2 The Changing Role of Ministries of Finance

Ministries of Finance Then

It can be argued that during much of this century and prior to the 1980s, the role of Ministries of Finance, while significant, was by no means pre-eminent in the development policy process. The Finance Ministry was expected to manage the government's resources through the annual budget (taxes, expenditures and transfers) so as to ensure that economic decisions taken in the Planning Ministry or other ministries such as industry, agriculture, rural development, health, education, etc. were financially viable. While the Finance Ministry might have urged fiscal caution in the face of over-ambitious economic plans, it rarely acted as a barrier. Indeed, many Ministries of Finance in the past abrogated their cautionary role, allowing the burden of financing fiscal deficits to be passed on to the country's Central Bank.[1] The Finance Ministry's role therefore essentially used to be a *supportive* one, and was exercised through the annual ritual of the national budget, ongoing financial approvals of detailed programmes, and the monitoring of financial and monetary variables.

Ministries of Finance typically functioned with relatively short time horizons, and did not concern themselves with medium or long term economic planning. The latter was the job of the Planning Ministry or Planning Commission whose task was to set the long-term strategic direction for the rate of economic growth, its structure and patterns, the distribution of income and employment, the creation of physical infrastructure, human development, and poverty alleviation. In doing this the Planning Ministry functioned as a kind of apex body that co-ordinated and balanced the strategic plans of the other ministries, and worked with the Finance Ministry to ensure its financial viability.

Ministries of Finance Now

These roles and the division of labour between Finance and Planning Ministries have changed during the current period of structural adjustment-oriented economic reforms in many countries. Three factors – the end of the so-called global 'golden age' of economic growth of the 1950s, 1960s and early 1970s (Howes and Singh, 1995); a major technological revolution resulting in significant changes in the structures of output and employment away from manufacturing towards services in the OECD countries; and the rapid growth and diversification of global financial transactions – have had a number of effects. Critical among these effects has been the pressure in all countries for greater fiscal discipline, as well as a positive Balance of Payments in order to enable countries to compete globally while keeping inflationary pressures under control and managing external and internal debt.[2]

Almost all countries, both high- and low-income, have faced these pressures, but for the developing countries, there has been the additional dimension of a worsened climate for development assistance. The relatively greater availability of development aid in the 1950s and 1960s had generated the belief that development resources which could not be generated internally could always be obtained through external borrowing.[3] So-called 'aid fatigue' in the donor countries, in no small part the result of their own fiscal stress and growing unemployment, has increased pressure for fiscal belt-tightening, and increased export earnings to replace declining aid monies in developing countries. The fiscal stabilisation and structural adjustment packages espoused by the Bretton Woods institutions have been mechanisms to persuade governments to respond to the changed global economic realities.

The result has been a major change in the relative influence and economic standing of Ministries of Finance within most countries. At a time of sharply increased fiscal stringency, the role of Ministries of Finance has changed from a supportive one to a disciplining one. Planning Ministries are now required to cut their coats according to their financial cloth, and it is the Finance Ministry that determines how much cloth there is.

Table 1 The Changed Roles of Commonwealth Finance and Planning Ministries

Roles	Finance Ministry	Planning Ministry
Then	Ensuring financial resources for the plan; annual budgets; ongoing financial monitoring	Setting priorities and resources for growth of all sectors of the economy
Now	Maintaining fiscal discipline; setting strategic economic direction through structural reforms	Indicative planning for growth of physical infrastructure and human development

Figure 2 **Reconstruction and Development versus Macroeconomic Stabilisation in Post-Apartheid South Africa**

Nowhere is the tension between the needs of equitable and sustainable development versus the pressures for macroeconomic stabilisation so sharp as in post-apartheid South Africa. This tension has different stakeholders supporting one or the other of the Reconstruction and Development Programme (RDP) or the stabilisation plan entitled Growth Employment and Redistribution (GEAR).

Since the RDP was built through a process of bottom-up discussion and involvement in widespread debate in the country, it has the status of a people's plan – one which crystallises the aspirations of people who have long been denied economic, political or social opportunities or justice. It includes a considerable emphasis on job-creation and social development as well as gender justice. However, despite the laudable process through which the RDP was created, the country has no Ministry of Planning or apex body such as a Planning Commission which can take a comprehensive approach to implementing the RDP. Despite this, significant steps forward have been taken by a number of line ministries to move in the directions charted by the RDP.

