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Divisions remain in WTO as MC12 nears

Member states of the WTO need to iron out their differences if the trade body's 12th Ministerial Conference (MC12) in November is to yield agreement on several key issues. Major sticking points include such developing-country priorities as a COVID-19-related intellectual property waiver, greater leeway to hold public food stocks, and special and differential treatment under the WTO rules.

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South demands outcomes on TRIPS waiver, PSH and SDT at MC12

Deep differences among the membership are threatening to scupper chances of striking agreement in several crucial areas at the WTO's upcoming 12th Ministerial Conference.

by D. Ravi Kanth

GENEVA: Many developing countries on 30 September demanded outcomes on their core issues – including a temporary TRIPS waiver, a permanent solution on public stockholding programmes for food security (PSH), a balanced agreement on fisheries subsidies, and improvements in special and differential treatment (SDT) provisions – at the WTO's 12th Ministerial Conference (MC12) scheduled to begin in Geneva on 30 November.

At an informal Doha Trade Negotiations Committee (TNC) meeting held in hybrid (in-person and virtual) format on 30 September, sharp divisions surfaced between a large majority of developing countries on the one side, and the industrialized countries and some developing countries on the other, on all the issues that have been prioritized as "deliverables" for MC12, said people who asked not to be quoted.

With not many working days left before MC12, there is dim light at the end of the tunnel on all the deliverables.

DG's emotional pitch

In her introductory statement at the TNC meeting, WTO Director-General Ngozi Okonjo-Iweala made some rather emotional comments alleging that some WTO members did not want an outcome at MC12, said people familiar with her statement.

However, she did not name these countries, they said, suggesting that her statement seemed more like an attempt at a blame game.

Okonjo-Iweala said the fisheries subsidies negotiations had been going on for 20 years without any convergence yet, said people who preferred anonymity.

She also suggested that without any outcomes at MC12, members could opt for other avenues of trade liberalization, they said.

For the first time, the DG apparently indicated that an intellectual property package had to be part of the WTO's response to the COVID-19 pandemic, according to people present at the meeting.

Surprisingly, the rather sombre assessment in her introductory remarks of the state of play in the negotiations gave way to a more sanguine statement in her concluding remarks at the end of the day-long meeting, where she said she was "encouraged" by the statements made by members, despite continued divisions on all the major deliverables being targeted for MC12.

Interestingly, a news agency report claiming that Okonjo-Iweala was planning to resign because of her frustration with the inertia and lack of progress in the negotiations appeared to be false as it seemed more like "planted" news to create a scare that things were falling apart at the WTO amidst sharp divisions among the members, said people who spoke to the *South-North Development Monitor* (*SUNS*).

Reports presented at the TNC meeting by the chairs of the Doha negotiating bodies dealing with fisheries subsidies, agriculture and SDT seemed pretty bleak.

The chair of the fisheries subsidies negotiations, Ambassador Santiago Wills from Colombia, said some proposals could take the negotiations backwards by years, without specifying which proposals.

The statement raised eyebrows and caused some concern as to whether it was proper for him to target some proposals, said a participant who asked not to be quoted.

India contested the statement, saying that instead of being neutral, the chair was taking partisan positions by characterizing certain proposals as inimical to the negotiations, said a person who asked not to be quoted.

The chair of the agriculture talks said there had been little progress on the issues in her draft text released before the summer break.

The chair of the Committee on Trade and Development issued a rather bleak report about progress on the 10 agreement-specific proposals tabled by the Group of 90 developing countries to strengthen SDT.

Key members remain divided

More than 40 members took to the floor at the TNC meeting, reiterating their divergent positions.

The United States remained silent without making any statement, according to people who asked not to be quoted.

Perhaps the US Trade Representative Katherine Tai may have conveyed to Okonjo-Iweala Washington's expectations for MC12 during their bilateral meeting earlier in September.

A majority of developing countries which spoke at the TNC flagged the proposed TRIPS waiver as their core demand to be concluded at MC12.

Speaking on behalf of the African Group of countries, Mauritius' Ambassador Usha Canabady noted that it had been almost one year since India and South Africa introduced the proposal for a waiver from certain provisions of the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) relating to copyrights, industrial designs, patents and protection of undisclosed information in order to aid the prevention, containment and treatment of COVID-19. She expressed grave concern that WTO members "continue to discuss as people are dying", with Africa suffering from a dismal COVID-19 vaccination rate of 5% and remaining "very fertile ground for the incubation of new variants."

Canabady warned that "any protracted and inconclusive debate will only worsen the situation rather than address the shortage and inequitable distribution of vaccines."

"If the WTO were to show the world that it is effectively contributing to address the pandemic, conclusion of the TRIPS waiver discussions at the earliest would be central," she emphasized. "The TRIPS waiver is integral to any successful outcome at MC12."

India, South Africa and the other co-sponsors of the waiver proposal made it clear that a decision on the waiver was a sine qua non at MC12.

South African Ambassador Xolelwa Mlumbi-Peter stressed that the only way to address the growing vaccine inequality and stop the pandemic was to "ramp up and diversify production", cautioning that the delays in removing barriers to the expansion and diversification of production had a human cost.

Mlumbi-Peter said the WTO membership had a unique opportunity to demonstrate solidarity and reaffirm the relevance of the multilateral trading system in addressing common challenges.

South Africa, she said, believed it was possible to find an outcome that would include both the TRIPS waiver and the European Union's compulsory licensing proposal.

She said the ongoing process chaired by New Zealand Ambassador David Walker to formulate the WTO's response to the pandemic would be "incomplete" without addressing intellectual property barriers.

She underscored the need for aligning this process and the TRIPS Council process "if the WTO is to deliver an outcome. The TRIPS waiver is integral to a successful outcome at MC12."

India also issued a strong message that the TRIPS waiver must be agreed to at MC12.

China's Ambassador Li Chenggang said that "on the response to the pandemic, we support to have political commitments on WTO to COVID-19 and achieve specific decisions in certain areas including TRIPS waiver, at least on vaccines."

Speaking on behalf of the African, Caribbean and Pacific (ACP) Group, Jamaica said "we have consistently supported the general objectives of the TRIPS waiver proposal."

"A TRIPS waiver arrangement that accommodates the interests and addresses the concerns of the membership should be a priority for an MC12 outcome," Jamaica said.

It said the waiver "is an important element of the WTO's response to the impact of the pandemic."

It added that "an appropriate waiver arrangement would certainly improve our capacity to address future pandemics and unforeseen crises appropriately and help to limit all types of casualties we are enduring due to various bottlenecks that limit access to the vaccines."

