FISCAL STIMULUS PLANS:
THE NEED FOR A GLOBAL NEW DEAL

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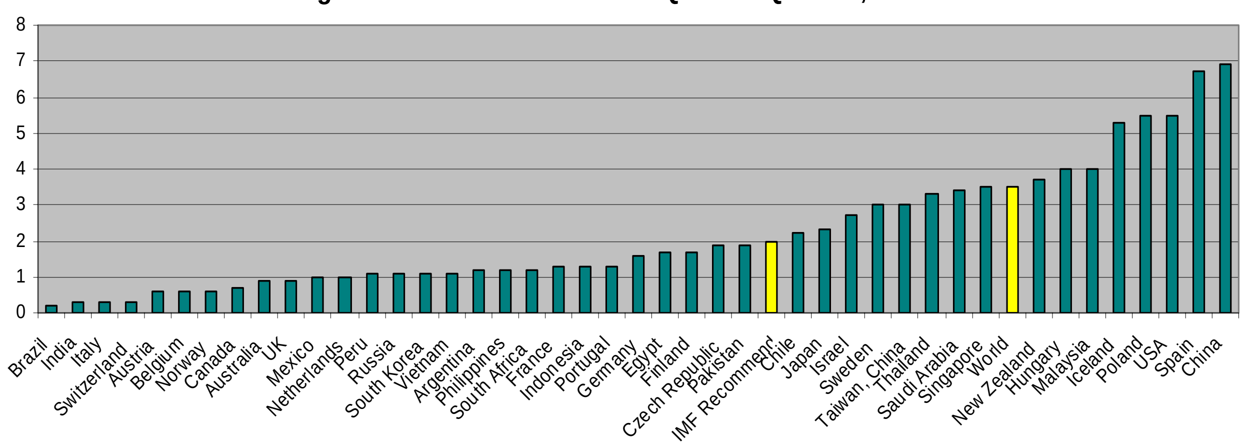
ABSTRACT: This article reviews the fiscal stimulus packages announced in 43 countries. In March 2009, the total amount announced for these stimulus plans is US$ 2.18 trillion, or 3.5% of world's GDP, mostly in higher income economies. The majority of these recovery packages contain measures to stimulate firms, consumers, and public investment in infrastructure. The author argues that a country approach is inadequate;a global crisis requires global responses. Developing countries will be hit hard; there is a need for increased ODA to enable them to engage in countercyclical stimulation. Stimulating global demand (and reducing poverty) will require further redistributive measures. Responses have been slow. There is an urgent need for a coordinated expansionary global stimulus package.

I. ANNOUNCED FISCAL STIMULUS PACKAGES

Initially, governments' response to the crisis was the conventional interest rate cut and rescuing banks and financial institutions[2], most notably the US, where $3 trillion have been spent on bailouts over the last two years[3]. After much controversy on the adequacy and conditions of the bailouts, soon it became clear that adjusting interest rates and rescuing banks would not be sufficient, and since the end of 2008 more than 40 countries have announced stimulus packages (Figure 1). The majority are higher income economies.

Figure I: Fiscal Stimulus Plans Q4 2008-Q1 2009, %GDP



In March 2009, the total announced for stimulus packages is US$ 2.18 trillion, or 3.5% of world's GDP (Table 1). The amount per country varies from US$ 1 billion (Sweden, Vietnam) to more than US$100 billion (Germany, Japan, Saudi Arabia, Spain). Exceptionally, USA and China have announced much larger stimulus plans, at US$787 and US$586 billion respectively. In relative terms, the countries with larger efforts in

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2 United Nations (2009) *World Economic Situation and Prospects 2009.* New York, UN DESA; Khatiwada and McGirr (2008): Current Financial Crisis: A review of some of the consequences, policy actions and recent trends, Geneva: IILS.

