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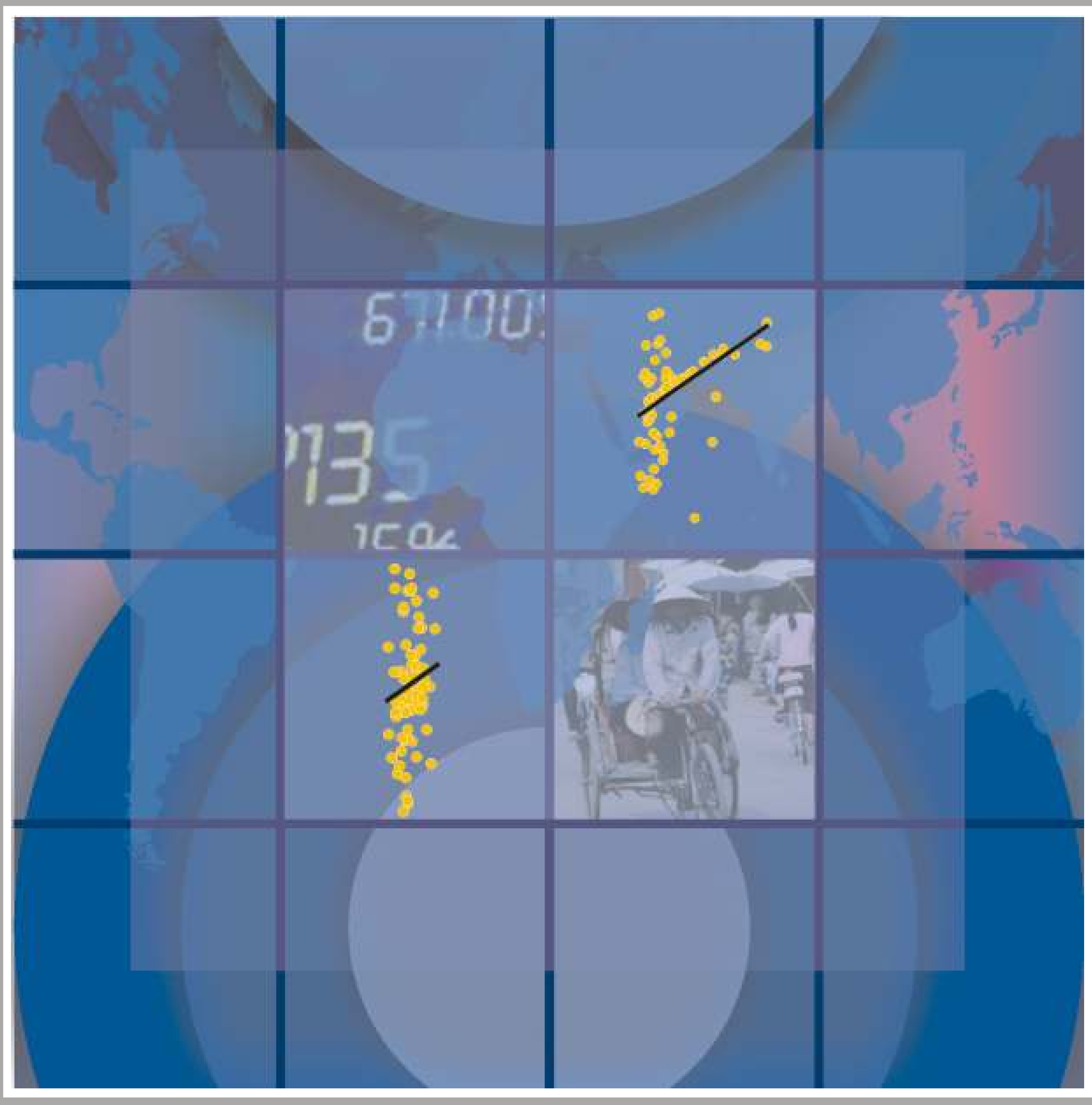
UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

TRADE AND DEVELOPMENT REPORT, 2004

OVERVIEW

UNITED NATIONS



UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT
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TRADE AND DEVELOPMENT REPORT, 2004

Overview

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UNCTAD/TDR/2004 (Overview)

OVERVIEW

Global trends and prospects

The situation of the global economy is brighter than it was a year ago. Since growth in world output and trade recovered in 2003, there is now widespread optimism that the acceleration of growth in 2004 could lead to a return of the performance experienced at the end of the last decade and that the world economy may enter an extended period of growth.

