G24 Secretariat Briefing Paper on

Monitoring the Monterrey Consensus

(March 2003)

The outcome of the Conference on Financing for Development (FfD) was a turning point in international economic cooperation. The adoption of the Monterrey Consensus at the summit level on 22 March 2002 not only signaled a new partnership in international economic relations but also reaffirmed the advantages of the new approach toward consensus building taken by the international community.

The nature of the consensus

A comparatively short document, the MC has three Chapters. The first Chapter sets out the main objectives, highlights the challenges of development financing in the context of globalization and stresses the need for a holistic approach. The second Chapter identifies the “leading actions” in the six major areas. This is the core of the Consensus. In their communiqué of 19 April 2002, the G-24 Ministers emphasized “that financial policies and instruments and the role of international financial institutions are a central part of the Consensus”. The third Chapter lays down the modalities for “staying engaged”.

Some areas of concern regarding implementation.

While progress to structure an effective and cooperative follow-up process of the Consensus has taken place and concrete actions have been taken in some areas, progress in several key policy areas has been meagre or non-existent. In a few cases there has been retrogression. What follows is a brief consideration of six important issues in the Consensus for which the score-card so far is unsatisfactory.

1. International trade. The MC reaffirms the commitment to trade liberalization and welcomes the decisions of the WTO to place the needs and interests of the of developing countries at the core of its work programme. It also acknowledges the issues of particular concern to developing countries such as trade liberalization in agricultural products and labour intensive manufactures, the need to make more precise and operational the provisions for special and differential treatment for developing countries, the reduction in trade distorting subsidies in agriculture, and the implementation and interpretation of the Agreement on Trade-Related Aspects of Intellectual Property Rights in a manner supportive of public health.

Since the Monterrey Conference, the United States increased various agricultural subsidies[1] contradicting, in a sense, trade guidelines in the Consensus. The EU – while having considered

[1] US Farm Security and Rural Investment Act in May 2002. It provides for an increase in various agricultural subsidies up to US$ 73.5 billion over the next ten years.

different options to modify its agricultural support schemes - has yet to take steps in this respect. Recent decisions would indicate that EU agricultural tariffs and farm spending will not decline before 2006.[2] The WTO Secretariat report for the Trade Policy Review of the EU (24-26 May 2002)[3] indicates that the simple average tariff on agricultural products is about four times higher than that of non-agricultural products, that tariffs well above average also apply to textile and clothing products[4], that at EU level the funding (support) for the Common Agricultural Policy continues to represent the single largest expenditure, and that at Member State level the State aid for agriculture amounts to 1% of GNP. The lack of actions in the agricultural related issues is compounded by the fact that in accordance with the WTO Agreement on textiles and clothing most of the existing restrictions in textiles and clothing will not be lifted before the end of 2004.

Two issues in the Doha Agenda of particular concern to developing countries have not made progress either. The Director-General of WTO, Supachai Panichpakdi, recently expressed his disappointment over the failure of WTO members to meet the year-end (December 2002) deadlines for agreement in negotiations on special and differential treatment for developing countries and enhanced access to essential medicines for poor countries lacking capacity to manufacture such drugs themselves.

2. Adequacy of the resources of the Fund. Noting the impact of financial crisis or risk of contagion in developing countries and countries with economies in transition, the MC states: "we underline the need to ensure that international financial institutions, including the IMF, have a suitable array of financial facilities and resources to respond in a timely and appropriate way in accordance with their policies". The MC also encourages the IMF to continue to enhance participation of all developing countries and economies in transition in its decision-making. Both concerns could have been addressed in the Twelfth General Review of Quotas. However, it has just ended without any modification on levels or distribution of existing quotas. It was a crucial opportunity for progress that was missed.