Around 10 countries largely from the Ottawa Group, led by the EU, Canada and several other countries, called for a robust outcome on the WTO's response to the pandemic to address export restrictions, trade facilitation and market access proposals.

Fisheries subsidies

As regards fisheries subsidies, the divide among members has grown further amidst attempts to ignore recent proposals submitted by the ACP and African Groups, India and China among others.

The proposals put forward by the ACP and African Groups, and India, appear aimed at rectifying the imbalances and asymmetries in the revised draft text issued on 30 June by the chair of the fisheries subsidies negotiations, said people who asked not to be quoted.

Speaking on behalf of the African Group at the TNC, Mauritius said the Group remained "concerned about the effectiveness of Article 5.1.1 [of the chair's draft] which we feel will maintain the status quo for most major subsidizers." That provision is seen as providing a carve-out to the big subsidizers.

It said the chair's current formulation on Article 5.1.1 "does not meet the sustainability test and we have stated the changes in this regard."

It pointed out that the African and ACP Groups have also proposed amendments to the SDT provision in the chair's draft, saying that "our proposal provides a good basis for further discussion in crafting appropriate and effective SDT as required in the negotiating mandate."

South Africa expressed concern over the imbalances in the chair's draft text, particularly with regard to the biggest threat to marine sustainability coming from large-scale and industrial fishing.

Jamaica, speaking on behalf of the ACP Group, said "it is important that we target major subsidizers and large-scale industrial fishing, as well as prevent loopholes to be exploited by those targeted."

It said the ACP and African Groups'

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proposal "encompasses Ministers' call for SDT in the form of policy space to facilitate the responsible development of the fisheries sectors in developing countries and LDCs [least-developed countries]."

Jamaica said that it looked forward to the chair's circulation of "a revised and balanced text that reflects the elements of our proposal."

While many industrialized and several South American countries remain satisfied with the chair's draft text, China said that it "supports a fair and balanced outcome for the final disciplines."

Agriculture

On agriculture, many developing countries, particularly India, called for a permanent solution on PSH.

India said PSH was its top priority at MC12, adding that it supported the G33 as well as the African Group proposals on the permanent solution.

South Africa said that disciplines on trade-distorting domestic support required reform; the longstanding injustices in the area of cotton remained a concern; a permanent solution on PSH was a necessity; and progress in the discussions on a special safeguard mechanism (SSM) was key.

The African Group as well as several other developing countries called for safeguarding Article 6.2 of the WTO's Agreement on Agriculture dealing with the "development box" that exempts developing countries from any commitments on irrigation and fertilizer support. The African Group said low-income and resource-poor producers should continue to be protected by Article 6.2.

The Cairns Group of farm exporting countries led by Australia called for a framework agreement on trade-distorting domestic support with a 50% downpayment by 2030.

Several South American countries pressed for market access negotiations.

Many countries, including China, South Africa and India, called for restoring the WTO's two-tier dispute settlement mechanism.

China said "restoring the Appellate Body and bringing the dispute settlement system back to normal operation is clearly the topmost priority for most members."

In relation to WTO reform, South Africa said that such reform "must be inclusive, taking into account the interests of all, particularly the interests of the poorest economies, developing countries and LDCs for sustainability and legitimacy."

South Africa argued that "it must therefore be premised on the principles of inclusivity and development with a view to create a fair and equitable MTS [multilateral trading system]".

It also urged members to "reflect on the legal status of JSIs [Joint Statement Initiatives] and their negotiated outcomes", saying that this was an important issue in the context of a rules-based system. *(SUNS9430)*

Uncertain outlook for WTO decision on public food stockholding

Despite recognition of the importance of public food stocks for promoting food security, prospects of securing a greenlight at the WTO for developing countries to maintain such stocks remain up in the air.

by D. Ravi Kanth

GENEVA: The fate of the permanent solution on public stockholding programmes for food security (PSH), demanded by a large majority of developing countries, hangs in the balance at the WTO's forthcoming 12th Ministerial Conference (MC12).

The United States, the European Union and members of the Cairns Group of farm exporting countries seem determined to block the mandated permanent solution, according to people familiar with the development.

The US Trade Representative Katherine Tai, during her meeting with WTO Director-General Ngozi Okonjo-Iweala on 22 September, apparently indicated Washington's three priorities for MC12, and agriculture did not figure at all, according to a 23 September report in the *Washington Trade Daily*.

Instead, the US' three major priorities at MC12 are a "meaningful" outcome on fisheries subsidies; the WTO's response to the COVID-19 pandemic; and reforms involving the negotiating function of the WTO that seek differentiation among developing countries on the use of special and differential treatment.

It is against this backdrop that a large majority of developing countries could face the prospect of one of their core issues, PSH, being eclipsed once and for all, said an analyst who asked not to be quoted.

FAO's assessment on PSH

Ironically, the countries that are opposed to the permanent solution on public stockholding programmes for food security had actually used these in the past before they became popular in the developing countries.

On 23 September, during a regular meeting of the WTO's Committee on

Agriculture, the Rome-based UN Food and Agriculture Organization (FAO) made a detailed presentation on public stockholding programmes and how they have historically been used by the EU and several other developed countries, according to people familiar with the development.

At the meeting, a senior FAO official said governments in Asia and the Pacific, Europe, Latin America and the Caribbean, and North America made public provision of food stocks a common feature of agricultural policy throughout history, people said.

For governments in both North and South, promoting food security, managing price risks and supporting rural incomes have been major priorities, particularly since the 2008 food crisis, the FAO official said.

In the recent past, PSH programmes suffered a big blow due to structural adjustment measures (imposed by the International Monetary Fund) and market liberalization in the 1980s and 1990s, according to the official.

With the COVID-19 pandemic having caused unprecedented disruption globally, the expansion of food procurement and distribution operations has assumed more importance than ever. The market uncertainty has forced governments to adopt PSH policies to address the food needs of their resource-poor and low-income people.

Explaining the ways in which PSH programmes can help governments in the Global South, the FAO official provided an account of the different policy instruments underpinning these programmes. Emergency stocks would reduce the vulnerability of consumers to supply or food price shocks caused by emergencies. Buffer stocks aim to stabilize prices over the regular agricultural production cycle to reduce the vulnerabilities of consumers to price shocks, and of producers to income variability. Finally, stocks for domestic food distribution/food aid seek to promote physical and economic access to adequate quantities of food for certain target populations.

According to the FAO official, the three basic elements of PSH programmes include procurement, management and release of stocks. Based on these three elements, governments take recourse to domestic agriculture support and trade policy measures.

