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SOME CONSIDERATIONS CONCERNING ETHICS IN FINANCIAL GLOBALISATION

JOSÉ T. RAGA GIL

First and foremost I would like to start by both thanking and congratulating Prof. Malinvaud for his very perceptive ethical reflection on a subject as complicated as international financing, in the context of the freedom of movement of capital and in a world where great inequalities between countries exist. Accordingly, the purpose of this paper is to recognize the content of his presentation, while adding one or two thoughts which, if they serve any purpose, it will be merely to support the ideas expressed in the main document.

Adopting the classification of countries that Professor Malinvaud uses in his excellent contribution, one which I fully agree with, I will focus on the financial flows to developing nations, above all those poor countries where the problem facing us exists most starkly. I will not therefore refer to industrialized countries, since I consider that the contractual relationship, both as regards giving and receiving financial resources, takes place between equal parties, even where such a relationship is between a given state and an international body like the International Monetary Fund or the World Bank. That relationship, on the basis of equality and the great number of financial opportunities that often exist between industrialized countries, makes those ethical problems in the contractual relationship, a particular cause for concern for the Church and the Academy, of little importance.

The problems arise when we turn to poor countries, that have poorly developed financial structures, where indeed they exist at all, and therefore find it very difficult to gain access to wide financial markets where they can defend their interests, choosing between various alternatives. Countries that, moreover, urgently need to escape from the poverty in which they are ensnared, having to face the challenge of being in a weaker bargaining position, which, in most cases, will lead them to accept contractual conditions that damage their economies, obliging them to continue in the so-called poverty spiral.

We underline this inequality between the parties, that exists between lender countries (industrialized countries and international financial bodies) and borrower countries (poor countries), because, in these cases, as is laid down in the Social Doctrine of the Church, freedom to contract is not sufficient to guarantee justice in the conditions of such contracts. On this point, Pope Paul VI said:

> ... if the positions of the contracting parties are too unequal, the consent of the parties does not suffice to guarantee the justice of their contract, and the rule of free agreement remains subservient to the demands of the natural law ... an economy of exchange can no longer be based solely on the law of free competition, a law which, in its turn, too often creates an economic dictatorship. Freedom of trade is fair only if it is subject to the demands of social justice.[1]

Here then is the root of our concern in a world where, not without certain fallacies, the flag of freedom is draped over intentions that would not meet the lowest standards of justice or are even consistent with the freedom that is proclaimed.

An initial distinction

When we refer to international financing and, above all, when we consider this scenario of inequality, it is worth distinguishing between financing directed at the productive sector (which can be broken down between financing for activities in the private and in the public sector) and that which is carried out, generally directed at the public sector, to finance the public activities of the government of a country.

In the *financing of productive activities*, above all if they are carried out in the private sector of the economy, there are, in principle, less ethical concerns. The first reason for this is that the parties that have negotiated the loan have done so, even from a position of inequality, in such a way that situations of alarming injustice are usually eliminated. In some cases, this is because they are multinational entities, with their bargaining power, which receive the loans, while in others, in loans to small local entities, it is

[1] Paul VI, Encyclical Letter *Populorum Progressio*, 26 March 1967, n. 59.

because, despite their size, such entities often have alternative sources of financing where the social purpose that the resources in question aim to support is a very significant factor (take, for example, the experience of microcredits in countries with limited business financing).

In addition, the Church itself has approved of the function of capital used to finance productive activity. In the words of Pius XI,

> ... the investment of superfluous income in developing favourable opportunities for employment, provided the labour employed produces results which are really useful, is to be considered ... an act of real liberality particularly appropriate to the needs of our time.[2]

This statement by the Pope, in a year – 1931 – when the effects of the Great Depression of 1929-30 were taking a heavy toll in terms of unemployment and where there were few grounds for hope for a better world, still holds true at the start of the twenty-first century, when much of mankind is still without the prospect of work and submerged in poverty.

The Social Doctrine of the Church therefore clearly distinguishes in this case between finance destined to aid productive activity and that whose destination is not known. Moreover, the requirement is not limited to the destiny of resources; rather, it includes two additional ethical requirements: on the one hand, that the production of goods be of those that are useful for people; and on the other, that the investment financed tends to increase the prospects of paid work. The first requirement could be considered today as the production of goods that are commercially justifiable (that is, those that aid human existence, without jeopardising their dignity), while the second would refer particularly to labour-intensive – rather than capital-intensive – productive activities. This situation coincides with the possibilities offered by an economy where education is rudimentary and the workforce is therefore poorly skilled.

In a similar way, the Vatican Council II stated that:

> The distribution of goods should be directed toward providing employment and sufficient income for the people of today and of the future. Whether individuals, groups, or public authorities make the decisions concerning this distribution and the planning of the economy, they are bound to keep these objectives in mind. They must realise their serious obligation of seeing to it that provision is made for the necessities of a decent life on the part of individuals

[2] Pius XI, Encyclical Letter *Quadragesimo Anno*, 15 May 1931, n. 51.

