INTERNATIONAL FINANCIAL ARCHITECTURE: MACROECONOMIC POLICIES & SYSTEMIC ISSUES FOR SOCIAL AND ECONOMIC JUSTICE

TWN – THIRD WORLD NETWORK

AWID FORUM, ISTANBUL, APRIL 2012

The Crisis, Macroeconomic Policies & the International Monetary Fund

FISCAL SHOCK OF THE CRISIS

- The crisis led to a steep fall in public sector accounts as fiscal stimulus packages, bank bailouts and automatic stabilizers, such as unemployment insurance and pension schemes, came into operation. **Revenues plunged, expenditures soared.**

- In **developing countries** public revenues were hard hit by excessive volatility in commodity and food prices, decreased world market demand for exports, erratic capital flows and a credit squeeze, among other issues.

- In **developed countries** the deleveraging process [banks restoring capital ratios and non-financial agents reducing indebtedness] and the conversion of private debt into public debt has squeezed the government purse. By 2010-end the public-debt-to-GDP ratio in developed countries had risen to well over 60%, surpassing the previous peak of 1998.

- **The fiscal shock affects women disproportionately for several reasons**. Because recessions are accompanied by job losses and men are seen as the "breadwinners," women can experience higher rates of lay-offs. This is exacerbated by women's concentration in precarious jobs—temporary, part-time, contingent, or sub-contracting employment—and they are structurally likely to experience greater decline and fluctuation in earnings, especially in developing countries.

A BRIEF KEYNESIAN MOMENT, OR CRISIS KEYNESIANISM

- Although the recent crisis is well-known for carrying out massive fiscal stimulus programs and expansionary policies of increased spending and social protection, in some cases, by early 2010 the IMF was already laying the groundwork for tightening fiscal and monetary policies for its member countries, again. The **short-lived enactment of fiscal stimulus during the crisis has not been followed up by a more profound re-orientation of orthodox macroeconomic policy ideology.**

- The current political consensus back to austerity and structural adjustment is a huge step backwards. It obstructs a full recovery from recession and **disregards the need to redress the structural asymmetries, imbalances and inequities in the international financial architecture.**

- Lack of **political determination**. **A people-first development strategy** would prioritize domestic demand and output, strengthen social sectors, especially health, education and social safety nets, and prioritize employment in the mandate of central banks.

- In this context of austerity, **gender equity** cannot be pursued through the participation of women in existing patterns of market-based production, the empowerment of women within existing paradigms of development, or gender mainstreaming within existing configurations of institutional power.

- It is the very **forms of production, the paradigms, and the institutions** themselves that need questioning and transforming, both through changes in the ideas that generate economic policies and through social mobilization.

THE DOWNWARD SPIRAL OF AUSTERITY

- FISCAL RETRENCHMENT → DECREASES AGGREGATE DEMAND → DECREASES CONSUMPTION AND EXPENDITURE → OBSTRUCTS EMPLOYMENT & DECREASES TAX REVENUE → DAMPENS ECONOMIC GROWTH & OUTPUT → DECREASES FISCAL REVENUE & EXACERBATES PUBLIC DEBT

- **The twisted logic of austerity is that of seeking to restore the confidence of the financial markets** (which are perceived as key to economic recovery), despite the almost universal recognition that the crisis was the result of financial market and credit rating agencies failure in the first place.

- It is indeed surprising that policymakers are once again putting their trust in the very same private finance institutions, whose irresponsible behavior had such deep costs on citizens, government budgets and development prospects. **This shows that little has been learned from the crisis.**

- **The current leadership of the IMF has acknowledged that too much austerity is risking jobs and growth**, and the Fund staff's report to the G20 suggested that developed countries "have scope to slow their current pace of consolidation, if offset by a commitment of additional tightening later."

- However, developing countries are not granted the same flexibility. International institutions called for, and supported, counter-cyclical policies in developed countries, while continuing to impose pro-cyclical conditions in bailout loans to developing countries. **It is a tragic, unjust irony that developing countries bear the brunt of the crisis impacts as innocent bystanders of Western wrongdoing.**

THE IMF'S NEOLIBERAL MODEL CONTINUES TODAY…

- **A UNICEF report on IMF surveillance and policy advice for 128 developing countries demonstrates** that the scope of austerity is severe and widening quickly. (70 developing countries reducing total expenditures by nearly 3% of GDP, on average, during 2010, and 91 developing countries will curb spending in 2012.)

