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The Covid-19 crisis poses an unprecedented global threat to people's lives and livelihoods. In its wake, persistent fragilities and deep fractures, accepted as part of the new normal in the post-2009 global economy, have been visibly exposed. Calls to build a better future, beyond the immediate task of containing the pandemic and restarting economies, will have to include a hard and frank examination of the governance of the global economy.

Even before the virus began to spread worldwide, a spluttering North, a general slowdown in the South and rising levels of debt everywhere were hanging ominously over the global economy; these, combined with increased market volatility, a fractured multilateral system and mounting uncertainty, were already signalling the danger of a global recession.

Over the second half of 2019, it became increasingly clear that the global economy was entering troubled waters with slower growth across all regions and a number of economies contracting in the final quarter. Still, there was a widely shared expectation that things would gradually improve in 2020, led by the large emerging economies, with global growth returning to its potential by 2021.

With the advent of the Covid-19 pandemic, levels of uncertainty in the global economy have reached new heights. Not surprisingly, economic projections for the year 2020 vary widely. However, the picture from the still limited data currently available points to a dramatic reduction in output and incomes from the widespread shutdowns of manufacturing and services, along with sharp falls in financial markets and knock-on effects on consumer sentiment and investment confidence, international trade and commodity prices.

Global recession amidst pandemic relief measures

There is little doubt that the global economy will experience deep recessionary conditions in the first half of this year with subsequent developments contingent on the trajectory of the pandemic and the effectiveness of government relief and recovery efforts, including debt relief for developing countries.

Estimates made with the UN Global Policy Model point to a contraction of global output in the range of 1.0 to 1.5 per cent in 2020 relative to 2019, assuming optimistically that economic activity restarts in the second half of the year and financial markets begin to recover, supported by 'whatever it takes' monetary stimuli. This would imply a swing of about 4 percentage points in global growth with respect to what would have occurred if the Covid-19 crisis had not taken place.

In recent weeks, a series of relief packages have been announced by policy makers in the major developed economies and China that appear to involve more explicit support to incomes, aggregate demand and government activity than was the case with the response to the GFC. Aside from special credit lines for businesses, the critical measures include government spending on healthcare, unemployment benefits, paid sick leave and cash transfers for households. Even so, preliminary estimates suggest that only a quarter of the \$5 trillion so far announced will effectively translate into higher demand for goods and services.

Policy makers in China have made several announcements about the size and nature of the stimuli in place for 2020. However, so far this has been considerably smaller than the package they implemented after the 2008 global financial crisis.

Assuming that global linkages continue to operate as normal, the measures adopted so far should soften the shock, and if the pandemic is quickly brought under control, could help bring global growth within the -0.5 to 0.5 per cent range in 2020. However, the effectiveness of government action to bring about a swift reversal in the face of unprecedented job losses and a reluctance of companies, given increasingly precarious balance sheets, to invest suggests that much will depend on the ambition of subsequent rounds of public spending. Effective coordination at the multilateral level, especially regarding the response in developing countries, will be critical if a rapid recovery is to take place .

The crisis-response measures adopted so far will have some positive impact not only on the implementing economies but on the world economy, including growth in developing countries. However, developing countries face distinct constraints, which make it significantly harder for them to adopt stimulus measures without facing strong foreign exchange pressures. And as these countries do not issue international reserve currencies, they can only ease those pressures through exports, debt accumulation or asset sales, all of which are problematic under recessionary conditions. What is more, efforts to raise exports will require significant imports of equipment, know-how and financial capital. Finally, the financial turmoil that this crisis has already triggered has caused sharp currency devaluations, making debt service and import bills far more onerous.

Thus, even with the stimuli enacted by the major economies, developing countries (excluding China) will lose significant export revenues in 2020. According to our most recent estimates, these losses will be upwards of \$950 billion, owing to falls in both volumes and prices. While, at the same time, economic contraction will see imports fall in developing countries, by at least \$750 billion, the additional pressure on current account balances, will see a squeezing of reserves that, in most countries have failed, over the preceding decade, to recover the levels reached before the global financial crisis.

The precarious position of developing countries

Many developing countries were already slowing down in the final quarter of last year with several entering recession. However, the speed at which the economic shock to advanced economies has spread to developing countries – in many cases in advance of the health pandemic – has been dramatic, even in comparison to the 2008 global financial crisis, resulting in widespread economic contraction.

Developing countries have suffered unprecedented capital outflows, growing bond spreads, currency depreciations and lost export earnings including from falling commodity prices, declining tourist revenues and reduced remittances. And with countries beginning to shut down in response to the health threat the economic damage seems certain to multiply many fold.

According to the IIF, since January 21st net portfolio equity and debt outflows from emerging markets have totalled close to \$100bn representing the largest quarterly outflow ever from these markets. Foreign direct investment has also fallen sharply. Currencies have fallen against the dollar between 5 and 25 per cent since the beginning of this year, faster than the early months of the GFC. The prices of commodities, on which many developing countries depend for their

foreign exchange, have also dropped precipitously since the crisis began. The overall price decline has so far averaged around 40 per cent, with oil dropping by over 60 per cent.

