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**Statement by Mr. Supachai Panitchpakdi
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**To the International Monetary and Financial Committee
and the Development Committee**

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Mr. Chairman,
Distinguished Ministers,
Excellencies,
Ladies and Gentlemen,

The global economy weakened significantly towards the end of 2011 and further downward pressure emerged in the course of 2012. The growth rate of global output, which had already decelerated from 4.1 per cent in 2010 to 2.7 per cent in 2011, is expected to slow down even more in 2012 to around 2.3 per cent (table 1). Developed economies as a whole are likely to grow by only slightly more than 1 per cent in 2012, owing mainly to the recession currently gripping the European Union (EU). This contrasts with a much stronger performance in developing and transition economies, where GDP growth should remain relatively high, at around 5 per cent and 4 per cent respectively. However, even in these economies growth is losing steam, showing that they cannot avoid the impacts of economic troubles in the developed countries.

Developed countries have not yet recovered from the financial crisis, which has left in its wake a highly indebted private sector and a vulnerable financial system, with a high proportion of non-performing loans and limited access to inter-bank financing. Significant deleveraging was set in motion as banks sought to recapitalize and the private sector was unable or unwilling to take on new debts, strongly hampering domestic demand. Expansionary monetary policies by the leading Central Banks proved inadequate for reversing this situation: the problem behind stagnating credit to the private sector is not the lack of liquidity. Banks are not expanding their lending to the private sector because households cannot expand their consumption and consequently firms do not intend to increase their investment. In many crisis-hit countries, high levels of unemployment and wage stagnation or compression further hinder private consumption. On top of already weak private demand, fiscal tightening has been adopted in several countries with a view to reducing public debt and

restoring the confidence of financial markets. However, these policies have further weakened domestic demand and growth, which is detrimental to the goals of fiscal consolidation and improved confidence.

Appropriate policy responses to the crisis must take into account the broad spectrum of macroeconomic impacts of policy measures, not only within a given country, but also at the regional and global levels. Recent experience shows that public spending has high multiplier effects, especially when that spending consists in social transfers or infrastructure investment, and when economic activity is already depressed. This is why fiscal tightening in many developed countries has had comparatively large social and economic costs while achieving relatively little gains in terms of fiscal consolidation. Some governments are trying to stimulate growth through increasing exports, and are working to improve their competitiveness by reducing nominal wages and other costs; for several European countries within the monetary union, this would be the way to achieve a real devaluation. The danger with this policy is that it will severely damage domestic demand before it can help to regain competitiveness, thus putting into question the adjustment process. Moreover, the fact that those policies are being applied in several important trading partners at the same time limits their benefits, since not all the trading partners can improve their competitiveness at the same time.

Developed economies should therefore change the focus of their policies from fiscal consolidation and internal devaluation to restoring growth, because this is the only way in which they can avoid a recurrence of a financial and fiscal crisis. Countries with larger fiscal space and current account surpluses should take the lead by expanding their domestic demand. This would be in line with their commitments at the recent G-20 Los Cabos Summit, and contribute to a growth-friendly global rebalancing.

Most developing and transition economies have actually supported their GDP growth by encouraging domestic demand and pursuing countercyclical policies, including the provision of fiscal stimulus and expansionary credit. They have also succeeded in preventing a significant rise in unemployment, and have enabled the continued growth of real wages. All this, together with public transfers in several countries, has

promoted private consumption, and consequently, productive investment, even though this has not always been sufficient to avoid growth deceleration.

Indeed, the developing and transition economies are being affected by slow growth or economic contraction in the developed countries. This is reflected in stagnating export volumes to those markets and a declining trend in commodity prices since the second quarter of 2011. Moreover, financial instability and excessive reliance on monetary policies in developed countries is affecting financial flows to emerging market economies and adding to the inherent volatility of commodity prices. In some countries, excessive short-term capital inflows have had a negative impact on their exchange rates and competitiveness, prompting them to take measures to manage capital flows. Finally, the risk of a new major shock in global financial markets cannot be excluded, with a potentially large impact on international trade volumes, asset and commodity prices, risk spreads, capital flows and exchange rates, all of which would affect developing and transition economies. These countries should continue to preserve their fiscal and financial room for manoeuvre, including by strengthening public revenues; capital and exchange rate management in order to avoid currency overvaluation and artificial credit booms; maintaining foreign currency reserves at an appropriate level for covering their precautionary needs; and enhancing regional monetary and financial cooperation.

