Chapter 2
Reforming the International Financial and Fiscal System for Better COVID-19 and Post-pandemic Crisis Responsiveness

Rolph van der Hoeven and Rob Vos

Abstract The global economic crisis provoked by the COVID-19 pandemic disproportionally hurt developing countries, increasing poverty, food insecurity, and income inequality. Richer nations cushioned their economies from the worst impacts with unprecedented massive fiscal and financial support programmes. Developing countries lacked such capacity and received feeble multilateral contingency financing, symptomizing the fundamental flaws in the international financial and fiscal system (IFFS). Four reforms will make the IFFS better suited to serve sustainable development: (a) an equitable international tax coordination mechanism; (b) a multilaterally backed sovereign debt workout mechanism; (c) overhauling policy conditionality associated with development finance; and (d) increasing Special Drawing Rights to be leveraged for development finance.

2.1 Introduction

The global economic crisis provoked by the COVID-19 pandemic once more has painfully revealed fundamental flaws in the international financial and fiscal system (IFFS). It failed to provide adequate crisis response, especially to the low-income countries which have been hard hit by the global economic repercussions of the pandemic. Even though the spread of the pandemic was less pervasive in affecting

R. van der Hoeven (✉)
UN Committee for Development Policy, New York, USA

International Institute of Social Studies (ISS), Erasmus University Rotterdam, The Hague, The Netherlands
e-mail: rolph@vanderhoeven.ch

R. Vos
International Institute of Social Studies (ISS), Erasmus University Rotterdam, The Hague, The Netherlands

Markets, Trade and Institutions Division (MTID), International Food Policy Research Institute (IFPRI), Washington, DC, USA

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health conditions in many low-income countries, they were hit disproportionally hard by the spill-over effects from the economic crisis in major economies, especially those of Europe and the United States, while possessing few financial means to mitigate the impact on livelihoods of their populations.

In this chapter, we assess the differential impact of the pandemic on livelihoods around the world. Specifically, Sect. 2.2 describes how the COVID-19 crisis has set off a deep global recession with potentially lasting setbacks in terms of human development, increasing poverty, income inequality and food insecurity. Some of the poorest countries, as those in Africa, are among the hardest hit economically even though being, thus far, less hurt by the spread of the pandemic itself. While high-income countries have taken unprecedented measures to mitigate impacts on livelihoods, poor nations' responses have been muted lacking financial space.

Section 2.3 then documents how the economic consequences of the pandemic have once more lay barren the weaknesses of the current IFFS, which fails to allocate sufficient contingency financing where it is needed the most. Where high-income countries could engage in massive and almost costless fiscal and monetary expansion, developing nations ran up debts to severe distress levels and faced liquidity shortages for undertaking even the smallest of deficit financing. This lack of fiscal space and access to finance has its origins in the weaknesses of the IFFS, including the pervasive biases in internationally poorly-coordinated tax systems causing tax base erosion and profit shifting, the inadequacy of international contingency financing mechanisms, the lack of appropriate sovereign debt management mechanisms, and the absence of a truly international currency that could serve both as a multilateral source of liquidity provisioning during crises and a basis for leveraging development finance to build resilience against the impacts of future crises.

Section 2.4 discusses options on how these weaknesses in the IFFS can be addressed in the short and medium run, including through reform of international tax coordination mechanisms, putting in place a multilaterally backed sovereign debt workout mechanism, reform of policy conditionality attached to contingency financing, and issuance of additional, truly international liquidity in the form of Special Drawing Rights both to provide additional contingency finance and to leverage new development finance. With such reforms already in place, the pandemic response would have provided a fairer level playing field for emerging and developing countries and have mitigated the pandemic's worst economic consequences. Beyond the pandemic, these reforms will aid the recovery and refocus international development finance towards the internationally agreed Sustainable Development Goals. As discussed in the concluding section, important political hurdles will have to be overcome to enact those reforms in the present-day context of withering multilateralism. It is of interest to note here, that since the time of writing (April 2021), the international community has taken several steps towards the fulfilment of these recommendations. First, the Group of Twenty (G20) of major economies agreed to establish a common 25% corporate tax rate in a concerted effort to discourage profit shifting by multinational companies, a phenomenon that is currently eroding the tax base of many countries. And, second, approval by the International Monetary Fund (IMF) of the issuance of US$650 billion in Special Drawing Rights (SDRs).

Although, a proper allocation mechanisms for use of the additional international liquidity is yet to be agreed upon, it is an important step in the right direction. It shows that reform is possible, though there is still a long way to go, as this chapter makes clear.

2.2 Economic, Social and Nutritional Effects of the COVID-19 Crisis

2.2.1 Economic and Social Effects

More than half of the world population has been, still is or is again under some form of social distancing regime designed to contain the health crisis posed by COVID-19. Business activity has fallen sharply because of a combination of policy action and personal responses designed to reduce risk of contracting the virus, with personal action probably more important than policy in reducing economic activity (Goolsbee and Syverson, 2020). Disruptions in production and income losses underpinned the combined supply and demand shock provoking a global recession much deeper than that of the global financial crisis of 2008–2009. The International Monetary Fund (IMF, 2021a, b) projects that the impacts could well be felt for some time to come. It estimates that despite tangible recovery in 2021, global GDP would still be 3.7% below pre-COVID levels by January 2022 (Fig. 2.1). Developing regions are being hit the hardest, with GDP losses in developing Asia (excluding China) estimated at 8% and in Latin America and Sub-Saharan Africa at 6.9% and 6.1%, respectively. Aside from supply disruptions caused by lockdown measures taken by governments in these regions, developing countries are hurt foremost by the transmission of the recession in Europe and the United States through channels of trade, finance and remittances.

