THE GLOBAL CRISIS AND ITS IMPACT OVER LATIN AMERICA*

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The current crisis is part of a process that began in recent years and may be explained largely by the boom and volatility of financial flows. One can already feel its impact over Latin America and, although the region is in a better situation than in the past, predictions indicate a 2% drop in gross domestic product (GDP) in 2009. This article aims to analyze the origins of the current crisis and its effects on Latin America. In addition, it reviews the steps taken to remedy the most serious deficiencies in financial markets and redirect them to development financing, starting at the 2002 Monterrey Summit, and in the last episode with the G-20 agreement on 2nd April, 2009. Finally, the document analyzes the challenges to be faced in moving towards sustainable development.

O IMPACTO DA CRISE GLOBAL NA AMÉRICA LATINA

A crise atual faz parte de um processo que teve início nos últimos anos e que se explica em grande parte pelo auge e pela volatilidade dos fluxos financeiros. Já é possível sentir seu impacto na América Latina e, ainda que a região se encontre em melhor situação que no passado, os prognósticos indicam uma queda de 2% no produto interno bruto (PIB) de 2009. O presente artigo tem por objetivo analisar as origens da atual crise e os seus efeitos na América Latina e, em seguida, rever os esforços empreendidos para sanar as deficiências mais graves dos mercados financeiros e redirecioná-los para o financiamento do desenvolvimento, que tiveram início na Cúpula de Monterrey, de 2002, e em seu último episódio com o acordo do G-20 de 2 de abril de 2009. Por fim, serão analisados os desafios a serem enfrentados para avançar rumo ao desenvolvimento sustentável.

INTRODUCTION

The current crisis is part of a process that was put in motion in recent years. Current globalization is characterized by a huge boom in financial flows that are remarkably volatile. These fluctuations are expressed in intense cycles that last long periods of time and affect the quality of resource allocation and equity, in addition to generating growing imbalance, ultimately bringing about costly recessions in the real economy. Latin America has been a favorite, recurrent target of these crises. Indeed, the region has endured deep recessions during the eighties, in 1995, in 1998-2003, and currently.

As known, this time the epicenter of the crisis originated in the major global economy, the one that intensely promoted the liberalization of financial markets. Currently, most of the world is caught in the crisis resulting from the globalization of financial volatility. The severe consequences at the global level should ultimately lead to urgent correction of the international financial architecture.

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Section 1 of this paper provides a brief account of financial globalization and the current global crisis. Section 2 examines the impact of financial crises on Latin America. Section 3 considers the major international effort in recent decades to correct serious failures in financial markets and redirect them towards funding for development. The United Nations Summit held in Monterrey in 2002 is also addressed, culminating with a brief summary of the Doha Summit and the G-20 Agreement on 2nd April. Section 4 concludes with the challenges to be tackled in the current crisis to ensure a shift towards sustainable development.

1 VOLATILITY OF FINANCIAL GLOBALIZATION AND THE CRISIS

The current global crisis was gradually generated in the preceding five-year periods. The growing short-termism and speculative bias of international financial markets was at the core of its origins. Capital markets have expanded dramatically in recent years with large diversification across segments that are increasingly shady and prone to speculation and high leverage. The growing presence of international financial offshore centers and tax havens with little or no regulation at all encouraged dodging of national financial regulation, capital controls and taxes. This phenomenon, together with the revolutionary breakthrough developments in information and telecommunications technologies, as well as the use of increasingly sophisticated financial techniques (many of which allow excessive leverage via off-balance sheet operations), contributed to a remarkable boom in international flows. Pro-cyclical macroeconomic policies completed a scenario prone to explosive imbalances, given the magnitude of resources involved and the volatility that characterized them.

