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ECONOMIC VIEWPOINT

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The Fate of the Innocent Bystanders

In the aftermath of the G-20 Summit, many are pointing to the positives of the meeting, which can be summed up as some renewal of confidence, some sense of moderate stimulus, some regulatory reform, and some numbers. The numbers tend to focus on the IMF, the institution that will see its resources significantly enhanced as a result of the meeting. In addition to a possible trebling of resources, there is a new SDR allocation of $250 billion, which like previous emissions of SDRs will be allocated according to existing IMF quotas. What is not very clear is what assistance will be offered to the innocent bystanders to this crisis, the developing countries, especially the low-income victims.

A quick tally of exogenous factors that will affect developing country prospects includes rapidly diminished external markets for exports; dramatically reduced flows of external capital (viz., the IIF estimates total flows to emerging and developing countries of $165 billion compared to three times that amount in 2008 and six-times that level in 2007); lower remittances, which for many countries is more important than either FDI or ODA; some visible signs of increased protectionism by both developed and developing countries according to the WTO and the World Bank; and significant remaining uncertainties in global confidence. One may legitimately ask what in the G20 pronouncements will offset this negative economic news!

Let's start with the increased IMF resources. Much is destined to the new Flexible Credit Line (FCL) that will offer precautionary access up to 1000% of quota with no conditionality if the macro policy stance is seen to be solid. Mexico is the first taker to the tune of $ 47 billion, although nothing is yet drawn. Whether the stigma of the Fund will be overcome so that countries in East Asia and Latin America access the FCL remains to be seen, but in any event this line is not an adequate substitute for normal capital flows.

The SDR allocation of $250 billion would increase the stock of this reserve asset from its current level of $35 billion but the rules and distribution formula do not favor developing countries. In fact, low-income countries gain only $19 billion of which about $8 billion would go to Africa. Notions of distributing SDRs to developing countries dates back to the origins of SDR creation (see Leipziger on the Distribution of SDRs, *Journal of Development Studies*, 1975) but have never materialized. Equally problematic is the idea of gold sales to help finance low interest borrowing from IMF facilities because the gold sales require US Congressional approval, and the lending instruments are highly conditional. It is noteworthy that there have been no takers for the Fund's Exogenous Shocks Facility, even though we have witnessed the largest exogenous shock in 80 years!

Looking further at low-income countries (LICs), we see that although the World Bank has accelerated close to $1 billion in fast approval credits to the LICs in response to the food, fuel, and financial crises, this amount is not additional, merely accelerated. Official Development Assistance has also not increased dramatically, so unless the LICs had existing fiscal space or can reprogram domestic resources, they will be faced with increasing deficits and greater unmet demands. For many emerging market economics (EMEs) who rely on international capital, the rate of rollovers for both sovereign and corporate debt is worrying. Recent improved economic performance may well be put at risk, with backsliding on poverty reduction and fewer opportunities for the middle class in EMEs.

Giving EMEs more political voice in the G20 will not necessarily protect them as the unintended casualties of the crisis. Even more alarmingly, the LICs, who have the most to lose in terms of welfare setbacks, are at the moment set adrift, not really well represented at the G20, unable to gain much from the new IMF resources, buffeted by declining commodity prices, and potentially hit hardest by resurgent protectionism. It's not a good time to be an innocent bystander.

*The views expressed here are personal and do not represent necessarily the position of either the World Bank Group or its Board of Executive Directors. Comments can be sent to *Dannyleipziger@gmail.com.*