

TRANSCRIPT OF DEVELOPMENT DRUMS [EPISODE 3 - WASHINGTON]

Host: Owen Barder. Guests: Ngaire Woods and David Roodman

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Owen Barder

Hello and welcome to the third edition of Development Drums, recorded on the 23rd of October 2008. Development Drums is a podcast about the current news in international development and the fight against global poverty. We summarize the main stories affecting development and try to offer some insights and opinions behind the headlines.

Today we have got two really big issues to discuss, both relating to the current international financial situation. First, we will be looking at proposals for the reform of global institutions, and then second, we will be looking at the possible impact of the financial crisis on developing countries. And I am joined by two real experts on these subjects. Ngaire Woods is Professor of International Political Economy at Oxford University and the director of the Global Economic Governance Program, which is a research program investigating how global institutions could better respond to the needs of developing countries.

Ngaire, welcome to Development Drums.

Ngaire Woods

Thank you, Owen.

Owen Barder

And my second guest is David Roodman, joining us from the Center for Global Development in Washington D.C. David is the architect of the Commitment to Development Index, which ranks the world's richest countries based on their adoption of policies that affect developing countries and it is widely recognized as the most comprehensive measure of rich country policies towards the developing world.

David, good morning.

David Roodman

Great to be here.

Owen Barder

The United States announced on 22nd of October, yesterday, that it would host a summit on November to discuss the causes of the financial crisis, to review progress being made to address it and to start developing reforms needed to ensure that it doesn't happen again. Interestingly, this isn't just going to be the G8 leaders, but the G20. The G20 consists of the G8 countries, that's Canada, France, Germany, Italy, Japan, Russia, the U.S. and the UK, together with Argentina, Australia, Brazil, China, India, Indonesia, South Korea, Mexico, Saudi Arabia, South Africa, Turkey and the European Union.

Our current arrangements can be traced back to the Bretton Woods conference in New Hampshire in 1944. That meeting established fixed exchanged rates, it established the IMF and the World Bank. Now, proposals for reform of these arrangements go back to before the current financial crisis. In a speech that is now looking quite prescient, Gordon Brown spoke about this in November in 2007. He called for a new coalition of democracies, a transformed IMF with a new mandate for crisis prevention, a World Bank with strengthened focus on poverty reduction and environment, and a new role for the UN in environmental protection. In the last week he has gone even further, calling for a new Bretton Woods conference. He has asked for an international financial system around agreed principles of transparency, integrity, responsibility, good housekeeping and cooperation. So let's ask Professor Ngaire Woods to take us through this.



Ngaire, you wrote a book, *The Globalizers*, a couple of years ago, which looked at the future of the World Bank and IMF and you pointed out that these organizations have been losing traction in the international system as emerging market borrowers like Brazil and Argentina have repaid their loans and are not borrowing as much as they used to and you called for reforms to make the organizations more responsive to their borrowers. And just last week, you pointed out that the IMF's role in the current crisis has been remarkable by its absence. They have not shown any sign of playing a leadership role. So Ngaire, why is the IMF on the sidelines at these discussions at the moment?

Ngaire Woods

Well, the IMF is on the sidelines because it's not been the first place that central bank governors and finance ministers around the world in difficulty have run to. Instead they have each tried to do their own thing and make a few bilateral phone calls. So you know, Hank Paulson doubtless has called central bank governors in other places. That's not an efficient way to resolve this crisis. If they had all headed to the IMF and had a plan that was collective, they would have had a much more effective solution. The IMF in turn, to have made that possible, would have had to have begun thinking creatively at least a year ago when this financial crisis began about what a collective bank bailout may look like. Even if the scenario looked unlikely then, the IMF is a place for creating ideas that will help financial stability should have been thinking along those lines.

Owen Barder

Ngaire, I remember when I was a young treasury official working on international economics in the Mexico crisis, we all turned to the IMF as the convening place to discuss what rescue plan would be put in place. Now, I am pretty sure, the IMF hadn't cooked up a plan in advance, but they even ten years ago seemed to have a convening power that they don't have now.

