Montes, Manuel F., and Rob Vos. "A Feasible Globalization." *Retooling Global Development and Governance*. Ed. Rob Vos and Manuel F. Montes. London: Bloomsbury Academic, 2013. 147–172. The United Nations Series on Development. *Bloomsbury Collections*. Web. 26 Apr. 2023. <<http://dx.doi.org/10.5040/9781472544933.ch-006>>.

Downloaded from Bloomsbury Collections, www.bloomsburycollections.com, 26 April 2023, 09:58 UTC.

Copyright © United Nations 2013. You may share this work for non-commercial purposes only, provided you give attribution to the copyright holder and the publisher, and provide a link to the Creative Commons licence.

Chapter VI

A feasible globalization

MANUEL F. MONTES AND ROB VOS

BUSINESS AS USUAL IS NOT AN OPTION

Enormous changes in the workings of and the mechanisms of governance over the international economy are under way as a result of the current global crisis, the deepest the international community has faced since the Great Depression more than 75 years ago. However, the actual shape of the outcome is uncertain. While there are powerful interests pressing to restore the system's configuration before the crisis, even these will be thwarted by the significant economic trends that are already in evidence and the unprecedented restructuring underway. Recovery from the global financial crisis of 2008-2009 has been slow and protracted, in part because of the thoroughgoing and cumbersome process of recapitalization and deleveraging taking in major financial sectors. Even if the world were simply to be rebooted worldwide so as to function exactly as it had, one might expect the scale of private flows to be more subdued in years to come. Yet, more limited flows could still cause additional severe damage in an unreformed system. The enhanced risk for sovereign debt crises in Europe that emerged in early 2010 was matched by equally risky surges in short-term capital flows to emerging markets, triggering renewed financial turmoil worldwide. The fact that policymakers have been slow to respond highlights once more the glaring gaps in global economic governance.

If nothing else, the feeble responses to the simultaneous occurrence of global food, fuel and financial crises towards the end of the first decade of the century revealed inadequacies in international coordination mechanisms. While a number of responses to the current crisis appear to have

had some effect, these were mostly ad hoc and insufficient to address the more systemic weaknesses in the world economy.

The European sovereign debt crisis which erupted in May 2010 is a case in point. This crisis revealed, first, that unaddressed inconsistencies between international private lending in periods of global liquidity, on the one hand, and uncontrolled national deficit spending, on the other, served as the basis for a crisis whose systemic repercussions could have been more limited if there had been more adequate international financial regulation and macroeconomic policy coordination. Second, in the throes of the crisis, there was no international mechanism in place for debt resolution that would not endanger the whole global financial system and/or would provide a credible national adjustment path for debtor countries over the medium term. Such debt resolution processes, while quite demanding, have long-standing precedents in national contexts through a burden-sharing process between the debtor and the community of creditors. Third, even with the already existing practice of European supranational cooperation, the crisis appears to have spiralled out of control because of coordination delays among nations operating under disparate political conditions. These issues merely underline the urgent need for a global governance system that can address the treacherous conditions endangering the world economy and ensure a more stable context for development so as to enable it to foster and build a sustainable future for all.

As emphasized in chapter I, the world community must wrestle with the economic and financial crisis on top of an already ongoing crisis of food and energy insecurity. The harmful effects of climate change are already being felt in many parts of the world and must also be addressed. These crises had been simmering for decades and their resolution will require many years of concerted efforts. Since the economic crisis erupted, there has been frequent reference to the truism that a global crisis requires a global solution. The problem is that the current global governance arrangements do not seem to be up to the task at hand, so that addressing these crises must be undertaken simultaneously with overcoming widespread weaknesses of multilateral mechanisms.

This chapter discusses the challenge of rebuilding global governance, while seeking to identify key requirements based on the survey of issues provided in the previous chapters. The key challenge is to establish a global governance system that will harness, instead of cower before the forces of globalization. If the experience of the global economy's last great crisis in the 1930s is any guide, the globalization process itself will come to a

sudden and catastrophic stop unless properly governed. Its sustainability and feasibility can be guaranteed only by an effective global governance system.

The international community is currently engaged in a piecemeal reform of global governance. This chapter argues that reforms need to be comprehensive. It outlines key areas for reform and the directions that reform should take when addressing these areas in an integral way. While the piecemeal approach has the advantage of gathering and relying on the support of dominant incumbent global players, it has the disadvantage of possibly being unable to keep up with the pace as the crisis continues to morph into more complex forms (as in the European example). Being piecemeal, it also has the potential disadvantage of introducing new elements of incoherence. From a purely logical point of view and one that recognizes the need to build confidence, a deliberate and deliberative global process entailing programmed preparatory conferences focused on various areas of concern, which would lead to the strengthening or the creation of international mechanisms—a Bretton Woods II, as it were—is clearly superior.

The appeal to the Bretton Woods experience reflects the political economy-related uncertainties that beset global economic governance reform efforts (see box VI.1). Rebuilding global governance will require adjustments involving the derogation of powers and privileges of nation states within international bodies. This means that the process is highly political and must be conducted in circumstances where technical questions are not yet completely settled. Thus, while the pressures to reform cannot be evaded, the overall outcome cannot be anticipated in the present discussion.

GLOBAL GOVERNANCE: QUO VADIS?

The world has changed enormously since the current system of global governance was put together with the founding of the United Nations and the creation of the International Monetary Fund (IMF), the World Bank and the General Agreement on Tariffs and Trade (GATT). While the governance system has not stood still, adjustments have not kept pace with requirements of increasing interdependence among national economies through trade, investment, finance, international migration, and the technological advances in transport and communications.