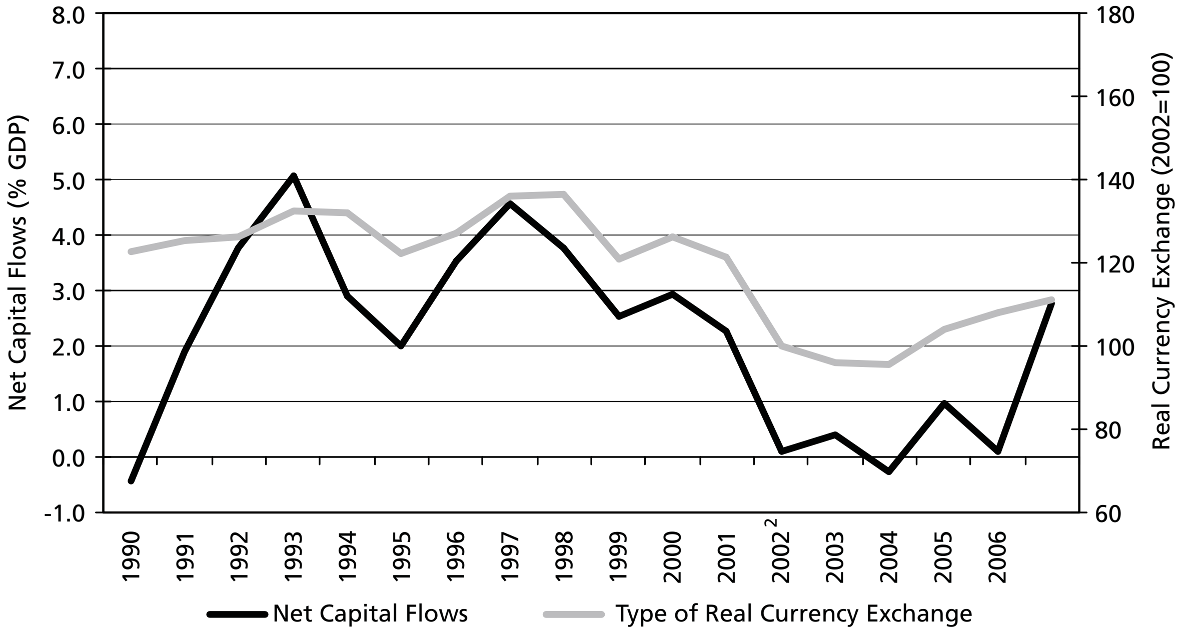
It is estimated, based on data by the Bank for International Settlements, that for every dollar of transactions in international trade of goods and services, as much as US$40 are transacted in currency exchange markets. Such an unequal ratio results from funds that are transacted several times per day, apart from real trade and productive investment. This complicates the macroeconomic environment for the real economy, where the overwhelming majority of enterprises and workers operate. In financial markets there are frequent "mood swings", which affect price expectations, for example, of the dollar and stock markets. This, in turn, enables net funds, unlike those invested in productive activities ("irreversible" investments), to migrate suddenly to another geographic market. These mood swings of financial and foreign exchange markets affect the real economy very strongly, i.e., in production, employment, utilities, and also tax revenues.

In general, the financial boom took place in a context of loose or partial regulation and supervision. It should be pointed out that the lack of regulation has not been uniform. In fact, for example, banking systems regulation persisted, particularly in developed economies. As we know, however, this regulation generally has a pro-cyclical bias, aggravated by Basel II (see Griffith-Jones and Persaud, 2005; Ocampo, 2007).

However, the main problem consisted of three very marked characteristics. (i) Growing or new segments (e.g., stock markets, international investment funds and derivatives markets) - which became the dominant share of financial markets - had weak or no regulation at all. These financial "innovations" involved intense shadiness. In a context of prolonged boom in these markets, the perception of the accumulating risks was undermined, including the significant cases of fraud detected later. (ii) Agents in these markets generally allocate resources with a short-term bias, exacerbated by the prevailing incentive systems (see Williamson, 2003). Also, they do so with net resources and at the international level, which creates enormous volatility for national macro-economies. (iii) In addition, a markedly pro-cyclical neo-liberal macroeconomic approach prevails (see Ffrench-Davis, 2005, chap. V, Ocampo, 2007), with strong currency exchange and monetary cycles. Two of its expressions were the huge foreign deficit in the United States, and the exchange delays that have occurred throughout Latin America on several occasions since 2004 (see graph 1).

GRAPH 1

Latin America 19[1] – 1990-2007



Source: Data by Eclac.
Prepared by the author.
Notes: [1] Data based on types of real exchange of 19 countries.
[2] Rate 2002 = 100.