A key symptom of the recession has been the substantial loss of working hours throughout the world. The International Labour Organization (ILO, 2021) documents that in 2020 globally, around half of working-hour losses were due to employment loss, while the other half can be attributed to reduced working hours (including workers who remain employed but are not working, see Fig. 2.1). It found further that there was significant variation between regions: employment losses, both as a share of the working-age population and in relation to working-hour losses, were highest in the Americas, and lowest in Europe and Central Asia, where reduced working hours have been extensively supported by job retention schemes. The ILO estimates that, despite the adjustment through reduced working hours, employment losses were nonetheless massive in 2020, with 114 million jobs lost relative to the pre-crisis employment level in 2019. However, this estimate may well understate the full extent of job losses: a model-based scenario analysis suggests global employment decline could have affected as many as 144 million jobs compared with a "no-pandemic" scenario (ILO, 2021).

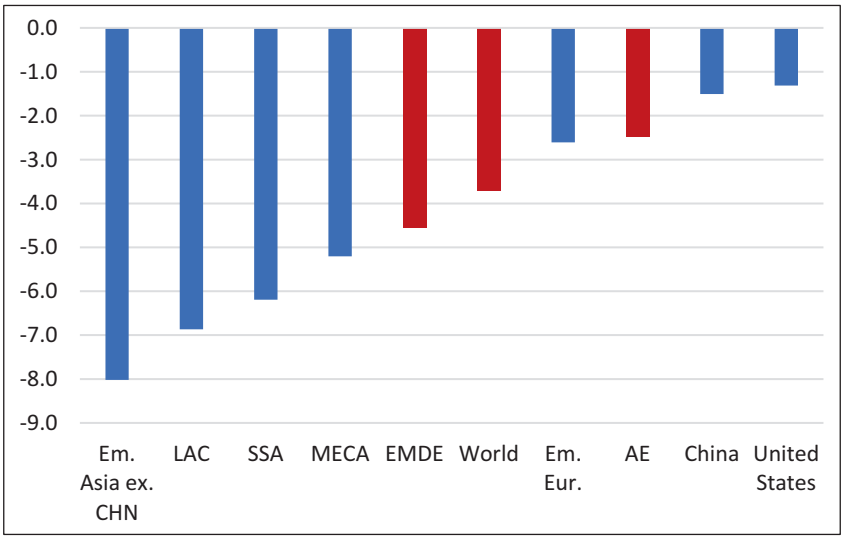

Fig. 2.1 GDP losses (projected levels for January 2022) relative to pre-COVID output levels (percentage change)
Source: IMF World Economic Outlook, January 2021 (IMF, 2021a)
Legend: Em. Asia = ex CHN emerging Asia, excluding China; LAC = Latin America & Caribbean; SSA = Sub-Saharan Africa; MECA = Middle East and Central Asia; EMDE = group total for emerging and developing economies; Em.Eur = emerging Europe; AE = advanced (high-income) economies

In stark contrast with the Great Recession of 2008–2009, the COVID-19 related fall in employment mainly translated in rising inactivity rather than rising unemployment rates: of the mentioned job losses 81 million refer to people shifting into economic inactivity, while 33 million became unemployed. As a result, the global labour participation rate dropped by 2.2% points during 2020 (compared with a just 0.2% points decline between 2008 and 2009). As shown in Fig. 2.2, only high-income countries saw, on average, a greater increase in unemployment than in inactivity (driven largely by labour market adjustment in the United States).

Owing to the massive losses in working hours, workers suffered large reductions in their income from work. The ILO estimates that labour income declined by 8.3% in 2020 relative to 2019 (Fig. 2.3). The greatest labour income loss, amounting to 12.3%, was experienced by lower-middle income countries. While average labour income losses were of similar magnitude in low-, upper-middle- and high-income countries, these averages disguise large disparities across and within these country groupings. When looking by geographic region, it shows that workers in the Americas lost an estimated 10.3% of their labour income, compared with 6.6% for workers in Asia and the Pacific.

Overall, in nominal terms, global labour income declined by about US$3.7 trillion (using 2019 market exchange rates) during 2020, corresponding to 4.4% of global GDP in 2019 (ILO, 2021).

