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Contents

President's summary

Development strategies in a globalized world: A new role for the government and fiscal policy

(Agenda item 8)

1. Discussions in formal and informal sessions focused on the new role for government and fiscal policy that has emerged since it became clear that monetary policy alone could not create the conditions for economies to recover from crisis and to reach a more equitable and sustainable growth path. Delegates agreed that the need to take effective action was essential, as "business as usual" could not continue. Any response had to involve a leading role for the State as a foundation for multilateral cooperation, alongside its national policy-making role and provide functional and responsive institutions. In addition, the capacity and ability of the State to enact appropriate legislation needed to be ensured.

2. Delegates heard that the global economy had entered a danger zone threatened by a relapse, as manifested by pronounced market instability. The initial recovery had been fuelled by expansionary fiscal policies that had since either expired or were being wound down in many countries. To one representative's question – "Are we in a post-crisis situation?" – panellists agreed that, even though the world economy was technically no longer in recession, the crisis was not over yet and many fundamental systemic issues still needed to be addressed. Developed economies had begun to stagnate with the waning fiscal stimuli and ineffective monetary policy, and while some developing economies were resilient, showing only a slowdown in growth rates, they were, however, not able to pull the rest of the world economy out of the crisis, due to their still relatively small share of the global economy.

3. One presentation commented on the fact that, despite the relative success of the fiscal policies used at the outset of the crisis, countries had not been comfortable with the new paradigms that these posed. They seemed instead to remain more comfortable with entrenched ideas that were reinforced by traditional institutions – even if those did not work. However, he said, countries were quickly running out of instruments to respond to the crisis and it was very risky to blindly follow traditional recommendations of fiscal consolidation. Other speakers concurred that austerity measures would not provide the short-term stimulus that was needed to overcome diminished demand, and so could not entice the growth in investment, of wages and economic growth that was needed; nor would it solve the prevalent debt problem. Similarly, the crisis had exposed the limitations of financialization as the driver of global growth. This was dangerous for the global economy, and no country could be de-coupled entirely from the adverse effects of the crisis.

4. During the informal discussions, members of the Board questioned the extent to which developed economies still retained sufficient policy space in which to put in place the stimulus measures that were needed. With the exception of a few extreme cases, it was argued that policy space in most developed countries was not exhausted, in part because the very low interest rates that governments still faced meant that borrowing costs remained cheap and there was no risk of crowding out as long as the private sector had not taken the baton. (On the other hand, speakers also noted that some low and middle-income countries were experiencing persistent external debt problems. This was seen as pointing to the limits of the existing arrangements for dealing with debt problems.)

5. The panellists in the debate agreed that the focus should be primarily on overall economic growth rather than specifically on the reduction of fiscal deficit, if the aim was to reach fiscal consolidation. They stressed that, without economic growth, it would be difficult to reduce public-debt-to-GDP ratios, owing to the negative effects of the tightening measures on economic growth, and that fiscal consolidation should be the end and not the means. Therefore, it was generally agreed that there was a real need to promote growth-friendly fiscal policies.

6. In this regard, panellists underlined the way that fiscal multipliers varied according to the types of public interventions. It was noted that (a) public expenditures usually had greater effects than tax cuts; (b) some forms of public expenditure had greater growth implications than others; and (c) tax cuts for the poor had greater demand-boosting impacts than tax cuts for the rich. This topic was also discussed during the formal session, where the experience of Asia during the recent crisis illustrated the benefits of a "functional finance" approach to fiscal policy, which recognized different multiplier effects of spending and taxing rather than focusing just on budget balances. This helped Asia to boost domestic demand and contribute to global recovery.

7. The Board also discussed the need for further reforms of the financial sector. Volatile exchange rate movements hindered the recovery efforts of some developed and developing countries. There was also a broader need for reform in the international economic architecture. Delegates called on UNCTAD to continue to engage in discussions and analysis of trade and development implications on this topic. Several speakers commented that the United Nations and UNCTAD were the most legitimate international forums for discussions on this topic.