In reality, however, the outlook for a sustained recovery is more clouded and uncertain than at the beginning of the 1990s. Large disparities in the strength of domestic demand persist among the major industrial countries, and increasing trade imbalances between the major economic blocks could lead to new protectionist pressures and increase instability in currency and financial markets, with adverse implications for developing countries. The sharp increase in oil prices and uncertainty about their future development, as well as their possible impact on inflation and interest rates, are an additional reason for concern.

Moreover, income growth is unequally distributed both among developed countries, where the euro area continues to lag behind, and among developing countries, where fast and sustained growth continues to be concentrated in East and South Asia. At the same time, per capita income in most of sub-Saharan Africa is stagnating, and the basis for sustained growth in Latin America is still very fragile. Indeed, the improvement in the global economy has been the result of exceptionally good performance in a small number of countries, with great variations in the spillover effects on other economies.

The recovery of the world economy has been driven largely by the United States economy and continued fast expansion in East and South Asia. Through its increasing fiscal and trade deficits, the United States economy has provided a strong demand stimulus to the rest of the world. On the other hand, several developing economies in Asia, in particular China, have been able to increase not only their imports – with strong spillover effects in economies in the Asia and Pacific region – but also their exports at double-digit rates.

The dependence of the global economy on the performance of the United States economy is not a new phenomenon, but United States deficits are much larger today than they were in the late 1990s. This is a matter for concern, since the high budget deficit of the United States will require fiscal adjustments and the unusually expansionary monetary policy stance may also need to be revised in light of inflationary pressures stemming from a surge in import prices and in particular from oil prices.

Geopolitical tensions and speculative forces explain much of the sharp rise in oil prices, which during the first half of 2004 reached their highest level since the early 1990s, but the rise has also been driven by the global recovery and rapidly rising demand from China. Substantially higher oil prices carry the risk of compromising growth in oil-importing countries, especially those in the developing world that are facing serious balance-of-payments and external financing constraints while benefiting to a relatively small extent from potentially higher exports to oil-exporting countries. Moreover, as in past episodes of rapidly rising oil prices, the oil-exporting countries may not be able immediately to translate additional oil revenues into higher demand for goods produced in oil-importing countries. Although higher oil prices have not had an immediate impact on inflation in the industrialized countries, such an effect cannot be ruled out should prices remain at current levels in the medium term. This in turn might lead to increases in interest rates.

Greater financial and exchange-rate instability may also result from the fact that the United States is increasingly immersed in trade-financial dynamics with East Asia. Expansionary fiscal and monetary policies in the United States have been providing a significant boost to exports from East Asia, including Japan, and are contributing to the large current account surpluses in the region. On the other hand, the East Asian developing countries have been following a policy of keeping their exchange rates at a competitive level following the currency depreciations in the late 1990s. This has required heavy intervention in the foreign exchange market, leading to fast reserve accumulation. As a result, East Asia has been recycling its current-account surpluses directly to the United States, thereby financing a large part of the United States current-account and budget deficits through the investment of increasing foreign exchange reserves in United States Treasury securities. In 2003, East Asian developing countries, including China, bought more than $210 billion of foreign currency, compared to a United States budget deficit of $455 billion and a trade deficit of $490 billion. This pattern is unlikely to be sustainable in the long run, especially if pressure on the dollar to depreciate mounts as a result of further rising United States deficits, which, in turn, could induce Asian central banks to minimize risks by diversifying their foreign exchange holdings into assets denominated in other currencies, in particular the euro.