Ngaire Woods

Yes. I think that is right. Ten years ago, the IMF was much better placed to be used by the G7 to tell emerging economies like Mexico, like Korea, like Argentina, what to do. And so, it was a natural place for the G7 to head to, knowing that it would lower the cost of any bailout that G7 countries had to make and on the other side of the equation, it was a very effective way for them to call emerging economies into line. Now the difference today is the crisis isn't in emerging economies, the crisis is in America and Europe, and so the real weakness of the IMF has come to the fore, which is that it's not an organization which those countries have permitted to constrain themselves.

Owen Barder

So the original Bretton Woods conception in 1944 was that the IMF wouldn't just focus on emerging market economies in developing countries, but that it would actually be a mechanism for the industrialized economies as well. What's the problem with the Bretton Woods conception? Is it that the world has changed and what was designed then doesn't apply today or is it simply that we never implemented properly what was envisaged by Keynes and others in Bretton Woods.

Ngaire Woods

I think it's a habit, it is a longstanding habit that the G7 have acquired since the late 1970s of using the fund and using the bank as a way of intervening in developing countries rather than using them as forum for multilateral negotiations. I mean, even most recently, when the IMF began financial sector assessment program and this is the one instrument that might have been relevant to this crisis, that is to say the IMF would assess the robustness of financial systems in different countries, having pushed for the IMF to do this, the United States was the very first country to refuse to do it and it did not agree to take part in such a program until July of this year. So it just underscores the sense to which the institutions became in the minds of G7 countries a way to get other countries, not themselves but other countries, to do what they wanted and that means they can't be institutions of cooperation.

Owen Barder

Interesting. So what significance do you attach to the inclusion of the whole of the G20 in these summits that President Bush announced yesterday. Is this the beginning of the end of the G8 as the major drive of the international system, is it a sign of a new era of global power?



Ngaire Woods

Yes. The shift has already come, hasn't it? The United States have become the world's largest debtor, Europe now has a huge crisis that needs to bailout and where are the world's reserves, the world's trillions of dollars worth of reserves are sitting in emerging market economies. So if you try to deal with this crisis without the very government to announce sitting on trillions of dollars worth of reserves would have been like trying to build Bretton Woods without the United States back in 1947.

Owen Barder

So what would these new institutions look like?

Ngaire Woods

Well, I think if the IMF is really going to be at the center of the kind of cooperation we are going to see at the meeting that's going to happen in Washington, it needs root and branch reform. We have to go right back and ask, what would the emerging economy, those who are actually sitting on trillions of dollars worth of reserves, what would they need the institution to look like for them to have confidence that it was their institution as much as the institution of the United States and other G7 members. And that means going right back and saying in what country should the institution be headquartered, who should decide who its leader is, what countries should be staffed, where can the institution come from and how a decision is made in the institution.

Owen Barder

Does that mean Ngaire that we need, does that mean that we need an institution that does the same as was envisaged in Bretton Woods, but simply with a different governance structure, that it's just a question of the ownership of the institution or does its function need to change compared to what Bretton Woods envisaged.

Ngaire Woods

No. The functions of the IMF already changed dramatically within months of the original charter being written. The institution has to be adaptable and that is where governance is important, because if you got the right governance structure the members can adapt the institution. So the IMF might become, for example, the institution in which a new collective way of bailing out banking sectors is organized. That was never envisaged at the outset but it could become that if its members want to. But for it to become that and for its members to be able to ensure that it's doing what they want they have to be included at the table. That is to say the big emerging economies that actually have the power, the authority, the resources to help resolve this crisis, have to feel that this is their forum, it's a forum they can trust.

David Roodman

Can I ask you a question, Ngaire?

Ngaire Woods

Yes.

David Roodman

It sounds to me like you are talking about two different problems here and there is no contradiction there but, just as someone trying to understand, I want to separate them. One is the lack of legitimacy of the IMF or similar institutions in what we call developing countries because they have very little role in its governance. And therefore has lack of legitimacy there. The other problem is that the rich countries themselves, who are the major financiers of these institutions have not really shown the willingness to submit themselves to its governance. Right, that was why the original IMF broke down, as I understand, as Nixon took the United States off the gold standard and the rich countries in the end were not willing to submit themselves to the discipline that was imagined that the IMF could help them impose on each other.

