GLOBAL ECONOMIC GOVERNANCE IN QUESTION: AFRICA'S ADVERSE POSITION AND POLICY REFORM

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ABSTRACT

In essence, the central focus of this study is the *governance of globalisation*, and more specifically, the (supra-national) economic governance of economic gobalisation. At its core, the challenge concerning globalisation in the 21st century is not to stop the expansion of global markets. The challenge is to find the rules and institutions for stronger governance – local, national, regional and global – to preserve the advantages of global markets and competition, and to provide sufficient space for human, community and environmental resources to ensure that globalisation works for people – not just for profits. Unfortunately, at present globalisation is primarily working for the rich nations at the cost of mainly the poor nations and it is increasingly becoming a source of serious global instability, which inhibits global economic prosperity for all. Making matters worse, global economic governance is found to be increasingly inadequate in providing good governance to the global economy and, in fact, contributes – whether intended or not – significantly to the marginalisation of the majority of the world's poor countries. This, however, is not to suggest that the International Monetary Fund (IMF), the World Bank and the World Trade Organisation (WTO) only contribute to these countries' marginalisation as they have, indeed, especially over the last decade, made notable attempts to help these countries develop and grow economically. The concern is that the global economic governance that is currently provided is incongruent to the needs for better supra-national governance as presented by globalisation and marginalisation, in particular. In the latter's case, the marginalisation of a region such as Africa is of specific concern, mainly due to the fact that, as a continent, it best illustrates the serious significance of the problem of global inequality the global economy is facing.

Hence, at issue in this study are two critical concerns regarding the progression of the global economy: a **governance void**, i.e. the inadequacy of global economic governance arrangements coupled with the declining authority of the nation-state in the global market place, and **global inequality**, i.e. the divide that is opening up between the developed and most of the developing countries, which appears to be perpetuated by globalisation and the technology revolution, thus making it harder for the latter countries to catch up.

Importantly, this presents the rationale behind the need for structural **reform** in global economic governance as well as policy reform in developing countries, most notably Africa, to ultimately improve the *governance of globalisation* and the enabling capacity of a region like Africa – to put itself in a better position to reap more of the benefits of globalisation. In its investigations, the study found that global economic governance is indeed severely deficient, that Africa is grossly underdeveloped and that its marginalisation is worsening, and that structural policy reforms in both Africa and global economic governance need to be complementary and be based on a clear and agreed-upon set of norms, goals and principles that is mutually beneficial to the interests of both the developed and the developing countries. In fact, in the case of global economic governance, it was found that not only reform, but a remodelling of this system is required. The key areas investigated in this study include conceptual interpretations and the co-historical progression of economic thinking and global economic governance, deficiencies in global economic governance and a number of contributing factors, Africa's marginalisation, reform and remodelling of the system of global economic governance and critical areas where economic reform is most needed in Africa. Finally, this study is important – as the current global financial crisis is once again revealing – because there is a pressing need for structural change in global economic governance arrangements and, given the severity of global inequality, a corresponding change (i.e. reform) is required on the part of developing countries, especially Africa, to become more globally competitive and restore some balance to current global asymmetries.

"If a free [global] society cannot help the many who are poor, it cannot save the few who are rich" – John F. Kennedy

DECLARATION

I declare that the dissertation hereby submitted by me for the Philosophiae Doctor degree at the University of the Free State is my own independent work and has not previously been submitted by me at another university/faculty. I furthermore cede copyright of the dissertation in favour of the University of the Free State.

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LIST OF ABBREVIATIONS AND ACRONYMS

AAF	–	Africa Alternative Framework
AD	–	Anno Domino
ADB	–	African Development Bank
A*ft*	–	Aid-for-Trade
AGOA	–	Africa Growth and Opportunity Act
APRM	–	African Peer Review Mechanism
AU	–	African Union
BCBS	–	Basle Committee on Banking Supervision
BIS	–	Bank of International Settlements
BWI	–	Bretton Woods Institutions
BWS	–	Bretton Woods System
CAO	–	Compliance Adviser/Ombudsman
CBs	–	Central Banks
CBA	–	Cross Border Initiative
CCL	–	Contingent Credit Line
CEMAC	–	Economic and Monetary Community of Central Africa
CEPGL	–	Community of Countries of the Great Lakes
COMESA	–	Common Market for Eastern and Southern Africa
C20	–	Committee of Twenty
DSB	–	Dispute Settlement Body
DSS	–	Dispute Settlement System
DTI	–	Department of Trade and Industry
EAC	–	East African Community
EBA	–	Everything but Arms Initiative
EB	–	Executive Board
ECA	–	Economic Commission for Africa
ECCAS	–	Economic Community of Central African States
ECOWAS	–	Economic Community of Western African States
EPZs	–	Export Processing Zones

EU	–	European Union
FDI	–	Foreign Direct Investment
FMs	–	Finance Ministers
FSF	–	Financial Stability Forum
GAM	–	Global Anti-Trust Mechanism
GATS	–	General Agreement on Trade in Services
GATT	–	General Agreement on Tariffs and Trade
GCF	–	Gross Capital Formation
GDP	–	Gross Domestic Product
GNP	–	Gross National Product
GS	–	Gold Standard
HDI	–	Human Development Index
HIPCs	–	Heavily Indebted Poor Countries
IBRD	–	International Bank of Reconstruction and Development
ICC	–	International Chamber of Commerce
ICT	–	Information and Communications Technology
IDA	–	International Development Association
IGEGs	–	Institutions of Global Economic Governance
IGOs	–	Inter-governmental Organisations
ILO	–	International Labour Organisation
IMF	–	International Monetary Fund
IOC	–	Indian Ocean Commission
ITO	–	International Trade Organisation
LDCs	–	Least-developed Countries
LICs	–	Low-income Countries
LIA	–	Lending into Arrears
MDGs	–	Millennium Development Goals
MNCs	–	Multinational Corporations
MAI	–	Multilateral Agreement on Investment
MRU	–	Mano River Union
NAFTA	–	North American Free Trade Agreement

NEPAD	–	New Partnership for Africa's Development
NGOs	–	Non-governmental Organisations
NIEO	–	New International Economic Order
ODA	–	Official Development Assistance
OECD	–	Organisation for Economic Cooperation and Development
OPEC	–	Organisation for Petroleum Exporting Countries
PPP	–	Purchasing Power Parity
PRSP	–	Poverty Reduction Strategy Paper
PWC	–	Post-Washington Consensus
R&D	–	Research and Development
RDBs	–	Regional Development Banks
SACU	–	Southern African Customs Union
SADC	–	Southern African Development Community
SAPs	–	Structural Adjustment Programmes
SARB	–	South African Reserve Bank
SBA	–	Standby Arrangements
SDR	–	Special Drawing Rights
S.E. Asia	–	South-East Asia
SRF	–	Supplementary Reserve Facility
SSA	–	Sub-Saharan Africa
TINA	–	There is no alternative
TMs	–	Trade Ministers
TRIAD	–	NAFTA, Europe and Japan
TRIMS	–	Trade-Related Investment Measures
TRIPS	–	Trade-Related Intellectual Property Rights
TPRM	–	Trade Policy Review Mechanism
UDEAC	–	Central African Customs and Economic Union
UEMOA or WAEMU	–	West African Economic and Monetary Union
UN	–	United Nations
UNCTAD	–	United Nations Conference on Trade and Development

US	–	United States
WAMZ	–	West African Monetary Zone
WB	–	World Bank
WC	–	Washington Consensus
WDI	–	World Development Indicators
WEO	–	World Economic Outlook
WIDER	–	World Institute for Development Economics Research
WTO	–	World Trade Organisation

Chapter 1

Problem-statement and method of investigation

1.1 Introduction: rationale and context

As global changes are accelerating and systemic risk is proliferating, the complete system of global economic governance has come under question. While the institutions created at Bretton Woods (the International Monetary Fund (IMF) and the World Bank (WB)) as well as the World Trade Organisation (WTO) – which was preceded by the General Agreement on Tariffs and Trade (GATT) – have adapted over their lifetimes, their ability to deal with contemporary global issues has fallen short of providing a more stable and just global economy (Held & McGrew, 2000:105). Challenged with increasing global inequality as regions such as Africa are becoming more peripheralised, governance arrangements in the world economy have reached a point where drastic change is needed.

A transnationalised and interdependent world economic order has highlighted glaring shortcomings in global policy frameworks (Siebert, 2003:14). At both national and international levels the quest for democratic practices has necessitated fundamental reform and restructuring of governmental institutions. Sovereign states – even those with authoritarian tendencies – have come under pressure to comply with the norms of democracy. Likewise, at the international level the voting structures of, for instance, the Bretton Woods institutions (BWI) are in need of review to make them more democratic and more accountable to contemporary norms of democratic governance. Of major concern is the fact that developing countries, and specifically those of the African continent, are not sufficiently represented in the BWI's voting structures, thus worsening the existing divide between rich and poor countries (Abedian & Biggs, 1998:23).

Economic globalisation is only one of many concurrent processes that currently contribute to the ever-advancing social evolution of human communities. It is clear that the present-day global economic order is in a *transitory phase* evolving towards a higher level system of organisation and structural complexity. As part of a broader process of globalisation, global economic integration has unleashed forces that are unparalleled in

the social evolutionary history of humankind. As noted by Abedian and Biggs (1998:24), the current transitory phase is characterised by two processes that may best be described as *integrative* and *disintegrative* forces. Elements of the integrative process help expand the web of global interconnectedness, while the disintegrative process contributes to systemic instability in the world economy. Both of these processes, however, play a large role in the systemic transformation of the global economic order. It is clear that current global economic and political shifts, with their contradictory tendencies, pose a monumental challenge to securing a stable international economic environment.