Because of the recycling of balance-of-payments surpluses of the East Asian and a number of other developing and transition economies through an unprecedented increase in reserve accumulation in 2003, there has been a continued net capital outflow, in the order of $230 billion, from developing and transition economies to the developed countries. This has occurred despite a substantial rise in the net inflow of private capital to the developing and transition economies, which has reached its highest level since 1997. On the other hand, although foreign direct investment (FDI) remains the most important type of private capital inflows to developing countries, it fell to its lowest level since 1996 as the wave of privatization, which had been a driving force behind FDI during the 1990s, levelled off. Conversely, credits and short-term capital flows rose considerably, but the bulk of these flows were directed to a small number of emerging-market economies, attracted by high interest rates or the expectation of currency appreciation. Indeed, a substantial proportion of private external financing did not flow to economies with external financing needs or low investment rates. Instead these flows were mainly directed to economies with often sizeable current account surpluses resulting from fast export expansion, adding to their foreign exchange reserves. This is another indication that capital markets cannot be counted on as a stable source of development finance. Moreover, the obvious fear of many developing countries with regard to floating their currencies in the presence of sharply fluctuating expectations on the international financial markets should give rise to increased efforts to strengthen the coherence between the international trading system, on the one hand, and the international monetary and financial system, on the other, an issue that is taken up below.

With East and South Asia forming a de facto dollar block, adjustments of global imbalances may require more pronounced exchange-rate changes in the rest of the world. In order to maintain the growth momentum in the world economy without constantly growing United States deficits and mounting pressure on the dollar, demand growth would need to be strengthened in the other major industrial countries. However, growth in most European economies continues to be itself dependent on exports. The euro area has benefited from the recent United States recovery, despite the appreciation of the euro vis-à-vis the dollar, confirming the competitiveness of its industries, but domestic demand remains sluggish, mainly due to the inability of economic policy to lift the income expectations of consumers in the three largest economies. Without a reorientation in the euro area away from fiscal and monetary orthodoxy, the rising imbalances in world trade will force further and even more dramatic changes in real exchange rates.

Regional trends and the new geography of trade

An exceptionally strong fiscal stimulus and a reduction of interest rates to their lowest level in 50 years have helped the United States economy overcome the phase of weakness that began in 2000. Rising government expenditure due mainly to a surge in defence spending, higher company profits that finally led to the long-awaited rise in business investment, and a recovery in household consumption all converged to produce a substantial rise in domestic demand. By contrast, despite the weakening of the dollar vis-à-vis the euro and the yen in 2003, external demand grew at a much slower rate than imports. The large and rising trade deficit thus remains a major concern, as it is likely to exert further downward pressure on the dollar.

Moreover, given the size of the United States budget deficit, fiscal policy will need to adopt a more restrictive stance, and a switch towards a more restrictive monetary policy would aggravate the high indebtedness of households, which could prove to be a major obstacle to sustained expansion. There are thus serious doubts that United States growth and its positive impact on the world economy will continue with the same strength as has been the case during 2003 and the first half of 2004.

In the euro area, domestic demand has remained flat. The European Central Bank was reluctant to follow a more aggressive expansionary policy. Despite slower growth, real short-term interest rates in Europe have been consistently higher than in the United States, while the space for expansionary fiscal policies is restricted by the Stability and Growth Pact. This is in contrast to the United Kingdom, where countercyclical fiscal policy in response to the global slowdown after 2000 contributed to considerably higher growth rates than those in continental Europe. The current attempt of many European companies to improve their international competitiveness by cutting wages will aggravate the weakness of domestic demand. Eventually, as the financial markets realize that the world economy is not receiving the stimulus needed to overcome the existing imbalances, the probability of a strong overvaluation of the European currency will rise significantly. In this case, the euro area and its major trading partners will run the risk of being trapped in a low-growth, high-unemployment scenario.

After a decade of stagnation, the Japanese economy finally achieved considerable recovery of output growth in 2003. Although there has been a rebound of corporate investment, the recovery was largely based on higher external demand. While exports to the United States fell in 2003, the export drive was mainly due to continued strong demand from China, suggesting a change in trade patterns within Asia and between Asia and the United States. However, given the strong reliance on foreign demand, the Japanese export-led recovery is vulnerable to changes in external conditions, particularly currency fluctuations.

GDP growth in the developing countries rose in 2003 and is likely to do so again in 2004. While growth has accelerated in a large number of developing countries, its level differs considerably across and within regions. Growth has been the strongest in East and South Asia, as a result of further expansion of domestic and external demand, and it is set to accelerate further in 2004. Economic policy in most countries of the region has maintained an expansionary stance through public investment in infrastructure development and the creation of favourable monetary conditions. The stability of exchange rates within the region, together with significant growth of investment and GDP, has favoured the trend towards specialization in the context of rapidly growing intraregional trade and investment.

