

**Concluding Statement by
Jomo Kwame Sundaram at the Workshop On
'Debt, Finance And Emerging Issues In Financial Integration',
Commonwealth Secretariat, London, 7 March 2007**

I would first like to thank the organizers, the Financing for Development Office, especially Benu Schneider for the fine job of putting all this together. A special word of thanks to all the partners involved: Commonwealth Secretariat, Commonwealth Business Council, for your work and cooperation in this matter.

As you know, the General Assembly has decided to have a follow-up conference to Monterrey towards the end of next year. This offers a very important opportunity to revisit and build on The Monterrey Consensus. Monterrey, in retrospect, represented an important point of departure from what might be termed the "Washington Consensus".

But to continue to be meaningful and relevant, this should be an ongoing process. We cannot just stop in 2002, or we will be quickly overtaken by events and new developments, especially in the very innovative field of finance.

This then is the time for us to look ahead as to how we might revisit old issues and build upon them to address new challenges. Hence, the convening of this workshop is particularly helpful in this regard.

Let me just remind you of the issues for which commitments were made at Monterrey and then hint at some issues where we might look ahead.

First is the issue of mobilization of domestic resources. One key assumption in traditional thinking about the relationship between savings and investments is that the major challenge is to create the incentives to raise domestic savings. Thankfully, there is now greater recognition that the key issue is raising investments, with savings (and finance) following investments, instead of expecting savings to lead investments.

The challenge of improving incentives to invest has to be examined and looked at in context. The orthodox view now seeks to strengthen property rights. But there is a great deal of evidence of effective incentives despite ill-defined property rights. Despite the ambiguity of weak private property rights – e.g. in China, the incentives to improve agricultural production in the 1980s and to invest in township and village enterprises (TVEs) until the mid-1990s -- credible and strong incentives ensured the investments deemed necessary or desirable.

A very closely related issue is the whole question of the functional distribution of income which has very important implications for "investible" resources, who is likely to invest and why.

At the UN, much more work has to be done to advance international cooperation on taxation in order to reverse the current race to the bottom as governments lower taxes to attract investors with 'beggar thy neighbour' consequences. All too often, developing countries' capacity to tax has been greatly undermined with the reforms which have taken place over the last couple of decades. The ability to overcome such

problems is extremely important for restoring fiscal space and government capacity to act developmentally and equitably.

Another challenge is how we move from what has been a vicious cycle into a more virtuous cycle involving growth and the creation of employment. Here, there are at least two issues:

In the last half decade, there has been more growth in many developing countries, but this has had very little to do with preceding economic reforms. We have to better understand what made this recent growth possible, including higher commodity prices as well as lower interest rates, and how to sustain it.

But on the downside, we must also recognize that recent growth has not been accompanied by commensurate improvements in employment. We all know there can be no sustainable reduction of poverty without employment expansion. There is recent attention in ECOSOC and the ILO to the employment implications of recent economic growth, but we need to give this much more attention.

A second area where the debate has settled significantly in recent years is trade. There is now general agreement, including World Bank research, that further trade liberalization offers very modest, one-shot output gains, mainly for the few leading agricultural and manufacturing exporters, with adverse consequences for others including the reduction, if not the elimination of existing productive capacities in manufacturing as well as agriculture. The implications for poverty reduction are even more dire. For countries just beginning to develop, to industrialize, to develop productive capacity, premature trade liberalization will reverse the developmental process.

Recently, there has been a great deal of interest in Aid for Trade. But there is a real danger that AFT will be diversionary by diverting funds which might otherwise go for other purposes and allocating them specifically for AFT. Given the recent track record of aid flows, in contrast to rhetoric, this is something we should especially be vigilant about.

The aid for trade discussion has involved unprecedented recognition of three important issues for which developing countries need compensation and assistance. Serious trade economists have long recognized the need to compensate and make provisions for those who will be adversely affected by trade liberalization. For example, the beginning of the Kennedy round in the 1960s required a deal between US business, government and labour -- to ensure that trade liberalization would not adversely affect organized labour in the USA -- negotiated between the new US President Jack Kennedy and the AFL-CIO chief George Meany. We now have to think about such deals at the global level and what this implies in the present period especially for developing countries who do not have the means to make such compensatory payments to losers.

For many of the poorest countries, tariff incomes have been the most significant source of tax revenue. The tremendous collapse in tariff revenue and productive as well

as export capacity due to trade liberalization have to be compensated. Compensation for loss of tariff revenues and reduced production capacities as well as productive employment opportunities have to be made for past and future trade liberalization.

