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Systemic Issues and Changes in the Global Institutional Architecture

In mid-2001, supranational (and national) processes, institutions and mechanisms for effective global governance – in a world that has been globalising very rapidly over the last 15 years – are obviously inadequate. They have been inordinately slow in responding to the demands of rapidly changing circumstances. They lag too far behind the reality of globalisation for it to proceed as smoothly as it should, or for ironing out the asymmetric concentration of its gains and losses across countries in real or conscionable time. In addressing these truisms, SGR makes 22 recommendations about what might be done to remedy the situation. Of these only two involve specifically actionable measures.

SGR makes the case that the UN should be the centrepiece of any future system of global governance; with other international institutions being well-articulated parts of the UN system and coming under a single UN roof. Unfortunately the case is unconvincing. It is presumptuous and axiomatic. It ignores the failings of the UN system which make it: (a) a dysfunctional bureaucratic quagmire; (b) impervious to the tenets of organisational logic and to a long overdue requirement for streamlining and rationalisation of its multiplicity of fragmented agencies, programmes, conferences and funds determined to maintain their own unviable identities; and (c) immune to the principles of sound institutional management. In short, the UN appears incapable of governing itself properly and thus lacks the public credibility needed for it to be the pivot around which any future system of global governance might revolve.

8.1. Systemic Issues Raised by the Zedillo Panel Report

Perhaps with this deficiency in mind, ZPR is more cautious and selective about its views on systemic issues and modifications in the existing global architecture and limits itself to the following seven key recommendations:

- Increase the administrative budget of WTO substantially to enable it to provide a wider array of assistance to its developing member countries;
- Establish a small steering group in WTO responsible for negotiating consensus on future trade accords among member countries;
- Strengthen and reform the ILO to deal with the issue of labour standards;
- Collapse and consolidate the various intergovernmental environmental bodies that exist into a single Global Environment Organisation with a standing equivalent to that of the WTO, IMF and World Bank;
- Prune back conditionality applied by the IMF and World Bank to the bare essentials required and correct anomalies in the governance of these institutions in which industrial countries have the majority (and the decisive voice);
- Create a new International Tax Organisation to: (a) cope with a world in which the principle of national territoriality is becoming obsolete and which permits, if not encourages, legal tax avoidance by individuals and corporations that have multiple

domiciles; (b) recapture the increasing proportion of public revenue that is not being collected because it is falling between the cracks of tax jurisdictions inhibited in their reach by national boundaries; (c) limit, if not eliminate, harmful tax competition among countries; (d) conduct research, engage in surveillance of emerging tax policies and developments, permit multilateral sharing of tax information, and provide a forum for co-operation and co-ordination among national tax authorities; in due course (e) develop and secure international agreement on the unitary taxation of multinational entities; and (f) develop, negotiate and operate international arrangements for the taxation of emigrants;

- Convene a Global Economic Governance Summit as a prelude toward enshrining it as an Economic and Security Council within the UN.

ZPR's seven recommendations have been made on the basis of reasoning that appears artificially truncated. It is perhaps limited in presentation to avoid making the report too long, thus omitting the deeper deliberation that probably took place in Panel discussions. Its recommendations are, in some respects, sweeping and have substantive implications. By the same token, it is silent on key issues, especially on global financial architecture, that are of great concern to developing countries. The following sub-section attempts to deal with these issues in greater depth.

8.2. An Agenda for the Commonwealth

Reforming the WTO

The WTO was set up after the Uruguay Round to ensure that future rounds of trade liberalisation were not 'zero-sum games' but 'positive-sum games' from which all sides won through a progressively liberalised, open world economy. It is widely perceived – in the developing world, labour organisations and proactive NGOs (euphemistically labelled civil society) – that the rules of the game in international negotiations, and the dice used to play the game, are loaded in favour of global firms, mainly from the developed world. These entities are seen to have an embedded structural advantage in terms of greater financial, managerial, technological and institutional capacity, as well as domination of cutting edge knowledge that will shape future products and markets. When competitors from developing countries learn how to play the game and pose a competitive threat, as in East Asia, the rules and/or dice are changed. Such perceptions are adversely affecting the implementation of Uruguay Round Agreements and delaying a new round of WTO negotiations. These were to have begun in 2000 but were derailed by the failure of the Seattle meeting in November-December 1999.

One reason for WTO negotiations being stymied is that the expectations generated by the URAs are not being realised by developing countries to the extent anticipated. The positive-sum game is turning out to be a zero-sum game after all. TRIPS and GATS are proving to be extremely problematic for most developing countries. Through the 1990s, there has been backsliding by OECD countries on a variety of their UR commitments. They have not yet liberalised trade in agriculture and textiles. Arrangements that were agreed to provide special and differential treatment for the least developed countries have not as yet been legislated for by many OECD countries. Yet pressure is being exerted on developing countries to open up sensitive markets in telecommunications, transport and financial services, and in government procurement, that OECD firms have an interest in dominating. At the same time, issues have been introduced for the new round that developing countries are deeply concerned about, for example labour and environmental standards. They believe that such standards are being introduced into trade discussions not on their merits but as devices to justify continued protectionism on the part of industrial countries. There has been increasing, often unfair, resort to contingency protection measures against imports from developing countries with frequent resort to litigation that violates the spirit of the URAs.

Developing countries have been unable to cope with the administrative and legal workload imposed by URAs and by delaying tactics being deployed by industrial countries to slow down market opening. Many developing countries face serious difficulties in implementing these agreements and drafting the domestic legislation that would bring them into force. Most do not have the institutional capacity to do so. The investment required for improving the institutional and negotiating capacity of developing countries to cope with another round of trade negotiations has not been made. As a critical part of the global institutional architecture, WTO's organisation, governance and functioning need to be geared more toward enhancing the knowledge and capacity of its developing member countries than they are now.

At the moment WTO is too small and too driven by OECD country interests to be as useful as it should to its developing members. Its transformation from GATT – which was a rich country club – is still incomplete. Whereas the IMF and World Bank need to be shrunk in size and scope, the WTO almost certainly needs to be enlarged but in an intelligent manner.

Hemispheric and region-to-region dimensions, as well as certain preferential dimensions of arrangements such as those between the ACP (African, Caribbean and Pacific) countries and the EU, need to be accommodated in the process of continued trade liberalisation rather than treated as exceptions to global rules. WTO's processes and staff capabilities need to facilitate such hemispheric and region-to-region trade dialogue in virtually every region, while ensuring its compatibility with the emerging global regime. To avoid circuit overload in developing countries in dealing with all of these issues during a new trade round, WTO will need be more responsive, and provide substantially more technical and advisory assistance to developing countries than it was able to do under the Uruguay Round. Its present budget, staffing and institutional capacities simply do not permit this.

For all these reasons, ZPR's recommendation that WTO's administrative budget, staffing and overall institutional capacity should be increased should be supported by Commonwealth Finance Ministers. They should ask at UNCFD for a plan of action from WTO's management outlining the steps to be taken towards making it a more accessible organisation for its developing country members and lessen its institutional bias in catering primarily to the interests of its industrial country members who now account for the bulk of world trade but are unlikely to do so in coming decades.

Labour Standards and the ILO

ZPR's recommendation that labour standards should be delegated to the ILO should be supported by Commonwealth Finance Ministers. Industrial countries need to agree to this proposal and co-operate in strengthening the ILO sufficiently to develop appropriate standards that take into account the structural attributes and characteristics, as well as levels of income and stage of development, of developing countries and their labour markets. In doing so, ILO must avoid the trap of being too heavily influenced by trade unions in industrial countries that are determined to see unrealistic and inappropriate standards applied to developing countries. Such insistence is aimed at diminishing the trade competitiveness of developing countries and amounts to imposing protectionism through an indirect route. ILO must also develop the capacity, the credibility and the legitimacy to propagate voluntary adherence to agreed but properly attenuated labour standards and enforce such standards when this becomes necessary. In supporting this recommendation, Commonwealth Finance Ministers should ask for a study that would outline the practical and cost implications of implementing this proposal before endorsing it in practice.

Environmental Issues and the Global Environmental Organisation

ZPR's recommendation that all international environmental organisations should be consolidated into a single GEO is unarguable in theory and in principle. It might well facilitate overdue institutional rationalisation in a key area of global concern. But this recommendation appears to have been made without awareness of its practical implications. ZPR does not provide any indication that the Panel was aware of how many such organisations there are at present, under which parent agencies and umbrellas they are located, how they are funded and managed, and how they interact (or fail to). It provides no indication that the Panel was aware of what these multifarious agencies do, why they exist, how they are co-ordinated and what the net result of the present situation is. Until these aspects are clearer, Commonwealth Ministers run the risk of endorsing and supporting a recommendation that may be sound in theory but inoperable in practice.

Many large environmental units are located within the MDBs as part of their departmental structures. One significant institution – the Global Environmental Facility (GEF) – is effectively a joint venture between the World Bank and UNEP but is run under the aegis of the World Bank. It is unclear how much these units cost, exactly what it is they do, how effective they are and what their objectives are. It would be unwise for Commonwealth Ministers to take any position on this issue – except to say that it is an idea that should be examined further – until: (a) an exhaustive inventory has been undertaken of all the international and multilateral environment units and agencies that presently exist and their parent organisations; (b) an assessment has been made of whether the extant fragmented structure is dysfunctional or not; and (c) how consolidating them into a single GEO would work, what the governance mechanisms would be, how voting power would be distributed and how much this would cost.

The Official Financial System and the Bretton Woods Institutions

ZPR's treatment of the global financial system and the urgent need to change its architecture to accommodate evolving circumstances, is weak. Its analysis is conspicuous by its absence and does not address the concerns of developing countries. With the breakdown of the Bretton Woods Agreement in 1971, followed quickly by the first oil shock in 1973, a spate of financial crises have occurred with destabilising effects on the global financial system. Post-1971, the world has seen a departure from the stability of a fixed exchange rate system that brought with it 25 years of unprecedented stability and prosperity. Since then the world of global finance has become more uncertain and fraught with risk for countries that are not industrialised and are financially and economically weak.