So those are two different problems. One is about whether developing countries should have more voice, the other is about whether rich countries should be willing to cede in some sense more sovereignty to this institutions for the collective good.



Ngaire Woods

But right at the corner of that is the reason why they are linked. It's not the rich countries that finance the IMF. And as I say in my book, it's the borrowing countries that finance the IMF and it's because the borrowing countries, the major emerging market borrowers have walked away that the IMF now has a financial crisis. It's made 600 of its senior staff redundant over the last year. And that's because emerging markets are not choosing to borrow from it and it poses the question so who is going to pay for the organization now.

Owen Barder

Can I focus on what impact this will have on developing countries and what you are talking about is the greater role in the IMF for the emerging market economies, for China, for India, for Brazil. What about the poorest countries. Are they – there was talk earlier in the year that they needed a greater voice both in the IMF and the World Bank. Are we now going to lose our focus on that and simply focus on the IMF as a solver of financial crisis and is that a bad thing if that is where we go?

Ngaire Woods

I think the argument for why poor developing countries need more voice is an argument about responsiveness. That if the IMF is going to be very effective in the poorest countries, it needs better to understand what's going on in them and that the way to do that is to give those countries more voice, but it's also to make sure that nationals from those poor countries are more represented on the staff, you know, there are similar arguments to how you reform them to make them more responsive to those countries.

Owen Barder

I'm going to ask each of you this question, yes or no. Do you think that the kind of change that you are describing, Ngaire, is actually going to happen as a result of this processes now being launched to people talking about a new Bretton Woods II or do you think it's too difficult for people with entrenched positions to move in that direction?

Ngaire Woods

I think we are going to see a brand new form of multilateral monetary cooperation and financial cooperation and the IMF will either be completely marginal to it or will manage very rapidly to transform itself to be part of it.

Owen Barder

And, David, what's your view?

David Roodman

Well, I've thought much less about this than Ngaire but I would offer two thoughts. My guess is that change is going to be much more incremental. Maybe that reflects my own lack of vision. But first of all, I visited the IMF website this morning and the headline is that basically countries are trying to knock down their door, 'IMF In Talks On Loans To Countries Hit By Financial Crisis'. So Pakistan is coming to them, Belarus, Hungary. And so it's looking like we may see a return to some of the older patterns we saw in the last financial crisis where the IMF does start to play more of a role. It's interesting though that and on the IMF's website one of the things that highlights is that it says the loans will be quick disbursing with fewer conditions than in the past.

So the IMF itself, I think, has been bruised by its own history with trying to impose a lot of conditions on borrowing countries in return for the finance and, and as Ngaire says as a result lost all its clients, lost almost all of its customers. And so this time around it's going to, I guess we are going to see a kinder, gentler IMF or at least that's what they're saying this time we will see what actually happens. But it does seem like there is a possibility there for incremental change in how the IMF behaves with respect to developing countries.

When I try to understand what has happened with this crisis and what the policy implications are for what we call the international financial architecture. I see it in three stages. The first is what are called the global



imbalances which we can think of in cartoon version as China lending a trillion dollars to the United States. That is one source of the fuel for the bubble that just burst. And so that in itself is part of the problem.

The second stage has to do with how the bubble actually played out through the credit system in the United States and in other countries and when one wants to think about how to prevent that from happening again you are talking about more regulation, better prudential supervision in banks and so on. And the third stage was the way that the crisis once it started spread internationally very quickly.

And so we can ask at each of these stages what is it that the international financial system, or international financial organizations should be doing to make this not happen again. It seems to me whether it's the realistic prospect for progress would be on the second stage which is better supervision of financial institutions, so that these kinds of bubbles don't do as much harm when they occur. And that leads to a discussion of Basel II and what I guess maybe would be Basel III improving international norms for supervision of international financial institutions. So what I am suggesting is we might see incremental change in both the IMF and in the Basel type arrangements but perhaps Ngaire can correct me on this.

