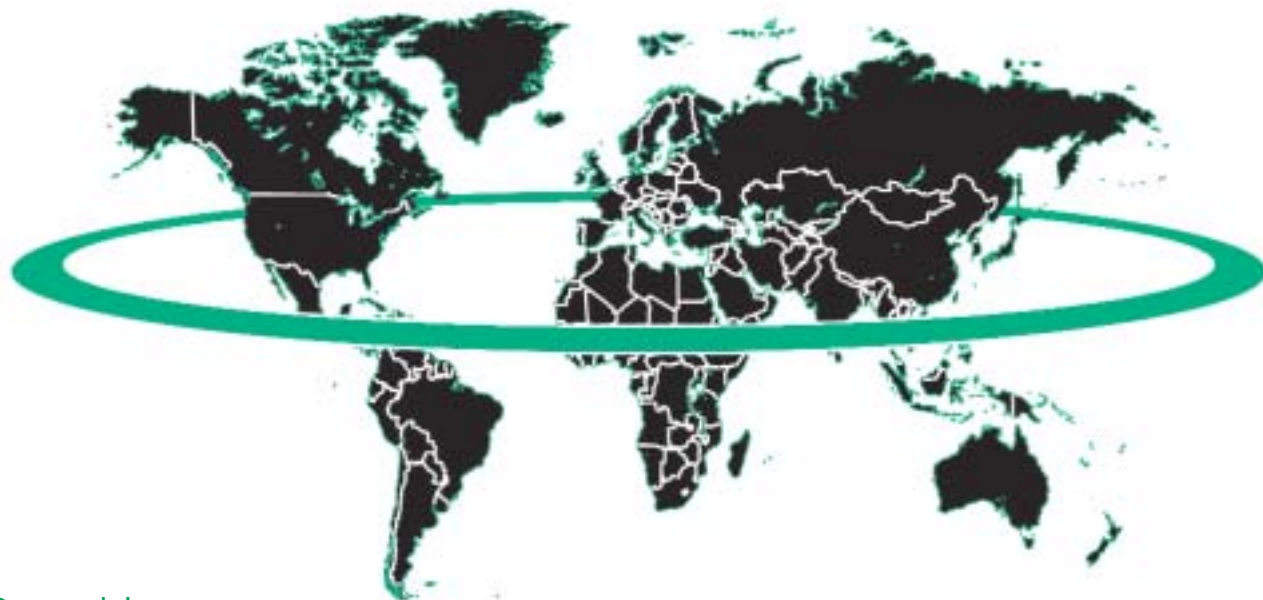


# Civil Society Statement on the Role of International Financial Institutions in Promoting Trade Liberalisation

Prepared for the Commonwealth Finance Ministers Meeting

*29 September 2004*



## I Preamble

1 We, representatives of civil society organisations from across the Commonwealth, met in London, United Kingdom from 26 to 29 July 2004 to share views and analyses on the role of the international financial institutions (IFIs)<sup>1</sup> in influencing trade liberalisation processes in low income and vulnerable countries.

2 We recognise the commitment of the Commonwealth to people-centred, sustainable development and the elimination of poverty; we attach great importance to the promise of the Harare Declaration 1991, reaffirmed in the Aso Rock Declaration 2003, to work towards an effective, equitable, rules-based, multi-lateral trading system in support of pro-poor development and democracy.

3 These commitments compel a strong response to the development crisis engulfing many of our countries. According to the UNDP Human Development Report 2004, 'an unprecedented number of countries saw development slide backwards in the 1990s; in 46 countries people are poorer today than in 1990.' Ten of the 20 countries that experienced a reversal in the human development index (HDI) between 1990 and 2002 are Commonwealth member states. In contrast, only one Commonwealth member was among the three countries that experienced a drop in the HDI in the 1980s. HIV/AIDS presents particular development challenges for the Commonwealth where an estimated 22 million people, of the 42 million worldwide, are infected with HIV/AIDS.