China is playing a central role in this process. Indeed, in 2003 and the beginning of 2004, it was a major engine of growth for most countries in the region. A large proportion of its imports, which have been growing even faster than its exports, are coming from the rest of Asia. In 2004 rapid growth is likely to continue in East and South Asia, and particularly in the two largest economies, China and India. However, in China there is now overheating in certain sectors of the economy, and the policy stance is becoming more restrictive, with attendant effects on other countries in the region, including Japan.

Although exports to the United States continue to be an important component of total output growth in East and South Asia, this region has generated an intraregional pattern of demand and specialization that should allow it to maintain a relatively stable growth path independent of cyclical and structural problems in the rest of the world.

After two years of negative per capita growth, economic activity in Latin America began to improve in the second half of 2003. Several countries have regained international competitiveness and have increased their room for manoeuvre in macroeconomic management by shifting away from rigid exchange rate regimes and overvalued currencies. While improved trade balances in 2002 were largely the result of import compression, further improvement of trade performance in 2003 was mainly due to a rise in exports, stimulating economic recovery. Although for the region as a whole growth is expected to accelerate further in 2004, serious obstacles to a return to high and sustained growth rates in Latin America persist. Despite improved monetary conditions, in several countries fixed capital formation has fallen to its lowest level in decades. The new policy initiatives taken in some of the major economies in the region could lead to a more sustainable recovery if they succeed in stimulating domestic demand. In order to achieve a substantial recovery of both investment and private consumption, it will be necessary to ease the public debt burden, reform fiscal structures in some countries, and enhance the supply of domestic credit at lower interest rates than in the past, as well as achieving a more equitable distribution of income.

The African continent benefited from the recovery in the world economy less than other developing regions. The moderate rise in African growth was driven by higher prices of primary commodities. Growth in North Africa increased substantially as a result mainly of improved weather conditions, higher oil prices and a revival of tourism, whereas in sub-Saharan Africa, where poverty and social deprivation continue to take their greatest toll, real GDP growth remained sluggish, implying a further stagnation of per capita incomes. Given the severe financing constraints of most sub-Saharan economies, investment rates remain too low to achieve the required degree of diversification into higher value-added production and more dynamic products in international markets that would allow for faster integration into the world economy and a reduction of the persistent vulnerability of the region to external shocks. The required rise in the level of both public and private investment cannot be achieved by relying on domestic savings and private capital inflows. Debt relief and the additional provision of official development assistance in the form of grants are indispensable for alleviating poverty and improving social conditions in these countries. In light of the persisting weakness of per capita income growth, it now appears increasingly unlikely that sub-Saharan Africa can attain the Millennium Development Goals, in particular that of halving poverty by 2015. In most countries, growth would need to be doubled and sustained over a decade in order to meet those goals.

The transition economies of Central and Eastern Europe also registered higher growth rates in 2003, and their GDP should accelerate again in 2004, thanks to higher exports and strong domestic demand. In the countries members of the Commonwealth of Independent States, growth was strongly supported by considerably higher revenues from oil exports. European Union enlargement and the relocation of activities to the low-wage transition economies are facilitating their closer integration into a new division of labour on the continent.

The processes that have led to the recovery of the world economy and the regional growth patterns in the developing world confirm the importance of proactive fiscal and monetary policies. The economies that provided growth stimuli to the rest of the world were those where monetary and fiscal policy supported domestic demand growth. This is true for both developed and developing countries. Moreover, a competitive exchange rate can play a decisive role in forestalling external constraints and creating policy space for monetary easing.

The introduction of a large number of security-related measures since late 2001 is likely to have an adverse impact on the cost of trade and the movement of goods, in particular from developing countries. Nevertheless, world trade expanded significantly in 2003 and the first half of 2004, but unlike the second half of the 1990s, when rapid trade expansion was mainly the result of increasing export volumes, two thirds of trade growth in 2003 was on account of a surge in the dollar unit value of exports. Trade expansion was driven by the recovery in the United States and the phenomenon that has come to be called the “new geography of trade”. Developing and transition countries have played a more important role in the expansion of world trade than ever before: in 2002 and 2003, they accounted for around three quarters of the increase in export volume and for 60 per cent of the increase in import volume. This reflects the increasing relocation of manufacturing production to some regions, especially East and South Asia and the transition economies of Central and Eastern Europe, as well as the international pattern of demand growth. Indeed, a number of developing countries, especially in East and South Asia, have become important markets for a wide range of manufactures and commodities, while expanding their own manufacturing industries at a very rapid pace. Consequently, their growth is more energy-intensive and requires more primary-commodity inputs, such as metals and agricultural raw materials, than growth based on an expansion of the services sector. Moreover, given the size of these countries in terms of population, the demand for food products has been expanding vigorously.