Some governments are looking to implement structural reforms to overcome the crisis. UNCTAD has always supported the need for structural reforms, since no development process can happen without changes in economic and social structures. However, today, structural reforms are often focused on attempts to introduce greater labour market flexibility. Yet, by promoting wage differentiation at the firm level, such reforms would undermine the incentives for investment and innovation. Indeed, if less efficient firms can compensate for their lower profits by cutting wages, they are not forced to increase their productivity to survive and expand. Such reforms also threaten to further undermine domestic demand. In order to revitalize sustained growth, governments must take measures to reduce income inequality, by assuring the participation of all social groups in productivity gains stemming from economic and technological advancement.

As UNCTAD has shown in its Trade and Development Report 2012, labor market reforms are not a way out of the crisis, because the crisis did not originate in the labor market. Additionally, structural policies cannot be a substitute for pro-growth macroeconomic policies. Structural reforms have to address the very roots of the present crisis, namely the fragility of the financial system and the trend towards increasing income inequality.

In contrast, the structural reforms being adopted by a number of developing countries have tended to create or reinforce social safety nets and to expand the role of public policies for supporting investment and structural change. Most of these measures are countercyclical, as they aim to safeguard employment and support economic activity in troubled times. However, some of them are not just temporary measures that will be reversed when the international environment becomes more favorable. For sure, extending social security, unemployment benefits and pension coverage has a countercyclical component through its immediate effect on demand, but there is no reason to dismantle these social advances once growth resumes.

However, in developing economies, and in commodity producing countries in particular, the benefits of higher commodity prices and better terms of trade have not been spread widely among the entire population. One reason is that the ownership of natural resources is typically less equally distributed than that of other assets. Commodity production and their trade are dominated by large transnational corporations (TNCs) and trading companies. In this context, it is often the large TNCs – and financial investors – that capture most of the gains from the commodity price increases, and only a small proportion goes to the commodity producers and workers in this sector, or to the governments of the producing countries.

To achieve more inclusive growth in commodity-exporting economies, governments can take advantage of favourable commodity price developments and modify their fiscal regimes to ensure more equitable rent sharing. The increase in government revenues can reduce income inequality and prevent deindustrialization through enhanced public investment and transfer payments that target those segments of the population that do not directly benefit from resource revenues. Policies should also aim at promoting and diversifying industrial production, by encouraging exporting

firms to add value locally and create a network of domestic suppliers, maintaining a competitive exchange rate and pursuing a monetary policy that stimulates private investment.

The total external debt of developing countries and transition economies had surpassed \$4 trillion by the end of 2010. This corresponds to a 12 per cent increase of total external debt compared to 2009, marking a much higher growth rate in comparison to previous years. While 2011 data from the World Bank Debtor Reporting System are not yet available, UNCTAD Secretariat estimates indicate that debt levels continued to grow by approximately 12 per cent over 2010-2011, bringing total external debt to \$4.5 trillion. Export and GDP growth in the developing world (measured in current dollars) compensated this recent increase in debt and led to decreases in debt ratios. Average debt went down from nearly 80 per cent of exports in 2009 to approximately 71 per cent of exports in 2010 and the average debt to GNI ratio decreased slightly from 21.8 per cent to 20.4 per cent in 2010. Estimates for 2011 suggest a further decrease of debt to 65 per cent of exports and 19.5 per cent of GNI.

