IDEAs Conference on International Money and Developing Countries: Theoretical and Policy Issues in the Current Context

16-19 December 2002, MGM Beach Resorts, Muttukadu, Tamil Nadu, India

International Development Economics Associates (IDEAs) recently organized an international conference on "International Money and Developing Countries: Theoretical and Policy Issues in the Current Context". This conference was held during 16-19 December 2002 at the MGM Beach Resorts, a hotel near Chennai, India. A number of noted scholars from across the world participated in the conference. IDEAs also funded some young scholars from across Asia to attend the conference. A detailed list of the participants is given in the annex.

This conference was held in the backdrop of increased awareness about how international financial flows shape the context and limits the possibilities of macroeconomic policy in developing countries far more than ever before. The objective of the conference was to have a thorough investigation into the nature and workings of current capitalism as a world system and provide better understanding about the precise nature of the limitations that that the current international financial system imposes. The conference also looked into policy alternatives which are more appropriate to the needs of developing countries than the standard neo-liberal prescriptions.

The conference was held over three and a half days, beginning on the morning of Monday 16 December 2002 and was concluded by lunchtime on Thursday 19 December. The first three days had three sessions each. On each of these days, the first session had three papers followed by one paper in the second session. The final session of the first three days consisted of a panel discussion. On the final day, panel discussions in the morning concluded the conference.

Monday 16 December

Session 1: Theoretical Issues

The first session was on theoretical issues and had three papers. The first paper was by **Prabhat Patnaik** titled "The Theory of Money and World Capitalism". This paper looks at a fundamental divide in economics, which springs from differing perceptions about money, between those who see capitalism as a crisis-ridden system and those who celebrate the "invisible hand" of the market. This paper argues that any attempt to determine the value of money exclusively from the sphere of demand and supply is logically flawed; and that,

consequently, monetarism is not just unrealistic theory, it is logically faulty as well. This argument when extended to a multi-country multi currency setup, leads to the conclusion that the removal of restrictions on capital flows in the name of "globalization" is harmful for the third world. It follows that protectionism in the third world has the effect of raising the level of activity in their own economies as well as in the world as a whole.

In the second paper of the session, **Franklin Serrano** presented a paper titled "From 'Static' Gold to the Floating Dollar". This paper discusses some essential features of the balance of payments position of the country which issues the key currency under different international monetary standards. Using a Sraffian framework, where the monetary rate of interest of the central country is seen as an independent policy variable, this paper discusses the historical evolution of the international monetary system and criticises some "monetarist" hypotheses which are implicit or explicit in many well known, and often otherwise critical, analyses of the subject. Following the analysis of the theories and experiences of the earlier international monetary standards, this paper provides a simple but sufficiently precise characterisation of the current international monetary standard, that it calls the "floating dollar standard".

The third paper of this session was titled "Reflections on Currency Crises" and was presented by **Korkut Erturk**. This paper analyses currency crises of the 1990s at different levels of determination and reviews the first, second and third generation models of currency crisis. According to this paper, looking at the currency crisis at the national level, they can be seen to signify the pitfalls of betting on financial liberalization to attract foreign capital on a massive scale. Looked at the level of the international monetary system, according to the paper, many of these crises are caused by a new breed of speculative attacks that have beleaguered global financial markets in recent times where expectations tend to become self-fulfilling prophecies. At this level, abrupt reversals of capital flows caused by so-called contagion effects expressing capricious shifts of investor sentiment emerge as the main problem. The paper also suggests that the currency crises can also be looked at the level of the structure of international trade and the world economy and argues that the deteriorating terms of trade of might have played a role in the recent currency crises.

Session 2: Overview of Liberalisation Experience

In this session, **Lance Taylor** presented a paper titled "External Liberalization in Asia, Post-Socialist Europe, and Brazil" This paper reviews the experience of 14 countries with external liberalization and related policies. Based on different national case studies written by authors

following a common methodology, this paper summarises how diverse economies responded to a similar "reform" packages and offers lessons about ongoing institutional change and how it might be guided by sensible policy to help support economic performance better in the future than it has been in the past.

Session 3: Current world conjuncture and its implications

Panel discussion with Thandika Mkandawire, Cui Zhiyuan, Alex Izurieta, Sunanda Sen, Chair: Jomo Sundaram

Thandika Mkandawire spoke about the growing unilateralism in today's world and weakening of the nation state. While there is need for democratisation of the nation sates, equally important is a change in the global system that is currently in place. Professor Sunanda Sen discussed the implications of the current conjecture of financial liberalisation on developing countries. She spoke of the dangers of the retreat of nation states and advances of the market, as these are loaded in favour of the interest of the MNCs in industrialised countries. Alex Izurieta discussed the causes behind the expansion and slowdown in the US economy, the main features of these cycles, and concluded that the imbalances that drove the recent expansion in the US were allowed to continue for much longer, and deeper, than the point at which both financial resolution and growth resumption could happen simultaneously and painlessly. Putting forward an empirical tool to analyse the world economy that would be beneficial for a coordinated global reflation is the need of the hour.