Commodity prices in current dollar terms rose for the second consecutive year in 2003 as a consequence of higher demand, particularly from the rapidly expanding Asian economies. However, as the dollar prices of manufactures exported by developed countries also rose, overall commodity terms of trade did not improve, and for some commodity groups they even worsened. Moreover, the development of commodity prices quoted in dollars has to be seen against the depreciation of the dollar against other major currencies. For many large consumers, the rise in dollar prices has been offset by these exchange-rate movements, and the export earnings of commodity producers whose currencies are pegged to the euro, in particular the African commodity producers in the CFA zone, have been negatively affected. Moreover, the situation in financial and currency markets has also increased speculative demand for commodities, and this may be reversed as the conditions in international financial markets change. In any case, in real terms non-oil commodity prices still remain at very low levels and considerably below their level of the early 1980s.

Policy coherence, development strategies and integration into the world economy

Since the mid-1980s, many developing countries have made close integration into the international trading system a pillar of their economic reform agenda. They have sought to achieve this not only through active participation in multilateral trade negotiations, but also through rapid unilateral trade liberalization. In many countries, this has been accompanied by an opening up of their financial sector and capital account. To date, this strategy – which may be called the "openness model" – has not enabled most developing countries, with some notable exceptions such as Chile, to establish the virtuous interaction between international finance, domestic capital formation and export growth that underpinned the catching-up process of Western Europe after the Second World War and of the East Asian newly industrializing economies (NIEs) as from the 1980s.

A feasible development agenda requires a more complex analytical and policy framework than that offered by the "openness model". A fundamental question is how to reinforce coherence between national development strategies and global processes and disciplines, as well as policy coherence among and within the various sectors of the global economy that impact on development prospects of developing countries. Of particular importance is the interface between the international trading system and the international monetary and financial system.

Openness, integration and national policy space

A coherent treatment of the interdependence between trade, macroeconomic and financial issues was an important element in the debate leading to the post-War international economic system. The set-up of the post-War international trade regime was predicated on the belief that, in conditions of strictly limited private international capital flows, an international monetary system with convertible currencies at fixed, but adjustable, exchange rates would provide a stable environment conducive to trade and investment. Under the aegis of the General Agreement on Tariffs and Trade (GATT), this regime considered tariffs as the only legitimate trade policy measure. The adopted exchange rate regime supported the GATT approach, as participants in international trade negotiations could predict the full extent to which the competitive position of domestic industries would be affected by tariff cuts without having to be unduly concerned about other exogenous factors.

The specific problems of developing countries participating in the post-War international trading system were largely absent from the mandates of the intergovernmental institutions created immediately after the Second World War. This was despite the fact that, with international private capital flows constrained and official development assistance still limited (and often tied), the role of international trade was attracting increasing attention as a dependable means of removing the resource constraints on economic growth in developing countries. Multilateral efforts at designing a trading system that would take account of the policy options of developing countries, for which slow growth and adverse terms-of-trade movements were distinctive features, culminated in the First United Nations Conference on Trade and Development in 1964. The Report to the Conference spelt out a strategy designed to help poorer countries develop outwardly through strong capital formation and continuing and accelerated expansion of exports – both traditional and non-traditional. Central to that agenda was the idea that developing countries can base economic development on their own efforts only if they have sufficient policy space to accelerate capital formation, diversify their economic structure and give development greater "social depth". This agenda also emphasized the interdependence between trade and finance, given that, particularly in the early stages of industrialization, imports would almost certainly grow faster than exports, and financing the gap would be key to accelerating growth.

