

The Challenges of Meeting the Millennium Development Goals (MDGs)¹

By Professor Joseph E. Stiglitz
University Professor, Columbia University
Executive Director and Co-Founder, Initiative for Policy Dialogue
Nobel Laureate in Economics, 2001

The moral necessity of meeting the Millennium Development Goals is now well understood by the entire global community. There is a consensus that more resources are needed and that more sustainable resources can be well used, but there is also a need for understanding that more than aid is required. The World Bank has emphasized, in the last few years, the importance of a comprehensive approach to development. This is an important advance in our understanding of the development process.

Given the limited amount of time, I want to draw attention to three initiatives which could be taken at the international level, which could help the world achieve the shared aspiration of the Millennium Development Goals. The first one has to do with trade. In an address I gave in Geneva in March 1999, I called for a development round of trade, even before the breakdown in Seattle. So I welcomed the commitment of the trade ministers at Doha in November of 2001 to have a development round, but I have been saddened by what has happened since then.

There has been one item of good news, and that is the step by Europe to open up its markets to the poorest countries of the world, specifically, its “Everything But Arms” initiative. Elsewhere, however, not only has there been a renegeing on some of the commitments made at Doha, but it has become increasingly apparent that those commitments do not, in fact, go far enough. After the failure of multilateral trade negotiations at Cancun in 2003, the Commonwealth asked me to look at what a true development round would look like. The conclusion we reached, in a study done by the

¹ Transcript of comments made on June 29, 2005 by Professor Joseph E. Stiglitz at the “Voices Against Poverty” presentation at the High Level Segment of the Economic and Social Council (ECOSOC) meetings at the United Nations headquarters in New York.

The Challenges of Meeting the Millennium Development Goals (MDGs)
by Professor Joseph E. Stiglitz

Initiative for Policy Dialogue, is that what has been sold under the rubric of a development round does not deserve that epitaph.

Agriculture has been singled out as reflecting most strongly the developed countries lack of commitment to the Development Round. With 70% of those in the developing world depending on agriculture for their livelihood, the failure of the developing countries to cut back their subsidies is deeply disappointing. The subsidies, which are enormous, depress incomes in developing countries; many lose far more as a result than what they receive in aid. But it is not just a question of agriculture. There are a host of ways in which the current trading regime discriminates against developing countries and impairs their development. What is needed is a fair trade regime, a trade regime that would promote the sort of development which would make an enormous difference in achieving the Millennium Development Goals.

The second issue involves global financial stability. We do not pay enough attention to the looming problems of global financial instability. The IMF, which is charged with the responsibility of overseeing the global financial stability, has regrettably failed in addressing these fundamental issues.

Why do the developing countries suffer so much from this global instability, and what can be done about it? The quick answer is that there is, in a sense, a massive market failure. Standard economic theory says that risks – the risk of interest rate and exchange rate volatility – should be borne by those most able to bear those risks, namely the advanced industrialized countries. But unfortunately, the way the global economic system works, it is the developing countries which disproportionately bear these risks.

It is one of the reasons why the problem of debt has not been adequately dealt with. Even with debt relief, unless we do something about the underlying problem, there is a good chance that the debt problem will resurface again. Manageable debt levels have been

The Challenges of Meeting the Millennium Development Goals (MDGs)
by Professor Joseph E. Stiglitz

turned into unbearable debt levels as a result of increases in interest rates and changes in exchange rates. Latin America, for instance, knows this all too well. Twice in recent decades, the debt burden of some of the Latin American countries has become totally unbearable, and there have been massive defaults – not because of any change in policy, but because of changes in the global economy which have increased interest rates and changed exchange rate. The answer as to what should be done about this problem is, in a way, simple. The IMF should try to design ways of shifting risks from the developing countries to the developed countries, so that the developing countries no longer bear so much of the risks of exchange rate and interest rate fluctuations.

Why is there so much instability in the global economy? And, what can be done about it? There are currently a number of global imbalances, but there is a single factor contributing more to global instability than any other: U.S. macroeconomic policy, with the associated huge fiscal and trade deficits. So long as these deficits continue, global financial markets are likely to be marked by high levels of uncertainty.

All the same, there is a deeper, underlying problem – the structural problem of the global reserve system. This system not only contributes to instability, but also exerts a deflationary bias on the global economy, making sustained growth more difficult. Moreover, there is a fundamental sense in which it is unfair, an allegation which I will explain shortly.