3 *US Emergency Economic Stabilization Act,* 1 October 2008; Bloomberg News and Reuters Feb. 2009

2009 are China (6.9% GDP), Spain (6.7% GDP), and USA (5.5% GDP). The IMF generic recommendation is 2% GDP, but half of the countries have so far engaged in larger stimulus packages.

Table I: Announced Stimulus Plans (Q4 2008-Q1 2009)

Country	Amount US$ billion	% GDP	Country	Amount US$ billion	% GDP
Argentina	3.9	1.2	**Netherlands**	7.5	1.0
Australia	10.1	0.9	**New Zealand**	5.0	3.7
Austria	3.7	0.6	**Norway**	2.9	0.6
Belgium	2.5	0.6	**Pakistan**	7.6	1.9
Brazil	3.6	0.2	**Peru**	3.2	1.1
Canada	43.6	0.7	**Philippines**	6.1	1.2
Chile	4.0	2.2	**Poland**	31.4	5.5
China	586.0	6.9	**Portugal**	2.7	1.3
Czech Rep	7.8	1.9	**Russia**	20.0	1.1
Egypt	5.4	1.7	**Saudi Arabia**	126.7	3.4
Finland	2.6	1.7	**Singapore**	13.9	3.5
France	33.0	1.3	**South Africa**	3.7	1.2
Germany	103.3	1.6	**South Korea**	10.8	1.1
Hungary	6.5	4.0	**Spain**	113.3	6.7
Iceland	2.1	5.3	**Sweden**	1.0	3.0
India	4.0	0.3	**Switzerland**	1.3	0.3
Indonesia	6.7	1.3	**Taiwan Province of China**	12.0	3.0
Israel	5.0	2.7	**Thailand**	8.5	3.3
Italy	6.3	0.3	**UK**	36.3	0.9
Japan	110.0	2.3	**USA**	787.0	5.5
Malaysia	17.2	4.0	**Vietnam**	1.0	1.1
Mexico	11.4	1.0	**Total World**	**2180.6**	**3.5**

Source: Updated from national news from IILS and ILO (forthcoming 2009); Gallagher et al. (2009): *Survey of Stimulus and IMF Rescue Plans During the Global Financial Crisis;* Prasad and Sorkin (2009) *Assessing the G-20 Economic Stimulus Plans: A Deeper Look*, Washington, Brookings; and IMF (2009) *Staff Note to the January G-20 Meeting*, Washington IMF.

Details of most stimulus plans are still unclear, but the majority of these recovery packages contain measures to stimulate (i) firms, (ii) consumers, and (iii) public investment, mostly in the form of economic and social infrastructure:

(i) Fiscal Stimulus to Firms: Generally, this includes subsidies and corporate tax breaks, most often support to cash-strapped small and medium-size companies (SMEs) and large export earners. Brazil, Canada, Chile, France, Germany, India, Indonesia, Portugal, Russia, Spain, South Korea, US, among others, plan cuts in corporate taxes and tax rebates. In Germany, [4] the new Act guarantees US$514.4 billion worth of interbank loans with maturities of up to three years and allocates US$ 25.7 billion to back up this guarantee; in addition, to stimulate the economy, the German Federal Cabinet introduced a package focused on tax incentives and subsidies to industry. Some countries have focused on strategic sectors, such as construction (e.g. Canada, Germany,

[4] Financial Market Stabilization Fund, effective on October 18, 2008 *(Gesetz zur Errichtung eines Finanzmarktstabilisierungsfonds)*

Norway), agriculture (e.g. Russia, Vietnam), auto industry (e.g. Brazil, France, Germany, Hungary, Russia, Spain, US), tourism and miscellaneous exporters (e.g. Spain, Chile, Finland, Switzerland). In Argentina and Japan, the package includes incentives for SMEs to hire and put on the books workers who currently are informal/temporary[5], and in Spain and the UK, to companies contracting unemployed heads of households.[6]

(ii) Fiscal Stimulus to Consumers: This includes tax cuts to low income households, and expansion of existing social security programs to sustain populations. Most countries have announced cuts in personal income taxes (e.g. Australia, Canada, Chile, Finland, France, Germany, Indonesia, Italy, Norway, Spain, Thailand, UK, US), while others have announced reductions in indirect taxes (e.g. India, UK), incentives to buy cars and appliances (e.g. Argentina, Brazil, Italy, Germany), or subsidies to basic goods (e.g. Indonesia, Malaysia, Mexico).

