

INTRODUCTION AND SUMMARY

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Introduction to the New Rules For Global Finance Coalition

New Rules for Global Finance¹ is an informal coalition of human rights, labor, environmental, development and religious organizations and scholars dedicated to the reform of the global financial architecture (GFA) in order to stabilize the world economy, reduce poverty and inequality, uphold fundamental rights, and protect the environment. The Coalition began in 1999 in response to the 1997 Asian financial crisis. The original purposes of the Coalition were: to enable its members to understand the official proposals to reform the Global Financial Architecture; to share that understanding with partner NGOs, think-tanks and academics, throughout the South and the North; to evaluate the official proposals in terms of criteria developed for the international financial institutions themselves; to identify or develop alternative policies; and to develop strategies to promote the acceptance and implementation of alternative policies. Most members of the New Rules Coalition attend in their personal capacity not representing the formal positions of their organizations.

The Coalition uses the following criteria to evaluate GFA proposals from government, academia, and NGOs:

1. Does the proposal promote greater financial stability?
2. Does it promote social equity between countries and within countries?
3. Does it promote environmental sustainability?
4. Can it be implemented (and did it originate) through transparent and participatory processes?
5. Does it respect subsidiarity, i.e., are the problems addressed as close to the base/grassroots as possible?

We served as co-chairs of the New Rules for Global Finance conference on *Alternatives to Neoliberalism* at the Carnegie Foundation in May 2002. This conference presented viable alternatives to the failed policies of neoliberalism. We are pleased to make available to a wider audience the papers presented at the conference. More than a hundred participants attended the conference from non-governmental organizations, academia, and think tanks. The conference produced a rich dialogue on alternatives to neoliberalism among activists and researchers from around the world. The Coalition is grateful to the Mott Foundation, the Böll Foundation, and the Ford Foundation whose funding made the conference possible. The New Rules for Global Finance Coalition invites the readers of these conference papers to apply the New Rules criteria to these papers.

¹ Please visit the New Rules website at <http://new-rules.org>. New Rules for Global Finance Coalition, 1112 16th Street, NW, Suite 600, Washington, DC 20036, jbaker@oxfamamerica.org.

Summary of Conference Proceedings

The keynote speaker on May 23 was Dani Rodrik, Rafiq Hariri Professor of International Political Economy at the Kennedy School at Harvard. Professor Rodrik based his talk “After Neoliberalism What?” on the empirical evidence of the effects of neoliberal policies. These policies have failed to produce economic growth, to reduce poverty, or to sustain the environment. Therefore, alternative policies must be put forward.

Rodrik argued that we should not reject the wisdom of mainstream economics. He laid out three sound principles of mainstream economics that should be observed. First, the rule of law should be upheld and contracts and property rights should be enforced so that investors can expect to retain the return to their investment. Second, the importance of private incentives should be recognized, and they should be aligned with social costs and benefits. Third, financial and macroeconomic policies should be managed with due regard to debt sustainability and prudential principles.

Rodrik further maintained that the alternative we put forward should not be against economic growth. It should be adamantly in favor of economic growth. Problems of poverty and the environment are much easier to handle in the context of robust economic growth than under stagnation.

For Rodrik, alternatives should not be against globalization. Poor countries need markets and technology, which they can access only through close access to the world economy. The need is to change the rules for such access.

An alternative to neoliberalism must be based on the empirical record of successful economic growth. Rodrik summarized the lessons of experience in four propositions:

1. Transitions to high economic growth are typically sparked by a relatively narrow range of policy changes and institutional reforms.
2. The policy changes that initiate these growth transitions typically combine elements of orthodoxy with unconventional institutional innovations.
3. Institutional innovations do not travel well. What works in one setting often does not work well in another.
4. Sustaining economic growth, once launched, cannot be taken for granted.

Rodrik then emphasized the importance of an investment strategy that can get domestic entrepreneurs excited about investing in the home economy. An efficient investment strategy needs to do two things: (a) encourage investments in non-traditional areas and (b) weed out projects/investments that fail. The specifics of how these things can be achieved are likely to differ considerably from country to country. They cannot be imported via a Washington Consensus.