It is hard to predict the precise moment when a crisis will break out, but it is possible to identify when the circumstances leading up to it are brewing. It has often been observed that emerging economies (EEs) have been driven by massive capital inflows to enter ***vulnerability zones***. They include: (i) large current account deficit; (ii) high foreign liabilities, with a significant net component, greater than foreign reserves; (iii) high real exchange rates and currency devaluation; (iv) domestic assets at high prices (stock exchange, bonuses, and real estate assets); (v) high household indebtedness vis-à-vis wages and profits; and (vi) decreasing interest rates with significant increases in monetary supply.

The longer and deeper the entry into these *vulnerability zones*, the stronger the *financierist trap* authorities may fall into, and the less likely to escape from it without experiencing a crisis with major economic and social costs.

Several combinations of these variables were present in the Latin American crises of 1982, 1995 and 1999, with gradual worsening of vulnerabilities. However, since the processes involved continuous increases in asset prices, they have provided increasing returns to financial operators, despite generating macroeconomic imbalances. Herein lies a serious contradiction between the “rationale” of financial operators and that of macroeconomists, who should focus on sustainable stability without the distortions that undermine productive development.

The U.S crisis shares many of these sources of vulnerability with EEs: for example, very low interest rates, bubble in real estate prices, incentives to provide increasingly risky loans driven by high liquidity, high leverage, and rating agencies behaving pro-cyclically. On the other hand, the U.S. crisis differs substantively from that of EEs, in that the United States is the issuer of the leading international currency and it was in US markets that the channels of expansion were created, with a large amount of financial engineering, which is then globally exported. It should be noted that these channels involve highly veiled risks, with intense leverage.

The area of sub-prime mortgages only triggered the crisis, but if it had been the major source of vulnerabilities, the scope would have been limited to one sector of the U.S. economy. Clearly, this sector experienced an unsustainable boom, based on the misperception that prices would continue to rise permanently (a feature shared by many situations leading to the crisis in LACs). However, in parallel, numerous other imbalances of a financierist origin were generated.

(i) On the one hand, the U.S. mortgage market bubbles spread across the globe[1], but with a rather “micro” scope worldwide: it was not possible to trigger a crisis in a world with GDP amounting to over US$ 60 billion. (ii) “Financial innovations” also spread worldwide, in the absence of effective

1. In addition, housing booms occurred simultaneously in many other countries.

regulation, facilitating massive cases of fraud, with real impact, but also with pro-cyclical impact on expectations. (iii) Many of these investors were operating with significant leverage, which could be justified in the case of actual producers and users of products, as they are backed by real activity; however, it could not be justified in the case of speculators, who operate with minimum capital. (iv) There were major stock market booms, inconsistent with the increase in the support base for stock prices, which are actual flows of net profits.

At the macroeconomic level, the U.S. economy incubated a growing current account deficit during the nineties. In the first phase, until 2000, rising external deficit was explained by the private sector. With the 2001 recession, the private sector adjusted, but the government initiated a process of increased fiscal deficit, which lasted until 2003, reaching almost 5% of GDP. Between 2003 and 2006, the public sector began to readjust, at the same time that the private sector boom worsened the already high current account deficit, which reached 6% of GDP in 2006.

Along the same lines, for several years, long-term interest rates fell in the U.S., reaching historically low levels; this trend was intensified after 2002, associated with a significant increase in demand for U.S. Treasury bonds. A similar trend occurred in real estate assets, whose prices nearly tripled (191%) between 1996 and peaked in mid-2006, growing at a 2-digit yearly rate between late 1999 and 2006 (see Table 1).

TABLE 1
United States – Home price index S&P Case-Shiller

	Level (Jan.)	Rate (Dec./Dec.)
1989	81	6.1
1990	82	-3.6
1991	78	-1.8
1992	78	-1.7
1993	76	-1.3
1994	77	1.7
1995	77	-0.4
1996	78	1.9
1997	80	5.4
1998	87	9.1
1999	95	10.8
2000[1]	107	14.1
2001	120	8.9
2002	133	15

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	Level (Jan.)	Rate (Dec./Dec.)
2003	151	13.4
2004	179	18.7
2005	209	15.9
2006	225	0.2
2007	215	-9.7
2008	182	-19.1

Source: Standard & Poors (S&P).
Note: [1] Jan./2000 = 100.

The stock markets of many nations played a central role in the bubbles, since they were also on increasingly unsustainable paths. In turn, the price of natural resources skyrockets. Over time it became evident that derivative markets for these products were invaded by speculators, which is clearly confirmed by the rapid collapse in the downward cycle (see Table 2). There were obvious signs of bubbles, not only in the U.S. housing sector, but on a global scale.