Almost trapped between these opposing forces are governments and the wide-ranging need for new direction in global economic governance. With nation-states being placed under growing pressure by the changing nature of economic dynamics in the global sphere – for instance, as markets escalate *cross-borderly* – the question of what the implications of this will be from a governance perspective becomes crucial. In fact, this makes the contemporary period unique in that it is a time when effective governance arrangements are most needed, yet it is also a time when the governance of the global economy in particular is arguably the most difficult due to the multitude of interdependencies on the rise. A classic example of this is the current sub-prime and global financial crisis. In a recent keynote address at a gala dinner in Pretoria, Tito Mboweni (2008:4), Governor of the South African Reserve Bank (SARB), mentioned the fact that this is one of the worst crises the financial world has had to face, at least since the Great Depression, and ascribed it to a combination of reckless lending and unsophisticated borrowing, which emanated from the United States (US). It was specifically pointed out that the IMF and the World Bank have not kept pace with the changing conditions in their operating environment in that their governance and representation structures have lagged behind the changing global economic realities. A particular concern was raised that the IMF and World Bank found themselves completely on the sidelines as the crisis engulfed world markets.

Currently, in terms of a broader context and contemporary trends and concerns, as Kobrin (1997:148) observes, globalisation is disturbing the basic symmetry of political

organisation (governments) and economic organisation (financial, services and product markets). As a result, markets expand in space well beyond the limits of government control and national territories. A rising asymmetry is emerging between the rule of government and globally expanding markets. Held and McGrew (2000:11) are led to believe that "the exclusive link between territory and political power has been broken". In addition, Gilpin (2000:108) confirmed that "many observers believe that a profound shift is taking place from a state-dominated to a market-dominated international economy. Humanity, many argue, is moving rapidly toward a politically-borderless world". Notably, such developments on the international landscape and the resultant uncertainty stress the importance and urgency of meaningfully addressing the governance needs of the day, and in particular those of the global economy.

Judging by the disputes within multilateral institutions as well as the adherence to nationalistic tendencies and practices despite their inefficacy, governments have displayed a lack of proficiency in coping with the challenges of globalisation. More specifically, the Commission on Global Governance (1996:137) already stated in 1996 that: "it is becoming increasingly evident that the pace of globalisation of markets is currently outstripping the capacity of governments to provide the necessary framework of rules and cooperative arrangements to ensure stability and prevent abuses of monopoly and other market failures. National solutions to such failures within a globalised economy are severely limited". By implication, therefore, globalisation involves a *massive shake-out* of societies, economies, institutions of governance and world order. In this regard, Strange (1996:72) underlines that politicians and governments have lost the authority they used to have and that their command over outcomes has diminished. The author argues that "the impersonal forces of world markets, integrated over the post-war period more by private enterprise in finance, industry and trade than by cooperative decisions of governments, are now more powerful than states". Both the authority and legitimacy of states are in decline, creating a serious *vacuum* in the international order; "a yawning hole of non-authority, ungovernance it might be called". Hence, a significant improvement in governance arrangements on the supra-national level is urgently required to fill this void and reduce its destabilising effect (as a result of growing governance uncertainty) on

specifically the global economy. Moreover, in the 1990s – already – Giddens (1990:188) and Beck (1999:131) pointed out that the present era of globalisation has to be understood as embodying much more than simply a *capitalist logic*. Apart from trade and investment, the driving forces of globalisation are also to be found in the dynamics of technology, communication, international relations, and the global diffusion of risks – from the ecological to the financial. Rather than globalisation defining a new post-modern age, in which the local is superseded by the global, both of them point to the growing tensions between a world still mainly organised by the *modern container* of social life – nation-states – and new patterns of socio-economic organisation which transcend them (e.g. the rise of the global civil society). Such tensions produce an ongoing dialectic of change and uncertainty – *a global risk society*. Importantly, the problem with this is that now, at the advent of the 21st century, the world is increasingly facing growing global problems but with an inadequate system of global governance.

In light of this, a major concern regarding the structure of contemporary global economic governance is that inherent elements in the establishment of the IMF, World Bank and the WTO have led to subsequent breaks from the rules and ideals of inclusive cooperation envisioned in their creation. In fact, when a closer look is taken at these institutions, certain institutional flaws become apparent, resulting primarily from the shift from global monetary concerns to pursuits of the structural reformation of individual debtor developing countries. Within the IMF, World Bank and the WTO, inequality pervades, with conditionalities linked to aid and loans. In fact, according to Stiglitz (2003a:51), this is the expression and incorporation of a single, narrow point of view representing the interests of developed countries into nearly all actions and agreements put forth by the IMF, World Bank and WTO, and unequal decision-making processes.

Being seriously disconcerting in terms of the severity of uncertainty in the guidance of the global economy, it certainly appears that the global economic governance system is proving to be imperfect as well as lacking an effective global institutional framework and regulatory mechanisms to realise the claimed aims of stability, growth and economic development. Varma (2002:1) insists that the IMF, World Bank and WTO are lacking

even in the basic elements of good institutional governance: adequate and equal representation and ownership; formal, fair, impartial, and transparent workings, and the existence of flexible, adaptable, and universally accepted norms. The argument continues by claiming that it is the very nature of the system, as maintained by these flawed institutions and the powers behind them, that has resulted in the marginalisation of developing countries in global economic decision-making.

It must be underlined, though, as Camdessus (2004:427) rightly points out, that "we are the first generation in history to be confronted by the need to organise and manage the world, not from a position of power … but through a recognition of the universal responsibilities of all peoples, of the equal right to sustainable economic development and of a universal duty of solidarity and cooperation". The challenge is to find mechanisms for managing the global economy that do not compromise the sovereignty of national governments, that help the smooth and effective working of markets, that ensure global financial stability and that offer solutions to problems that transcend the boundaries of the nation-state and to which it is currently very unsatisfactorily responded to by, on the one hand, frequently *over-stretching* institutions, and on the other, an inherent inertia by the IMF, World Bank and WTO to reform and adjust to the supra-national governance needs of the 21st century. A Herculean task indeed, yet possible and, especially in view of the present global financial crisis, highly necessary.

In summary: forming the essence of what this study is most concerned about, it can thus with a fair degree of certainty be construed that the structure of the global system is becoming increasingly inadequate to provide appropriate governance to the immense explosion of cross-border economic activity. The added concern is that, mainly due to the lack of appropriate systems of global economic governance, markets are currently expanding in such a fashion that the gap between rich and poor countries (i.e. global inequality) is rapidly widening. The continuance of this *risk situation* is considered to be a significant threat to global stability and prosperity. It is commonly accepted that this state of affairs is unsustainable over the long term. Particularly for a developing region like Africa, which is already living on a knife's edge, this situation puts the continent in an even more

vulnerable position. Clearly, changes (i.e. structural reforms) to the structure of the international system, especially from a governance point of view, are becoming indispensable. To assure its *beneficiality* to both Africa and the global system, this, however, also requires a corresponding adjustment – through policy reform – on the part of Africa.

1.2 Research problem

Against the above background, it is clear that wide-ranging deficiencies continue to exist within the structures of contemporary global economic governance. Not only are the institutions involved – mainly the IMF, World Bank and the WTO – providing inadequate governance in terms of current global challenges, they are also lethargic with respect to adjusting their structures in answering the *governance needs* of the day. In addition, governments adversely find themselves under growing pressure as the forces of globalisation are, in effect, weakening their ability to govern cross-border economic activity more sufficiently. Importantly, both of these critical aspects are encapsulated in, and form the essence of, one of the two central concerns of this study: the governance void. The other central and better known concern is global inequality, which, in terms of the focus of this study, is primarily investigated and brought into perspective by considering Africa's marginalisation. What is more, though, the true danger of these two concerns is their combined effect (and, even worse, their possible interrelatedness) on the stability and sustainable progress of the global economy.

In light of this, the **problem statement** of this study is essentially that deficient global economic governance arrangements are perpetuating the governance void, with local and global ramifications. This is then exacerbated by rising global economic inequalities (e.g. Africa's marginalisation) that, reciprocally, make the task of governing the global economy disproportionately challenging. Hence, it is resulting in insufficient change/reform on various fronts and an increase in the vulnerabilities of the global economy. Accordingly, as a central **hypothesis**, the study will aim in testing that institutional deficiencies and the contributing factors that are debilitating contemporary global economic governance exist, and that it together with a lack of a holistic African economic reform strategy will

continue to marginalise the continent. From this, five basic **research questions**, which the study will attempt to answer, are raised:

- What are the institutional deficiencies and the contributing factors that are debilitating contemporary global economic governance?
- In what way do these deficiencies and factors affect and/or pose worrying concerns for Africa?
- How can global economic governance in its current operation be reformed and/or redesigned, both in general (to make it more effective and just) and in terms of its approach towards Africa?
- What reforms and approachs are necessary for Africa to end its underdevelopment and become more competitive in the global economy?
- What changes/reforms are required on the part of developed countries to create a more just and inclusive global economic system?