A tenet of the *American Recovery and Reinvestment Act*[7] is the expansion of social security benefits, by increasing spending on public health, unemployment and disability benefits, food stamps and other social security programs. Brazil and Mexico are expanding their cash transfer programs to millions of citizens[8], South Africa lowering retirement age and extending child benefits up to 18 years-old. Most governments announced plans to expand social security benefits for the population, such as strengthening unemployment benefits (e.g. Canada, France, Russia, UK, US), increased cash transfer programs (e.g. Brazil, Canada, Chile, France, Italy, Indonesia, Japan, Mexico, Philippines, South Korea, Thailand), housing support (e.g. Australia, China, Italy, Mexico, Spain, US), child benefits (e.g. Australia, Brazil, Germany, Mexico, South Africa, Spain) and pensions (e.g. Argentina, Australia, Canada, China, France, Philippines, Russia, Spain); or extending concessional loans to low-income citizens (Saudi Arabia). Some governments, like Taiwan Povince of China, have issued coupons for consumers valid at all wholesale and retail stores, a kind of basic income.[9]

(iii) Public Investment in Infrastructure: Virtually all countries are allocating large sums to infrastructure development. The People's Republic of China will focus most of its stimulus package in social infrastructure (low-income housing; sanitation, schools…) as well as economic infrastructure, including railways, highways, airports, upgrading of power grids, post-earthquake rebuilding.[10] In France, €11.1 billion (nearly half of the stimulus package) will be provided for direct state investment, including large state-run companies to improve rail and energy infrastructures and the postal service, higher education, research and improvement of state-owned properties.[11] Other countries are introducing incentives for development of environmentally friendly technologies (Canada, China, Germany, Poland, Portugal, UK, US).

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5 Argentina Law 26476 on Anti-Crisis Measures (R*égimen de regularización impositiva, promoción y protección del empleo registrado, exteriorización y repatriación de capitales)*.

6 *Plan Espanol para el Estimulo de la Economia y el Empleo, "Plan E"*, January 12 2009

7 *The US American Recovery and Reinvestment Act*, February 17 2009.

8 Mexico, *National Agreement in Support of Family Households* 7 January 2009.

9 *Special Statute for Distributing Consumption Vouchers for Revitalizing the Economy,* December 5, 2008.

10 *Premier Wen Jiabao Presides over State Council Executive Meeting, Decides on Ten Measures to Increase Domestic Demand*. Xinhuanet, Nov. 19, 2008.

11 *Loi 2008-1061 du 16 octobre 2008 de finances rectificative pour le financement de l'économie, Journal Officiel,* Oct. 17, 2008

II. ISSUES:

A. A country approach is inadequate: a global crisis requires global responses

This is a global crisis, the solutions must be global. No government can solve the crisis on its own, or isolate a country from its impacts. There is a need for coordinated international action, not just lead by the G-20, but a multilateral response in which all world countries are included. This coordinated international action should address global imbalances. The 21st century starts with large asymmetries caused by an unsustainable model of development. For instance, consumption is concentrated in upper income groups, a situation somehow similar to the pre-1930s crisis. Inequality has been growing among and within countries. According to the UN, in 2000, the richest 10% of adults accounted for 85% of total world assets; in contrast, the bottom half of the world adult population owned barely 1% of global wealth. [12] This raises serious questions on the adequacy of current development models (development for whom?). The US cannot continue to increase its debt and be the main driver of world demand; US deficit needs to be addressed, and a coordinated global expansion plan thought out.

