TWN
Third World Network
Website: www.twn.my

Briefing Paper

June 2020

Covid-19 reveals everything

The intertwined health and economic crisis calls for urgent responses, systemic reform and ideological rethink of the international financial architecture

Bhumika Muchhala

1. Introduction: Covid-19 requires urgent response and systemic reform

Covid-19 has swept across the world with staggering scope and speed, instigating a historically unprecedented public health and economic crisis of inestimable proportions. With the global economy and human society in near-total suspension for several months, every part of the world economy is experiencing upheaval. This has created sharp contractions and mass unemployment in manufacturing, trade, tourism, travel, retail and commerce. The global economy is projected to shrink by 5.2% in 2020, with 170 countries experiencing negative per capita growth.[1] The cost of the Covid-19 crisis to the world economy is projected to amount to approximately $9 trillion over the next two years.[2] The economic recession unfolding from Covid-19 is the deepest since World War II.

For the first time since 1998, global poverty will increase. At least half-a-billion people may fall into poverty by the end of 2020, with some 60 million at risk of being pushed into extreme poverty.[3] And the poorest countries in the world will undoubtedly be the hardest hit, further entrenching inequalities within and between countries. The World Bank estimates that sub-Saharan Africa will see its first recession in 25 years, wiping out nearly half of all jobs across the continent.[4] South Asia will experience the most severe economic downturn in 40 years.

Countries most reliant on global trade, tourism, external financing and commodity exports are likely to be hit the hardest. Developing countries have already experienced the greatest ever capital outflow of $100

---

1 World Bank. 2020. "Covid-19 to Plunge Global Economy into Worst Recession since World War II," Press Release, 8 June, https://www.worldbank.org/en/news/press-release/2020/06/08/covid-19-to-plunge-global-economy-into-worst-recession-since-world-war-ii

2 International Monetary Fund. 2020. *World Economic Outlook: The Great Lockdown*, April, https://www.imf.org/en/Publications/WEO/Issues/2020/04/14/weo-april-2020

3 World Bank. 2020. "Covid-19 to Plunge Global Economy into Worst Recession since World War II," Press Release, 8 June, https://www.worldbank.org/en/news/press-release/2020/06/08/covid-19-to-plunge-global-economy-into-worst-recession-since-world-war-ii

4 World Bank Group. 2020. "Covid-19 (Coronavirus) Drives Sub-Saharan Africa Toward First Recession in 25 Years," 9 April, https://www.worldbank.org/en/news/press-release/2020/04/09/covid-19-coronavirus-drives-sub-saharan-africa-toward-first-recession-in-25-years

Third World Network (TWN) is an independent non-profit international research and advocacy organisation involved in bringing about a greater articulation of the needs, aspirations and rights of the peoples in the South and in promoting just, equitable and ecological development.

Address: 131 Jalan Macalister, 10400 Penang, MALAYSIA **Tel:** 60-4-2266728/2266159 **Fax:** 60-4-2264505
Email: twn@twnetwork.org **Website:** www.twn.my

billion, amounting to five times the outflows during the global financial crisis of 2008.[5] Capital outflows have led to currency depreciations, while commodity prices collapse, global trade and supply chains come to a halt, and already existing debt distress across the developing world explodes into a debt crisis. Achieving the economic, social and environmental Sustainable Development Goals by 2030 may well become a dream deferred, as the pandemic threatens to reverse existing milestones on the SDGs.

The pandemic has pulled the curtain back on intersectional inequalities of every scale and form, exposing how embedded they are within our economic structures and social systems. The most marginalised in society experience vastly disproportionate health and economic distress. These include the elderly and immunocompromised, low-income communities and in particular women, children, migrant workers, informal sector and gig economy workers, the disabled, the incarcerated, refugees and those living in conflict zones. The reproduction of inequalities occurs in a global context of a hurtling climate crisis, social protests and uprisings, the rise of nationalism, discrimination and human rights violations, and unsustainable systems of consumption and production.

The public health crisis generated by illness and fatalities from Covid-19 across the world has cast a spotlight on the erosion of public systems, in large part resulting from decades in the neoliberal economic turn. The ramifications of the institutionalised bias of policy paradigms towards austerity, liberalisation, deregulation and privatisation are being revealed. The inadequacy of public health systems, public services, social insurance and social safety nets is in large part a direct consequence of public budgets that have been systematically cut over years if not decades.

Out of the numerous lessons illustrated by Covid-19, this briefing paper seeks to highlight three key points. First, the global governance institutions of the 21st century must channel the political will and policy action to protect the most vulnerable and hard-hit countries and communities. Second, the ideology through which the role of the state has been deployed to serve markets through institutions, norms and laws that protect and facilitate private sector needs at the expense of the public sector, needs to be re-evaluated. And third, the way forward should be led by a renewed multilateralism to carry out a global plan for economic and health recovery for developing countries. For long-term structural change to address inequalities and imbalances at all levels, systemic reforms to the policies and paradigms in the international financial architecture are required.

Global economic governance and policy choices will determine the fate of economies and people in the fallout from the Covid-19 health and economic crisis. There are four key areas that bear urgent relevance for developing countries in the coming months and even years.

First, sovereign debt is bound to accrue as fiscal expenses rise. Temporary debt moratoriums or suspensions provide temporary relief but are not cancellations. In the possible eventuality of a cascade of external debt defaults in the coming years, there needs to be a fair and effective sovereign debt restructuring mechanism.

Second, this pandemic has underscored the life-or-death imperative of fiscal space to respond to the immediate health emergency, with the United Nations Conference on Trade and Development (UNCTAD) estimating a $2 trillion to $3 trillion financing gap facing developing countries over the next two years.[6] While concessional loans and grants are being made available, Special Drawing Rights (SDRs) need to be considered as a low-cost and immediate fiscal resource. In the aftermath of the health crisis, a fiscal redirection away from austerity will be required in order to revive ailing public systems and social services. The very bias towards fiscal consolidation that has led to the erosion of public systems must not, in tragic irony, be upheld as the policy framework advised by international financial institutions for developing countries in the aftermath of the public health emergency.

5 Congressional Research Service. 2020. "Global Economic Effects of Covid-19," 1 May, https://fas.org/sgp/crs/row/R46270.pdf
6 United Nations Conference on Trade and Development (UNCTAD). 2020. "UN calls for $2.5 trillion coronavirus crisis package for developing countries," 30 March, https://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=2315

Third, capital account and other financial regulations are called for to respond to the panic deluge of capital out of developing countries. And fourth, progressive taxation, including on the financial sector, can mobilise additional financial resources urgently required in the economic fallout from the Covid-19 crisis.

A global crisis of unparalleled dimensions requires an unparalleled response in the short term and visionary reform in the long term. If we look to history, in the aftermath of World War II, European economies recovered only because the leading surplus government, the United States, intervened with the large-scale grant package of the Marshall Plan. Today, a multilateral plan in a similar spirit of solidarity, responsibility and political will is required for the recovery of developing economies, many of which do not possess the fiscal space for stimulus packages commensurate to their needs. The way forward in the long term requires a sustainable and equitable development paradigm that effectively addresses climate change. The three dimensions of the 2030 Agenda for Sustainable Development (environmental, economic and social) serve as a foundation upon which to reform trade, economic, social and environmental policies.

2. Debt cancellation and a restructuring mechanism are essential to recovery

In 2018, the total debt of developing countries, including private, public, domestic and external debt, reached 191% of their combined gross domestic product (GDP), the highest level on record.[7] Much of this debt is rooted in the skyrocketing levels of private corporate indebtedness, primarily in high-income developing countries. Almost half of poorer economies, eligible to the Poverty Reduction and Growth Trust (PRGT), have been assessed by the International Monetary Fund (IMF) to be at high risk of sovereign external debt distress or already in debt distress at the end of 2019. As the Covid-19 crisis unravels across developing countries, many of the most vulnerable states are up against a sea of debt servicing in the 2020s decade.

According to UNCTAD, in 2020 and 2021 alone, repayments on public external debt for developing countries overall are estimated at nearly $3.4 trillion.[8] This figure comprises between $2 trillion and $2.3 trillion in high-income developing countries and between $666 billion and $1.06 trillion in middle- and low-income countries. In a context where many developing countries are already spending more on debt service than on public health, the scenario of debt distress amid a pandemic literally risks human survival.