1.3 Research objectives

It is clear that globalisation presents modern theories on democracy and the free market system with a daunting task: how to reconcile the principle of rule by the people with a world in which power is exercised increasingly on a transnational, or even global scale. But also how to reconcile the principle of equality with a world in which competition and profit-seeking is defining the nature of nearly all economic activity. Although the task of advancing global economic governance is very important, it must be recognised that it is immensely challenging. Halliday (2000:51) confirmed this by stating that "it involves some deep resistances in the international system and some obstacles that have arisen in the very process of global change over recent years". The argument is not whether such a system is desirable or not because a multi-layered global governance system already exists (and to overcome its defaults through reform has for decades been generally indisputable). The question is how to make this governance system more effective, more just, and more responsive to the changing international situation.

In this context, the study has primarily **two aims**. **First**, to examine two critical global economic concerns in terms of their role/function as growing threats to the current and

future stability and security of the global economy: the *governance void* and *global inequality*. In the case of the former, the study aims to draw attention to the disturbing deficiencies evident in contemporary global economic governance as well as a number of disquieting contributing factors. For the latter, in particular, the critical *case* of Africa is assessed in terms of its marginalisation, thus serving to illustrate – as one significant example – the severity of global inequality. By considering how global economic governance affects Africa's marginalisation, the study will also attempt to qualify a possible relationship between the governance void and global inequality, which, if *positive*, is a serious concern for the future stability and progression of the global economy.

The **second aim** of the study is to investigate what policy reforms would be most critical to: (1) redesign/remodel global economic governance to make it and its institutions, in particular, more accountable to contemporary norms of democratic governance and *build* a more integrative and inclusive global economic governance system/framework, and (2) help Africa to re-position itself in the global economy to be better able to reap more of the benefits of globalisation and thus put an end to its peripheralisation so that it can become more integral to current global economic integration. The study aims to highlight the importance of creating a *complementary* relationship between reforms involving global economic governance, Africa and the developed countries to serve as a basis for addressing serious concerns regarding the governance void and global inequality.

In terms of these two broad aims, a number of more detailed and **to the point** objectives – based on the above – would suffice:

- To bring terminological clarity to the concepts of global economic governance, contemporary globalisation, economic globalisation and Africa's marginalisation.
- To bring to the fore the co-historical development of economic thinking and global economic governance.
- To contextualise the globalisation debate in order to accentuate the significance of divergent ideological point of views in the global economic landscape.
- To unveil the deficient nature of global economic governance and shed light on some factors (that are not often linked to it) that make its task more problematic.

- To connect the global economic governance debate with Africa and investigate this linkage – something that is (also) often lacking in literature.
- To examine the extent of Africa's marginalisation in the global economy and to detect how it relates to the continent's underdevelopment.
- To investigate the reform and a remodelling of global economic governance based on principles and norms of good governance that are shared globally.
- To explore how Africa could respond best to its marginalisation, the challenges brought about by globalisation and its say in the IMF, World Bank and WTO by considering and prioritising areas where structural reform is most needed – as well as where a change of approach is required.

Note that, not mentioned as a specific aim, an underlying focus and area of investigation of the study is that of *globalisation*. Besides being viewed as the primary cause of change in the global economy, the study views contemporary globalisation to be mainly responsible for increasing concerns regarding the governance void, global inequality and challenges in respect of structural reform in the developing and developed world and global economic governance. Globalisation and the significant challenge of making it more egalitarian, in particular, is thus central to both the first aim (i.e. examining critical problem-areas) and the second aim (i.e. investigating much-needed reform solutions).

1.4 Research design and methodology

It is proposed that the present study be conducted in both the qualitative and quantitative paradigms. However, the majority of it will be of a qualitative nature. Whereas chapters two, three, four, and eight will entirely fall into this category, chapters five, six and seven will be partially qualitative. The moderately quantitative design of these latter chapters, especially chapter five, will consist of secondary data analysis. All this will take place within the context of a **literature study** involving current literature on the subjects of global economic governance and Africa. As a descriptive study, it employs an *ex post facto* design, where the researcher has no control over the variables. Thus, the general approach being followed is a **theoretical conceptual analysis** guided by exploratory, descriptive and in some cases causal questions that are being asked throughout the study.

In essence, it is a critical theoretical analysis of current global economic governance arrangements and Africa's underdevelopment and reform requirements. The reason for choosing this design is because a theoretical conceptual analysis will serve as a good guide to first weigh up the different opinions and theoretical interpretations. And secondly, to draw conclusions by means of deductive and retroductive reasoning.

Importantly, although other key actors also feature in the global economic governance landscape – such as the United Nations (UN) and the International Labour Organisation (ILO) – the IMF, WB and WTO have emerged as central pillars in terms of decision-making and ideological influence on member countries' policy-making. Therefore, when considering issues regarding global economic governance, the study mainly concentrates on these three institutions, unless otherwise stated. These three institutions will also often be referred to as the institutions of global economic governance (or the IGEGs).

Then, it should be underlined that Africa as a region has been chosen as part of the study's investigations and not, as such, individual African countries, sub-regions or groupings (e.g. oil-exporting and non-oil-exporting countries or in terms of high (above 5%) or low growth rates). The reason for this is to obtain a good picture of what the effect of global inequality is on a large scale – as in the case of a large region, or even better, a continent. For this, there is no more apposite case in point than Africa. Of course, being an African myself also contributes to this choice. Although the study may occasionally refer to individual African countries, the emphasis is by and large on Africa as a whole (a *continental* approach), particularly for the purposes of comparing it with other developing and developed regions. The choice of Africa in an investigation on global economic governance also makes sense due to the fact that the IMF, WB and WTO spend a significant part of their attention on Africa, yet the continent remains vastly underdeveloped – something for which the IGEGs also ought to take responsibility.

1.5 Outline of chapters and intended contribution

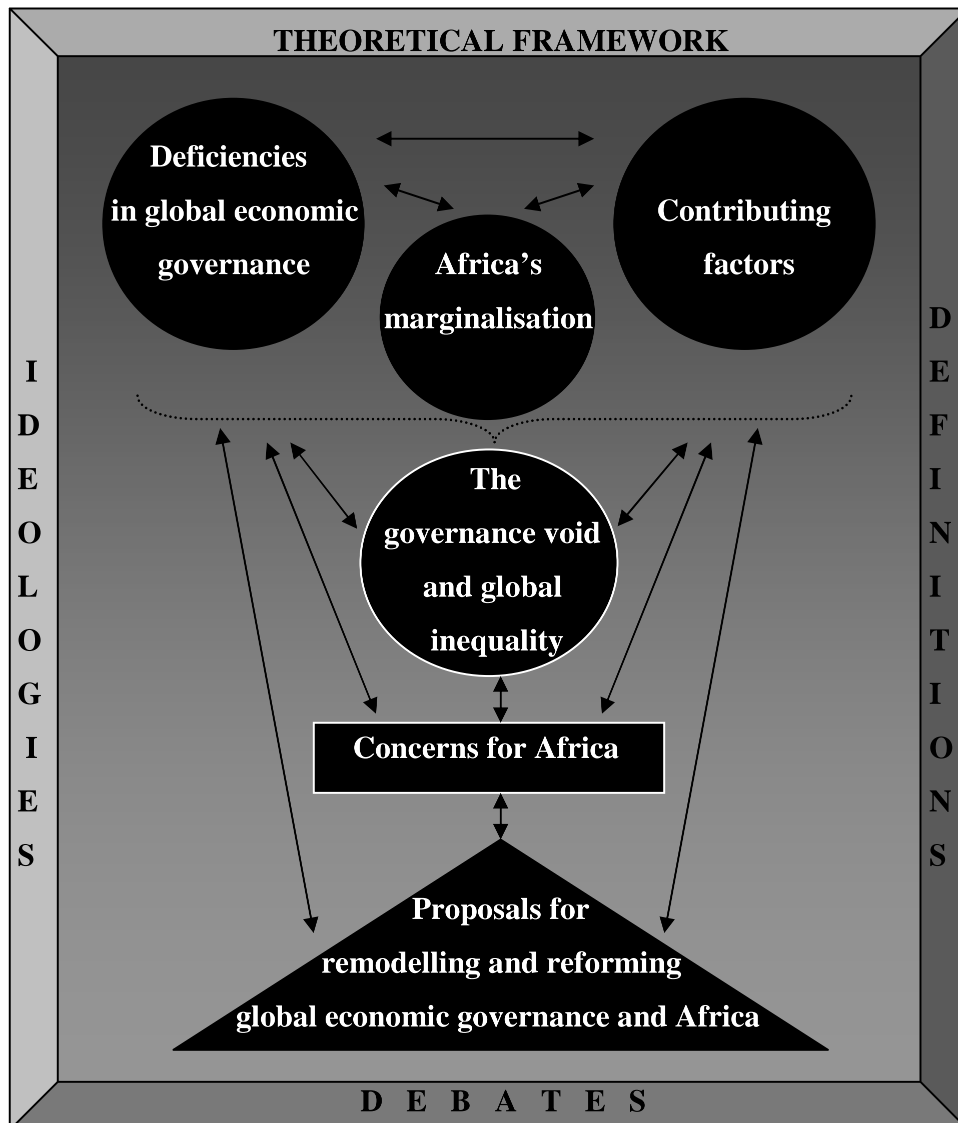
The overarching approach followed in this study comprises three parts. **Part one**, the theoretical underpinning of the study, attempts to provide a theoretical framework which

will give context to the remainder of the study's investigations. This part, which is embodied by chapter two, forms the foundation of the study as it offers background to and a theoretical delineation of key issues and concepts addressed in this study.