On many occasions, the international community has issued pronouncements on the purposes of the global economic governance system. One of

Box VI.1: The Bretton Woods conference and economic development

The Bretton Woods conference, officially called the United Nations Monetary and Financial Conference, was a gathering of 730 delegates from all 44 Allied nations^a in Bretton Woods, New Hampshire. The conference was held from 1 to 22 July 1944, less than a month after the Normandy landings and with more destruction and countless deaths yet to come before the Second World War ended. The negotiations at Bretton Woods towards the establishment of the International Bank for Reconstruction and Development (IBRD) and the International Monetary Fund (IMF) followed two years of preparatory work entailing background studies and discussions between the United States Treasury and the Chancellor of the Exchequer of the United Kingdom.

The Bretton Woods experience highlights the fact that, in creating new international mechanisms, full representation of all parties and stakeholders (India and the Philippines, although not yet independent States, still attended) is essential. The British proposal that the negotiations over global arrangements be conducted only by the United States and the United Kingdom (the 1940s version of the “G2”, with the United States as the rising power) was not accepted by the United States.

Policymakers at the Conference were driven by the desire to assert the role of public authority within the realm of international finance in the wake of a major international financial meltdown. This overall goal culminated in three sets of proposals: (a) those designed to regulate international financial markets more tightly, (b) those aimed at addressing global economic imbalances and (c) those promoting international development. The third set of proposals, sometimes overlooked, constituted a fundamental part of the envisioned new international order.

These proposals reflected the belief that the promotion of the economic security of individuals throughout the world would provide a crucial foundation for post-war political stability, domestically and internationally. These sentiments were strongly supported not only by the United States and British delegations, but also by many other delegations represented at Bretton Woods, particularly those from developing countries. In fact, well over half the countries attending were from non-industrialized regions. Strong support for the development function of the Bank came from Latin America, China and still colonized India.

In this regard, article I(i) of the IBRD Articles of Agreement^b affirmed that one of the purposes of the Bank was to encourage “the development of productive facilities and resources in less developed countries”. Far from being an accident, the Bank’s mandate to promote development was strongly supported at the time. Article I of the IMF Articles of Agreement^c sets out the same objectives, albeit with slight differences in wording.

Fifty years later, GATT member countries created the WTO through the Agreement Establishing the World Trade Organization.^d The parties to the Agreement recognized “that their relations in the field of trade and economic endeavour should be conducted

with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services, while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development" and "that there is need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development".

Three other issues were in the agenda governing the Bretton Woods negotiators' efforts to integrate development goals into the post-war international financial architecture, although they were not incorporated in the purposes set out in the final agreements: (a) the problem of capital flight from poor countries, (b) the question of restructuring the debts of poorer countries and (c) the promotion of government policies (particularly in Latin America) designed to build more diversified, industrialized and inward-focused national economies. The last-mentioned objective was to be attained by endorsing the use of capital controls, activist monetary policy aimed at domestic goals, adjustable exchange-rate pegs and government-controlled central banks.

In the face of increasing global inequality, pervasive financial crises and climate change, the pursuit, through such efforts, of a fairer and sustainable globalization, should be resumed.

- a Besides 19 Latin American countries, other non-industrialized countries from outside Europe that were represented in the conference included China, Egypt, Ethiopia, India, Iran Islamic Republic of), Iraq, Liberia, the Philippines and South Africa.
- b Available from <http://go.worldbank.org/WAUZA5KF90>.
- c Available from <http://www.imf.org/external/pubs/ft/aa/aa01.htm>.
- d Available from http://www.wto.org/english/docs_e/legal_e/legal_e.htm

the earliest statements of purpose, subsequently restated with slight changes in the agreements establishing other international institutions, such as the World Trade Organization, appeared in the IMF Articles of Agreement. Article I (ii) thereof affirms that one purpose of the Fund was to "facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members". Such phrases, in this specific case applicable to IMF but subsequently associated with other institutions, can be read as embodying the international community's view that the expansion of international interaction must in the first place support high and stable employment. Most

importantly, by calling for the development of the productive resources of all member countries, the international community has put development at the centre of multilateral cooperation and global governance.

Parsing of this overall objective, Ocampo (2010) comes up with finer criteria for evaluating global governance arrangements. They should (a) manage interdependence, (b) further the development of societies and (c) overcome the asymmetries that characterize the world economic system. This proposal recognizes that the construction of international public processes and institutions may entail facing the inevitability of certain context-specific trade-offs. Through the putting in place of public institutions and mechanisms, the global community has conveyed its commitment to prioritizing the fulfilment of these criteria (thereby going beyond adherence to the standard economic formulation that public goods exist only in a situation of non-rival and non-excludable consumption).

The formulation of “common but differentiated responsibilities” is treaty language that encapsulates an international approach to reconciling the three above-mentioned goals. While some international arrangements will emphasize one goal more than the others, reconciling all three will be critical. There is a need to allocate agendas and responsibilities between global mechanisms and nation states and also among the international processes, in a coherent and mutually reinforcing way. The focus of previous chapters has centred mainly on the first two goals. This chapter highlights the issue of global asymmetries.

GLOBALIZATION AND NATIONAL POLICY SPACE

Nation states must assume the primary responsibility for their own development (United Nations, 2002, para. 6), a conception that corresponds to the second key pillar of global governance provided by Ocampo (2010). Close on the heels of the current economic crisis and the multiple threats from climate change, food insecurity and increased political instability, a full-blown restoration of the government’s indispensable economic role is very much under way.