TABLE 2
Basic goods price index

	2003[1]	2004	2005	2006	2007	2008
General index	100	120	134	175	197	250
Food	100	114	122	145	158	228
Oilseeds	100	113	102	108	165	225
Agricultural raw material	100	113	118	136	151	185
Minerals and metals	100	141	178	285	321	352
Oil	100	131	185	222	246	353

Source: United Nations Conference on Trade and Development (UNCTAD).
Note: [1] = 100.

The pro-cyclical behavior of rating agencies worsened the imbalance by influencing the expectations of agents. It is amazing that those who should safeguard sustainability and foster transparent assessment of agents and markets - rating agencies - in general, fueled imbalances with their assessments. In fact, their assessments continued to be highly pro-cyclical, as occurred in the beginning of the Asian crisis (see Reisen, 2003).

Today, the world faces the urgency of resolving the largest crisis since the thirties. It has been possible to avoid widespread and destructive panic, with more pragmatic and effective policies than those of the thirties. Paradoxically, this may discourage the correction of current globalization failures. However, the reality of the real economy shows that correction is essential. Indeed, in 2009 most of the world's production capacity is undergoing recession, well below capacity. Indeed, even if a chaotic situation has been avoided, the total losses in production, employment, profits and tax revenues are remarkable.

Thus, one should not miss this opportunity and introduce reforms to correct the speculative bias and the current lack of clarity, as they have clear regressive implications. No doubt, there is a substantial shortage of macroeconomic and financial regulation at the current stage of an unbalanced globalization, as well as a significant imbalance among the voices, opinions and interests that are taken into account in the design and implementation of public policies. "Productivism" has to replace "financierism" (Ffrench-Davis, 2005), so as to bring into being a market that fosters the financing of development and growth with equity, as discussed in Section 3. Beforehand, Section 2 examines the impact of the crisis over Latin America.

2 GLOBAL CRISIS AND ITS IMPACT IN LATIN AMERICA

Countries in Latin America have gone through frequent crises associated with financial volatility. The most severe in recent times was the eighties' crisis. But later on, the region was affected by the contagion of the Asian crisis for a period of six years.

The scale of purely financial flows far exceeds all other international transactions, whether by way of foreign direct investment, trade credits, official development assistance, or remittances by migrant workers.

After the brief 1995 crisis (the so-called "tequila crisis"), the return of capital flows to Latin America in 1996-97 once again allowed for improvements both in economic activity and price stability, but at the expense of exchange rate appreciation and rising external deficits. The result was the subsequent entry into vulnerability zones. Consequently, in 1998, when the Asian crisis contagion hit Latin America, it brought about widespread recessionary adjustment in the region, especially in South America, with massive capital outflows and strong currency depreciation. Subsequently, recessive gaps lasting around six years led to reduction in total real productivity factors and GDP losses, as well as stifling of investment in physical and human capital. That is, with the deterioration of the present and the future, development is undermined and the achievement of productive development and equity is hindered.

Thus, between 1998 and 2003, regional GDP growth plummeted to 1.4% a year, i.e., less than the increase of the population. This, in turn, had an impact on employment: for example, the average unemployment rate in Latin America after the in East Asian crisis increased by 3-4 percentage points in between 1999 and 2003, as compared with 1997. This is one of the most glaring failures in resource allocation: the allocation of resources to unemployment benefit. And correction requires reforms in national macroeconomic policy making and in international architecture.

In the following years, vigorous recovery was observed, with 5.5% GDP growth in the region in the 2004-07 period. The change was quite abrupt, and in 2004 GDP growth shot up to 6.1%, a major contrast with the 1.4% slump of the previous period. There was no preliminary step in productive investment or sharp technological revolution. The driving force of such hasty leap was the positive external shock, especially as regards the terms of trade in the region. But the latter, even if national economies were macroeconomically balanced, could not have responded so positively. An irrefutable proof of the intense imbalance was the large gap between real GDP and potential GDP in the period[2]. The abundance of external funds, based on an improvement of 25% of the terms of trade, generated strong surpluses in external balances, debt reduction, and significant accumulation of international reserves. All these strengths contribute to reducing vulnerability vis-à-vis eventual negative external shocks. There was widespread rumor that Latin America was able to detach from external shocks.