The need for coherence between the international trading system and the international monetary and financial system has gained in importance with the abandoning of the system of fixed, but adjustable, exchange rates and the adoption of widespread floating, combined with a return of private international capital flows to levels similar to those that had caused much economic and social instability in the inter-war period. In particular, the liberalization of capital movements has, on balance, had little impact on levels of development finance, and the balance-of-payments constraint of developing countries has not been removed. Rather, there has been a de-linking of financial flows from international trade. This is most clearly the case with short-term flows, where over 80 per cent of transactions relate to round-trip operations, motivated by hedging, arbitrage and speculative considerations. Moreover, the increased level and volatility of short-term private international capital flows, associated with the often sharp swings in exchange rate expectations of international investors, have an adverse bearing on the principle of non-discrimination in trade and on developing-country trade performance.

Thus, an evaluation of the functioning of the international trading system should take account of the way in which its rules have been modified to deal not only with changes in international trading relationships, but also with international monetary and financial relationships that have an impact on trade.

Fostering coherence between the international trading, monetary and financial systems

An important lesson from the experiences of countries that combined successful integration into the world economy with sustained growth is the critical role of active and well sequenced policies to augment the stock of physical and human capital, enable the use of more efficient technologies, and shift resources away from traditional, low-productivity activities towards activities that offer a high potential for productivity growth. Under some circumstances, and particularly when a period of real currency appreciation has hampered export performance, real currency depreciations can improve international cost competitiveness and boost exports.

One condition for successful trade performance is that developing countries are able to manage their exchange rates in a way that allows them not only to sustain competitive rates over the longer term, but also to retain enough policy space to be able to make orderly adjustments when faced with exogenous shocks. The post-War institutional set-up had thought to achieve this through the creation of an international monetary system on an intergovernmental basis with convertible currencies at fixed, but adjustable, exchange rates and strict limitations on private international capital flows. However, partly due to the liberalization of capital flows in the last 30 years and to the sizeable increase in the scale and variety of cross-border financial transactions, whose direction can change rapidly in response to shifts in expectations of international portfolio investors, the currencies of financially open developing countries have been subject to strong volatility and gyrations. Such volatility has frequently contributed to problems in managing interest rates and exchange rates and to financial crises, including in countries with track records of macroeconomic discipline. These currency movements have often been characterized by prolonged periods of exchange rate appreciation followed by abrupt and sharp devaluations.

Given that real currency depreciations can generally be expected to improve a country's trade balance, it could be assumed that sharp depreciations of the real exchange rate will provide an even greater impetus to the international cost competitiveness of domestic exporters and a boost to a country's exports. However, effects that accompany large depreciations of the real exchange rate can, at least in the short term, seriously compromise the ability of domestic exporters to benefit from their increased international cost competitiveness stemming from the depreciation.

Such effects can occur at two levels. At the level of individual enterprises, nominal exchange rate changes can have a major impact on investment and international competitiveness, as they affect the instruments that firms can use to foster international cost competitiveness in a sustainable way. Firms may not be able to benefit from sharp real currency depreciations if the goods that they export have a high import content, so that the net effect on their international cost competitiveness is small. More importantly, recent experience shows that sharp real currency depreciations can compromise the ability of firms to expand production capacity or even maintain production at pre-depreciation levels. This is so because the easing of capital controls will have seriously compromised the availability of trade finance from international sources in the aftermath of sharp currency depreciations. Moreover, the tightening of domestic monetary conditions associated with the depreciation has often made it difficult for domestic lenders to maintain their provision of short-term credit.

With regard to effects at the macroeconomic level, discussions on the impact of exchange rate changes on trade flows have frequently emphasized the effect of exchange rate volatility on trade, or the contribution of currency depreciations to the removal of temporary imbalances in a country's current account. Typically, the focus has been on the impact of exchange rate changes that are relatively small, whereas since the early 1990s developing countries' real exchange rates have frequently undergone large gyrations, adding an additional dimension to the traditional debate for at least two reasons. First, sharp exchange rate changes in one economy can adversely affect the external trade position of other economies where the exchange rate remains relatively stable. For example, evidence from the Asian crisis points to competitive depreciations as an important form of contagion through trade linkages, as countries whose exporters compete directly with those in the crisis-affected country also face pressure to depreciate their currencies in order to avoid a loss in international competitiveness. This also means that exporters in the crisis-affected country do not experience the rise in demand for their products hoped for.

