

Conference Participants Agree on Key Issues

On June 8–9, 1998, the IMF held a conference on economic policy and equity at its headquarters in Washington. Despite a diversity of views that made for lively discussions, the participants agreed on a number of key policy issues.

Vito Tanzi

AT THE CONFERENCE, which was organized by the IMF's Fiscal Affairs Department, senior policymakers, academicians, religious leaders, and labor representatives from around the world (see box) discussed the operational issues faced by governments seeking to formulate and implement equitable policies. A number of policy lessons emerged from the discussions and, despite the broad range of views presented, there was substantial agreement—and even consensus—on a number of important issues.

Solid, sustainable macroeconomic policies are a necessary condition for effectively promoting equity over the medium and long run.

This point was stressed by Eduardo Aninat, Chile's Minister of Finance, who pointed out that fiscal restraint had been a crucial element in Chile's reform program, allowing Chile to repay its debt, reduce interest payments, and, over the years, provide more resources to finance equity-oriented social expenditures. Professor Grzegorz Kolodko, former deputy prime minister and finance minister of Poland, noted that robust growth made it easier to promote equity: sharing the burden in a stagnant economy is more contentious than sharing the gains in a growing one.

More equity need not hamper growth.

Until recently, greater income inequality was thought to be a necessary precondition for faster growth—that is, overall savings would increase, making more resources available

for investment, only if a large share of a country's total wealth were held by a small number of individuals. And, as Professor Kolodko noted, it may be necessary to tolerate increased income inequality temporarily while a country firmly establishes itself on a high-growth path. But the consensus among the conference participants was that more equity would not dampen long-term growth but that it could indeed reinforce it. Deputy U.S. Treasury Secretary Lawrence Summers noted the strong negative link between a highly unequal distribution of assets and subsequent rates of growth.

The main focus of equitable policies should be to increase the prospects of the least fortunate.

As Professor Amartya Sen noted, "the greatest relevance of ideas of justice lies in the identification of *patent injustice*, on which reasoned agreement is possible, rather than in the derivation of some precise formula for determining how the world should be run." This point was reinforced by both Minister Aninat and Professor Anibal Cavaco Silva, former prime minister of Portugal, who stressed in their presentations that policies to reduce poverty and social exclusion should be given high priority. None of the speakers identified high incomes per se as a problem, because equity requires equality of opportunity, not necessarily equality of outcomes. Wealth need not be divisive if it is acquired fairly and used fairly and wisely. This view can be contrasted with the one that prevailed in the 1950s and 1960s, when high marginal tax rates—90 percent and higher (for example, in the United



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Kingdom)—were considered essential for reducing the incomes of the wealthiest.

In this context, IMF First Deputy Managing Director Stanley Fischer cautioned that the goal of complete “equality” of opportunity was both unrealistic and unattainable. Rather, governments should focus on the more attainable goal of providing all members of society with an adequate or acceptable level of opportunity. In Professor Sen’s terminology, this would imply eliminating absolute “deprivations” and reducing relative ones.

Equity should not be viewed solely as an issue of income distribution.

Equity is a multidimensional concept covering equality of opportunity and access as well as the distribution of consumption, wealth, and human capital. Because equity is multidimensional, it cannot be measured by a single aggregate index, nor can it be achieved by a single best policy prescription. Each country is unique and must address its own poverty indicators. The manifestations of inequity and the reactions to them vary greatly across countries—and these variations depend not only on a country’s stage of development but also its political climate, initial distributions of wealth and income, social norms, and a host of other influences.

In the long run, the best way to help the poor is to empower them.

To succeed, the poor need to increase their human capital. This, in turn, requires access to education, basic health care, and nutrition. Government spending on these services can enable people to pull themselves out of poverty. However, a mere increase in government spending on social services is not sufficient; the quality of the output is also important. Enrique Iglesias, President of the Inter-American Development Bank, made this point forcefully in the context of education. High dropout rates in Latin America continue to affect student attainment levels. As a result, large wage differentials between skilled and unskilled workers remain a problem in this region.