GEAR on the other hand, despite the presence of 'redistribution' in its title, is essentially a programme for fiscal stabilisation which differs only marginally from most programmes of structural adjustment. The Congress of South African Trade Unions (COSATU) as well as a number of others have strongly criticised GEAR as reneging on the promises of the RDP, and working in the narrow interests of the economic elite in the country.

Ministries of Finance and Macroeconomic Management

The changed role of the Finance Ministry vis-à-vis other ministries and especially relative to the Planning Ministry and the Central Bank also reflects a major change that has occurred worldwide in the meaning and parameters of macroeconomic management. During the heyday of Keynesian macroeconomic policy from the end of World War II to the end of the 1960s, the principal objective of short-term macroeconomic management (at least in the countries of the North) was to minimise unemployment and recessions through fine-tuning government spending and taxation. From the late 1970s onwards, however, effective macroeconomic management has meant less focus on reducing unemployment and much greater focus on inflation rates and exchange rates.

Stabilising a national economy within a liberalised global economy has meant ensuring that inflation rates remain low and exchange rates remain stable; the freedom to manoeuvre government spending so as to reduce unemployment or to pull the economy out of a recession appears to be significantly curtailed. It is within this context that one has to view the new role of Ministries of Finance in relation to macroeconomic management. Maintaining fiscal discipline and strengthening the Balance of Payments is now central to macroeconomic management for which the Finance Ministry has the prime role.

There are four related sets of instruments that the Finance Ministry typically uses for this purpose:

- the budget;
- the government's fiscal deficit;
- internal and external debt;
- the Balance of Payments.

In low-income countries, structural adjustment programmes promoted by the Bretton Woods institutions have used the leverage of external debt to ensure that Ministries of Finance exercise strict restraints on government deficits and on the overall budget. In practice, as is well known, the kinds of fiscal restraints adopted by some governments have had significant recessionary impacts in many countries as well as drastic cuts in public spending on both physical investment and human development.

It is arguable that, even if government expenditures have to be cut, there are different ways in which this could be accomplished. But Ministries of Finance have by and large resorted to 'the politics of the squeaking wheel' in deciding where spending cuts should be made. As a result, sectors and programmes which do not have an effective public 'voice' or whose beneficiaries are poor and socially disenfranchised have tended to suffer disproportionately.

Ministries of Finance and Structural Reforms

The relative weight of Ministries of Finance has changed in another important sense as well. The need to ensure greater fiscal discipline has been viewed not as a temporary result of external shocks but as more fundamentally related to poor economic management by governments. This is believed by some to have resulted in weak economic growth, excessive controls over private economic activity, curbing of economic incentives, and therefore weak capacity of the government to mobilise resources. Maintaining fiscal and monetary discipline has therefore become part of the larger structural reform process which includes:

- liberalising markets;
- limiting state economic activity; and
- supporting the private sector.

Ministries of Finance have come to have a key role in setting the new strategic economic directions for long-term growth. The role of Planning Ministries is now typically limited to indicative planning for long term infrastructure – both physical and human.

Along with privatisation of the public sector and of public services, the liberalisation of markets and the deregulation of private economic activity are key ingredients of the current structural economic reforms supported by most Ministries of Finance. The aim of these changes is to correct biases in the allocation of economic resources that are purported to have resulted from excessive government intervention, and thereby to lay the basis for a fiscally sound pattern of economic growth and government expenditures over the medium and longer term.

Liberalisation and deregulation

Liberalisation includes a group of measures intended to raise the efficiency of resource use by removing quantitative restrictions on private investment and trade flows domestically and internationally, and reducing government controls on prices (commodities, labour, money, foreign exchange, and other services) so that prices give a better reflection of the true scarcity values of resources. The explicitly stated intention is to remove the policy bias against the production of tradable goods, and thus to allow production to shift so that it more accurately reflects the economy's factor endowments, typically in favour of the production of labour-intensive goods for export markets. Investment, production and prices, it is argued, will thus become more closely aligned to the external sector. Deregulation is also expected to reduce wastage of resources by reducing petty corruption and exploitation at the hands of government officials, once their discretionary authority to grant permission for a range of economic activities is removed.