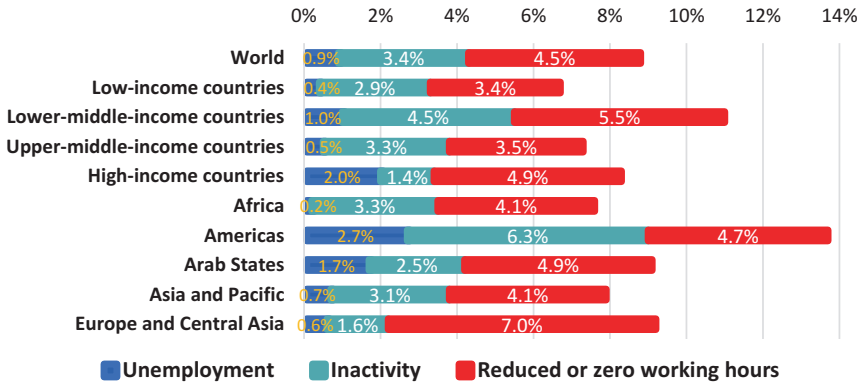

Fig. 2.2 Decomposition of working-hour losses into changes in unemployment, inactivity and reduced working hours (averages for the world and by income group and region in 2020, percentage change)
Source: ILO (2021: Fig. 7).
Note: The overall working-hour loss is decomposed into changes in unemployment, inactivity and reduced or zero working hours. Unemployment plus inactivity equals the total employment loss. Unemployment and inactivity have been transformed into their working hour equivalent using the average working hours per week. The working-hour equivalent of changes in employment, unemployment and inactivity is computed using the estimated average working hours per week, which ranges from 35 to 48 h per week across the income groups and regions.

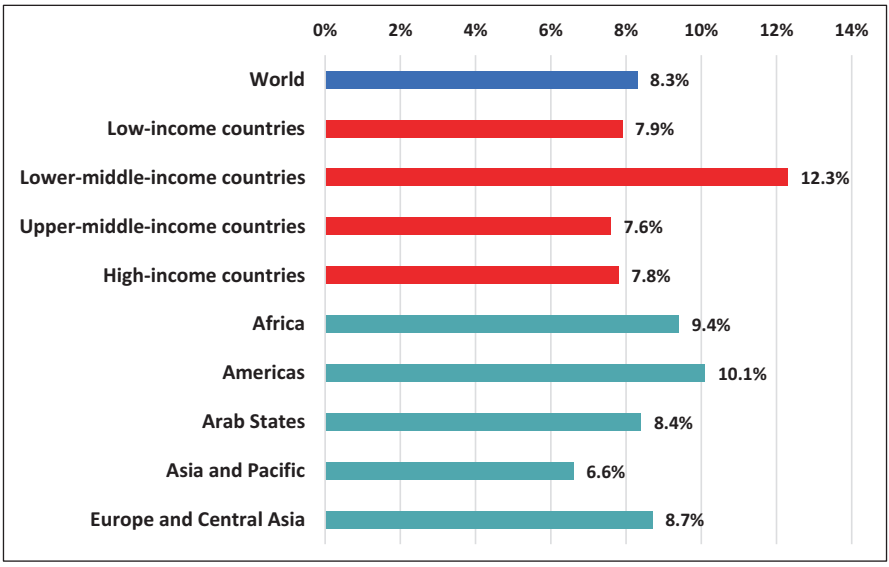

Fig. 2.3 Share of labour income lost due to working-hour losses in 2020, before income-support measures (average for the world and by income group and region, percentage change)
Source: ILO (2021: Fig. 9).
Note: Labour incomes were aggregated across countries using purchasing power parity exchange rates.

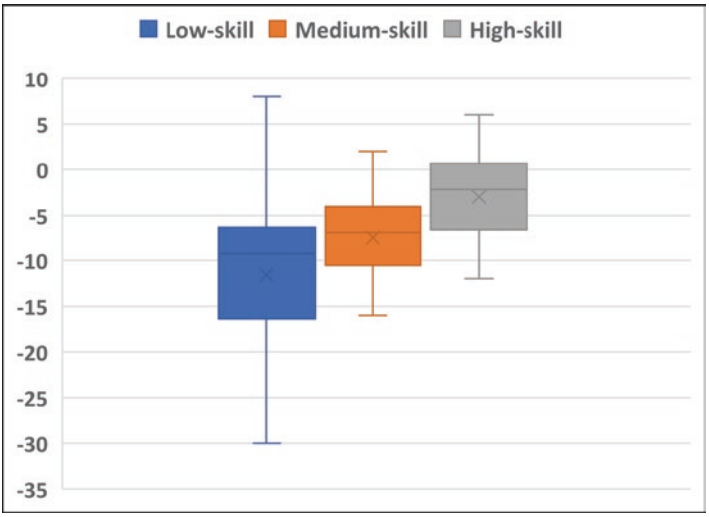

Fig. 2.4 Year-on-year country-level changes in employment, by skill level, second quarter of 2022 (percentage change)
Source: ILO (2021: Fig. B2).
Note: The sample consists of 50 high- and middle-income countries and territories with employment data for the second quarter of 2020 and disaggregated by occupation. The box graph should be read as follows: (a) the vertical line in the middle of the box represents the median value (50th percentile; (b) the lower side of the box (whisker) represents the 25th percentile; (c) the upper side of the box (whisker) represents the 75th percentile; (d) the adjacent lines to the above and below the box represent the highest and lowest values, respectively
Legend: Low-skill = elementary occupations and skilled agricultural workers*;* Medium-skill = clerical support workers, services and sales workers, craft and related trades workers, plant and machine operators, and assemblers; High-skill = managers and technicians, and associate professionals. The skill level categories are based on ISCO-08. See ILOSTAT for further details on these definitions

Labour income losses caused by the pandemic show stark inequalities between groups of workers (Murshed, 2021). Generally, low- and medium-skilled workers were much more affected by employment and income losses than better skilled workers (Fig. 2.4). This is in part because teleworking more often proved an option for those workers, while social distancing measures hampered executing many lower skilled jobs. Where the capacity to strengthen social safety nets is weak, the labour income losses pushed many households into poverty (forcing them to reduce spending on necessities once savings were used up) and further deepened the recession because of demand fallout. We take a closer look at the poverty and consumption impacts in the next subsection.

