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Cooperation for Development and Transition to Market Economies--The Way Forward

Address by Michel Camdessus
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It is a pleasure to participate in this Congress, and to speak to you about the way forward for international cooperation for development and transformation--cooperation to enhance development in these closing years of the twentieth century and to assist the countries in transition from central planning.

I am addressing you at a time of serious concerns. Instead of enjoying the favorable perspectives opened up by the end of east-west tensions, our world still feels itself under threat from the age-old curses of famine; war; and new forms of pestilence, from which our ancestors used to pray to God to be delivered. And at the same time, unemployment in many industrial countries is rising to levels not seen for decades. So it is no wonder if we ask ourselves--where are we? And what can we do? Let us try to answer these two questions, knowing full well that our increasingly integrated world implies a greatly heightened need for effective international cooperation if we are to reach a solution.

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Where are we? The extraordinary combination of opportunities and risks with which we are faced, following the remarkable sea change of the past few years, has been commented on ad nauseam; but as to the overall assessment, there is little consensus. Was the past decade a "decade of the people," as suggested by my colleagues of the UNDP? Or was it in fact, as it is described more frequently, a "lost decade," and a premonition of a somber future?

The end of the cold war; a new consensus on market-oriented economic systems and policy; the advance of pluralism; and the increasing globalization of the world economy--these are four obviously positive developments. But let us also recognize the obstacles.

Some of these welcome developments have brought new problems in their wake--among them, disruption and conflicts associated with the dismemberment of nation states; increased risks of arms proliferation; and the immense difficulties associated with transition from central planning to market-

oriented economic systems. Moreover, some old, familiar economic and social problems remain. In most of the industrial world, persistently sluggish growth or recession are feeding, and in turn are feeding on, a loss of confidence among producers and consumers. One result, which I view with great concern, has been the increasing tendency toward protectionism. Economic weakness has also been contributing to a loss of confidence in political leadership and institutions, and to social frictions. Meanwhile in the developing world, even though there are many success stories, economic progress has been uneven, bypassing many of the world's poorest. In terms of GDP, the successfully adjusting developing countries account for roughly half of the developing world. In the other half, there are many countries caught up in tragic situations of poverty and conflict. For people in these countries, and also for many others--yes, it has been a "lost decade" indeed. I shall mention Angola, Haiti, Liberia, Somalia, Sudan, and Zaire, but the list is much longer. Many other developing countries have made little or no progress over the past decade in raising the living standards of their people. We have in these countries--and particularly in Africa--a very urgent agenda....

In the wake of this mixture of developments, and in the face of this lack of confidence, what should we try to achieve? What needs to be done?

What we should try to achieve is what I call <u>universal high-quality growth</u>. By high-quality growth I mean growth that is sustainable, that brings lasting full employment and poverty reduction, that promotes greater equality of income through greater equality of opportunity, and that respects both human freedom and the environment. And at the international level, high-quality growth must mean adequate growth in living standards especially in those countries where living standards are lowest. This last requirement is additionally important because of the increasing integration of national economies in today's world, which makes it even more intolerable that some countries stagnate or even regress while others develop more or less steadily.

Universal high-quality growth is clearly a tall order. But surely we can aim for nothing less, because anything less would be either unsustainable, or offensive to our human values, or both. High-quality growth for all countries is the ultimate objective of our work in the IMF, and it is fully in line with the objectives of "human development" and "people-centered development" proclaimed by our friends here.

This is our common objective. We have to pursue it through a cooperative strategy based on three elements that are of greater urgency today than ever before:

- universal adjustment and reform;
- free trade;
- revitalized international financial cooperation.

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<u>Universal adjustment and reform</u>: three key words.

First, universal. It has always been clear that the developing countries need sustained, non-inflationary growth in the industrial world; and the same need is now felt by the countries in transition. What has become more clear in recent years is the increasing dependence of the industrial countries on economic success in the developing world. This is not only a matter of the industrial countries' export markets and investments in the developing world. Progress in the developing countries is in the interests of the developed countries for other reasons as well--because it helps to stem the flow of economic refugees, because it helps to counter the threats of disease, drugs, terrorism, etc. I hardly need to add that the industrial countries need, and stand to gain immeasurably from, the successful transformation of the formerly centrally-planned economies.