Several measures are invariably used for achieving these objectives and they include: market price support linked to procurement of stocks; import barriers to maintain minimum procurement prices; consumer support/social safety net measures for the release of stocks at subsidized prices; export restrictions to maintain low prices for consumers; and export subsidies for the release of stocks on the world market.

The FAO official suggested that PSH policies can play an important role for both poor farmers and consumers, with guaranteed outlets preventing distress at low prices in places where infrastructure and risk management instruments are lacking.

Countries in Asia and the Pacific like China, India, Indonesia, Pakistan and the Philippines seem to have opted for procurement from domestic farmers at administered prices. While China releases stocks through auctions when market prices or demand is high, India, Indonesia and the Philippines operate food distribution programmes aimed at specific target populations (in India, it is referred to as the public distribution system, where targeted populations are offered food grains at below market prices).

Since the 2007-08 food crisis, countries like Brazil revitalized the national food supply agency to manage food stocks for both emergency purposes and price stabilization.

The FAO official said that procurement at government-set prices or administered prices can be linked to any type of public stocks in maize, rice and wheat. Over the past 10 years, the administered prices in national currencies have been rising while international prices have tended downward. Several countries have also witnessed the rising trend in administered prices being somewhat reversed because of conversion to US dollars and due to significant currency depreciation. Also, the administered prices can experience a downward trend if they are adjusted for inflation.

Seeking a permanent solution

It is well established that the methodology adopted in the calculation of market price support based on 1986-88 reference prices, and the *de minimis* threshold (of 10% of the value of production) for calculating countries' domestic support under WTO rules need fundamental change.

In the run-up to the WTO's 10th Ministerial Conference in Nairobi in 2015, the G33 group of more than 40 developing and least-developed countries proposed a permanent solution based on three options: (1) adding a new paragraph to include market price support for food security in the so-called Green Box category of subsidies under the Agreement on Agriculture that are exempted from any subsidy reduction commitments; (2) modifying the existing rules to ensure that the acquisition of food stocks by developing countries to support low-income and resource-poor farmers is not required to be included in the calculation of the Aggregate Measurement of Support (AMS, or trade-distorting farm subsidies); and (3) modifying or amending the rules that calculate subsidies based on the external reference period of 1986-88 prices, which was decided during the previous Uruguay Round of negotiations.

The G33 proposal was fiercely opposed by the US in Nairobi, following which the issue was deferred to the 11th Ministerial Conference in Buenos Aires in 2017. However, a modest proposal for the permanent solution as submitted by India at MC11 was blocked by the US, which also blocked any outcome on agriculture at the Buenos Aires meeting.

Subsequently, undeterred by opposition from the US, the EU, Australia and some South American countries, the G33 circulated its proposal on 15 September to drive home the message that the permanent solution is crucial for a successful MC12. According to the G33, the central elements of the permanent solution must include:

"1. Members agree to put in place a permanent solution as set out below, for the use of public stockholding for food security purposes by developing country Members and LDCs [least-developed countries].

"2. Provided that the conditions set out in paragraphs 3 to 4 are met, Members shall not challenge through the WTO Dispute Settlement Mechanism, compliance of a developing Member with its obligations under Articles 6.3 and 7.2(b) of the Agreement on Agriculture (AoA) in relation to support provided for foodstuffs in pursuance of public stockholding programmes for food security purposes, that are consistent with

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the criteria of paragraph 3, footnote 5, and footnotes 5 and 6 of Annex 2 of the AoA.

"3. A developing Member benefiting from this Decision must have notified the Committee on Agriculture that it is exceeding or is at risk of exceeding either or both of its Aggregate Measurement of Support (AMS) limits (the Member's Bound Total AMS or the *de minimis* level) as result of its programmes mentioned above in respect of the concerned foodstuff for which the Member is seeking benefit of paragraph 2 of this Decision.

"4. For the programmes referred to in paragraph 3, the Member shall notify to the Committee on Agriculture in the format specified under the Annex to this Decision.

"5. A developing Member shall endeavour not to export from the procured stocks covered under paragraph 1 of this Annex unless requested by an importing Member.

"6. Paragraph 5 shall not apply to exports for the purposes of international food aid, or for non-commercial humanitarian purposes."

With only weeks to go before MC12, the developing countries have one last opportunity to wage a battle to secure the permanent solution on PSH. *(SUNS9427)*

US calls for post-MC12 action plan while Doha issues are marginalized

The US has proposed a "disaster preparedness and resiliency" plan for the WTO that envisages greater trade liberalization and could end up sidelining issues of interest to developing-country members.

GENEVA: The United States has circulated a concept paper on "WTO response to the pandemic: disaster preparedness and resiliency action plan" that appears to put forward trade liberalization, including market access in goods and services, and work on trade facilitation, investment, transparency and regulatory issues as the way forward to address the COVID-19 pandemic.

The three-page restricted document circulated on 20 September is presented as a contribution to the "Walker process" of crafting the WTO's response to the pandemic.

Ambassador David Walker from New Zealand was appointed in June as the facilitator to oversee the "horizontal and multilateral process" for finalizing the trade body's response to the pandemic.

The US proposes a post-MC12 (the WTO's 12th Ministerial Conference beginning in Geneva on 30 November) action plan with key pillars that include "issues related to Trade in Goods (Market Access, Trade Facilitation, Technical Barriers to Trade, and Regulatory Cooperation); Services and Investment; Transparency including the Trade Policy Review Body; and WTO engagement with relevant international organizations and the private sector".

The US also proposes that the WTO General Council "establish a Disaster Preparedness and Resiliency Action Plan Coordinating Body, chaired by an ambassador designated by the Chair of the General Council to oversee implementation of the plan".

The paper suggests that WTO member states issue a ministerial decision to this effect at MC12.

During an informal meeting convened by Walker on 1 September, attempts to include the issues of "export restrictions, trade facilitation, regulatory coherence, cooperation and tariffs" as part of the WTO's response to the pandemic were opposed by some developing countries.

India was reported to have called on members of the Ottawa Group of countries to stop pushing the narrative for the so-called trade-facilitating measures, including a ban on export restrictions. It said in that meeting that WTO members need policy space during the pandemic to respond effectively to the evolving situation.

South Africa was also reported to have voiced its concern about including extraneous issues in the WTO's response to the pandemic, suggesting that the core issues concerning intellectual property rights must be addressed without delay.