2.2.2 *Poverty and Food Consumption Effects*

Assessing the poverty impact of COVID-19 is no trivial matter. This is so not only because the crisis is still unfolding and available information of its precise socio-economic consequences is incomplete, but also because the channels of influence are multiple and interconnected globally. Several widely cited analyses have used simplistic approaches calculating the projected impact of the global recession on average per capita incomes to estimate poverty impacts, using household survey data available through the World Bank's PovcalNet website (see, for example, the studies by the World Bank in Mahler et al., 2020 and World Bank, 2020a, 2020b; and that of UNU-WIDER by Sumner et al., 2020). A major drawback of this approach is that it assumes that the crisis has had no impact on within-country income distribution and, consequently, that workers across sectors and type of activity were all affected to the same degree.

Laborde et al. (2021) point out that this assumption fails to account for the complexity of the channels of effect and may substantially underestimate the impacts of the pandemic. They use a global general equilibrium model linked to country-specific household models to simulate the impacts of the COVID-19 pandemic on poverty and food security, considering all key transmission channels, including the labour market impacts discussed in the previous sub-section.[1] Beyond the direct effects of the disease on the ability to work, income losses arise from people's desire to avoid catching the disease and their altruistic concerns to avoid infecting other people, and from policy responses designed to reduce the adverse externalities associated with an unmitigated pandemic. Many of the related changes in behaviour and in the functioning of economies are not yet fully understood, while it is also difficult to rely on experience from past events, since no events like the COVID-19 pandemic have occurred on this scale in today's globalized world. Therefore, Laborde et al. (2021) have had to make several assumptions about the responses of economic agents to this unprecedented situation.

They distinguish four drivers of COVID-19 impacts: domestic supply disruptions, global market disruptions, household behavioural responses and policy responses. In a scenario with assumptions based on evidence available by September 2020, Laborde et al. (2021) project a 7% decline in global GDP in 2020 (compared with a scenario without COVID-19) and, consistent with the IMF projections presented earlier, they show that developing countries are being hurt disproportionally through declines in trade and remittance incomes and disruptions in businesses caused by social distancing measures.

Without any significant social and economic mitigation measures, e.g. in the form of a fiscal stimulus and expansion of social safety nets in the global South (scenario assumption, but see also Sect. 2.3 below), the impact on extreme poverty (measured against the PPP$1.90 per person per day international poverty line) is devastating, as shown in Fig. 2.5. The number of poor increases by 20% (almost

[1] For details and model assumptions see Laborde et al. (2020, 2021: online appendix)

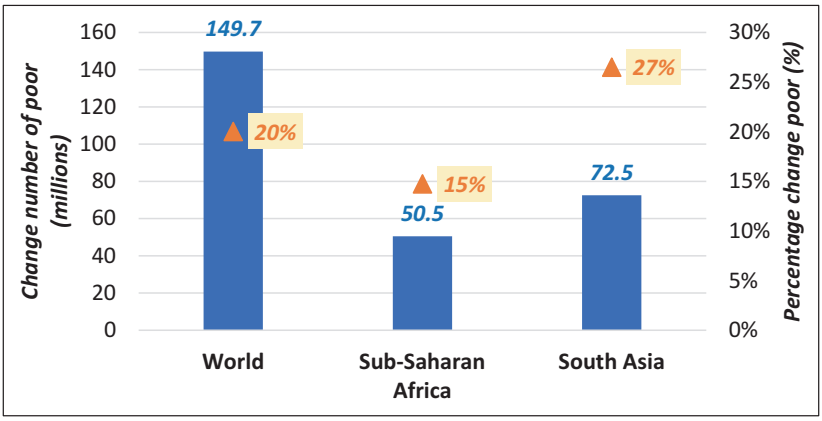

Fig. 2.5 Global and regional poverty impacts of the MIRAGRODEP COVID-19 scenario (September 2020; absolute and percentage change from baseline values)
Source: Laborde et al. (2021: Table 2).

150 million people) with respect to the situation in the absence of COVID-19, affecting urban and rural populations in South Asia the most, where 72.5 million more people would be joining the ranks of the poor (equivalent to a 27% increase in that region). The poverty increase in rural areas is expected to be smaller than that in urban areas, partly because of the lower rate of transmission of the disease and partly because of the robustness of demand and supply for food relative to many other, more vulnerable sectors. The number of poor people in Sub-Saharan Africa is projected to increase by 15% or 50.5 million people.

A decomposition of the poverty impact shows that the estimated increase in the number of poor by 150 million is substantially higher (i.e., about 50 million more) than when assuming a uniform drop in average per capita incomes in each country, as done by the earlier cited studies of the World Bank and UNU-WIDER. It indicates that COVID-19 must have significantly worsened within-country income inequality, as well.