Ngaire Woods

I very much agree with you that first that the IMF is going to have a lot of countries knocking on its door. But its capacity to respond to those countries is lesser partly because it's lost a lot of its staff and that's another reason which quite positively could lead to it doing faster disbursing, less conditional loans, it simply doesn't have the staff to deploy to do large and intricate multiple conditionality loan packages.

I think that that is certainly going to happen but how the fund when it does that, what credibility is going to be acutely watched not just by the G7 countries, but by the other countries as well because it's the other countries who are going to be affected both directly and indirectly from the falling out of this. Which goes to an issue that about the consequence of this crisis for development and the fact that I think we probably all agree that this crisis will lead to a dramatic reduction in aid and a dramatic reduction in the resources made available for developing countries. That's going to put a real onus on more effectively using the remaining aid that's made available to both countries. And I think that's another role that the institution should be playing and certainly the World Bank will be playing.

Owen Barder

So let's come on in a second to the impact of the financial crisis on developing countries and particularly on foreign aid. Before we do that, you touched there on the World Bank. A little noticed announcement in the development communication, in the recent annual meetings was an announcement that there was now a consensus that the next president of the World Bank would be appointed by open competition as opposed to simply appointed by the U.S. government as in the past and also that there would be a third chair for sub-Saharan Africa which at the moment only has two seats on the board of the World Bank, and that will now go up to three.

Is that a welcome step in the right direction? Is this just a symbolic gesture or, what do you read into those announcements?

Ngaire Woods

It's definitely not a symbolic gesture. The country that appoints the World Bank President is the country that holds that person to account. It's the country that decides whether after five years that person gets another five years. So it's not just about the passport of the person as the head of the World Bank, it's about who it is that holds to account, the person making all the hiring and firing and promotion decisions. Who it is that sets the goals for the whole staff of the organization and measures and holds them accountable to those goals. So it's a really big issue and the way that system works at the moment is that, it's very much the luck of a draw whether you get somebody competent or not. You know, Bob Zoellick is doing a very good job in lots of ways but this is luck of the draw. And in the end the countries who are really depending on the World Bank and providing a lot of financing to the World Bank by borrowing from it, those countries at the moment have absolutely no say. So I think it's a really important step.

David Roodman



Yeah, I think arguably, the historical lack of legitimacy of the IMF which is tied in part to how the managing director is chosen is arguably a source of the current crisis because the experience in the late 1990s, the countries like Korea in some sense having to absorb these insults to their national pride by borrowing from this rich-world institution was so traumatizing that it's one reason that many developing countries decided to build up large reserves, not the only reason. And that in turn is one source of the fuel for the bubble.

Ngairé Woods

Yeah, I think that's absolutely right. The only last thing I would say that the emerging economies, China are prominent among them, have become important donors in their own right, a lot of publicity as surrounded China's aid to Africa and so forth. And it means they have a real interest in trying to make that aid effective and to an ensuring economic growth in the countries that they are increasingly linked to. So they have an interest in making multi-lateral organizations that try to make that aid relationship more effective work in their own right, and I think that will bring a new expertise to the organizations, which will actually improve them.

Owen Barder

Let's hope so.

[Music]

Owen Barder

Great, let's turn now to the implications of the financial crisis for developing countries. Here in Ethiopia, the Prime Minister Meles Zenawi met recently with foreign ambassadors and I am told from somebody who was there that he allowed himself a little smile when he was able to tell that the banks in Ethiopia were quite safe from the direct effects of the credit crunch, precisely because the government of Ethiopia has ignored pressure from foreign governments to liberalize their banking sector.

Let's start with foreign aid. David, you've done an analysis published on the Center for Global Development website, and I'll put a link into the show notes for this podcast to your blog entry, which – you looked at four financial crisis since 1970, Japan after the real-estate and stock bubble, Finland, Norway and Sweden after their crisis in 1991. And in each case you found that aid decline sharply after the crisis. Norway cut aid by 10%, Sweden by 17% and Finland, which had the worst of the crisis, cut foreign aid by 62%. And you were quoted in the Washington post as saying that you wouldn't be surprised to see global aid flows fall by a quarter or maybe even a third.