In response to the economic suspension created by the pandemic, on 15 April the leaders of the Group of 20 (G20) major economies announced a debt moratorium on official bilateral debt of the world’s 76 poorest economies from May to December 2020. The IMF and the World Bank also announced amplified lending facilities for developing-country members to respond to their heightened fiscal needs for public health and national economies. The IMF has increased access limits to its Rapid Credit Facility from 50% to 100% of annual country SDR quotas and to 150% on a cumulative basis from now until October 2020. Together with its Rapid Financing Instrument, the Fund’s emergency financing is expected to amount to approximately $100 billion. The World Bank has put in place a $14 billion fast-track package to respond to immediate health and economic needs and envisages using around $160 billion in longer-term financial support over the next 15 months.

While debt moratoriums, concessional financing and grants offer urgently needed fiscal resources in the immediate term, there are five key dilemmas foreboding an exacerbation of sovereign debt and a scenario of multiple debt defaults. First, debt suspensions keep the debt itself intact, accumulating interest with time, while concessional financing is a debt-creating instrument. Rather than resolving external debt burdens in order to create fiscal space, resources are generated through the continued and unsustainable augmentation of debt. This could result in a debt crisis which stalls recovery while undoing the hard-won economic and social gains of many years and deepening poverty levels.

[7] United Nations Conference on Trade and Development (UNCTAD). 2020. “The coronavirus shock: a story of another global crisis foretold and what policymakers should be doing about it,” 9 April, https://unctad.org/en/PublicationsLibrary/gds_tdr2019_update_coronavirus.pdf

[8] Ibid.

Second, the IMF's eligibility criteria for concessional financing are still based on assessments of "very strong fundamentals and policy frameworks" that centre on sustainable public debt and positive capital account positions, access to international capital markets at favourable terms and sufficient foreign reserves – all of which are highly restrictive, if not entirely unrealistic, in the present crisis context.[9]

Third, the debt suspension measures, as insufficient as they are, do not apply to middle-income developing countries, which are also facing fiscal pressures, particularly in light of currency depreciations triggered by massive capital outflows.[10] Data from the Institute of International Finance (IIF) show that 13% of all emerging market corporate debt is dollar-denominated.[11] As the dollar strengthens through developed-country monetary expansion, and local currencies weaken through capital outflows, debt servicing costs are now increasing, further constricting fiscal policy space for all developing countries.

Fourth, the private sector has not shown willingness to grant a debt moratorium to private sector debt, much less cancel or relieve any portion of the private debt. Instead of meeting urgent health and social protection needs, therefore, fiscal resources released by official debt forgiveness may be directed towards repaying debts to private creditors. The explosion of debt owed to private sector creditors in the last two decades has generated tens of billions of dollars of external debt in developing countries, often borrowed at high interest rates, due by the end of 2021 to private creditors. Even the IIF, which represents private sector creditors to emerging markets, has underscored that the private sector has to share the debt burden with developing countries. In a letter addressed to the IMF, World Bank and Paris Club, it shows initial steps towards developing terms of reference for a potential approach to voluntary private sector participation.[12] Unfortunately, this letter has had no impact on the IIF membership as of yet, and the institution still requires debt payments from sovereign debtors.

It is unconscionable if the financial resources made available by multilateral institutions are directed not to local health emergencies and poverty alleviation measures but to repaying private creditors, especially those such as large global banks that continue to reap dividends at a time of global crisis. G20 policymakers at all levels, from ministers, legislators and governors to heads of state, have attempted to mobilise the private sector around a voluntary plan to address poor-country debt distress. Unfortunately, this has not had any effect as of yet.

Meanwhile, the World Bank argues that a debt moratorium would erode its available resources and risk its own credit downgrades. The World Bank's bonds are rated triple-A and it relies on bond markets to raise money. In April, it announced a Sustainable Development Bond and raised $8 billion from the largest ever dollar-denominated bond issued by a supranational.[13] World Bank President David Malpass informed the G20 that multilateral development banks would only consider a suspension of debt repayments if the amount was fully compensated by new donor contributions.

Fifth, the IMF's use of the Catastrophe Containment and Relief Trust (CCRT), which is comprised of official aid funds, to cover six months of debt repayments by 25 low-income countries implies that official aid money is financing debt relief.[14] New pledges to the Trust have been finalised from the Netherlands, Germany and China. Crucially, the Trust pays back the IMF on behalf of low-income countries.

---

9 International Monetary Fund (IMF). 2020. "Flexible Credit Line (FCL)," 12 February, https://www.imf.org/en/About/Factsheets/Sheets/2016/08/01/20/40/Flexible-Credit-Line

10 Intergovernmental Group of Twenty-Four on International Monetary Affairs and Development Communique, 14 April 2020, https://www.g24.org/wp-content/uploads/2020/04/G-24-Communique-Final-Spring-Meetings-2020.pdf

11 Institute of International Finance. 2019. "High and Rising Debt Levels: Should we worry? Global Debt Monitor Slide Deck," August, https://www.iif.com/Portals/0/Files/content/GDM_July2019_vf3.pdf

12 Institute of International Finance. 2020. "IIF Letter to IMF, World Bank and Paris Club on a Potential Approach to Voluntary Private Sector Participation in the G20 Debt Service Suspension Initiative," 4 May, https://www.iif.com/Publications/ID/3885/IIF-Letter-To-IMF-World-Bank-and-Paris-Club-On-a-Potential-Approach-to-Voluntary-Private-Sector-Participation-in-the-DSSI

13 Chhibber, Ajay. 2020. "Global solutions to global 'bads': 2 practical proposals to help developing countries deal with the Covid-19 pandemic," Brookings Institution Blog, 22 April, https://www.brookings.edu/blog/future-development/2020/04/22/global-solutions-to-global-bads-2-practical-proposals-to-help-developing-countries-deal-with-the-covid-19-pandemic/

14 See: https://eurodad.org/imf_debt

By eliding debt cancellation or debt waiver measures in favour of mere debt moratoriums, the IMF-World Bank spring meetings in April were a missed opportunity to relieve the acute debt distress in the 76 low-income and lower-middle-income countries supported by the World Bank's International Development Association. Civil society organised a petition letter signed by over 150 civil society organisations (CSOs) calling for debt cancellation, not merely moratorium, by all creditors, including bilateral creditors, multilateral institutions such as the Bank and Fund as well as by the private sector.[15] The letter also highlighted the issue of private sector debt and payment obligations that are amplified by public-private partnerships (PPPs) promoted by the World Bank. Many of the contingent liabilities linked to infrastructure and health PPPs, for example, could materialise this year, creating even more external debt pressure on developing countries.

A key proposal disseminated by UNCTAD on 23 April is for an International Developing Country Debt Authority and global debt deal to prevent a protracted debt crisis.[16] Three broad steps for a global debt deal are called for:

- Step 1: Automatic temporary standstills to provide macroeconomic "breathing space" for all crisis-stricken developing countries by requesting forbearance to free up resources normally dedicated to servicing external sovereign debt.
- Step 2: Debt relief and restructuring programmes, with the suggestion that a trillion-dollar write-off would be closer to the figure needed to prevent economic disaster across the developing world.
- Step 3: The establishment of an International Developing Country Debt Authority to set out the institutional and regulatory foundations and oversee the implementation of a more permanent international framework to guide sovereign debt restructurings. Such a body could follow the path of setting up an autonomous international organisation by way of an international treaty between concerned states. Essential to such an international agreement would be the establishment of an advisory body of experts with independence from both creditor and debtor interests.

There is evidence that countries in debt distress experience stubborn challenges in arriving at a debt restructuring agreement with their sovereign and private creditors, particularly in the absence of effective institutions that can facilitate the process. Box 1 clarifies this challenge by highlighting the case of Argentina's private debt crisis.

3. Special Drawing Rights provide urgently needed liquidity

While G20 countries are extending an aggregate $5 trillion fiscal stimulus to their economies, most developing countries do not have the fiscal space to provide a lifeline for the vast majority of the world population. The disparity between the fiscal firepower of developed countries and the lack of fiscal space in most developing countries bodes a deepening of global inequalities. High public debt, record capital outflows, depreciating currencies and the tightening of global financial conditions are creating multiple and layered constraints to fiscal space for stimulus efforts in the developing world.