The income and price changes associated with the recession and supply disruptions caused by pandemic are furthermore likely to have resulted in substantial changes in patterns of food consumption, with adverse nutritional consequences. Laborde et al. (2021) project that these will induce shifts in demand away from nutrient-dense foods, such as fruits and vegetables, dairy products and meats, and towards calorie-rich basic staple foods, such as rice, maize and other basic grains, raising concerns about dietary quality and likely increase in micronutrient deficiencies. The dietary shift is (on average) similar in both developed and developing regions.

2.3 Fiscal and Financial Crisis Responses: Save Thyself First?

The strongly integrated world economy facilitated the rapid spread of COVID-19 and its economic repercussions around the world. As we showed in the previous section, poorer nations and more vulnerable households have been hurt disproportionally by the economic consequences of the pandemic. Economic response capacity was very uneven. While rich countries engaged in unprecedented responses in macroeconomic terms to mitigate impacts on livelihoods of their citizens, most of the worst-hit countries lacked such economic response firepower. Multilateral mechanisms should have provided a cushion but proved to be unfit for such purpose.

2.3.1 The Scramble for Access to Vaccines

In Spring 2020, there was certainly a greater awareness than before of a necessary global response including the need to save lives. A search for and the production of reliable vaccines took off with much national government support. Internationally, the World Health Organization (WHO) swiftly moved to set up its ACT[2] Accelerator and the COVAX.[3] The purpose of these mechanisms was to finance the acceleration of the development of COVID-19 vaccines, to secure availability of sufficient doses for all countries, and distribute those doses fairly, beginning with the highest risk groups and spreading to cover the entire global population as soon as possible. However, because of limited and falling domestic resources in developing countries, by April 2021, both the production and distribution of vaccines was still heavily skewed in favour of serving the populations in high-income countries. The COVAX remained heavily underfunded more than a year into the pandemic, and unable to buy the vaccines needed to cover even a fraction of the population of developing countries, as global supplies have been by and large captured by the wealthier nations.

In effect, inequalities in access to vaccines to combat the pandemic have been reflective of how financial responses have worked out. A lagging behind in vaccination rates in developing countries has serious repercussions for global immunity rates as the virus still can mutate and cause again worldwide infections compounding already grave economic consequences.

A further complicating factor is that production of vaccines in poorer countries is hampered by persistence of patent rights allowing pharmaceutical companies a monopoly of production, either by themselves or by companies able to purchase

[2] ACT stands for Access to Covid-19 Tools (https://www.who.int/initiatives/act-accelerator)

[3] COVAX stands for COVID-19 Vaccines Global Access Facility, led by the World Health Organization, the Coalition for Epidemic Preparedness Innovations, and Gavi, the Vaccine Alliance. See: https://www.who.int/initiatives/act-accelerator/covax

production licenses. The WTO agreement on Trade-Related Intellectual Property Rights (TRIPS) allows for compulsory licensing, while the Doha declaration on TRIPS and public health contains an explicit clause permitting compulsory licensing essential drugs in case of public health emergencies.

A refusal by rich countries to set in motion existing clauses in international trade rules and underfunding of financial support to purchase and develop vaccines in poorer countries resulted in a highly unequal distribution of vaccines towards these countries. By Spring 2021, 130 countries had not yet administered a single dose to their populations and at current rates of distribution some people in developing countries will not receive a vaccine until 2024 (INET, 2021: 7). A continuing threat of COVID-19 contamination in countries with low vaccination levels increases social and economic uncertainty hampering prospects for economic recovery and progress. Furthermore, it is no coincidence that developing countries, where the availability of vaccines is low, have also less resources to stimulate their economies.

2.3.2 Stark Inequalities in Financial Response Capacity

Governments not only need additional resources to address the health impacts of the COVID-19 crisis and for the development and roll-out of vaccines, but also to finance the costs of the various lockdowns necessary to halt the spreading of the virus as well as to stimulate the economy to make up for the fall in final demand caused by the COVID-19 crisis. Globally, fiscal and monetary stimulus and emergence support measures amounted to US$14 trillion or 13.5% of world GDP. Fiscal support measures summed to almost US$8 trillion (or 8% of world GDP). The government response was vastly larger than that following the 2008–2009 global financial crisis, and likely has prevented a much deeper global recession. Inequalities in the fiscal and monetary response capacity run as deep as the overall response has run high. Figure 2.6 shows the stark differences between high-, middle- and low-income countries. High-income countries provided fiscal stimulus to the tune of 12.5% of GDP on average; this was three times more in relative terms than emerging and other middle-income countries were able to provide and almost ten times more than that provided by governments in low-income countries. In per capita terms, the inequalities run even deeper. UN-DESA (2021) estimates that the stimulus packages per capita by the developed countries has been nearly 580 times bigger in size than those enacted by the UN category of least developed countries (LDCs). Put in perspective, the average income per capita of developed countries is “only” 30 times that of the LDCs.

Lacking sufficient domestic resources to support their economies to pay for health costs and to stimulate their economies developing countries need to look for outside resources. This proved difficult for many developing countries for several reasons.