So let's start perhaps with the United States. Barack Obama and Joe Biden have said in the debates that they would probably slow down their promise to double the U.S. aid. And John McCain has proposed a one-year spending freeze on everything except defense, veteran affairs and the entitlement programs. So what's your expectation of what could happen to U.S. foreign assistance as a result of the financial crisis, David?

David Roodman

Well, I also told the Washington Post reporter – I guess, I quoted Niels Bohr who said that predictions are difficult, especially about the future. He didn't put that part in the article, but so – but I chose my words carefully. I did not say that I predicted a quarter or a third fall globally. I just said I would not be surprised if it happened.

So I wouldn't go so far as to say I have expectations about where aid is going to go, but certainly history suggests that it's going to go down. Now, in Norway it only went down 10% and it recovered within a few a few years so that they had a mild crisis. In Finland and Japan, they had much more severe crises and aid fell roughly half in each. And so, I guess the question is where in that spectrum do donors as a group now lie. And it's probably in the middle somewhere, maybe not as bad – at least we hope it won't be as bad as Japan in the 1990s. But this is a pretty serious crisis and it's putting a lot of budgetary pressure already on rich country governments. So yeah, I would not be surprised to see aid fall significantly.



In the U.S. in particular, there are a set of forces at work on the aid number and some of them are positive and some of them are negative. On the positive side, the politics of aid really has shifted here in the last 10 years since the Jubilee 2000 debt cancellation movement, which brought together people on both the left and the right. Jesse Helms who was a famous opponent of aid ended his career actually supporting more aid and we see very strong support for foreign aid, especially in Africa from the Bush administration – the current Bush administration. And that shift I think is long-term and won't go away and is reflected in Barack Obama's promise to double foreign aid. I don't think a serious candidate has proposed that in at least a generation, if ever. So there maybe continuing support for foreign aid that we hadn't seen historically, which would push aid up.

And to move from the abstractions, one of the biggest U.S. aid programs now is PEPFAR, President's Emergency Plan for AIDS Relief, which is spending a lot of money to pay for treatment, HIV, AIDS treatment, which is very expensive and as one of my colleagues, Mead Over, has said is the world's first global entitlement. It's pretty hard to imagine cutting back that funding and taking people off drugs that are keeping them alive.

So there are some upward forces there. Also, it's easy to imagine U.S. aid to Afghanistan going up. On the negative side, U.S. aid to Iraq if probably going to continue to fall and there is of course the budgetary pressure we've already talked about. And there is still the strong faction in Congress that's quite skeptical of foreign aid in general.

Owen Barder

And, Ngaire, do you have a sense of what might happen in Europe?

Ngaire Woods

I think, as David was saying, in other crises, if we think about the crisis of '79, '80, '81 where you had a banking crisis, you had a food and oil price-hike, a food security crisis and rising security expenditures with the new cold war, you have got some of the same factors we are looking at today. And then it led to a dramatic reduction in aid. I mean, first, the bilateral donors, the individual countries, simply pushed their commitments over on to the IMF and World Bank that you saw this dramatic reversal of flows to Africa where Africa actually began paying back more money than it was receiving in a year in terms of aid. So there is real risk that we are heading to that same position now and that programs that have been put in place are simply going to be snatched away with very severe consequences for the countries concerned.

Owen Barder

And do either of you think that this is the result of a change in public attitudes, people saying, well, things are tough for me, I would like to help but we really we can't afford it? Or is it simply just the fiscal arithmetic that a treasury trying to balance his books, he's got less money to spend on discretionary programs like foreign assistance? Well how much of this is simply bookkeeping and how much of it is a change in mood?

David Roodman

I'd say it's both, they are interacting, there is budgetary pressure, so congress here in United States and of course the governments around the world, they are going to be asking where can we cut and they are going to cut first aid for people who don't vote in their elections and also the argument that we are having trouble here at home, why should we be sending our money overseas?

Ngaire Woods

So I agree very much with what David is saying, and I also think that the fact that aid might suddenly be switched off or turned down in the crisis, tells us something about the structure of aid and the extent to which the way most countries and most foundations are structuring their aid makes it very shiftable. It's – because it's often very short-term linked to sort of year-on-year goals. There is a structure to it which means that we can turn the tap on and off without too much cost to our own constituencies, to our own public reputations. I think that's a bigger point that needs looking at about aid.