The action plan proposed by the US could in effect morph into a post-MC12 work programme with a dedicated body primarily focused on market access, transparency, regulatory disciplines, services liberalization and work on investment, an analyst said.

The US proposes work on investment under the WTO when WTO members had decided by consensus in 2004 that no work on investment would be undertaken during the Doha Round.

Despite this, a "Joint Statement Initiative" of plurilateral talks on "investment facilitation" has been underway since MC11 although its legality under WTO rules is seriously disputed by several WTO members.

At a time when the Doha work programme remains in limbo and uncertain, the US-proposed action plan, if included in a consensual multilateral ministerial decision, could form a new work programme, with no meaningful deliverables for issues of concern to developing and least-developed countries, including agriculture and strengthening of special and differential treatment.

The paper also does not address the massive challenge of COVID-19 vaccine inequity between the developed and developing countries due to the artificial scarcity created by intellectual property monopolies held by the pharmaceutical industry that continue to cause huge loss of lives and affect economic recovery in developing countries.

While not specifically mentioned in the US paper, in a fact sheet released in conjunction with President Joe Biden's Global COVID-19 Summit: Ending the Pandemic and Building Back Better, a virtual summit held on 22 September on the margins of the UN General Assembly, the US restates its support for a COVID-19 TRIPS waiver for vaccines, stressing that "extraordinary times call for extraordinary measures".

Interestingly, the US paper also calls for more transparency and oversight on the WTO secretariat's activities "as part of its cooperation, coordination, or engagement with other relevant international organizations and as part of the Third Way dialogue".

The "Third Way" dialogue is an initiative of the secretariat to engage international organizations and manufacturers to bridge the vaccine inequality gap. However, thus far, the dialogues have failed to provide a concrete roadmap to expand and diversify manufacturing to promote equitable access to COVID-19 vaccines.

A staged process post-MC12

The US wants members to work towards a "Ministerial Declaration for MC12 on the WTO Response to the Pandemic" that would include all the discussions held from February 2020 to November 2021. Such a declaration, what the US refers to as "a preamble-type of statement", would "frame a forward-looking Decision" on the Disaster Preparedness and Resiliency Action Plan proposed by the US.

The Decision, according to the paper, "would establish a framework for future activity aimed at improving preparedness and resiliency of members to surmount future possible public health or natural disaster events … [and] would establish the political level commitment to initiate a WTO-convened process for action following MC12 to identify issues of relevance to Members and establish modalities".

The US calls for "jump-starting work streams across a wide range of WTO issue areas aimed at examining good practices or possible actions that would contribute to crisis response and disaster preparedness and resiliency".

It says the initial focus on COVID-19 could provide "exchanges of information, options, and lessons learned among WTO members as we continue to move through the different challenges and stages of the current pandemic".

Subsequently, the US wants discussions to focus on "addressing supply chain vulnerabilities, promoting greater vaccine production, improving regulatory cooperation and enhancing regulatory compatibility, creating new transparency, accelerating implementation of the Trade Facilitation Agreement and best practices in implementation, evaluating export restraints, opening-up discussions on services and disaster preparedness and resiliency, and discussing new paths for cooperation, coordination, and engagement with other relevant international organizations and the private sector".

The US claims that "a dedicated focus on 'resilience and preparedness' would provide structure and relevance to the WTO efforts and allow it to examine and discuss those policies that members believe contribute to stronger economic foundations".

It argues that the ministerial decision "would establish the General Council as the primary oversight and convening body".

According to the US, the designated oversight body will oversee several activities, including the "Third Way" dialogue.

The US concept paper showcases a business-as-usual approach based on market access and trade liberalization using the COVID-19 pandemic as the basis.

As next steps, the US will "turn [the] concept and proposed operations into draft ministerial language". *(TWN/SUNS9425)*

World Bank riddled with major flaws beyond its Doing Business Reports

Development campaigners have welcomed the World Bank's scrapping of a controversial series of reports but caution that the publications' deregulatory ethos continues to permeate the Bank's policy agenda.

WASHINGTON: The World Bank has announced that it will discontinue the publication of its flagship Doing Business Reports. The decision came after a series of internal audits and the publication of a damning investigation that revealed serious ethical improprieties, conflict of interest within the Bank's advisory services and data manipulation in the development of the Doing Business rankings.

The termination of the Doing Business Report marks a major victory for over 360 civil society organizations, academics and trade unions from 80 countries which had demanded that the World Bank stop publishing its Doing Business rankings earlier this year, and for all those who had advocated the same since the report's inception.

Since the Doing Business Report's launch in 2003, the World Bank has ranked countries on the "ease of doing business" and guided regulatory changes attractive to private investors with scant regard for the fact that what is good for business is not always good for people and the planet. The Bank has documented more than 3,800 policy changes related to the Doing Business Report, including lowering corporate taxes, reducing contributions to workers' pensions or healthcare and relaxing environmental protection rules.

"The World Bank's decision comes 18 years too late. Much harm has been done in countries cutting back social and environmental standards and deregulating their economies to climb on the rankings. We remain concerned by the Bank's commitment to advance the role of the private sector in development through new assessment methods. If shape and form change but content remains the same, the Bank's ideological prescriptions will lead to equally harmful impacts and deepen inequalities," said Flora Sonkin, Society for International Development (SID), USA.

The discontinuation of the Doing Business Report is testament to the fact that the current global finance, debt and economic architecture is not fit for developing countries' structural transformation needs and global commitments under the 2030 Agenda for Sustainable Development. "Policies informed by approaches and methodologies aimed at benefiting wealthy countries and multinational corporations have been the order of the day at the expense of African economies," added Adrian Chikowore, African Forum and Network on Debt and Development (AFRODAD), Zimbabwe.

> "The data rigging found in the report is merely the tip of the iceberg and the legitimacy crisis of the World Bank Group extends deeper into its biased narratives, ideologies and policy agenda..."

The latest Doing Business scandal reveals deeper institutional flaws that include corruption and political handling of research and analysis. It also raises questions on what other methodological leeways were given in the development of World Bank statistics, which ultimately impact widely used development indicators. "The data rigging found in the report is merely the tip of the iceberg and the legitimacy crisis of the World Bank Group extends deeper into its biased narratives, ideologies and policy agenda which supports private returns at the expense of public interest regulations that safeguard social equity and the environment. A new manifestation of the Doing Business Report that continues to promote global tax competition, labour rights deregulation and environmental harms must be prevented at all costs," said Chee Yoke Ling, Third World Network, Malaysia. She added that the World Bank Group must stop standing in the way of an active developmental role of states to sustainably diversify developing-country economies and generate decent work opportunities that protect the environment for an actual green and just recovery.