Under current structural adjustment policy reforms in many countries, markets are typically liberalised by:

- reducing or removing controls on investment and production;
- reducing or removing price controls;
- removing interest rate ceilings;
- allowing freer capital movements within and across national boundaries;
- removing quantitative restrictions on imports/exports;
- reducing tariffs;
- reducing corporate and individual income and wealth taxes;
- easing anti-trust regulations;
- weakening labour laws and/or their implementation so as to reduce the bargaining strength of labour unions; and
- easing environmental controls.

Privatisation

Like liberalisation, privatisation is a key ingredient of the structural reforms espoused by Ministries of Finance today. Like liberalisation, it too is expected to have both short-run and medium/long term effects on the economy. The privatisation process in many countries has had two components – government divestiture from public sector enterprises, and cutbacks in government financing of public services. Each has different implications. The government sale of public sector enterprises has been viewed as necessary in order to reduce subsidies to loss-making enterprises and introduce an element of fiscal discipline. Takeovers by the private sector have usually been accompanied by labour force reductions and job losses. In some cases, public sector enterprises remain in government hands, but are encouraged to operate like private enterprises, including their treatment of labour.

Despite the fact that, in theory at least, the main purpose of privatisation is supposed to be structural and not financial, *viz.*, changing the ownership and management structure of badly managed public enterprises, governments under severe financial pressure, have also viewed the sale of public enterprises as a mechanism for earning revenues (albeit one-off and short term only) and reducing fiscal deficits. This has been true in many countries.

Actual experience with privatisation has been mixed, since the private sector is interested in buying precisely those public enterprises that have been managed well hitherto and whose books are not in the red, and not the ones that the government may be keen to get rid of. Regardless of the merits and demerits of different privatisation experiences, it is important to recognise that all three of the key ingredients of the current economic reform processes under way in many countries, *viz.*, liberalisation, deregulation and privatisation, have significant implications when viewed through a gender lens. This discussion follows in Section 3.

Liberalising credit markets[4]

In recent years, financial liberalisation and financial sector reforms have been complementary. While the former implies the removal of controls and barriers to financial mediation including interest rate controls, the latter includes measures to improve the financial regulatory climate and strengthen financial institutions in a more liberal environment. Although such reforms are part of the larger reform process, we treat them separately here because they are directly within the purview of the Finance Ministry's and Central Banks' normal tasks and always have been.

Key aspects of financial liberalisation include changes in interest rate management practices; in the availability and distribution of credit to different sectors of the economy; in the cost of credit to different sectors particularly if credit subsidies are removed; and changes in the laws governing banks and other financial institutions.

Recent experience with financial liberalisation in a number of countries reveals both a diversification and upgrading of credit services to the higher and middle income end of the market, as well as greater integration into global financial markets, with resulting instabilities and loss of governmental control over the process. The impact on women has been mixed; on the one hand they have suffered from the reduction of credit subsidies, but on the other hand a variety of micro-credit schemes have improved women's credit access in a number of countries.

To summarise: this section has discussed the changing roles and relative standing of Ministries of Finance, and their importance in the structural reforms that are under way in many countries. Fiscal stabilisation and structural reforms directed at liberalising and privatising the economy have thus come to set the parameters today for any attempt to mainstream gender.

Notes

[1] It is another matter of course that Central Banks often did not play this role either, allowing governments to finance fiscal deficits through uncontrolled internal borrowing or simply printing money, thereby fuelling inflation and allowing the government's budget constraint to remain 'soft'.

[2] The only country that has been able to run large fiscal deficits indefinitely without corresponding belt-tightening has been the US because of the special role of the US dollar in international financial transactions. US concern over the size of their fiscal deficit stems not from fears regarding the Balance of Payments, but from the so-called tax-revolt of the middle class and the wealthy, and the social security needs of an aging population.

[3] The extensive economic literature on the so-called two-gap growth models was the analytical counterpart of this belief.

[4] The discussion on credit liberalisation and financial sector reform draws extensively on Baden (1996).