While developed countries can borrow directly from their central banks in their own currencies (unless they tied their own hands through legal restrictions), developing countries have to borrow from international capital markets in global reserve currencies, leading to higher borrowing costs in a context of longstanding debt distress. Adding to these structural constraints, lockdown measures, mass unemployment and the disruption of global trade, transport and investment have already inflicted greater damage on developing and emerging economies than on the rich world.

---

15 See: "A debt jubilee to tackle the Covid-19 health and economic crisis," April 2020, https://jubileedebt.org.uk/a-debt-jubilee-to-tackle-the-covid-19-health-and-economic-crisis-2

16 United Nations Conference on Trade and Development (UNCTAD). 2020. "A matter of life and debt: UN agency proposes global debt deal to prevent health pandemic spreading economic disaster across the developing world," 23 April, https://unctad.org/en/pages/PressRelease.aspx?OriginalVersionID=551

Box 1: Excerpts from "Restructuring Argentina's Private Debt is Essential", a letter by Joseph E. Stiglitz, Edmund S. Phelps and Carmen M. Reinhart, 6 May 2020, https://www.project-syndicate.org/commentary/argentina-sovereign-debt-restructuring-private-creditors-by-joseph-e-stiglitz-et-al-2020-05

Against the backdrop of this global emergency, Argentina is spearheading its public debt-restructuring process in a constructive manner, in good faith, and with the support of all domestic political sectors. Since 2016, when the country regained access to international markets, external creditors made a bet by acquiring debt with high coupons, but compatible only with extremely robust growth rates that did not materialise. There is consensus that the debt is unaffordable, with interest payments having doubled as a share of government revenue. To be blunt, the cost of refinancing has become excessively high.

A renegotiation requires the commitment of all parties. Argentina has presented its private creditors a responsible offer that adequately reflects the country's payment capacity: a three-year grace period with a minor cut in capital and a significant cut in interest.

Debt relief is the only way to combat the pandemic and set the economy on a sustainable path. Before the crisis, the World Bank estimated that urban poverty in Argentina stood at 35.5%, and child poverty at 52.3%. The UN now regards the impact of the shock on the country as among the worst in its region, with the IMF projecting a 5.7% contraction in GDP in 2020.

Creditors are being asked to trim the revenue stream but would still receive reasonable interest rates in the future. Argentina has ratified its willingness to service the restructured debt, precisely because it will become feasible at the new interest rate proposed. Only an economy that grows sustainably can meet its financial commitments over time.

The difference in treatment between capital and interest is designed precisely to alleviate the burden of debt service, while the country fights Covid-19 and works to restore growth. Indeed, the reduction of the average bond coupon offered by Argentina (from the current average of 7% to 2.3%) is reasonable, given the current global interest-rate environment.

At this exceptional moment, Argentina's proposal also presents an opportunity for the international financial community to show that it can resolve a sovereign-debt crisis in an orderly, efficient, and sustainable manner. The absence of an international legal framework for sovereign-debt restructuring should not deprive indebted countries of the possibility to protect their people and provide for economic recovery during the greatest global crisis in our memory.

We believe a sustainable agreement benefits both sides: a struggling economy with 45 million people and the creditors themselves. Now is the time for private creditors to act in good faith. A responsible resolution will set a positive precedent, not only for Argentina, but for the international financial system as a whole.

The monetary expansion led by the US Federal Reserve's quantitative easing policies of printing the dollar currency and extending bilateral swap lines to certain countries has expanded the fiscal capacity of developed and some emerging market countries.[17] These monetary manoeuvres inject liquidity into the global financial system, lower borrowing costs, purchase domestic bonds and introduce new lending facilities for specific sectors and enterprises. It is in this context that a bridge is needed between the global credit created by monetary expansion and the fiscal lifelines urgently needed in much of the developing world.

One of the most feasible, accessible and low-cost means to mobilise the fiscal resources urgently required by developing countries is the creation of Special Drawing Rights. The SDR is an international reserve asset based on a basket of five currencies (the US dollar, the euro, the Chinese renminbi, the Japanese yen and the British pound). It was created by the IMF in 1969 to supplement its member countries' official foreign reserves.[18] SDRs would provide low-cost emergency assistance to developing countries to help them address the health emergency needs as well as the economic fallout from the Covid-19 crisis.

To tackle the global financial crisis that broke out in 2008, the IMF issued $250 billion worth of new SDRs in 2009. The scale of the Covid-19 crisis certainly calls for a significantly higher issuance. A new issuance

17 "Global Economic Brief: The Fed Rushes to Stem Credit Crisis," *Wall Street Journal*, 24 March 2020, https://deloitte.wsj.com/cfo/2020/03/24/global-economic-brief-the-fed-rushes-to-stem-credit-crisis/

18 See: https://www.imf.org/en/About/Factsheets/Sheets/2016/08/01/14/51/Special-Drawing-Right-SDR

of SDRs would have the effect of building up the level of foreign currency reserves in the central banks of developing countries. Such a boost to reserves is critical in a time of capital outflows, rising import costs due to depreciating currencies, and mass disruption in global trade and financial flows. Besides financing stimulus needs, SDRs would also facilitate borrowing at lower interest rates and purchase of needed imports. Unlike the IMF's credit financing tools, SDRs are an unconditional resource and do not create additional debt. This would enable some developing countries to avoid signing on to a conditional IMF loan or credit line. SDRs are essentially a countercyclical financing tool that appropriately addresses exogenous shocks such as the current pandemic, and are allocated to all member states regardless of the Fund's macroeconomic assessment of the country.

However, a key flaw of SDRs is the basis of their allocation. Countries receive SDRs according to their IMF quotas, or financial contribution shares, rather than their level of fiscal need. This creates an unfortunate irony by which the countries which have the most need receive the least amount of SDRs. However, despite this imbalance, an SDR issuance would be an important contribution to meeting low-income countries' fiscal needs. SDR issuance also marks the only case in which developing countries have the opportunity to create international money.

Since March, wide support for SDR issuance has been voiced by a range of actors, including the IMF Managing Director Kristalina Georgieva, the Group of 24 developing countries in the IMF and World Bank, UN agencies, as well as academics, policymakers, analysts and civil society from around the world. The calls for new issuances have ranged from $500 billion to $4 trillion. Former British Prime Minister Gordon Brown and former US Treasury Secretary Larry Summers, who supported the 2009 SDR issuance, have called for a $1 trillion-plus new issuance. They noted that "if ever there was a moment for an expansion of the international money known as Special Drawing Rights, it is now."[19] To address the issue of SDR allocations by IMF quota rather than by fiscal need, a new mechanism is proposed, by which countries that do not use their SDRs can voluntarily provide them to countries that need SDRs.[20]

Despite widespread support for a new SDR issuance, the IMF's Executive Board failed to secure enough votes at the April spring meetings. US Treasury Secretary Steven Mnuchin delivered a statement on 16 April saying that a better, more targeted approach would be the enhancement of IMF support to low-income countries by providing grants to the CCRT and through new grants and loans to the PRGT.[21] The statement also mentioned that rich countries could also explore reallocating existing SDRs to developing countries on a bilateral basis or to bolster PRGT resources. An underlying reason for this stance may be the reluctance of the US to open new avenues of condition-free funding for its adversaries, such as Iran, Venezuela and China, which would benefit from a new SDR issuance that would be allocated to all 189 IMF members.[22] Besides being tragically short-sighted, the abuse of the IMF as a venue for disputes among rival powers brings the institution's legitimacy into question.