The decline in the responsibilities and corresponding capabilities of national authorities paralleled the rise of economic interdependence and globalization. This trend was “man-made”: states surrendered some of their powers, along with the corresponding responsibilities, to the market, on the principle that market outcomes were superior to state interventions. Rodrik (2002) takes up a phrase—the “golden straitjacket”—introduced

by a popular columnist to capture the naivety of this view. There were asymmetries between developed and developing countries in the context of the state's retreat from market oversight. Advanced countries tend to have a superior informational infrastructure and superior legal powers for monitoring market developments. In developing countries, an early deregulation often precludes achievement of the institutional development needed to govern the market. Reporting requirements on capital-account transactions, which would be necessary not only for macroeconomic policymaking but also for prudential financial regulation, are a key example of such development. As discussed in chapter V, the golden straitjacket in financial deregulation subjected developing countries to greater volatility in capital flows.

Part of the above-mentioned decline has been induced by unavoidable constrictions arising from increased economic interdependence and the spread of largely unregulated private transnational economic operations through global value chains (see chap. IV). Countries that manage to impose restrictions on capital inflows, for example, risk saddling neighbouring countries or economies in the same investment class with increased flows. The financial crisis saw bank depositors withdrawing their balances in distressed countries and investing these in other centres perceived to be more stable. International financial institutions withdrew balances and credit lines in overseas branches when they needed to shore up their balance sheets in their mother institutions based in developed countries.

Rebuilding the international governance system will require rebuilding the capabilities of the state, both domestically and internationally. States must be allowed to keep the powers that will prove necessary if they are to take the primary responsibility for their own development. Primary responsibility applies not only to the implementation but also to the design of development strategy (see chap. II). As discussed in chapter III, this principle requires that external assistance programmes align behind national development strategies. Sovereign states must respect and not undermine the domestic resource mobilization efforts of other states (see chaps. III and V).

The 15 November 2008 Declaration of the G-20 Leaders Summit on Financial Markets and the World Economy¹ underlined the role of nation states in global regulation by affirming that “[r]egulation is first and foremost the responsibility of national regulators who constitute the first line of defense against market instability”. While this formulation clearly recognizes and assigns responsibilities and powers to national authorities,

it does not ultimately resolve the difficult issue of rebalancing powers between global mechanisms while preserving adequate policy space for national governments. The issue of the economic impact of individual states' policies on those of others cannot be completely resolved by a "first line" approach.

Managing financial interdependence will require setting up minimum global standards and commitments to adjust domestic policies which will reduce national policy space. It will require that each layer of international governance be provided with sufficient space and monitoring and enforcement capability to fulfil its role. As elaborated on in chapter V, a key objective of opening up policy space for developing countries is reducing the volatility of private flows to which they have been subjected from international markets.

Important priorities identified in previous chapters include: social development (chap. II), controlling aid donor activities (chap. III), industrial development and economic diversification (chap. IV) and re-establishing capital-account controls and prudential regulation (chap. V).

The key national policy issue for developing countries concerns the space for experimenting with the utilization of a broader range of development tools, while building on existing domestic institutions and capabilities and proceeding along the lines suggested in chapter II. The international community finds itself at the end of the era in which global development was promoted through social engineering approaches that sought to create the preconditions for the emergence of vibrant private markets. The experience in many successor economies of the former Soviet Union suggests that building private markets and releasing private initiative for development are context-specific and that the rapid importation of Western legal and administrative institutions can be costly in human terms. For example, rapid privatization of state enterprises not only led to asset stripping but also dismantled the informal social support mechanisms that had been built up around these enterprises in the socialist period, which led to rapid increases in indigence, especially in the first phases of the economic transition (Ellerman, 2010).

The negative experiences arising from the transition matter just as much as the positive ones. The major lesson to be learned from the post-communist transition is precisely that state institutions are of crucial importance. Whereas the example of the Soviet Union had proved that a non-market economic system with an all-prevailing state cannot be efficient, the transformational recession of the 1990s proved that the market without

a strong state results in the substitution of unaccountable state power for unregulated private wealth accumulation, leading to economic and social decline (Holmes, 1997).

REFORMING GLOBAL ECONOMIC GOVERNANCE

In 2002, in the Monterrey Consensus of the International Conference on Financing for Development, the international community made a commitment to “good governance at all levels” (United Nations, 2002, para. 4), recognizing that striving for good governance at the national level is incoherent if not matched by good governance in international bodies and mechanisms. Commonly accepted norms for good governance might need to be applied systematically to international bodies and processes.

As embraced by the Bretton Woods institutions in their lending operations, good governance is commonly thought to have the following characteristics: transparency, accountability, efficiency (or effectiveness, in common parlance), fairness and ownership (Woods, 2000). The situations in which these general values are relevant are very much overlapping and they need to be applied to the specific operational issues confronting international organizations. Conflicts-of-interest issues may result in the undermining of the values of transparency and accountability. These conflicts of interest exist, for example, in international debt resolution mechanisms where the Bretton Woods institutions, themselves creditors with a material interest in maintaining debt service, have a key role in the Paris Club process, which passes judgements on the sovereign debt obligations (see chap. V). Unfocused agendas and expansion of activities beyond their assigned role in international governance or core competencies violate principles of accountability and efficiency. The expansion of the areas under World Trade Organization disciplines into financial services and investment rules is one product of an unfocused agenda (see chap. IV).

Effectiveness and fairness require that all stakeholders, particularly minorities and small economic players, be assured of having a voice. The question of sufficient voice and participation of developing countries in the design of prudential standards, highlighted in chapter V, is one aspect of this. Fairness and ownership are evidenced through an emphasis on participation and democratic processes. Efforts to accelerate progress in reallocating voting weights in the Bretton Woods institutions to reflect the increased significance of developing countries are consistent with promoting good governance.