Owen Barder



I think that's a really good point. I myself would like to see us gradually re-conceptualize aid not as an act of charity, but as an ongoing fact of social global justice that we will end up probably always transferring money from those who have most – some of whom – most of whom will be in rich countries to those who have least, most of whom will be in poor countries, and that I should be part of a – as it were a global entitlement program, as a matter of social justice rather than a discretionary decision of rich countries. But we seem to be a long way from that thinking about aid at the moment.

David Roodman

I think there is also a point to be made here about what the pattern will likely be if there is a global aid cut, because it won't be a uniform hair-cut, it's going to be a little bit more like a Mohawk, I suppose. Aid to Pakistan, at least from the United States will probably be fairly well protected, or if it is reduced, that will be for broader foreign policy reasons, not because of budgetary constraints. So a lot of aid is still motivated by geopolitical considerations and we know that generally those policy rationales are stronger than the argument that we need to do this for humanitarian reasons. So – and then we also have the AIDS treatment program now which is probably going to be relatively well protected. So that means countries that are not of geopolitical significance are going to see a disproportional cut. I would also guess that countries that are getting a lot of aid now for their size are going to see the larger cuts, because I think there would be some tendency among aid agencies when forced to choose between aiding fewer countries and giving less aid to each country will give less aid to each country. So they are going to make bigger cuts where their bigger programs are now so that they can still remain active in as many countries as possible. So that could be in donor darlings like Uganda, Ghana I don't know about Ethiopia, could see the largest cuts.

Owen Barder

It's been fashionable in recent years to say that aid is not all that important, not all that effective, not as important as private investment flows and remittances and so on. So should we worry about a big fall in aid or if aid isn't that important and isn't making that much of a difference, perhaps we should think that this isn't going to make – in the grand scheme of things this isn't going to make an enormous difference to what happens in developing countries?

David Roodman

Certainly a lot of aid is wasted, and some even does harm but in particular cases we can imagine that cutting aid would do a lot of harm. If it means taking people off of HIV or AIDS medicine it's very clear that that would be quite harmful. It is important not to exaggerate the role of aid. It's only one channel through which this crisis will transmit to the poorest countries.

Ngairé Woods

But I think an important aspect to this is that over the last decade the United States, Britain, European countries have created a real compact with countries. They have said if you countries commit to democracy, to healthcare, to poverty reduction, to all of these things we will give you aid. And now if in a time of financial crisis, those countries continue to do what the compact said they would do but we for our part simply switch the tap off, we are breaking the compact, we are exposing the asymmetry of it in the sense that if they stopped doing what they are supposed to do we can turn off the aid. But if they keep doing what they are supposed to do and we turn off the aid in any event I think we are breaking the compact where we risk increasing what I see as a great disillusionment in many aid receiving countries with what the so-called traditional donors have been doing. They will keep getting aid but they will keep getting, they will increase the amount of aid they are getting from other donors from China, from the Gulf States and from elsewhere.

Owen Barder

So this is all pretty pessimistic; you are both saying that you are seeing quite a substantial possibility of a big cut in aid and that's rather important. Is there anything that we can do to minimize this effect?

David Roodman

Well if we are going to reduce the aid quantity we could make up for some of that by improving the aid, the quality of the aid. Because there are all sorts of inefficiencies in how the foreign aid system works today, countries are – United States is still a major tier of aid meaning that it will give aid to most and say you



must spend it on our tractors or our contractors and that reduces their ability to shop around for the best deals and therefore reduces the value of aid. We have got an increasing number of donors both public and private operating in so many countries that if we could organize more specialization. So each donor works in a small number of countries that would reduce the fragmentation of aid and the administrative burden on the receiving countries. There is such huge opportunities for making the aid that we do spend work better.