The third element arising from the aid for trade discussions may be seen as more developmental. The development of new capacities and capabilities requires a fairly long gestation period in most instances and usually needs facilities and incentives to induce private investments including public infrastructure as well as social services to improve the quality of human resources.

Given the nature of the preceding discussion as well as the time constraints we face, I will not review the two p issues of Debt and Aid.

Instead, let me quickly turned to remittances. There has been an ongoing effort in recent years by some countries and institutions to promote remittances as a substitute for aid. Correspondingly, facilitation of remittances is sometimes seen as an alternative to fulfilling aid obligations. We have to be vigilant, not least because there are all kinds of issues involved in remittances which are quite different from aid, but this has to be linked to ongoing debates on international migration, etc.

In recent years, there has been some welcome interest in exploring innovative sources of financing. And there has, in fact, been some modest progress in some countries in Europe and Latin America. It is important to consider the analytical, egalitarian and counter cyclical potential of some of these innovative sources of financing, but there is an unfortunate tendency to overstate some claims in this connection, as the late Jim Tobin warned in connection with the so-called Tobin tax. Well-meaning proponents of the tax have made great claims, not only to finance global public goods, but also to prevent future financial crises. These claims are sometimes exaggerated, and we have to be rigorous and balanced in such discussions.

In connection with current concerns about global warming and climate change, there are likely to be proposals for new carbon taxation and trading initiatives as well as greater compensation to reduce deforestation, but we have to ask some tough questions about the inadequacy of existing arrangements while recognizing the successes that have occurred.

In connection with the fifth issue of private capital flows, big generalizations have been made. Actual situations are often very complex and sometimes fast changing. How often do we hear that while portfolio flows may not be desirable, in contrast, FDI is desirable without any reference to the distinction between brown field FDI (mergers and acquisitions) and green field FDI. As is now well-known, the evidence suggests that mergers and acquisitions have little to do with improving efficiency. Instead, size matters, as a lot of recent work on corporate governance reminds us.

The final matter to mention here is actually a bundle of issues often referred to as systemic issues implying the interconnected nature and consequences of international financial arrangements and relations. For instance, advocates have claimed that international financial liberalization and integration will bring about a net

flow of funds from the capital rich to the capital poor, lower the cost of funds as well as reduce volatility and instability in the international financial system through financial deepening.

But as far as international capital flows are concerned, with the capital account liberalization that has taken place, the net flow of funds has actually not been from North to South, or from the capital rich to the capital poor; instead, the converse has been true. Harvard University Professor Ken Rogoff, former chief economist of the IMF, recently told the UN that the United States has the largest single foreign aid programme -- but as recipient, with countries buying dollar denominated Treasury bills despite the low interest rates and the declining exchange-rate of the greenback. But even before this relatively recent phenomenon, most developing countries, including most in Africa, experienced net outflows of billions of dollars every year. It is true that some fast-growing emerging markets have succeeded in temporarily attracting a great deal of funds, only to experience sudden massive reversals, in turn exacerbating financial crises.

I suggested earlier that recent growth in developing countries has been due not only to higher commodity prices accompanying oil price increases, as in the mid- and late 1970s, but also to the reduction of the cost of funds in recent years due to low interest rates in the United States and greater liquidity with the availability of petro dollars and huge Asian trade surpluses. This recent period has been good for economic growth, but it has undoubtedly been exceptional. And there is no evidence whatsoever that it has been due to the financial liberalization which has taken place in the preceding period, as is sometimes claimed.

Let me now turn to the third claim of reduced volatility and improved stability with the deepening of financial markets. Recent IMF research suggests otherwise. Rogoff -- who once criticized Stiglitz for having a "Beautiful Mind" a la John Nash for being paranoid about the role of the IMF -- has acknowledged that financial globalization has not contributed to economic growth, but instead has exacerbated volatility and instability.

Four other consequences of the last couple of decades of financial liberalization are important for us to be mindful of because of their adverse implications for sustaining economic development. While there is a general consensus against very high rates of inflation, there is also widespread concern about the contractionary consequences of deflationary influences on macroeconomic policy due to lobbying by financial interests. The weakening of productive sectors has resulted in the growing influence of financial interests, with such adverse consequences for macro-economic policy in much of the developing world. We all want growth and do not want inflation, but there are difficult trade-offs here which we need to think about seriously.

The undermining of counter-cyclical macroeconomic policy capacity, with the discrediting of Keynesian economic thinking from the 1970s, also needs to be revisited,

especially given the greater vulnerability of most developing countries to the vicissitudes of the global economy and various kinds of business cycles.