The **second part**, consisting of chapters three, four and five, is devoted to emphasising the problem-areas addressed in this study. These include: deficiencies and shortcomings in contemporary global economic governance and key contributing factors, and Africa's marginalisation. The function of this part is to provide the rationale behind the study, i.e. that which gives impetus to what is investigated. More specifically, chapter three identifies several institutional flaws in the structure of global economic governance which primarily involves the IMF, World Bank and WTO. Chapter four pinpoints certain factors (or sources of global instability) within the broader framework of global governance that might be considered somewhat political in nature, which play a significant role in making global economic governance more arduous. Chapter five provides valuable perspective on the debate about Africa's marginalisation as well as evidence of its severity.

Part three, consisting of chapters six, seven and eight, considers the study's proposals for solutions to the problem-areas mentioned above, i.e. policy reforms for both global economic governance and Africa. Chapter six focuses on what reforms are necessary – based on key guiding principles – to make the IMF, World Bank and WTO more democratic, accountable, transparent, independent and effective with sustainable economic development as the ultimate aim. It also investigates how the whole system of global economic governance can be remodelled to make it more integrative and participatory. Chapter seven identifies and prioritises critical areas of reform for Africa by specifically focusing on economic development-specific reforms, financial sector reforms and trade reforms. It also considers the way forward for Africa in terms of regionalisation and building global partnerships. Chapter eight is the concluding chapter that outlines the study's main findings, recommendations and contributions.

Figure 1.1: Structure of the study



Source: Own contribution

Figure 1.1 provides a summary and outline of the key focus-areas of the study. It presents first a structure of key problem-areas that the study is investigating and secondly, reform-proposals as regards global economic governance and Africa. Note that the deficiencies and contributing factors are both presenting concerns for Africa and worsening the governance void. Figure 1.1 further shows that Africa's marginalisation is contributing significantly to increased global inequality. All of this makes the case for structural reform, of which the benefit could be the mitigation of the deficiencies, the contributing

factors and Africa's marginalisation, and therefore the study's central concerns: the governance void and global inequality. Figure 1.1 shows that the study attempts to follow a holistic approach in which all the components affect each other reciprocally. In essence, the problem-areas provide the rationale behind the reforms, mainly due to the resultant governance void and global inequality, while the reforms (being largely structural in nature) are intended to provide – to a meaningful extent – solutions to the problem-areas.

The study's **intended contribution** is essentially to identify specific reform alternatives that would significantly improve global economic governance and enhance Africa's competitiveness in the global economy. More specifically, the study intends to contribute towards a more clarified understanding of the indistinct processes of globalisation and global economic governance. It also intends exploring whether there exists a significant relatedness between a number of factors (which it considers as contributing) – as sources of global governance uncertainty – and global economic governance. In terms of reform proposals, the study intends to contribute towards highlighting the importance of structural reform in global economic governance combined with a complete remodelling[1] of this system (as it will attempt to propose), and meaningful reform priorities for Africa and its efforts to de-marginalise. As a new emphasis, it will attempt to underscore the value of creating reform complementaries as a central focus for the key role-players.

The next chapter involves an investigation of the theoretical roots of global economic governance and its institutional evolution alongside economic thinking over history. This will be complemented by a conceptual analysis of global economic governance and globalisation as well as an examination of the debate surrounding these two concepts.

[1] The remodelling/redesigning of the system of global economic governance could entail either suggestions for dramatic changes in its current structure and operation, or to present a completely new structure as regards governing the world economy. Importantly, as both of these options represent the search for solutions to specific problems in this area, they also emphasise why there is a need for more research in this field.

Chapter 2

Historical evolution of global economic governance, globalisation and economic theory: A review of relevant literature

2.1 Introduction

The contemporary era is specifically characterised by global processes that increasingly determine the greater part of social life. On the face of it, national economies, national cultures and national borders are virtually dissolving. Adding to this complexity, the world economy has internationalised in its basic dynamics as it is presently dominated by largely uncontrollable market forces. Due to the growing emphasis on the global context of economic actions, distinct national economies and, therefore, domestic strategies of national economic management have become less important (Hirst & Thomson, 2003:1). As a result, continuous efforts to govern the world economy are being made with, in many cases, varying degrees of success. As central pillars in contemporary global economic governance, the economic doctrines and beliefs of the IMF, World Bank and WTO (the IGEGs) are becoming more influential in the international environment (Varma, 2002:1). Conspicuously, world governments are – especially since the early 1990s – increasingly adopting very similar ideologies as the world economy becomes more interdependent and as these institutions of governance are becoming more globally authoritative. The concern, though, is that this is, ironically, contributing to the rising uncertainty regarding the governance of the world economy (Castells, 1996:13). As a central aspect of what this study is investigating, the aim of this chapter is to explore the theoretical foundations, cogitations and historical background behind this issue, and in particular, the global processes it engages with.

This chapter examines the history, theory and progression of two evolving and interrelated global processes, namely globalisation and global economic governance. It aims to add historical depth and context to the theoretical analysis of these processes, given that all claims regarding contemporary discourse require, as a precondition, a comprehensive understanding of the past. The analysis is also supplemented by bringing to light various issues of debate which involve both the globalisation thesis and the changing nature of global economic governance. The aim with this is to categorically delineate the

contentious characters of these processes and to draw attention to the strong connection that exists between them, especially in the present era. Lawson (2003:110) underlines that many discussions of world order and global governance, especially with respect to the economic dimensions, have revolved around the phenomenon of globalisation. Due to its focal relevance to the study, this chapter consequently assigns a significant amount of attention to the globalisation thesis. The fact is that, when investigating global economic governance, it would be erroneous to exclude the closely associated dynamics of globalisation. These two processes are co-integrated and directly impact on each other. Hence, as Held *et al.* (1999:7) point out, "at issue is a dynamic and open-ended conception of where globalisation might be leading and the kind of world order it might prefigure".

The study recognises that there are different ways of interpreting the issues associated with the overarching theme of *global economic order* – and do attempt to highlight it. Of equal importance, though, is the fact that the ideological positions held by specifically the IMF, World Bank and WTO have to a large extent dominated most (member) countries' policy priorities as the primary agents of global economic governance. The study thus focuses on elucidating their views, dispositions, and actions since their establishment. This chapter, in broad terms, combines theoretical analysis, historical interpretation, progression delineation (of the operations of the IGEGs), and the contextualisation of specific issues of debate. It first focuses on explaining the conceptual framework underlying contemporary global change, i.e. transformations caused by the processes of globalisation and global economic governance. This is followed by an exploration of the historical dimensions of these two processes. Thirdly, a thorough investigation (with five sub-sections) highlights how economic history and theory evolved along with the development of the IGEGs, with most attention being paid to the period after the Second World War. Lastly, particular issues of debate that underscore the litigious natures of globalisation and global economic governance are pointed out.

2.2 Conceptualisation and context: interpreting global change

When exploring issues and concerns relating to the governance of the world economy, one first needs to answer the question of what exactly needs to be governed? By

implication, what is required is a classified interpretation of what kind of *reality* or condition the contemporary world economy is asserted to be in. This is, not surprisingly, a very contentious issue. However, before determining this, one needs to investigate the meaning of what some consider as "the defining issue of our time: globalisation" (Legrain, 2004:4). Also known as *the globalisation thesis*, the concept characteristically does not attract universal agreement in terms of its meaning and application. Although various forms of *globalisation* have over time been identified (see section 2.5), the current debate[2] mainly centres on the merits and interpretation of contemporary globalisation. As many **globalists** would argue, contemporary globalisation encompasses a host of interwoven processes, including the increasing transnational movement of capital, goods, and people; closer ties via new communications technologies; a rapid turnover of patterns of objects of consumption; a growing awareness of risks and dangers that threaten the world as a whole, and a quantitive increase in, and growth in prominence of, transnational political and economic institutions, and globally interlinked civil and political movements (Randeria, 1998:18). What is of significance, though, is the interpenetration of these processes both horizontally and vertically, and at national, sub-national, and transnational levels.

Contemporary globalisation is thus a complex multi-dimensional process of de-bordering and de-spatialisation, on the one hand, and of compaction and interlinkage, on the other. It can be viewed as an acceleration of integration that substantially alters the scope and character of economic and social relations (Hertel, 2003:48). It finds its expression in enduring webs of worldwide economic, cultural, political and technological interconnectedness as it is essentially driven by a confluence of forces while embodying dynamic tensions. Hence, the *language* of the globalisation thesis is polylogical in that it presupposes multiple images to be placed in the network of interacting forces in the world (Hoogvelt, 1997:56). **Contemporary globalisation** could thus be defined as *"a process of interaction and integration among the people, companies, institutions and governments that involve different nations, a process driven by international trade and*

[2] Although section 2.5 explores the various issues related to the **debate** about globalisation and global economic governance, the first issue – that of its conceptual interpretation – is examined in this instance in order to clarify from the outset the meaning of these concepts and how they are understood in this study.

investment and aided by information and telecommunications technology" (Centre for Strategic and International Studies, 2002:1). Globalisation could be regarded as a progressive increase in the scale of economic and social processes from a local or regional to a world level. The growing economic dimension of contemporary globalisation, in particular, amplifies its impact around the world. **Economic globalisation**, as part of the broader process of contemporary globalisation, is therefore defined by Held (2000:92) as *"the process by which markets and production in different countries are becoming increasingly interdependent due to the dynamics of trade in goods and services and flows of capital and technology"*. Economic globalisation is an increasingly important feature of international economic relations in terms of its implications for global economic governance, trade and productive investment. According to globalists, it has irreversibly transformed the global economic landscape, involving various measures of politico-economic structural changes in the world economy. In this perspective, a global consciousness is emerging which views the rapid integration of national markets with one another as a new dimension being added to the creation of a *global web of interconnectedness*. Globalists point to the surfacing of a new global structure whose rules are determining how countries, organisations and people participate in the global economy. For Gill (2003:130) and other globalists, globalisation is an inevitable trajectory of development, making any attempts to resist it, futile.