The global dimension of the challenge of achieving high-quality growth makes it a key responsibility of the multilateral institutions to help all countries to strive together to remove obstacles before it, and to try to implement consistently what experience teaches us are the four, basic, universal ingredients of high-quality growth.

- First, <u>sound macroeconomic policies</u>. This means a firm anti-inflationary monetary policy, a sound and sustainable fiscal position, a realistic exchange rate, and a financial sector that is free of excessive regulation and control. For countries with high rates of inflation--and this includes all countries in the early stages of the transformation from central planning, following the liberalization of prices--the primary objective must be to bring inflation down to low levels, since hyperinflation is unfriendly, to say the least, to both growth and democracy.

- Second, <u>appropriate structural policies and an appropriate development strategy</u> relating to investment, resource allocation, and project financing. Here, what is required is what the World Bank has called a "market-friendly" approach to development. The government has to provide both a regulatory framework for the operation of a competitive market system, where liberalized prices bring about efficient resource use and spur innovation, and also a tax system that does not distort production, saving, or investment decisions. But governments also have to intervene where necessary--to invest in infrastructure, to invest in human capital through health and education spending, and to protect the environment. The countries in transition face major tasks under this heading, since they have not only had to liberalize a profoundly distorted system of prices, but have also needed to build virtually from scratch the institutional structure of a market economy.

- Third, <u>integration with the global economy</u> through a liberal trade and exchange regime that provides openness to trade and investment. Competition from the outside world is an essential spur to efficiency, and foreign investment is a vital source of innovation. In fact, open economic

relations with the rest of the world provide one of the most reliable generators of growth. The jury is no longer out on this issue: the verdict is clear--the most open economies have been the most successful.

• Fourth, social policies--policies needed to help ensure broad-based participation by the population in economic, social, and political life. I include here policies that alleviate poverty, protect the most vulnerable, and promote greater equality of opportunity; the provision of adequate health and education services; policies to slow down excessive population growth; and the promotion of human and democratic values through the protection of human rights, the encouragement of broad-based political participation, and good governance.

Each of these four ingredients is essential for high-quality growth, and they are all mutually reinforcing. Thus if the macroeconomic framework is weak so that inflation is high, then not only will structural policies and the development strategy be compromised because market signals will be distorted, but also social policy will be impaired because of the way in which rapid inflation attacks the poor and the vulnerable. And let me emphasize that the fourth ingredient, social policy, is necessary not only because the quality of growth depends upon it, but because the quantity of growth depends on it too. Poverty, and inadequate education and health care not only offend human values: they also represent wasted human potential that in the longer run is immensely costly to development.

Also in the category of social policy, I would place special emphasis on the importance for the developing countries of policies to contain population growth. If we are to achieve a speedy and significant improvement in the standards of living of the hundreds of millions in poverty in the developing world, it is most important that high priority be attached to effective action in this area. If the problem is not attended to promptly, our other efforts to attain high-quality growth will achieve little. There are various approaches to the problem, but experience shows that in the education of women we have a powerful force that could, besides its other benefits, help significantly in slowing down population growth.

In describing these four key ingredients of high-quality growth--the only kind of growth that is worth the effort of the international community--I have referred particularly to how they apply to the developing and transforming economies. But let me repeat that they are equally imperative for the industrial countries, especially since it is mainly their responsibility to ensure the environment of global macroeconomic stability that all countries need in order to thrive. We need to promote there sustained growth with low inflation, low real interest rates, reasonable exchange rate stability, and adequate saving to finance both domestic investment and resource flows to the rest of the world. I do not need to tell you that these are the central issues arising in our work with these countries at the present juncture. I am happy to note, after our April meetings, their basic agreement on the essential elements of this strategy,

even if the present recession in Europe and the weakness of the fiscal position of many of them does not make its implementation easy.