At the same time, there are deep internal political differences between the US Treasury and legislators, made visible by a bill introduced in the US House of Representatives titled "Robust International Response to Pandemic Act."[23] The bill proposes that the US Treasury Secretary is to instruct the US Executive Director at the IMF to use the voice and vote of the United States to support the issuance of a special allocation of at least $3 trillion in SDRs so that governments are able to access additional resources to finance their response

19 Brown, Gordon and Lawrence H. Summers. 2020. "National governments have gone big. The IMF and World Bank need to do the same," 14 April, https://www.washingtonpost.com/opinions/2020/04/14/national-governments-have-gone-big-imf-world-bank-need-do-same/

20 Gallagher, Kevin P., Jose Antonio Ocampo and Ulrich Volz. 2020. "IMF Special Drawing Rights: A key tool for attacking a Covid-19 financial fallout in developing countries," 26 March, https://www.brookings.edu/blog/future-development/2020/03/26/imf-special-drawing-rights-a-key-tool-for-attacking-a-covid-19-financial-fallout-in-developing-countries/

21 See: "U.S. Treasury Secretary Steven T. Mnuchin's Joint IMFC and Development Committee Statement," 16 April 2020, https://home.treasury.gov/news/press-releases/sm982

22 See: "U.S. stalling massive IMF liquidity boost over Iran, China: sources," Reuters, 15 April 2020, https://www.reuters.com/article/us-imf-worldbank-sdrs/u-s-may-stall-massive-imf-liquidity-boost-over-iran-china-sources-idUSKCN21X0L8

23 United States House of Representatives 6581 – "Robust International Response to Pandemic Act," 116th Congress (2019-2020), 21 April 2020, https://www.congress.gov/bill/116th-congress/house-bill/6581/text

to the Covid-19 pandemic. The bill also calls for the relaxation of fiscal targets and opposes the approval or endorsement of any loan, grant, document or strategy that would lead to a decrease in healthcare spending or in any other spending that would impede the ability of any country to prevent or contain the spread of, or treat persons who are or may be infected with, the Covid-19 virus. Yet another way that liquidity can be generated is the consistent call by many CSOs for the IMF to sell its gold reserves and other assets in its General Resources Account, estimated at $140 billion, for cash liquidity. This was advocated during the 2008 global financial crisis as well.

While the inequalities in fiscal space available to developed and developing countries are not new, the imperative for the most economically powerful countries to act in the "spirit of solidarity," as mentioned by the G20, has never been greater.[24] During the last global pandemic in 1918, the developing world, much of which was still under colonisation, suffered a far greater loss of life and livelihood. A century on, the international community must do better in forging international cooperation that delivers on both short-term financial needs and longer-term policy reform. A clear way to act on short-term needs is the countercyclical and unconditional issuance of SDRs. A global health emergency and economic crisis is a time for countercyclical monetary and fiscal policies of scale being made possible for all countries, not just the rich.

While bilateral donors and multilateral institutions publicly announce support packages, the financing provided is not infused with new or additional money. The Development Assistance Committee of the Organisation for Economic Cooperation and Development (OECD) has thus far stated a voluntary pledge to not cut aid budgets for low-income countries.[25] However, there is no pledge to increase the aid budget. The implication is that new and additional financing is not forthcoming to create an enabling financing environment for developing countries to cope with the pandemic and its economic fallout. A simultaneous challenge is that the reallocation of aid budgets and financing harms developing countries through the defunding of other important sectors, while also undermining the predictability and stability of aid flows and country ownership when donors suddenly reallocate funds without much consultation with sovereign aid recipients. Box 2 expands on the challenges posed by the lack of new and additional funding for developing countries to cope with the pandemic.

4. Renewed fiscal austerity in the aftermath of temporary fiscal space?

More than 90 countries have asked the IMF for assistance. In response, the key development by the Fund has been to redesign its previous Flexible Credit Line into a Short-Term Liquidity Line (SLL), the first addition to the IMF's financial toolkit in almost 10 years. Similar to a credit card, the SLL provides reliable and renewable credit lines that can be drawn up to a limit, as long as borrowing countries demonstrate strong fundamentals and policy frameworks.[26] As the Fund states, a country which signs up for an SLL will be signalling the IMF's endorsement of its policy frameworks and institutions to markets. This endorsement can lower its borrowing costs during the current period of crisis-induced volatility. Only a few countries have passed the rigorous pre-approval procedures for the SLL, however, posing problems of accessibility (as well as debt creation) in the IMF's financial assistance strategy in response to the Covid-19 crisis.

The IMF's *Fiscal Monitor* publication in April revealed that the Fund's support for fiscal stimulus is limited to the immediate fallout from the Covid-19 crisis. Once the public health emergency diminishes, developing countries are expected to carry out the traditional fiscal consolidation measures to stabilise debt ratios on a "firm downward trajectory."[27] The chief of the IMF's Fiscal Affairs Department, Vitor Gaspar, stressed the

---

[24] See: https://g20.org/en/media/Documents/G20_Extraordinary%20G20%20Leaders%E2%80%99%20Summit_Statement_EN%20(3).pdf

[25] Organisation for Economic Cooperation and Development (OECD). 2020. "Covid-19 Global Pandemic: Joint Statement by the Development Assistance Committee (DAC) of the Organisation for Economic Co-operation and Development (OECD)," 9 April, https://www.oecd.org/dac/development-assistance-committee/DAC-Joint-Statement-Covid-19.pdf

[26] Okamoto, Geoffrey, 2020. "The Short-Term Liquidity Line: A new IMF tool to help in the crisis," IMFBlog, 22 April, https://blogs.imf.org/2020/04/22/the-short-term-liquidity-line-a-new-imf-tool-to-help-in-the-crisis/

[27] International Monetary Fund (IMF). 2020. *Fiscal Monitor*, April, https://www.imf.org/en/Publications/FM/Issues/2020/04/06/fiscal-monitor-april-2020

Box 2: The lack of additional funding for developing countries to cope with Covid-19

by Bodo Ellmers, Director, Sustainable Development Finance Program, Global Policy Forum Europe

Donors and international organisations are announcing substantial financing packages in response to the coronavirus crisis, including in the context of development cooperation. A big problem is however the lack of additional funding. Packages, such as the $14 billion support that the World Bank announced in April, are funded through either reprioritisation or frontloading of resources. The same applies to bilateral donors. This is highly problematic: reprogramming means that ongoing projects are terminated or commitments that have already been made are not being met, a big issue for development planning and aid predictability. Frontloading implies that there will be less money available in future periods, obviously not good either. Many voices including from CSOs therefore ask for truly additional assistance to help developing countries cope with the coronavirus crisis.

A key problem is that it is procedurally difficult for donor country governments to come up with additional resources spontaneously, in an ongoing budget year. It would require passing supplementary budgets. Many countries already did this in the crisis, but development budget lines have been systematically sidelined. It is difficult to find any trace that development cooperation budgets were considered in the multi-trillion rescue and stimulus package passed in different parts of the global North. The German development ministry asked for an additional allocation of 3.1 billion euro through the supplementary budget, but this has not been approved yet, and there are no signs that it is seriously being considered by the ruling coalition government in Germany.

For the EU, the situation is even more difficult when it comes to fresh money as the EU budget is fixed for a period of six years through the Multiannual Financial Framework (MFF). This gives the European Commission predictability, but of course also implies that no additional things can be done, it is all reprogramming. We are in the last year of the ongoing MFF period, which lasts from 2014 to 2020, so they cannot even frontload. The Commission asked for a substantially larger MFF for the coming period, but EU Member States are reluctant to channel more money through the European institutions.

The only funder who can come up with “additional” resources without passing a supplementary budget are banks, as they can leverage their balance sheets to some extent. Hence the reliance on the European Investment Bank in the overall EU response to the crisis. But banks can only provide loans, and even if they do so at concessional terms, assistance in this form drives up debt levels in recipient countries. Many developing countries already have critically high debt levels. According to the IMF, almost half of all Low Income Countries are in debt distress, or in high risk of debt distress – and this assessment was made before they were hit by the Covid shock. So new loans might drive them even further into the debt trap, and ultimately into crisis, and do more harm than good.

To ensure additional and sustainable transfers, it is key that an “external action component” for transfers to developing countries is programmed in automatically whenever a rich country passes a new budget for a stimulus package. This is the prerequisite for having corona-related actions funded through additional money down the road.

slogan publicised by IMF Managing Director Georgieva for governments “to do whatever it takes now but keep the receipts.”[28] Essentially, the Fund’s fiscal consolidation measures that retrench government spending on public systems and social services will remain unchanged in the long term.

While the *Fiscal Monitor* acknowledges that public investment as a share of GDP has declined in advanced economies and that the growth rate has significantly slowed in emerging and developing countries, governments are still advised to “manage expectations” by “making clear that support measures to address the Covid-19 crisis are temporary.”[29] Emerging markets and low-income countries are advised to maintain fiscal “credibility” and prepare for an “ambitious” fiscal consolidation. According to the Fund, fiscal credibility is essential to restore investor confidence and attract much-needed investment once economic conditions start to normalise. This adherence to the neoclassical fiscal rulebook stems, in large part, from the idea and theory that fiscal credibility is achieved by preserving the expenditure ceiling rule and reducing debt levels, even if such measures decrease growth and stall employment creation while weakening public systems and services.