Conversely, **sceptics** contend that the process at work in the world economy is merely extensive and intensifying international economic relations, and not globalisation (Hirst & Thomson, 2003:4-7). Although they admit that there are various degrees of *internationalisation*, sceptics interpret this process as conjunctural change towards greater international trade and investment within an existing set of economic relations. Tendencies toward internationalisation still give a major role to national-level policies and economic actors. Although this implies some degree of change with firms, governments and international agencies that are being forced to behave differently, they can, in general, use existing institutions and practices to do so. Hence, the sceptical interpretation does not include any structural changes in the world economy. Furthermore, the distinction between internationalisation and globalisation is of particular

significance to issues relating to global economic governance. Internationalisation reflects a *world order* dominated by nation-states, with the emphasis on strategic relationships for aid, development and exploitation. It is closely linked with, and dependent on, autonomous nation-states. By contrast, globalisation reflects global competitiveness between great market blocs and intensified collaboration and competition in the emergence of new regional blocs that are not only economic, but also social and political (Muller *et al.*, 2001:244). It suggests a less state-centric world order.

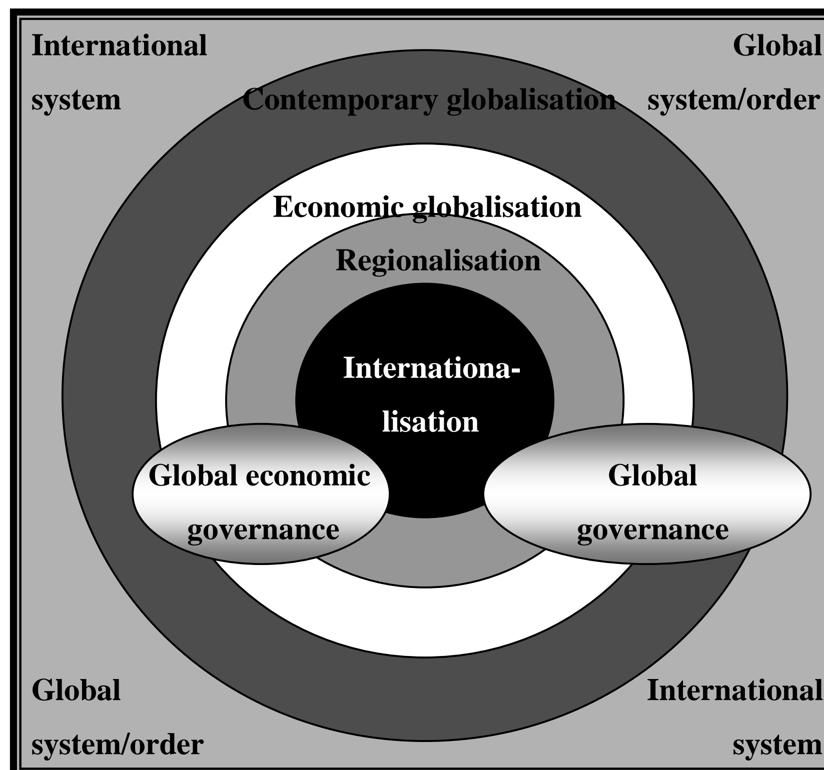
Sceptics also consider *regionalisation* to be more closely associated with the present character of the world economy (especially trilateral (TRIAD) regionalisation), than globalisation. According to Anderson and Blackhurst (1993:1), regionalisation (or regionalism or regional integration) is generally understood as an integrative process occurring at a supra-national level, but within a certain geographical area. It is characterised by significant coordinated economic interactions. It involves reducing the economic significance of national boundaries within a geographic area as it leads states to work together on a regional scale (Lawson, 2003:110). **Globalists** view regionalisation and globalisation as complementary rather than opposing processes.

The basic issue is the relationship between forces of globalisation and forces of regionalisation. In the **sceptical** view, regionalism is one possible approach to a new multilateralism. In this sense, regionalism can be a world-order concept – a *world order* consisting of regional groupings as the defining element. Sceptics regularly use this interpretation to challenge the globalisation explanation, thereby suggesting that the process of change at work in the world economy is in fact regionalisation and not globalisation. In the sceptical argument, the majority of economic activity is viewed as still being essentially regional rather than truly global in spatial scale. They emphasise a higher degree of regional economic interdependence, economic homogeneity, and coherence (Held & McGrew, 2000:157; Hall & Biersteker, 2002:45).

Although this study recognises the dominance of especially trilateral regionalisation in the world economy, it concurs in this instance with the globalist view that regards

regionalisation as complementary to the overarching process of globalisation – as indicated by Figure 2.1. It therefore considers contemporary globalisation to be the process mainly responsible for transforming the world economy. Furthermore, an important aspect that the study, in particular, wants to bring to mind is that in governing the world economy, not only the interests of strong regional groupings should be the ones that receive attention (for instance the North American Free Trade Agreement (NAFTA) and the European Union (EU)), but also the interests and concerns of countries that are not involved as much in regional groupings, as well as countries (e.g. African) that are part of seemingly less significant regional blocs. This implies that global economic governance should be directed by global concerns and not be dominated by the concerns of only certain *important* regional blocs. The illustration in Figure 2.1 serves to configure to what extent the processes of interest (as classified within the ideological framework of this study) are asserted to be governed.

Figure 2.1: Conceptual classification and different spheres of governance



Source: Own contribution

In the final word on distinguishing globalisation from other processes, Beck (1999:26), in a very extreme **globalist** view, considers globalisation synonymous with globalism as he contends that the world market completely displaces or replaces political action. This radical version of the globalisation thesis is an example of an extreme form of the ideology of world-market dominion. It views the many other dimensions – i.e. globalisation in the cultural, political, environmental, and civil society domains – in a way that assumes the dominance of the world-market system (Lechner & Boli, 2000:215). This study, however, distances itself from this radical view due to its interpreting the world economy as being fully globalised (i.e. a finished product).

In entering the next and most critical stage of the debate about conceptual interpretation, a key feature is the fact that literature is confusing as regards the interchangeable use of descriptions such as world economy, international economy, global economy, and globalised economy. An often *missing link* exists between describing the world economy as an international economy and as a globalised economy. A primary source of confusion is the usage of the term *global economy* in both these contexts. In fact, this is the essence of the debate. Before examining this issue, it is important to draw a lucid distinction[3] between the *condition* the world economy is in and the integrative *processes* at work in shaping the world economy. Notably, the processes interpret the changes that are taking place in the world economy, while each of the conditions provides a description of the state the world economy is deemed to be in.

Continuing with the above issue, an international economy *links* distinct national markets while a global economy *fuses* national markets into a coherent whole (Hall & Biersteker, 2002:47). Both of these, however, should not be confused with being a fully globalised economy – a different beast altogether. According to Hirst and Thomson (2003:8), an international economy is one in which the principal entities are national economies. Trade and investment produce growing interconnection between these still national

[3] To clarify, the *processes* (in which boundaries shift) that are causing change are globalisation, economic globalisation, regionalisation and internationalisation. The processes that attempt to manage them/change are global economic governance and global governance. The *conditions* (descriptions of the state of the world economy) are global economy, international economy and globalised economy. The study gives recognition to *globalisation* and *global economy,* and is mainly concerned with *global economic governance*.

economies. In this **sceptical** understanding, the emphasis is on the differential performance of separate national economies and the intensification of linkages between them. At the other end of the spectrum, extreme **globalists**/globalisers believe that the world economy is in fact a globalised economy – something closely associated with globalism (or new universalism) (Ionov, 2003:83). In their view, the international economic system becomes autonomised and socially disembedded, as markets and production become truly global. Hence, extreme globalists argue, national economies are completely subsumed and re-articulated into the system by international processes and transactions (Hirst & Thomson, 2003:10). A less extreme interpretation would, however, suggest that the world economy is a global economy. This study would prefer to distinguish between a fully globalised economy in which globalisation has served its purpose of fully integrating the world economy, and a global economy, a system that signifies the prevalence of globalisation as a process in progress, and where there still exists some degree of resistance (in the form of anti-globalisation sentiment, divergence and disintegration). The world economy is indeed more than merely international; it is *global* in scope but not close to being fully globalised. This is the reason why this study would not consider contemporary globalisation as equivalent to *hybridisation*. Although a globalised economy could be viewed as a hybrid system, the contemporary global economy does not, at this stage, involve hybrid globalising tendencies.