Empowering the poor requires not only providing them with adequate access to opportunities but also improving the opportunities open to them.

In this regard, it is also important to provide the poor with access to credit, justice, and public services. Several speakers, including Professor Sen, related the concept of empowerment to employment. They observed that the debilitating effects of unemployment are important manifestations of inequity, even if transfer programs protect consumption.

Several speakers argued that the promotion of labor market flexibility is an important example of the substantial synergy between equity and growth; flexibility in labor markets makes it easier to realize returns on investments in human capital. In this context, Professor Cavaco Silva highlighted the seductive appeal regulations (such as minimum wage

legislation) that appear to promote legitimate social goals without requiring tax or spending programs have for politicians. He stated that unwise labor regulations should be avoided because they generate large market distortions, helping “insiders” (union workers) while hurting “outsiders” (young workers, the less skilled, or the unemployed). He also stressed that an important role of the economic advisor is to reduce the temptation of politicians to employ market-distorting regulations.

Social safety nets and well-targeted transfer programs are important means of softening hardships.

Social safety nets are particularly critical during adjustment periods. They must be carefully designed so that incentives to be a productive member of society are not unduly diminished and to avoid creating an inefficient “welfare bureaucracy” with the potential to become self-sustaining. In this context, Professor Alberto Alesina warned that too much government involvement (often seen in the countries belonging to the Organization for Economic Cooperation and Development)—even in the name of equity—can create a culture of dependency on the government.

To facilitate improvements in equity and build wider ownership of and support for reforms, governments will need to operate more efficiently and to improve the quality of public services.

Professor Alesina made this point most strongly with respect to developing countries, which often have inefficient tax systems and lack both the revenue and the political will needed to provide a strong infrastructure and an effective social safety net. Those safety nets that exist are inefficient, and many of the benefits are captured by the middle classes, primarily urban groups. Moreover, developing countries tend to have inefficient bureaucracies and relatively high levels of corruption.

In some developing and transition economies, the growth of the informal sector has seriously limited the government’s ability to finance equitable policies. Improving the fairness of tax systems—and of their enforcement—will attract activity to the formal sector and provide governments with the resources to finance investments in empowerment initiatives and safety nets. Karin Lissakers, the U.S. Executive Director at the IMF, mentioned the IMF’s effort during the Asian crisis to move beyond numbers and look at issues of institutional structures and government organization. She observed that the benefits of macroeconomic adjustment can be fleeting if they are not underpinned by sound institutions and public management.

With respect to developed countries, Professors Anthony Atkinson and Anibal Cavaco Silva both noted that political support for traditional tax and transfer policies is waning and that policies to promote equity will therefore have to be funded primarily by restructuring expenditures rather than by raising taxes or increasing government spending. (This was, in fact, a major theme of Minister Aninat’s paper.)



Left photo, conference panelists; right photo, Archbishop Ndungane and Nieves R. Confesor.