Most of the recent increase in debt was due to short-term borrowing linked to trade credit which, in turn, was associated with rapid import growth in developing countries. Total short-term external debt went from \$773 billion in 2009 to more than \$1 trillion in 2010. This increase in short-term borrowing is unlikely to lead to liquidity problems due to its nature (trade credit) and to the fact that most countries have international reserves that more than cover their short-term debt. Total international reserves of developing countries also surpassed their stock of total external debt. Therefore, developing countries, as a group, are net creditors. However, this average masks substantial heterogeneity among developing countries. Out of 123 countries for which data are available, there are 28 countries that do not have net external debt while in 31 of these countries debt is more than three times international reserves.

A number of countries are still in debt distress or at high risk of debt distress, including some countries that just completed the HIPC Initiative. The increasing importance of short-term debt may also lead to greater vulnerabilities, especially if the economic situation in developed countries deteriorates, thereby hurting the growth performance of developing countries. Moreover, many countries may now be facing vulnerabilities related to their increasing domestic public debt.

UNCTAD welcomes the emerging interest in re-opening the debate on the creation of a structured mechanism for dealing with sovereign debt restructuring, and believes that the first step in opening this debate should be a clear definition of the problems that such a mechanism should address. While costly crises are sometimes driven by exogenous shocks, they may also be caused by irresponsible behaviour from both lenders and borrowers. Prudent behaviour can thus limit the cost and prevalence of debt crises. With this objective in mind, the UNCTAD Secretariat has developed a set of principles on responsible sovereign lending and borrowing which have gained support from a growing number of developing and developed countries. It is our hope that adherence to these principles can help to reduce the incidence of debt crisis.

In view of the fragile global recovery, official development assistance (ODA) flows are of particular importance as they can help developing countries weather the negative effects that the global economic and financial crisis has had on trade, investment, remittances, exchange rate volatility, and capital flows. They also constitute an important source of financing to pursue the objectives outlined under the MDGs and other development goals. In recognizing the importance of ODA flows, the international community has repeatedly committed itself to progressively increase ODA to developing countries to 0.7 per cent of donor countries' GNI. Thus far, however, only five Development Assistance Committee (DAC) donor countries have reached or surpassed the target. In 2011, total DAC aid still stood at 0.3 per cent of total donors' GNI, with the majority of countries still far from the 0.7 per cent target.

Furthermore, in 2011, ODA to developing countries from DAC donors decreased by 3 per cent with respect to its 2010 level, and total net ODA excluding debt relief grants and humanitarian aid decreased by 4.5 per cent in real terms. This outcome, which marks the first decline in ODA excluding debt relief in more than a decade, reflects

the impact of the global recession on donors' aid budgets. The uncertain global economic outlook is likely to continue to affect aid budgets, thus raising concerns about the predictability of planned aid in the years to come.

Yet, it is precisely in times of crisis that the importance of aid increases. As global economic growth prospects hang in the balance, the provision of aid to the most vulnerable to achieve the MDGs and to help shield them from adverse economic shocks becomes crucial.

This is particularly the case for the Least Developed Countries. The United Nations uses a holistic approach based on income per capita, human assets and economic vulnerability to classify countries as Least Developed, whereas the Bretton Woods Institutions only base country groupings on income per capita. As a consequence, there are 16 LDCs that are classified as Middle Income Countries and one LDC which is classified as a High Income Country. This is problematic because graduation from low income to middle income status often leads to a rapid decline of development assistance. For instance, countries no longer qualify for IDA soft loans after their GNI per capita exceeds the low income threshold for three years in a row. The fact that many countries have graduated from Low Income to Middle Income status has thus resulted in a situation in which major forms of aid are no longer available for a number of countries that still might need it.

Mr. Chairman,

The renewed fragility of the world economy, and the growing downside risks, including for developing countries, have brought us to the brink of a second recession. The developing countries cannot bear the burden of supporting global growth alone. Urgent action is therefore needed to restore growth, particularly in the developed world, and to take measures to prevent a recurrence of the financial and economic crisis.

