Statement by Juan Pablo Bohoslavsky

UN Independent Expert on the effects of foreign debt and other related financial obligations of States on the full enjoyment of all human rights, particularly economic, social and cultural rights

Side Event

Co- organised by the United Nations Research Institute for Social Development (UNRISD), the mandate of the Independent Expert on Foreign Debt and Human Rights, the Office of the High Commissioner for Human Rights, the International Labour Office and Friedrich-Ebert Stiftung

"Economic Inequality, Financial Crises and Human Rights"

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Excellencies, distinguished Delegates and participants,

It is a pleasure for me to address you today. Earlier this week I presented four reports to the human rights council, including my thematic report on the interrelationships between economic inequality, financial crises and the enjoyment of human rights.[1] I am glad to have another opportunity to present this report in more detail and I would like to pay particular thanks to UNRISD, especially to Katja Hujo, as well as the other partners for the organisation of this event and for contributing to this important topic.

Global inequality currently stands at extremely high levels and is further increasing. This worrisome trend has been documented very well.[2] There is as well an emerging consensus that extreme economic inequalities need to be tackled. For instance, at the international level, States have committed to reduce inequality within and among countries in Goal 10 of the Sustainable Development Goals.

And yet, there is one particular facet of inequality that has been frequently neglected: the linkages among economic inequality, financial crises and human rights. In my report, I explored three broad questions: 1) Does inequality lead to more financial instability? 2) Does financial instability lead to higher levels of inequality? 3) What are the impacts of increased inequality on the enjoyment of human rights?

Distinguished participants,

Inequality as a source of sovereign debt increase and crisis

Let me first start by highlighting inequality as both a direct and indirect cause of sovereign debt increase and financial crises. Inequality may exert a considerable direct influence on the structure and the level of government revenues and spending. Increased levels of inequality also mean that the income tax base of the State concerned is rather small, at least if income taxation is not progressive. This diminishes sovereign revenues, making the State more dependent on borrowing.

There is empirical evidence which suggests a clear nexus between inequality, income tax base and sovereign debt. For example, one study found a negative correlation between income inequality and the tax base and a positive correlation with sovereign debt.[3] Increased inequality is also found to contribute to the degeneration of sovereign debt into sovereign debt crises.

One possible explanation for these links is that in very unequal societies there are higher incentives for default. By defaulting, a government may obtain new fiscal freedom — even if

[1] A/HRC/31/60

[2] See UNDP, *Humanity Divided: Confronting Inequality in Developing Countries* (New York, 2013).

[3] See J. Aizenman and Y. Jinjarak, "Income Inequality, Tax Base and Sovereign Spreads", *FinanzArchiv: Public Finance Analysis*, vol. 68, No. 4 (2012), pp. 431-444.

this freedom might be short-lived — permitting tax cuts or spending increases to the benefit of the poorer. Yet, in the long run, default normally implies future costs owing to a (temporary) exclusion from financial markets. As the government cannot use any more debt to smooth taxes, it is forced to adjust its tax revenues to any short-term fluctuation. The resulting volatile taxation harms poorer households in particular.

Inequality can also indirectly contribute to increased sovereign debt and consequently to sovereign debt crises. There are at least two avenues to such outcomes: (a) high levels of inequality contribute significantly to the generation and increase of private debt, with strong interrelationships between excessive private debt, which in turn may adversely affect sovereign debt and the stability of financial markets; and (b) inequality adversely affects social and political stability, thereby hampering growth and eventually affecting both government revenue and spending.

Distinguished participants,

Impact of financial and sovereign debt crisis on inequality

My report analyses also how financial and sovereign debt crises have in turn entrenched economic inequalities. To start with, financial crises may massively hamper economic growth, principally because of decline in investment in production, as a result of credit contraction. Banking crises usually lead to a significant output drop. On average, the real per capita GDP drop amounts to over 9 per cent, with a recovery time of two years.[4]

Another study which analysed banking and currency crises has revealed that the average output loss is 20 per cent of GDP, with an average recovery time of three to four years.[5]

Currency crises also have a magnifying impact on both the spread of poverty and inequality. After a financial crisis there may not always be an immediate impact resulting on increase inequalities, as top income earners may experience in the immediate aftermath of a financial crises a particular sharp decrease of their revenues because of their higher dependence on capital income. However, reductions of income and wealth of the more affluent related to the collapse of stock markets are often only of a short duration, while income levels of the poor remain low for a longer duration.

Austerity measures adopted in response to financial crises have had robust negative social impacts, exacerbated inequality and pushed disadvantaged groups below minimum income thresholds.

Adjustment programmes without consistent debt reliefs have proven to be detrimental to human development and human rights, at least in the short term.

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[4] See C.M. Reinhart and K.S. Rogoff, "The aftermath of financial crises", *American Economic Review*, vol. 99 No. 2 (2009), pp. 466-72.

[5] See M.D. Bordo et al, "Is the crisis problem growing more severe?", *Economic Policy* Vvl. 16 No. 32 (2001), pp. 51-82. The authors also demonstrate that banking and currency crises have become more frequent in the last quarter of the twentieth century.

Distinguished participants,

Impacts of increased inequality on the enjoyment of human rights

International human rights law has something to say about economic inequality. Economic and social rights oblige States to address and prevent inequality that undermines the enjoyment of human rights.

While human rights law does not necessarily imply a perfectly equal distribution of income and wealth, it does require that States ensure conditions in which rights can be fully exercised. As a consequence, a certain level of redistribution is expected in order to guarantee individuals an equal enjoyment of the realization of their basic rights without resulting in discriminatory outcomes. When income inequality creates discriminatory outcomes, it becomes a human rights issue.

International human rights norms require States as well to ensure that all persons live with dignity. The existence of extreme inequality implies often that States are failing to meet their minimum core obligations under international human rights law, including the International Covenant on Economic, Social and Cultural Rights: Either States fail to mobilize maximum available resources for the progressive realization of rights, or they fail to ensure essential minimum levels of satisfaction of economic and social rights.

Economic inequality also matters from a human rights perspective when it translates into other types of inequalities. The enjoyment of human rights does not depend only on access to goods and services reflecting the minimum needed for survival; an individual's access to resources relative to others is also of crucial importance. Data suggests that high levels of relative inequality may have substantial negative effects on the enjoyment of human rights, including political and civil rights.

Furthermore, inequality often contributes to social exclusion and marginalization of certain groups and individuals. It is also common for poorer segments of the population to be marginalized or even effectively excluded from the political process. If we do not recognize the connection between social and economic inequalities and civil and political rights, there is a risk of capture of the political system by economic elites, effectively undermining the right to vote and democracy.

Excellencies, distinguished Delegates and participants,

Conclusion

As highlighted above, there are many linkages between inequality, private and sovereign debt and the occurrence of financial crises. Indeed, human rights and the social and economic sphere are inseparably intertwined, and one cannot prevent financial crises without addressing human rights shortcomings that contribute to them, including those connected to inequality.

Last but not least, my report makes a number of recommendations on how to address inequalities in the prevention of financial crises and in their response. I stress the contribution financial market regulation, minimum wages, progressive taxation, and social protection floors would make to combat excessive inequalities and ensure better human rights compliance. Structural adjustment measures should be subjected to robust human rights impact assessments and not only orientated at short term fiscal targets to regain debt sustainability. The distributive impact of adjustment should be carefully analysed and measures prioritized to protect the most vulnerable.

I thank you for your attention and look forward to a fruitful discussion.

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