Specialization and coordination

By design, the international system relies on specialized institutions and processes to address specific global issues. As discussed in previous chapters, the proliferation of the agendas of existing institutions is a key source of system incoherence. In order to eliminate costly duplication and conflicting policy agendas, the process of defining more precisely the roles of existing institutions and refocusing their existing activities on core competencies—a process that has already begun—needs to be accelerated. The previous chapters have indicated the general directions in which reform efforts can proceed, but have not provided a blueprint. Similarly, this chapter offers general directions—not a blueprint—for strengthening governance.

The World Trade Organization

The World Trade Organization should remain the champion of the multilateral trading system. Its singular role of proscribing engagement in discriminatory trade practices by powerful trading nations should be strengthened. This will require more rigorous disciplines over free trade agreements and economic partnership agreements which not only tend to generate unwanted trade diversion but also rechannel commerce into venues where developing countries tend to be at a disadvantage.

The main thrust of the reform process should be towards helping developing countries secure access to the markets and technologies available in developed countries on a non-reciprocal and preferential basis. Some concrete suggestions relating to the realization of such an aim, were presented in chapter IV, particularly in regard to strengthening and democratizing the World Trade Organization's dispute resolution process. As discussed in chapter IV, the World Trade Organization's agenda has expanded to include trade-related areas, such as financial regulation and migration, whose challenges would be better addressed in more specialized venues.

Most likely, the global regime that emerges from climate change negotiations combined with individual-country climate change policies will have a significant impact on the global trade regime. For example, there are many proposals for border adjustment measures to make up for the negative impact on international competitiveness of domestic environmental regulations. Disciplines under the trade-related aspects of intellectual property rights could prove too restrictive or expensive to facilitate a big push in clean energy investment in developing countries. Reconciling climate change imperatives with existing World Trade Organization disciplines will pose challenges but, as argued in chapter IV,

the process of seeking greater coherence between the two regimes should begin with a conferring of primacy on the objectives of averting the threat of climate change.

Similarly, attempts at strengthening financial regulation and creating more national policy space through capital control are creating tensions with rules of the World Trade Organization regarding liberal trade of financial services under the General Agreement on Trade in Services, where—as suggested in chapters IV and V—primacy in rules setting would seem to lie more appropriately with objectives of global financial stability pursued as part of financial regulatory reforms.

The International Monetary Fund

IMF must play a critical role in operating and managing a reformed global reserve and payments system and must be the venue for multilateral cooperation in exchange rate setting through its surveillance function, under the principles elaborated in chapter V.²

IMF responsibilities and capacities will need to be significantly augmented if macroeconomic policy coordination is to be institutionalized and surveillance strengthened (see chap. V). This will involve extending the purview of IMF to include capital movements. In the years immediately following the Second World War, when the World Bank and IMF were being set up, the focus was on the current account. An emphasis on flexibility evolved into a fostering of unsafe volatility as IMF adopted a hands-off—and even a cheerleading—stance with regard to expansion of private financial flows. As indicated in chapter V, IMF could play a constructive role in assisting countries install, operate and coordinate controls in the capital account.

IMF programmes should simplify conditionality and refrain from imposing trade and domestic governance conditions that are relevant to payments and exchange-rate issues only in the very long term. A more even-handed international debt resolution approach, as suggested in chapter V, would determine that IMF should not be the sole source of macroeconomic programming since it would be a member of the group of creditor-claimants. Debtors, as members of a “cooperative” pool, could accord IMF claims some level of seniority, and on the grounds that IMF is a public entity. The same conflict-of-interest argument would require that IMF, as one of the players in international lending, should not be the coordinator of financial regulation.

IMF must seek to be perceived as an organization basically intent on helping countries deal with payments difficulties while preserving the

growth of their economies, consistent with its articles of incorporation. A more even-handed approach to surveillance, applied particularly to countries whose macroeconomic policies have an impact on developing countries, as discussed in chapter V, is critical in governance terms for protecting the integrity of IMF as an organization that intervenes solely in the interest of ensuring systemic stability. A redistribution of the IMF capital contributions, with greater weight for developing countries, may prove helpful in bringing about the desired reorientation.

Multilateral development banks

Multilateral development banks have a critical role to play in contributing to an adequate flow of financing for development by leveraging global private savings to support critical development projects. In the last decade, the flow of non-concessional financing from the World Bank particularly has been found to be inadequate (if not negative, net of repayments on existing loans), especially with regard to middle-income countries. Increased reliance on private lending by the Bank's potential borrowers has been necessitated by the competitive costs of private loans which do not come with policy conditionality. Rethinking the role of policy conditionality and, by extension, of the kinds of purposes for which multilateral bank resources should be applied is therefore critical to ensuring that these banks are able to fulfil their critical role. There is in fact a possibility that refocusing the activities of multilateral development banks so as to align their lending to national development strategies, including a withdrawal from policy lending, could actually increase the volume and quality of the finance that these banks are able to intermediate for developmental purposes. Genuinely finance-oriented multilateral development banks would steer clear of policy conditionality and this would also be consistent with the donor-accepted principle of country ownership (see chap. III).

In the case of the World Bank, as a result of reform efforts and shifting pressures from donors, which reflect the evolution in approaches to development (see chap. II), its resources are being applied in a wide variety of areas. Currently, the World Bank, inter alia, is a repository of knowledge regarding development, sets standards in the area of debt distress and debt resolution, operates a variety of donor-driven trust funds beyond the reach of its shareholders, and finances not only development projects but also governance reforms in developing countries.