Looking ahead, there are three main channels through which the Covid-19 shock can be expected to increase the financial pressures on developing economies over the coming months.

The first is the pressure on government budgets from the public health crisis. While developed countries have the administrative capacity and, generally, the fiscal space to backstop their lockdowns and buttress their social protection systems, in developing countries sharp contractions of incomes are all but inevitable. Tighter fiscal space and weaker healthcare and social protection systems will expose developing countries to greater human and financial damage while limiting their ability to respond, triggering a potentially dangerous vicious circle. With an increasing need for imports of specialized goods and services to deal with the health crisis the balance of payments constraint can only expect to tighten further.

The second channel is through trade. Exports will not recover for some time, particularly for commodity exporters. At the same time, other items on the current account, such as remittances, royalty payments and profit outflows have already added to the financing difficulties facing many developing countries.

Importantly, the strong recovery in developing country trade that occurred in 2010 seems less likely this time. Even if the damage to global supply chains is not irreparable, as lead firms recover from the crisis they will likely have to rethink their business model, including fewer links in these chains, and with more that are closer to home. In addition, China has steadily diminished its dependence on external suppliers through an increase in domestically produced intermediate products. At the same time, there has been too little diversification of economic activity in many developing countries over the past decade – with greater commodity dependence in many countries -- leaving them more exposed than ever to new shocks and disturbances

Commodity prices have been well off their post-recovery highs since the price slump in 2016 but there seems little likelihood of the kind of pick up in prices seen between 2009 and early 2011 which was well ahead of the recovery in global output.

The third channel is financial. The flight to safety has, as noted earlier, already caused record capital outflows from emerging economies, triggering large currency depreciations against lead currencies and widening spreads. In countries with a high exposure to foreign debt, be it private or public, these trends put enormous pressure on their debt sustainability, by undermining refinancing of outstanding external debt while driving up their value in foreign currency. This comes against a background of increasing debt in many developing countries over the past decade. Total developing country debt stocks stood at 193 per cent of their combined GDP at the end of 2018, the highest on record, compared to just over 100 per cent in 2008.

On top of rising debt servicing costs since 2012, developing countries are facing a wall of repayments due on foreign-currency denominated public debt over this year and the next. The total amount of sovereign debt repayments due at the end of 2021 is \$2.7 trillion (\$1.62 trillion in 2020 and \$1.08 trillion in 2021); of this, \$562 billion are due for repayment by governments in low- and middle-income countries, with the bulk of this amount due this year (\$415 billion in 2020 and \$147 billion in 2021). In “normal” times, much of this debt would be rolled over, adding to future debt burdens but providing vital breathing space to honour overall obligations.

But with sudden stops to external refinancing possibilities, suspending sovereign debt repayments due over this and the next year, at the very least for low- and middle-income developing countries, is key to averting immediate and wide-spread debt crises. Clearly, the amounts that would be involved in suspending sovereign debt repayments in poorer developing countries are relatively small compared to the economic rescue packages hurriedly put together across the developed world.

Recovering better: from emergency measures to long-term reforms

Advanced economies have embarked on a dramatic change of policy direction in response to the crisis. Measures that were unthinkable just a few weeks ago have been embraced and implemented in response to the scale of the crisis. Discussion of what developing countries should and could do has, by contrast, lagged behind, and particularly when it comes to international support. That is now beginning to change.

Given the role of the dollar in the international system, the United States' Federal Reserve can extend its role as lender of last resort beyond the country's borders, although it currently does so in a selective and strategic manner. The Federal Reserve has currency swap programmes with nine Central Banks (enabling these to provide dollars to their own banking systems that lend and trade in dollars), including just three developing countries - Brazil, Mexico and Singapore. This comes as the role of the dollar in the developing world has become more central since the global financial crisis, largely due to developing countries' growing recourse to international financial markets to meet external financing needs. By the end of 2019, outstanding international debt securities - such as bonds, asset-backed securities and commercial paper issued by their governments and firms - denominated in dollars stood at \$3.36 trillion, or 80 per cent of the estimated total amount of developing countries' outstanding international debt securities of \$4.2 trillion.

While advanced country governments are sending checks to their citizens and opening emergency credit lines for their companies, this clearly is not an option for most developing countries which are highly dependent on access to US dollars and lack the financial infrastructure and financial fire power to follow suit.