4 We share the concern of the Commonwealth Expert Group on Development and Democracy about the asymmetry of the global trading system and its unequal benefits. While liberalisation has increased the importance of trade in the world economy, its impact has been very uneven among and within countries. Deteriorating terms of trade and the loss of trade preferences are having major, adverse impacts on small and vulnerable countries within the Commonwealth. For example, the proposed EU sugar regime reform could mean an annual revenue loss in the Caribbean of some US\$90 million dollars from 2008.<sup>2</sup>

5 In the face of the above-mentioned asymmetry, we are concerned about the expanded involvement of IFIs in trade-related activities and the consequences for developing countries, which are pressured to liberalise their trade regimes with scant regard for pace, sequencing and capacity.

6 In this context, civil society encourages the Commonwealth to make truly meaningful the call of Millennium Development Goal (MDG) 8 for the international community, including the IMF and World Bank, to forge a global partnership for development and 'develop further an open, rules-based, predictable, non discriminatory trading and financial system' and address the needs of least developed countries and small island developing states. This has been reaffirmed by governments in recent international fora.

<sup>1</sup> The term 'international financial institutions' is used in this document to refer primarily to the World Bank Group and the International Monetary Fund, which are also known as the Bretton Woods Institutions.

<sup>2</sup> CARICOM, 2004. Communiqué issued at the conclusion of the 25th Regular Meeting of the Conference of Heads of Government of the Caribbean Community, 4 to 7 July 2004, St. George's, Grenada.

# II Concerns and Recommendations

## Declining policy space

7 In the face of increased convergence between the agendas of the IFIs and the multi-lateral trading system, opportunities for national governments to determine their own policies are being reduced. The tension between the shrinking policy space and the constricting framework of international disciplines, commitments and global market considerations were highlighted in the 2004 São Paulo Consensus of UNCTAD XI, where participants noted the need for appropriate balance between national policy space and international commitments.

8 Since the creation of the World Trade Organization (WTO) in 1995 and the Ministerial Declaration on Coherence in Global Policy Making, the IFIs have consistently expanded their involvement in trade liberalisation by influencing the policies of borrowing countries through such measures as: conditioned lending; shaping the agenda and goals of trade-related technical assistance and research; and ex ante mechanisms or instruments that tie lending to adoption of "good policies", such as the Country Policy and Institutional Assessment (CPIA).

9 Developed for the purpose of rating the policy and institutional performance of borrowing countries' governments, the CPIA establishes one-size-fits-all 'good' policy norms. This powerful instrument helps determine the size of a country's allocation of loan and grant resources; the principal policy conditionalities for new operations; and its debt threshold or ceiling.

10 The constraints to developing country policy making imposed by the rules of trade agreements and the trade-related policies promoted by the IFIs are compounded by skewed policy decision-making within the IFIs due to the concentration of voting power in the hands of a few developed countries. Under the Bretton Woods Institutions' governing structure, five countries together control almost 40 per cent of the votes.

11 The promise of national ownership of Poverty Reduction Strategy Paper (PRSP) processes and consequent commitment to recognise governments' policy space has not been delivered, as evidenced by the IFIs' own evaluations. The IFIs' trade-related operations are expanding in many countries even though PRSPs rarely contain substantive analysis of trade-related policy options and preferences. Moreover, national authorities and IFIs are usurping the policy space that should be used for open parliamentary and social dialogue, debate and decision-making. PRSPs should be country-owned through inclusion of parliaments and civil society in their formulation.

12 In light of the above, we recommend that Finance Ministers:

- a urge implementation of the World Bank's Operation Evaluation Department Review 2003 recommendation that 'the development of generic 'best practice' should be augmented and where necessary, be replaced by the development of knowledge adapted to local problems generated in collaboration with local expertise';
- b urge implementation of the 2004 recommendations by the World Bank's Operation Evaluation Department and

IMF's Independent Evaluation Office to revamp the Joint Staff Assessment process so it does not undercut ownership of PRSPs; and

c actively engage in the debate on changes in the voice and vote of developing countries within the Bretton Woods Institutions.