Since 1971 much has been learnt about how and why financial crises arise and about the usefulness and effectiveness of the different kinds of measures attempted to remedy them. In one way or another, apart from the ever-pervasive issues of policy and governance, all these crises relate to the adequacy and appropriateness (i.e. type, concessionality, terms and tenor) of the financing made available for development before the crisis occurred. The 1970s were shock-prone, with tectonic shifts in the pattern of global resource transfers altering the foundations of international finance. It was the post-1982 era, however, that witnessed repeated default in response to the successive financial shocks that derailed development. In light of this, developing countries have been pressing for overdue reforms in the policies, instruments, *modus operandi*, governance arrangements and architecture of the IFIs and the international financial system. Apart from their basic problems with (and lack of sufficient influence in) the governing structures of the principal IFIs, developing countries have become concerned about a systematic bias in these institutions toward crisis management remedies that result in greater dislocation and structural damage in developing countries than is necessary or desirable before recovery occurs.

The contrast is striking between remedies applied when a financial crisis threatens, or a recession looms, in *industrialised* countries (for example in 1971, 1987, 1994 and 1998) and when these events occur in developing economies. In the developed world the usual policy-response combination is for domestic and global liquidity to be loosened, fiscal policy to become more accommodating, internal corporate debts to be quickly re-organised through orderly proceedings to avert bankruptcy, co-ordinated OECD central bank action being taken to stabilise global exchange and interest rates, social safety nets being widened and strengthened, with contingency financing being made available to facilitate expeditious economic restructuring in order to ensure a rapid rebound.

When a financial crisis occurs in the *developing* world (1982, 1985, 1994–95, 1997–98, 2000–01) the policy response is the opposite. Domestic liquidity is stifled through draconian increases in interest rates, ostensibly to stabilise exchange rates and avert capital outflows, though this rarely happens as quickly as anticipated. Exchange rates are devalued and/or floated, resulting in either spiral devaluations thereafter (for example in Africa) or free falls and excessive overshooting on the downside (in Asia) before any attempt is made at stabilisation. Fiscal policy is simultaneously tightened with wasteful recurrent expenditure being protected (because of the absence of time, in a crisis, to create the necessary political consensus for cutting it), but essential development investment being cut back, along with subsidies that protect the poor. Budget cutbacks result in the reduction or elimination of social safety nets. No contingency financing is made available and debt-rescheduling policies are applied that make early economic recovery almost impossible.

The stark asymmetry between the ways in which financial crises in the industrial and developing worlds are managed has two different outcomes. It ameliorates financial, economic and social costs in industrial countries, while it exacerbates those inflicted on developing countries, particularly on the weakest countries and the weakest segments of their societies. In some instances, for example Indonesia, *financial* crisis management has a hidden *political* agenda on the part of creditor nations (and the IFIs they control) in achieving a change of regime. The success of Malaysia's home-grown approach to crisis management has been arguably more successful than events in Thailand and Indonesia where external interlocutors played a controlling role. It offers a contrasting alternative to the IFI template if developing countries are bold enough, and resourceful enough, to shun the ministrations of these institutions and take the risk of devising their own approach to crisis management.

Crisis management in developing countries has another peculiarity. Foreign private creditors, who often trigger a crisis through imprudently excessive short-term lending followed by panic withdrawal that drains reserves and creates a run on the currency, are invariably the first to be bailed out at public expense. The immediate gains of crisis management are thus privatised and exported, while the costs are socialised and borne by the poorest segments of society in the country affected. Consequently, the crisis is prolonged with all its attendant costs in terms of corporate bankruptcies, loss of export markets, increased unemployment and retrenchment, with almost no funding for retraining, retooling of skills and re-absorption of the labour force. What starts out as a financial crisis, resulting from creeping disequilibria exacerbated or detonated by an external shock, becomes a structural social and political crisis (for example in most of Africa and Indonesia).[53]

This entrenched asymmetry in policy responses to crisis management bears further scrutiny. It is becoming less acceptable to developing countries as the theoretical and practical justifications for these divergent policy responses are inexplicable. It simply reflects the structural reality that the present international monetary system, and the policies governing it, have a systemic bias toward protecting the interests of creditors (official and private) in industrial countries while prejudicing the financial and economic interests of developing countries. For the latter, international liquidity is artificially limited, unevenly distributed and inaccessible. In a crisis they are compelled to pay an excessively heavy price over which they have no say and no control.

On the other hand, issuers of international reserve currencies reap significant benefits by way of seignorage, large cash holdings of their currencies in safe-haven accounts (including holdings from illegal capital flight as well as proceeds from criminal activity) on which they derive a large interest-saving benefit. Their advantaged position confers on them the ability to borrow almost unlimited amounts in their own currencies, if not formally, then by having their otherwise unsustainable current account deficits financed through capital inflows reflecting purchases of their debt obligations or inflows of foreign direct and portfolio investment. This enables them to incur larger current and capital account disequilibria for longer periods of time without dislocating adjustments being forced upon them by either the world community or by any agency. They have the ability to inflate or devalue their way out of debt or pass on the costs of their own delayed adjustment to other participants in the world economy.

Since the mid-1970s, mutual support arrangements among members of the G-7, the OECD and/or EU clubs have enabled developed countries to elude the disciplines of the IMF in managing their monetary, fiscal, trade and exchange regimes in ways that contribute to a wider global interest. They are no longer subject to official international criticism (except of the mildest variety in the annual Article IV surveillance reports that are produced). Nor are they obliged to take corrective measures when their policies impinge directly and adversely on the interests of developing countries. The implicit notion is that these few countries are developed enough for their *national* policy-making mechanisms to suffice in exerting the necessary economic disciplines and self-correcting measures in order to avert crises while other countries must have *extra-national* discipline imposed on them.

That conviction has resulted in seven countries placing themselves beyond international discipline and deploying power asymmetrically (through G-7 that also controls OECD) to manage the global economy, govern the conduct of international finance and control the IFIs. The appropriation by G-7 of the right to make all the critical decisions affecting the global economy, without participation by others, has resulted in the arrogation of global power without the necessary global consensus legitimising this model of economic domination.

53 The exception was the Tequila crisis of 1994–95. It was more sensitively handled by the IFIs (under the watchful eye of the US Treasury Department) to avoid the spill-over into the USA of yet another crisis in Mexico.

Though not explicated as a salient feature of the present global financial system architecture, the G-7 arrangement has effectively resulted in a hierarchy of nations differentiated by the degree of sovereignty they retain over their economic affairs.

A global caste system has now emerged. It has two major divisions – the industrial and developing worlds. In the first division, G-7 members are the *brahmins*; larger member countries of the OECD/EU clubs (the warriors) come next; with the smaller economies of the same clubs (the merchants) occupying the third tier of the first division. The second division is headed by seven or eight of the larger, littoral developing powers (not necessarily with the highest per capita incomes) in the fourth tier (the servants), followed by middle-sized, middle-income countries in the fifth, and the least developed countries (the untouchables) in the sixth.

The application of greater imagination might yield a larger number of castes and a different basis for determining their memberships; but it would not invalidate the point being made. What has evolved in the post-Bretton Woods era is a global financial system in which developing countries have little or no influence. Nevertheless, they are obliged to accept its oppressive, neo-colonial disciplines and strictures. Continuing dissatisfaction with the way in which such a system operates will weaken it and make it increasingly dysfunctional. That is not in the interests of the industrial or the developing worlds. UNCFD presents an opportunity to scrutinise thoroughly, but dispassionately, how the international financial system and the IFIs are evolving, and to consider measures that deflect them from the path of eventual paralysis and change their evolutionary trajectory in a way that restores their functionality.

With the shift that has occurred in managing the balance of payments under the pressures of globalisation, and with developing countries moving progressively toward opening their current and capital accounts, their requirement for balance of payments financing, and especially for large amounts of emergency balance of payments support in the event of a financial crisis, are changing. The financial crises of the 1990s suggest that in countries that rely on private capital flows to finance their development, managing movements on the capital account – especially the inward and outward surges referred to earlier – is becoming more important than managing the current account. Such countries need to hold sufficient international reserves to give global markets a sense of comfort and to convey an image of credibility and liquidity, as well as having the robustness to withstand occasional financial tremors.

The issue for these countries is no longer a matter of the number of months of imports that their reserves can finance. This has become almost irrelevant, as long as countries retain sufficient creditworthiness and market standing to obtain large credit lines from global banks and mobilise resources from global financial markets to fund their 'working capital' requirements for regular trade. Instead, the focus is now on whether they have sufficient reserves to withstand a sudden outflow of their liquid foreign capital liabilities – especially foreign-held portfolio equity and short-term bank borrowings – without incurring the risk of recession-inducing monetary policy and a collapse of currency values. It is not just the extent of FPI and short-term bank borrowing that heightens their vulnerability. Recent experience suggests that when a crisis looms, even foreign direct investors (and domestic investors) are becoming sophisticated risk-managers in reducing their net exposure to a troubled economy. They borrow (from domestic sources) against their asset holdings and move that liquidity abroad, thus hedging their risk of loss. Hence even immovable foreign assets can be liquefied and add to volatility.

Of course, not all developing countries are in this situation as yet. As recognised earlier, private capital flows to the developing world are concentrated in the 25–30 larger and more industrialised developing countries that account for the bulk of the population, trade, reserves and output of the developing world. The 175 or so other developing countries include about 55 poorer countries in Africa, South Asia and East Asia, and more than 100 small middle-income countries, including island micro-states dependent for their export earnings on tourism, sugar, bananas, rum or copra. This numerous, but mixed, group of countries continues to have the old problem of managing their external accounts; they remain vulnerable to sudden shifts or secular declines in prices of (and demand for) their primary exports. They are also particularly vulnerable to the vagaries of nature – cyclones, floods, droughts and earthquakes – as well as to movements in global exchange rates and overall economic conditions in their major markets. Since the 1980s, many of these economies have become burdened with debt overhangs beyond their capacity to service on contracted terms.