Ngairé Woods

I agree with that and I think the risk is that aid will not only be reduced but that the aid that's ring fenced, the aid that's not touched is the worst kind of aid. It will be some of the aid to Pakistan, which is not good performing aid in terms of development outcomes. It would be ring fencing tied aid, in other words aid given to countries to buy American or European products. If the aid is reduced and the kind of aid that continued being given is the worst form of aid then we get a doubly bad outcome. So the alternative in the way in which I think commentators and policymakers can try to go in the opposite direction is to think of David's thinking of how can you more effectively use, improve the quality of a smaller quantity. That's going to take a lot of pushing by civil society, by government officials, by commentators, by academics, by scholars to really push governments so that there is an equal pressure on them to do better quality aid as there is pressure on them to keep tied aid or to keep ring fenced aid to Pakistan.

Owen Barder

And let's not give up on putting pressure on governments not to cut aid in the way that these rather gloomy predictions imply.

Let's move on now to the broader effects on developing countries. Clearly, it's not just the possible impact on aid, but, for example, the prospects for export led growth are diminished as demand falls in industrialized countries, there is a possibility of growth of protectionism, slower liberalization of trade, less market access for emerging economies and developing countries to the industrialized country markets. There is a danger of smaller remittances if migration to industrialized countries is chocked off by rising unemployment and of course there is a possibility of falling commodity prices which would mean that those countries that export commodities would see smaller endings. This sounds like a pretty potent mix of economic factors that could have quite significant impacts on developing countries. David, do you have any sense of, which of these are likely to come about, which of these, well, how big these effects might be?

David Roodman

I think they are all likely. It's difficult to say precisely what the magnitude of the effects will be but that will be substantial in many countries. What the crisis is highlighting is that rich and poor countries are now linked in many ways through this process of globalization and there are many good things about that. It has allowed China to reduce poverty quite quickly and grow quite rapidly through export led growth but now we are seeing the down side which is that these crises can transmit with incredible rapidity and in the end usually the aid crisis hurts those who are least able to protect themselves meaning the poor.

You can go down the list of the linkages between rich and poor countries, and as you have just done Owen and see the impacts, I think a really big one in Latin America perhaps especially Central America will be declines in the money that workers in the United States and Canada are sending home, what we call remittances. A lot of workers were coming to North America and were working in the construction industry which is now of course plunged in its activity and so the first people who get fired of course are the ones who are never even legally hired. And, so, for example, Honduras gets remittances equal to about quarter of its GDP or at least it did in 2006 and similar levels can be seen in El Salvador and Guatemala. And so those countries are going to be hit very hard for that particular linkage. We are already seeing plunges in stock markets and spikes in interest rates in many developing countries would reflect the growing reluctance of foreign investors to take a risk on those countries and that means it's difficult for companies to raise any finance and to grow and hire more people.

Owen Barder

Ngairé do you want to jump in?

Ngairé Woods



No, I think David has put it very well. I think that there was a moment in the crises when the rest of the world or parts of the rest of the world thought they could look on with tranquility as Europe and the United States imploded but that moment has passed and the crisis certainly will affect countries in all the ways that David suggested.

David Roodman

Owen?

Owen Barder

Yeah.

David Roodman

I think there is a distinction to be made here between the immediate effects of this shock and the possibility that rich countries, especially the United States, are turning an economic corner and there is going to be a permanent change in how our economies are structured. What I mean it's one thing for us to experience the shock and – and for that to send waves abroad. But what maybe going on here in slightly longer timeframe is that Americans, both corporations – well, corporations, individuals and the government are going to have to reduce how much they borrow. And in the United States that means we may be importing less of those manufactures from China and other countries. And so that can be could spell a more permanent change in the economic prospects for developing countries.

Owen Barder

Is there anything that we should be thinking about doing as a development community? Clearly we can't single handedly solve the problem of slow economic growth in the coming years or perhaps even in the longer term. But there are things that we could perhaps do to provide safety nets for the people who have least security and least ability to be cushioned from this kind of a shock. Is there anything that we should be doing now to put in place for these kinds of effects?

Ngairé Woods

I think that the one role the development community can be playing is to really as I said scrutinize, monitor and publicize the impact of the different measures being taken on communities in other countries in the world. I think that's what policymakers under great pressure from domestic constituencies don't get enough countervailing pressure from their own public because their own public simply doesn't know what the consequences are on other countries. So I think that's the role the development community can play.