First, after a period of falling external debt levels supported by the Highly Indebted Poor Country (HIPC) initiative during the 2000s, external debt burdens of

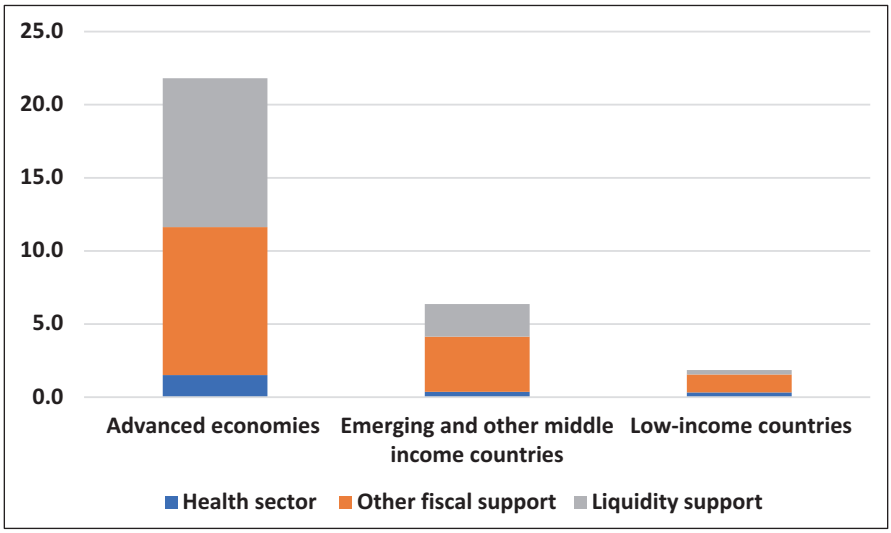

Fig. 2.6 Fiscal and monetary support in response to COVID-19 per January 2021 (% of GDP) *Source*: IMF (2021b), Fiscal Monitor, Database of Country Fiscal Measures in Response to the COVID-19 Pandemic

many low-income developing countries surged again during the 2010s. In 2019, the IMF assessed that half the low-income countries faced high risk of or already were in debt distress; more than double the 2013 share. The average external debt ratio of low-income countries had already increased to 65% of GDP in 2019, up from 47% in 2010. Increased borrowing from private lenders significantly added to the public debt burden in many countries, with the share of private non-guaranteed debt in total external debt stocks of low-income countries increasing from 3.2% in 2010 to 10% in 2019 (Chandraskhar, 2021). During 2020, these high levels of external indebtedness caused substantially more distress with the steep declines in GDP and export earnings owing to the global recession caused by the pandemic.

To alleviate some of the stress, the IMF cancelled US$213.5 million in debt-service obligations for 25 eligible HIPCs during 2020. This debt relief, while welcome, proved far from sufficient, however, to avoid increased debt distress. Likewise, the G20's debt service suspension initiative (DSSI) thus far has provided little debt relief and, in essence, only helped kick the can down the road, as no debt was cancelled, with interest continuing to accrue during the all-too-brief suspension period (Chowdury & Jomo, 2021).

Second, during 2020, developing countries also faced an outflow of capital to developed countries and were hit by the appreciation of the dollar (and depreciation of their own currencies). Gallagher et al. (2021) point to the high degree of uncertainty and an initial lack of coordinated policy responses, which intensified market panic and volatility; this led to the largest outflow of portfolio capital from emerging market and developing economies in history and caused a global shortage of dollar

liquidity. At the same time, the external financing needs of most developing countries increased staggeringly, as they saw export earnings collapse with the global demand fallout (and, for many, this was compounded by declines in major commodity prices), while the currency depreciation increased their import bills. As per the above, their financing needs further increased because of the need to combat the health and economic impacts of the pandemic. Despite a general awareness and pledges made by the G20, in practice, the response of IMF and the World Bank was far from commensurate with the magnitude of the crisis (see Afesorgbor et al., 2021). While the IMF indicated it would commit its US$1 trillion lending capacity, as of March 15, 2021, it had provided no more than US$107 billion worth of financial assistance to 85 countries around the world. The World Bank announced a US$160 billion pandemic support program in September 2020. While significant, elements of this program have been criticized for not helping to remove fiscal barriers and lack of attention to accessible healthcare. Only 8 of the 71 COVID-19 health projects (funded by the World Bank) include measures to support low-income people that now face financial barriers to access health services (Oxfam, 2021a).

Third, the additional resources that were made available have come with conditions that in fact made these less effective as a response to the impacts of the pandemic. An analysis of the contents of recent and ongoing IMF agreements by Oxfam (2020) revealed that, between March and September 2020, 76 out of the 91 IMF loans for 81 countries with a total value of US$89 billion had conditionality attached that required recipient governments to slash public expenditure in ways that could result in deep cuts in the funding of public healthcare systems and pension schemes, while requiring economy-wide wage freezes and reducing public sector employment. Nearly one-third of the countries with IMF loans also face surcharges on unpaid interest (amounting to more than US$4 billion) even in the midst of the pandemic, substantially increasing debt-servicing cost (INET, 2021: 10).

In short, the current IFFS proved inadequate as a financial safety net for countries put in extraordinary need because of a pandemic. As a result, it only exacerbated global inequalities given that countries with ample fiscal and monetary resources were able to take unprecedented fiscal and financial support measures to protect the livelihoods of their own populations but without much consideration of dealing with the international repercussions on the livelihoods of the populations in less affluent nations. This apparent lack of international solidarity during the pandemic is further reflected in a projected decline of almost 40% in bilateral official development assistance during 2020 (Development Initiatives, 2021).[4]

[4] According to a February 2021 briefing by Development Initiatives (2021), bilateral donors have decreased aid commitments by 36% between 2019 and 2020 (over the same January to November period). Of the thirteen bilateral donors considered in this analysis (covering 97% of 2020 bilateral commitments by value), seven have seen total ODA commitments fall, with four seeing falls by 40% or more.