He next turned his attention to institution building and laid out four types of required institutions:

1. Market creating institutions such as property rights and contract enforcement;

2. Market regulating institutions to deal with externalities, scale economies, informational incompleteness;
3. Market stabilizing institutions for monetary and fiscal management;
4. Market legitimizing institutions such as social protection and insurance, redistributive policies, institutions of conflict management, and social partnerships.

The keynote session on May 24 addressed “Can Sustainable Development Survive Neoliberalism?” and was delivered by David Reed, Director of the Macroeconomics Program at WWF. Reed’s fundamental premise is that addressing environmental problems in rural areas and responding to the needs of the world’s 700 million rural poor lies at the heart of moving beyond the neoliberal economic regime.

Reed’s presentation was divided into three sections. First, he reviewed the operative environmental assumptions on which neoliberalism is constructed and then proposed three alternative principles on which a sustainable economic regime could be constructed. The most fundamental predicate of neoliberalism is that there are no limits to the scale of economic enterprise, we can continue to expand the size of the economic sphere indefinitely. The second major assumption is that everyone in the world will eventually attain a reasonably high level of material welfare, so there is no need for redistribution of the world’s resources and wealth. The third assumption concerns substitution, i.e., if a resource is exhausted in one locality, investors will shift resources to another site until scarcity is reflected in rising prices. Substitutes will be developed. The fourth assumption is that environmental issues can be addressed only when a country has reached a high level of consumption. Adequate resources will be available to correct environmental costs.

Next, he focused on three policy foundations that are required to change the current status and treatment of the rural environment and rural poor in developing countries. The first principle regards the equitable distribution of environmental goods and services and distribution of environmental costs. Today, access to environmental goods and services and environmental costs are grossly skewed in favor of the rich. Sustainable development would ensure provision of basic free water, protection against natural disasters, access to basic energy, and clean air. The second principle states that the costs of environmental irreversibilities must be central to all economic and social planning. We cannot wait until countries have reached a certain level of income to take care of these costs. The third is the precautionary principle. We cannot carry out sectoral investments nor societal priorities that may harm public health or the ecological integrity of any nation.

Third, Reed discussed the Forces of Change to examine the shortcomings of civil society in addressing the many changes neoliberalism poses in promoting a sustainable future. He discussed three policy foundations that are required to promote sustainable development in rural areas of developing countries:

1. Promoting multi-faceted investment in rural areas to strengthen productivity and improve management of environmental resources;

2. Reorienting neoliberal institutional reforms so as to increase control and access of the rural poor to environmental assets;
3. Promoting domestic demand-driven growth that encourages diversification in rural areas.

David Reed concluded his talk with a call for environmental NGOs and developmental NGOs to work together toward joint goals in developing countries.

Besides the two speeches by Rodrik and Reed, the conference was organized around debates on a series of papers, which had been prepared and distributed to the participants in advance.

Group Session 1. Tom Palley, Assistant Director of Public Policy at the AFL-CIO opened a discussion of his paper on “Domestic Demand-Led Growth: A New Paradigm for Development.” He claimed that the Washington consensus, with its emphasis on export-led growth, has failed. It is time for a new development policy agenda that focuses on domestic demand-led growth. Achieving such an outcome will require a new constellation of policies. Domestic demand-led growth rests on four pillars: (1) improved income distribution, (2) good governance, (3) financial stability and space for counter-cyclical stabilization policy, and (4) an adequate fairly priced supply of development finance. The policies needed to put these pillars in place are (1) labor and democratic rights, (2) appropriate reform and regulation of the financial architecture, (3) a combination of debt relief, increased foreign aid, and increased development assistance provided through expanded Special Drawing Rights, the monetary accounting unit of the IMF.