The last external crisis emerged in mid-2007. A year later, the theory of detachment seemed to be confirmed, as the region maintained the pace of growth experienced in recent years. Similar to the Asian crisis contagion, this crisis arrived with a lag. But it did arrive, despite the region's strengths. Undoubtedly, the strengths are a valuable asset once contagion hits. In effect, they allowed for the implementation of counter-cyclical fiscal policies and for the moderation of exchange rate depreciations.

However, the region has been affected by substantial recessive and regressive impacts.

3 FROM THE MONTERREY CONSENSUS TO APRIL 2009 G-20

In 2002, the international community held a summit in Monterrey aimed at agreeing on measures to correct the path of financial globalization. At that time, a threatening globalization of volatility was brewing, and the boom in financial flows was contributing little to financing for development (Ffrench-Davis and Ocampo, 2001, Rodrik 1998, Stiglitz, 2000). The trends at that time indicated that the world's pace was to slow to achieve the Millennium Development Goals (MDGs).

2. In the 2004-2007 period, driven by vibrant global economic activity and marked improvement in the terms of trade, there was major reduction in the GDP gap. While potential GDP grew around 3%, real GDP grew by 5.5% during the four-year period.

The Consensus represented a shift towards a pragmatic approach, as it stressed the need for "adequate" level of productive investment. Greater productive investment required financial development, with considerable strengthening of long-term capital market segments and the creation or promotion of segments focused on financing small and medium enterprises (SMEs) in domestic markets. This represents an essential link between economic growth and equity, as it extends to low and medium income agents - major suppliers of productive jobs - the ability to access markets more effectively.

The text in the Consensus stresses the importance of "sound macroeconomic policies." In addition to concern with price stability and fiscal balances, it highlights the need to also consider the achievement of full employment, poverty eradication and sustainable external balances, which, in turn, require an "appropriate exchange rate system."

The Monterrey Consensus confers priority to the prevention of potential crises, with particular attention to short-term capital flows. It underscores that international financial institutions, including the International Monetary Fund, should strengthen compensatory financing in order to avoid or mitigate the deepening of crises.

The United Nations has prepared comprehensive yearly monitoring reports on compliance to the commitments undertaken in 2002, and made recommendations on how to achieve the agreed goals.[3] Similarly, the General Assembly has organized high-level dialogues on financing for development. The dialogues culminated with the Doha Summit, held in late 2008, amidst full-blown global financial crisis.

Such documents show that the United Nations were anticipating the worsening of the international financial environment, which culminated in the ongoing global crisis. Meanwhile, international financial institutions had a complacent attitude, oblivious to the global imbalances being generated and expanding. In different ways, they even encouraged the liberalization of speculation markets and financial market-oriented policies. It was the prevailing, widespread trend.

UN reports, especially the 2007 Report, address many aspects of the Consensus and suggest a coherent policy-making approach aimed at the achievement of the goals established by signatory countries. Four main points are highlighted here: styles of conducting macroeconomic policy; intensity and coverage of counter-cyclical regulation and supervision; formal compensation mechanisms for external shocks and international liquidity; and the role of the quality of domestic capital markets in developing countries.

3. The United Nations Secretariat has made excellent assessments of implementation progress and setbacks. See details and references in Ffrench-Davis (2009, section 2).

The progress recorded in the report, regarding the understanding of macroeconomic issues, is of great importance, as the approach adopted seeks to reduce the gap between real production and potential GDP, an approach termed *macroeconomics for development*.[4]

It underlines the need to strengthen regulation, supervision and transparency of financial markets, including hedge funds and derivatives. It should be pointed out that the position taken in the report precedes the explosion of the mortgage lending crisis in the United States and the intensification of the speculative ingredients related to rising prices of several commodities. It addresses several issues related to the international financial architecture and its backwardness as compared with other forces in globalization.[5]

One of the most prominent topics is that the international community has not created a compensation tool to offset reduced liquidity in developing countries. In this regard, the report suggests urgent resumption of the issuance of Special Drawing Rights, as an essential part of a new international financial architecture.