The announced stimulus packages are a first country-based response, but more is needed. Particularly regulating the financial sector, given that the Asian crisis in the late 1990s and the present crisis are a result of an overinfluential and underregulated financial sector. Policies need to be coordinated, combined with regulatory measures, so stimulus packages are development-oriented and solve fundamental flaws of the system.

B. Developing countries will be hit hardly: the need for increased ODA

Stimulus packages have been announced so far in higher income economies, but, what happens to developing countries? Without increased aid, lower income economies will have limited capacity to engage in countercyclical stimulation.

Given this is a crisis generated by the "barons" of the financial sector in the North[13], a strong argument exists to compensate the South, particularly not to make taxpayers in developing countries pay for the mismanagement of Northern banks. Using words of President Obama, leaving governments the responsibility to finance their own stimulus plans implies that "main street" will bail out "Wall Street". Countries like Peru or Egypt have to take loans to respond to the consequences of a crisis they have not created.

Since 1970, the world's richer countries committed to spend 0.7% of their GNP in overseas development aid (ODA), but this remains at only 0.3% as an average. The current global crisis requires ODA to increase massively, preferably in the form of grants and concessional terms, accompanied by adequate monitoring mechanisms to ensure that aid is accountable to citizens.

The issue of quality of aid is as important as its quantity. Several OECD countries have announced willingness to increase capital at the IMF and development banks; however, governments in emerging economies strongly question the conditionalities that these institutions impose on borrowers and claim the need to reform the IFIs. In words of the Thai Prime Minister, *"When the G20 talks about reform of international financial institutions, it is not just a question of increasing capital, but also of how that capital is used…that means making sure there are new facilities for fiscal stimulus, continued*

[12] United Nations World Institute for Development Economics Research (2006) The World Distribution of Household Wealth. UN WIDER, Helsinki; United Nations (2005). The Inequality Predicament: Report on the World Social Situation 2005. New York: UNDESA

[13] Kemal Dervis, The Times, 20 March 2008. *"It is the super-bankers, hedge fund managers and owners of private equity firms that have become the new barons of 21st-century capitalism,"* the former Turkish finance minister, vice-president of the World Bank and UNDP head pointed "*40% of total corporate profits in the US in recent years went to the financial sector that in itself does not produce"*

development and social safety nets for developing economies... one of the lessons of the 1997 financial crisis in Asia was that the conditions enforced by the IMF had caused unnecessary pain".[14] Things have not changed much, for example, the Asian Development Bank announced in its 2008 Annual Meeting and ADB Strategic Framework 2020 that it would not invest on social protection –at a time when is most needed. Coordinated international action, including the world's 192 countries instead of only the voice of the G-20, is an imperative.

C. Content of stimulus packages: the need for redistribution

Many of the announced stimulus packages to revive economic activity have missed three points: (i) Banks will not lend while they fear interbank lending and try to improve their balance sheets; (ii) Investment in infrastructure –often, the major component of stimulus plans– has impacts only in the relatively long term; (iii) Lowering taxes and interest rates will not be effective while people are worried about losing their jobs, pensions and homes; likely, these will be put into savings and paying off debt, rather than consumption. Indeed it would be quite indefensible to encourage people who have been induced to borrow beyond their capacity to service debt to borrow even more – or to do anything other than pay down their debts to a more sustainable level.

How well thought out are current stimulus plans? In general, policymakers worldwide have underestimated the depth and breadth of the financial crisis, and their decisions have often resulted in myopic (and expensive) quick fixes. It is interesting to observe that policy-making in developing countries has been paralyzed in recent years because of the claimed need of "evidence-based policies"; many public programs such as social security were stopped because of pilot approaches to evaluate what may be best. However, now politicians are taking fast decisions with no clear evidence whether their trillion dollars expenditures will work. And most of it is going to bailing out financial institutions, or to infrastructure, instead of people. A much greater part of the money should be allocated for cash transfers to consumers, which would quickly stimulate demand in the economy, as well as alleviating poverty.