Tuesday 17 December

Session 1. Changing Structures in International Finance

The first paper of the first session on 17th December was by **Jayati Ghosh** and was titled "Independent or Irrelevant? Notes on the Political Economy of Central Banking in the Brave New World". In this paper the author argues that though mainstream economists try to portray central banks as the dominant agency that effectively determines both the microeconomic conditions of the financial sector and the aggregate macroeconomic stance of the economy, in the current macroeconomic scenario, financial liberalisation and financial innovation have rendered the central banks comprehensively incapacitated. The paper suggests that in spite of the demise of the importance of the central banks, "central bank independence" continues to be a popular theme among the policymakers because certain rentiers and other groups, who are more interested than others in keeping inflation low, can benefit from such an arrangement. The author also points out that autonomy of central banks has not helped

developing countries attract more foreign resources but has reduced their control over their domestic monetary policies.

The next paper was by **Ajit Singh** and was titled "Capital Account Liberalization, Free Long-Term Capital Flows, Financial Crises and Economic Development". This paper examines the theoretical and empirical case for full capital account liberalisation in developing countries (DCs) and finds it unconvincing. Indeed, analysis and evidence presented here point to a strong case against it. The second part considers the liberalisation of only the long-term capital account, particularly FDI - a form of inflow favoured by most economists. This paper argues that a multilateral agreement on investment, which denies countries the discretion to regulate FDI, will not be in the interests of DCs.

The final paper of this session was by **C. P. Chandrashekhar** and was titled "New Financial Structures, Transmission Mechanisms and Deflation in the Global Economy". This paper starts with an analysis about how and why the structure of the world's financial system has transformed in the last two decades. This paper then goes on to discuss the worldwide domination of finance capital over manufacturing capital and the global impact of financial liberalization. This paper concludes that the dominance of finance capital slows world growth; desynchronises the economic cycle across countries; strengthens economies like the US and UK with stock market-based financial systems; weakens successful late industrialisers like Japan and countries in East Asia whose predominantly bank-based financial systems are substantially restructured; and enhances volatility in the so-called emerging markets of developing countries and adversely affects their real economic growth. But in the process of doing so, the process encourages speculation, and fraudulent accounting and management practices aimed at sustaining the speculative boom.

Session 2: Is Africa Marginalised?

The paper in this session was on "Maladjusted African Economies and Globalisation" by **Thandika Mkandawire.** During the last two decades liberalisation of trade, privatisation and reliance on markets have replaced the widespread state controls associated with import substitution in Africa. However such changes have failed as a prerequisite for development, let alone as a 'strategy for accelerated development'. The key 'fundamentals' such policy changes have sought to establish relate to these financial concerns rather than to development. The Structural Adjustment Programme, due to its deflationary bias, has placed African economies on a low growth trajectory. The "low-growth" path that the BWIs have placed

African economies on, and the one they seem to have resigned to, will not only lead to Africa's greater "marginalisation" but will deepen poverty in African economies.

Session 3: Panel Discussion with **Nirmal Chandra, Berhanu Nega, S.K.Rao**

The broad theme of the panel discussion, chaired by Utsa Patnaik, was **'International Institutions and Their Role'**.

Berhanu Nega felt that poor performance of World Bank and IMF assisted countries in Africa is largely attributable to the lack of a proper understanding of the conditions in Africa by the Bretton Woods institutions. This has resulted in reduced confidence in these institutions in Africa. Further, with Africa particularly in mind, he felt that there is a necessity to explore the link between the state and society, on the one hand, and the international donor institutions on the other. This is particularly important in a situation when the link between the state and the society are weakened or broken.

Professor **Nirmal Chandra** was of the view that the ability of international institutions to keep the MNC's and other players of the new open global economy in line with the developmental objectives of the developing nations should be enhanced. For example, he advocated the application of the U.S bankruptcy laws and India's laws against bonded labour to the global economy through the international institutions.

Professor **S.K.Rao** said that the attempt of the G-7 countries to create a less risky financial system has not yielded anything of that order because of the breaking down of the walls between credit banking, futures markets, stock broking etc., financial innovation resulting in new instruments, consolidation of markets and the functioning of the international institutions themselves. He observed, with the IMF in mind, that the response along the lines of enforcement of codes and standards, establishment of credit lines and collective action to deal with default only added to risk.

Wednesday 18 December

Session I: Patterns in Emerging Markets

This session started with **Erinç Yeldan** presenting his paper "Behind the 2000/2001 Turkish Crisis: Stability, Credibility, And Governance, For Whom?" The author argues that contrary to the official wisdom, which suggests that the crisis was the result of the failure of the public sector to maintain the austerity targets and the failure to fully implement the free market

rationale of globalization, the current economic and political crisis in Turkey is not the end result of a set of technical errors or administrative mismanagement unique to Turkey, but is the result of series of pressures emanating from the process of integration with the global capital markets.