2.4 Changes Needed to Address the Weaknesses of the Current International Financial and Fiscal System (IFFS)

The COVID-19 crisis revealed that the current IFFS is unfit to provide adequate emergency and development finance to countries and populations most in need, thereby exacerbating global inequality and impeding the attainment of the Sustainable Development Goals by 2030 (see also Mukhtarov et al., 2021). Reform of the IFFS is thus an imperative of the first order. The global nature of the pandemic might give impetus to such reform, but the political obstacles remain vast. Without attempting to be comprehensive, we focus on four key reform proposals: (i) a much stronger international tax coordination, including harmonizing higher corporate tax rates (especially on profits of globally operating firms) and the reduction of Base Erosion and Profit Shifting (BEPS) in developing countries; (ii) sovereign debt restructuring and relief; (iii) reform of policy conditionality attached to lending by the international financial institutions (IFIs); and (iv) an increase in international liquidity by issuing additional Special Drawing Rights (SDRs), including for leveraging additional developmental finance.

2.4.1 International Tax Reform

Lower taxes and various forms of tax avoidance have left governments with less resources to face important priorities in the wake of the COVID-19 pandemic. Tax avoidance diverts 40% of foreign profits to tax havens. This "profit shifting" causes estimated government revenue losses between US$500 billion and US$600 billion per year (FACTI, 2021). Tax evasion by wealthy individuals and illicit financial transactions add to the substantial amounts of forgone government revenue.[5] Illicit flows are expected to have increased during the pandemic.

The Independent Commission for the Reform of International Taxation (ICRIT) has proposed the following changes in the international tax system: a higher corporate tax rate to large corporations in oligopolistic markets allowing them to earn excess rates of return; a minimum effective corporate tax rate of 25% worldwide to stop base erosion and profit shifting; progressive digital services taxes on the economic rents captured by multinational firms; country-by-country reporting for all corporations benefitting from state support; publication of data on offshore

[5] The High-Level Panel for Financial Accountability, Transparency, and Integrity (FACTI) estimates that about US$7 trillion in private asset holdings is kept hidden from tax collectors in tax-haven countries; 10% of world GDP may be held in offshore financial assets, while an additional US$20 billion to US$40 billion is estimated to be paid in the form of bribes on investment deals. Furthermore, revealed money-laundering transaction by criminals are estimated to represent 2.7% of global GDP. Estimates drawn from the FACTI interim report (FACTI Panel, 2021).

wealth to enable all jurisdictions to adopt effective progressive wealth taxes on their residents and to better monitor effective income tax rates on highest income taxpayers (ICRIT, 2020). These measures would greatly increase the fiscal space in low and in middle income countries.

2.4.2 Sovereign Debt Restructuring and Relief

Twenty years after the start of the HIPC initiative for debt relief and restructuring, many countries are still in a precarious debt position, as analysed in Sect. 2.3. The Commission on Global Economic Transformation (led by Nobel Prize-winning economists Joseph Stiglitz and Michael Spence) observed that while attention to poor countries' needs for debt relief and restructuring regained some traction in 2020 when the pandemic broke out, this soon fizzled out: 'in the beginning of the pandemic there was an agreement among the G-20 for a moratorium on servicing of the debt for the poorest countries for their official (bilateral) debt, called the Debt Service Suspension Initiative (DSSI), as mentioned earlier. The hope was that others would join, the private sector in particular. But they did not. The lack of comprehensive participation has a devastating effect: those who might be willing to join are hesitant to do so, as they see the net beneficiary not being the poor people in the poor country, but the recalcitrant creditors' (INET, 2021: 11).

The international community should create better conditions for sovereign debt restructuring. The dire situation caused by the COVID-19 pandemic gives all the reasons to accept the principle of force majeure: countries should not be forced to pay back what they cannot afford. In this sense, Gallagher et al. (2021) propose the creation of an appropriate Sovereign Debt Restructuring Regime, building on earlier proposals made in the aftermath of the global financial crisis (see e.g., Herman et al., 2010). Although existing mechanisms to renegotiate sovereign debts with private creditors have improved, they are still far from adequate because of the multiplicity of debt contracts, some of which are not subject to collective action clauses. A global institutional mechanism to renegotiate sovereign debts should therefore be put in place as soon as possible. Many developing countries were already close to external debt insolvency due, in part, to the recent surge in private external borrowing, as noted above. The massive capital flight and exchange rate depreciation that took place during 2020 has compounded the developing-country debt distress, increasing the likelihood of default, and making the need for orderly sovereign debt workouts the more urgent, not only to bailout debt-distressed countries, but also to safeguard global financial stability.

