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Foreword

Reflecting its concern with the social implications of economic reform, as well as with the quality of macroeconomic adjustment and growth, the IMF held a conference in June 1998 on economic policy and equity, the proceedings of which are presented in this volume. This conference followed up on one the IMF had held in 1995 on income distribution and sustainable growth (papers presented at that conference were published as *Income Distribution and High-Quality Growth*, edited by Vito Tanzi and Ke-young Chu, MIT Press, 1998). Since that time, experiences with globalization as well as the financial crisis that has affected several countries have deepened the IMF's concern about the need to find the proper responses to equity issues.

The second conference represented another opportunity for the IMF to listen to ideas by outside experts on how to formulate and implement equitable policies, bringing together not only senior policymakers and academics but also religious leaders and labor representatives from around the world to discuss practical issues faced by governments in promoting equity. The significance of equity concerns in today's world has been reconfirmed by the awarding of the 1998 Nobel Prize for Economics to one of the speakers in this conference, Amartya Sen, an economist who has spent his professional life pushing the boundaries of our understanding of poverty and equity.

In its work, the IMF promotes economic policies that help countries achieve macroeconomic stability and high-quality growth. High-quality growth is growth that is sustainable in the face of external shocks; accompanied by adequate investment (including in human capital, to lay the basis for future growth); respectful of environmental and national concerns; and, last but not least, consistent with policies that reduce poverty and improve equity.

This last feature—policies that reduce poverty and improve equity—is important for a variety of reasons. First and foremost, reducing poverty and promoting an equitable distribution of income are important objectives in their own right, but they can also serve other objectives. The macroeconomic and structural policies to promote sustainable growth—which may include some painful but necessary measures—typically require broad domestic political support. Such support is more likely to be forthcoming when the course of economic adjustment is perceived by the population as fair and socially just.

Sustained growth is an important element in reducing poverty in a meaningful way. But experience worldwide teaches that growth is often not enough to move a substantial portion of the population out of poverty or to improve the distribution of income. Growth has to be accompanied by policies that also benefit the least fortunate. In fact, equity-oriented policies that lead to more investment in human capital can reduce poverty through a synergy of growth and equity: greater investment in human capital enhances the growth potential of the economy, and targeting these expenditures to the poor enhances their chances to seize economic opportunities and improve their standard of living.

Many countries have taken bold steps aimed at achieving high-quality growth. They have pursued sound monetary, fiscal, and exchange rate policies and have implemented strong structural reforms. These policies have been accompanied by appropriate social policies and measures to achieve good governance. Indeed, many countries have made impressive economic progress. Nevertheless, despite these commendable policy efforts, high-quality growth remains elusive in many regions of the world. Although global output has grown by more than 3 percent annually since the beginning of this decade, the growth has been shared unevenly. Income inequality has remained high in Latin America and sub-Saharan Africa and has even risen there and elsewhere, most notably in the transition countries but also in several industrial countries and, more recently, in some East Asian countries.

To respond to these developments, I would like to stress the need for a "second generation of reforms," to complete the transformation of the state's role in the economy. Of particular importance are the establishment of simpler, more transparent regulatory systems that are equitably enforced and help to reduce corruption, one of the more cynical factors of inequity; a strengthening of the professionalism and independence of judicial systems; and an improvement in the efficiency and equity of public expenditure and tax systems.

Attention to the level and composition of government spending is essential in promoting equity. A central ingredient in efficient and equitable expenditure policies is the trimming of unproductive expenditures, such as those for excessive public sector payrolls, subsidies to inefficient public enterprises, untargeted consumer subsidies, and excessive military spending. A shift in public expenditures toward primary education and basic health care can promote both equity and growth. Finally, in the context of a strong reform effort, adequate resources must be provided in the budget for social safety nets to shelter the poor and other vulnerable groups from the short-term adverse effects of reforms.

The recent turmoil in international financial markets has shaken the world, highlighting the role that equity and social policies must play in the global economic system. In Asia, the adverse impact of the crisis and the reform programs on poverty and human welfare is substantial, especially considering the many decades of impressive gains in poverty reduction. Now the task of the world community is to draw on the lessons of the recent experience in Asia and elsewhere. The international monetary system will have to be strengthened, for example, by extending to the global level the same principles and rules that have long existed in the most developed financial systems at the national level, and by involving the private sector in the prevention of crisis and resolution. But reform of the international monetary system cannot ignore social policies. The international financial system must be based on equitable socioeconomic policies and a concern for the most disadvantaged. As poor countries become more fully integrated into the global economy, the poor must be allowed to improve their standard of living.

The IMF has learned that its policy advice inevitably has equity implications, and, therefore, that despite being a macroeconomic policy institution, it must address equity issues in its work. Consequently, the IMF must improve its own understanding in this area, while drawing on and collaborating with other international organizations, including the World Bank, regional development banks, and the United Nations Development Programme, International Labor Organization, and other UN agencies that have more expertise in equity and related issues.

The world's knowledge of the links between economic policy and equity is still insufficient, and the IMF and all policymakers must be attentive to the findings of academics, colleagues in other international organizations, and all those who are addressing such issues in member countries. The IMF organized the 1995 and 1998 conferences in this spirit. Similarly, the IMF recently commissioned a team of external experts to review the enhanced structural adjustment facility (ESAF) operations—the IMF's concessional facility—which has become the centerpiece of the IMF's support for the poorest countries. This review pointed to areas where the IMF's approach to social policies could be strengthened. To this end, the IMF launched in the fall of 1998 a pilot program in six ESAF countries where, in collaboration with the World Bank, it will undertake a more intensive analysis of the social impact of adjustment.

The IMF hopes that the lessons learned in these countries can, in due course, be applied to other countries that implement ESAF-supported adjustment programs.

I hope that, in going through the proceedings of this conference, readers will be encouraged to share their reflections with those who participated in this seminar and with the editors—a dialogue that the IMF looks forward to. Several policy lessons with clear implications for the future work of the IMF have already emerged from the discussions, and, despite the broad range of views presented, there was substantial agreement on a number of important issues. No doubt the proceedings from this conference will contribute to more constructive debate and more progress.

MICHEL CAMDESSUS
Managing Director
International Monetary Fund

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We are grateful to the IMF's Managing Director, Michel Camdessus, for his suggestion to organize this conference and for providing guidance in its design. We are also thankful to the First Deputy Managing Director, Stanley Fischer, for his active role throughout the two-day event.

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Diane Cross meticulously edited the manuscript. Lawrence Hartwig, aided by Amy Deigh and Cecilia Pineda, typed the successive versions. J.R. Morrison of the External Relations Department edited the final manuscript and coordinated the production process.

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