The high level of instability necessitates that all countries, including developing countries, put aside substantial amounts of reserves, effectively burying in the ground money that could be used later on in times of need. In the old days, we had a gold reserve system, and it was indeed very peculiar: enormous amounts of money were spent taking gold from the beneath the ground (in a process which have severe adverse environmental consequences), and then, even more was spent burying it back in the ground in secure vaults. Somebody from Mars looking at this would say, “What are

The Challenges of Meeting the Millennium Development Goals (MDGs)
by Professor Joseph E. Stiglitz

these people doing?” Well, we have gone a little bit beyond that, but not that far; we now have a system in which billions of dollars --if fact trillions of dollars—are held in reserves.

These reserves amount to the developing countries lending vast amounts of money to the richest countries of the world at very low interest rates (1, 2 or 3%). Of course, at the same time, these poor countries borrow vast amounts of money from the banks of industrialized countries at very high interest rates (10, 15 or 20%). This lending-borrowing cycle between the developing countries and the developed countries is of immense help to the growth of the developed countries, but not to the developing countries. The net transfer from developing to developed countries (the difference in the borrowing and lending rate) is huge – so large that it exceeds, in many cases, the amount of foreign aid received.

Changing the global reserve system could not only be helpful for development, but it could also help enhance global economic stability and promote sustained economic growth. The fact that so much purchasing power – essentially three to four hundred billion dollars – is buried in the ground every year obviously acts as a deflationary pressure on the global economy. Money that could have generated aggregate demand does not. In the past, the deflationary bias of the reserve system has been offset by expansionary policies of central banks and deficit spending by governments. But with the spread of responsible central banks and governments trying to bring budgets into balance, the offsets to the deflationary bias of the global reserve system are much weaker. The performance of the system would be worse were it not for the fact that the United States has been willing to be a consumer of the last resort.

But something is wrong with a global economic system in which the world’s richest country lives beyond its means by as much as two or three billion dollars per working day – and, without which spending, it might decline into recession.

The Challenges of Meeting the Millennium Development Goals (MDGs)
by Professor Joseph E. Stiglitz

This deflationary bias is not the only reason that the current global reserve system is marked by instability. With dollars being used as a reserve currency, there is a huge demand for its bonds, and the U.S. has obliged with an enormous supply. But it is hard to see how this process in which the U.S. becomes increasingly in debt can be, in the long run, viable: as the debt grows larger and larger, so do doubts about the wisdom of holding the dollar as a reserve currency. This is already happening; and as these doubts mount, the dollar weakens, undermining its usefulness as a store of value. The question is then raised: for how long can the current system last.

Though one might think that the U.S. benefits from the low interest loans from other countries, even the U.S. would benefit from a change in the global reserve system. It suffers, like the rest of the world does, from the global instability of the current regime. And the U.S. faces the additional problem that without the huge fiscal deficit and with the huge level of trade deficit, it has a consistent deficiency in aggregate demand (with the exception of the last half of the 1990s, when an irrational exuberance led to a stock market bubble and an investment boom).

The international community needs to begin to think about alternatives. One such alternative is for the international community to issue reserves (much as it has done periodically with the issuance of Special Drawing Rights – SDRs – at the IMF.) The “money” issued could be spent on global public goods and to help developing countries. The enormous amounts of money could provide finance for the resources needed to meet the aid requirements necessary for achieving the MDGs. This new kind of reserve system would, at the same time, increase equity, promote development and increase global stability. By increasing global financial stability, this reform would contribute to meeting the MDGs in another, important way: counteracting the global financial instability that has exacted a huge toll on developing countries, and especially on the poor in those countries. Every major crisis gives rise to a significant increase in numbers in poverty, and it often takes years to reduce poverty to pre-crisis levels. Education gets

The Challenges of Meeting the Millennium Development Goals (MDGs)
by Professor Joseph E. Stiglitz

interrupted in a crisis, as parents no longer can afford to send their children to school, and once interrupted, students often do return to school.

The third initiative also has to do with finding innovative sources of finance for development that has been on the UN agenda (including the initiative of the Four Presidents; since the meeting at the UN in the fall of 2004 which drew enormous attention, discussions have continued in a variety of venues.) There is recognition that meeting the MDGs will require substantial increases in aid flows, and there is, accordingly, an imperative to explore innovative ways of finding these funds. The global reserve reform, which I described before, is one such initiative (motivated, at the same time, by a desire to do something about another major global problem, global financial instability), but there is another one to which I want to call attention. Here again, there is a link between finance and addressing a major global problem – in this case, the problem of maintaining our global environment.

The developing countries are currently providing enormous services to the global community, including to the developed countries, for which they are not being compensated. These are environmental services, including a reduction of greenhouse gases and the preservation of biodiversity.