When disequilibria in *current accounts* were the only matter for concern in ensuring adequate balance of payments support – in the event of sudden changes in circumstances – the extant instruments and facilities available to these countries from the IMF, the World Bank or the regional and sub-regional development banks, in meeting their needs were inadequate. That reality was borne out during the three successive energy price shocks of the 1970s, and in the global interest rate shock of 1981–82 that triggered the debt crisis. Since 1990, a substantial increase in private capital flows has created the added need, on the part of the larger developing countries, to manage their capital accounts adroitly as well.

If the external resources available to the IFIs to manage transient current account balance-of-payment crises were insufficient, it is obvious that the system does not have sufficient resources to cope with unanticipated disequilibria in capital accounts as well, regardless of what the IMF believes. The deficiency would become tragically obvious if financial market crises were to erupt and contagion spread across even 15 of these 25–30 countries leading to systemic failure. To an extent, that reality is compelling too many developing countries to hold much larger levels of reserves (over $850 billion) than was formerly necessary or financially desirable. Reserves in many of these 25–30 countries are approaching or exceeding levels that would finance 12 months of imports. The cost of such holding such reserves can be unduly high, especially when they are borrowed and do not represent accumulated current account surpluses.

With each crisis that occurred in the 1990s, calls were made to increase the resources available to the IFIs and to create new financing facilities and contingency mechanisms that would be prophylactic as well as curative, in nature. Though some ideas were floated in the late 1980s and early 1990s, they gained momentum and currency with the crises of 1994–5 and 1997–8. Intellectual, policy, institutional and instrumentation advances on these issues have been made, for example the compensatory and contingency financing facilities that have been developed in the IMF. But progress in this direction has not been as rapid or as wide as evolving circumstances require. Too many developing countries that might find themselves in balance of payments difficulty would be at risk in the event of a systemic, contagious crisis affecting several countries simultaneously. With increasing regionalisation of trade and investment, especially in Asia and Latin America, such a risk cannot be dismissed.

Regional Monetary Funds

In Asia and Latin America there is an immediate need to create a second line of defence to cope with sudden balance of payments disequilibria at the *regional* level through the creation of appropriately designed institutional, instrumentation and financial capacity that would result in the equivalent of a *regional monetary fund* (RMF). The idea of establishing such funds should constitute a basic plank in the platform of developing countries at UNCFD. But the specific modalities, structures and frameworks for such regional funds need further exploration. Different types of frameworks may be needed in different regions rather than all such arrangements being based on one standard template.

An RMF could be linked to existing regional or sub-regional development banks (i.e. those that are financially quite strong). Alternatively, it could be an independent, free-standing institution in its own right. In that connection it is interesting to ask whether, if the Bretton Woods Conference were taking place today, instead of 55 years ago, it would result in a separate IMF and World Bank or whether the two institutions would be fused. The answer to that question should guide thought about whether an RMF should be linked to RDBs or be separate. By the same token an RMF could be a loose arrangement providing a framework under which participating central banks took a cascading set of pre-agreed measures to cope with a crisis, snuffing it out before the risk of contagion spread. Alternatively, it might be a tighter arrangement mirroring the IMF in the same way, for example, that the regional banks mirror some of the capacities of the World Bank (the wrong model for them to follow in the twenty-first century).

8.2.5.3. Some of the functions of the RMF and its institutional provisions may also require a design that permits some of the activities performed by the Bank for International Settlements (BIS) at the global level to be performed at the regional level under the same institutional structure as the RMF. Two key conditions are paramount in creating RMFs: (a) the involvement of the developed countries of the region – the USA and Canada in the case of Latin America and Japan in the case of Asia – to convey to markets the strength of resolve and financial capacity behind them; and (b) a larger voice for developing countries in the application of these funds and the triggering of their facilities than they have in the IMF. In retrospect, the Japanese proposal to create an embryo for such a fund in Asia in September 1997 was an opportunity that should have been accepted and followed through. In 2001 it certainly needs to be revived.

Bolstering balance of payments support at the global level: Under the above proposal, in the event of a balance of payments crisis, a country's own reserves and stand-by credit lines would represent the first line of defence. The RMF would provide the second. There would still need to be a third line of defence at the global (IMF) level. It is possible, that *if* a regional line of defence is created, and *if* the additional resources needed to support developing countries in a balance of payments crisis are allocated to that tier first, then there may not be a case for adding to the resources that already exist with the IMF. This issue, along with the configuration of facilities and instruments at the regional and global levels respectively, and the co-ordination of institutions acting at those two levels, needs to be more carefully considered at UNCFD.

Given the implications of the RMF idea, and the number of issues that need to be examined and resolved in connection with it, it may be premature to attempt to examine and resolve all the pertinent issues and reach agreement on creating RMFs at UNCFD. But it would be the right occasion on which to introduce the concept and to agree on a time-bound plan for following through on its implementation, with RMFs in Asia and Latin America being in place within two years of UNCFD being concluded. RMFs would obviously incorporate some arrangements involving the pooling of reserves and swap facilities among the central banks of the participating countries of the region. But such arrangements may need to be bolstered by formal agreements with the IMF to avail of its facilities through the RMF.

The SDR-FfD Link

In the same connection, the idea of an SDR-Aid link should be revived. The creation of RMFs may require a new SDR issue with SDRs created under the new issue being allocated to the RMF quotas of countries, where RMFs exist, and to their IMF quotas where they do not. This issue should be revisited under the new circumstances that have emerged, although these will keep changing and evolving as globalisation proceeds.

Reforming the International Financial Institutions

The need for root-and-branch reform of the Bretton Woods Institutions, i.e. the IMF and World Bank, has been discussed *ad nauseam* since the Bretton Woods regime ended in 1971. But it has never been properly attempted. Instead a series of steps have been taken in response to crises and the need to address FfD needs. A patchwork of measures deploying the IMF, World Bank and the regional development banks has been cobbled together on different occasions to cope with the various financial crises that have occurred since 1973. On each occasion demands have been made for more durable arrangements to be put in place. But that task has yet to be undertaken. It remains puzzling that a wiser, more far-sighted approach to modifying the global financial architecture has proved so elusive. That a better division of labour, along with improved co-operation and co-ordination, is needed among all the institutions in the *official* multilateral system is beyond dispute. But it has yet to be acknowledged that these institutions are really parts of a single *official* financial system.

Reform of the IFIs should be a priority at UNCFD. The objectives should be to change: (a) the roles, orientations, governance structures, management selection processes and *modus operandi* of these institutions in financing development; and (b) the way in which IFIs respond to structural or transient disequilibria in the external and internal accounts of developing countries. Reform should aim at making these institutions more transparent, participatory, democratic, development-friendly, and more supportive of developing countries, while being less oppressive and intrusive in their approach.

To begin with *the weights of developing countries within the quotas and shareholding of these institutions should be changed as soon as possible by using PPP exchange rates rather than nominal exchange rates in the standard formulae that are used to calculate quotas in the IMF, shareholdings in the World Bank (and regional banks) and voting rights in these institutions*. Such a step would go a long way toward reflecting more accurately the reality of the global situation, including the increasingly important role of developing countries in the global economy and their growing share of global output (45 per cent at PPP exchange rates vs. the 22 per cent reflected in nominal exchange rate comparisons).

In a globalising world, it is neither tenable nor acceptable that developing countries should be indefinitely (if not permanently) disenfranchised as second-class ticket-holders in the IFIs. Nor should industrial countries remain permanently as the only legitimate holders of decisive authority and power while, at the same time, exempting themselves from the surveillance and disciplinary functions that IFIs are supposed to exercise in the global interest. It is often the case that crises in developing countries have their origins in the imbalances that build up in industrial countries and that trigger large external shocks. Developing countries are then drowned in the backwash.

In contemplating IFI reform, particular attention needs to be paid to: (a) the nature and adequacy of capital flows (and particularly of net transfers) from IFIs to developing countries; and (b) the roles and mandates of IFIs, including their roles in influencing national decision-making, governance and patterns of development through the conditionalities imposed. In the interests of inducing more transparent, fairer and better performance on the part of the BWIs, autonomous, external governance mechanisms involving experienced senior global statesmen from around the world need to be established to evaluate, monitor and critique the work and performance of the BWIs on a five-yearly basis. These commissions should be detached from the managements of IFIs, their evaluation offices, which are not independent despite their claims to that effect, and from their Boards of Governors and Executive Directors. The mandate of these independent bodies should be to hold the IFIs accountable for the outcomes of their prescriptions in developing countries, and to moderate the excessive influence of some industrial countries over the activities and policy orientation of the IFIs.[54]

The case for revamping the architecture of the international financial system rests on three realities. The *first* is that financial globalisation will occur at an accelerated pace. This will happen irrespective of whether it is seen as good or bad. It is inexorable. The *second* is that the risks of damage to the global economy and to the stability of the global financial system are too great to incur if financial globalisation occurs through a purely *laissez-faire* approach. *Third*, official or quasi-official intervention capacity to cope with regional or global financial market disruption is necessary. Such intervention has to provide compensating capital inflows to balance sudden outflows triggered by financial shocks and market failure. The institutional capacity for undertaking such intervention needs to reside in the IFIs. What appears to be missing at this juncture is an effective mezzanine *regional* tier of intervention in present global financial architecture.

Experience in several emerging markets over the 1990s suggests that financial market failures will probably become more, not less, frequent as globalisation intensifies. Such failures are not exceptions that can be avoided at any cost. They are unavoidable when capital flows at great speed in large volumes across borders into markets with different levels of capacity, liquidity, efficiency and institutional development. In small illiquid markets incapable of absorbing the shocks of large capital surges, financial and asset price distortions *will* occur when standards for regulation, transparency, accounting, disclosure and valuation are inadequate. In such instances, opportunities for arbitrage in differential operating and regulatory standards can and will be exploited. That should be expected even though it is officially frowned upon or condemned. It cannot be stopped by fiat.

