Reply to the Comments

Arjun Sengupta

I must say I was quite surprised to listen to Gerry Helleiner's comments on my paper. Admittedly, my paper was rather long, dealing with many issues, some of which were highly controversial and on some my views were quite provocative. Still Gerry could not have glossed over the main point I was trying to make in the paper if he had read it carefully. I am sure that his views have evolved much beyond the rhetorics of the sixties, in which all of us had indulged, at some time or other. He must have also recognised that there is now a much broader consensus about the basic tenets of economic policy whether in the developing or in the developed countries. We now rarely talk about our "own" programmes of policy as against those "imposed" by more powerful countries or by the Fund and the Bank. We argue about the right or wrong policies or appropriate 'conditionality'. We enter into policy dialogues and negotiations and we may have to compromise by accepting not the most preferred option. But we do that out of our own volition and judgement and not because we have to accept punishment from the donor or their "bullying and abuse".

Similarly, when we talk of a preference for deregulation, it is not rooted in any ideology - it is simply a product of experience. I had mentioned in my paper that governments have realised that the regulation of prices, investment, trade and exchange or restrictions on the movements of goods and services, and of factors of production, usually result in a substantial loss in welfare. I also mentioned there is a rethinking about the role of the state in economic activities, about central planning, policy coordination and the state's ability to influence the evolution of the economy. Gerry is clearly uncomfortable with such statements. He talks about "sophisticated and functional deregulation," a "moderate and nuanced approach," "the efficacy of selective and targeted instruments."

Gerry is a respected development economist and he cannot be unaware that we have had quite a long experience of practising "selective", "targeted", "functional" regulation and control guided by the theories of market failure and the governments commanding more information than the private entrepeneurs, and in the process landed ourselves in the current mess.

Gerry's comments on performance and policy commitment also betray an attitude of distrust that the aid-givers and the Fund-Bank are somehow interested in imposing on developing countries wrong policies. If we can

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perform without following the policies prescribed and solve our problems, then either it is a fluke and a result of exogenous factors, which should be no comfort as the problems will recur again, or the policies prescribed are wrong. Normally, it does not happen this way. The policies prescribed are adopted by the developing countries after a good deal of deliberation only after being convinced of their usefulness. Still quite often they cannot perform, because given the state of our knowledge a right policy can be only directionally right in terms of the first derivations of the function, i.e., can be said only as leading to the achievement of the target. A policy X can lead to the objective Y. It can rarely be said that a given amount of X will result in a definite amount of Y. It is a matter of empirical specification of the functional form and very few policy prescriptions in the developing countries are based on any strict empirical estimation of the relationships. That is why I am saying that there should be no insistence on performance in a set of policy conditions attached to the programme, but only a check on policy commitments. The problem then would be to find some proper indicators of policy commitments, and these are not very difficult to find through reviews and monitoring as the Fund has tried in many instances. In any case, it would introduce a significant flexibility in the conditionalities, which I am sure Gerry would welcome.

This brings me to the main point that I tried to make in my paper. I am not opposed to the traditional form of aid for poverty alleviation, human development and the building of infrastructure. But I feel that the case for even that form of aid will be stronger if it can be linked to improving the political and economic feasibility of implementing the programmes of reform that most developing countries have adopted in the recent period. The industrial countries must accept the reciprocal obligation of helping these countries through aid and balance of payments finance as well as improved market access and flows of investment and technology. The case for such reciprocal obligation has to be argued and campaigned for, and although it is rational in terms of increasing global welfare, one cannot hope that it will be accepted easily by all countries.

Mr. Fugmann of course does not misunderstand the main point of my programme. He brings in the old argument that the developing countries need more adjustment and reform and less finances. I do not mind that because it is an empirical point and it is possible to estimate how much finance a developing country would need to carry through an adjustment programme over a number of years. If Mr. Fugmann and his colleagues from the industrial countries accept that they have an obligation to make available the finances required for adjustment, I have got what I wanted and would focus henceforth on designing the appropriate adjustment programmes. But he does not quite commit himself to accepting such obligations and claims

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that he does not believe that "any international monetary system should have as an integral part development assistance and aid." It probably does not, if an international monetary system is concerned only with the adequacy of international liquidity. But if it is concerned with an orderly growth of world trade, output and employment with price stability, it has to deal with the problems of the developing countries. Those problems, even in the short-run and even when they are limited only to the balance of payments, cannot be abstracted from the provision of finance necessarily linked with their needs of development.

Finally, a few words about my exercise on resources. It has to be looked at in the context of the 0.7 per cent targetry of official development assistance. My proposal of calibrated obligation of different donors is no more unrealistic than the uniform target of 0.7 per cent for all ODA countries. Suppose we are able to estimate X as the per capita income of the ODA countries which can be regarded as sufficient to meet all the basic needs of food, shelter, clothing, health and education. It is quite legitimate to assume that if the per capita income of such an ODA country exceeds X, its marginal contribution to that country's human development, well-being or utility declines. I have used a formulation from Atkinson, as adopted in the Human Development Report 1992, to estimate for each ODA country the amounts by which their nominal income should be adjusted to reflect its contribution to human development or utility. It appears that for most countries the adjustment would exceed 60 per cent. Obviously, this feature would depend upon the form of utility function that has been assumed. It can be much less than that or more, but it does not matter very much for my exercise. Suppose it is only 10 per cent, which with a $17 trillion combined nominal income of the ODA countries would yield $1,700 billion of income with negligible utility. If only 10 per cent of that is transferred as aid to developing countries, and 90 per cent is used for social expenditure in the industrial countries themselves, the aid amount can go upto $170 billion. I am only advocating a tiny fraction of the nominal incomes of the industrial countries to be transferred as aid to the developing countries since that would make a negligible difference in the ODA countries' well-being or utility, leaving enough scope for fulfilling the requirements of the poor of the industrial countries themselves. Accordingly, I have calculated the separate obligations for aid of the different ODA countries, as distinct from the uniform 0.7 per cent target for all of them.

Now it is of course possible that the ODA countries would reject this exercise by suggesting that their welfare functions are such that the marginal contribution to welfare of per capita income does not diminish at all except at a very high level so that there is very little difference between their nominal income and its contribution to welfare. In other words, they would have very

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little to spare for the developing countries without substantially hurting themselves. Maybe it is true, since nobody knows the actual form of their welfare functions. However, I doubt that very much. Looking at the numbers we are talking about, it should be quite possible for the ODA countries to substantially increase their aid without sacrificing much of their welfare.

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