[28] See: https://twitter.com/kgeorgieva/status/1250411106100809730

[29] International Monetary Fund (IMF). 2020. *Fiscal Monitor*, April, https://www.imf.org/en/Publications/FM/Issues/2020/04/06/fiscal-monitor-april-2020

The World Bank is in agreement with the IMF, as the institution's President Malpass has expressed to G20 finance ministers that "countries will need to implement structural reforms to help shorten the time to recovery and create confidence that the recovery can be strong."[30] He added that "for those countries that have excessive regulations, subsidies, licensing regimes, trade protection, or litigiousness as obstacles, we will work with them to foster markets, choice, and fast growth prospects during the recovery." Explicit in his remarks is the reinforcement of the World Bank's foundational policy support for deregulation and privatisation.

A new future round of fiscal austerity in developing countries would be consonant with a tragic irony, in that the very structural adjustment policies that have chronically underfunded public systems and social safety nets will be required as economies eventually start to recover. Such a perpetuation of public spending retrenchment is akin to medicating a patient with the very poison that made her ill in the first place. This stance demonstrates that fiscal credibility through debt servicing is disconnected from economic stability and social development and well-being. The implication for the continued deprivation of public health systems, particularly in the context of a global health pandemic, reflects a failure to see health as part of the development policy arsenal.

Over the last several decades, the specific measures contained in IMF fiscal consolidation requirements or advice involve the elimination or reduction of subsidies, including on fuel, agriculture and food products; cuts and threshold ceilings on public sector wages, particularly the salaries of education, health and other public sector workers who comprise a large portion of the public wage bill in developing countries; rationalising and further targeting social safety nets and insurance programmes, pensions, housing benefits, child benefits and disability benefits; and broadening consumption taxes, such as value-added taxes, on basic products that are disproportionately consumed by poor households.[31]

New research by ActionAid International on recent IMF advice and loans to 78 low-income and many middle-income countries finds further evidence of widespread public wage bill suppression by the imposition of low inflation and deficit targets and freezing or cutting public sector wage bills, with consequences for health, public services and care.[32] The debt crisis already cemented in many developing countries only exacerbates the erosion of public systems and services through protracted spending cuts. Several low-income countries spend more on debt servicing than on education and health combined.

The steep social costs of fiscal contraction entail, for example, weak public health and education systems, diminished access to essential social services, loss of livelihoods in the public sector and increased unpaid work and time poverty.[33] Budget cuts by the state often reduce or eliminate the programmes and services which primarily benefit women, children, the elderly, disabled and physically ill – the very populations most vulnerable to the coronavirus. Social protection programmes, which are a critical source of economic survival for marginalised and vulnerable people, are often the first services to be reduced, even in countries that suffer extreme poverty.

The crisis triggered by Covid-19 needs to compel a fundamental rethink of the neoclassical economic ideology that prescribes and institutionalises fiscal consolidation and austerity measures. Under current fiscal discipline rules, many countries are assumed to lack sufficient fiscal space to undertake public investment. The degree

---

30 See: https://www.worldbank.org/en/news/speech/2020/03/23/remarks-by-world-bank-group-president-david-malpass-on-g20-finance-ministers-conference-call-on-covid-19

31 Ortiz, I., M. Cummins, J. Capaldo and K. Karunanethy. 2015. "The Decade of Adjustment: A Review of Austerity Trends 2010-2020 in 187 Countries," International Labour Organization, The South Centre, Initiative for Policy Dialogue-Columbia University, SS Working Paper No. 53, http://www.ilo.org/secsoc/information-resources/publications-and-tools/Workingpapers/WCMS_431730/lang—en/index.htm

32 ActionAid. 2020. "Who cares for the future: finance gender responsive public services!," 13 April, https://actionaid.org/publications/2020/who-cares-future-finance-gender-responsive-public-services#downloads

33 Razavi, Shahra. 2016. "Rising economic and gender inequality: intersecting spheres of injustice." In ISSC, IDS and UNESCO, *World Social Science Report 2016, Challenging Inequalities: Pathways to a Just World*, UNESCO Publishing, Paris, http://publishing.unesco.org/details.aspx?&Code_Livre=5160&change=E

of fiscal space is effectively circumscribed by limits placed on a country's public debt relative to GDP. The current approach to establishing debt ceilings defines fiscal sustainability for the short term, an approach that ignores the interaction between fiscal policy and growth over the longer term.[34] Relatedly, current guidelines for assessing fiscal space and sustainability ignore what the fiscal space is used for. Most budgets classify current and capital budgets separately, but this distinction is not made when evaluating fiscal deficits. The result is restrictive fiscal targets, which have led to a decline in public-investment-to-GDP ratios in many countries.

The challenge is for governments to reframe their thinking on public expenditures by recognising the virtuous cycle, or positive feedback loop, of public expenditures.[35] The counterfactual costs of not investing and sustaining a long-term recovery for the poorest countries from the Covid-19 crisis are unconscionable. Most developing countries, and certainly all poor countries, simply do not possess the fiscal policy space, low borrowing costs or ability to raise capital that developed countries have employed to enact massive countercyclical monetary and fiscal policies in response to the exogenous shock of Covid-19. This is precisely why the public finance architecture must reform its response to developing countries by preventing fiscal

Box 3: Excerpts from "Ecuador, Covid-19 and the IMF: how austerity exacerbated the crisis," by Ana Lucía Badillo Salgado and Andrew M. Fischer, 9 April 2020, https://issblog.nl/2020/04/09/covid-19-ecuador-covid-19-and-the-imf-how-austerity-exacerbated-the-crisis-by-ana-lucia-badillo-salgado-and-andrew-m-fischer/

Ecuador is currently (as of 8 April) the South American country worst affected by Covid-19 in terms of the number of confirmed cases and fatalities per capita. The recent IMF Extended Fund Facility (EFF) Arrangement, signed in March 2019 with the Government of Ecuador, was already the subject of massive protests in October 2019 given the austerity and "structural reforms" imposed on the country. It has also directly contributed to the severity of the pandemic in this country given that health and social security systems were among the first casualties of the austerity and reforms. In particular, the government's Covid-19 response has been severely hindered by dramatic reductions of public health investment and by large layoffs of public health workers preceding the outbreak of the virus.

Within the framework of the EFF, the government implemented a large layoff of public healthcare workers (including doctors, nurses, auxiliary nurses, stretcher-bearers, social workers and other healthcare workers). The layoffs continued throughout 2019, despite protests by the National Syndicate of Healthcare Workers of the Ministry of Health. It is difficult to know the exact number of layoffs because of the fragmented functioning of the health system, although within the Ministry of Public Health alone, 3,680 public health workers were laid off in 2019, representing 4.5% of total employment in this Ministry and 29% of total central government layoffs in that year.

Thus, it is not a surprise that Ecuador is currently doing so poorly in handling the Covid-19 crisis. The retrenchment of the public health system together with an already weak and retrenched social protection system coupled for the perfect storm. But even more worrying is that, in the face of the pandemic, the government paid $324 million on the capital and interest of its sovereign "2020 bonds" on 24 March instead of prioritising the management of the health crisis. This decision was taken despite a petition on 22 March by the Ecuadorean assembly to suspend such payments, along with a chorus of civil society organisations lobbying for the same. The government nonetheless justified the payment as a trigger for further loans from the IMF, World Bank, Inter-American Development Bank, and Andean Financial Corporation. This is especially problematic given that Ecuador has been hard hit by the collapse of oil prices and, as a dollarised economy, its only control over money supply and hence hope for economic stimulus rests on preventing monetary outflows from the economy (and encouraging inflows).

The payment is also paradoxical given that the IMF and the World Bank are currently calling for the prioritisation of health expenditure and social protection and for a standstill of debt service, and have announced initiatives for debt relief and emergency financing. Nonetheless, despite such noble rhetoric, it appears that the precondition for such measures continues to be the protection of private creditors over urgent health financing needs. From this perspective, even though the IMF has recently moved to offer finance and debt relief to developing countries hit by the Covid-19 pandemic, a much more serious change of course is needed. For this, it is vital to understand its own role – and that of other international financial institutions such as the World Bank – in undermining health systems before the emergence of the pandemic in various developing countries, lest similar policy recipes are again repeated.