A structural overhaul of the World Bank's policies and governance mechanisms is the need of the hour for it to have any credibility left. "The Doing Business case revealed the internal accountability deficit of the World Bank. Its announcement to discontinue the rankings along with personal penalties are not enough. The external investigation highlights once again the structural problems of the institution. Far-reaching reforms with regard to internal accountability structures are necessary and external control is urgently needed," said Dustin Schäfer, Campaigner at Urgewald, Germany.

Roberto Bissio, Social Watch, Uruguay, added, "Corruption is not only a matter of the Bank's flagship publication or political manipulation by its management. It is also deeply ingrained in the way the World Bank picks who it supports through its private-sector lending window, the International Finance Corporation (IFC). Only diplomatic immunity saves the World Bank's private sector lending from a landslide of corruption cases."

In fact, the Doing Business data tampering is only the latest in a long list of wrongdoings by the World Bank Group. An institution ridden with conflicts of interest and marked by an unaccountable and undemocratic governance structure should not be defining what makes good economic advice for the world. *(Society for International Development)*

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Why emerging markets must remain wary of a taper tantrum 2.0

The likely tightening of monetary policy in the US and other advanced economies could trigger financial turmoil in developing countries unless the latter take early and decisive policy action to contain its effects.

by Kavaljit Singh

On 22 September, the US Federal Reserve signalled plans to start reducing its large-scale asset purchases – a process known as tapering – this year and hinted at raising interest rates as early as next year. The formal announcement on tapering could come at the next meeting of the Federal Open Market Committee (FOMC), scheduled in early November, if no major risks materialize and the Fed achieves its maximum employment and price stability goals. "If progress continues broadly as expected, the Committee judges that a moderation in the pace of asset purchases may soon be warranted," said the post-meeting statement issued by the FOMC.[1] At his post-meeting news conference, Fed Chairman Jerome Powell affirmed that the tapering process "could come as soon as the next meeting"[2] and conclude by mid-2022.

The tapering process represents the first big step towards the normalization of monetary policy in the US following the outbreak of the COVID-19 pandemic. Once the tapering process is completed, the Fed would proceed with policy rate hikes and downsize its balance sheet, which currently stands at $8.2 trillion.

Similar to his Jackson Hole speech on 27 August, Powell underlined the need to delink the tapering process from interest rate hikes in his press conference. He stated: "The timing and pace of the coming reduction in asset purchases will not be intended to carry a direct signal regarding the timing of interest rate liftoff for which we have articulated a different and substantially more stringent test."[3]

Despite repeated attempts by Powell and other Fed officials to delink interest rate liftoff from tapering, many questions loom large: What if the Fed decides to hike interest rates earlier than what is currently projected? What if the timing of the Fed's decision and miscommunication around it trigger panic selling in the markets? Would we not then see a repeat of the 2013 "taper tantrum"?

Quantitative easing and its unintended consequences

To contain the economic fallout of the COVID-19 pandemic, the Federal Reserve took a broad array of actions, including expansionary policy (slashing policy rates to near zero) and quantitative easing (QE) (large-scale buying of bonds and securities).

The Fed has been purchasing $120 billion ($80 billion of treasury securities and $40 billion of mortgage-backed securities) every month since 18 March 2020 to support the US economy. In the aftermath of the 2008 global financial crisis, the Fed also ran a similar quantitative easing programme, through which it bought trillions of dollars in long-term securities during 2009-14.

The Fed buys such assets to induce liquidity into the economy. The increased money supply helps lower interest rates and encourages businesses to expand investments and consumers to consume more, thereby increasing aggregate demand. However, the central bank expands its balance sheet and runs the risk of higher inflation by doing so.

On the other hand, growing evidence suggests a positive correlation between a QE programme and a booming stock market. Critics have questioned the effectiveness of QE on the grounds that massive cash injection is channelled not into productive investment avenues but to speculative activities in the stock market, thereby causing a boom in the stock market. A low-interest-rate environment is generally more beneficial for stocks than bonds and fixed-income investments. Since stock ownership is highly concentrated among the wealthy and asset-rich class, the QE programmes tend to benefit them when asset prices go up. Put simply, the benefits of QE are often reaped more by financial investors than non-investors.

What happens next?

Once the US Fed takes the lead towards unwinding its QE programme, many other central banks from advanced economies – and some in emerging markets (EMs) too – would follow suit as they had also launched similar programmes following the outbreak of the pandemic.

The European Central Bank (ECB) recently announced a reduction in net asset purchases under the Pandemic Emergency Purchase Programme introduced in March 2020, while its traditional Asset Purchase Programme would continue. On 23 September, the Bank of England's monetary policy committee indicated that recent price developments had strengthened the case for a "modest tightening of monetary policy." Among the G10 countries, Norway's central bank announced a hike in interest rates on 23 September. Small advanced economies such as South Korea and Iceland have also raised interest rates in recent months.

The upcoming reversal of QE programmes in advanced economies would result in sucking out ample liquidity from the global financial markets. Since the US Fed buys $120 billion of bonds each month, the tapering process would alter the supply and demand dynamics and could potentially induce short-term volatility in certain market segments such as long-dated bonds and fixed-income assets.

The prospects of the US Fed hiking interest rates sooner than later could prove highly disruptive to emerging markets as global investors are likely to pull out money from the riskier EM assets and invest in "safe-haven" assets, similar to the infamous 2013 "taper tantrum" episode.

2013: Taper tantrum 1.0

During an appearance before the US Congress's Joint Economic Committee on 22 May 2013, the then-Fed Chairman, Ben Bernanke, spoke about the possibility of scaling back the asset purchases programme (QE3) launched in response to the 2008 global financial crisis.

His statement triggered one of the most turbulent phases in the global financial markets as investors interpreted Bernanke's statement as signalling an impending end to the Fed's highly accommodative monetary policy. Investors started panicking, bond yields shot up, and stock prices dropped. Despite subsequent attempts by Bernanke and Powell[4] to reassure investors that interest rate hikes were still far off and should not be linked with the tapering process, the taper talk prompted investors to sell riskier assets and head for the safety of bonds in the US markets.

The disruptive impact of the market frenzy was not limited to the US markets. It was more pronounced in emerging markets that experienced sharp reversals of capital inflows, resulting in sizeable currency depreciation. In particular, the turbulence was felt most in the "fragile five" emerging market economies – South Africa, Brazil, India, Indonesia and Turkey. These economies had high current-account deficits, and a strong dependence on foreign capital inflows made them vulnerable to sudden stops in capital inflows.

