear and outstanding regulatory deficit in world finance, and the International Monetary Fund is facing the worst crisis in its history. The follow-up to the Monterrey Conference on Financing for Development should therefore be seen as an opportunity to generate new momentum for reform of the international monetary and financial architecture.

The major deficiency of the current system in the macroeconomic area is the large reliance of the global reserve system on a *national* currency, the US dollar. This system is not only inequitable, as it confers excessive privileges to one country in terms of seignorage powers and monetary policy autonomy, but also unstable, as it leads to cyclical swings in the confidence in the major reserve currency, a dramatic phase of which we are living today. Let me say, however, that a system based on competing reserve currencies from industrial countries, say the US dollar and the euro, would not only continue to be inequitable but may be even more unstable, as the world economy lacks mechanisms of macroeconomic policy coordination and is thus subject to large exchange rate swings among those currencies. Mechanisms for global policy coordination have been not only ad-hoc (the G8 today) but also weak. These inherent

deficiencies of the global monetary system can only be solved by reliance on a true global reserve currency and the creation of stronger mechanisms of macroeconomic policy coordination. In the redesign of the International Monetary Fund, these issues should be high on the agenda. The SDRs are, indeed, the only global reserve currency, so far considerably under-utilized, and the “multilateral surveillance” mechanisms launched by the IMF a couple of years ago may be seen as the seed of a new global macroeconomic policy coordination framework, though its results so far have been largely frustrating.

The ongoing US financial crisis has made us all conscious of the large regulatory deficit that characterizes world finance. The major step forward after the Asian crisis was the strengthening of prudential regulation and supervision in developing countries. But the major industrial centers, and thus global finance, faces significant gaps in regulation associated, among other things, to lack of transparency and regulation of derivatives markets and hedge funds, of banks’ off-balance sheet transactions, of the risks associated with the issuance of asset-backed securities, and of the lack of regulation of rating agencies. To this we should add the lack of focus of the Basle Committee on Banking Supervision on the major failure that characterizes financial markets: excessive risk-taking during macroeconomic booms. This means that a counter-cyclical focus should be built into world financial regulation, an issue that absent from the existing agenda. Further, given that capital is increasingly global in character, a claim can be made that we need to create a truly global regulatory institution or mechanism.

The Asian crisis led to a series of important innovations in IMF financing: the creation of the Supplemental Reserve Facility and the Contingency Credit Line. The latter was correctly seen as a preventive line to manage pro-cyclical swings in capital flows, but was never used and was soon discontinued. A new framework for lending to low-income countries has also been put in place. A troublesome feature was the excessive conditionality that continued to characterize all forms of lending. This includes the compensatory financing facility that could play an important role in the face of record oil and food prices, but which has ceased to be used due to excessive conditionality. The need for agreed rules on the limits of conditionality as well as a preventive credit line for capital account crises continue to be, therefore, major deficits in this area. These two factors are largely behind the large build up of foreign exchange reserves by developing countries, as a form of “self-insurance” in response to the lack of collective insurance provided by the world monetary and financial system, as well as the limited demand for IMF funds to avoid its overburdening conditionality. Although positive from the perspective of these countries, such a build up has contributed to global macroeconomic imbalances.

The initiatives to manage over-indebtedness of poor countries, the Heavily Indebted Poor Countries (HIPC) and the Multilateral Debt Relief (MDRI) Initiatives must be seen as a bright spot in the global agenda of the last decade, though their effects have been insufficient for many countries. The Paris Club continues to play an important role for official financing, though it has not overcome its traditional reliance on sequential rescheduling, which means that debt overhangs affect developing countries for excessively long periods. The generalization of collective action clauses in bond issuance

is also a step forward. However, the lack of a regular institutional framework to manage debt overhangs at the international level –i.e., an international debt court similar to those created to manage bankruptcies in national economies, the decisions of which are legally binding—is one of the major deficiencies of the current global system. One of its effects is the tendency to rely on ad-hoc mechanisms such as the HIPC and MDRI Initiatives, and the Baker and Brady Plans in the 1980s, as well as traumatic individual debt renegotiations.

Finally, let me just point out two issues in relation to governance. The first is that the Monterrey Consensus was a major step forward in calling for broadening and strengthening the participation of developing countries and economies in transition in economic decision-making and norm-setting. The discussion of this issue in the Bretton Woods institutions is a step forward, including the decision taken this spring on quotas and basic votes in the IMF, even though the latter was only a modest first step of a longer-term process. But let me underscore that the Monterrey Consensus applies to many more institutions, such as the Basle Committee on Banking Supervision and many other norm-setting bodies in which developing countries have no representation. The second is to underscore that, in this area, developing countries also have part of the solution in their hands, through the creation of regional and sub-regional institutions. The major advance in this area has been the Chiang Mai Initiative of ASEAN+3, and the Latin American Reserve Fund is an older mechanism of its kind. A better and more equitable international system to manage finance must rely on a dense institutional network, which includes strong global, regional and national institutions. The regional dimension is crucial in this mix, particularly for smaller countries. In this light, the large foreign exchange reserves of many developing countries may be seen as an opportunity to create or strengthen these initiatives

This is, of course, an ambitious agenda, but the challenge of the follow-up to Monterrey is to put in place the comprehensive agenda that is already part of the Consensus, and to face the several emerging issues that have come up since its adoption in 2002.

I thank you very much for your attention.