The world economy could thus be considered a global economy, but not a globalised economy. If economic globalisation is associated with the integration of separate national economies, such that the actual organisation of economic activity transcends national frontiers, then a global economy might be said to have emerged. In a global economy world market forces take precedence over national economic conditions as the real value of key economic variables (production, prices, wages and interest rates) respond to global competition. Increasingly, this is proving to be typical of the current world economy (Held & McGrew, 2000:20). In following a less radical globalist view, one can, to this end, conclude by stressing the importance of *systemic economic interdependence* as a differentiating factor. Hirst and Thomson (2003:10) describe this as the national level that is being permeated and transformed by the international. In this sense, the study would

consider an *international economy* to enclose a very small measure of systemic economic interdependence, a *globalised economy* as encompassing full systemic economic interdependence, and a *global economy* to possess a significant degree thereof. Now that it has been clarified that, as asserted in this study, both the global economy and the overarching process of globalisation need to be governed, more emphasis can be placed on delineating the kind of governance processes that are involved.

Given that this entire study is chiefly concerned with various governance aspects in the global economy, the aim in this instance – apart from providing further context – is to concisely define and distinguish between global economic governance and global governance. Varma (2002:3) defines **global economic governance** as *"the institutions, norms, practices and decision-making processes from which rules, guidelines, standards, and codes arise in order to manage the world economy"*. This includes multilateral organisations, the private sector, governmental and regional organisations, and civil society.

By transcending the state system in similar fashion, **global governance** is defined by Held (2000:140) as *"a process of political coordination among governments, intergovernmental and transnational agencies (both public and private); it works towards common purposes or collectively agreed goals, through making or implementing global or transnational rules, and managing transborder problems"*. Importantly, as Messner and Nuscheler (1996:31) emphasised, it differs dramatically from a concept of world government that presupposes the idea of one central global public authority legislating for humanity. Analogous to global economic governance, global governance is based on the acceptance of divided sovereignties, the strengthening of the global rule of law, and the recognition of universally valid values and principles. However, whereas global governance specifically refers to the political dimension of governance in the international system[4], global economic governance refers to the governance of the global economy. Inclusively, global economic governance also forms part of the larger process of global governance, which emphasises the interwovenness of economic and political issues. In essence, as Figure 2.1 indicates, global economic governance aims to provide governance

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[4] Note that the terms *international system* and *global system* are used interchangeably in this study.

to the economic elements of contemporary globalisation, while global governance attempts to perform a governing function in the wider global system, which also includes the political and sociological dimensions of contemporary globalisation. Significantly, both processes are functional within the framework of the international/global system.

2.3 Background: historical identity of globalisation[5]

The globalisation of economic activity and the governance issues it involves are often thought to have appeared only after the Second World War, and particularly during the 1960s. This, in fact, should essentially be viewed as merely a continuation of globalisation's progression since the 11th century. Driven by the growing interconnectedness of markets around the world, the process of contemporary globalisation could be viewed as the consequence of continuously escalating global modifications that have been evolving through history. Modelski (1972:144) furthermore asserts that "globalisation is the history of growing engagement between the world's major civilisations". The author views this as not so much a phenomenon of the modern age as one which begins with the sporadic encounters between the earliest civilisations[6]. Importantly, the nature and the shape assumed as a result of the process of historic globalisation remain even today one of the basic constituents of international economics and politics (Held & McGrew, 2000:49). Thus, we have a spontaneously globalising social and economic reality in need of a historical interpretation.

According to Kilminster (1997:257), the term *globalisation* first appeared in Webster's Dictionary in 1961, marking "the beginnings of an explicit recognition in the contemporary period of the growing significance of the world-wide connectedness of social events and relationships". A concept that had been developing over many years was thereby formally named. Philosophical ideas about global interconnectedness are, in fact, centuries old especially in theories embracing a universalist approach to humankind. Ideas about humanity continued to find expression in the universalist ideologies of liberalism and socialism that developed in the wake of the French Revolution. Originally,

[5] The purpose of this section is to place the process of globalisation in an appropriate historical context.
[6] Although these events, by definition, cannot be compared with contemporary globalisation, they laid the foundation for this evolving process as being an essential part of historic globalisation.

though, the Stoic notion of *cosmopolis* was used to conceptualise a *community of humankind* (Lawson, 2003:120). Although these may seem remote from present-day discussions of globalisation, they nonetheless embodied the essential idea of transcending particular political and economic communities.

The opening period[7] of globalisation is considered to be approximately 1000 AD when the Moslem world was the nearest approximation to a worldwide political order (Held & McGrew, 2000:49). The origins of the Moslem world lay in the Arab conquests of the 7th century, and its binding force was Islam. For several hundred years, the Moslem world was arguably the true seat of civilisation. Indeed, by occupying a central position in the Eurasian-African landmass and using it for their far-flung trade, the Moslems had already brought together the major centres of world civilisation (Modelski, 1972:86). After 1500, and especially in the latter stages of what is called *archaic globalisations*, the Moslem world was strategically outflanked by European naval operations, and its vitality gradually declined (Bell, 2003:808). The work of political unification of the world and the expansion of the capitalist world economy now fell to Europe. In one sense, the drive that produced it was a response to the prosperity of the Islamic world and the threat that was perceived to emanate from it. The Europeans not only circumnavigated the globe, but also followed up this feat with the establishment and maintenance of a permanent network of worldwide contacts. For the next 500 years, they mainly determined the speed and character of globalisation (Hirst & Thomson, 1999:19). Consequently, this was essentially the real beginnings of the globalisation of economic activity, when organised cross-border trading operations of a private corporate nature were initiated.

The eras of historical globalisation that followed were first *proto-globalisation* between 1600 and 1800. This period was characterised by the mutation of political and economic institutions throughout large parts of the world and the emergence of distinct state systems. The next brief era was that of *modern globalisation* (1800-1820). It evolved alongside the modern state, nationalism and full-blown industrial capitalism, and

[7] It must be underlined that there is, however, no general consensus concerning the historical identity of the globalisation phenomenon – especially not with regards to when it officially started.

signified the advent of new technologies (Bell, 2003:807). An interesting feature of *post-colonial globalisation* (1820-1920) – the era[8] that followed this – was the fact that, in leading up to the First World War, the global economic order during this period was liberal. This was a general characteristic of eras of high growth in the world economy (Levy-Livermore, 1998:4). It denoted a trend towards the inclusion of non-European societies, such as Japan, in the *international society*. This resulted in greater internationalisation,[9] mainly due to growing cross-border trade flows, and the significant increase in the number and speed of global forms of communication. The beginning of the subsequent era (1920-present) can be considered the incipient stages of what is today called *contemporary globalisation* (Bell, 2003:807). This era saw, among other things, the formal entanglement of virtually the entire non-Western world in the web of globalisation. Moreover, it particularly signified the rise of the developing world voice in international affairs and, globally, specific attention was being paid to the notion of *humanity* – especially in the aftermath of the Second World War and later the Cold War. There was also a significant increase in the number of global institutions and their growing global influence. There are even those who believe that the true *open world* was born (and globalisation reborn) at the beginning of this period in 1944 at Bretton Woods (Legrain, 2004:104; Moore, 1998:71). In fact, the development of a global telecommunications infrastructure and global financial systems as well as increased emphasis on global standards and statistics facilitated the enhancement of a global consciousness (or *global village* sentiment). Notably, history has shown that each successive mode/era of globalisation was layered on top of the previous ones, serving to channel and shape patterns of trade, consumption and communication. Hence, as Bell (2003:808) points out, the new (era) always carries with it traces of the old.

It was especially since the 1960s that the application of the term *globalisation* became commonplace as it was used increasingly in relation to a variety of social, political and economic developments concerning the spreading network of relations around the world.

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[8] As a core feature of the world economy at the time, and with long-term global implications (e.g. the after-effects of colonialism), imperialism and globalisation proceeded hand in hand in the 19th century.

[9] Although particular attention was earlier paid to the distinction between internationalisation and globalisation, one should bear in mind that internationalisation forms part of globalisation's historical identity, and more specifically, *historical globalisation*, which preceded contemporary globalisation.

In social terms, contemporary globalisation started to be viewed as a process whereby the population of the world is increasingly bonded into a single society (Kilminster, 1997:257). Politically, it implied not only the increasing enmeshment of people within the networks of global governance, but also the spread of more widely shared political values around the world, as illustrated by the general trend towards democratisation. Economically, contemporary globalisation is ever more viewed to be at its most dynamic, especially since the collapse of communism. This is signified by the increasing bias towards privatisation and deregulation, which have given freer reign to market forces. In this regard, Lawson (2003:119) suggested that "contemporary globalisation may be seen to represent the triumph of capitalism".

Finally, contemporary globalisation is considered to be the process that caused an emergent *new global economy*[10]. This can arguably be recognised as the *latest progression* of contemporary globalisation. Ohmae (1993:81) argued that the development of a new economic structure has already started to take shape, and not just conjunctural change towards greater international trade and investment within an existing set of economic relations. In this respect, the new global economy is viewed as being more than merely extensive and intensifying international economic relations (Hirst & Thomson, 2003:7). Although it is hard to pin down its exact origin, Castells (1996:92) traces the genesis of the new global economy to the 1970s when it was the latter stages of the transition from structuralism to post-structuralism. At the time, technological innovation and productivity growth, in particular, were driven by intensifying competitiveness and growing demand for profitability. It proved to be a new economy growing within the old economy, as directed by the process of globalisation. According to Held and McGrew (2000:134), what has changed is not the kind of activities humankind is engaged in, but its technological ability to use it as a direct productive force. What distinguishes the present global capitalist economy from that of prior epochs is arguably its particular historical form. Over recent decades, the core economies in the global system have undergone a profound economic restructuring – especially after the

[10] To clarify, although the world might be witnessing the emergence of a new global economy, it should not be confused, at least not in this study, with a fully globalised economy.