One possible target of refocusing would be the financing of large infrastructure projects, as was the case when the World Bank was first

founded. Similarly, the Bank could have a role to play as an implementing arm of large-scale energy and infrastructure projects in the area of climate change mitigation and adaptation. First, even with liberalized financial markets and financial innovations like build-operate-and-transfer and build-operate-and-operate, the private sector has not managed to generate the kinds of volumes required to finance infrastructure requirements without requiring elaborate government guarantees and standard-setting. Moreover, the fact that large infrastructure projects, such as dams and road construction, are often accompanied by social adjustments and political controversy raises the risks to private financiers. As a public institution, the World Bank can, in its operations, be asked to assist the private sector in the design and co-financing of large development projects within the framework of addressing the adjustment and social issues that naturally arise from these. It can build on capacities already established through incorporating environmental impact assessments in its operations and can apply these techniques in handling other social priorities.

For purposes of coherence, large infrastructure projects financed by the World Bank would need to be part of national development plans in recipient countries (see chap. II). A focus on large infrastructural projects implies that the World Bank could move out of the area of policy conditionality. Policy conditionality had been introduced almost as an accident of history in the 1980s to ramp up financing for developing countries beyond project lending levels. This was perceived to be a means of rescuing deposit money banks in danger of bankruptcy from the sovereign debt crisis through more rapid loan disbursements aimed at funding institutional reform programmes for market-oriented development strategies. Reforming sovereign debt mechanisms (see chap. V and below) should obviate the need for this type of policy conditionality.

Multilateral development banks can also increase the volume of their development finance through bond purchases and bond guarantees, particularly at the regional level, for funds devoted to infrastructure and energy development. Because of the increased probability of the emergence of secondary bond markets facilitated by such intervention, this approach could actually help lead to the development of financial markets locally and regionally and would be in sharp contrast to the previous approach of policy lending intended to facilitate the emergence of private bond markets through deregulatory and liberalization reforms.

Increased use of special drawing rights (SDRs) would open the possibility of expanding the financing activities of the multilateral development

banks beyond intermediating private savings into development projects (United Nations, 2012). Such an approach would be especially appropriate if development-oriented macroeconomic policy indeed became more widespread and the requirements for large scale financing become more prevalent. This would be particularly applicable to climate change financing, which might be supported by allocation of SDRs, assuming that the projects concerned were in harmony with the global climate change regime.

In undertaking a loan evaluation, the World Bank would necessarily incorporate the probability of repayment based on the best available information. However, in the event of a need for debt resolution, because of the conflict of interest, as a creditor institution itself the World Bank should have the status of being one among other creditors, notwithstanding the element of seniority built into the original loan agreement with a public lending institution. Governance principles suggest that if the Bank recused itself from juries that passed judgement on debtor obligations, it would improve internal incentives for effective loan evaluation.

Regional development banks could consider incorporating these same governance imperatives. They could co-finance large-scale infrastructure projects with the World Bank and also focus on development of regional and national financial markets by taking bond positions in those markets (see chap. V). These banks are better placed to participate through their expertise in institutional development in their regions. According to Ocampo (2010, p. 14), “[i]nstitutional development, the creation of mechanisms of social cohesion, and the accumulation of human capital and technological capacities (‘knowledge capital’) are essentially endogenous processes” and are better developed locally.

Missing or weak international institutions

Surveys in previous chapters have identified critical areas that are characterized by a lack of international mechanisms and institutions.

International financial regulation

International financial regulation constitutes the most current challenge. Much of the existing international financial architecture relies on private organizations and, as the current crisis suggests, public oversight over and regulation of those organizations are indispensable. Accounting standards are determined in the private International Accounting Standard Boards, whose activities are mainly financed by large global accounting firms. The

international coordination of equity market regulation is dependent on the deliberations of the International Organization of Securities Commissions (IOSCO). There is also a need to improve private oversight over credit ratings agencies. Chapter V emphasized that financial sectors in mature industrialized economies must bear the additional burden of maintaining financial standards so that their activities do not impose instability on other economies. It also suggested the need for an independent international process overseeing international financial regulatory mechanisms, which would take precedence in rule-setting over the World Trade Organization, because expanding global financial services need to be accompanied by robust regulatory arrangements.

Sovereign debt workout mechanisms

As discussed in chapter V, a new framework for sovereign debt restructuring is critical to developing a stable international financial system that promotes economic development. The existing ad hoc and piecemeal approaches to both official and market-based sovereign debt restructuring have been inefficient and costly, especially for developing countries. Workouts often take place with undue lags which prolong distress and economic hardship and, as a result, the solutions more often than not provided enough debt relief to give debtor countries a “fresh start” in returning to growth. There are two key governance challenges. First, the process should mediate effectively and fairly between debtors and creditors, because this is the best guarantee that enough resources will be made available for a fresh start, which is in the interest of both parties. This means that the adjudication must be lodged with an independent body. Second, the process should be enforceable on all creditors in all jurisdictions, which means that all States must commit to enforcing debt resolution decisions. National courts would have to recognize the legitimacy of the international arbiter and respect its rulings, which would require amendments in domestic contract laws.

Technology transfer

Technology is a critical input to development and a key driver of global inequality and thus is a key arena within which to overcome international asymmetries (Ocampo, 2010). Aside from the World Intellectual Property Organization (WIPO) mechanism, which has dealt mainly with disseminating intellectual property standards internationally, the World Trade Organization intellectual property regime is the only enforceable approach applicable to the international transmission of technology.

As discussed in chapter IV, developing countries must rely on so-called flexibilities to obtain access to needed technology. The need for a development-friendly international technological regime is an issue being debated in connection with the proposed work programme of WIPO.

