

Square Pegs, Round Holes, and Why You Can't Fight HIV/AIDS with Monetarism

An Issue Briefing by Rick Rowden, ActionAid International USA

On how the International Monetary Fund is Blocking Progress in the Fight Against HIV/AIDS March 2005

The Problem

How to get a square peg through a round hole? How can poor countries invest in the doctors, nurses, and teachers needed to meet the Millennium Development Goals (MDGs) when current International Monetary Fund (IMF) loan conditions limit the spending of recipient country governments? There is a fundamental contradiction between the need to greatly scale-up social spending to fight HIV/AIDS and what can actually be spent under the IMF's current low-inflation monetary policy. How can significantly more money be spent in these economies without producing higher levels of inflation than the IMF's low-inflation policy permits?

In order for many poor countries to receive foreign aid from the World Bank or any of the rich countries, borrowing countries must first be given the "green light" by the IMF, an action that signals to other lenders that their national macroeconomic policies are sound. Because it opens the door to all the other major foreign aid donors and creditors, this "signaling effect" gives the IMF tremendous leverage over many aid-dependent countries in terms of the economic policy reforms it attaches as loan conditions. Unless a borrowing country is satisfactorily implementing the IMF's

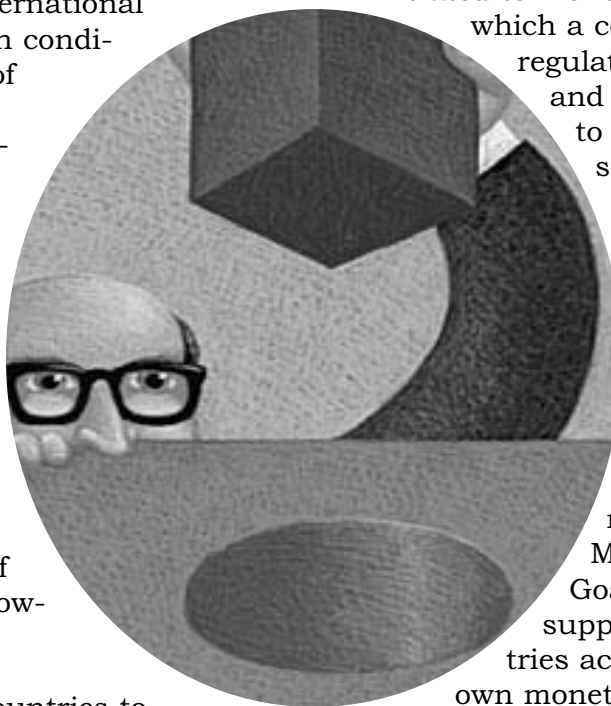
preferred economic reform policies, it risks getting the "red light" – and being cut off from access to the major sources of foreign aid, credit, or debt relief programs. Of particular concern among the IMF's binding loan conditions are economic policy reforms related to monetary policies (policies in which a central bank attempts to regulate the money supply and interest rates in order to control inflation and stabilize the currency).

Some of these monetary policy reforms that are binding IMF loan conditions, particularly the low-inflation targets, make it impossible for poor countries to increase public spending to the levels needed to achieve the Millennium Development Goals. The IMF says it supports helping poor countries achieve the MDGs, but its

own monetary policies prevent countries from being able to increase spending to the levels that will be required in order to achieve those goals. Something has to give.

The Square Peg

There is a consensus that spending on public health and education systems will need to be substantially increased in order to effectively combat HIV/AIDS and achieve the other UN Millennium Development Goals by 2015. The UNAIDS 2004 Global Report released in Bangkok stated that



countries would need to be spending about \$20 billion a year by 2007 in order to effectively address the HIV/AIDS epidemic. The Joint-Learning Initiative, a collective of over 100 top world health specialists analyzing the global health workforce, recently released a strategy report concluding that sub-Saharan African countries would need to triple their health workforces in order to meet the MDG on reducing maternal mortality, and even this might not suffice to effectively achieve MDG#6, to stop the spread of HIV/AIDS and other major diseases by 2015. The January 2005 UN Millennium Project report on the MDGs estimated that only \$16 billion of \$65 billion in foreign aid in 2002 supports direct MDG investment needs at the country level. Foreign aid for direct MDG support will need to rise to \$73 billion in 2006 and \$135 billion in 2015 if all countries are to meet the Goals. After adjusting for the fact that several countries will not meet the minimum governance thresholds required to scale up public investments for the Goals, these figures are likely to be lower—\$52 billion in 2006 and \$110 billion in 2015. The report estimated that total foreign aid volumes need to rise to 0.54 percent of rich country Gross National Income (GNI) in 2015, up from 0.23 percent in 2002 and 0.25 percent in 2003.