The next paper in the session was on "Trade And Financial Liberalization and Its Effects on Growth, Employment and Income Distribution in Latin American Countries" by **Carlos Aguiar de Medeiros.** This paper argues that given the diversity of experiences of liberalization in the continent and the superposition of many economic and social changes, to identify and even more to isolate the effects of trade and financial liberalization on income distribution it is not a simple question. This paper tries to address this issue by looking at how the balance of payment constraint has historically influenced the income distribution in Latin America countries; the determinants of the large capital flows and their connections with balance-of payment liberalization in the continent; and evidences on growth, employment, relative prices, wages and income distribution in the continent. The last section explores some questions for future research.

The final paper in this session was by **Arturo O'Connell** titled "The Recent Crisis of the Argentine Economy: Some Elements and Background". Arturo's paper examines some of the long-run trends in the Argentine economy and its performance during the 1990s. He also studies the development of severe imbalances that led to the Argentine crisis and the interaction among the various imbalances as intensified by the peculiarities of the Argentine economic-institutional set-up. The final section is a brief description of the major events over the first half of year 2002 and the unresolved problems that stand in the way of a recovery and return to some normal economic and political life in Argentina.

Session 2

In this session **Sushil Khanna** presented a paper titled "Has India Gained from Capital Account Liberalisation? Private Capital Flows and the Indian Economy in the 1990s". This paper discusses the effect of foreign capital inflows on the Indian economy. The analysis in the paper shows that at a macro level, India's economy has not benefited from the increased short term capital flows in the Indian economy. But the ebb and flow of short term capital forced the Central Bank to pursue a counter cyclical monetary policy and to stabilise the rupee in the foreign exchange market. The micro analysis of the stock markets fails to provide any evidence that the entry of foreign institutional investors has reduced the cost of capital to

the Indian corporate sector or has helped the corporate sector to shift from their dependants on internal resources and funds from public sector development banks to the capital market. The paper concludes that the overall cost to the economy of increased short-term capital flows has been substantially higher than any current or potential benefits.

Session 3: Panel discussion with **Jomo Sundaram, Nilufer Cagatay, Abhijit Sen**

The broad theme of the panel discussion, chaired by Professor V. K. Ramachandran, was **'Macroeconomic Policies in Developing Countries'**.

Professor **Jomo Sundaram** explained that the reasons why underdeveloped countries are worried about international financial liberalisation. According to him, first, it is accompanied by a strong macroeconomic deflation, and secondly, because of the erosion of the potential for financial instruments to have macroeconomic interventions and impacts. He felt that there was a need to recognise other fiscal instruments available other than monetary policy alone as well as to promote macroeconomic policies that can influence redistribution and growth.

Nilufer Cagatay observed that fiscal retrenchment, contrary to the claims of growth has resulted in lower growth rates than in previous periods, increased capital mobility and volatility and more crises. This has resulted in increasing demands for social nets and public expenditure as well as a massive redistribution towards the 'haves' relative to the 'have-nots'. She also felt that in these crises and inequality, the impacts were greater on the lives of women than men.

Professor **Abhijit Sen** felt that challenge and question before the developing countries was of "how to get macroeconomics back". In other words, given the fact that the only option for them is to either remain a part of the system or fall out of it, with differing impacts though, how do developing countries regain their policy autonomy?

19 December

Session I: Alternative strategies

Panel discussion with Terry McKinley, Ritu Dewan, Gerald Epstein and Suraj Kumar. This session was chaired by Manuel Montes.

In the morning of December 19, the last day of the conference, four panelists participated in the discussion on 'alternative strategies'. Terry McKinley said that we all know the strategies to which we are trying to provide an alternative. The challenge before us is to put forward a viable alternative, a major concern of UNDP as well. We need to try to embark on our

poverty reduction programmes within the overall development framework of the country. Public investment needs to go up, rather than the other way round. Asset redistribution and land reforms need to be taken up on a priority basis. We need to adopt more labour-intensive growth strategies, but not by throwing everybody back into agriculture. In a word we need a larger, stronger, more active, and more developmental state. Ritu Dewan talked about the need to harmonize our roles as activists alongside the ones we take up as economists. We need to define all concepts by our own parameters, and not get dictated by the neoliberal agenda. She cautioned against the tendency to believe that all old institutions are progressive, and stated how the elections are fought on people's issues, but once the elections are over the electorate is attacked. She talked on the issue of violence of different kinds that are taking place everyday-against some particular religion, against sovereignty of nations, against the poor, against women. The violence is getting internalised and is related to the attack on our economic rights. Another important issue outlined by Ms. Dewan is the impact of globalization on land markets and rural livelihood. Gerald Epstein talked about the possible alternatives to inflation policy. He discussed the five pillars of inflation targeting, and talked about the urgency to reform Central Banks of countries. He said that Central Banks of countries should actively promote investment and implement growth targets through democratic processes. Most Central banks are not even aware of the relationship between instruments and targets. There is a need for new instruments, and for the Central Bank to make more connections with the civil society.

The final session was an open discussion on future research agenda chaired by C. P. Chandrasekhar.

List of Participants
Conference on International Money and the Macroeconomic Policies of Developing Countries

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Muttukadu, Tamil Nadu, India

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