Environmental protection and climate policy

The Conference of the Parties to the United Nations Framework Convention on Climate Change is the treaty body dedicated to promoting collective action to reduce global warming and to cope with corresponding temperature increases. The Kyoto Protocol to the United Nations Framework Convention on Climate Change binds 37 participating developed countries and the European community to limits on the emission of greenhouse gases. Of the four agreed pillars of the Framework Convention—mitigation, adaptation, finance and technology—the last two in particular have implications for coherence in global economic governance, as has been pointed out in earlier chapters.

The United Nations Framework Convention on Climate Change has inadequate reach (not all countries are party to binding commitments) and limited enforcement capability. Ongoing climate change negotiations must address this weakness. A key governance challenge related to the Framework Convention concerns mechanisms of transfer from developed to developing countries, raising resources to the required levels, and implementation and monitoring in this regard (see chap. V, box V.2; and Clark, 2010). The Framework Convention could be assigned the responsibility for setting overall guidelines, based on treaty commitments, for the contribution and the use of funds. If empowered, it could monitor these flows and evaluate country compliance to commitments.

Migration and labour services

The challenges of establishing a more humane and mutually beneficial migration process were discussed in chapters II and IV. Labour migration requires difficult social adjustments in receiving and sending countries and does not involve only the issue of filling needed jobs. A dedicated multilateral process to deal with these complex issues is needed. As in the case of climate change, the configuration of a future regime is the subject of international negotiations. The recognition by the World Trade Organization that the principle of liberalization also encompasses the movement of natural persons (under Mode 4) represents a significant step forward, even though in respect of applying this principle, developed countries have so

far showed interest mainly in persons with a very high level of education and specialized skills. Meanwhile, based on its many years of work on migration, the International Labour Organization (ILO) has developed a Multilateral Framework on Labour Migration (MFLM), proceeding from a rights-based approach. While focused more on the rights of migrants, the Multilateral Framework also calls for international cooperation to facilitate both temporary and permanent migration. One may note, for instance, that immigrants comprise 88, 71 and 70 per cent of the population in Qatar, the United Arab Emirates and Kuwait, respectively.

Until a more favourable situation emerges for permanent immigration, temporary labour flows could be managed in order to enhance global welfare and protect the human rights of migrants. Given their prior work on migration, ILO and the International Organization for Migration (IOM) might cooperate in creating a global clearing house for world labour demand and supply. Such a global labour regime could bring order to the currently chaotic situation of spontaneously arising labour flows, some of which are illegal, which impose significant costs on the migrants themselves (they sometimes pay with their lives) and often provoke the ire and resentment of the people in destination countries.

Global economic coordination

A corollary of the need for more strongly focused international institutions is the need for a strengthened multilateral coordination mechanism, to ensure that the activities of individual agencies and commissions are not in conflict and do not encroach on each other's purviews. The previous chapters have presented numerous instances of the kinds of agenda-related conflicts that might be adjudicated or even eliminated by such a coordinating council. The mechanisms through which such a council could so act would depend on the kinds of enforcement capabilities with which nation states would be willing to invest it. This will be discussed below.

Additionally, such a coordinating body could address the cases of missing international institutions, as mentioned above. A coordinating body could advance progress by commissioning research reports and convening discussions among key parties. Such a functioning coordinating body, with its own tradition of procedures and working methods, would be a natural venue within which to address the challenge of braking global crises, such as the food, energy and the financial crises.

Bodies already exist that could discharge this needed function. The Economic and Social Council is the United Nations organ charged with

coordinating the economic and social and related work of the 14 specialized agencies, the functional commissions and the 5 regional commissions. Along with the strengthening of governance and international procedures, the Council could be mandated with a coordinating function that encompassed more than just United Nations entities. There have been a variety of proposals regarding the creation of a body along the lines of the United Nations Security Council, the most recent proposal focusing on a global economic coordination council, supported by an international panel of experts (United Nations, 2009d). Among the key arguments underpinning the proposal for the establishment of a more powerful body is that the challenge presented by the current crisis appears to call for a thoroughgoing reform of existing institutions. According to another argument, the kind of interconnectedness of issues that has been discussed in this report requires the presence of such a body.

VOICE, LEGITIMACY AND EFFECTIVENESS

The Monterrey Consensus called for the modernized governance structure of global finance institutions to be more consonant with the fundamentally changed structure of the global economy, which stems mainly from the much greater weight of developing countries therein. The developing countries are also home to a much greater proportion of the human population. Functionally speaking, the argument for an increased voice and participation of developing countries in global governance was based on the need for the users of the resources and services to be assured of the effectiveness, relevance and accountability of those mechanisms.

When the original Bretton Woods institutions were established, their potential users had been allocated a weight of voice and governance that was undoubtedly much greater than what could be justified on the grounds of economic significance in a world in which, by any measure, the United States had the overwhelming economic weight. The argument that providing users with an ample voice would be a guarantee of the responsive and accountable agenda-setting and operation of a public institution applies now as it did then; but in terms of both economic weight and accountability to users, developing countries are underrepresented in decision-making in these institutions. Recently proposed reforms (such as the G-20 targets of a voting weight increase in favour of developing countries of at least 5 per cent in the IMF and at least 3 per cent in the World Bank) are being pursued but progress is very slow. In any case, these reforms would not

offer the ample weight that potential users were allocated in the beginning. Fortright voting reforms in the World Bank and the Fund are critical because their constituency-based systems, enhanced by a system of basic votes, provide a stake in the organizations for the smallest economies, and could be an important model for other international institutions.