Before 2013, these economies had received large capital inflows thanks to the ultra-loose monetary policy of the US Fed. The foreign investors borrowed cheap money in the US and invested in higher-yielding assets in India, Indonesia, South Africa, and other emerging market and developing economies (EMDEs). But when Bernanke raised the possibility of tapering and financial tightening, investors dumped EM financial assets en masse and moved their capital to safe-haven assets in developed markets. This episode of sharp market frenzy was dubbed the "taper tantrum."

As indicated in Figures 1 and 2, several Asian and Latin American EMs experienced sharp reversals in capital inflows, resulting in sizeable currency depreciation. For instance, in the Indian debt and equity markets, foreign investors pulled out $10 billion during June-July 2013.

The 2013 taper-talk episode is a timely reminder that even the mere suggestion of reducing monetary stimulus could be hugely disruptive for EMDEs because global investors are hypersensitive to changes in the Fed's monetary policy stance.

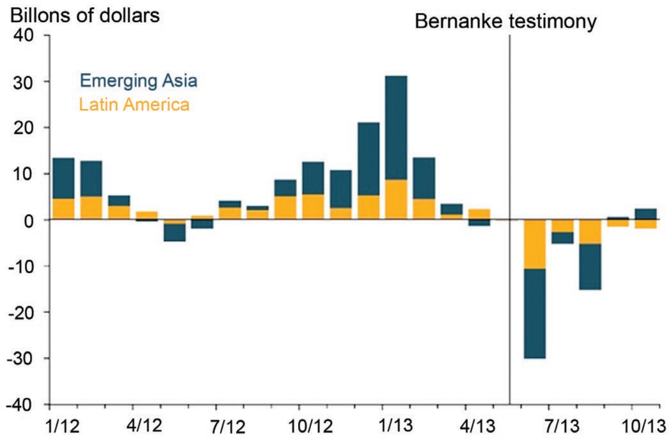
Why EMDEs cannot afford a taper tantrum 2.0 in 2021-22

Looking to the year ahead, the billion-dollar question is whether EMDEs would experience a repeat of the 2013 taper tantrum. Some market watchers argue that EMDEs may not experience a similar episode in 2021-22 because domestic and global economic environments have changed in the last eight years. However, such arguments miss an important distinction: the rapid deterioration in economic fundamentals in the post-COVID-19 period makes EMDEs particularly vulnerable to external shocks emanating from financial tightening in the advanced economies.

The uneven global distribution of COVID-19 vaccines has led to most EMDEs lagging behind their advanced peers. The slow pace of vaccinations in EMDEs makes them increasingly vulnerable to new waves of infection and the spread of virus variants. The risk of future lockdowns is holding back investment and consumption, thereby delaying the economic recovery in EMDEs.

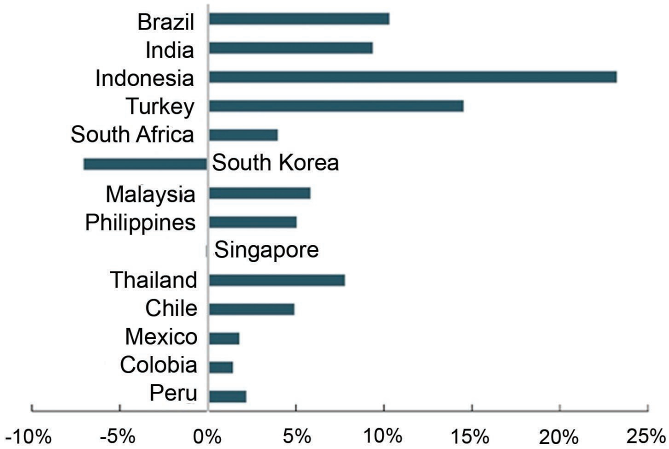
Because of the global financial interconnectedness, the eventual normalization of monetary policy in the US and major advanced economies could pose significant financial stability risks in the EMDEs. These risks are especially prominent in EMDEs with low foreign exchange reserves, large external

Figure 1: **Emerging Market Bond and Equity Fund Flows (2012-13)**



Sources: Jerome Powell and Fernanda Nechio.

Figure 2: Exchange Rate Depreciation (May-December 2013)



Source: Bloomberg, 2014.

refinancing needs, significant dollarized banking systems, thin domestic financial markets, and higher current-account deficits. Since December 2020, net capital inflows into emerging markets have been slowing down (Figure 3).

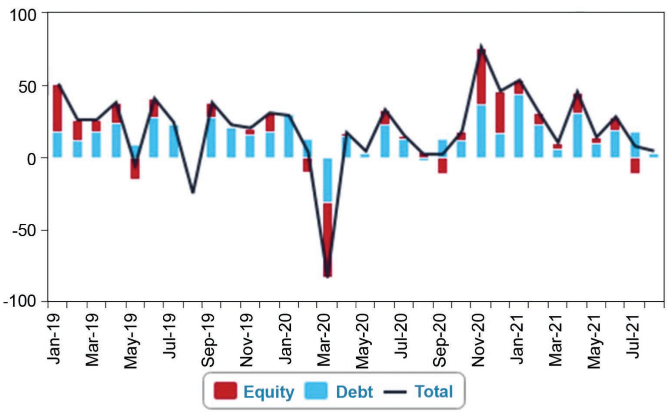
There is no denying that the timing and pace of policy normalization matter. Still, a rise in US yields and interest rates reflecting heightened concerns about inflation could trigger large capital outflows from emerging markets.

Why? Because global investors who had borrowed money in US dollars at near-zero interest rates to invest in EMDEs would sell off their financial assets in these economies en masse and move their capital to safe-haven assets. The selloffs would put depreciating pressures on EMDE currencies because foreign investors would convert domestic-currency-denominated investments into the US dollar and other foreign currencies.

A rapidly depreciating domestic currency will prompt even more investors to pull out their money as they may fear the currency falling further. This could eventually result in a run on the domestic currency, thereby perpetuating a currency crisis.

In response, the EMDE central banks may have to raise interest rates to defend the home currency even though the domestic economic conditions may not warrant a rate hike. Hence, EMDEs face the risks of repeating the currency crises witnessed in the 1980s and 1990s coupled with an increase in inflation via exchange rate pass-through.

Figure 3: **Emerging Markets: Net Capital Inflows ($bn)**



Source: Institute of International Finance and Fitch.

Little room to manoeuvre

Significant inflation pressures have emerged across EMDEs due to higher commodity prices, supply chain disruptions and weaker exchange rates. In particular, rising food prices have a significant impact on headline inflation as food expenditures represent more than 30% of the consumption basket in many EMDEs.