The last Nobel Prize for Peace to the micro-credit pioneer, Professor Muhammad Yunus of the Grameen Bank in Bangladesh, has given greater prominence to the broader, but related question of inclusive finance. The main focus of modern financial systems has been on credit for big corporations. More recently, there has been some interest in micro-credit, sometimes touted as a miracle cure-all for poverty. Unfortunately, there has been very little recognition of the financial and credit needs of those in between. In this connection, we need to have a much more inclusive and broad-based approach. If one is serious about developing dynamic enterprises, and larger firms have their needs met by domestic credit sources and have access to international financial markets, an immediate priority should be affordable credit provision to medium-sized and small enterprises.

The last point to make in this connection is the urgent need to revisit development finance. There have been a lot of stories of failure associated with developmental finance, e.g. with national development banks. But we run the risk of “throwing the baby out with the bath water” by neglecting the challenges of improving development finance institutions to fulfill the tasks for which they were first conceived.

Allow me to make four other points. First, there is a growing and widespread sense that crisis prevention is no longer an urgent issue because we have not had a major crisis for some time. Unfortunately, there is nothing like a recent catastrophe to remind us of the urgent need to strengthen crisis prevention efforts. But the severity of recent crisis experiences reminds us that we cannot afford to be too complacent. I am not suggesting another crisis around the corner, but there is little disagreement about how vulnerable we are and the inadequacy of existing crisis prevention arrangements. Almost 10 years ago, during the Asian crisis, countries like Laos, which did not get any of the financial inflows into the region, were nonetheless devastated for being in the wrong neighbourhood due to the effects of contagion from neighbouring Thailand.

Thankfully, Germany, the host of the next G8 meeting, has put problems raised by hedge funds on the agenda. Nowadays, nobody buys the old claim that hedge funds were completely irrelevant in the 1997-1998 East Asian crisis. Today, hedge funds are far more significant than they were a decade ago. There are a whole range of other related issues one should look at, not only in connection with hedge funds but also, other sources of vulnerability.

As for the related challenge of crisis management, we need to know much more about how to deal with crises and to mitigate their adverse consequences while expediting sustainable recoveries.

The next issue is the question of international economic governance, where developing countries are fighting a battle which would be considered almost farcical if it was not happening right before our eyes. The IMF staff have offered to double the basic vote -- shared equally by all members, and thus favouring developing countries --

to 4.3 per cent. When the Fund was created in 1944, it had 44 members, who shared 11.3 per cent of the total vote in the form of basic votes. And now that there are 184 members, you would think that they might quadruple the share of the basic vote is, but instead, we have a diminution to 2.2 per cent! Hence, the developing countries have been unable to improve their lot because of their very weak voice in the Fund and the Bank. Only the international community can exercise moral suasion to fundamentally change this incredible inequity at the beginning of the 21st century.

Another proposal in this context is to promote regional monetary and financial cooperation. Some of the more exuberant hopes in 1997-1998, e.g. the idea of an Asian Monetary Fund, are now considered non-starters. But that does not mean we should be content with the modest Chiang Mai compromise, with its almost dysfunctional arrangements. We really need to think more boldly about alternative financial initiatives at the regional level, and there is much we can learn from each other, not only from the European experience, but also from other regional experiences in the developing world.

Lastly, two years ago, at the end of 2005, the heads of states at the United Nations made a commitment to support National Development Strategies to achieve the internationally agreed development goals, including the MDGs. That was a very important commitment, reinforcing and updating the Millennium Declaration of 2000. President Bush came to the meeting saying he felt humbled that from 9/11 to Hurricane Katrina, it had been the international community that had consistently rallied to America's aid at its moments of need. Perhaps mid-September 2005 was a very special and exceptional moment, but President Bush signed on to these commitments. It is a very unusual commitment which broadens the scope of what was achieved by UNCTAD 11 in Sao Paulo 2004, where there was a commitment to try to expand policy space in line with a greater commitment to 'national ownership'.

We really need to think seriously about what this means in terms of true national ownership because, as you all know, almost 80 percent of the Poverty Reduction Strategy Papers have nothing to say about employment. I do not know how such Poverty Reduction Strategies as well as the World Bank's country assessments expect to reduce poverty without creating decent jobs. We are really obliged to think seriously about viable and feasible alternatives. The G24, G77 and other such organizations are trying to do something. All of you here and the organizations you represent can contribute to this noble effort with your collective wisdom and experience. Clearly, there is much to be done in the year ahead as we prepare for Doha 2008.