As a general rule, voting distributions should be appropriate to the purpose of the organization. In the financing of development projects, a scheme of equal weights in voting power of capital providers and borrowers does have precedents, for instance, within the Inter-American Development Bank, and could constitute an appropriate voting allocation within the World Bank as well. Enlarging the resources and capacities of international institutions over the long term will ensure organizational effectiveness, but will also require the exerting of greater influence by the community of developing countries.

Inequality, exit and enforcement

The main underlying reason for the deficiencies of the current institutions of globalization is the structural inequality of economic and political power between the developed and developing countries (Nayyar, 2010). It pervades various multilateral institutions and bilateral relations and, in a sense, is a legacy of the colonial era.

Inequality

This underlying structural inequality implies that mere changes in formal rules may not be sufficient to counteract the processes of divergence and differentiation and make globalization sustainable. The processes unfolding at the World Trade Organization illustrate this reality. Unlike the World Bank and IMF, where decisions are taken on the basis of subscription- or contribution-weighted voting, the World Trade Organization operates on the basis of the “one-country, one-vote” principle. However, this apparent democratic decision-making process is not doing much to make the World Trade Organization work in favour of developing countries or to make globalization sustainable.

The basic inequality in economic and political strength stymies and effectively nullifies the equality in voting power in one forum (the World Trade Organization), and this is much like what happens through the mechanism of interlocking markets which ties sharecropper to landlord in the model of Bhaduri (1973). When a developing country is tied to developed

countries in so many other ways through unequal relationships, it is difficult for it to assert its equality in one particular arena. Besides failing to influence the outcome of World Trade Organization negotiations, many developing countries fail to otherwise make use of several avenues for remediation that offer formal equality of access. For example, many developing countries find the World Trade Organization's dispute settlement mechanism to be beyond their reach because of the cost and technical sophistication requirements associated with its utilization (see chap. IV; and Toye, 2010). Indeed, it is difficult for a small developing country to take retaliatory measures against the large, powerful developed countries on which it may depend in so many ways (for example, as a source of remittance income), not to mention the simple fact that retaliation is effective only if the size of the trade volume is large, which is usually not the case for developing countries.

Exit

The progressive reduction of global asymmetries is the third criterion for global governance arrangements offered by Ocampo (2010), and is indispensable. The international precedents for application of the principle of differentiated responsibilities stretch back to the GATT; and modernizing the application of affirmative action and protection for the weak is critical to ensuring the increasing engagement of these countries in international commerce. International arrangements arguably would be robust if they provided time-bound opt-out rules (Toye, 2010) for those with a clear incapacity to meet them. The single-undertaking approach of the World Trade Organization makes it difficult to implement such rules (Drache, 2010), and this, combined with its expansive agenda, makes it difficult to reach agreement. Clear, predictable standards with respect to differentiated responsibilities are required.

If there are too many exceptions, of course, there is the chance that powerful countries will exit international disciplines. Exit, which is the ultimate enforcement mechanism available to economically powerful countries, would have a negative impact on developing countries.

The role of caucuses

The emergence of the G-20 as a self-selected grouping arranged to oversee economic recovery and reform has raised many questions about the role of these kinds of formations in global governance. The G-20, which is an expansion of the Group of Eight (G-8), is often described as an improvement. Caucuses' limited memberships are often seen as necessary

for the taking of timely decisions that can be enforced by economic players having the actual power to do so. This criterion of effectiveness in reaching enforceable decisions should indeed be one basis on which all groupings must be judged. In terms of this criterion, the G-20 has succeeded on some fronts but not on others. One notable success is the increase in resources for IMF, which basically involved ensuring that other important economies would support a change in the stance long maintained by the United States regarding the matter.

On other issues, the effectiveness of the G-20 is still in doubt. It has formulated general objectives for macroeconomic coordination without setting out the details of a process of institutionalization (see chap. V). There is no guarantee that the technical designs on international financial regulation requested by the G-20 from the Financial Stability Board and IMF will be accepted by all G-20 members. Countries that are represented both in the G-20 and in official international bodies such as IMF do not have to take the same position in both bodies, making the effectiveness of these kinds of groupings unpredictable. Still, inadequate as they are, only official international bodies have enforcement capability and ultimately caucuses must implement their own decisions through those bodies. Improving the effectiveness of official international bodies with enforcement capability should be a priority shared by all countries and by all caucuses.

The effectiveness of a caucus or grouping in implementing its decisions through official bodies depends on its own internal cohesion, which depends in turn on the ability of all its members to participate fully in its deliberations and accept the group's decisions as their own. The tendency of these groupings to rely, for technical and staff support, on institutions in which some members may feel they have insufficient influence (the G-20, for example, relies on Organization for Economic Cooperation and Development (OECD) and IMF staff) undermines cohesion.

The organization of country groupings is based on a perceived inherent common interest of its members. The fact that new country groupings have presented themselves as acting in the global interest immediately raises the governance issue of representativeness. Using the most expansive determination of the size of the European Community, G-20 members like to point out that they account for 91.5 per cent of world gross domestic product (GDP) and 66.5 per cent of the world's population. These highly documented demonstrations of representativeness still violate principles of fairness and recognition of the rights of the weak and minority interests, which are unlikely to be internalized by members. There do exist representative

organizations, such as the United Nations, but their effectiveness has been questioned. That there is a parallel existence of groupings claiming global reach, on the one hand, and of globally representative organizations, on the other, does act as a spur to both types of entities to raise their effectiveness and representativeness. Establishing channels of communication and coordination between these two kinds of global body must be a priority.