The Round Hole

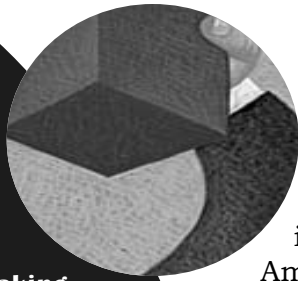
Current IMF monetary policies may have seemed appropriate for combating the crisis of hyperinflation in many developing countries during the late 1970s and early 1980s, but its tactic of tightly constraining public spending in order to get inflation down and keep it down is at odds with what is needed today: new monetary policies that allow for a major increase in public spending. For over 25 years, teams of IMF staff have negotiated with finance ministries and central banks behind closed



doors to agree on low-inflation targets. Budget decisions (how to slice the pie) are constrained by the parameters set by the monetary policy decisions (the size of the pie). Once the low-inflation target is agreed upon, the amount of “fiscal space” within which budget spending is possible is then constrained accordingly. The IMF begins with the objective of keeping inflation low and spending needs are subordinated to that objective. Regardless of how much revenue is raised through domestic taxes or from foreign aid, the IMF arrangement ensures that the right amount of money is used for external debt servicing to foreign creditors, to pay down the domestic deficit, or to be put into reserves or surpluses so that over-spending cannot occur and inflation will not increase above the set target. Yet, higher inflation may well be a side effect of higher spending, higher employment, and more workers spending more money. However, currently, countries are not able to increase public spending to the levels necessary for achieving the MDGs while also complying with the IMF’s preferred low-inflation/low-spending policies. HIV/AIDS advocates must ask: “How is the square peg of increased public spending to fight HIV/AIDS supposed to get through the round hole of the IMF’s low-inflation targeting?”

Low-Inflation Targeting: A Debatable Prospect?

There is no consensus on the most acceptable level of inflation among economists. Many economists, including some at the World Bank, disagree with the IMF that inflation needs to be “in the low-single digits” (5 percent per year or lower) to constitute macroeconomic stability. There is significant disagreement among economists about the level at which inflation begins to undermine national economic growth rates, with several respected economists suggesting that up to 15-30%



Speaking at the World Bank in November 2003, UNAIDS Executive Director Peter Piot stated, "When I hear that countries are choosing to comply with the... ceilings at the expense of adequately funding AIDS programs, it strikes me that someone isn't looking hard enough for sound alternatives..."

...In response to UNAIDS Director Piot, World Bank President James Wolfensohn acknowledged that the problem of the strict budget ceilings in the medium-term expenditure frameworks (MTEFs) were "a very real issue" and that the World Bank was "working with the IMF on this issue of limits on medium-term expenditure framework."

- Speech by World Bank President James Wolfensohn, Presidential Fellows Lecture, World Bank, Nov. 20, 2003.

per year is a moderate level of inflation. The historical record indicates that Latin America in the 1950s and 1960s and East Asia in the 1960s and 1970s experienced very high economic growth rates that were correlated with inflation levels averaging 20 percent per year. While the IMF generally prioritizes low-inflation goals, and focuses on constraining spending in order to achieve these goals (monetarism), other economists believe that even from a purely economic perspective, slightly higher inflation may be an acceptable side effect of much higher public spending, higher employment, and higher economic growth rates, and it is really a question of trade-offs. UNAIDS also viewed the situation as involving a range of possibilities and trade-offs in its 2004 Report on the Global Epidemic: "The short-term inflationary effects of increased and additional resources applied towards tackling the HIV epidemic pale in comparison with what will be the long-term effects of half-hearted responses on the economies of hard hit countries. AIDS is an exceptional disease; it

requires an exceptional response." The point is that the IMF is not the sole authority on acceptable levels of inflation, but instead holds one of many competing positions within a broad spectrum of opinion. And while many economists agree that more research needs to be done on the question, the leverage the IMF is able to exert is such that many aid-dependent countries desperate to access foreign aid will comply with the IMF's policy preference. Discussions of alternative monetary policies that would allow for such trade-offs between slightly higher inflation and more public health workers are currently precluded from the outset. But it is precisely these discussions that HIV/AIDS advocates must insist on.