- **The following adjustment measures, recommended by the IMF for the central objective of reducing budget deficits and inflation levels, illustrate how policy space for development strategies and recovery are still being constrained, despite the recessionary impacts of the crisis:**

(1) CUTTING OR CAPPING THE WAGE BILL

- 56 countries are cutting or freezing their wage bill, which tends to form the largest component of national budgets due to recurrent expenditures like salaries. TWN and Eurodad research also showed that the IMF recommended wage and hiring freezes for public-sector workers in countries such as Benin, Malawi and Zambia.

- However, significant risks persist of social service stagnation, particularly in high poverty areas, where salaries are reduced or eroded in real value, and payments in arrears, hiring freezes and/or employment retrenchment occur. Gender dimension: Women form the majority of health and education personnel around the world. Low pay is a key factor behind absenteeism, informal fees and brain drain.

(2) INCREASING CONSUMPTION TAXES

- An estimated 53 governments have adopted or are planning to adopt some form of consumption-based tax change, (either through increasing or expanding value-added tax (VAT) or sales tax, or by removing exemptions).

- Essentially a form of revenue extraction from citizens to state, this is one of the most common adjustment measures under consideration, which directly exacerbates inequality and poverty, especially for women and children.

- VAT and sales tax are regressive tax policies because the absence of class discrimination in the tax shifts tax burdens to low-income communities [e.g. poor families spend a higher proportion of their income on food and basic consumer items, and thus they are subjected to the taxes at higher proportions too].

- IMF country reports indicate that the following countries are: **Increasing foodstuff taxes**: Ethiopia, Moldova and Jordan among others. **Increasing fuel and energy product taxes**: Antigua and Barbuda, Belize, Dominican Republic, Guyana, Jordan, Kyrgyz Republic, Mexico, St. Kitts & Nevis and Turkey.

(4) REDUCING SOCIAL PROTECTION PROGRAMS AND REDUCING PENSIONS

- 34 countries, from the Philippines to Mongolia, are planning to decrease, or better target spending in social protection programs as a way to contain overall expenditures and achieve cost-savings.
- **Social services are particularly important**, which entails increased funding and wider coverage for health, scaled up access for education and more robust and extensive social insurance programs, including pensions and unemployment insurance.
- Social protection cannot be based on the **male breadwinner model**, nor should it be tied to **paid formal employment,** which excludes the vast informal and unpaid care sectors where the majority of women worldwide are situated. Rather, it must be oriented to individuals, and recognize their varied social roles, including the different requirements of women and girls in specific contexts.
- Infrastructure investment must also serve to reduce the **burden of unpaid work that falls primarily upon women.** This does not necessarily mean trying to price all human activity, but rather socially investing in areas such as care work, in all its forms, which would shift some of the burden of these tasks from women to governments.
- With regard to pension-cutting, in poor households across developing countries, an older relative receiving a pension is a valuable income source, a cash injection to rural economies with positive impact on local development. Policymakers should safeguard this income support, and if pension reform must occur, alternative support and service delivery, especially health, must be guaranteed.

HOW THE IMF’S ORTHODOX/NEOLIBERAL MACRO-STABILITY PARADIGM ENDANGERS RIGHTS-BASED PEOPLE-CENTERED DEVELOPMENT

- The **long-standing macroeconomic ideology** of the IMF is designed to achieve and maintain price stability, access to external capital and trade and financial liberalization. To attain these goals, the measures imposed by the IMF on developing and transition economies are **low fiscal deficits, low inflation and low public debt levels.**

- **Employing only a short-term timeframe and a primary intent of winning investor confidence**, these measures sabotage of public policy and developmental strategies through private and financial sector interests.

- **Reigning in the IMF**, and tempering if not eliminating its ability to impose conditionalities that strangle growth and recovery, needs to be part of any humane global economic architecture that emerges from this crisis.

- **Structural change needs to be grounded** in a commitment to international human and women’s rights, sustainable development, equity of income, access and opportunities, investment in social development, especially health and education, and a return of the role of the state in the economy.

- **Domestic sufficiency and security of food, energy and livelihoods** ought to be prioritized over international competitiveness and trade liberalization, the real economy should be prioritized over the financial sector (which should service the needs of the productive sector instead), and domestic producers, workers and investors need to be placed before foreign and corporate interests.

A BRIEF RUN-DOWN OF CRITICAL ISSUES IN IMF POLICY BLUEPRINT

(1) The IMF's downward bias in fiscal and monetary policy setting only takes into account the solvency costs of financing a fiscal deficit, while failing to factor in the costs of foregone growth and poverty reduction if the deficit-financing is allowed.

- **The goals of employment, equitable income distribution and social sector development cannot be foregone in the singular and static pursuit of balanced budgets and low debt.**
- The failure to consider these dynamic effects was what led to adverse outcomes for the Southeast Asian countries that carried out IMF conditionalities in the wake of the Asian financial crisis of 1997-98.