Second, the domestic impact of a sharp and abrupt exchange rate depreciation is more complex than the adjustments resulting from small exchange rate fluctuations, because sharp currency depreciations are typically associated with a drop in domestic economic activity and a need to cut imports of intermediate and capital goods. Combined with the sharp decline in the availability of trade finance, this is likely to hamper the domestic supply response. Thus, while the trade performance of developing countries generally improves after "normal" depreciations, major real currency depreciations do not generally result in proportionally larger improvements, as they tend to undermine the ability of exporters to take advantage of the rise in international cost competitiveness.

In effect, volatility in international financial markets and particularly in short-term private capital flows can reduce international competitiveness and the profit incentive for investors to undertake productivity-enhancing investment in developing countries. Hence, there is inconsistency in the policy advice that encourages developing countries to adopt rapid financial liberalization and yet to increasingly rely on productivity-enhancing investment to strengthen their competitiveness for improved trade performance.

Existing modalities in the multilateral trading system do not address the problems of trade performance that originate in the monetary and financial system. Moreover, there are no mechanisms under the existing system of global economic governance for dispute settlement or redress regarding these impulses. One possible solution could be a review of the balance-of-payments provisions of the GATT. Otherwise, developing countries that have liberalized their capital account at an early stage of their integration process may have to adopt measures to limit the impact of private capital flows on exchange rate movements that adversely affect their trade balance and the international competitiveness of their exporters.

The changes required in the international trading, monetary and financial systems to enable a more equitable distribution of the benefits from international trade and to maximize the developmental effects of globalization for developing countries call for an integrated treatment of trade problems and the increasingly interlinked issues of development and overall payments balances. Decisions on the international monetary and financial system should not be circumscribed by narrow monetary and financial considerations, but should take account of the fact that they have a strong and lasting impact on the real sectors in both developed and developing countries.

Measures at the national level cannot substitute for appropriate trading, monetary and financial arrangements. Nevertheless, avoiding currency overvaluation has become the chosen strategy of an increasing number of developing countries. East Asian countries pioneered this approach. They did not apply the "open capital market strategy" at an early stage of their catching-up process and tried to avoid dependence on foreign capital flows. This gave them the possibility of simultaneously managing the real exchange rate, a key determinant of exporters' international cost competitiveness, and the real interest rate, a key determinant of domestic investment.

Managed floating, however, faces an adding-up problem at the global level. Not all countries can simultaneously manage the movements of their exchange rate and achieve their targeted rates. The exchange rate is, by definition, a multilateral phenomenon, and attempts by many countries to keep their currencies at an undervalued rate may end up in a race to the bottom – or in competitive devaluations – that would be as disastrous for the world economy as the experience of the 1930s. Moreover, given the size and inherent volatility of international short-term capital flows, only those developing countries that are big and competitive enough to withstand strong and sustained attempts of the international financial markets to move the exchange rate in a certain direction will be able to manage the floating successfully. A small and open developing economy will hardly be able to continue fighting a strong tendency for its currency to appreciate over a longer period of time.

Since exchange rate policies have the same international dimension as trade policies, multilateral or global arrangements similar to those of the multilateral trading system would be the best solution to this problem. Indeed, the main idea behind the establishment of the IMF in the 1940s was to avoid competitive devaluations. In a well-designed global monetary system, the advantages of a currency devaluation in one country have to be balanced against the disadvantages for the others. As changes in the exchange rate that imply deviation from purchasing power parity affect international trade in a way comparable to tariffs and export duties, such changes should also be governed by multilateral regulations. Such a multilateral regime would, among other things, require countries to specify their reasons for real depreciations and the dimension of necessary changes. If such rules were strictly applied, substantial changes in the real exchange rate of individual countries could be avoided.

In a world without a multilateral solution to the currency problem, the only way out for high-inflation or high-growth countries that are not members of a regional monetary union is to resort to controls on short-term capital flows or to follow a strategy of undervaluation and unilateral fixing. If developing countries are able to prevent destabilizing inflows and outflows, either by taxing those flows or by limiting their impact through direct intervention in the market, the hardest choices and misallocations due to erratic exchange rate changes may be avoided; but resort to controls or permanent intervention should not replace the search for an appropriate exchange rate system at the regional and global levels.

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Secretary-General of UNCTAD