The answer is not simply to inhibit capital flows till markets are better developed. It lies instead in developing more rapidly the capacity of all financial markets, and particularly emerging markets, to cope with capital flows that will occur anyway, efficiently or inefficiently, and legally or illegally. Large differentials in operating, and regulatory standards across financial markets, can only be ironed out when markets around the world have more or less the same standards and characteristics. That will happen only when artificially segregated small markets transcend national borders and become large enough, through regionalisation and globalisation, to display the common characteristics

54 In some instances, IFIs have behaved as extensions of the Treasuries of major industrial countries rather than as independent institutions with wider obligations.

that are essential for financial markets to work properly.

The Role of the Bretton Woods Institutions

In a globalising world, the only plausible rationale for official intervention in the global financial system is not to intermediate official resources *ad infinitum* but to enhance the credit-worthiness (or more accurately the 'market-worthiness') of developing countries as rapidly as possible. This is necessary to ensure that, in the long run, all countries have access to global market resources for financing needs that cannot be met from tax revenues without relying on the largesse of other countries. As part of that process, the BWIs need to focus on ensuring that domestic financial markets in emerging economies are developed quickly. That needs to be accomplished perhaps even ahead of changes in the real economy, in order to enable emerging markets to interface and integrate more effectively and seamlessly with global financial markets, whose inexorable evolution is now forcing the pace of change in that arena.

Accelerated development of *domestic financial markets* is essential not just to meet the pressures of financial globalisation. Achieving world-class standards of regulation and functioning will impel commensurate improvements in the real economy of these countries as well. As financial globalisation occurs, domestic financial markets will reflect the same intolerance as global markets of political systems and machineries of governance that do not permit economic freedoms and are not transparent and accountable. They will punish lax corporate behaviour and demand higher standards of transparency, probity and accountability in commercial dealings. Financial globalisation will unleash a variety of positive domestic impulses that militate in favour of better governance through internal compunctions rather than the demands of external interlocutors through conditionalities.

That implies a continuous evolution in the role of the IFIs commensurate with, and responsive to, globalisation. As global markets develop greater capacity and extend the risk-reward spectrum in their financing preferences, IFIs should vacate the space they formally occupied in favour of markets and go beyond it to the next frontier. But in doing so they need to ensure the global financial system is not weakened but strengthened as globalisation unfolds. For that, two types of *official intervention capacity* are needed:

- *normal or proactive* intervention capacity on an ongoing (non-crisis) basis aimed at improving the macro-policy framework as well as meso/micro-institutional functioning of firms in emerging markets (i.e. the prophylactic role);
- *extraordinary or reactive* capacity to intervene decisively and effectively when crises do erupt, i.e. the curative role.

If facilitating market-driven globalisation is to be the future agenda of the IFIs and RDBs, what roles should these institutions play? The obvious division of labour, given their respective institutional heritages and areas of comparative advantage, would be that:

- The **IMF** should focus on dealing with the *macro* policy, problems and issues (with a view to achieving co-ordination at the national, regional and global levels) that are likely to influence the course of financial market globalisation;
- The **World Bank** should focus more on the meso and micro policies, institutions, markets and market-supporting structures, enabling conditions, and tackle the practical, ground-level problems and issues involved – i.e. those of market-building, market-supporting institution-building and capacity-building in its broadest sense, in and across emerging markets;

- The **Regional Development Banks** should take over ground-level development support, poverty reduction, and human and social capital development, i.e. activities that the World Bank presently attempts to monopolise, as well as regional infrastructure financing and facilitation of the processes of closer economic integration in their regions.

In the twenty-first century, the IMF should not compete with the World Bank to occupy development financing turf to justify its existence. It should be concerned with ensuring that financial globalisation occurs in an orderly fashion with as few dislocations and crises as possible. In performing this role, it should deal with the cross-border impact of changes in global monetary policies and in capital-flow, investment and exchange regimes by:

- Ensuring that the interplay of macro-financial (i.e. monetary, fiscal and exchange rate) policies at the global, regional and national levels supports rather than subverts the process of financial globalisation;
- Averting, or swiftly correcting, disruptions caused by temporary market failures in either developed or emerging markets through macro measures such as bolstering central bank reserves, restoring credibility and arresting contagion by activating pre-arranged and pre-negotiated stand-by lines of credit to central banks and other key institutions in crisis-affected emerging markets;
- Undertaking continual oversight and support for the progressive *regional and global linkage* of *national* monetary, investment, exchange and financial system regulatory regimes through both its normal Article IV surveillance and consultations, as well as added surveillance powers over processes of financial regionalisation.

The IMF should cease to compete with IDA and the RDB soft windows for scarce grant aid resources for its Enhanced Structural Adjustment Facilities (ESAF) (rechristened Poverty Reduction and Growth Facility) to be replenished. It should depend instead on *quota increases*, part of which should be lent on concessional terms. It should also expand its ability to raise intervention resources and contingent facilities directly from markets – a justifiable amendment to its charter since the IMF would not be directly engaged in assisting global markets to expand their scope and reach. In fulfilling its new role, the IMF needs to continue developing a range of prophylactic products and services. These should include a wider range of *contingent facilities* to suit a variety of circumstances. Such facilities could operate in the same way as guarantees. They could be associated with co-financing arrangements involving private market sources. These should be organised so as to result in private creditors incurring immediate moral hazard risk and confronting a conflict of interest if they were to indulge in counter-productive speculative attacks on currencies and securities markets in emerging economies when the threat of a crisis loomed. Added to the IMF's normal range of facilities for crisis management, contingent facilities could provide an additional bulwark to discourage crisis-exacerbating market speculation of the kind that occurred in Asia. They would provide the IMF with ongoing operational relationships in many emerging markets, in addition to monitoring and surveillance relationships. Such contingent facilities might incorporate clauses that required countries to adhere to a time-bound agenda for financial system and other supporting reforms on a number of fronts – reforms aimed at bringing all financial market standards up to the level of standards prevailing in developed markets.

In contrast to the *macro*-orientation of the IMF, the World Bank should focus on handling the *meso* (i.e. sector level) and *micro* policy and institutional issues and tasks, aimed at accelerating the development of emerging financial markets. It should recede into a wholesale role with the bulk of its operations focused on attracting private capital to developing countries. *The World Bank should leave retail development financing to the RDB concerned in each region.* Its involvement with the RDBs should become closer – possibly even going so far as to become the custodian of industrial country shareholdings in the RDBs. While the World Bank's shareholding might continue to reflect a 60/40 ratio, moving rapidly to 55/45, in the shares of industrial and developing countries respectively, that ratio should be reversed in the shareholdings of all the RDBs with the developing countries in each region holding a majority of at least 60 per cent.

Reflecting this change in role, the World Bank's range of products should be modified, with guarantees replacing loans as its main instrument. Indeed, direct World Bank loans should be made only in exceptional instances. As a wholesaler, the Bank should focus on the *financial sector* of developing countries and aim at improving the efficiency and quality of domestic financial market firms and operations. Its agenda for 2002–2020 should be to:

- Strengthen commercial banking systems in developing countries;
- Create asset reconstruction funds;
- Improve regional investment banking and corporate finance capacity, as well as securities trading and brokerage capacity;
- Develop and strengthen electronic exchanges to enable more efficient functioning of secondary markets;
- Develop national and regional derivatives markets to permit global standards of risk management;
- Participate in building stronger institutions at the long–term and involuntary savings end of the financial services spectrum, such as insurance companies, asset management firms, mutual funds, investment trusts and pension funds;
- Facilitate rapid privatisation in a manner that is in keeping with government efforts to maximise domestic resource mobilisation and to attract foreign capital to finance productive investment in infrastructure and increasing the goods/services output capacity of the economy.

The World Bank also needs to create direct access to financial markets for *sub-sovereign* levels of government, both in domestic financial markets and in regional and global markets. Confining market access to the sovereign level of government in developing countries has damaged and retarded the quality of governance at sub-sovereign levels. It is time to consider whether the task of inducing fiscal responsibility at lower levels of government might not be better performed through market discipline than via centralised heavy-handedness. The Bank should support projects and programmes that directly or indirectly improve the transparency and accountability of all government operations in emerging markets as an essential precondition for access to domestic and global financial markets.

Second to its task of improving domestic financial market capacity as rapidly as possible, the World Bank needs to accelerate *privatisation* and *private investment in infrastructure*. It needs to focus on arranging and financing the exit of governments from activities that can be undertaken more efficiently by the private sector and serve to attract more private investment from abroad. That approach would relieve the binding budget constraints that now limit the ability of governments in emerging markets from making the necessary capital investments and maintenance expenditures for essential physical infrastructure. In performing this role, the World Bank should confine itself to very large projects and privatisations (in excess of $500 million in total financing requirements), leaving smaller projects and programmes to the regional banks.

In addressing its reformed agenda, the World Bank should co-operate more closely than it does at present with regional and sub-regional development banks, not as an overbearing senior partner, but as an equal. It should construct appropriately structured 'wholesale-retail' partnership arrangements with each RDB that reflect a better division of labour based on comparative institutional advantage in each region. Despite many calls to achieve such partnerships, insufficient thought has been given to how the World Bank and the RDBs can operate as an inter-linked family of complementary institutions. The reform agenda proposed should require the World Bank to leave 'micro-development' functions and poverty reduction tasks to the RDBs, bilateral aid agencies and the increasingly influential and pervasive NGO community that can relate and communicate much more effectively with the poor in developing countries than can the World Bank.