As a matter of urgency, the international community will need to co-ordinate appropriate financial rescue packages to pre-empt a global debt crisis. These would have to include, as a minimum, the following measures:

First, a coordinated global response to liquidity shortages to address immediate financing needs. The IMF has signalled that it is willing to fully deploy its current \$1 trillion lending capacity to help deal with the crisis. However, not only is this likely to prove insufficient, but current lending facilities and financing instruments are complex, tied to inappropriate conditionalities under the circumstances and therefore difficult to access quickly, in particular for developing countries. While the IMF has promised flexibility in this regard, an additional and faster avenue to address, at the very least, current liquidity shortfalls is a new allocation of *Special Drawing Rights* (SDRs). This system gives IMF member countries claims on other members' reserves providing hard currency liquidity at no cost for public budgets. Under current quota arrangements, this instrument heavily favours advanced countries, thus a new allocation of 730 billion SDRs (\$1 trillion) should go mostly or exclusively to developing countries. This could be achieved through a new allocation of SDRs and an IMF "designated" reallocation of current and new but unused SDRs from advanced countries to poorer developing

economies. The required new allocation of SDRs would, no doubt, have to be multiple times that agreed in 2009 (of 183 billion in SDR or \$287 billion at the time), depending on developing countries' liquidity needs and options for a "designated" reallocation of existing and newly allocated SDRs. But this would be an appropriate response to the scale of the crisis.

Second, *capital controls* should be endorsed by the IMF as a necessary and fully legitimate part of any policy regime and wherever appropriate introduced to impose a small tax on inflows during booms, curtail or reduce the surge in outflows during busts, reduce illiquidity driven by sell-offs in developing country markets, and smooth the adjustment of currency and asset prices after financial shocks. Implementation should be coordinated by the IMF to avoid stigma and prevent contagion, and who, in cooperation with other appropriate international bodies, should also be tasked with lending the technical support needed to ensure their effectiveness and extending advice on complementary measure needed to deal with related disruptions.

Third, even if large liquidity injections to developing country reserve accounts stave off financial and economic meltdowns and serial sovereign defaults in developing countries, it is important to avoid that debt crises re-emerge in the longer term. Measures to this effect are ***temporary standstills*** on debt service payments, or a formal or informal agreement between a debtor and one or more of its creditors to suspend these payments for a given period of time to allow debtors to propose restructuring plans. During this time creditors cannot seek legal remedies, a critical provision to keep non-cooperative and litigious creditors (or so-called vulture funds) in check. While there has been ongoing debate about the institutional avenues to govern temporary standstills, UNCTAD continues to argue that such standstills should be triggered by the unilateral decision of debtor countries to declare their need to freeze debt repayments temporarily, and should subsequently be sanctioned by an independent panel of experts, rather than creditor organisations. While there may be little time, in the current circumstances, to create new international bodies to govern temporary standstill procedures, this would be just one of many extraordinary measures taken with unusual speed over the past months.

Fourth, and in addition to temporary standstills as a kind of emergency break, new ***debt relief programmes*** need to be agreed on as soon as possible. On 25 March, the World Bank and the IMF called on all official bilateral creditors to suspend debt payments from the world's 76 poorest economies, currently in receipt of support from the International Development Association (IDA). While a first tentative step in the right direction, more systematic, transparent and co-ordinated steps towards writing off developing country debt, based on need rather than bargaining power, are critical. As pointed out, the wall of debt repayments about to hit a large number of developing countries is unsustainable. For now, African Finance ministers have indicated that a waiver of all interest payments on their debt, estimated at \$444 billion for 2020, and a possible extension to the medium-term would help to provide immediate fiscal space and liquidity to their governments. However, unless more comprehensive debt relief programmes are agreed, future redemption schedules will fast look very much worse than is the case at present. It should not be a matter of over-stretching global economic governance capacities, to design an immediate debt relief package for stricken developing countries, beginning with those already in default and, according to IMF debt sustainability assessments, at high risk of debt distress. A measure of ambition is provided by the cancellation in 1953 of half the German debts accumulated over the previous three decades and future payments made contingent on export earnings.

Fifth, Official Development Assistance (ODA) must be ring-fenced by all donor countries. Despite a majority of donors having routinely missed agreed ODA targets in the past, and despite ODA flows being spread ever more thinly across additional donor-determined objectives, ODA remains a vital source of external financing for the poorest of developing countries. Over the decade since the financial crisis an additional \$2 trillion would have reached developing countries had the 0.7 per cent (of global national income) ODA target been met by DAC members. This, therefore, is the time, for donor countries to, finally, honour their collective commitment and deliver ODA to developing countries in full and unconditionally. As an extraordinary measure given the immediate situation, channelling a significant amount of the missing amount of ODA – say one quarter of that total – into a *Marshall Plan for Health Recovery* would be a fitting way to demonstrate the international solidarity needed to mitigate the crisis in developing countries.

As the health pandemic is brought under control and economic shocks dissipate, a more profound reassessment of the multilateral system -- promised but not delivered in 2009 -- will be needed to ensure that resilience and fairness become integral characteristics of our more interdependent world.

The current shock, coming a little more than decade after the GFC, the rampant inequalities and the fast-accelerating environmental destruction from rising global temperatures, are the wake-up call that should push all governments and international institutions to mobilize against the stresses and fractures that have produced an increasingly fragile and anxious world. Immediate steps in response to the crisis should therefore be used to signal a new beginning for global governance.