In response to mounting scientific evidence, at Rio in 1992, the international community recognized the risks posed to the entire planet by the increases in greenhouse gases leading to global warming and with attendant side effects, such as an increase in sea levels. After Rio, I served on the Intergovernmental Panel on Climate Change (IPCC), the international panel that reviewed the scientific evidence, and I can say that, even at that time, the evidence on the increases in greenhouse gases and their adverse consequences was overwhelming, and the case for doing something was compelling. At Kyoto, the international community agreed on a framework for doing something about the problem, and the developed countries committed themselves to cutting back on the

The Challenges of Meeting the Millennium Development Goals (MDGs)
by Professor Joseph E. Stiglitz

level of emissions. Since Kyoto, evidence has mounted both on the severity of the problem and on the rapid pace at which global warming is occurring, including studies about the melting of the arctic poles, and about how, within a few decades, the United States glacier national park will be without glaciers. And since the time I first looked at this issue, the already-abundant evidence has become even more overwhelming.

Kyoto was a major achievement, but there were at least three problems. First, the United States, the world's largest polluter, has refused to sign, and done little to cut its emissions. Second, the world's developing countries did not assume obligations. They rightly felt that the developed countries had been the major source of past pollution, and they worried that committing to significant reductions would adversely affect their growth, directly related to attempts to reduce the level of poverty in their country. Thirdly, they recognized that forests play an important role in reducing the level of greenhouse gas concentrations (see below). However, though there was a provision that gave countries that planted new forests credit for their contribution to reducing greenhouse concentrations, there was no similar provision for *avoided deforestation*. This meant that a country could be paid if it cut down its old, hardwood forests and then replanted them, but could not be paid if it preserved these same forests. This was, of course, absurd.

The magnitude of what is at stake is enormous – both environmentally and financially. We now have a method of valuing, for instance, one part of the environmental services provided by the developing countries – the services performed in conjunction with reducing greenhouse gases. As the Kyoto Protocol has gone into effect, the European trading system (in which those who are emitting less than their quotas can in effect “sell” those excess to those who face a deficiency) has put a dollar value on carbon: a firm that can reduce its emissions by a ton can get paid for doing so. Underlying the carbon trading system is the market mechanism: if the price put on a ton of carbon is greater than the cost to a firm of reducing its emissions, it will pay the firm to do so. It also

The Challenges of Meeting the Millennium Development Goals (MDGs)
by Professor Joseph E. Stiglitz

means we can value carbon sequestration – carbon stored inside a tree, and therefore not added to the atmosphere. Forests also take carbon dioxide out of the atmosphere, and convert it into oxygen. Hence, maintaining forests is of enormous importance to anyone concerned with the increased concentration of greenhouse gases in the atmosphere. Conversely, there is an enormous environmental cost from deforestation. By some estimates, the deforestation in Indonesia and Brazil alone will by 2012 undo some 80% of the gains from carbon reduction by the EU and others under the Kyoto Protocol.

The value of the “carbon” services provided just by the tropical rainforest countries is enormous, exceeding thirty to sixty billion dollars at current market prices per year. If these countries were to be compensated for the services provided, that money would obviously be an important source for finance to these countries, greatly enhancing their ability to meet the MDGs.

Today, unfortunately, there is a major obstacle to the developing countries being paid for providing these environmental services. And in the absence of compensation for providing these services, these countries face enormous economic incentives to cut down their forests, *even though from the perspective of global efficiency the best use of these resources is to preserve them as tropical rainforests*. Kyoto’s mistake in not including compensation for avoided deforestation is likely to have enormous global consequences. But while those from the developed world have been slow even to recognize the existence of the problem – let alone its size – a number of developing countries have responded. Under the initiative of Papua New Guinea and with the strong support of Costa Rica (which itself has begun to compensate its own people for providing similar environmental services), the Rainforest Coalition has been formed. They have not only recognized the problem, but have been actively exploring a variety of ways by which it might be addressed. Some of the developing countries have come forward and said they will voluntarily submit to the constraints of the Kyoto Protocol, and that they will reduce their carbon emissions, but they also want to be compensated for the environmental

The Challenges of Meeting the Millennium Development Goals (MDGs)
by Professor Joseph E. Stiglitz

services which they provide, and that there must be compensation for avoided deforestation. It is not just a matter of fairness – compensating them for services from which the entire world benefit; but it is also a matter of efficiency, providing an incentive to them to continue to be the stewards of these global resources. This initiative, like the previous one, can play a vital role in achieving the MDGs. Adverse climatic changes will make the achievement of the MDGs all the more difficult. We now recognize the close link between poverty and the environment. This initiative will both contribute to a better global environment and provide that a very large set of countries, those with large forests, receive a substantial amount of the finance required to achieve the MDGs.

The challenge of meeting the MDGs will require concerted efforts by the entire international community. But as I said, more than aid will be required. We will have to address some of the fundamental structural problems affecting global trade, finance, and the environment. The three initiatives I have described are win-win ideas: the vast majority in the developed countries will benefit, even as it helps lift out of poverty the poorest in the poorest countries.