[34] Roy, R., A. Heuty and E. Letouz. 2009. "Fiscal Space for Public Investment: Towards a Human Development Approach." In *Fiscal Space: Policy Options for Financing Human Development*, R. Roy and A. Heuty (Eds.). London: Earthscan Publications.

[35] Seguino, S., G. Berik and Y. Rodgers. 2010. "An Investment that Pays Off: Promoting Gender Equality as a Means to Finance Development," Friedrich-Ebert-Stiftung Occasional Paper.

austerity and debt accumulation, and instead committing to international coordination to support fiscal space for the most vulnerable people and states. In order to construct a viable case for the ability of expenditures to uphold equality, rights and justice, the theory, assumptions, discourse and consensus on fiscal space will need to be systematically contested and reshaped.

Box 3 demonstrates how austerity measures linked to IMF financing have exacerbated the pandemic in Ecuador, and highlights the urgency of protecting and strengthening public systems through long-term public financing.

5. Capital controls are central to crisis toolbox

In March, emerging markets and developing countries experienced the greatest ever outflow of investment capital, amounting to $100 billion.[36] By May, outflows instigated by the panic selling of foreign portfolio investors had exceeded $150 billion, weakening developing-country currencies and sharply constricting their domestic macroeconomic policy options.[37] With the exception of China, all emerging market economies ranging from Brazil to India, Mexico, South Africa and Thailand are experiencing large capital outflows from both equity and bond markets.

Even countries with strong reserve holdings and windfalls from plummeting oil prices have seen currency declines against a strengthening US dollar of 5-10%, with some as high as 15-20%.[38] Brazil, South Africa, Russia and Mexico have all seen their currencies devalue more than 20% against the dollar between March and May. Analysts have highlighted that what is unprecedented in this crisis is the scale and speed of capital outflows.

The lack of political will in those developing countries which are able to spend more on health and economic recovery but are not doing so, reveals a pervasive fear of worsening an already disastrous scenario of capital flight. More than a quarter of developing countries' local currency debt is held by foreigners, while capital account liberalisation norms have enabled domestic residents to easily shift their investment funds abroad.[39] Meanwhile, sovereign credit ratings of developing countries have been downgraded, despite the fact that Covid-19 is a purely exogenous shock. These vulnerabilities leave many developing countries hesitant to enact even urgently required fiscal policies out of a fear of losing even more investors.

The role of capital account regulations to manage the panic exit of capital in the Covid-19 crisis is thus of paramount importance to national and global macroeconomic and financial stability.

Regulations focused on cross-border financial transactions can reduce the chance that a country will experience a massive outflow of short-term financial resources that can trigger a crisis.[40] The benefits of capital account regulations, or capital controls, include a reduction of macroeconomic volatility and exchange rate volatility, and thus economic insecurity, as well as the imperative to bolster depleted foreign reserves that may be necessary to meet import payments. Empirical records of countries that have employed capital controls, such as Malaysia in the aftermath of the Asian financial crisis of 1997-98[41] and Brazil in response to the

---

36 Singh, Kavaljit. 2020. "Covid-19: A Triple Whammy for Emerging Markets and Developing Economies," 23 April, https://www.madhyam.org.in/covid-19-a-triple-whammy-for-emerging-market-and-developing-economies/

37 "The same stimulus that rich countries lean on could worsen poor economies," *Economic Times*, 2 April 2020, https://economictimes.indiatimes.com/markets/stocks/news/the-same-stimulus-that-rich-countries-lean-on-could-worsen-poor-economies/articleshow/74944062.cms

38 Ibid.

39 United Nations Conference on Trade and Development (UNCTAD). 2020. "The coronavirus shock: a story of another global crisis foretold and what policymakers should be doing about it," 9 April, https://unctad.org/en/PublicationsLibrary/gds_tdr2019_update_coronavirus.pdf

40 United Nations Conference on Trade and Development (UNCTAD). 2019. *Trade and Development Report 2019: Financing a Global Green New Deal*, https://unctad.org/en/PublicationsLibrary/tdr2019_en.pdf

41 Ali Abbas, S.M. and Raphael Espinoza. 2007. "Evaluating the Success of Malaysia's Exchange Controls (1998-99)," *Oxford Development Studies* 34(2): 151-191.

global financial crisis of 2008, show that taxes on speculative, short-term investment capital reduce both the volume of speculative flows and the volatility of interest rates.

However, a key force that works against the prioritisation of capital controls is neoclassical economic theory, and the internalisation of its rationale among policymakers in countries across all development levels. Neoclassical rationale suggests that capital account regulations can drive up the cost of capital and curb incoming investments. Neoclassical economists present what is said to be evidence consistent with the hypothesis that capital controls increase market uncertainty and carry the risk of reducing the availability of external finance, which in turn lowers investment levels.[42]

In the economic crisis triggered by Covid-19, emerging markets and developing economies have been hit by simultaneous and interlocking factors: collapse of commodity prices, supply chain disruptions, a decline in trade revenue and a sudden record arrest in investment capital flows. Emerging market countries have over the decades self-insured their economies through accumulating foreign exchange reserves as a buffer in times of financial crisis and capital outflows, as well as building local debt markets to raise capital. However, capital outflows in previous financial crises never exceeded $25 billion. During the global financial crisis of 2008, outflows were more ‘manageable,’ albeit long and painful. The magnitude of current capital outflows is exceptional, generating vulnerabilities that leave developing countries with dangerously narrow policy space. A petition addressed to international financial institutions and the G20 countries has been endorsed by leading economists and advocates from around the world clearly stating that “developing and emerging countries need capital controls to prevent financial catastrophe.”[43]

6. Progressive taxation redistributes financial resources

During the global financial crisis of 2008, a concerted campaign for a financial transaction tax (FTT) ensued. The argument is that an FTT would curb speculative and excessive trading by imposing a low tax on each trade transaction. As a result also, much-needed financial resources would be generated for stretched public purses. Although the FTT has been politically blocked for many years, the exceptional circumstances of Covid-19 could justify it. The income could be used for the emergency health financing needs of developing countries, including supporting essential workers, informal sector workers and the unpaid care economy.

A proposal for a Corona Survival Tax (CST) by civil society illustrates how the Covid-19 crisis is an opportunity to reformulate the financial industry through re-regulation towards economic recovery.[44] The CST is proposed as a tax that elevates the average effective tax rate of large investment banks and financial firms to 35% from an average rate of between 18% and 22% in 2019. The actors being spotlighted are the global too-big-to-fail banks such as JPMorgan Chase and United Bank of Switzerland, for example, and large asset managers such as Goldman Sachs Group, BlackRock and Pimco. Such financial firms are seen to have facilitated and profited from short-term and speculative investment and financial transactions, while also receiving dividends and benefiting from share buybacks. Hedge funds, private equity funds and high-frequency traders are also important actors, as are the big tech firms, such as Amazon and Zoom, that have disproportionately benefited from the global lockdowns. Such companies should pay proportionately higher tax rates on the high profits they made.

During an extraordinary crisis, extraordinary measures such as a CST, as well as progressive taxation on the incomes and assets of the high-earning deciles in society, can feasibly direct idle private money towards meeting urgent health and economic needs, particularly in developing countries. Progressive tax policies

---

[42] Alfaro, Laura, Anusha Chari and Fabio Kanczuk. 2014. “The Real Effects of Capital Controls: Credit Constraints, Exporters and Firm Investment,” Swiss National Bank, https://www.snb.ch/n/mmr/reference/sem_2014_06_02_alfaro_chari_kanczuk/source/sem_2014_06_02_alfaro_chari_kanczuk.n.pdf

[43] “Developing and emerging countries need capital controls to prevent financial catastrophe,” 24 March 2020, https://criticalfinance.org/2020/03/24/developing-and-emerging-countries-need-capital-controls/

[44] Vander Stichele, Myriam. 2020. “Finance must serve society during the Covid-19 crisis – not disrupt it,” 16 March, https://www.opendemocracy.net/en/oureconomy/its-the-viral-excesses-of-finance-that-are-to-blame-for-current-volatility-the-markets-should-pay-for-covid-19/

also imply that regressive indirect taxes, such as value-added or general sales tax, are avoided due to their disproportionate costs to the poor.