Persistently elevated inflation poses a major vulnerability for EMDEs because foreign investors are concerned about inflation-adjusted returns. High levels of inflation lower the inflation-adjusted return on investments and make EMDEs less attractive to foreign investors.

That's why several EMDE central banks are inching towards monetary policy normalization to address both domestic inflation pressures and exchange rate developments. The central banks of Brazil, Russia, Mexico and Chile have hiked policy rates in recent months.

Higher interest rates are problematic too. Higher rates contribute to higher debt service costs, leading to heightened debt sustainability concerns in the EMDEs.

Most EMDEs have little room to manoeuvre macroeconomic policies because of the limited credibility of their currencies. Their fiscal situation has rapidly deteriorated after the outbreak of the pandemic. Since then, the EMDE governments have stepped in to tackle the virus, enhance health expenditures and provide relief to households and businesses.

Unlike advanced economies, most EMDEs have not engaged in strong fiscal interventions due to limited fiscal space. Instead, their governments adopted a fiscal-monetary policy mix to cushion the economic fallout of the pandemic.

Nevertheless, with tax revenues down and public expenditures soaring, the budget deficits of EMDEs have increased. Their governments borrowed heavily from domestic and external sources to overcome the COVID-19-induced recession. According to data compiled by Fitch Ratings, the median EM total government debt rose from 34% of gross domestic product (GDP) at end-2012 to 62% at end-2020, making these economies more sensitive to higher global and local interest rates. As EMDE public debt levels are forecast to increase in 2021-22, it would further weaken their ability to respond to future economic shocks.

Similarly, a substantial rise in foreign currency borrowings by EMDE sovereigns and the non-financial sector since 2013 makes domestic currency depreciation more problematic for these economies.

Besides, there are risks to social and political stability too. The EMDEs would find it challenging to hike indirect taxes or withdraw fiscal support to vulnerable households in the near term as the pandemic has further worsened income inequality. That poses an additional risk of widespread social unrest, as witnessed in South Africa, Colombia and Chile in recent months.

Growing external debt vulnerabilities

While debt-to-GDP and debt service ratios are useful economic indicators, the currency composition of debt along with exchange rate vulnerability provide a better understanding of a country's financial fragility in the context of exogenous financial shocks.

Unlike low-income countries that rely on concessional loans and aid to meet their external financing needs, most EMDEs raise money through issuing foreign currency bonds in the international capital markets. Despite market turmoil during March-May 2020, many big emerging markets have raised resources via foreign-currency-denominated bonds in global markets over the past year, albeit at a higher premium.

However, a sudden stop in capital flows could trigger an external debt crisis in EMDEs if they have a large stock of foreign-currency-denominated debt and low foreign exchange reserves. Put simply, the higher the size of the foreign-currency-denominated debt, the higher the likelihood of a debt crisis during risk-off events. Hence, EMDE sovereigns and corporates that have issued large foreign currency bonds need to watch out once capital flows reverse.

Even if sovereign and corporate bonds are issued in domestic currency, foreigners' sizeable ownership of such financial instruments could transmit external financial shocks in EMDEs, as witnessed during the March-May 2020 panic.[5]

During sudden stop events, the EMDE banks with high exposure to foreign currency loans or reliant on foreign currency funding would face additional pressures in terms of higher foreign currency funding costs and rise in non-performing loans due to unhedged foreign currency loans by corporates and lower profitability prospects. In particular, African countries with dollarized banking systems need to watch out. Close to 90% of bank deposits and loans are denominated in the US dollar in the Democratic Republic of the Congo, 42% in Angola, and more than 30% in Tanzania, Uganda and Namibia. Approximately 25% of the banking system in Nigeria, Ghana and Egypt is dollarized.[6]

The weakening of domestic currencies would further complicate the debt sustainability of EMDE debt levels because currency depreciation would automatically increase the stock of foreign-exchange-denominated liabilities in domestic currency.

Already six countries – Argentina, Ecuador, Belize, Lebanon, Suriname and Zambia – have defaulted on their sovereign debt. More debt defaults could ensue in the coming months as more than a dozen countries (including Egypt, South Africa and Sri Lanka) face acute debt distress. These countries would find it extremely difficult to refinance their existing external debt.

The EMDEs need a minimum of $3 trillion to overcome the health and economic fallout of the COVID-19 pandemic and build a sustainable recovery. Although the International Monetarry Fund (IMF)'s recent $650 billion Special Drawing Rights (SDR) allocation is a welcome move and would help smaller distressed economies, it may not prove to be a game-changer for systemically important emerging markets.

The ongoing Debt Service Suspension Initiative (DSSI) by the G20/Paris Club, at best, could only provide temporary debt relief because several EMDEs are not eligible for it. Furthermore, without the participation of private creditors, the DSSI debt relief would be partial for a large number of EMDEs that owe substantial portions of debt service to foreign private sector creditors.

The "fragile fifteen"

Back in 2013, the "fragile five" – South Africa, Brazil, India, Indonesia and Turkey – had high current-account deficits, and a strong dependence on foreign capital inflows made them vulnerable to shifts in capital flows. Unlike in 2013, this time, the normalization of monetary policy in the US could also test the vulnerabilities of EMDEs with a high degree of capital-account openness and high levels of foreign-currency-denominated debt.

This time, we find at least 15 EMDEs are particularly vulnerable to global financial tightening. These are Sri Lanka, Indonesia, the Philippines, Bahrain, Egypt, South Africa, Tunisia, Zambia, Angola, Hungary, Turkey, Brazil, Colombia, Chile and Jamaica.

These 15 EMDEs are experiencing economic difficulties due to a combination of factors, including weak domestic currencies, low foreign exchange reserves, high foreign currency debt levels, sizeable foreign ownership of domestic financial assets, a sharp deterioration in fiscal position, rising inflation and weak growth prospects. Above all, most of these countries are experiencing new waves of the COVID-19 pandemic.

It is important to note that financial and debt vulnerabilities were already visible in many of these economies before the pandemic outbreak. The pandemic has exacerbated these vulnerabilities and added some new sources of financial vulnerability. The upcoming tightening of global financial conditions could further amplify financial vulnerabilities and trigger financial crises in EMDEs.

Rising forex reserves: boon or bane?

