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**Post-Crisis Growth in Developing Countries**

**A Special Report of the Commission on Growth and Development on the implications  
of the 2008 financial crisis**

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I had the privilege to contribute to the Commission on Growth and Development, led by Professor Michael Spence, with my experience from Central Europe's transition to the market economy and that of member of the European Commission in charge of European regional policy. A policy whose main objective is to enhance growth from below.

European regional policy is an investment policy which catalyzes new investment patterns, mobilizing local and regional development potential, and facilitates catching up of processes in the EU as there are still huge development disparities.

The policy has been an important part of the European recovery package, providing a short term boost to demand and an investment in long term competitiveness.

I would like to share with you a few observations from my experience in the context of *real* economy crisis. This crisis can not be discounted from the long term development.

First of all, we should therefore think twice before we abandon growth strategies and policy choices that were agreed upon before the crisis hit. It hit

the global economy in a time of many pending reforms and structural transformations such as the fight against poverty under the Millennium Development Agenda, the reflection process on global governance, new emerging approaches to development aid, and climate change related policies.

But also it hit when many national growth strategies have been agreed which have taken those challenges into account. The crisis can be an excellent opportunity to look at all those reform strategies and policies, adapt or revise them, but not necessarily to abandon them. Actually, crisis is the time for reform and restructurizing. There is no doubt that there is much to be done globally, because we are in a "development emergency". But national and local policy choices matter.

Secondly, there is no doubt that the crisis is real; people lost their jobs, their homes, their savings, and their hopes. In everything we do now, we have to ask ourselves: how did we get where we are? But it is important to take note of the fact that the crisis hit the world when it already was in a turbulent state due to successive food, fuel, and climate change related shocks. We must take all those factors into account when working on an exit strategy to avoid or reduce the risk of structural aftershocks.

Thirdly, maybe it is legitimate that due to slowing growth, rising unemployment, and falling or relapsing into poverty, gains of previous decades are in jeopardy of being lost, there is a temptation to look inwards. Turning inwards, however, would be a historical mistake because the crisis does not wipe away the interdependence between all of us, the more as well as the less developed. The interdependence of economy, prosperity, security, and values will stay with us.

In practical terms it also means that recovery in some economies will drive recovery in others, or even worldwide. Global interdependence is also an opportunity to get out of the crisis smarter and stronger. This opportunity of exploiting the interdependence will work only for those who will stay open. Protectionism is a dead end street: at the end of the day it only hits back.

Fourth, I would like to stress that the crisis can not be disconnected from the long term development agenda - both globally and nationally. Exit strategies must focus policy choices on long term sustainable development. That means that the challenge should not be to aim only at eliminating production gaps: keeping productivity gains on track is also important. Measures boosting demand do not necessarily enhance long term transformation. While they are usually very conservative, they do have a direct impact on public budgets and deficits. These fiscal measures can also have an impact on investment and growth patterns, and we may not have to worry about paying back the borrowing if the growth that it generates is sustainable. Therefore, massive fiscal support and borrowing could prove to be a foundation for a new crisis unless it truly lays foundations for sustainable jobs, growth, and competitiveness.

My fifth message is that today it is not the crisis as such but the way we get out of it which should be our major concern. We know the channels of impact. We know about the direct impact of the financial crisis on developing countries through private capital market flows, in particular FDI, and through remittances, which contribute to large parts of GDP in many LDCs.

We know about the impact of the contraction in global trade and shrinking export revenues leading to reduced imports and growing financing gaps. We know that governments have difficulties in maintaining levels of social expenditure and public investment in infrastructure or schools.

We know that what matters most is the capacity to cope with impacts. This ability varies significantly across developing countries, both with respect to growth support measures and the cushioning of crisis impacts. The real challenge is to have appropriate exit strategies and the capacity to implement policies avoiding devastating short term impacts and allowing to go the distance. Striking the right balance between supporting growth and cushioning social impact may not be easy but additionally synergies between the two

should be fully exploited. Smart governance remains key, which has been already emphasised in our core Report of 2008.

My sixth point is on development emergency. Global efforts to fix the financial sector and system are highly relevant to developing countries, but there are many of them that will indeed "slip through the cracks" of global solutions. They risk missing new opportunities due to their excessive vulnerability and limited resilience capacity. Therefore, I feel that tailor-made aid is needed. The real challenge is to relaunch growth. This is what we said in our core report, as soon as possible and as much of it as possible. This depends on current work on new national and global regulation, but we can not regulate our way out of the crisis. It also depends on current policy choices, we must avoid getting stuck in the past. It depends on how strong risk aversion will be among business and banks - hopefully we will not regulate out 100% of the risk. It will also depend on how efficient fiscal regimes will be in terms of tax collection. After all, this represents the money that we will need to use to pay the newly incurred debts. For all that we need smart governments and a new public-private partnership deal.