13 If CPIAs continue to be used, we call on Finance Ministers to advocate:

- a that governments not be penalised for adopting policies through open and democratic processes, even if these policies do not conform to the CPIA;
- b that CPIA-derived policies do not override the policy prescriptions included in the PRSP, as they do at present; and
- c the release of the now-secret CPIA ratings for the Commonwealth and other countries so that parliaments and citizens' groups can engage in a dialogue about the appropriateness of CPIA trade, investment and fiscal policy ratings (among others) in their countries.

## Impact of trade and financial policies on access to essential services

14 It is questionable whether essential services for all can be guaranteed where service provision falls under the disciplines of the General Agreement on Trade in Services (GATS). The GATS permits governments to exclude public services from the jurisdiction of the agreement where "public services" are defined as those services provided on neither a commercial nor a competitive basis. However, the IMF and World Bank are facilitating service provision on a competitive basis, including attendant cost recovery provisions. This constrains or eliminates the option for governments to claim the public services exclusion and hence facilitates the application of GATS to these services.

15 Moreover, the GATS commitments made by governments "lock in" liberalisation and privatisation and restrict their ability to reassume responsibility for service delivery, which could be calamitous if market failures make universal service obligations unachievable.

16 The World Bank is attaching policy conditions to loans that require governments to grant "national treatment" in procurement of services, which could result in undermining local service industries that cannot compete with trans-national service corporations.

17 In many developing countries the IFIs are accelerating the pace of commercialisation and privatisation of services in the absence of strong regulatory control, including protection of the public interest. The expansion of private provision of basic services with cost recovery is creating two tiered service sectors that increase inequality and often deprive poor people of access to affordable services.

18 The IMF is expected to change accounting rules to ensure that budget targets exclude commercialised infrastructure services for which there will be full cost recovery. Excluding infrastructure spend from fiscal targets would leave other categories of government expenditure, such as health and education, more exposed to budget cuts during adjustment processes. Beginning in 2005, this policy

may, if adopted, lead to massive investment in infrastructure services with fees that are unaffordable by poor and marginalised groups.

19 In light of the above, we recommend that Finance Ministers urge the IFIs to:

- a refrain from advising governments to make GATS commitments for essential services; and
- b discontinue using loan conditionalities to press governments to adopt trade policies in areas that are still under international negotiation.

20 Furthermore, we recommend that Finance Ministers work with trade authorities as well as the IFIs to ensure that:

- a GATS negotiations are postponed until an acceptable standard for necessity that takes into account human rights and social goals is determined;
- b all service-related IFI operations and trade agreements, such as the GATS, support the universal service obligations of all governments. Governments should not be required to define and protect universal service obligations in their sector-by-sector negotiations, as is currently the case. In addition, under "national treatment" rules, governments should not be asked to provide the same subsidies to foreign and domestic service providers; and
- c any effort to enforce compliance with international trade and finance agreements does not pre-empt sub-national laws and regulations or leave sub-national jurisdictions fiscally or legally liable in the event that trade claims are brought against them.

### Ensuring the public interest: health and TRIPS

21 The Trade Related Intellectual Property agreement (TRIPS) and the pressure to enact "TRIPS Plus" provisions must be evaluated in light of their impact on development and on the ability of people to enjoy their right to health. The enforcement of these agreements and pressures to expand them are eroding the ability of governments to set domestic standards and restricting their ability to provide life-saving drugs to affected populations.

22 In light of the above, we call on Finance Ministers to ensure, in instances of pressing public health interest, that the sovereignty of governments in granting compulsory licenses for necessary drugs continues to be recognised.