In the aftermath of the 1997 Asian financial crisis, many emerging markets have been accumulating large foreign exchange reserves to self-insure against volatile capital flows and other potential external shocks. There is no denying that forex reserves could play a critical role as the first line of defence when countries defend their currencies in the face of speculative attacks and exchange rate volatility. However, large forex reserves are not always better, and holding excess reserves entails fiscal costs.

The policies and management of forex reserves will vary depending upon the country's circumstances. Take the case of India, which is now the fifth-largest forex reserves holder in the world after China, Japan, Switzerland and Russia. Large inflows of portfolio investment and foreign direct investment have led to an accretion of foreign exchange reserves that reached a historic high of $642 billion as of 3 September 2021. This includes SDR12.5 billion (equivalent to $17.8 billion) allocated by the IMF to India on 23 August 2021.

Many analysts believe that India's $633 billion of forex reserves would be sufficient in fighting against capital flight and currency depreciation after the onset of tapering and global financial tightening.[7] We may disagree for three key reasons.

First, the composition of India's forex reserves is a serious cause for concern. Unlike China and many other emerging markets, India has not accumulated reserves through its current-account surplus. Much of India's forex reserves has been accumulated out of its capital-account surplus. As rightly pointed out by Rakesh Tripathy of the Reserve Bank of India, "reserves held by India are not truly 'earned', but rather 'borrowed' in nature, and … they may be required to be 'returned' should the capital flow reverse as it did during 2008-09."[8]

The recent increase in India's forex reserves has been mainly fuelled by short-term portfolio investments in domestic equities and bond markets. Currently, foreign portfolio investors' cumulative value of investments in the Indian markets is estimated at approximately $580 billion. Given their potentially volatile nature and destabilizing effects, portfolio flows could reverse suddenly and sharply due to the tightening of financial conditions in advanced economies, thereby putting downward pressure on India's forex reserves and the rupee.

Second, interventions by central banks in foreign exchange markets to mitigate the impact of capital outflows on domestic currencies are considered to be most effective for a short duration (less than a month). Otherwise, the central banks run the risk of depleting substantial forex reserves without having much impact. China, for instance, spent roughly $1 trillion of forex reserves defending its currency in 2015. Hence, long-term interventions in forex markets are unsustainable.

Third, it is difficult to assess the overall quantum of capital flight during a crisis-like situation because capital can move out of India through multiple sources (including abusive transfer-pricing practices and outright smuggling of foreign currency by domestic residents). Hence, these critical concerns should guide India's approach towards managing its forex reserves, especially when dealing with spillovers of global financial shocks.

Global monetary cooperation is more vital than ever

Ideally, in an increasingly financially interconnected world, international coordination is a prerequisite for managing the spillover effects of the monetary policies of advanced economies. Despite repeated attempts by several EM central banks to consider some rules-based international monetary policy coordination, the Group of Seven (G7) leading industrial economies have undermined prospects for global cooperation. Not long ago, G7 finance ministers and central bank governors issued a statement stating: "We reaffirm that our fiscal and monetary policies have been and will remain oriented towards meeting our respective domestic objectives using domestic instruments."[9]

Nonetheless, one should not miss the big picture: Increased financial fragility in systemically important emerging markets would also generate significant spillover and spillback effects on advanced economies. To illustrate, take the case of the ongoing liquidity crisis at China Evergrande Group, a debt-ridden property developer. On 20 September, concerns over contagion from a possible default of Evergrande Group sparked a broad selloff in the stock markets of Europe and the US. Even the prices of bitcoin, etherium and other cryptocurrencies fell sharply during the widespread market selloff and suffered an estimated loss of more than $250 billion in value.

Hence, it is imperative to develop a global collective response to manage policy spillovers and spillbacks in response to challenges posed by the growing interconnectedness of the global financial markets.

What about global financial safety nets? Could they be of any assistance to EMDEs experiencing rapid capital outflows and currency depreciation? Currency swap lines, IMF support and regional financial arrangements could play only a somewhat limited role, given their inherent limitations. For instance, only a few emerging markets that have strong financial and trade linkages with the US were offered access to ad hoc dollar swap lines in March 2020. Many EMDE policymakers hesitate to seek support from the IMF because of the associated strict policy conditionalities and a "stigma" stemming from the fear of adverse market reactions. In the Asian context, regional and other financial arrangements such as the Chiang Mai Initiative Multilateralization (CMIM) and the BRICS Contingent Reserve Arrangement (CRA) could meet short-term liquidity needs. However, their effectiveness is still unknown as these two arrangements have never been tested in a crisis.

Regulate volatile capital flows

In this scenario, where EMDEs have no control over changes in monetary policy stance in advanced economies, only a swift and decisive domestic policy response can minimize adverse effects of cross-border spillovers.

EMDE policymakers must act early and decisively before the actual tapering process begins in the US and other advanced economies. In the near to medium term, they could undertake policy measures to minimize its impact on domestic growth sources and insulate their economies from volatile capital flows. These policies may take the form of macroprudential tools, capital controls and currency-based measures. The proper targeting of these measures could play a vital role in reducing financial vulnerabilities.

Available evidence suggests that countries that imposed tight capital controls recovered more quickly from the 2008 global financial crisis than those with an open capital account. As noted by IMF economists,[10] EMDEs that adopted tighter macroprudential policies and capital controls before the taper-talk phase of 2013 coped better with the market pressures during the taper tantrum.

Controls on outflows could be prudent to prevent abrupt capital reversals and currency depreciation, as seen in Malaysia (1998), Iceland (2008), China (2016) and Argentina (2019).[11] Further, controls on outflows are even more relevant for poor countries that do not have large foreign exchange reserves or access to currency swap lines and regional financing arrangements.

Once capital inflows to EMDEs resume, policymakers should deploy a different set of macroprudential measures and capital controls. Since asset price boom-bust cycles are often correlated with capital flows, EMDE policymakers could deploy ex-ante macroprudential policy tools (such as higher capital buffers, limits on loan-to-value and debt-to-income ratios) to prevent domestic asset price booms.

Such measures could be complemented by imposing capital controls on inflows in the form of restrictions on foreign ownership of domestic financial assets, limits on short-term borrowings, and imposition of a tax or unremunerated reserve requirements (URR) on certain types of capital inflows.

Controls on inflows could alter the composition of capital inflows towards longer maturities to reduce financial fragility, besides providing greater leeway to conduct an independent monetary policy. Further, these measures could reduce the need to rely on ex-post policy interventions that are often less cost-effective.

In addition, EMDEs need to strengthen regulation and supervision of their financial sector to identify potential systemic risks and risk build-up in specific sectors.

Time is of the essence. A belated policy response is akin to closing the stable door after the horse has bolted!

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