David Roodman

Where this will really come to a head, the problem that the world's poor going to be most vulnerable to these shocks, is in cutbacks in domestic social spending in developing countries. The government of Argentina does not have the luxury that the United States has in that we can borrow our way out of this in a sense. The government of Argentina is going to have to cut back its spending and one area that's going to be particularly vulnerable is the very kinds of programs that can provide a social safety net for people who are hurt by this crisis. And so, if there is a way for the World Bank and perhaps even the IMF to buttress their finances so that those programs are not cut, that's probably one of the most valuable things we can do.

Owen Barder

It does seem to me that this crisis has exposed some weaknesses in the model of globalization and global capitalism that rather chime with the analysis that many people in civil society and kind of progressive internationalists have had. And is there not an optimistic view that says that this is, you know, although it will be painful for the next couple of years that this crisis will actually help us to remake a new global order with a more equal power structure, better governance, that there will be less hubris on the part of – of the rich nations and that this might actually give multilateralism the spur that it needs.

Ngairé Woods

I don't think necessarily. I mean I think the shift has already occurred. There is already a strong competition in aid in many countries in Africa posed by the fact that China has now become a donor so there is already a shift in how multilateralism works in some countries on that continent.



David Roodman

One important and optimistic thing that should be said is that this crisis will pass. Every other crisis has, even the Great Depression, didn't perturb the United States from its long-term economic development path. Our economy shrank for some years and then shot up above the trend during World War II and then settled back about where it would have been if the depression had never happened. But that is not to say that there won't be serious long run harm from this crisis if it means that poor children don't get enough to eat and therefore cognitively impaired for the rest of their lives in some countries. Or a few people even die because of the heightened poverty for a few years. They don't show up in GDP per capita figures.

Like Ngaire I'm not real optimistic about permanent changes in global – in institutions of global governance. I think the basic power structures in the world drive that and won't be dramatically different after this crisis. I do think that we are, with the likely election of Barack Obama and the end of the Bush administration in the United States, I do think that we were going to move away from the harmful hubris that we have seen on this side of the Atlantic for the last eight years and the election that's about to occur here in the United States could be a turning point election in the same way that Ronald Reagan's election in 1980 was. And United States is of course a shrinking actor on the world stage but it's still an important actor and we could see a more humble and cooperative foreign policy going forward here.

Ngaire Woods

I agree with that and I think American businesses need the government, whoever is elected at the next election, to engage much more multilaterally. They need a financial and banking regulation that puts the rest of the world on the same level playing field is then they need a trade negotiation round which actually does come to a conclusion because they are finding it so costly to have to deal with endless bilateral arrangements. I think in all sorts of areas there's a push from the forces that drive American policy back towards more multilateralism. In security, the expenditures in Iraq and the lack of progress and outcomes in Afghanistan I think have already pushed the United States to a more multilateral approach. So I think whether it's Obama or McCain I think we are going to see a United States government pushed by many Americans towards a multilateralism that they need to make their businesses work.

Owen Barder

Well thank you both. Although it's a depressing outlook it's a real call to arms as well to those of us engaged in development to make sure that we keep bringing to policymakers in industrialized countries evidence and analysis of the impact of this in the developing world and prescription for how aid can be sustained and spent better and how we can make sure that the impact of this crises on the world's poor is minimized.

That's all for this week's edition of Development Drums. I want to thank both my guests, David Roodman and Ngaire Woods. It's been great having you on. If you want to find out more about the history of the Bretton Woods institutions and some very practical analysis of the options for change I really do recommend Ngaire's book, *The Globalizers*, which you can get on Amazon.

And please do visit developmentdrums.org. Give us your feedback on this edition of Development Drums. We want to hear from you about what you like and what you didn't like about this podcast and what you want to discuss in the future and if you have suggestions for guests or you want to come on the show yourself please do get in touch.

From me Owen Barder here in Addis Ababa from David Roodman in Washington and Ngaire Woods in Oxford. Thanks for listening and I hope you will join us again next time.

