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Event report

Global Crisis, More Than Just Economics

With Jean-Marc Coicaud, Finn Tarp and Tony Addison

Worldwide in New York

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The event “Global Crisis, More Than Just Economics” featured Professors **Finn Tarp** and **Tony Addison**, Director and Chief Economist respectively, of the **World Institute for Development Economics Research of the United Nations University** (UNU-WIDER). Professor Tarp opened the forum by explaining the context that pushed UNU-WIDER to explore the consequences of the economic meltdown from a broad angle. As the global economic crisis unfolded, he sustained the view that the issue could not be studied or explained exclusively by economics due to its potential to undermine social stability. This argument was then developed in the UNU-WIDER Working Paper No. 2010/10 entitled ‘**The Triple Crisis and the Global Aid Architecture**’.

Prof. Tarp began by stating the immediate concern that the financial crisis resulted from turmoil in the global economy. However, this concern has masked the fact that there are three interrelated global crises undermining the prosperity and welfare of present and future generations. The responses to these crises suggest that they have been treated in separate silos rather than from an angle that aims to understand its interconnections and global implications for development assistance and policy.

The first of these crises, the **financial meltdown**, has seen the deepest economic downturn in 60 years and no region or country has been spared. The speculations about an upturn are sustained by tentative signs which should not lead to a delusion of a full recovery: all current predictions by economists are uncertain. Moreover,



global trade has suffered a sharp decline, which according to some accounts, has exceeded that of the Great Depression. In addition, net private capital flows (including remittances) to the South have fallen in aggregate and to every region, and global foreign direct investment flows have decreased.

The response of the global economy to the financial crisis has been marked by an unprecedented monetary and fiscal expansion, 'a heavy dose of Keynesian medicine' as described by Prof. Tarp. However, it is too early to say whether these measures will work. Indeed, governments of Northern countries are close to their borrowing limits and reductions in fiscal deficits are already being discussed. The implications for the South are potentially damaging given that this geographic region is dependent on foreign aid. It seems that business as usual will no longer be sufficient to maintain development assistance in the South.

Prof. Tarp reminded the audience that the average banking crisis reduces the output per capita by 10%, generating a loss that takes at least 7 years to be restored. In addition, the current target for foreign aid is expressed as a percentage of Gross National Income (GNI). This indicates that in order to maintain the current volume of assistance, aid would need to increase faster as a percentage of total spending – a very unlikely phenomenon under the business-as-usual scenario. Further, while the UN sets a goal of 0.7% of GNI of net Official Development Assistance (ODA), many countries are far from reaching this goal, contributing an average of 0.47% of GNI. Data collected by the OECD also shows that the ODA/GNI ratio decreased for 12 out of 22 DAC donors before the crisis, on top of the fact that net ODA disbursements have been inflated by debt relief. Excluding debt relief, foreign aid to Africa has not risen in real terms since the late 1980s.

Aid critics tend to take two stances toward the subject. Some argue that if aid were eliminated, growth would rise; others say that aid is simply ineffective. However, Prof. Tarp discussed empirical evidence which proves the positive impact of aid at



the macro, meso, and micro levels, conforming to modern growth theory, thus dismissing Dambisa Moyo's suggestion of ceasing aid to Africa. Aid is at a critical juncture; Africa's modest progress in attracting private capital flow could be seriously hampered if aid flows stop.

The second crisis – the **food crisis** – was characterised by a sharp increase in the food prices in 2007-2008, after which they dropped. Prof. Tarp argued that changes in price reflect three issues: the low priority given to agriculture and food production; the shift in demand patterns; and an increase in the use of biofuels combined with lack of research in alternative energy sources. Thus, the underlying structural problems behind the recent crisis still exist. Additionally, he mentioned that the global food architecture is not adapted to deal with supply shortages, which can in turn push governments to adopt protectionist measures to satisfy domestic demand.

In terms of responses to the crisis, Prof. Tarp observed that measures in Africa were essentially focused on macro-policies, whereas in the rest of the world a greater emphasis was placed on social protection. Both approaches entailed high costs and were implemented ad-hoc rather than systematically. More importantly, however, is the threat of a double-edged sword: if recovery stalls, there is a risk of reoccurring trade and financial shocks; if recovery is sustained, food and energy prices will climb, affecting energy and food importers. Although there is a great need for public action, fiscal action is limited in poorer economies.

Finally, Prof. Tarp explored the **climate crisis**. He argued that the current growth model is unsustainable, thus requiring the transformation of our existing energy systems and a simultaneous adaption to the effects of climate change. According to Prof. Tarp, the failure to stop fossil-fuel dependence is exemplified by the increase in oil prices prior to the financial crisis, resulting from a lack of investment in energy research. If growth resumes, energy prices will also increase, placing major burdens on poor countries and making states more aid-dependent. Interestingly, Prof. Tarp



mentioned that the costs of mitigation and adaptation per annum far exceed the current level of aid. He also pointed to a number of important issues related to climate change finance based on the outcomes of COP15; comparing climate change financing – seen as compensation – with aid processes, which are conditional.

In his concluding remarks, Prof. Tarp recalled that there is not only one but three interrelated global crises that must be addressed in a global, coordinated fashion, and for which a business-as-usual recovery scenario could have disastrous consequences. With the world at a turning point, Dr. Tarp highlighted the importance of having global institutions take global action.

Question and Answer Session

The Q&A session was marked by a lively exchange between the audience and the panel. A question on the current global arrangements for the production, distribution and pricing of food and its effects on food security and nutrition was answered by Prof. Addison. In response, he outlined three changes that were needed to amend the current system: increased investment in the agricultural sector at the national level by governments; increased assistance to poor governments (constrained on aid over the last 10 to 20 years in the agricultural sector) in order to raise their productivity; and the creation of good systems of social protection (following the examples of Brazil, Mexico and India). He affirmed that all of these changes were needed if countries are to cope adequately with malnutrition and food scarcity.

Another question touched on the issue of the growing global population, which according to Prof. Addison has already been built into UNU-WIDER's research models. He agreed that population growth is a force propelling oil and food prices and is a major issue on which a lot of work is currently being carried out.



The speakers were also asked their opinion about the need for systemic ecosystem change as opposed to adaptation in the context of climate change. Prof. Addison mentioned that there is a great need for research on the effects of climate change at the country and regional levels so that societies are in a better position to choose their investment priorities. He also placed emphasis on the fact that it is essential to link the science of climate change with the social sciences. Prof. Tarp complemented the answer by stating that investment decisions taken today are irreversible, and will significantly impact the future of the environment so should not be taken lightly; therefore he underlined the need for a better understanding of the effects of climate change on the economy. Additionally, both speakers recognized the increasingly crucial role of technology in tackling climate change as well as the need to have businesses engaged in collaboration with public institutions to address this issue.

Finally, Professors Tarp and Addison discussed the importance of having the United Nations system work on economic issues. As a political body, the United Nations has to be very aware of the connection between economic issues and conflict – the three crises being a potential source of dispute among nations. The UN is the global actor par excellence, and as such it is responsible for making nation-states and people think and take action with regard to these critical issues.