Taking the reforms outlined above for the World Bank as a point of reference, the future agenda of the RDBs should be developed around five key themes. In pursuing this agenda an appropriate division of labour and *modus vivendi* must be worked out in each region. The areas of activity on which the RDBs should focus are:

- Improving the quality of governance, empowerment and inclusion;
- Promoting the development of efficient markets for factors, goods and services;
- Promoting integration regionally and globally;
- Investing in their region's human and social capital;
- Enabling their regions to manage 'regional commons'.

Regional Development Banks

The distinguishing characteristic of RDBs is that they are quintessentially regional. They should therefore differentiate their operations and activities from those of the World Bank by highlighting that attribute and using it as a comparative advantage. *They should model themselves on the European Investment Bank (EIB) rather than on the traditional World Bank-type MDB model.*

Financing Regional Integration: RDBs should focus on supporting the regional integration impulses of private players and transnational enterprises that aim to expand their operating space and to benefit from static and dynamic gains, as well as economies of regional scale. They should support regionalisation of national markets by helping to remove the barriers that obstruct natural processes of market integration, i.e. tariff and non-tariff trade barriers, as well as those embedded in laws, rules, regulations, product standards and specifications, and in their discretionary (rather than rule-based) application. The RDBs should also finance physical and social infrastructure that enables their regions to better co-ordinate themselves. They should do so less through regional projects than through supporting *private* and *quasi-private* enterprises involved in constructing, managing and operating infrastructure assets and services (for example transport, power and communications) on a trans-regional basis. The same should occur with social infrastructure, especially in health and education services. The RDBs can and should do more to build productive alliances with one another to create region-to-region trade and financial linkages between and across all developing regions.

Financing Regional Commons and Public Goods: What sovereign states do within their borders affects the environment of their neighbours and of the world. Developing countries and the international community have simply not done enough to minimise the negative consequences of their actions or to maximise positive outcomes. RDBs need to initiate programmes of managing regional commons better. Their interventions in such programmes need to be selective, carefully focused and properly targeted. Along with the relevant UN agencies and the GEF, the RDBs should develop specific programmes to monitor the commitments made by their members to the Montreal, Rio and Kyoto protocols. They should be proactive in developing quickly their regional markets for trading carbon emission rights in an organised manner in association with work aimed at strengthening financial markets. The RDBs should also play a deeper and wider role in examining the effects of other issues, such as deforestation and dams, on the ecology and environment of their regions. They should go beyond merely examining these effects and devise remedial measures or viable development alternatives, and be prepared to finance them.

Unifying the MDB System

At present the World Bank, the major RDBs and several sub-regional development banks act as a disparate, fragmented set of institutions that overlap in their operations and activities. They duplicate their resources and efforts to an excessive degree in the same countries and operate at odds with one another. The MDB system needs to function instead as a streamlined network of inter-linked financial institutions that maximise the joint throw-weight of their equity capital, their global borrowing power and their staff resources, which are very uneven in terms of quality and effectiveness.

The aim should be to create a more holistic global MDB system of institutions linked through a leaner World Bank at the apex, performing wholesale rather than retail functions. That would imply cutting the World Bank's staff from around 10,000 to no more than about 2,000 people at headquarters and concentrating its role on global issues. The bulk of its operational staff resources, i.e. all its resources in its regional vice-presidencies, the staff supporting these units, and all staff in the field, along with their respective budgets, should be distributed across the respective RDBs as quickly as possible. This would result in immediately strengthening the institutional capacity of all the RDBs, especially that of the African Development Bank. The AfDB is at present the weakest link in the MDB system; given the challenges its region faces, it needs to be the strongest.

In a revamped MDB system, the RDBs should become the key line agencies (retail financing entities) interfacing directly with borrowing countries. The World Bank's role at the interface should be limited to financial system and capital market development, financing large infrastructure projects and accelerating privatisation, until that process reaches its logical limit. Eventually – by 2050 at the latest – the World Bank should become a financial holding entity that combines industrial and developing country shareholdings on a 50–50 basis to support the global official financing system. It should operate through the RDBs and, where necessary, through private commercial financial institutions and capital markets (global, regional or domestic) in guaranteeing and underwriting risks which private entities are as yet unwilling to finance. The RDBs would eventually evolve into institutions like the EIB, owned and operated entirely by countries in their respective regions.

A beginning toward this type of 'integrated MDB system' could be accomplished by swapping the shares held by industrial countries in the RDBs for shares in the World Bank. The World Bank would reinvest the equivalent amount in the shareholding of each RDB to a maximum of up to 40 per cent of each RDB's shareholding structure. It would nominate suitably qualified statesmen to represent the industrial countries (one each for the developed countries of Asia, Europe and North America) on the Boards of Directors of each RDB, thus saving on unnecessary administrative expenditures by individual countries and introducing greater consistency in policies and decision-making in all the Boards of these regional institutions. The shareholding structure of the World Bank would, of course, need to be adjusted, through rights issues, to reflect at all times a minimum shareholding of 45 per cent by the developing countries, mirroring their real weight in the global economy at PPP exchange rates. That share might reach 50 per cent by 2025 and even go beyond that as the share of these countries in the world economy (in PPP terms) grows.

Global Taxation and the International Tax Organisation

Section 6 of this report set out arguments on the impracticality of global taxation and the issues to be considered in implementing it. The same reasoning leads to the conclusion that ZPR is premature in recommending the creation of a new International Tax Organisation. Notwithstanding the possible theoretical benefits of such a step – and there may be many – this proposal is likely to create a firestorm of opposition in key industrial countries, for example the USA. This could stop UNCFD having any positive outcome.

Many of the problems and issues about which ZPR expresses concern, for example public revenue being foregone through legitimate tax avoidance because it falls between the cracks of territoriality, can be easily resolved by changes in national tax laws and through revisions of bilateral tax treaties that already exist and that could be standardised to a greater extent. A new international organisation is not needed to bring this about. If OECD governments agreed that they wanted to avoid these anomalies, they would have done so by now. Nor is there any obvious need for an ITO to undertake the other functions that ZPR suggests. Its argument is belaboured and contrived.

The tasks of statistical compilation and analysis of global tax data, reporting on global tax developments, tax monitoring and surveillance, sharing tax information across countries, converging toward unitary taxation of multinationals and taxing emigrants could just as easily be performed by national tax authorities, informal groupings or associations of such authorities or, in some instances (for example data, reporting and surveillance), by the IMF and the OECD. The OECD is already in the process of persuading tax havens to desist from 'harmful' tax competition. Many countries are convincing each other of the pointlessness of offering competitive tax incentives to attract FDI or FPI. None of these tasks justifies creating ITO.

It is disconcerting that ZPR actually legitimises the notion of 'harmful tax competition' recently invented by OECD countries. Most tax havens have been created in response to the domestic tax legislation of OECD countries themselves. They are operated almost entirely by offshore banks, global law firms and global accounting/audit firms with headquarters in OECD countries. This issue reared its head when continental European governments encountered widespread public antagonism to further taxation and decided belatedly (and retrospectively) to prevent tax leakage. In these unfashionably *dirigiste* economies, the public sector absorbs 45–70 per cent of GDP and faces public demand to reduce that proportion closer to the 33 per cent level of the USA, or the 38 per cent level of the UK, in order to remain globally competitive. The response of continental European economies has, unfortunately, been the same as in other areas, such as labour and environmental standards, i.e. that tax should not be an issue on which countries compete.

It is unfortunate that the concept of harmful tax competition has gone unchallenged from an intellectual viewpoint. It is an oxymoron. If governments are to provide public goods and services efficiently and effectively, at the least possible cost, how can tax competition among governments be harmful? If there were no pressure against raising public revenue, and no competition among governments to provide the most attractive home for risk capital, governments would have a perverse incentive of wasting public revenue with no incentive to be efficient or effective. They would know no restraint.

Before the spectre of unfair or harmful tax competition is raised, the different circumstances of developed and developing countries need to be taken into account. Industrial countries need to encourage consumption to keep their production engines going. They do not need to encourage savings to the same degree. Their need for development investment is not as great as that of developing countries. Their emphasis on social equity requires steeply progressive marginal tax rates to discourage wealth accumulation and achieve redistribution. They can manage with investment (and saving) ratios of 18–20 per cent of GDP to maintain real growth of 2–3 per cent. They can indulge in higher marginal rates of direct and indirect taxation and capital gains tax, levied on individuals and corporations, to provide the public goods and services their societies choose to have provided through the public sector. Except for a few exceptions in Continental Europe, where some countries have marginal rates on income and corporate taxation of 55–68 per cent, the global average appears to be converging toward a top marginal income tax rate (for individuals and corporations) of 30–40 per cent, indirect taxes (usually in the form of a value-added tax on goods and services) of 15–25 per cent and capital gains taxes of 10–40 per cent, depending on the period over which the gain is derived (long-term gains are taxed less).

Developing countries face an entirely different situation. They need to mobilise domestic and foreign private resources to sustain growth rates of at least 8 per cent annually if they are to have any hope of converging, even very slowly, with the industrialised world. East Asia is already performing at that level; in spite of the hiccup in 1997–99, growth rates in that region are again recovering. For that to happen in other developing regions and countries their investment rates need to be increased from an average of 20 per cent to 30–33 per cent of GDP. Correspondingly, their savings need to increase from an average of 17 per cent to 28–30 per cent of GDP. At the same time, they need to attract foreign private capital equivalent to 3–6 per cent of GDP annually on a sustained basis.

Developing countries therefore need to encourage domestic after-tax income, discourage public dissaving, and encourage financial saving and capital accumulation to the greatest extent possible. They are disadvantaged in not having the same degree of physical and social infrastructure, the same endowment of human, social and institutional capital, or the same monopoly over knowledge and intellectual property, as the industrial countries. Enterprises in developing countries have to pay a much higher risk-adjusted, real cost of capital (6–10 per cent compared to 2–3 per cent in industrial countries) and of energy and imported inputs, than their counterparts in the industrial world. Their main advantage is a lower cost of unskilled and semi-skilled labour, which is shut out of the global labour market and the cost of which is being artificially increased through insistence on labour standards and pressures to exercise good corporate citizenship. This means that TNCs pay wages that are far out of line with domestic affordability, creating a dual labour market with unfortunate consequences.