Group Session 2. Didier Jacobs, Researcher at Oxfam America, opened a discussion of his paper on “Democratizing Global Economic Governance.” Based on an innovative conceptual framework, he explained the sources of inequity in the existing institutional setting of global economic governance. He assessed the merits and shortcomings of short to medium term reform proposals aiming at increasing the influence of poor people over global economic policy, and laid out a vision to democratize global institutions in the long term. The key element of that vision is universal suffrage along the “one person, one vote” rule. The struggle for democratic global governance must be positioned in the liberal tradition of universal suffrage, which has over centuries been extended from rich men to women, the working class, and people of color. Since global decisions affect people of all nationality, individuals of any nationality should have an equal weight in shaping those decisions.

Group Session 3. Frances Horner, Policy Advisor at the US Conference of Catholic Bishops, opened the debate on her paper “International Tax Cooperation and Development Beyond Monterey.” She emphasized that the present system of international coordination of taxation is unjust and inefficient because it reflects the first-at-the-table principle, as it is led by the Organization for Economic Cooperation and Development of which developing countries are excluded. The residence principle, the rules allocating transnational corporations profits across tax jurisdictions, the denial of

the right not to tax, the taxation of portfolio income, and the emphasis on income taxes are all biased toward rich countries. All these important rules were ignored at the Financing for Development conference in Monterey, as were proposals for new systems of international taxation such as a unitary tax, which would give developing countries a larger share of tax revenues from mobile assets.

Group Session 4. Randall Dodd, Director of the Derivative Studies Center, prepared a paper on “Improving Financial Markets: Regulatory Proposals to Dampen Disruptions and Deter Distortions.” He recalled that starting in Mexico in 1994, a series of financial crises swept through emerging market countries and left in their wake a badly damaged set of *neo-liberal* economic policies and the painful realization that the speed and direction of international capital flows were crucial policy goals. Proposals to address this problem, particularly those from a left-perspective, have focused on reducing the volatility of capital flows through capital controls or transactions taxes. The goals of these proposals were to increase the stability of financial systems around the world and reduce the vulnerability of developing economies to disturbances in those systems. Prudential market regulations – requirements for registration and reporting, standards for capital and collateral – will accomplish many of the same goals that capital controls and transactions taxes claim to achieve. This approach, although it is a break from the *liberalization* advocated by a *laissez-faire* approach to financial markets, is not entirely different from the history of financial market regulation in advanced capitalist countries. Instead of strict quantitative restrictions, it employs a combination of regulations and surveillance to discourage excessive flows and enhance the stability of financial markets in advanced as well as developing economies. While it is based on the experience of regulating financial markets in advanced economies, those lessons can be helpful in designing policies if they are properly adapted to the different circumstances present in developing economies.

Group Session 5. Kunibert Raffer, Professor at the University of Vienna, presented a paper on “Sovereign Debt Workout Arrangements.” Although the idea of sovereign insolvency had been around for two decades, it did not get much attention until Anne Krueger proposed it as the IMF’s “new” approach in 2001, countered by a proposal of the US Treasury to include collective action clauses in bond contracts. Raffer discussed the merits and shortcomings of Krueger’s version, contrasting it with the arbitration model based on the main principles of US municipal insolvency (so-called Chapter 9), also called Fair and Transparent Arbitration Process (FTAP). This model shares the concerns of the US Treasury about the IMF’s “statutory approach.” The IMF’s proposal would increase its power, despite the conflict of interest it would face as a creditor, and exempt its loans from any restructuring. In contrast to Krueger’s assertion, Raffer argued that sovereign insolvency can be implemented immediately, even to redress Argentina’s current crisis. He also emphasized the importance of hearing the affected population as well as the role of independent arbitrators, which are absent of both the IMF and the US Treasury proposals.

Fernando J. Cardim de Carvalho, from IBASE Brazil and the Institute of Economics at the Federal University of Rio de Janeiro, responded to Professor Raffer. He made the

important distinction between illiquidity and insolvency crises, and argued that a lender of last resort is needed in cases of illiquidity. Of the two proposals before the world today, he finds that the bankruptcy court is a much more promising instrument than the collective action clause proposal.