Higher levels of quota and a new quota structure are both crucial aspects of the MC. An increase in the quota level will help to ensure adequate IMF resources in case of simultaneous crises in a number of middle-income countries. There will be less need of protracted negotiations with third parties to assemble a financial support package for countries with immediate needs. This will lessen the danger that third parties, rather than the IMF, will determine the adjustment framework. Moreover, higher quotas will be more in consonance with developments in international trade. Total IMF quota in relation to world imports is about a tenth of what it was in 1950 and only two fifths of what it was in 1970. Also a higher quota for an individual developing country – and the accompanying larger access that it implies - should likely lead to an improved trade-off between finance and adjustment for that country in the eventuality of an IMF stand-by

[2] A proposal by the European Commission that received unanimous support by its members in January 2003 contains the following three elements: cut in agricultural imports tariffs by 36%, export subsidies for agricultural products to be slashed by 45% and reduction in trade distorting in domestic farm support by 55%. The proposal would be implemented in the course of six years commencing in 2006.

[3] WTO Press Release, Press/TPRB/198, 26 juky 2002.

[4] The report also indicates that "To date the EU has lifted restrictions on 20% of products restricted in 1990, leaving the elimination of the remaining 80% of resticted imports *back-loaded* for the final stage at the end of 2004."

arrangement. Analysts have observed that "under-funded" programmes have less chances of success.[5]

3. Participation of developing countries in economic decision-making. The lack of action on quotas in the Twelfth General Review implies unchanged quota structures and persistence of existing anomalies in the present quota structure. Members of G-24, such as Brazil and Mexico, have GDP and import levels significantly above some industrial countries whose IMF quota is higher than that of either of the former two countries.[6] Korea has a GDP and imports which are at least twice the size of those of Austria, Denmark or Norway. Yet, its IMF quota is lower than that of those three countries.

But, the foundations for equitable participation should consider aspects that go beyond merely economic and financial factors. The global push for more democratic institutions and enhanced participatory structures at the national and international levels should also be part of the picture. If the donor countries were to be consistent with their own principles and practice, they should push for more effective participatory structures in the Fund.[7] The push for democracy also strengthens the initial justification of basic votes being a significant part of the voting power. A larger weight in basic votes might substantially change the participation of African countries - 45 of which are represented by only two of the twenty-four IMF Executive Directors.[8]

4. Coordination of macroeconomic policies among leading industrial countries and surveillance. The MC calls for strong coordination of macroeconomic policies among the leading industrial countries - which is critical to greater global stability - and stresses the need for the IMF to further strengthen its surveillance activities over all economies. In the IMFC Spring meeting of 2002, the Managing Director of the Fund called attention to the danger of an increasing external deficit in the United States. This situation required firm control over public spending and a long-term strategy to increase national savings in this country. Nonetheless, the US external deficit has continued to grow and is now above 5% of GNP.

The high external deficit of the US and its increasing fiscal deficit – probably reaching $ 300 billion - pose a significant risk to the world economy.[9] An abrupt adjustment – sharp reversal –

[5] Many observers, particularly since the mid 1980s, have discussed the link between adjustment and financing and concluded that the severity of the adjustment is closely linked to available resources. See, for example, "Financial Management of Globalization – IMF and Developing Countries" (Arjun Sengupta, Economic and Political Weekly, Mumbai, India, 15 January 2000) and "An Analysis of IMF Conditionality" (Ariel Buira …) .

[6] Mexico has higher imports and a much larger GDP than Australia, Belgium or Switzerland; nonetheless, it has a significantly lower IMF quota. Brazil has imports similar to those of Australia or Switzerland and a GDP close to double that of either of those two countries; yet, its IMF quota is lower.

[7] While the argument that in the decisions affecting the use of the Fund resources those who provide the resources should have a major say has a strong basis, there is not a strong basis for the disproportionate weight of a few members in decisions that do not lead to the use of Fund resources. Factors such as the number of countries and relative size of population affected by the decisions should be taken into account.

[8] Some of the political and the statutory implications of changing basic votes are discussed in "Governance of the IMF – Decision-making, Institutional Oversight, Transparency, and Accountability" Leo Van Houtven, IMF 2002, (Pamphlet series No. 53).

[9] The recent federal budget proposal forecasts a deficit of $ 304 billion in fiscal year 2003 and $ 307 in fiscal year 2004.

of the US external deficit, particularly if accompanied by a substantial weakening of the dollar, can trigger financial and real economic shocks in the rest of the world.[10] The problem is further compounded by the lingering effects of the major setback in the confidence of economic agents due to pervasive corruption or mismanagement in several large US corporations.[11]

Yet, a medium-term framework to reduce imbalances in the United States is only part of the solution. Without a solid recovery in Europe and a strong recovery in Japan, US efforts to reduce imbalances can lead to major strains in the world economy with adverse implications for developing countries.