23 We also call on Finance Ministers from OECD countries to play their part in ensuring that radically scaled-up levels of resources are available as grants as part of the international response to HIV/AIDS, including the assurance of access to affordable medication and the strengthening of health systems to support treatment and prevention on a sustainable basis.

### Trade and financial policies in support of the productive economy

24 The gains from liberalisation have been concentrated among countries that export manufactured goods with high technology and skill content, while countries dependent on primary commodities and low-skill products have been further marginalised. Industrial countries' share of income from manufactured goods grew from 73 per cent to 77 per cent between 1980 and 1999, even while their share of

manufactured goods in world trade fell from more than 80 per cent in 1980 to less than 70 per cent in 1999.

25 Developing countries are unable to penetrate the high value-added export space occupied by developed countries in part due to IFIs' policies that direct the liberalising of developing economies so abruptly that fledgling domestic industries do not gain competitiveness.

26 Domestic agricultural support and export subsidies in OECD countries have intensified while the trade preferences available to developing countries have been reduced and become time bound and restrictive in terms of country and rules of origin stipulation. As noted by UNCTAD XI, the IMF and the World Bank cannot adequately deal with loss of preferential treatment; this must be addressed explicitly through trade negotiations.

27 The IFIs are currently considering changing rules so that budget targets do not cover commercialised infrastructure. Such exclusion, in and of itself, is insufficient to improve productive infrastructure critical to small-scale agriculture.

28 In this light we call on Finance Ministers to commit at national level to:

- a protect and ensure national food security by providing the necessary fiscal and monetary mechanisms;
- b promote public investment in infrastructure that supports small-scale agriculture and rural development and ensure that these are effective for women farmers given the gender biases that operate against them;
- c work with their colleagues in trade ministries to formulate a coherent strategy that supports the productive structures needed for improved export performance, including policy and financial support to the indigenous productive sector and an improvement in the competitiveness of primary commodities; and
- d advocate for flexibility in creating special borrowing and lending windows for small and subsistence farmers to enable them continue production.

29 At the level of IFIs, we recommend that Finance Ministers:

- a support calls for the exemption of key sources of food security from liberalisation;
- b advocate a reappraisal of IFI loan conditionalities and policy advice regarding the productive structures of the economy and policies that contribute to the oversupply of agricultural market products; and
- c push for flexibility in finance policies to support food security.

### Sustainability of debt and the trade system

30 In 1970, developing countries as a whole owed only \$72.7 billion, or less than 10 per cent of their collective GDP, to the rest of the world. By 2000, this figure had skyrocketed to \$2,527 billion or 37 per cent of GDP.<sup>3</sup>

31 The Highly Indebted Poor Country (HIPC) Initiative is being extended beyond 2004, but with weak commitments by donors. To date, the Initiative has been unable to fulfil its very modest goal of achieving debt sustainability in 42 countries, with debt burdens representing only eight per cent of total developing country debt.

3 2002. Pettifor, A. and R. Greenhill. Debt Relief and the Millennium Development Goals. Jubilee Research at New Economics Foundation. UNDP Human Development Report Office. Occasional Paper. Background Paper for HDR 2003.

32 The debt sustainability proposal which will be presented for consideration at the 2004 annual meetings of the IMF and World Bank would establish a country-specific debt threshold for each borrowing country based on its debt burden, vulnerability to shocks and its scores on the CPIA. We cautiously welcome the fact that the debt sustainability proposal would abandon a uniform debt threshold in favour of country-specific thresholds. However, we are concerned that the threshold will be "policy-dependent," with each country's performance, measured by the CPIA, considered a principal input to calculation of the threshold.

33 We believe the proposal is unlikely to ensure sustainability as it does not adequately take into account the impact of external trade policies and dynamics on the levels of debt of indebted countries, an impact that has been recognised by the World Bank.<sup>4</sup> A sustainable exit from debt cannot be achieved in the absence of measures to ensure that when existing trade rules and the trade policies promoted by the IFIs are considered jointly, they allow developing countries to reduce their debt levels.