Stimulus packages should not be about patching-up policies to return to what the world was (so the poor return to be as poor as they were?). What it brings is the need to bring redistribution to the policy agenda. This is mostly an ideological problem, decades of neoliberalism have discouraged redistribution, but there are many arguments for it:

- Inequality is economically inefficient/dysfunctional
- The world suffers a problem of overproduction and global excess capacity in the context of weak effective demand
- Consumption is concentrated in top income deciles in all countries (how much can the rich consume?)
- Raising the incomes of the poor will increase domestic demand and, in turn, encourage economic growth by expanding domestic markets
- Huge disparities in income inequality encourage uncontrolled migration
- Reducing poverty and inequality can be effective to prevent conflict, terrorism and create politically stable societies

Redistribution can be an effective instrument to boost economic growth by raising domestic demand/internal markets; enhance human capital and productive employment (a better educated and healthier workforce); and promote political stability and nation-building, ensuring the electoral support of citizens.

The 1929 financial crash led to a New Deal (Box 1). Before and during the Depression, poverty was widespread in "developed" countries. The financial crisis in the 1930s gave the political will to expand social security systems (making systems universal, for all),

[14] Financial Times, 15 March 2009

provide social assistance for the poor, employment and rural programs in many countries. The same opportunity exists today in developing countries. Some governments have already started to expand cash transfers programs, even consumer vouchers programs. These are correct moves, to be encouraged in other world countries.

BOX 1: THE US NEW DEAL (1933-)
MAIN POLICIES:

- Bank reforms
- Social Security Act (1935)
  - Universal old-age pensions
  - Unemployment insurance
  - Social assistance for poor families and persons with disabilities
- Employment programs (public works), collective bargaining, minimum wages
- Farm/rural programs

A developmental approach to Southern countries is particularly important. It is necessary to ensure that funds serve as stimulus for poor communities in developing countries, having a multiplier effect at the national and regional level. For example, it would be particularly desirable to channel expenditure on staple foodstuffs to local or regional producers rather than (typically subsidized) imports from developed countries, especially bearing in mind the predominance of the rural sector in most low income countries.

D. Speed matters: responses have been slow, people are going to die

The impacts of the crisis are just starting. The world is going to experience an increase in unemployment, poverty and hunger. Pensions are under severe strain because of the collapse of capital markets. People around the world already have lesser access to social services, benefits, remittances and credit. The crisis is going to have severe negative social impacts. According to the World Bank, 45 million people will fall under extreme poverty and as a result 400,000 children will die in 2009; this comes on top of the vulnerability created by the food and energy crisis, which pushed more than 130 million people into poverty in 2008.

No lessons were learnt from the 1997/98 Asian Crisis:

- Responses to social consequences of the Asian crisis were temporary safety nets, too little and too late.
- There were no early warning systems, neither social protection systems in place, this had a high toll on populations.
- Malnourishment, morbidity and mortality rates grew, not yet recovered a decade after. In children, hunger left a generation of children stunted and malnourished, a huge social debt.
- Violent riots erupted (e.g. xenophobic pogroms against Chinese communities in Indonesia, in other countries against migrant workers) in which thousands were killed.
- When governments and donors realized that social investment was urgently needed, it mostly went to temporary safety nets. Temporary safety nets absorbed lots of funds, but left nothing behind. In 2007, when the 10 year anniversary of the Asian Crisis was held, there was no mention of social issues, because the large amount of funds spent on temporary safety nets did not leave any system in place.
- The World Bank reported that 40% of funds going to emergency social safety nets in Indonesia disappeared in corruption, as is normally the case with emergency aid, where no governance checks and balances exist.
- It was a lost opportunity for Asian populations; now they could enjoy social security systems to assist them in this crisis.

This is an economic tsunami coming, we know that people are going to suffer –and die. There is an urgent need for a coordinated expansionary global stimulus package, in which social protection has a strong role in all countries to increase domestic demand and reduce poverty.