5. HIPC. The MC highlighted that speedy, effective and full implementation of the enhanced Initiative was critical. It stressed that the enhanced Initiative should be fully financed through additional resources and that the computational procedures and assumptions underlying debt sustainability analysis need to be kept under review. The Development Committee in the Spring meeting of 2002 agreed that, inter alia, the success of the Initiative depended on the donor community providing adequate and appropriate concessional financing. It also agreed to discuss the issue of debt sustainability at its next meeting.

Recent assessments would indicate that, in the past, assumptions regarding the parameters that underlie sustainability have been in most cases too optimistic. A stronger dose of reality is needed. Regarding resources, a prompt fulfilment of the pledge made by the G-7 in Kananaskis, Alberta, Canada, in June 2002, of an additional US$ 1 billion seems critical. The pledge was reiterated in the Fall meeting of the Development Committee. Yet, actual contributions are taking longer than expected and, therefore, the implementation of the Initiative is being delayed. The record of the initiative is not satisfactory. In six years only 6 countries have reached the completion point.

6. SDRs. Paragraphs 44 and 59 of the MC refer to special drawing rights. The Consensus calls for keeping under review the need for special drawing rights allocations. Three different aspects could be considered. First, several proposals in the FfD process pointed to the need to authorize the IMF to make quick decisions for a temporary issue of SDRs to swiftly stamp out international liquidity crises in member countries.[12] Once the emergency is over the SDRs would be destroyed. Secondly, allocations should be made to avoid "reverse aid" as proposed in the "Zedillo Report".[13] The original intent of issuing SDRs was to allow international reserves to be increased, in line with need, without imposing real costs on the average country. Without SDRs allocations, in order to reach an adequate level of reserves developing countries have either to run a current account surplus or to borrow on terms much more onerous than those associated

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[10] A recent analysis of the possible risks confronting the world economy and the sustainability of the external deficits of the United States appears in "World Economic Situation and Prospects 2003", United Nations DESA/UNCTAD (Sales No. E.03.IIC.2).
[11] According to "Business Week" of 30 December 2002: "The problems revealed by the scandals were systemic, not the result of a few bad apples". (*What we learned in 2002*, page 170)
[12] See, for, example, " Report of the Secretary-General to the Preparatory Committee for the High-level International Intergovernmental Event on Financing for Development" paragraph 159 (A/AC.257/12) and " Existing proposals to ensure availability of sufficient international liquidity in order, inter alia, to avoid unnecessary recessive adjustment processes" UN A/AC.257/27 add. 9)
[13]" Report of the High-level Panel on Financing for Development". (United Nations, A/55/1000, 26 June 2001).

with SDRs. Thirdly, a global issue of SDRs could facilitate recovery of the world economy. In many countries export capacities are under-utilized. World inflation is the lowest in many years and there is a risk of deflation in some of the large industrial economies. A global allocation is unlikely to be inflationary, should lead to an increase in import demand in a number of countries and thereby assist the recovery.

The Ministers of theG-24 called again in the 2002 Spring meetings for a swift implementation of the Fourth Amendment of the IMF's Articles of Agreement on the special, onetime allocation of SDRs and urged those countries that had not done so to ratify promptly the Fourth Amendment. Yet, no progress has taken place on this front or on the proposals above. The issue seems to have been set aside despite its critical importance for a large number of countries.

Conclusions

With the FfD process, financing for development returned to the top of the international agenda. Living up to the commitments in the MC remains a major challenge for all countries and multilateral institutions, in particular the BWIs.

The follow-up in the UN has largely concentrated on procedures. The effort has focused on finding ways to ensure effective and comprehensive implementation inside and outside the Organization. Indeed, actual decisions for action in most areas of the Consensus – including the most critical ones – have to be taken elsewhere. The responsibility lies in individual countries and multilateral institutions, in particular the WTO and the BWIs. There is the danger that the latter do not accord priority or urgency to crucial issues in the Consensus and that concrete actions are selective, paying attention to only partial aspects of the Consensus.