Progressive income taxation directed at rich individuals and firms has been a historical fiscal tool to redistribute financial resources from the wealthy to the poor. During both World Wars, the US government imposed direct taxation on companies that made high profits by manufacturing for the war. Tax measures in the War Revenue Act included direct caps on prices, special war taxes, high marginal income tax rates on war manufacturers, and Congressionally mandated "renegotiation" of corporate profits deemed "excessive" by the national War and Navy Departments.[45] The War Revenue Act effectively contained the dilemma of profiteering, while addressing public outrage at perceived illegitimate profit-taking in times of crisis. In the current pandemic, targeted taxes and controls could similarly limit hoarding and profiteering and shore up fiscal balances, while generating necessary public financial resources.

The Indian think-tank Madhyam points out five key reasons why a progressive "solidarity tax" is important in the current moment.[46] First, tax revenues will be stunted over the next two or so years due to a slowdown in economic activity, particularly for countries which rely on commodities, natural resources, trade, tourism or consumption taxes for public revenues. Second, the spike in expenditures needed for healthcare and economic recovery will require a significant scaling up of financial resources. Third, there is a strong correlation between economic recovery and public health and economic spending. Fourth, analysts warn of a rise in protests and civil unrest with the deepening of hunger, poverty and unemployment. And fifth, taxes on wealth, estate and inheritance are the most effective policy tools to reduce economic and social inequalities.

7. Rethinking ideology to reorient the role of the state

One of the major lessons from this pandemic is that austerity measures have led to a systematic shrinking of the strength and resilience of public systems, which has in turn led to the lack of state capacity to adequately respond to the pandemic itself. Without state capacity and resources, the legitimacy of the state comes into jeopardy.[47]

The pandemic implores policymakers and international institutions to rethink the ideology that shapes the role of the state. Governments today find themselves in the driver's seat, steering the entirety of their national economies for the first time in a generation. There is an opportunity now to restructure the balance of power between states and markets in order to salvage the social contract between government and people.

A task of this order involves a deeper examination of how the role of the state has been positioned. Rather than the widespread perception that the role of the state has been rolled back since the rise of neoliberal economic policies in the 1970s, the state has been effectively deployed to serve and facilitate the market through the development of institutions and universal rules, policy norms and legal protections. The neoliberal ideology in practice, as opposed to theory or concept, does not necessarily enact the self-regulation of markets as autonomous entities. The core of 20th-century neoliberal ideas involves the construction of meta-economic or extra-economic conditions for safeguarding the market at the global scale.[48] The neoliberal project is focused on developing strong institutions, not to liberate markets but rather to encase them. The imperative of the ideology is on redesigning states, laws and other institutions to protect the market.[49]

---

45 Wilson, Mark R. 2020. "The 5 WWII Lessons That Could Help the Government Fight Coronavirus," 19 March, https://www.politico.com/news/magazine/2020/03/19/coronavirus-defense-production-world-war-two-lessons-135814

46 Singh, Kavaljit. 2020. "It's Time for a Solidarity Tax," Madhyam Briefing Paper #37, 15 May, https://www.madhyam.org.in/its-time-for-a-solidarity-tax/#

47 See: "Has austerity led us to the Covid-19 pandemic?," May 2020, https://www.kcl.ac.uk/news/has-austerity-led-us-to-the-covid-19-pandemic

48 Slobodian, Quinn. 2018. *Globalists: The end of empire and the birth of neoliberalism*. Cambridge, MA: Harvard College.

49 Harvey, David. 2005. *A Brief History of Neoliberalism.* Oxford: Oxford University Press.

Such meta-economic formations have re-routed the role of the state from guiding economic development, retaining ownership of key sectors such as industry and banking, and using resources to meet the social and economic needs of its people.[50] Where the developmental state plays a strategic role in shaping the output and structure of the economy while balancing growth and social well-being, the neoliberal state is disciplined by international institutions to normalise policy frameworks that allow markets to own key sectors, control resources and shape decision-making. Disciplinary mechanisms include, for example, the risk ratings produced by the three global credit rating agencies (Moody's, Fitch and Standard & Poor's), the assessments provided by the IMF's macroeconomic surveillance reports and the World Bank's Doing Business Indicators (DBI). Together, they construct a constellation of ratings, rankings and signals that generate conformity to the particular policy ideas of austerity, deregulation and privatisation.

The neoliberal turn promoted by British Prime Minister Thatcher and American President Reagan in the 1980s ushered in an era of structural adjustment programmes. The one-size-fits-all straightjacket of deregulatory supply-side policies, also labelled the Washington Consensus, created a structural legacy of impoverishment and inequality through loan conditions and policy advice to privatise public services and state-owned enterprises, liberalise trade in goods and services, and deregulate capital flows and financial transactions, among other policies.

Structural adjustment underscores "fiscal fundamentalism" over economic and social equality and fulfilment of human rights. This is seen by how governments prioritise reducing their fiscal deficits as a first-order priority, even when history shows that government intervention is indispensable to pull economies out of recession.[51] A Keynesian fiscal perspective follows that the state must act as a "counterweight" to regulate the magnitudes of economic recessions.[52] In the Keynesian analysis, the government implements the social contract that binds individuals and institutions in a pact of accountability, responsibility and mutual trust. During times of economic recession, governments should increase public spending in order to stimulate the economy with an influx of labour and wage-led economic momentum.

The global pandemic demands that the centrality of public financing, regulation and coordination can no longer be deliberately obscured. The international community can no longer look the other way when the state protects the market at the expense of its people. Left unchecked, the pandemic will endanger three decades of progress in reducing poverty and expanding economic sectors and employment across the developing world. It is now time to revive the leadership role of government in establishing the framework of economic strategy, setting the boundaries for the private sector and defining the nature of collaboration, the direction of compliance and the distribution of resources and benefits.

8. The way forward: Global recovery calls for a new and bold multilateralism

The Covid-19 pandemic lays bare the unequal nature of the structures and norms of the international financial architecture. Institutional power imbalances and the primacy of the financial economy over the real economy have generated exponential inequalities, economic and social rights violations, an unequal gender division of labour, climate change, migration and refugees, and the transgression of planetary boundaries, among other failings. The distributional function in the international financial architecture is wholly inequitable, while decision-making structures tend to reflect geopolitical realities dating back to the post-World War II era. This results in a tragic reality where even in the midst of a pandemic, countries are competing for scarce resources. The way forward must entail both a resuscitation and a reboot, one rooted in the principles of equality, rights, historical responsibility, feminist and ecologically just values, and international cooperation and solidarity.

The way forward can encompass two imperatives. First, the response to an economic recession of historic magnitude can inspire a renewed multilateralism for health and economic recovery in developing countries. Specific policy actions have been outlined by UNCTAD, global civil society and progressive academics and

[50] Khor, Martin. 2013. "The Role of the State in Developing Countries under Attack from New FTAs," Inter Press Service, 17 August, http://www.ipsnews.net/2013/08/the-role-of-the-state-in-developing-countries-under-attack-from-new-ftas/

[51] Keynes, J.M. 1936. *The General Theory of Employment, Interest and Money*. London: Macmillan & Co.

[52] Ibid.

analysts. Second, transformative reform to global economic and financial governance can be consonant with sustainable and equitable systems of consumption and production in the reality of a warming world.

A global plan for recovery in developing countries

Integrating the call by UNCTAD for a composite $2.5 trillion package of measures[53] as well as key elements of civil society recommendations entails, but is not limited to, the following:

1. A **$1 trillion liquidity injection** through reallocating existing SDRs at the IMF and issuing a new allocation that will need to go considerably beyond the 2009 allocation made in response to the global financial crisis.

2. A **debt jubilee for distressed economies**. An immediate standstill on sovereign debt payments should be followed by significant debt relief. A benchmark could be the German debt relief administered after World War II, which cancelled half of its outstanding debt. On that measure, around $1 trillion should be cancelled this year overseen by an independently created body.

   2.a. The Civil Society 20 group clarifies that all principal, interest and charges on sovereign external debt due in 2020 and 2021 should be **cancelled immediately and permanently**, and should therefore not accrue into the future. The proposed debt relief should involve official bilateral and multilateral banks (both global and regional ones) and private creditors. All debt relief should be designed without economic reform conditionalities attached, while ensuring funds and public expenditure are targeted at protecting the rights and needs of populations, especially to maintain and increase social protection and health spending for those most in need in response to the crisis. The provision of emergency additional finance should not create additional debt.