Enforcement mechanisms

At this juncture, the international community has only one effective enforcement mechanism in place, namely, the dispute settlement mechanism, which is able to generate binding rulings that authorize countries to impose trade sanctions on others. It happens to be based in the World Trade Organization, and this is one reason why many countries find that it would be in their interest to expand the World Trade Organization agenda. This approach relies on the Westphalian principle that sovereign states are the world's highest-level independent actors.

Chapter IV has discussed how, even within the World Trade Organization, the dispute settlement mechanism is heavily skewed against countries with small markets and small public sectors. As an enforcement mechanism, it appears to be quite effective. Should such a mechanism be applicable in other areas, though perhaps not through the World Trade Organization? Assuming that a strengthened Economic and Social Council or a global economic coordinating council could adjudicate cases in the same way that dispute panels in the World Trade Organization do today, should trade sanctions be the enforcement instrument of choice?

Other proposed enforcement mechanisms either have, historically, been proposed or, like the “scarce currency” powers of IMF, exist but are not applied. The scarce currency sanction (under article VII of the IMF Articles of Agreement) represented a compromise with the original Keynesian proposal that IMF function as a genuine currency union where countries would have to pay a penalty on surplus payments balances. Such penalties would have provided debtor nations with unrestricted access to the clearing fund without having to seek approval or make domestic adjustments. Following the rejection of the idea by the United States, a compromise was reached in the form of the scarce currency clause which authorizes, upon the determination of IMF, capital restrictions and trade discrimination against countries with chronically excessive trade surpluses. An assessment in the United Nations report on the *World Economic Situation and Prospects 2010* (United Nations, 2010, p. 94) led to a proposal to consider

another type of enforcement mechanism involving the imposition of sanctions on countries for non-compliance with internationally agreed prudential regulations.

In the monetary-financial area, there are effective mechanisms for enforcing changes in domestic policy, but these have been applicable only to debtor countries, through Bretton Woods programmes. Greater enforcement power over countries whose domestic policies have systemic impact could potentially elevate the role of the Bretton Woods institutions internationally: rather than enforcers of the collection of international claims on developing countries, they could become genuine instruments of global governance.

WHAT IS TO BE DONE?

The risks associated with the deeper interdependence of national economies exposed by the crisis can foster a drastic retreat from globalization. There are, however, feasible approaches to initiating more sustainable globalization processes. The previous chapters have examined various approaches to retooling the existing aid, trade and financial architectures with a view to filling such gaps and eliminating such traps in the international system as undermine development efforts. Overcoming institutional weaknesses in the key international organizations, such as IMF and the World Bank, and eliminating inequities in respect of the access to participation, particularly at the World Trade Organization, are also important. There are glaring inadequacies in the global coordination of economic decision-making, including conflicting agendas and conflicting rules in the areas of trade, aid and debt.

The previous chapters have identified a number of challenging directions for reform, including:

- Providing sufficient policy space for developing countries so as to allow them to deploy a broader range of development policies
- Reforming the technology regime, particularly in the light of the climate change challenge, so as to ensure greater access for developing countries
- Reforming the global regime overseeing international labour flows
- Establishing and resourcing coordinated counter-cyclical mechanisms among economies
- Coordinating international financial regulation and controlling regulatory and tax competition among countries

Retooling the rules of the game for a fair and sustainable global development is necessary, but not sufficient. Retooling is also about the players. Providing developing countries having weaker initial conditions with more of the time, resources and policy space needed for them to become full participants is to be regarded not as an act of charity or goodwill on the part of the powerful but as an imperative for realizing the shared goal of expanding international commerce. The principle of common-but-differentiated rights and obligations, which are to be defined as a function of level of development, will need to be applied in practice and embedded within a system of clear-cut rules.

Reshaping rules is easier said than done. Players will need to agree on the common global sustainable development goals to be pursued and will need to be convinced that cooperation will provide net benefits for all—benefits serving present and future generations. However, within any scheme of international cooperation, net benefits may be perceived as not being equal for all; and any expected unevenness in outcomes may impede the reaching of effective global solutions. Because of differences in living standards, and therefore in capacity to pay, some countries will be expected to shoulder larger shares of the total costs of providing global public goods, which may reduce their incentive to cooperate in providing them. Hence, with respect to establishing multilateral agreements, the proposed pattern of burden-sharing is as important as the extent of the benefits to be conferred by the public goods.

The international community must face a key fact, namely, that the pattern of uneven development brought about by globalization so far has been sustainable neither economically nor environmentally, nor has it been feasible politically. As this time around, developing countries are much more significant and much better integrated into the world economy, the global crisis has profounder implications and more serious consequences for development. While the present crisis only highlights the ever-present risks associated with the deeper integration of national economies into the world economy, the issue is not so much a retreat from globalization, as a feasible reshaping of the globalization process. The proposed means of retooling the existing aid, trade and financial architectures aim at overcoming present shortcomings.

There is a need to strengthen the global coordination of economic decision-making so as to minimize the number of cases where rules dealing with trade, aid, debt, finance, migration, environmental sustainability and other development issues come into conflict. At present, there is no

international agency dealing systematically with questions of coherence and consistency in multilateral rules-setting. The global crisis has provided painful evidence of the weaknesses of the present system. The issues of climate change and demographic changes demand even greater coherence among the spheres of global governance and between decision-making processes at the global and national levels. Whatever its shape, international coordination based on shared principles and transparent mechanisms is more urgently needed than ever.

NOTES

- 1 Para. 8. Available from http://www/g20.org/Documents/g20_summit_declaration.pdf.
- 2 The Commission of Experts of the President of the United Nations General Assembly on Reforms of the International Monetary and Financial System proposed to replace IMF with a totally new organization, having the capability from its inception to create global liquidity (see United Nations, 2009d).