Conference participants

Adelman, Irma	Professor, University of California at Berkeley
Alesina, Alberto	Professor, Harvard University
Aninat, Eduardo	Minister of Finance, Chile
Atkinson, Anthony	Warden, Nuffield College, Oxford University
Barr, Nicholas	Senior Lecturer, London School of Economics
Birdsall, Nancy	Executive Vice President, Inter-American Development Bank
Cavaco Silva, Aníbal	Professor, Nova University of Lisbon and Portuguese Catholic University, former Prime Minister of Portugal
Chia, Siow Yue	Professor, Director, Institute of Southeast Asian Studies, Singapore
Collins, Susan M.	Associate Professor, Georgetown University
Confesor, Nieves R.	Presidential Advisor for Human Resource Development and International Labor Affairs, the Philippines
Dmitriev, Mikhail	First Deputy Minister of Labor and Social Development, Russia
Fischer, Stanley	First Deputy Managing Director, International Monetary Fund
Guo, Shuqing	Secretary General, State Commission for Restructuring the Economic System, China
Iglesias, Enrique	President, Inter-American Development Bank
Kanbur, Ravi	Professor, Cornell University
Kolodko, Grzegorz	Professor, Warsaw School of Economics, former Deputy Prime Minister and Finance Minister, Poland
Levy, Santiago	Undersecretary of Expenditures, Mexico
Lissakers, Karin	U.S. Executive Director, International Monetary Fund
Martin, Monsignor Diarmud	Secretary, Pontifical Council for Justice and Peace, Vatican City
Milleron, Jean-Claude	Executive Director, France, International Monetary Fund
Munnell, Alicia H.	Professor, Boston College
Ndungane, The Most Reverend Njongonkulu	Archbishop of Cape Town and Metropolitan Church of the Province of South Africa
Ouattara, Alassane D.	Deputy Managing Director, International Monetary Fund
Perry, Guillermo	Chief Economist for Latin American and the Caribbean, World Bank
Ramos, Maria	Director-General, Department of Finance, South Africa
Rodríguez Maradiaga, Monseñor Oscar Andrés	President, Latin American Council of Bishops and Archbishop of Tegucigalpa, Honduras
Sen, Amartya	Master, Trinity College, Cambridge, and Professor of Economics, Harvard University
Sengupta, Arjun	Professor, School of International Studies, Jawaharlal Nehru University
Sewell, John	President, Overseas Development Council
Smith, David	Director, Public Policy Department, AFL-CIO
Summers, Lawrence	Deputy Secretary, Department of the Treasury, United States
Tanzi, Vito	Director, Fiscal Affairs Department, International Monetary Fund

Improved government efficiency is important for another reason. Designing reforms that improve ordinary citizens' daily lives could bring about greater ownership of, and support for, reforms. This would be achieved by, for example, promoting competition in electricity, transportation, and other services to improve their quality.

Globalization of the world economy does not explain higher income inequality within individual countries.

While some have argued that globalization poses a threat to the well-being of less skilled workers in industrial countries and that domestic policies are powerless against this threat, participants were of the view that it is not so much increased

trade but technological developments and changing social norms that explain the growing disparities between the wages of skilled and unskilled workers in developed and developing countries. As Deputy Secretary Summers noted, not only have new technologies tended to be skill-reinforcing but "greater market forces . . . have tended to make everyone be paid more like salesmen on the basis of what they produce." In this sense, he echoed Mr. Fischer's observation that, although globalization by itself does not explain changes in income distribution, the interaction of globalization and technological change may have a larger impact.

Professor Atkinson stressed that globalization has not curtailed the ability of governments to promote equity. He

believes that many societies have changed their views of what constitutes a "fair" distribution of wages, but that globalization has not forced these changes. In this sense, the constraints on governments are political, rather than economic, as evidenced by the declining support for tax and transfer programs.

Deputy Secretary Summers cautioned that equity is not only an important moral issue but that it is also critical to the political viability of globalization. Support for open economies will be difficult to muster if too many people doubt that openness works for them.

Communication and collaboration between the finance and social ministries in formulating and implementing policies affecting equity need to be improved.

Even the perception of discord among ministries on eco-

“Social safety nets are particularly critical during adjustment periods.”

nomics and social goals can impede progress, while open discourse can lead to broader agreement on both long- and short-term strategies; the various ministries should not work at cross purposes.

In summing up the conference, Mr. Fischer noted that because IMF advice on macroeconomic and structural issues has implications for equity, the IMF has no choice but to address equity in its core activities. More troubling for him, however, was how much the IMF

can do and when it should do it. Should the IMF lend to corrupt governments? Where does national sovereignty end and the interests of the IMF and its membership begin? There are no easy answers, he commented. This observation formed a fitting conclusion to the conference: although important steps were taken in framing the debate, work is far from complete. **F&D**

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