(2) The IMF does not dynamically assess the budgetary position of low-income and developing countries based on the potential to mobilize additional domestic revenue, such as through employment-boosting measures, scaling up economic output and productivity, tax compliance/restructuring, trade tariffs, and so on.

The IMF does not consider possibilities for creating fiscal space in countries afflicted by deficits through debt restructuring and cancellation, donor compliance with aid commitments and external grants, for example.

(3) In 2010 the IMF advised poor countries such as Ethiopia, Ghana, Sierra Leone and Zambia to tighten monetary policy by increasing interest rates to maintain the single-digit inflation targets of 2008-9, which intensifies the economic recession these countries are already experiencing.

- Inflation targeting continues to be advised or required by the IMF in spite the fact that inflationary pressures in these countries are coming from external shocks, such as the **excessive volatility of world food and commodity prices**, not from excess internal demand.

(4) **Public sector expenditure and taxation is not neutral:** Changes in different types of revenue or expenditure generate different macroeconomic outcomes. An increase in infrastructure spending, social transfers or targeted subsidies for private investors is more stimulating to the economy than tax cuts, because it leads to increased purchases and domestic demand.

- On the other hand, disposable incomes from reduced tax payments are most likely to be spent only partially, as indebted households use part of the tax savings for repaying outstanding debts rather than for consumption and investment.

(5) The IMF **advises low-income countries in particular to increase current account expenditures, as opposed to capital account expenditures.** For example, in Mongolia and Tajikistan, 2010 capital expenditure was programmed to decline by over 4% of GDP. Such cuts in capital investment jeopardize the basis for long-term growth and development.

POLICY OPTIONS FOR A NATIONAL DEVELOPMENT STRATEGY AND RECOVERY FROM CRISIS/RECESSION

- Policymakers should be resisted and pushed by citizens to refuse the current political consensus and pressure from various fronts (IFIs, donors, creditors, financial and trade markets) to adopt austerity measures. They should instead pursue policies that have proven to be effective in stimulating not just recovery from recession and crisis, but **structural advances toward a long-term national development strategy.**

- *Such options, which vary in importance across different countries and their individual circumstances and needs, include:* 1) quality of life indicators; 2) human rights, including women's rights; 3) decent work; 4) economic diversification between primary commodities, manufacturing, services and research & development that facilitates technology and science development; 5) a robust public sector that channels investments into productive capacity-building; 6) domestic self-sufficiency for food security; 7) financing for agricultural development and climate resilience and adaptation; 8) access to social services and meaningful life opportunities, among others factors. [Quantifiable measures on new indicators and targets would have to be developed & monitored to hold governments & other agents accountable.]

- To serve a transformed policy agenda for genuine development, **macroeconomic policies need to be expansionary**. The design of prioritizes full employment need to situate full employment in the mandate of central banks and allow not only higher budget deficits and inflation levels, but also deficit-financing—which expands productive expenditure to nourish the real economy of production, jobs and income.

- The **prevailing rationale for austerity** is that the fiscal space for continued stimulus is exhausted and that surging debt ratios have reached levels where fiscal solvency is at risk.

- **However, a national economy does not function in the same way as an individual firm or household,** which can increase savings by cutting back spending (because cutbacks don't affect its revenues). **Fiscal retrenchment** for a state has multiple negative ripple effects (such as dampening demand, output, employment, wages and thus tax base and revenues).

- Reduction of fiscal deficit by 1% has the **same multiple** for national income—it reduces the national income by 1% as well. **This downward spiral will ultimately hamper the austerity itself.**

- Austerity takes the form of large cuts in public investment rather than wages and entitlement programs (current expenditure). Reduction in public expenditure/investment leads to a **fall in future government revenues** and debt sustainability that is usually larger **than the immediate fiscal savings** obtained by austerity. Alternately, with a long-term view, future revenues, expected from a push of public investment, can pay off the public debt and reduce the deficit over the long-term.

- **Monetary tightening** involves raising interest rates and squeezing the amount of domestic credit in circulation. These two measures effectively constrain peoples access to credit at affordable rates, which further slows down domestic demand, output, employment and development prospects.

(2) WAGE GROWTH AND INCOMES POLICY

- WAGE GROWTH IS CRUCIAL FOR both livelihood security & genuine development. When wages don't grow as fast as productivity, demand is slower than supply. In this situation, economies remain depressed. An underpinning reason for low wages is the 'race to the bottom' in the globalization of labor & production, especially in EPZs.

- One of the numerous critiques of the **export-led development model** is that the bulk of domestic productive resources, including labor, is used to make exports. Meanwhile, the foreign exchange earned from these exports is used for repayment to international creditors. This diminishes the public resources available for actual domestic development and employment and demand creation.