Table 1: World output growth, 2006-2012 (Annual percentage change)

	2006	2007	2008	2009	2010	2011 ^b	2012 ^b
World	4.1	4.0	1.5	-2.2	4.0	2.8	2.3
Developed countries	2.8	2.6	0.0	-3.8	2.6	1.4	1.1
<i>of which:</i>							
Japan	1.7	2.2	-1.0	-5.5	4.4	-0.7	2.3
United States	2.7	1.9	-0.3	-3.1	2.4	1.8	2.1
European Union (EU 27)	3.3	3.2	0.3	-4.3	2.1	1.5	-0.4
<i>of which:</i>							
Euro area	3.2	3.0	0.4	-4.4	2.1	1.4	-0.5
France	2.5	2.3	-0.1	-3.1	1.7	1.7	0.1
Germany	3.7	3.3	1.1	-5.1	4.2	3.0	0.9
Italy	2.2	1.7	-1.2	-5.5	1.8	0.4	-2.3
United Kingdom	2.6	3.6	-1.0	-4.0	1.8	0.8	-0.8
European Union (EU 12) ^c	6.5	6.0	4.1	-3.7	2.3	3.1	1.0
South-East Europe and CIS	8.4	8.6	5.2	-6.6	4.2	4.5	4.1
South-East Europe ^d	5.3	5.9	4.2	-4.2	0.6	1.1	-0.1
CIS incl. Georgia	8.7	8.9	5.3	-6.8	4.6	4.8	4.4
<i>of which:</i>							
Russian Federation	8.2	8.5	5.2	-7.8	4.0	4.3	4.5
Developing countries	7.6	7.9	5.3	2.4	7.6	5.9	4.8
Africa	6.1	6.0	4.8	0.9	4.6	2.4	4.1
North Africa (excl. Sudan)	5.4	4.7	4.6	3.2	4.0	-1.1	4.1
Sub-Saharan Africa (excl. South Africa)	6.9	7.2	5.6	0.5	6.0	4.7	4.8
South Africa	5.6	5.6	3.6	-1.7	2.8	3.1	2.7
Latin America and the Caribbean	5.6	5.6	4.0	-2.0	6.0	4.2	3.2
Caribbean	9.3	5.8	3.0	0.2	2.8	2.6	2.9
Central America (excl. Mexico)	6.4	7.0	4.1	-0.2	4.0	4.9	4.3
Mexico	5.1	3.4	1.2	-6.3	5.8	3.9	4.0
South America	5.5	6.6	5.4	-0.2	6.5	4.5	2.7
<i>of which:</i>							
Brazil	4.0	6.1	5.2	-0.3	7.5	2.7	1.5
Asia	8.6	9.0	5.9	4.1	8.5	6.9	5.3
East Asia	9.9	11.0	6.9	5.9	9.5	7.6	6.1
<i>of which:</i>							
China	12.7	14.2	9.6	9.2	10.4	9.2	7.8
South Asia	8.5	8.9	5.8	5.5	7.3	6.0	4.9
<i>of which:</i>							
India	9.6	9.7	7.5	7.0	9.0	7.0	5.6
South-East Asia	6.2	7.0	4.0	1.3	8.0	4.5	4.9
Western Asia	6.7	4.5	3.8	-1.1	6.5	7.0	3.3
Eastern, Southern and South-Eastern Asia	9.1	10.0	6.3	5.2	8.8	6.9	5.7
Asia and Oceania	8.6	9.0	5.8	4.1	8.5	6.9	5.3
Oceania	3.0	3.6	2.7	2.1	3.4	3.8	3.6

Source: UNCTAD secretariat calculations based on United Nations, Department of Economic and Social Affairs (UN/DESA), National Accounts Main Aggregates database and World Economic Situation and Prospects (WESP) 2012; ECLAC, 2012; OECD, 2012; IMF World Economic Outlook, April 2012; Economist Intelligence Unit, EIU CountryData database; J.P.Morgan, Global Data Watch; and national sources.

Note: Calculations for country aggregates are based on GDP at constant 2005 dollars.

a Average.

b Preliminary estimates for 2011 and forecasts for 2012.

c New EU member States after 2004.

d Albania, Bosnia and Herzegovina, Croatia, Montenegro, Serbia and The Former Yugoslav Republic of Macedonia.