34 Moreover, under this proposal, if governments exceed their debt threshold, their capacity to borrow will decline and eventually cease. Already, there are 34 countries that will be grant-dependent in the 14th replenishment of International Development Association (IDA) resources. Although more countries will find themselves increasingly reliant on external grant financing, the IFIs project that the demand for grants could far outstrip the supply. This shortfall could cripple efforts to meet the MDGs in many countries.

35 In light of this we recommend that Finance Ministers:

- a advocate with the IFIs for a holistic review of debt sustainability that takes into account the impact of constraints presented by current rules of the trade system in the ability of countries to achieve sustainable levels of external debt;
- b work with their colleagues in trade ministries in order to ensure that national debt and trade negotiation strategies, when considered jointly, protect the policy space needed to:
  - ▶ upgrade the productive structure to move into export of more dynamic products with higher skill and technology content
  - ▶ ensure greater value added to exports
  - ▶ diversify the economy and nurture infant industries
  - ▶ provide adequate levels of financing, in affordable terms, to the indigenous productive sector and
  - ▶ improve and stabilise the prices of primary commodities; and
- c demand that donors - together with the IFIs - provide deep debt relief to HIPC countries under conditions that are not onerous; the IFIs should reconsider proposals that could lead to the establishment of a rules-based, sovereign debt arbitration process.

36 If the IFIs apply the debt sustainability framework, this should be done in stages, as bilateral and multilateral grants become available to help successive groups of countries make the transition and advance progress toward the MDGs.

## Compensatory financing for trade-related losses

37 The costs and losses of trade liberalisation for many developing countries have been further exacerbated by the imbalances of the existing trading system. These imbalances have been perpetuated by weak special and differential treatment (SDT) measures, lack of commitment to beneficial market access and insufficient and ineffective preferential trade arrangements for LDCs.

38 While there is an urgent need for financial compensation for these losses, it is important to acknowledge that these imbalances call for fundamental changes in the trading system and cannot be addressed by compensatory financial measures alone. Furthermore, it should be acknowledged that, when not provided in the form of grant financing, compensatory financial measures lead to the undesirable result of increasing debt for liberalising. Additionally, these measures do not ensure that workers and producers who bear the direct cost and impact of trade liberalisation processes are the actual beneficiaries of compensatory financing.

39 In light of this, we recommend that Finance Ministers:

- a promote the establishment of compensatory financing mechanisms suitable to the sustainable development needs of countries, recognising the limitations of any mechanism that relies on financial transfers to compensate for trade losses originating in the imbalanced trade process and rules; and
- b call for the strengthening of SDT and preferential market access arrangements with mechanisms that take into account the irreversible nature trade of liberalisation agreements vis à vis the specific, short term timeframes for financing measures and, at least, guarantee:
  - ▶ additional resources in the form of grants or concessional financing
  - ▶ fast and automatic access by countries affected by trade-related losses. Mechanisms should not be linked to implementation of adjustment measures within or outside the context of an IMF programme and the assessment of trade losses should be carried out by an independent body to avoid conflict of interest
  - ▶ comprehensive coverage of all costs that relate to the trade liberalisation process, including terms of trade losses and costs associated with the diversification and upgrading of the economy.

## III Conclusion

40 We thank Ministers for taking the time to consider our recommendations and acknowledge and appreciate the space provided by the Commonwealth for civil society organisations to participate in such meetings.

41 As we prepare for the 2005 reviews of the implementation of the Monterrey Consensus and the Millennium Development Goals, we call on Ministers to continue to engage in dialogue with us and encourage further collaboration and partnership.

<sup>4</sup> See World Bank, *Debt Relief for the Poorest. An OED Review of the HIPC Initiative, 2003*, p. 81. ("Most countries became severely indebted in response to terms of trade shocks and a subsequent decline in revenues, but continued maintenance of overextended public sectors.")