   2.b. **Private creditors** should also participate in the cancellation of debt servicing by developing countries due in 2020 and 2021 in order to allow for health and economic recovery. The coordination of private lenders and investors should be facilitated by the donor countries.

   2.c. A **debt restructuring framework**, as reflected in the renewal of discussions in the UN system to design a global solution for the fair, effective and efficient restructuring of sovereign and private debt. Debt restructuring should be based on debt sustainability assessments that consider the impacts of SDG and climate financing requirements.

3. A **health recovery** for developing countries funded from some of the missing official development assistance (ODA) long promised but not delivered by development partners. UNCTAD estimates that an additional $500 billion – a quarter of the last decade's missing ODA – largely in the form of grants should be earmarked for emergency health services and related social relief programmes.

4. **Capital controls** should be given their legitimate place in any policy regime to curtail the surge in capital outflows, to reduce illiquidity driven by sell-offs in developing-country markets, and to arrest declines in currency and asset prices.

5. Fiscal deficits generated by public spending necessary for health and economic recovery **should not result in a new round of austerity measures** in the name of fiscal credibility to restore investor confidence and attract new capital investments. The fiscal policy response to the pandemic must recognise that austerity measures have in large part resulted in underfunded, under-capacity public healthcare systems and social safety nets. A rethink is required on fiscal discipline norms and rules in order to increase and maintain public spending for universal health systems, social protection and decent work.

[53] United Nations Conference on Trade and Development (UNCTAD). 2020. "The coronavirus shock: a story of another global crisis foretold and what policymakers should be doing about it," 9 April, https://unctad.org/en/PublicationsLibrary/gds_tdr2019_update_coronavirus.pdf

6. **Progressive tax measures** can raise much-needed additional financial resources to address the economic fallout from the pandemic. These include increasing the effective tax rate of systemically important global banks and large investment and financial firms, and progressive income taxation on the wealthy in society. Progressive taxation also includes targeting the private sector actors that have disproportionately benefited from the global lockdowns, such as the big tech sector and delivery and distribution services. Essentially, taxing the banking and investment sector, big corporations, and individuals with high incomes, wealth, inheritance, real estate and financial assets has the potential to feasibly generate financial resources in the near term.

7. A **global fund for universal social protection** to support the most vulnerable countries in responding to the pandemic.

8. A **global ban on short selling among all markets and greatly increased regulation of high-frequency financial trading**, with the objective of limiting speculative trading and arresting declines in currency and asset prices.

A renewed commitment to bold multilateralism in the United Nations

No country alone can or should finance a global plan. It needs to be built as part of a progressive multilateralism and global solidarity centred around the values of equity, rights and justice. The nature of the novel coronavirus clearly implies that no country can heal and recover alone, as the virus would surely find its way across borders. A failure to address the health and economic needs of the most vulnerable communities in the developing world would cost both lives and damage to the world economy.[54] Renewed commitment to multilateralism and global solidarity is the safest path forward.

Developing countries can coalesce in like-minded coalitions, equipped with a vision and will to catalyse new consensus for a way forward. Such consensus can pave the path to systemic reform and a rethinking of the ideological bias and assumptions in global economic governance. In the 1970s, developing countries came together in what economist Mahbub ul Haq called a "trade union of the poor nations."[55] They employed the forum of the UN General Assembly to pass resolutions on a New International Economic Order (NIEO) and a Charter of Economic Rights and Duties of States in 1974, calling for redistributive justice, colonial reparations, permanent sovereignty over natural resources, stabilisation of commodity prices, increased aid, and greater regulation of transnational corporations.

In the aftermath of the 2008 global financial crisis, the G77 and China group of developing countries in the UN General Assembly initiated the UN Conference on the World Financial and Economic Crisis and Its Impact on Development in June 2009.[56] The outcome document of the conference included a comprehensive range of action items: avoiding a new debt crisis, initiating the establishment of a sovereign debt restructuring mechanism, ensuring policy space, mobilising additional financial resources for development purposes (such as SDRs), reform for a more efficient global reserve system, financial regulation with respect to all major financial centres, instruments and actors, international cooperation in tax matters, IMF and World Bank governance reform, a more even-handed and effective IMF role in surveillance and avoidance of procyclical conditionalities in IMF lending facilities, and strengthening the role of the UN and its member states in economic and financial affairs. These action items are still relevant today, and can and should be employed in the policy actions and institutional reforms to address Covid-19.

In particular, the 2009 UN conference sought to establish the UN itself as a forum to address long-term systemic issues of economic governance. The discussions of the conference highlighted that if a small number of countries grouped in the G8 or G20 can agree on actions regarding the IMF and World Bank or on

---

[54] Ghatak, Maitreesh, Xavier Jaravel and Jonathan Weigel. 2020. "The World Has a $2.5 Trillion Problem. Here's How to Solve It," *New York Times*, 20 April, https://www.nytimes.com/2020/04/20/opinion/coronavirus-economy-bailout.html#click=https://t.co/wH0R7OhxvP

[55] ul Haq, Mahbub. 1976. *The Poverty Curtain: Choices for the Third World*. New York: Columbia University Press, 169.

[56] United Nations General Assembly. 2009. "Outcome of the Conference on the World Financial and Economic Crisis and Its Impact on Development," June, https://www.un.org/esa/ffd/wp-content/uploads/2014/09/Outcome_2009.pdf

systemic issues of financial regulation and flows, it is then unacceptable for leading members of these groups to prevent the UN, as a universal and legitimate body, from similarly proposing actions concerning global economic governance.[57]

To respond to the economic fallout of Covid-19, international civil society has called for an International Economic Reconstruction and Systemic Reform Summit under the aegis of the UN, to take place either in late 2020 or in early 2021.[58] The conference should be an ambitious UN and Financing for Development-centred process to assess the current economic crisis and agree on responses. The aim is to advance short- and medium-term solutions to strengthen multilateral cooperation and ensure adequate fiscal and policy space for all countries, with attention to developing economies, to tackle the health, food, social, economic and financial dimensions of the crisis.

The health and economic crisis triggered by Covid-19 is first and foremost defined by its human and social toll. With a projected half-a-billion people forced into deeper poverty, the origin points of global poverty must be located in the structural inequalities within and between countries. These inequalities are generated by an exploitative global and gendered division of labour and the historically skewed distribution of wealth and resources, where the G7 developed countries possess about 58% of the world's total wealth and 46% of the global GDP.[59] Women are being disproportionately affected by the crisis through multiple channels, including the unpaid care economy, employment in the informal sector, export processing zones, domestic work, migrant work and healthcare sectors, and greater reliance on public services and social protection systems.

In light of the deeply sobering forecast for the deepest global recession since World War II, it is morally imperative that the international community show political will and action through bold multilateral measures and equitable economic and financial governance. To actualise this, the universal participation of member states within the UN is essential. It is also critical to ensure that the responses to the crisis of poverty, livelihoods, health and economy are coherent with international human rights law, Agenda 2030 for Sustainable Development, the Financing for Development Conference outcomes, the Beijing Declaration and Platform for Action, and the Paris Agreement on climate change.

This is the time for the UN and all global governance institutions, particularly the Bretton Woods institutions – the IMF and the World Bank – to uphold a global transformation in the current unequal structures of finance. Just as the UN responded to the signs of the times at its founding moment 75 years ago, it should also assume leadership today. The counterfactual is an intertwined health pandemic and economic recession that will leave long-lasting scars and pose entrenched global challenges for equality, rights and justice. The time to act is now.

Acknowledgements

The author wishes to acknowledge valuable inputs from Meenakshi Raman, Bodo Ellmers and Nancy Alexander.

Bhumika Muchhala *is a policy researcher, advocate and activist on the international financial architecture, feminist economics and global economic justice. She has worked in international civil society for 20 years, including many years at the Third World Network based in Geneva and New York, focusing on finance and development as well as sustainable development. She is currently a PhD candidate in development economics at The New School in New York.*

57 Khor, Martin. 2009. "Follow Up to Conference: UN sets big agenda for economic crisis action," *South Bulletin* No. 38, https://www.southcentre.int/category/publications/south-bulletins/

58 Civil Society Financing for Development (FfD) Group. 2020. "2020 ECOSOC Forum on FfD – Civil Society FfD Group's response to Final Outcome," 23 April, https://csoforffd.org/

59 See: https://en.wikipedia.org/wiki/Group_of_Seven