Cold War. As Muller *et al.* (2001:97) suggest, in the process they have been transformed from essentially industrial to post-industrial economies. More specifically, as Castells (1996:93) underlines, the new global economy is considered to be a new social and economic structure – an unprecedented *network society*. In its character it is centred on informational capitalism in that it has involved a structural transformation in the relations of production and power. As the new technological basis for this new economy, the Internet is creating new rules as it induces the networking form. It is adding a new dimension to global competitiveness and social interaction. This new social structure is considered to be a transition from *industrialism* to the *network society* and is also associated with the diffusion of knowledge and innovation, not merely technology *per se* (Muller *et al.*, 2001:115). Although it is still in its infancy, history has remarkably shown that developments such as the current rise of the new global economy are of particular significance in stretching the confines of globalisation.

2.4 Global economic governance and economic theory: co-historical progression

The existing world order (i.e. its structures and maintenance) may, principally, be viewed as the result of a long historical process. It was to a large extent set off by the Industrial Revolution, which began in Great Britain in the early 19th century, spreading to the European continent and the United States (US). In the second half of the 19th century, it reached Japan and the *peripheral* countries of Scandinavia (Anell & Nygren, 1980:15). More contemporarily, the existing world order may be regarded as the result of the decisions taken by the allied powers during and immediately after the Second World War (Legrain, 2004:90). Notably, the process of economic development gave the major industrial countries a decisive influence over the world economy. In particular, the two world wars strengthened the military and economic position of the US – a global hegemon (with veto power in the IMF and World Bank), even until today.

The purpose of this section is, first, to depict how specific historical events and developments that shaped the world economy evolved in relation to both; actions that reflect the progression that took place in global economic governance, and advancement in economic theory/ideology and thinking. Secondly, it serves to complement and further

contextualise globalisation's historical identity. Initially, economic events and developments of historical significance prior to 1944 are briefly highlighted. The emphasis then shifts to an exploration of economic progress in and after 1944, with specific attention to how global economic governance (i.e. the IMF, World Bank, and WTO) evolved. Hence, the following sections combine the collective progression of economic history, economic theory, and global economic governance.

2.4.1 Cycles and volatility: world economic history and theory prior to 1944

The main features of the global economy, arguably, originated during the Industrial Revolution (1820-1913) (Legrain, 2004:85). Even before the Napoleonic wars in Europe ended, industrialisation had gathered momentum in Great Britain. The international consequences of this followed during the 19th century. Sparked and permitted by a cluster of inventions, sustained, long-term **economic growth** was made possible for the first time in history, with Great Britain as the engine of world economic growth. Steam-power, specifically, revolutionised the technology of long-distance transport, changed economic and social structures, and led to the eventual transformation of the domestic and international economy, societies and institutions. Levy-Livermore (1998:3-4) added that: "the primary effect of the Industrial Revolution on the world economy was to enable the linking of European and overseas economies in complementary development patterns that transmitted changes in the rhythm of economic growth in developed countries overseas". Throughout the hundred years which ended in 1913 world trade and the international transfer of capital increased far more quickly than population and production. At the start of the 19th century only approximately 3% of production was circulated through international trade. By 1913 world trade was equivalent to about a third of the total world output which can to a large extent be attributed to the fact that technological development was export-orientated (Anell & Nygren, 1980:15). The acceleration of technical progress also resulted in an average annual economic growth rate of real per capita GNP in the average OECD country six times higher than during the period of merchant capitalism prior to 1820. The extent of economic change between 1820 and 1913 was unprecedented and impressive: per capita income in the average OECD country more than tripled; the

volume of world exports grew more than thirty-fold, and international patterns of specialisation in production and trade emerged (Levy-Livermore, 1998:4).

Importantly, the *global economic order* during the Industrial Revolution and until the start of the First World War was liberal. **Economic thinking** mainly followed the Classical approach (until the 1930s) which, as expected, focused on supply-side factors and the market mechanism (Snowdon & Vane, 1999:2). Apart from high growth rates, the period 1820 to 1913 was also characterised by exceptionally free international trade, with no quantitative restrictions and relatively low or no tariffs on raw material. In addition, it featured unprecedented free international movements of labour and capital, as well as a fixed nominal exchange rate under a gold-sterling standard. By and large, the Gold Standard[11] (GS) can be perceived as a benchmark in world economic history because of its pivotal position as the first integrated economic mechanism (Hirst & Thomson, 2003:52). The GS-system, which existed from 1879 to 1914, carries great ideological and theoretical significance since it was not only voluntarily entered into by the countries involved, but also supposed to have embodied the principle of automaticity in its operation and adjustments.

The seeds, though, for this liberal ideological framework were, in fact, planted by Adam Smith's *The Wealth of Nations* in 1776 when he questioned the mercantilist orthodoxy. Smith was the first to present a systematic, coherent framework for examining trade policy and argued that free trade would allow the best allocation of society's resources while import regulations distort this pattern and so reduce national income (Legrain, 2004:87). In the early 19th century James Mill, Robert Torrens and David Ricardo made a crucial addition to Smith's work. Mill showed that trade could still be beneficial: countries should specialise in goods in which they have a comparative, rather than an absolute, advantage. Ricardo added that the rationale behind trade is that differences in labour productivity determine differences in pre-trade price ratios. By emphasising the merits of free trade, these ideas were very progressive in nature and greatly contributed to

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[11] The Gold Standard and other monetary and exchange rate regimes over history are significant to this study due to the fact that they can be recognised as concrete forms of economic governance in the world economy.

Britain's unilateral move to free trade[12] – something that many consider triggered the first big wave of globalisation: industrialisation (Irwin, 1994:38; O'Rourke & Williamson, 1999:56).

After the end of the First World War in 1918, the liberal international economy that had emerged before 1914 fell apart over the next 30 years. The Great Depression (1929-1933) that followed the Wall Street Crash of 1929 dealt liberalism an enormous blow: the economy could clearly not be trusted to regulate itself (Legrain, 2004:98). The growing degree of global economic instability caused extreme policy concern for prices, exchange rates and unemployment. The collapse of world trade was remarkable. It fell by two-thirds between 1929 and 1933 and was scarcely higher in 1948 than in 1913 (and still 9% lower than in 1929). Surprisingly, though, the real GDP per capita of the average OECD country fell by only 15% between 1913 and 1950. This development was particularly manifest in the US and Japan, while Great Britain's industrial output stagnated completely.

During the 1930s John Maynard Keynes's *General Theory of Employment, Interest and Money* (1936) signified the birth of modern macroeconomics after the high rates of unemployment appeared to shatter the classical assumption that full employment was the normal state of affairs. In response to the Great Depression, Keynes put forward a revolutionary theory to explain, and provide a remedy for, the then prevailing severe unemployment. Central to his analysis, he contended that capitalist market economies are inherently unstable. Keynes viewed this instability as the result of fluctuations in aggregate demand, and argued that the Great Depression resulted from a drastic fall in investment expenditure (Snowdon & Vane, 1999:3-5). Hence, the ensuing unemployment was involuntary, and mirrored a state of deficient aggregate demand.

Finally, it is significant to note that the interwar years still haunt the international economic system, and provide the rationale for the concerns and uncertainty associated with current trends in the international economy. Since the Second World War, the

[12] It lasted from approximately 1820 until 1914 and denotes the height of the *Pax Britannica* system. However, when the *Pax Britannica* ended in 1914, so did free trade.

constant worry of the international community is to avoid a repeat of this period, when global economic activity fell dramatically (Hirst & Thomson, 2003:54). This, coupled with the fear that man could potentially destroy the planet (as exemplified by the nuclear attacks on Hiroshima and Nagasaki), signaled a new era in history in which a new global fear was born. This was, ironically, the first true indication of an emerging global consciousness.

2.4.2 Bretton Woods and international economic recovery: 1944-1973

The Bretton Woods System (BWS) was designed in 1944 to avoid the external constraint imposed on national economies by the GS, which had operated so disastrously in the interwar period. The solution negotiated at Bretton Woods was for a fixed but adjustable system, linked to the dollar standard as numeraire. Currencies were fixed in terms of the US dollar, which itself was to be convertible into gold. The domestic impact of exchange rate interventions was *sterilised* by drawing on official exchange reserves and IMF credits. This acted as the buffer between domestic and international monetary conditions, and enhanced domestic autonomy. The Second World War caused a radical shift in the balance of power between the world's leading industrial states in both military and economic respects. The war had generated a period of pent-up demand and had destroyed capital and infrastructure in Europe and Japan. The institutional framework of capitalism, which had been temporarily abrogated by the command economies of wartime, was restored relatively quickly. The US, in particular, emerged from its isolationism of the interwar period as the world's dominant great power (*Pax Americana*) with definite plans to make the world *safe for capitalism*. This signalled the beginning of the American hegemony. The Marshall Plan of 1947 swiftly helped rebuild the capital stock destroyed during the Second World War and, in fact, generated an investment boom in Europe. In the aftermath of the Second World War, plans for the emergence of the Bretton Woods Institutions (BWI) came about in the context of rhetoric[13] for enhanced economic coordination between states as a way to ensure economic renewal, prosperity, and peace

[13] Although much of the literature points to the Keynesian belief and vision for a truly global system of codified rules and principles, which imposed obligations on states in monetary affairs, there are varying perspectives on the extent to which this was not driven by concerns with the decline of Britain's political and economic hegemonic power and the desire to make the US subject to a rules-based system.

