Comments on Kumi Shigehara's Issues Note on "The Future of Policy Advice by Intergovernmental Institutions"

by
Wolfgang Michalski*

Technological progress and the globalisation of economic activities are among the main driving forces of dynamic economic and social development. In particular since the end of the Second World War, the interaction of these forces, together with a basically positive policy response, resulted in rising incomes and prosperity world-wide. Looking at country-specific performance, it is important to note that through-out this period those countries fared best which flexibly adjusted to the permanent changing geopolitical, economic, social and technological environment conditions.

Both theory and empirical evidence demonstrate that structural adjustment is not only associated with economic and social benefits, but also with costs. Even if overall incomes and prosperity are rising, there will be at least temporary losers, and some of them may be left behind for a long time or for ever.

There are three aspects which frequently contribute to attributing politically more weight to the losses than to the benefits. First, to the extent that structural change results in job destruction, for the people concerned this normally involves beyond the loss of income also loss of social status, loss of stable neighbourhood and maybe loss of identity related to a place. Second, in the process of structural change, there is an asymmetry as regards the visibility of benefits and costs. The longer-term benefits such as the gains in macro-economic productivity, the jobs created elsewhere in the economy or the contribution to combat inflation, are spread thinly all over the economy, whereas the losses are immediately visible and in many cases in terms of sectors and/or regions highly concentrated. Third, jobs not created have no vote, jobs lost have.

* Managing Director at WM International. Former chief adviser to the Secretary-General of the OECD.

It is obvious that these effects represent powerful incentives for politicians, lobbyists and sometimes labour unions to argue against technical progress, globalisation and free trade. In a world where economic policy, including international economic policy, has become increasingly politicised, policy advice which does not take into account the dimension of political economics, will have increasingly difficulties to be accepted. Governments and their supporting parties want to be re-elected. Business associations and unions protect the narrow interests of their members. And people in modern democracies want to see their real concerns being addressed. Abstract macro-economic policy advice, in particular from intergovernmental organisations, rarely addresses the distributional and non-economic implications of the policies recommended, and of course there is the question whether and, if so, to what extend meeting such a request would be desirable or possible.

Intergovernmental organisations are facing a multi-layered dilemma in this context: On the one hand, they have an important role to play in assisting governments to design and pursue policies which would contribute to achieving the stated objectives; on the other, governments frequently know very well what the most appropriate policy is in theory, but in the light of fierce social and political opposition they do not know how to implement it. As long as the public perceived international organisations as trustworthy and independent authorities, their policy advice had been accepted without major resistance. In many cases it even helped governments to justify certain unpopular measures. Since intergovernmental organisations are perceived as part of the elitist establishment which does not care about the real problems of ordinary people, this is much less so. The recent rise of nationalistic populists in a number of OECD countries is clearly contributing to this development.

As a consequence, if international organisations want their policy advice to be relevant, they may have to go on a tightrope between general macro-economic and other policy advice on one side and analysis of country-specific options on how to deal with the economic and non-economic adjustment costs on the other.

The OECD has tried to do so in the early 1980's within the framework of its work on "Positive Adjustment Policies". The general policy guideline was to enable structural adjustment to rapidly changing geopolitical, economic, social and technological environment conditions at the highest speed that is socially acceptable and politically feasible. This conditionality was the decisive difference between the OECD concept of Positive Adjustment Policies and the approaches to structural adjustment at the IMF and the World Bank.

Critics of the OECD approach argued that the conditions of social acceptance and political feasibility could easily open the door for business associations, unions and other stakeholders to defend the status quo at all costs and for governments not to try hard enough. But one should not forget that the alternative may be that either the policy advice is ignored or is followed up and results in major economic and social disruption. Both these options could be worse than the second or third best solution based on policy advice that takes the political economics into account.

In principle, there are several levels of policy analysis and advice in this context. The first is including an assessment of the distributional effects of the policies recommended and let the government decide whether there is a need to compensate losers, and if this is considered as necessary, how to deal with that. A second level is indicating what the options are available for making the adjustment process socially less disruptive. This could include a broad range of measures from temporary adjustment subsidies over conditional income support to institutional arrangements regarding education and training. The third is providing a policy evaluation and recommendations with respect to these options, both in terms of their effectiveness and in terms of their compatibility with the basic principles of a market economy.

The first level is certainly the least controversial. The second could be very useful if it would contribute to push the limits of social acceptance and political feasibility further out. Apart from short-term interventions such as well targeted adjustment subsidies which are to be reduced according to a pre-determined timetable, it seems that institutional measures such as the establishment of an effective social net combined with strong incentives for education and training are the most promising option. [Here I agree with Leif.] The third level may be one step too far. International organisations have to be extremely careful not to interfere with county-specific problems related to national sovereignty which is easily done when dealing in very concrete terms with distributional issues.