It should be noted that the effects of capital inflows on economic growth also depend on the quality of domestic intermediation and foreign exchange policy. Fashionable approaches have failed miserably: intermediation has focused on consumer finance and overvaluation of existing assets and has been lacking or weak with respect to investment projects, while at the same time inflows in general have led to quotations outside a sustainable balance (outlier prices). Latin America has been an example of such failure: a boom in "financial savings" associated with stagnant national savings and minimal rate of productive investment (see Ffrench-Davis, 2005, chap. II). Consequently, it generates the need - in developing economies – for active exchange rate policies that are consistent with the evolution of internal productivity, as well as the need to concentrate financial reforms on the development of long-term and non-traditional segments within the national capital market.

Issues relating to illicitly acquired funds and tax evasion are addressed. In fact, a common feature in many developing countries is an extremely low tax burden combined with high tax evasion and avoidance. As a result, the ability to finance investments in infrastructure and human capital to ensure the efficiency of public spending is limited. Therefore, it is essential to strengthen international cooperation to fight tax evasion, money laundering, illegally acquired funds, funding of terrorism and corruption.

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4. The proposals are consistent with the recommendations we have repeatedly made on the need to change the predominant macroeconomic approach in Latin America, which features a neo-liberal bias or a financially-oriented macroeconomics, rather than concentrating on sustainable development. For an analysis of approaches to "financially-oriented and real" macroeconomics, see Ffrench-Davis (2005, Chapter I). The texts in quotes are from the UN report (2007).

5. Among other issues, the 2007 UN Report highlights environmental taxes, which contribute to mitigate environmental degradation and provide funding for research, mitigation and adaptation, and taxes or royalties over the use of natural resources.

The approval of the Doha Summit Declaration, which comprises an assessment of the progress made and obstacles faced in the implementation of commitments under the Monterrey Consensus, faced strong opposition, led by the U.S. government delegation, just ending its term of office. The final text reiterated the ideas of the Consensus and the purpose of strengthening the monitoring of compliance with the commitments undertaken; however, it was subject to intense negotiations, which ended up weakening it.

The most significant progress is related to three topics. (i) The agreement that a conference on the international financial crisis should be held in 2009. This implies the acceptance that the United Nations and its Member States are entitled to a say on an issue that some countries wish to limit to the IMF and World Bank spheres.[6] (ii) The recognition that the international economic system architecture also requires adjustments to meet the needs of middle-income countries. (iii) The explicit recognition, after lengthy discussions among delegations, that there should be space for so-called "innovative financing", with special recognition of the Action Against Hunger and Poverty Initiative, described below.

b) Action against Hunger and Poverty Initiative

In 2004, determined to contribute to the fulfillment of the Millennium Development Goals and the Monterrey Consensus, a group of countries in the North and South launched an initiative to identify innovative sources of funding to promote public goods, foster solidarity-based economic development, and finance the fight against public evils, such as hunger and poverty.

The presidents of Brazil, Chile and France and the United Nations Secretary General - later joined by the Heads of State of Spain and Germany - created the Action against Hunger and Poverty Initiative. The funds raised by innovative sources would be used to implement projects aimed at attaining the Millennium Development Goals (see Action against Hunger and Poverty, 2004, 2005).

In 2006, the Leading Group on Innovative Financing for Development was established. Currently, the group comprises 58 countries from the North and South, including the five mentioned above, whose representatives expressed their willingness to levy taxes for development and contribute to fundraising to fight "public evils", such as tax evasion and financial crises.[7]

6. The meeting was held in June, but with participation of few delegations, and reduced impact.

7. The Pilot Group addressed various issues besides those covered by the Initiative for Action against Hunger and Poverty. The Group's work includes an assessment of solidarity levies on air travel, issuing of Special Drawing Rights, such as financing counter-cyclical mechanisms to address trade and financial instability in developing countries, introduction of a modest tax on currency exchange transactions, repatriation of illicitly acquired funds, improving the role of the carbon market, linking migrant workers' remittances to microcredit in recipient households, the increasing efforts to fight fraud and tax evasion, and implementation of a digital solidarity contribution.

Concrete progress has been made. In 2006, it launched the pilot project for a solidarity levy on international airline tickets, earmarked for the fight against HIV/AIDS, tuberculosis and malaria. Currently, 34 countries contribute to financing the activities of UNITAID, the mechanism created to allocate funds, in collaboration with national health services in poor countries.

c) Fighting international tax evasion

Hunger and poverty are also associated with weak tax systems, mainly because of tax evasion through tax havens, among other reasons. Thus, curbing tax evasion can become a major innovative source of financing for development. This topic has sparked renewed interest, with the disclosure of significant cases of tax evasion in developed economies, sheltered by the secrecy of tax havens.