Tell your government to tell the IMF: "Loosen Up" on IMF Monetary Policy to Fight HIV/AIDS!

Given this degree of uncertainty, the IMF's low-inflation targeting approach to monetary policy must be abandoned in favor of alternative monetary policies. Health, education, and HIV/AIDS advocates should work together within civil society and with their parliamentarians and media to publicly call on their finance ministries or treasury departments to take concrete steps on the Executive Board of the IMF to stop loan conditions that call for "tight" monetary policies that constrain public spending at unnecessarily low levels. Instruct them to take actions on the IMF board to "loosen up" on the monetary policy in order to allow the "fiscal space" necessary to hire the many more doctors, nurses and teachers necessary for fighting HIV/AIDS effectively.

For further information about ActionAid International's two ongoing multi-country studies investigating the degree to which national fiscal policy is constrained by current IMF monetary policies, please contact Rick Rowden, Policy Analyst, ActionAid International USA at: Rick.Rowden@actionaid.org or David Archer, Director, ActionAid International's Education Campaign at: darcher@actionaid.org.uk



Jeffrey Sachs, Director
UN Millennium Project

“International Monetary Fund program design has paid almost no systematic attention to the [Millennium Development] goals when considering a country’s budget or macroeconomic framework. In the vast number of country programs supported by the IMF since the adoption of the goals, there has been almost no discussion about whether the plans are consistent with achieving them...In its country-level advisory work, the UN Millennium Project has found that multilateral and bilateral institutions have not encouraged countries to take the Millennium Development Goals seriously as operational objectives. Many low-income countries have already designed plans to scale-up their sector strategies, but due to budget constraints could not implement them. In other cases, countries are advised to not even consider such scaled-up plans.”

From: The UN Millennium Project’s January 2005 report, “Investing in Development A Practical Plan to Achieve the Millennium Development Goals” Chapter 3, p. 36



Stephen Lewis, UN Special
Envoy for HIV/AIDS in Africa

“[In Zambia] the imposed [IMF] macroeconomic policy means that the Ministry of Health can hire no more staff, and fully twenty per cent of the municipal districts have no doctors and no nurses. The Government urgently wants to confront the pandemic, but it cannot do so with its financial policy and planning in a strait-jacket. The Board of the IMF must come to realize that rigid macroeconomic conditionality is putting Zambia at risk...I have argued before in cases involving the IMF, and I argue again that it has failed to grasp the demonic force of the human and economic carnage caused by HIV and AIDS.”

From: “At the Heart of Everything Lies HIV/AIDS,” Statement by Stephen Lewis, UN Special Envoy for HIV/AIDS in Africa: Zambia Test Case for G8 Summit. June 11, 2004



Mark Malloch-Brown
Administrator, UNDP

In 2003, the United Nations Development Program’s annual Human Development Report called for a broad policy review of how best to lift the least developed nations out of extreme poverty rather than the “Washington consensus of the World Bank and International Monetary Fund,” that includes extreme budget discipline, deregulation and the liberalization of trade and Finance. The UNDP report documented that 54 countries had become poorer in 2003 than they were in 1990, while life expectancy fell in 34 countries and 21 countries were hungrier in 2003 than they were in 1990. The study said the IFI’s current policy approach, which is based on a total reliance on market forces and increased trade to achieve development, will not succeed. UNDP Administrator Mark Malloch-Brown called for a “guerrilla assault” on the neoliberal policies and for a reaffirmation of the role of the state in development policy: “Market reforms are not enough. You can’t just liberalize; you need an interventionist strategy.” The excessive budget discipline of IMF and World Bank leads to ceilings on national spending, and to direct cutbacks in basic government services provision in most countries that borrow from the IFIs. “The IMF and the World Bank should no longer set these kind of ceilings,” Malloch-Brown said.

From: Human Development Report 2003: Millennium Development Goals: A compact among nations to end human poverty.” United Nations Development Programme. 2003. and Quotes from: “The lost decade: They were promised a brighter future, but in the 1990s the world’s poor fell further behind.” by Larry Elliott, economics editor. The Guardian (UK). July 9, 2003

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