2.4.3 *Reform of Policy Conditionality Attached to Lending by IFIs*

In Sect. 2.3, we noted the stark disparities across countries at different levels of development in fiscal support in response to the COVID-19 crisis. The IMF plays a large role in the macroeconomic policies undertaken by borrowing developing countries, especially those that are facing balance-of-payments problems and turn to it for advice and support. The Commission on Global Transformation notes with satisfaction that the IMF leadership has actively supported the large multi-year fiscal stimulus for COVID-19 recovery enacted by the United States and most European countries. The IMF has further recognized the need for enhanced public spending by developing-country governments, also those facing debt distress. Unfortunately, as also noted in Sect. 2.3, in practice, the IMF has continued to provide pro-cyclical policy advice to borrowing nations, as reflected in the policy conditionality attached to its loans, asking for fiscal restraint rather than deficit spending when economies are in recession. Between October 2020 and March 2021, the IMF approved an additional US$18.6 billion in new loans to 16 countries, raising the total amount of lending approved during the pandemic to US$107 billion. Nearly all (93%) of the additional funding was allocated to alleviate fiscal stress in Latin America and the Caribbean and only a paltry 3% went to Sub-Saharan Africa, 2% to countries in Asia and the Pacific, and 2% to countries in North Africa, the Middle East and Central Asia. Out of the 18 new loans, 17 loans called for fiscal austerity by recipient countries (Oxfam, 2021b). The Oxfam report further observes that the IMF has introduced flexibility clauses in some non-emergency loans, allowing countries to increase social spending in case the pandemic worsens. Agreements further stress the importance of protecting social spending, also where fiscal consolidation is required. However, the language in the Letters of Agreement is often vague regarding this flexibility, while explicit and precise regarding targets for fiscal consolidation and spending cuts. For instance, where the IMF encourages governments to protect social spending, it also advises governments in the same documents to roll back pandemic-related social spending as soon as "the crisis abates". This is worrying considering that most countries were extremely unprepared to face the crisis with severely insufficient social spending. The emphasis on the need for fiscal restraint by governments receiving financial support from the IMF further points at the inadequacy of the contingency financing to provide the fiscal space needed to mitigate the worst impacts of the pandemic on livelihoods. In this sense, the practice of IMF's policy conditionality still looks very much alike it was before the pandemic, as analyzed by Gallagher and Carlin (2020) upon reviewing a pre-pandemic set of IMF loans.

The specifics of each IMF program should therefore be much better scrutinized before being presented to the board of Directors; any policy conditionality attached to lending policies by IFIs should more consistently be based on principles of supporting a countercyclical macroeconomic policy stance by recipient countries. In addition, short-term lending to face off balance-of-payments should be aligned with

adequate long-term development finance in support of achievement of the Sustainable Development Goals.

2.4.4 An Increase in Special Drawing Rights (SDRs) with Special Usage for Developing Countries

At the time of writing, the IMF was expected to approve the issuance of US$650 billion in new Special Drawing Rights (SDRs), and effectively did so in June 2021. The advantage of creating international liquidity in this way is that it is essentially costless. Earlier fears that this could be inflationary are not relevant in the current global economic conditions, especially as it is dwarfed by the monetary expansion in rich countries. This increase provides developing countries immediately with an increase in their reserves and enable them to engage in much-needed public expenditure with less concern for the effects on the external balance; it could also provide some means of repayment for countries with pressing external debt problems. This impact of the new SDR creation is not automatic, however, since SDR allocations are currently made in line with IMF quota (which in turn are linked to voting rights). Most of the new SDRs therefore will be made available to richer countries who are less in need of balance of payments finance and hence much of the new SDRs could remain unused reserves within the IMF. Any unused SDR reserves could be made available to developing countries in several ways (INET, 2021: 9; United Nations, 2021). First, it could be decided to use a part for writing off or reducing the external public debts of poor countries. Second, SDRs could be given or lent to specific countries with high balance-of-payments stress. Third, as has been proposed in the past (see, e.g., Haan, 1971; United Nations, 2012; Ocampo, 2015; Vos, 2017), a portion of unused SDRs not needed as a reasonable reserve buffer could be leveraged for development finance (through issuance of international bonds backed by those unused SDRs).

2.5 Conclusions

The COVID-19 pandemic and its social and economic outfall has led to a steep decline in economic activity, as other pandemics did (van Bergeijk, 2021). But people and countries have not been equally affected. In high-income countries in Europe and North America, the pandemic has increased inequality, as highly trained workers and capital owners were much less affected that other groups. Developing countries, and especially the vulnerable segments of their populations, were disproportionally hit, resulting in more poverty, greater food insecurity and worsening nutrition. As developed countries had greater fiscal space, they could inject ample resources into necessary health measures, expansion of social safety nets and

economic stimulus, something which most developing countries were not able to do. Thus far, the multilateral system failed to come to their financial rescue, owing to waning of multilateralism itself (van der Hoeven, 2020) and, importantly, because of fundamental shortcomings in the IFFS to serve as an international financial and social safety net in a global crisis. Proposals to reform the existing IFFS prop up with each crisis, but, as this chapter has made clear, if the key changes described in Sect. 2.4 would have been in place from the beginning of the pandemic, its global economic repercussions could have been less severe and much of the increase in global poverty could have been prevented. This is to say, they are now more needed than ever.

Changes in the IFFS are not acts of charity, but necessary to return to sustainable and equitable global growth, without which gains for some countries and country groupings that now propagate a 'me first' attitude in health issues and a return to protectionism will not be sustainable in the long-term leading to lower global growth and to a reversal in the upward trend in achieving the Sustainable Development Goals by 2030.

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