Permissive policies vis-à-vis the expansion of financial flows with little or no restrictions have accentuated this failure of globalization. It is well known that a considerable part of the resources that leak out of the tax systems of countries in the North and South are sheltered in tax havens.

Tax evasion is extremely unfair to honest taxpayers. Tax havens are one of the means by which this inequality is perpetuated. Tax evasion is also related to money laundering, corruption and terrorist financing, three global "public evils".

Given the precarious fiscal systems often found in developing countries, it is essential to strengthen their ability to raise revenues through the implementation of measures to prevent evasion through tax havens. The United Nations Committee of Experts on International Cooperation in Tax Matters can play an important role in this regard. The Organization for Economic Cooperation and Development (OECD) has also addressed the issue of tax evasion and tax havens. Collaboration between the two institutions could contribute to the adoption of concrete measures to fight international tax evasion and improve tax systems in developing countries.

4 CONCLUSIONS

The Action against Hunger and Poverty Initiative and the Leading Group on Innovative Financing for Development have drawn up proposals to strengthen anti-cyclical mechanisms and their funding with counter-cyclical issuances of Special Drawing Rights (SDRs) by the IMF . The United Nations Committee for Development Policy made convergent proposals in its 2008 and 2009 reports.

External crises, whose effects are transmitted through trade and capital accounts, usually have considerable negative economic and social impacts on developing economies. Installed economic capacity is used inadequately and resources are wasted. Therefore, economic crises may also prevent or delay the achievement of the Millennium Development Goals.

It is therefore necessary to establish an international financial architecture favorable to development, with comprehensive regulation and supervision of financial markets, that includes major reform of official counter-cyclical financing for developing economies affected by financial and trade shocks, supports the fight against tax evasion, and includes gradual release of an international reserve currency, like SDRs.

Given the deterioration of global economic prospects, its implications for developing countries, and the absence of effective compensation mechanisms, it is urgent to reform the compensatory financing architecture, in order to provide official liquidity and assistance to developing countries affected by the negative effects of external crises. In order to be effective, liquidity must "be adequate, of speedy disbursement, at a scale proportionate to the shock, and impose few conditions."[8] The G-20, on 2nd April 2009, agreed upon reforms in line with these approaches, taken up strongly and comprehensively by the Stiglitz Commission in its June report.

To fund a considerable increase in the volume and quality of compensatory financing, and taking into account the arguments in favor of a gradual transition into a global currency for reserves, the issuance of Special Drawing Rights (SDRs) should be resumed. A new reform should allow the IMF to allocate them to finance a significant increase in the availability of compensatory financing. The current prospects of downward adjustments in economic and financial turbulence constitute an appropriate context for a new allocation of SDRs, with an anti-cyclical function, so as to ensure a gradual shift towards a truly international reserve currency.

Considering the growing imbalances resulting from globalization, the restructuring of the international financial architecture to respond to deep changes in the global economy is an urgent task. Instability is a harmful feature of the current global financial architecture. The voice of developing countries should be taken into account and prevention and management of financial crises (including the proposed reform of anti-cyclical mechanisms) should be seriously addressed. Firstly, international finance generally pays little in taxes at the expense of the real economy, particularly immobile factors of production. The currency transaction tax could help improve financial equity, and generate a substantial amount of funds to stimulate equitable growth (see Williamson, 2006). Secondly, fashionable approaches advocating complete opening of capital accounts are markedly biased toward high-income producers and short-termist

8. The IMF approved a new mechanism in late 2008. It is the Short-Term Liquidity Facility, SLF. The arrival of the new IMF Managing Director, Dominique Strauss-Kahn, has been a positive shift toward pragmatism, with some valuable achievements away from the extreme neo-liberalism of previous years.

speculative agents. The latter are the new rent-seeking actors. It is necessary to reform the rules and institutions to redirect funding to typically excluded sectors such as small and medium enterprises and micro-producers. Thirdly, there is increasingly strong evidence that flows of foreign direct investment to completely new areas or sectors contribute directly to productive investment and promote development, while, on the contrary, short-term financial flows have a weak link with capital formation in periods of economic boom, are a common cause of deep economic depression, and deter productive investment.

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