> and of the whole community. They must also look out for the future and establish a proper balance between the needs of present-day consumption, both individual and collective, and the necessity of distributing goods on behalf of the coming generation.[3]

That does not mean that, given this state of things, the organization of production has to threaten the dignity and interests of workers and, in general, of those countries labelled as 'poor'. On the contrary, it should be considered as an intermediate state of affairs, which leads to an enrichment of capacities, skills and knowledge that will permit an advance to a more developed state. The threat to the dignity of the worker, on the other hand, is always unacceptable. This is established in the doctrine laid down by, among others, Pope John XXIII, who stated that,

> ... if the organisation and structure of economic life be such that the human dignity of workers is compromised, or their sense of responsibility is weakened, or their freedom of action is removed, then we judge such an economic order to be unjust, even though it produces a vast amount of goods whose distribution conforms to the norms of justice and equity.[4]

Although experience undoubtedly shows that the conditions of financing of public sector productive activities differ from those applying to the private sector, we shall not at present differentiate them, since this would lead to unnecessary divisions. In any event, there are wider differences within public sector financing, not connected to productive projects, and that are controlled by the lender, including, naturally, the financing of transport or communication infrastructures, so necessary for development and, of course, those related to education, health and so on, that are vital for an organized and dignified life.

Financing of the public sector that is unconnected to controllable productive projects is especially worthy of consideration. This is because of the onerous conditions often attached to such lending, where 'onerous conditions' means those that are more stringent than normal market conditions, and that, accumulated over time, end up constituting an unbearable burden on the borrowing countries.

In many cases, the loan is granted when there exists more than reasonable doubt about the ability to repay it. Such doubt is already present

[3] Second Vatican Council Pastoral Constitution *Gaudium et Spes*, 7 Dec. 1965, n. 70.
[4] John XXIII, Encyclical Letter *Mater et Magistra*, 15 May 1961, n. 83.

because of the very nature of the borrower (countries that are classified as 'high risk'), but it is aggravated by the high interest rates applied to the loan which reflect, it is said, the probability that the debtor country will be unable to pay. In short, a premium is applied to the market rate of interest that, drawing an analogy from insurance theory, covers in an actuarial sense the probability of the risk of failure.

It is clear that even if we are to accept the reasoning behind the additional interest rate, we cannot ignore the problems that this high cost of capital entails when financing works of infrastructure or service, or the simple general expenditure of public authorities.

We must add to this the volatility of governments of poor countries, for whom indebtedness is not seen as a problem because they will not be faced with the responsibility of having to pay back money borrowed, and who view accumulating debt as almost an objective per se, rather than a difficulty. The problem may be aggravated even further, if such lending occurs at a time when there is a surplus of financial resources on the international market, as happened in the second half of the 1970s and the beginning of the 1980s.

Foreign debt is a burden that creates insoluble problems for those countries that suffer it. This is why the voice of John Paul II has been heard, stating that:

> At present, the positive efforts which have been made ... are being affected by the ... unsolved problem of the foreign debt of the poorer countries. The principle that debts must be paid is certainly just. However, it is not right to demand or expect payment when the effect would be the imposition of political choices leading to hunger and despair for entire peoples. It cannot be expected that the debts which have been contracted should be paid at the price of unbearable sacrifices. In such cases it is necessary to find ... ways to lighten, defer or even cancel the debt, compatible with the fundamental right of peoples to subsistence and progress.[5]

This call could not be more timely, particularly when creditor countries and international financial bodies, that know the financial world well, are aware from the outset that paying back such loans will be difficult, particularly if they are in a strong, stable currency and the debtor country has a fragile, volatile currency. Such attitudes, rather than favouring debtor

[5] John Paul II, Encyclical Letter *Centesimus Annus*, 1 May 1991, n. 35.

countries, prevent them from developing and entering the developed world, rendering them incapable of benefiting from the advantages that a wide and free market could have on the movement of financial resources.

It is for this reason that rich countries have a particular responsibility towards their poorer brethren, a responsibility to help them to integrate into the world economic community.