It should not be surprising then that developing countries, with their limited competitive options, should choose to offer attractive after-tax returns to domestic savers and to global capital by having lower marginal rates of direct and indirect taxation. If the argument is taken to the extreme, the poorest developing countries should consider abolishing income and capital gains taxes (as many tax havens and some successful economies, such as Dubai, have done). They should rely instead on expenditure and transactions taxes that are broadly based but that apply a low average tax rate. To increase savings to the extent desired, the marginal rate on income and profits tax in developing countries should be no higher than 20 per cent, capital gains tax should be abolished if such gains are reinvested, expenditure taxes (for example sales taxes and VAT) should be in the range of 5–10 per cent to avoid being too regressive, and appropriately designed transactions taxes (similar to the Tobin Tax) should be introduced, not to throw sand in the wheels of activity but to raise revenue.

These differences make it immediately obvious that the circumstances of industrial and developing countries should lead to tax competition as a naturally desirable state, rather than as an undesirable aberration. Indeed, tax competition should be encouraged rather than discouraged in order to make developing countries less dependent on official transfers and more reliant on their own resources and global capital markets. If that line of reasoning is accepted, then ZPR's suggestions about global taxation and ITO require fundamental reconsideration as being against the interests of developing countries.

Global Governance Summit and the Economic Security Council

ZPR's rationale for proposing a Global Governance Summit harks back to the recommendation of the Commission on Global Governance in 1995 on the creation of an Economic Security Council (ESC). The Commission envisaged a Council with no more than 23 members and with the same standing on international economic matters that the Security Council now has with respect to peace and military security matters. The world's 10–12 largest economies (in terms of GDP measured in PPP exchange rates) would be represented on the ESC as a matter of right. The remaining 11–13 seats would rotate among constituencies organised to provide balanced representation among regions and permit participation by smaller states. The organisation of constituencies would be facilitated if established regional organisations (for example the EU, ASEAN, the African Union and Mercosur) had a permanent single seat representing all their members.

The tasks of an ESC would be to: (a) monitor the state of the world economy; (b) supervise interactions across major policy areas; (c) provide a strategic framework for policies made in several international organisations to secure consistency among their various policy goals; and (d) promote intergovernmental dialogue on the evolution of the global economic system. The ESC's legitimacy would be based on the authority of leaders who participated in its deliberations rather than constitutional powers to make binding decisions. It would meet twice annually, once at a heads-of-government level and once at the level of finance ministers, and have a supporting infrastructure of deputies and a small secretariat.

The ESC would extend the G-7 and G-20 concepts to their logical conclusion in permitting a greater developing country voice in the determination of global economic affairs. But whether it would necessarily result in improved global economic and financial governance remains an open question. It is not clear that G-7 plays an effective role in global economic governance or in achieving economic coordination within the OECD. After several years, meetings of the G-7 have become tedious, routine media circuses. They are now attracting undesirable attention that further reduces their utility and makes them an unnecessary (and extremely expensive) security risk that the global public is unwilling to subsidise. It is not clear that an ESC, operating under UN auspices, would fare better in achieving the co-ordination and co-operation needed – especially in bridging the divide, and reconciling conflicts of interest, between the industrial and developing worlds.

What appears to be needed instead, as more practical and meaningful interim measures toward effective global economic governance, are the following steps:

- More representative structures for decision- and policy-making in the governance mechanisms of the IMF, World Bank, WTO and BIS that would reflect the 45 per cent *real* weight (in PPP terms) of developing countries in the global economy;
- Closer relationships between the World Bank and the RDBs cemented through cross shareholdings so that the MDB system operates as a singular system;[55]
- Quarterly meetings at the heads of institution level in these four key global economic institutions, with a clear agenda aimed at achieving better dovetailing and co-ordination of the global economic agenda;
- Frequent liaison at senior management and operating levels of these institutions;
- Restructured Boards of Executive Directors in these international institutions with seats being filled by a much higher level of representation than is presently the case, i.e. by former heads of government, finance ministers and central bank governors rather than by relatively inexperienced mid-career bureaucrats without the requisite experience at sufficiently senior political and technocratic levels;
- Consolidating the 100 or more separate funds, programmes, conferences and specialised agencies that litter the landscape of the UN's fragmented development assistance system into a single UN Agency for International Development (UNAID) that would deal primarily with the human dimensions of development, i.e. social policy, democratisation, governance and human rights,[56] and complements the IFIs. That would rationalise the enormous waste that goes into paying salaries and administrative costs at the UN and redirect a more significant proportion of the funds provided by donors directly to developing countries.

These measures would bring about more meaningful global economic co-ordination and a more effective voice for developing countries in the management of global affairs than the creation of yet another talking-shop at the UN. For global *economic* institutions to articulate better with the UN's *political* system, regular meetings could be held between the head of the UN and their counterpart in the four key global economic institutions. These institutions could be represented at head-of-institution level at G-7 meetings, at ECOSOC and at G-20 whenever necessary, to avoid a situation of ritualistic meetings being held for no practical purpose in the name of co-ordination.

The Role of the UN in Development

Since 1980 the presence of the UN in development affairs has progressively diminished. It no longer plays the commanding role it did between 1950–80 in: (a) focusing the world's attention on development challenges; and (b) prioritis-

55 See Section 8.2 on this subject.

56 See, for example: (1) Swedish Ministry for Foreign Affairs, *Mobilising Support & Resources for the UN Funds & Programmes*, 2001, Stockholm, Sweden; (2) The Nordic UN Project, *The United Nations in Development* (1996), Ministry for Foreign Affairs, Stockholm, Sweden; and (3) The Nordic UN Project, *The United Nations: Issues & Options* (1990) Ministry for Foreign Affairs, Stockholm, Sweden. See also the following paragraphs where this theme is developed further.

ing the development agenda to be pursued by the global community and its institutions. As the UN (and particularly UNDP) has waned, the BWIs have waxed. With the onset of the era of debt and adjustment, neo-liberal market solutions to development failure became resurgent in the 1980s. Since then the IMF and World Bank have occupied centre-stage as preferred creditors policing developing economies, setting priorities, objectives and targets for their governments, establishing the development agenda, as well as strategy and policy, and promoting neo-liberal market paradigms. With the benefit of hindsight, it is clear that the BWIs were the main vehicles through which the Reagan-Thatcher ideological revolution of the 1980s was exported to the developing world. That was something that a highly politicised UN would not have been able to do. In fairness, it must also be acknowledged that the restoration of the market paradigm and the rolling back of the predatory state that emerged (rather than the developmental state that was intended), was overdue. In that era the UN was by-passed. Deliberations concerning development in ECOSOC became exercises in the repetition of futile rhetoric.

The focus of global policy-making and decision-making – not just on loans to countries for projects and programmes – but on development ideology, strategy, policy, tactics and operations has now shifted decisively to the Boards of the IMF and World Bank and, regrettably, even more so to their managements. The full-time Executive Boards in both institutions and the RDBs – who have to cohabit on a daily basis with the management and staff of these institutions – are unusually prone to regulatory capture. They have effectively become rubber-stamps (perhaps less so in the IMF than in the World Bank and RDBs) that invariably endorse, rather than influence, decisions made by management. These decisions are usually made in close co-ordination with G-7 Treasuries with which the senior managers of IFIs often communicate directly, thus by-passing the Board.

The decisions and precedents set by the managements of the BWIs and their Boards establish the framework and benchmarks within which the executive and governing boards of the RDBs operate. Unlike the UN, decision-making in the BWI Boards is weighted (2:1 in terms of voting power) in favour of the majority shareholders, the OECD countries, which provide both the market and concessional funds that these institutions deploy. The OECD club dominates in these Boards. Decisions rarely come to a vote. Executive Directors representing the G-7 countries work hand in glove with the management of the institutions in organising the Boards' agenda and affairs, so that contentious issues affecting development are usually steam-rolled in the direction favoured by them.

This shift in the centre of gravity from the UN system to the BWIs for determining the international community's response to development challenges, has not resulted from the actions of OECD governments and the IFIs alone. It has occurred because the UN's operational capacity in development matters has atrophied, with the lack of sufficient financial support from its vociferous constituency in the developing world to offset declining contributions from industrial countries which still finance 97 per cent of the free resources of the UN's *development* funds and programmes (UN-DFPs).

Consequently, the UN and its development agencies no longer have the same weight, legitimacy or credibility in the development debate. Their internal disorganisation and fragmentation within the UN system exacerbates the problem. Yet, despite these disabilities, the UN has made seminal contributions over the last two decades in influencing development thinking. For example, UNDP and UNICEF have succeeded – despite initial resistance from the IFIs – in putting a human face on adjustment, drawing the world's attention to human development, and to the importance of human and social capital. These clothes have been stolen by the BWIs and donned as their own garb. Its intellectual contribution notwithstanding, the effect of the way in which the UN system works (or does not work) has been for the value of any UN development-oriented initiative to be dissipated by the time it actually reaches the outside world.

Individual UN-DFPs are too many, too small and too fragmented to have any impact on their own, against the weight of the IFIs. The survival of these disparate agencies often depends on the scraps that the IFIs dole out by way of sub-contracting their services for soft interventions. UN-DFPs spend more of the limited resources available to them on administrative costs and bureaucracy than on development *per se*. They have separate offices in too many developing countries, leading to even more duplication and waste. That makes them unattractive to the major donors as vehicles of choice for delivering technical assistance. Their internal jealousies, their proclivity to cling to their outdated individual identities, and their inability to co-ordinate as effectively as they should, makes them unattractive to donors as an alternative to the BWIs for setting the development agenda or delivering effective development services. Some of that unfortunate heritage is changing. But it is changing much too slowly to make a difference.