<u>Second, free trade</u>.

I shall be brief on this, because it is the central responsibility of our sister institution, the GATT. Free trade is essential for the industrial countries. But I cannot fail to remind you that the developing and transforming countries need trade even more, and most importantly they need access to the markets of the industrial countries. But they are confronted by protection, which has grown over the past decade. It has been estimated that developing countries lose about $100 billion a year in export revenues as a result of market barriers in industrial countries. This is almost twice the official development assistance (ODA) that the industrial countries provide. This makes no sense: taxpayers in the industrial countries pay both for aid and for costlier imports as a result of trade barriers; and the poorest developing countries lose more in trade than they gain in aid. This is one of the worst examples of incoherence in industrial countries' policies toward the developing world. And the transforming economies also are affected: they have a special need for access to markets in which they may have a comparative advantage, because much of their old export base is no longer economically viable, but they also confront major impediments in important markets. These are some of the reasons why further progress with trade liberalization through a successful conclusion of the Uruguay Round is so urgent. No effort should be spared to this end, since free trade can do so much for growth in all countries.

But as we all know, growth and trade have to be complemented by adequate financial cooperation. And here we have another major problem.

So <u>third</u>, we need <u>revitalized international financial cooperation</u>.

What is the problem? Basically, and put most simply, it is that the needs for international financing are undoubtedly growing, while the resources available to satisfy those needs are shrinking. But of course reality is not that simple. We observe, for instance, that developing countries in the process of implementing strong programs of adjustment and reform not only get the external financing they need, but are faced from time to time with embarrassing excesses of capital inflows or reflows which give rise to problems of monetary management. We also see, in general, that when programs are credible and governments take early, courageous steps to implement them, we succeed in catalyzing the required external support. We have recently experienced this, for example, with the Baltic countries and Kyrgyzstan among the countries in transition, and with Bangladesh, India, Laos, Peru and Zimbabwe to cite a few developing countries.

But reassuring as this may be, the problems remain serious. We also observe, for instance, that:

- external support frequently is well short of what is needed, particularly in the social area; 1/

- operations such as rehabilitation and demobilization are precariously financed, at best; and humanitarian agencies have tremendous difficulties in finding resources to tackle emergencies;

- external support is often insufficient to allow an adequate recovery in investment in basic infrastructure, an essential requirement of faster growth;

- and last but not least, we see immense challenges emerging outside the domain of development economics to which our instruments of cooperation have been tailored hitherto. These challenges have the common feature of being of a global nature, and the international community has to meet them. It will be sufficient to mention just a few of them:

    - the need for adequate financing of the UN at a time when it is being asked to take on vital new responsibilities;

    - threats to the environment, including the risks of deforestation, global warming, etc.;

    - drugs;

    - epidemics; and so on!

All of this, at a time of weak activity, when it is crystal clear that the urgent need for budget consolidation is competing strongly in many industrial countries with the need for financial assistance to developing countries. ODA continues to languish at a level of about 1/3 of 1 percent of industrial countries' GNP--roughly half the UN target of 0.7 percent. I am doubtful that we shall see any significant real increase in ODA in the near term. There are more reasons for my pessimism: the incentive of cold-war competition among some donors no longer exists; competing demands for assistance to Russia and other economies in transition have increased; and public support for aid in general, and for concessional aid in particular, seems to be weakening significantly. I fear that this shortage of financial support in relation to the need for it may be approaching critical proportions. We urgently need to consider how to respond, as we are

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1/ Here I cannot but deeply sympathize with the calls of the NGOs working for those who are truly the poorest in the world--the fourth world, in recognition of which the General Assembly has declared an International Day for the Elimination of Poverty.

obligated to do when a crisis must be prevented: we must face up to the situation, and see what changes are called for.

Any suggested response to this problem can at this stage only be tentative; but the following elements may certainly be relevant.