> Stronger nations must offer weaker ones opportunities for taking place in international life, and the latter must learn how to use these opportunities by making the necessary efforts and sacrifices and by ensuring political and economic stability, the certainty of better prospects for the future, the improvement of workers' skills, and the training of competent business leaders who are conscious of their responsibilities.[6]

In this responsibility, a specific appeal is made by the Second Vatican Council addressed to the richest nations:

> In financial transactions they should beware of hurting the welfare of their own country or of the countries. Care should also taken lest the economically weak countries unjustly suffer loss from a change in the value of money.[7]

In addition, an examination of the actual state of events is highly instructive as regards this series of problems. The high indebtedness of developing countries has not been matched by the creation of wealth or the growth of availability of productive, transport or communication infrastructures. Not even the parity of their currencies compared to the currencies in their real economic world has been reinforced and stabilized. In other words, without going into more detail at present, it can be said that the financing of the public sector in its widest sense but particularly that which is not related to specific projects that are controllable by the financing entity, far from being an economic or social advantage for the debtor country, ends up being a burden that is enormously difficult, if not impossible, to bear.

This statement reminds us of the appeal made by Monsignor Mendes de Almeida, at that time President of the Bishops' Conference of Brazil, who within an international symposium, in the presence of a number of multinational companies from different productive sectors and also in the presence of various banks and financial entities, requested that they all returned to Latin America, bringing investment and technology to improve

[6] John Paul II, Encyclical Letter *Centesimus Annus*, 1 May 1991, n. 35.
[7] Second Vatican Council, Pastoral Constitution *Gaudium et Spes*, 7 Dec. 1965, n. 70.

the living conditions of its people, while at the same time issuing a warning, mainly to financial institutions, that any financial loan be made in the private sector, *never* to the public sector, for the reasons set out above.[8]

Certain fallacies

Naivety, which is typical of childhood or even adolescence and a sign of hope in such phases of life, can be disastrous if it is the trait of those who have to manage public assets or those who have in their hands the task of rationally and efficiently allocating scarce resources for different ends among the great human family, particularly if we consider that the ones who suffer most are the ones that have the least.

For this reason, the repetition of fallacious arguments that cannot stand up to any rigorous examination in the context of responsible decision-making is a clear example of social irresponsibility, incompatible with ethical reflection based on Christian principles, as exists in the Social Doctrine of the Church. This is particularly so if the decision-making in question aims to alleviate situations of poverty, that in many cases are alarming, reducing the enormous gap between rich and poor that constantly causes the Christian conscience so many problems.

When the fallacy, which can be understood to mean the deception or lie used to cause harm to another, is applied against those that lack almost everything, against those who, like Lazarus, wait outside the banquet hall before picking up the left-over crumbs, those that enjoy the feast have a responsibility that cannot be denied. Building a theoretical world which has little to do with reality, in order to apply the so-called rules of the game so as to enjoy privileges that marginalize the most needy, is tantamount to building models on the foundations of evil. Nothing good can come of this asymmetry, of this egoism and deception, for humanity. All it leads to is a predominance of conflict and aggression.

Market freedom

According to the texts currently in force and the treaties that regulate international bodies and relations, market freedom has become accepted as

[8] Speech of Mgr. Mendes de Almeida in the Symposium on 'Multinational Enterprises and Investments in Developing Countries', UNIAPAC, Wolfsberg (Switzerland) 17th to 19th May 1989.

the indisputable way of guaranteeing, so it is said, a greater degree of efficiency in the international employment of resources. The claims made are taken even further. Thus, it is now said that the problem of underdevelopment is precisely due to the lack of universality of such freedom or, what amounts to the same thing, obstructions of such economic freedom in poor countries.

Previously in the GATT, and now in the WTO, considerable advances have been made in dismantling tariff barriers that reduced freedom in international trade. International finance has become ever more streamlined; financial resources flow effortlessly from one market to another, thus demonstrating an aspect of transparency and freedom that has little to do with reality, as also occurs in product markets.

Now is not the moment to become involved in a debate about the goodness of the classical and neoclassical models with respect to the objective of economic efficiency and its improved capacity to generate income and wealth, other things being equal. We are even prepared to accept that in optimum conditions the market exercises its distributive function and that, through the natural incentives that the market provides, it is capable of improving the living conditions of the poor in a more efficient manner than when this objective remains in the hands of the state.

What we will analyse here is this: the fallacy of freedom. What we call freedom, in the markets for both goods and financial resources, appears to be threatened by protectionism in the former and preferences in the choice of debtors in the latter. Those countries that claim to enjoy the greatest amount of freedom – the Member States of the European Union and the USA – are in fact those that close their markets most quickly and most effectively when they believe that their products may be damaged by imports. Consider the scandalous example – albeit not the only one – of the market in agricultural products in both cases.

From the perspective of honesty, and without needing to call on arguments based on ethics and solidarity, since these must be considered after those concerning justice have been fulfilled, the question that needs to be addressed is this: what is the point of the productive and financial efforts of all developing countries as producers of agricultural goods – banana, pineapple, papaya, mango, sugar, cocoa, coffee and so on – when they find that rich countries have closed their markets to such products, in order to protect their products or rather, put more crudely and more cruelly, the income of their farmers from those who work in poor countries?