The shift of locus from the UN to the BWIs has been sustained for over two decades. As a result, OECD countries are ambivalent about whether the UN should play a role in global economic and development affairs, instead of concentrating on global political and security issues and on maintaining structures for supporting world commerce and global commons. Left unresolved, that uncertainty will lead to the development agenda being determined entirely by bilateral aid agencies and the IFIs, raising several difficult questions. These questions require thoughtful answers if global trade and aid architecture in the twenty-first century is to achieve more positive outcomes than in the previous half-century.

For example, should the global system for development assistance accommodate, and perhaps encourage, constructive intellectual co-operation and competition across intergovernmental institutions in the public domain? Or should it permit (by design or default) an IFI-driven *global creditor monopoly* to dominate development thinking? Is it appropriate for institutions that are quintessentially creditors, and have their own vested financial interests at stake, to set the agenda for four-fifths of the world to which they lend? Might that kind of monopoly not detract from their role and judgement as lenders of supposedly last resort? Does it not compel multiple conflicts of interest in the roles that IFIs play? Might the developing world and the global community at large not benefit from more neutral, multilateral 'safety-valves' (without a creditor's axe to grind) that might permit more impartial, disinterested and objective interlocution and intervention in development matters, especially of the 'soft intervention' (technical advice and assistance) rather than the hard (credit and finance) variety?

If the UN system did not exist, it would need to be invented. The world cannot do without a legal-cum-constitutional, as well as an operating, framework for dealing with a plethora of cross-border problems and issues that national governments – on their own or in self-selected groups, working on a bilateral or plurilateral (regional) basis – cannot handle. It is likely that a *de novo* construction of a UN system in the twenty-first century would be quite different from the inherited patchwork quilt that now exists. Its present design dates back to the very different world of 1945. The system has evolved in fits and starts ever since to accommodate continual geopolitical change. Regrettably, much of its ethos (especially the nexus between OECD members and others) still seems trapped in the artificial divisions created and nurtured by the Cold War.

It is questionable whether the UN system's evolution suits the post-1990 world that is taking shape or whether the constraints operating on it have led to an institutional mutation. Yet any future UN edifice or system that evolves must necessarily be built on foundations that exist. There does not appear to be any desire on the part of the global community to scrap what has emerged and start afresh. What is clear is that the UN cannot continue for long with the degree of internal fragmentation, overlapping and lack of co-ordination that characterises the operations of its specialised agencies and its DFPs. Its capacity to provide value-added services depends on how well it can intermediate between conflicting economic interests that could spill over into becoming major political problems between countries and regions. To do that it needs its own internal capacity to assess and advise, and particularly to advise developing countries on global economic developments and how best to protect their economic interests.

However long it takes, the objective for the UN has to be that of rationalising and merging its disparate DFPs into a *single UN organisation for development*, with an appropriate organisation and management structure that would embrace both sectoral and regional divisions for assisting global development through soft interventions. The sector divisions could be formed by consolidating under a single organisation the specialised sector agencies, funds and programmes that have been set up willy-nilly and that have 'grown like Topsy'. The *regional divisions* could be formed by collapsing the present Regional Economic Commissions under the same roof. Such an approach would result in significant cost, staff and administrative savings. It would also result in better co-ordinated and more credible UN interventions in economic affairs *within* the UN system and between the UN and the WTO, IFIs, RDBs and bilateral aid machinery.

Hopefully, UNCFD will be a landmark event that marks a fundamental change in course and rolls back the role that IFIs now play in dominating development in the same way that the IFIs argued for rolling back the role (and diminishing the importance) of government in development at the national level. The twenty-first century should see the BWIs returning to the boundaries of the roles circumscribed under their respective Charters. UNCFD should pave the way for the UN to regain a key policy role in dealing with development and FfD issues. That would require reinforcing and updating its mandate, and endowing its economic affairs secretariat, as well as UNDP and UNCTAD, with the necessary human and financial resources to play more effective research, policy, and advocacy roles.[57]

Bilateral Aid and OECD-DAC in the Global System

Coherent architecture for FfD cannot be structured without taking into account the role that bilateral aid agencies play in influencing international economic relations between the industrial and developing worlds. Strictly speaking, national aid agencies are not part of inter-governmental global economic architecture, although OECD-DAC certainly is. Like central banks, the role of the bilateral aid agencies of major donor countries is sufficiently pervasive (and pernicious) to influence the behaviour of the international system, especially when their policies are co-ordinated within the OECD club through the Development Assistance Committee. What IFIs do in the global arena where aid and lending are concerned is a

57 *Mobilising Support and Resources for the UN Funds and Programmes* (Study 2000:1); Ministry for Foreign Affairs, Stockholm, Sweden.

derivative of the priorities and preferences of the national aid agencies that fund them.

Twisting the Development Agenda out of Shape

One reason why the aid system is losing coherence is the increasing difficulty that OECD governments face in extracting parliamentary appropriations for aid. There are, of course, exceptions, as in small like-minded countries (for example the Nordic group and the Netherlands) with a wide public constituency for aid. But even in these countries, bilateral aid agencies seek political support from any quarter they can find for increasing aid appropriations. That process is resulting in the development agenda becoming hostage to single-issue lobbies that are passionate in their beliefs and quite energetic in 'getting the vote out'.

National aid agencies are finding that they have to accommodate a number of such interests in order to avoid a collapse of aid appropriations. These include environmental, pro-democracy, right-to-life and gender lobbies, animal rights activists, advocates of nuclear disarmament, active religious groups, children's rights organisations, protectionist labour lobbies or whatever other special interest happens to be in vogue. Unholy alliances between national aid agencies and single-issue lobbies (i.e. civil society – which excludes government and the private corporate sector) are destabilising the development agenda and leading to an increasing degree of dissonance and incoherence in the aid system. In a sense, this phenomenon is also a reflection of globalisation, albeit of a different sort. It is twisting the development agenda out of shape. There is now a serious conflict between what providers of aid think is necessary to achieve sustainable development, which appears to have boiled down to the simplistic singularity of poverty reduction, and what governments actually responsible for delivering development know to be necessary, where poverty reduction is only a minor part.

A strong case can be made for re-orienting the agenda and *modus operandi* of national aid agencies. These organisations need to stop micro-managing aid programmes and become lean, minimalist organisations rather than employment-creating organisations with field offices in every developing country that they can justify being in. Such justification is invariably achieved by having large, but ineffective, aid programmes, the motives of which are not driven by development objectives *per se* but by the objective of gaining bilateral advantage over other OECD countries in commercial relationships. As far as poverty reduction is concerned, bilateral aid agencies might be more effective in channelling their funds through NGOs in their own countries, the recognised international NGOs and local level NGOs in the developing countries concerned.

They could extend their reach by dealing with and through chambers of commerce, professional associations and academic institutions. A major step toward achieving greater coherence in the aid system would be to have national aid agencies lessen their dependence on single-issue lobby groups for ensuring adequate levels of aid appropriations from their parliaments. Another step would be to have such aid agencies detach themselves from cosy, incestuous relationships with the IFIs, concentrating instead on working with the UN's development funds and programmes, with organisations like the Commonwealth Secretariat and with RDBs and NGOs to achieve cost-effective delivery at the ground level and make a more meaningful impact on poverty alleviation.

Development strategies in individual countries, and for the developing world as a whole, are being grossly distorted. Aid programmes are becoming more sensitive to use of the right 'labels' and to development fashions than to substantive content. Developing country governments are being deflected from putting in place and anchoring the real foundation blocks of development. They are being compelled to pursue strategies that are politically correct rather than sticking to unfashionable strategies that are the only ones that work in the long run.

Donors and their instrumentalities, for example IFIs, invariably portray themselves as knowing more than developing country governments about how to deliver development. More often than not they do not even bother to establish their credentials. As long as money is attached to a particular priority the development agenda is compromised in terms of balance and sustainability. Aid donors and IFIs do not have the task of managing development in impossibly difficult environments. Developing country governments do. When the perception gap is large, then 'ownership' and 'partnership' become meaningless subterfuge. Regardless of whatever policy or strategy papers they may sign, developing country governments can never, in any substantive sense, be expected to 'own' or be genuine 'partners' in an agenda they do not believe in, looked at from the day-to-day challenges they face and the domestic constituencies (not necessarily democratic) that they are accountable to.

Good Governance of the International System

In suggesting how a coherent international architecture might be best structured, it needs to be emphasised (especially in OECD countries) that *good governance*, like charity, begins at home. At the end of the Cold War, development assistance ceased to be an instrument for influencing recipient governments to choose which of the two or three main global camps they wanted to belong to. Aid donors were then seized by the idea of propagating *good governance* as part and parcel of the multi-faceted globalisation process. They have stressed the importance of that attribute at every opportunity and introduced good governance conditionality in lending by IFIs and RDBs. In a logical world, no one can possibly argue for *bad governance*. But there is considerable debate about precisely what good governance is (apart from knowing it when you see it) and how it might be brought about in developing country circumstances. That issue aside, industrial countries might contemplate, with some humility and realism, the moral authority with which good governance can be preached when the simplest concept of good governance is not applied in the case of global financial institutions.

Recent embarrassing *contretemps* in the appointment of the heads of several multilateral institutions illustrate the point. To extend it further, the quality of leadership in most international institutions of significance leaves much to be desired. In rare cases, leadership is of exceptional calibre (for example at the Inter-American Development Bank (IADB)). But these seem to be the exceptions that prove the rule. The way in which heads of global institutions are selected and appointed would find no favour in any respectable civil service or other walk of life. The process is so flawed that the most qualified people do not make themselves available for these jobs. Clearly something needs to be done if the international system's credibility is not to be damaged irreparably. The problem affects not just the heads of global agencies but the appointment of second and third ranking officials as well. It threatens sensible management and the coherence of the global system. What some governments do to get favourite sons appointed is tantamount to corruption no matter how elegantly the transaction is clothed.