My first point, of course, is that everywhere in the world--in industrial, developing, and transforming economies--a conscious and determined effort needs to be made to reduce wasteful public expenditure. Much can be said on this subject and I have dwelt on it elsewhere; today let me say simply that determined efforts all around the world to reduce military expenditures, spending on prestige projects, and wasteful subsidies being given for a variety of different purposes could release vast amounts of public sector saving. It would facilitate the task of fiscal consolidation in the industrial countries, and this could help to boost the provision of financial support to the neediest countries.

Second, we must recognize that from now on, ODA and the international financial institutions cannot, and should not, continue to occupy the same, central territory that they have occupied for so long. In view of the new agenda that is taking shape, at least two needs should be recognized:

1. the need to allocate ODA to the range of tasks where there is no alternative form of financing, in particular from domestic or private sources;

2. the need to facilitate the mobilization of private investment.

Allocating official assistance first to the areas where there is no substitute for it must go hand in hand with an effort, which is equally necessary, to improve the effectiveness of assistance to get better value for the aid provided. One key to this is to give priority in aid to countries that are pursuing the kind of sound policies directed toward high-quality growth that I outlined earlier. Another key requirement is that the financial assistance to any country should consist of an appropriate mix of balance of payments support and project financing, and when needed, humanitarian aid. I must stress that it would be naive to gauge the effectiveness of assistance in terms of its visible or tangible impact on the very neediest. Of course, an impact is what we are looking for; but a clearly identifiable connection with particular assistance is another issue. Balance of payments support, for instance, can have extremely powerful effects, even though its results may be less clearly identifiable and tangible than an investment project or humanitarian assistance.

In addition, it is of course a must that the donor countries and international institutions improve the quality of their programs; and we should not apologize if this sometimes implies stronger conditionality. But recipient countries also have a major responsibility, to prevent the recurrence of the frustration of donors with the poor results of some of their past efforts--a frustration too easily marshalled by those always

ready to argue that money is best spent in their own constituencies. It is by demonstrating their commitment not to spare their own efforts at adjustment and reform that developing and transforming countries can best exert leverage over international assistance. The stronger the effort they make, the stronger will they find international support to be.

This applies particularly to the need I have mentioned for mobilizing private investment. The role of the business sector in the developing and transforming countries will be critical in the coming years. And I hardly need to remind this audience that enlightened businessmen in the developed world also have a major role to play. The economic scene in the developing and formerly centrally-planned economies is changing rapidly, and all of you will doubtless be alert to the new business opportunities that are appearing. If you seize them, by investing in those countries when appropriate with a long-term perspective, at the same time transferring to them your technological know-how and managerial abilities, you will play a major role in achieving the high-quality growth we are trying to promote. But you will be in a position to do so only if those countries adhere unambiguously to the kind of policies--market-friendly and investment-friendly--that I referred to earlier.

Assistance provided by the multilateral institutions must also be improved and amplified. With regard to the IMF, our concessional support to the poorest countries for adjustment and reform efforts has been provided mainly through the enhanced structural adjustment facility (ESAF). But later this year, the ESAF is due to expire and the subsidized resources supporting the facility are expected to be exhausted. There is a broad and strong consensus among our member countries that the ESAF has proved to be an effective mechanism for Fund support of reform efforts in low-income countries, and that a successor facility needs to be established. We are therefore now making all possible efforts to make this instrument even more effective in light of the lessons of experience, and to appeal to our membership for the contributions that are needed for ESAF's successor. Also, only two months ago, the IMF introduced a new facility, the Systemic Transformation Facility (STF), designed to address at an early stage the special problems of the countries in transition.