Group Session 6. Aaron Goldzimer, Social Scientist at Environmental Defense, introduced a paper on “Globalization’s Most Perverse Secret: The Role of Export Credit and Investment Insurance Agencies.” A 1997 article from the financial magazine Euromoney had the following revealing text: “Bankers are always very secretive about the precise structuring of their deals, but essentially the strategy is simple. The key is to get as high a return as possible, while palming the risk off on somebody else. That is why you should never listen when people tell you that export credit agencies are defunct dinosaurs. What could be nicer in times of turmoil than having the risk picked up by the taxpayer?” Export Credit and Investment Insurance Agencies (ECAs) have become both the largest single source of official finance flowing to developing countries and, according to the World Bank, the largest official component of developing-country debt. Yet few people recognize the large-scale global economic and financial impacts and implications of ECAs – much less their human and environmental costs. Goldzimer presented the role and impact of ECA, and pointed the way towards needed corrections. Areas touched upon included trade distortions, political economy concerns, the potential for moral hazard in lending, debt impacts, lack of transparency, negative environmental, social and human rights impacts and corruption. The lack of environmental and social safeguards in ECAs and the financing of large resource extraction and infrastructure projects lead to a two-tier international system for public financing of large projects. While Multilateral Development Banks (MDBs) have somewhat meaningful safeguard policies, they are routinely undercut by ECAs, which often finance projects that MDBs have rejected on economic, social, or environmental grounds.

Group Session 7. Ilene Grabel, Associate Professor of International Finance at the Graduate School of International Studies at the University of Denver, led a discussion on her paper “Capital Account Controls and Related Measures to Avert Financial Crises.” She argued that neoliberal financial reform exposes developing countries to five mutually reinforcing risks (namely, the risk of currency collapse; the risk of capital flight; the risk that governments, firms and banks will pursue fragile financing strategies; the risk of contagion from financial crises that originate elsewhere; and the risk that external actors will exercise undue influence over domestic decision making). She went on to explain how policymakers in developing countries can reduce their vulnerability to particular risks by adopting one or several of the following sets of measures: trip wires and speed bumps, restrictions on currency convertibility, Chilean-style capital controls, transaction taxes on currency and/or stock trading, and/or a publicly-managed closed-end mutual fund for developing economies. She concluded that most financial crises can be avoided and that the potential benefits of increased financial regulation outweigh the immense human and economic costs of crises.

Filomeno S. Sta. Ana III, Director of Action for Economic Reform in the Philippines, made comments following Ilene Grabel’s presentation. He emphasized that there is no

single bullet for crisis prevention. Complimentary policies must be put into place. He confirmed that the Chilean model of capital controls provided the incentive for investors to shift to longer-term credits and foreign direct investments, which reduced volatility. He also argued that too much credit, of whatever type can undermine the economy. He concluded that the state should have the capacity to direct private capital and that investments should rely primarily from domestic savings.

Group Session 8. John Grieve Smith of the University of Cambridge introduced his paper “Exchange Rate Management.” He asserted that a more stable exchange rate regime is the least discussed but most fundamental reform of the global financial system. Both fixed and freely floating exchange rates have serious disadvantages. “Fixed” rates tend to be adjusted only under crisis conditions, while floating rates leave industry at the mercy of inappropriate and unforeseeable movements. We need to devise a system of managed but flexible rates, which can be adjusted to changing conditions such as relative movements in costs. The general model for such system could consist of publicly stated parities and bands, regular but small changes to these parities, and *automatic* interventions through special stabilization funds set up for that purpose. Moving towards a more stable, managed exchange rate regime would require a two-tier approach, with regional arrangements that may vary between different regions, and global arrangements to link them. Initially the regional arrangements could form around a European group, managing the rates between the euro and non-EMU countries in the EU, a North and Latin American group based on the dollar, and an Asian group based initially on the yen. Such a tripolar system would then require a global arrangement under the IMF to manage the rates between these three groupings. But until such groupings were established, informal moves to manage the relation between the three major currencies would help to achieve greater stability.