Beyond the question of leadership lies the selection of members of Executive Boards and governing bodies. Again, the selection processes that apply to these positions in the global economic system are flawed. As a result, governing bodies do not function as they should in exercising checks and balances over management. The result is institutional and policy failure. Boards of multilateral institutions are co-opted by managements, resulting in a lack of transparency, accountability and responsibility. There are a host of governance obstacles to be overcome in reforming the global system. Global institutions need to be governed differently and managed differently and more efficiently. They need different kinds of leaders, managers and staff, vetted through more rational and transparent processes than are presently applied to ensure that they have the requisite attributes, knowledge and qualifications. Suffocating bureaucratic cultures need to undergo substantial change to achieve overdue downsizing. Without such measures, whatever else is done to introduce rationality and coherence in global economic architecture is unlikely to have much effect.

A New Rationale for Government-to-Government Resource Transfers

Although its rationale is becoming weaker and less justifiable with each passing day, the present system of development assistance (aid) has become sacrosanct because it has existed for over 50 years. In that time it has created an array of vested institutional interests in both the public and private sectors that prevent it from being abandoned or changed. Yet contrary to popular belief, the system protects the industrial world at the expense of developing countries. It lowers the cost of OECD resource-flow obligations to poorer countries while suggesting the opposite to their taxpayers who are now disillusioned with the failure of aid to achieve its goals.

In a globalising WTO-orientated world – in which the primacy of markets, of open market access and of legally enforceable redress are accepted as the foundation stones for global transactions – the proper basis for resource transfers from rich to poor countries must be compensation for the damage done by discriminatory denial of access to, and protection of, developed country markets for certain goods, for example textiles, certain types of basic services, agriculture and particularly for unskilled and semi-skilled labour. Estimates of the damage done to developing countries in each instance, industry and factor market vary widely depending on the source and available information. But data that are available suggest that an order of magnitude of US$500–600 billion in compensating damages would be defensible. That is more than 10 times what the present development assistance system yields by way of ODA transfers. Clearly the technical details and mechanical intricacies of operating such a compensatory system would be more complex than is the case with the present development assistance system.

The mathematics and complexities could be handled if there was political will to change the system. The challenge that industrial countries confront is to accept the legitimacy and logic of a new basis for resource transfers instead of clinging to a rationale that is no longer respectable. A WTO-driven world strips away the pretence of charity and goodwill in the present logic of development assistance. It makes transparent the damage being done in denial of market access, while exposing the hypocrisy of providing a sop to developing countries at nine cents on the dollar. That situation cannot last much longer. Developing countries have so far failed to change the raison d'être of resource transfers. Yet it is inevitable that the present basis of resource transfers through aid must eventually change. Even if OECD governments find the change difficult to accept in theory or in practice, there will be no dearth of high-priced international lawyers lining up to argue the case for damages suffered by developing countries in international courts on the basis of lucrative contingency fees as the WTO regime unfolds. Strangely enough, industrial countries are being given a period of grace by developing countries that are resisting the accelerated evolution of a rule-based world

Differing Perceptions of Priorities for Achieving Sustainable Development

Donor Country Priorities	Developing Country Priorities
Good Governance:	***Infrastructure:***
Democracy	Electricity, Water, Sanitation, Telecoms
Elections	Roads, Railways, Ports
Political Parties	Airlines, Shipping
Civil Society Representation	
Human Rights	***Capital Markets:***
Corruption	Securities Exchanges
	Derivative/Commodity Markets
	Global Financial System Integration
	NPAs in Banking Systems
Policy:	***Policy:***
Poverty Reduction	Macroeconomic (MFE)
Macroeconomic (MFE)	Deregulation of Controlled Sectors
Privatisation/Corporatisation	Proper Regulation of Markets
Trade Liberalisation	Labour Markets/Employment Absorption
Education, Health, Social	Industrialisation and Exports
	Global Market Access
Gender/Children:	Mitigating Impact of Globalisation
Rights, Equality, Access	Cultural Compatibility of Modernisation
Participation	Coping with E-Commerce Revolution
Child Rights/Child Labour/Soldiers	
	Governance:
Environment:	Administrative Efficiency, Effectiveness, Honesty
Global Emissions Protocols	Decentralisation/Devolution
Global Warming, Ozone, CFC	Quality of State, District, Local, Municipal Government
	Civil Service Rationalisation
	Managing Resurgent Ethnicity
	Reducing Costs of Governance
	Gender/Children:
	Reducing Malnutrition, Starvation,Poverty
	Assuring Survival
	Reducing Population/Fertility
	Coping with Cultural Traditions/Constraints
	Environment:
	Local Focus on Emissions, Pollution
	Protection of Trees, Forest Cover/Fires
	Coping with Drought, Floods, Cyclones
	Water and Irrigation Constraints

Source: Ministry for Foreign Affairs, Government of Sweden, *Mobilising Support and Resources for the UN Funds and Programmes, 2001*, Stockholm, Sweden. (This report was written by P.S. Mistry, Oxford International, UK and Niels Olesen, COWI, Denmark.)

trading and financial regime because of the mistaken view that such an outcome may not be in their best interests.

The War of Global Competitiveness

Of relevance to UNCFD and FfD is the reality that an unprecedented war of global competitiveness has been unleashed with the Uruguay Round. It will intensify with the new WTO round of negotiations. Its outcome remains uncertain. As with every war, the fortunes of combatants will shift with time. This is a war that has no foreseeable end. Theoretically, it will end only when the world unifies under a single global trade, finance and exchange regime. That may happen. But it is a long way off. A considerable amount of collateral damage will be done along the way. It is not at all clear how the fall-out of global competition will be dealt with, who will pay the price and how?

Policy-makers in the developed world – and in the more successful and competitive developing countries as well – no longer argue against the merits of competition and competitiveness in the universal emerging global market. But policy-makers in dispossessed and disadvantaged countries that do not yet have the basic wherewithal to compete on level terms are perplexed and confused about the enormous challenges they confront and about being marginalised before they have had a chance to emerge. For example, is Africa to become a large game reserve with an advantage only in eco-tourism?

The merits of globalisation have been presented as axiomatic and obvious by supposedly knowledgeable protagonists. Its critics, on the other hand, are invariably portrayed as dinosaurs out of touch with reality and with the times in resisting the forces of natural evolution. But that may be too simplistic. Industrial countries believe, perhaps somewhat complacently, that they will always retain a globally competitive edge in knowledge-based industries and services. That is an odd belief when developed countries are falling over themselves trying to import IT workers from India to cover shortfalls in their own labour markets for these knowledge-intensive skills.

In industrial countries, resistance to globalisation is gathering force as it becomes apparent that there is no plan for taking care of those displaced or marginalised as a consequence of continually shifting advantage in global competition. It is not enough to offer social safety nets through generous welfare payments. These will become increasingly unaffordable as demographic changes manifest themselves in OECD countries. Moreover, such safety nets are a magnet for unwanted immigration. Nor is retraining and retooling of skills a panacea. Not everyone has the capacity to be trained or retooled for knowledge-intensity. The bell-curve distribution of human capacity suggests that a proportion of the populations of developed countries will not have the skills needed for knowledge-intensity no matter how much money is thrown into education or re-education. Jobs that once absorbed the unskilled and semi-skilled in a manner acceptable to them have disappeared. The jobs that have replaced them are jobs that many find demeaning and unacceptable. That attitude problem will have to be overcome with a change in work and welfare culture.

But such problems pale in comparison to those faced in developing countries. There the gaps between haves and have-nots and the educated and the uneducated will continue to widen. Most of these countries have effective unemployment rates of around 20–30 per cent and effective underemployment rates of 40–50 per cent. For absorption of a growing young population to occur, such surplus labour has either to be exported or employed in domestic labour markets. But markets for unskilled labour in developed countries have serious problems of their own. They are unlikely to open dramatically, limiting the scope for labour exports from the developing world. Nor is productive investment in developing countries likely to double or triple from current levels. In the absence of these two conditions, it is difficult to envisage the full absorption of a rapidly growing number of dispossessed people through increased productive employment.

What are the consequences likely to be for a globalising world? In truth, no one knows. Between 1950–2000 a very rapid increase in the number of very poor people (from about 1.5 billion in 1950 to nearly 3.5 billion in 2000) has occurred without severe global disruption. Of course, local and regional ructions caused by such growth have increased in frequency and severity. This increase has also had social, ecological and environmental consequences the long-term impact of which is only beginning to be appreciated. It has resulted in rapidly increasing crime and reduced personal security along with deforestation, desertification, land degradation and immense pressure on finite water resources.

With the change that has occurred in global communications and access to information in the last decade alone, is it likely that an addition of another two or three billion of the very poor over the next 25 years will be coped with in the same manner? Or is the dam closer to bursting? No one knows. Much more needs to be discovered about how the world can cope with the social fall-out of untrammelled global competitiveness, especially in developing countries, before it plunges headlong into creating a monumental problem with simply a hope and prayer that it may be able to cope with the consequences.

The list of residual issues in this discussion of 'systemic issues' covers many that have not been addressed by SGR or ZPR. It has been offered with the intent of provoking thought among Commonwealth policy-makers, and particularly among its developing country members, about where their interests lie in resolving these difficult questions and the line they wish to take at UNCFD to achieve positive, constructive outcomes.

For the governments of the Commonwealth, this paper represents just a starting point in a process that will unfold over the coming months. Hopefully it will aim at determining the overall platform and position that developing countries as a whole (and the Commonwealth as a unique multilateral body) should take at UNCFD. Clearly, the positions taken by member governments must recognise the differences that exist between regions as disparate as East Asia and Africa. But it should not let that issue weaken its compulsion to construct a common platform and present a common front on the larger, broader issues that affect the developing world as a whole. Eventually the positions taken by both industrial and developing countries must be shaped on the basis of more intensive research and study than this synoptic paper, prepared under the pressures of time, can provide. The development challenges that each country (and region) confront – and what it needs by way of FfD to address those challenges – need to be examined more carefully.