It is also clear that especially in times such as these, we must ensure that none of the instruments we have available is under-utilized. One instrument available to the IMF, and to no other institution, is an allocation of special drawing rights (SDRs) to member countries to supplement their foreign exchange reserves. This instrument has not been used since 1981, and it is my judgment that there is now a pressing need for it to be activated. Reserve levels are low for many countries in relation to their international transactions--especially low-income developing countries and countries in transition, which need to build up their reserves to protect their reform and adjustment programs. Many of these countries--in fact all members who have joined since the last allocation twelve years ago, numbering 39 in all--have never received an SDR allocation. Moreover, the proportion of global reserves accounted for by SDR holdings has fallen

steadily to very low levels even though the Fund's members have accepted an obligation to make the SDR the principal reserve asset of the international monetary system. These are among the reasons underlying my proposal for an allocation of SDR 36 billion, which represents a modest proportion of the prospective growth in demand for total reserves over the next several years. I would also favor establishing a mechanism whereby a new allocation could be redistributed toward the most needy member countries on the basis of policy conditions. We are continuing to work toward gathering a sufficiently broad consensus in favor of such an allocation.

The international institutions can also, of course, strive to improve their cooperation and the coordination of their work. We at the Fund are particularly aware of the need to work closely with the three other major pillars of global cooperation in the economic sphere--the World Bank and the regional development banks; the GATT; and the UN system. Each has its own special and distinct responsibilities, which broadly correspond to the four ingredients of any strategy for high-quality growth that I mentioned earlier. It is a special responsibility of the IMF to support the application of sound macroeconomic policies; the World Bank is concerned mainly with the support of structural reforms and the financing of development projects; it is the task of the GATT to strengthen the multilateral trading system; and last but not least, the UN system, apart from its crucial role in peace-keeping, has among its core responsibilities, together with environmental issues and many forms of technical assistance, such tasks in the social sphere as relief and rehabilitation, poverty alleviation, and assistance to refugees, children and other vulnerable groups. Just as the four ingredients of high-quality growth are all essential and self-reinforcing, so are the four pillars all essential; and they must necessarily work in cooperation with one another. In fact, in the time remaining to me I should like to refer to the role that the UN Summit on Social Development scheduled for 1995 could play to reinforce the fourth one.

The purpose of the Social Summit is to strengthen social development in all--industrial, developing, and transforming--countries by giving political impetus at the highest level to the promotion of social policies. The three core issues that have been established for the Summit--the alleviation of poverty, the growth of employment, and the enhancement of social integration, especially of disadvantaged groups--are all quite essential.

What should we expect from this Summit? Of course, as usual when such a gathering of world leaders is arranged, expectations will be very high. But I would like to suggest that they could be invited modestly to consider the following basic objectives:

- to recognize together the importance of the social component of a <u>strategy for high-quality growth</u>, and to pledge their support for it in a spirit of strengthened universal cooperation;

- to commit themselves to improving their own <u>respective social policies</u>, though not, of course, at the expense of any of the other three ingredients of the strategy, keeping in mind in particular that durable social progress can take place only in the context of sound macroeconomic policies and never at their expense;

- to help improve <u>cooperation among the four international families of organizations</u> in the field of social policy--an effort to which the IMF stands ready to contribute;

- to help increase the <u>strength and effectiveness of what I call the social pillar</u>: namely the family of agencies in charge of promoting social development. The UN and its relevant agencies are natural leaders in the field of social policy, and are doing an admirable job in many parts of the world, often with too little recognition. I have witnessed their work on the ground myself, in Ethiopia, Peru, Zambia, and many other countries. But as I said earlier, the Organization and its agencies are under-resourced. We can hope that the Social Summit will lead to a strengthening of their presence in the social field and to stronger financing of their missions.

We must all of us demonstrate our redoubled commitment to a strengthening of policies for social development--we must demonstrate our readiness to streamline permanently our procedures and organization, and our determination to address the problems where they are the most urgent, at the lowest possible cost, to avoid duplication and turf disputes, and to target our action where people are most committed to self-help and where we can most efficiently join forces with NGOs and all other contributors, particularly the private sector.

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In concluding, I return to the question I asked at the beginning. What do we need to do? What I have said leads to the answer that we all--governments, international organizations, public servants, businessmen, and citizens--need to commit ourselves to the essential ingredients of high-quality growth which is our common objective. In particular, we must all recognize the essential global dimension of our objective, and we must all commit ourselves to strengthening international cooperation and, in this spirit of international cooperation, to strengthening its four institutional pillars.