- The neoliberal economic paradigm places **export-production** in its center, and thus obstructs an effective use of Keynesian deficit-financing to achieve full employment and productive capacity goals for long-term and equitable national development. The export model is essentially a '**double whammy**,' in that resources devoted to exports involve a sacrifice in foregone or lost output from domestic labor resources that are not mobilized for local needs.

- **An incomes policy would align wage growth to productivity growth in order to align domestic consumption with domestic supply**. This would temper inflation and allow monetary policy to divert its attention from price stability (& inflation targeting) and focus on securing low-cost finance for investment in real productive capacity, which would in turn create new jobs and opportunities.

(3) DECENT WORK

- **Central banks are connected to employment concerns. In the post-World War II period, development and full employment was seen as crucial part of central banks' tasks.** However, this has past mandate has gone astray in recent decades with the European Central Bank (ECB) focusing explicitly on price stability (inflation at below 2 percent), and developing countries signing on (implicitly or explicitly) to "inflation targeting" in the low single-digits as their primary operating framework.

- Integrating full employment into central bank mandate means that monetary policy will facilitate **access to credit at affordable interest rates**. This will facilitate domestic economic activity, and thus hiring. The basic logic is that if economic actors **can access credit** more easily, **hiring** will also increase in a virtuous cycle of stimulation.

- Employment can be boosted by a **gender-enabled fiscal policy** as well, through directing resources and investment to the sectors in which women work (such as agriculture and informal activities), areas in which they live (regions with poor or inadequate infrastructure), and elements of production that they possess and outputs that they consume (such as food).

- Social, sectoral and industrial policies that improve **women's economic bargaining power in the household** have myriad positive ripple effects on children and community. The productivity of the labor force improves and, as a result, costs of production fall. There is an intrinsic connection between improving women's bargaining power and strengthening gender equality.

(4) PROGRESSIVE TAXATION & (5) NORTH-SOUTH & SOUTH-SOUTH TRANSFERS

- **Progressive taxation** involves avoiding consumption taxes (sales and VAT) and focusing instead on corporate profit taxes, property taxes, capital gains taxes and tiered income taxation (with higher incomes taxed more), among others.

- **Consumption taxes can be progressively designed** by ensuring that basic goods are exempted from taxation for low-income families, while setting higher rates for luxury goods principally consumed by wealthier families.

- [For example, Antigua and Barbuda is *exempting sales taxes* for basic commodities, Kenya is *lowering taxes* on fuel and food staples consumed by vulnerable populations, & many developing countries also seem to be considering *tax increases on luxury items*, like vehicles, such as in Ghana and in the Republic of Congo.]

<u>(6) NORTH-SOUTH AND SOUTH-SOUTH TRANSFERS:</u> Includes low-cost development loans from creditor countries and institutions, donor grants, meeting aid commitments, regional financing arrangements such as the Chiang Mai Initiative Multilateral among ASEAN+3 countries and ALBA countries.

- Also addresses illicit financial flows from the South to the North such as tax evasion, transfer pricing by MNCs, and so on.

A RIGHTS AGENDA IS A JUSTICE AGENDA [FOR SOCIAL, ECONOMIC AND GENDER JUSTICE]

- A rights agenda is an alternative to the current growth paradigm, which in many ways is an anti-development paradigm.
- **A rights agenda is an alternative rooted in rights and justice**, in the collective resistance and struggles of people and communities against myriad structures of oppression and in not just a vision, but a conviction, that a better world is possible and is already happening, in many ways.
- The **acquisition of rights** (to goods, services, security, livelihood, & so on) is necessary for genuine democracy. It amounts to winning crucial battles for human dignity in the unequal neoliberal economics paradigm.
- But the **goal** is not to keep fighting battles in a condition of vulnerability to the vicissitudes of the neoliberal model, nor is it to fix, reform or even transform a failed paradigm---the goal is to transcend and revive a multitude of alternatives into the normative.
- The **logic of capital and growth** is based on competition, accumulation and inequity. As such it is politically and morally **incongruous** with a recognition of rights.

- Rights are **at the mercy** of finance capital and economic growth priorities.
- A **rights-based paradigm** would be an inversion of this: Social and political arrangements are designed based on the priority of maximizing rights.
- ***Thus if justice movements base their agenda on rights it would be an integral part of the effort to contest and resist finance capital and economic growth, which does not accept a rights-based approach to development***.
- The narrative of "rights of the people" is also an essential component of **democracy**, in that the violation of rights is fundamentally **anti-democratic**.
- This proposition underpins the rights-based paradigm and it paves the path for building democracies that function as such, not just termed as such.