We advise them, with great expertise, to make every effort to achieve a balance of payments and to prevent their trade relations with foreign countries from deteriorating. This task is difficult to achieve when, faced with the rigidity of oil imports and those of industrial and manufactured products of rich countries, markets where demand for their products exist remain inaccessible for those who simply hope for an opportunity.

In the light of this, the developed world continues unchanged, preaching about the virtues of freedom, about a model that it has created with efficiency rather than solidarity in mind, a model that it is not even prepared to support when it sees some domestic interest – which, on occasions, is simply electoral interest – to be endangered.

Before promoting solidarity, which is also necessary, we must first satisfy the need for justice. Justice in this case clearly means respecting the rules of the game that, in the context of globalisation, have been designed by the rich countries themselves, emphasizing the efficiency advantages that we expect from them. We must start trying to satisfy, for requirements of world order, the old legal principle of *pacta sunt servanda* – agreements must be kept. Once this principle is guaranteed, then we can act on the basis of solidarity; otherwise, we run the risk of confusing attitudes, calling something virtuous when it does not even fulfil the requirements of fair behaviour.

Governments and the common good

Believing that all governments are committed to the common good of the people, that is, the well-being of each and every one of a country's inhabitants, is an expression of naivety. Such naivety deserves be punished in cases where the government is controlled by bloody dictators that subject society to their will, denying them their natural inalienable rights, governing for the enrichment of themselves and their families and those close to them who helped them to remain in power.

Financing these governments, alleging that the international financial system cannot become involved in the internal problems of each country is pure hypocrisy that conflicts with the Christian message. It is obvious that such financing will have no beneficial effect at all for such a society, which, moreover, becomes indebted, thus limiting its prospects of future growth. It is clear that if the effects of financing end up being noticeable at all, it will be in the purchase of arms which the dictator will use to punish increasingly his own people. The innate corruption of these financial agreements should prevent them from ever being entered into, as indeed they are not in the developed world.

The concept of honour, the basis of the principle of financial activity that is summed up in the scrupulous fulfilment of obligations entered into, amongst others the very objective of the financing, appears to have been forgotten, as is clear from the number of cases that exist of the financing of corrupt governments. Without reducing at all the responsibility of the recipient of the financing, he who grants it is not free of blame either.

We should recall the papal doctrine of Pope Pius XI, where he considered the use of capital to provide opportunities for paid work to be a commendable sign of freedom, provided that such work is used to produce goods that are useful for the community. Conversely, we can say that capital used to feed corruption springs from corruption itself. And here euphemisms have no place.

A doctrinal appeal

John Paul II has expressed the point eloquently:

> ... one must denounce the existence of economic, financial, and social *mechanisms* which, although they are manipulated by people, often function almost automatically, thus accentuating the situation of wealth for some and the poverty for the rest. These mechanisms, which are manoeuvred directly or indirectly by the more developed countries, by their very functioning favour the interest of the people manipulating them. But in the end they suffocate or condition the economies of the less developed countries. Later on these mechanisms will have to be subjected to a careful analysis under the ethical-moral aspect.[9]

It is clear that the problem does not reside in the mechanisms, but rather in the people that designed them or now manage them for their own gain and to the detriment of the most needy. Unfortunately, examples abound of attitudes that, far from extolling man, humiliate and degrade him. Because

> ... among the actions and attitudes opposed to the will of God, the good of neighbour and the *structures* created by them, two are very typical: on the one hand, the *all-consuming desire for profit*, and on the other, *the thirst for power*, with the intention of imposing one's will upon others.[10]

[9] John Paul II, Encyclical Letter *Sollicitudo Rei Socialis*, 30 Dec. 1987, n. 16.
[10] John Paul II, Encyclical Letter *Sollicitudo Rei Socialis*, 30 Dec. 1987, n. 37.

Profit and power: ingredients that often form part of the conditions of an asymmetric market and, of course, largely shape the attitude of the corrupting party and that of the corrupted in international relations.

Perhaps for this reason once again it is instructive, however hard it may be for modern ears, to start using again terms that apply to any epoch of life and, therefore, also to a financial scenario of globalisation such as the one we are now considering. In the words of John Paul II:

> *Sin* and *structures of sin* are categories which are seldom applied to the situation of the contemporary world. However, one cannot easily gain a profound understanding of the reality that confronts us unless we give a name to the root of the evils which afflict us.
>
> One can certainly speak of *selfishness* and of *shortsightedness*, of *mistaken political calculations* and *imprudent economic decisions*. And in each of these evaluations one hears an echo of an ethical and moral nature.[11]

It is this moral resonance which justifies and underpins the valuable contribution given by Prof. Malinvaud.

[11] John Paul II, Encyclical Letter *Sollicitudo Rei Socialis*, 30 Dec. 1987, n. 36.