(Skidelsky, 2000:47). This signified a prominent shift in approach to global economic management, moving away from one which was based on *ad-hoc* bilateral cooperative arrangements primarily among central banks in the major economies to one which was centred on a formalised multilateral system[14] (Varma, 2002:5). Hence, in the presence of 44 countries, a new, post-World War II economic order was consolidated at the New Hampshire Conference in 1944 with the birth of the Bretton Woods twins: the World Bank (then the International Bank for Reconstruction and Development) and the IMF (then the Stabilisation Fund). Together with the International Trade Organisation (ITO), the world economy was to be organised around these *three cornerstones* (Driscoll, 2004:59).

The **World Bank** (WB) would make loans to help rebuild war-torn economies and to finance development in general. This, coupled with the Marshall Plan, served to initiate European recovery and stave off the threat of communism – thereby channelling international investments along desired lines. The IMF was designed to take care of short-term problems relating to international liquidity. It would lend money to countries that had temporary difficulties financing a balance-of-payments deficit and sanction an adjustment in their exchange rate if the problem seemed permanent. The ITO, alternatively, would help to create a liberal system of regulations governing world trade, and it would be the vehicle to carry the world towards a system of free trade (Legrain, 2004:105). However, the intended ITO was never established at a conference in Havana in 1947-48. Disagreements between the US[15] and Britain over the extent of the authority of the proposed ITO over the actions of governments prevented the ratification of the charter for the ITO (the *Havana Charter*). In fact, in 1946, while early negotiations on the charter took place, the US took an initiative in preparing a document on a general agreement on tariffs and trade to speed up tariff reductions. Subsequent deliberations between a group of 23 nations, meeting in Geneva, resulted in a set of mutual tariff reductions which were codified as the (General Agreement on Tarrifs and Trade).

[14] As the architects of the BWS, John Maynard Keynes (head of the British delegation) and Harry Dexter White (an assistant secretary at the US Treasury) envisioned a multilateral system which could safeguard the world against the disruption of the 1930s that had led to the Second World War.

[15] The failure to establish the ITO provides an early indication of the influence of the US in the operation of the post-war international trading system – US hegemony (or *Pax Americana*) in its infancy.

Because the ITO was never officially instituted, this left the GATT as the primary framework for trade relationships (Van Meerhaeghe, 1992:57). In addition to providing a framework for the conduct of trade relations, the other two main objectives behind the establishment of GATT were to provide a framework for (and to promote) the progressive elimination of trade barriers. Thirdly, it was to provide a set of rules (codes of conduct) that would inhibit countries from taking unilateral action.

The international economic order became liberal (again), with low non-agricultural tariffs and few quantitative restrictions in the OECD (Organisation for Economic Cooperation and Development) countries, as well as a fair degree of flexibility in tariff-setting in developing countries. Due to the new payments system, the liberal trading regime as well as the **rapid growth** of import-demand in the OECD countries, the volume of international trade expanded rapidly. From 1950 onwards, progress in the OECD countries continued at breakneck speed by historical standards. The compounded annual growth rate of real per capita GDP in these countries[16] escalated to just about 2.6 times that of the interwar period, and nearly doubled the previous peak growth rate of the Industrial Revolution era (Kuznets, 1968:35). Productivity growth more than tripled, compared to the same period, and investment rates rose sharply to over 10% of GDP. This led to a stable, expansionary national and global policy framework rooted in a confluence of unprecedented and surprisingly favourable economic and institutional circumstances (Levy-Livermore, 1998:13). The impetus from the unparalleled growth in the OECD countries was then transmitted to developing countries. World trade[17] was the main transmission mechanism, and capital flows resulted in growth that, historically, was quite spectacular with real per capita GNP for all developing countries rising above 3%[18]. The growth in world trade, especially in the late 1960s, could mostly (around 75%, by value) be ascribed to GATT's Kennedy Round (1964-67) of trade negotiations, when the most substantial tariff reductions in the post-war period were made (Södersten & Reed, 1994:41).

[16] Unless otherwise mentioned, the numbers cited in this paragraph – and in the remainder of this section – refer to all OECD countries taken together, apart from Greece, Iceland, Portugal, Spain and Turkey.

[17] Since the 1950s the Heckscher-Ohlin model (which explains that the cause of trade is different countries that have different relative factor endowments) became the dominant model of comparative advantage in modern economics. It emphasises that international differences in factor endowment result in differences in relative prices and comparative advantage, thus creating a basis for mutually beneficial trade.

[18] This figure is an unweighted average and was more than triple that of the early industrialisers.

During the 1960s, in particular, the **IMF's** role had been transformed by the explosive growth of international financial markets. These sprung from the off-shore financial markets – i.e. the Eurocurrency markets. Paradoxically, financial markets got another boost when America suspended the dollar's convertibility in August 1971 and the world moved to floating exchange rates, with markets, not governments, mostly setting currency rates. The reason for this was that the BWS had become increasingly inadequate to the liquidity needs of the world economy, and started to break down (Anell & Nygren, 1980:50). When the **US** breached the IMF agreement by no longer converting dollars into gold, it marked the end of an era for working within a multilateral framework of rules. Notably, this also reflected the problems which can occur when the dominant currency of the international monetary order is also that of a hegemon's power that can use its position to pursue its own agenda (Braithwaite & Drahos, 2000:54). The problems, however, could be traced back to the mid-1960s, when the large defence contracts for the Vietnam War began. This accelerated inflation and, as a result, the faith in the dollar was further undermined as it led to a dollar glut. Subsequently, in 1967, the ten leading OECD countries agreed on a procedure to create a new kind of international means of payment, the so-called Special Drawing Rights (SDR). This was adopted in the same year by the IMF and for the first time in history, an international reserve currency was created by a deliberate, multilateral decision (Legrain, 2004:105; Kreinin, 2006:337). Succeeding this, in 1971, the major financial nations at the time announced an agreement on the re-alignment of exchange rates and restabilisation of currencies (revalued against the dollar) under the Smithsonian Agreement. Hence, the BWS finally collapsed in 1973.

From 1944 to 1973 **macroeconomic theory** was to a large extent dominated by the Keynesian consensus – the framework within which the BWI were found. The ever-evolving Classical-Keynesian debate continued to divide views between, respectively, the efficiency of unfettered markets, and the belief that aggregate economic instability represents some sort of market failure and that limited state intervention is needed (i.e. *embedded liberalism*). Keynes's strong involvement in restructuring the world economy after the Second World War meant that his views played a dominant role in most policy frameworks – institutional and public – as well as in the formation of the **BWI** and the

Marshall Plan (Snowdon & Vane, 1999:5). The implication of Keynes's analysis was that fiscal and monetary policy could correct the aggregate instability exhibited by market economies and help stabilise the economy at full employment. However, by the mid-1950s the consensus that started to transpire, particularly in the US and within the BWI, was Samuelson's neo-classical synthesis, which made significant contributions, among other things, to the development of **growth theory**. With the mounting emphasis on the decolonisation of Africa and other regions after the Second World War and the exceptional economic growth experienced by the industrialised nations, proposals to enhance growth in poor nations started to emerge. Of particular significance were Rostow's stages-of-growth model, the Harrod-Domar growth model and Lewis's theory of structural change. In Rostow's explanation, for an economy to advance from a state of underdevelopment to development, it must go through a series of growth stages. The important factor is the mobilisation of domestic and foreign saving in order to generate sufficient investment to accelerate economic growth. The economic mechanism to achieve this became known as the Harrod-Domar growth model, which states that the rate of growth of GNP ($\Delta Y/Y$) is determined jointly by the national savings ratio, s, and the national capital-output ratio, k. Accordingly, by multiplying the rate of new investment, $s = I/Y$, by its productivity, $1/k$, it will give the rate by which GNP will increase (Todaro & Smith, 2003:112). Highlighting the importance of structural transformation in particularly labour abundant subsistence economies, Lewis's theory dominated economic thinking in the developing world in the 1950s up to the early 1970s. According to Lewis' theory the development process will be stimulated if labour is transferred from the traditional sector to the industrial sector in order to allow industrialists to increase their output, and eventually reinvest the so-called capitalist surplus. All these theories were growth centred and based on the assumption that capital accumulation would eventually increase per capita income.

During this period the **BWI**, whose establishment was based on Keynesian thinking, ventured into a new direction – that of neo-classical thinking – which was mainly growth-focused and dominated economic development thinking as well as the application of the BWI's policies. Given the significance of high economic growth rates that prevailed in

most economies in the 1950s and 1960s, the growth-centred models formed the main focus of economic theory.

2.4.3 A world order in crisis: 1973-1981

In the shadow of the dollar crisis, the governments in the industrialised countries began to lose control over inflation (or rather stagflation). During 1973 the US imposed an embargo on some of its exports as the already-increasing prices of raw material started to accelerate. Protectionist tendencies became increasingly evident. OPEC (Organisation for Petroleum Exporting Countries) quadrupled the price of oil and prohibited exports to the US and the Netherlands. This accelerated the decline of trade at the same time as the current account was seriously weakened in virtually all oil-importing countries. Economic policies fell out of rhythm. Unemployment reached a level reminiscent of the 1930s. Together with **slowing economic growth**, the symptoms of a crisis in the old economic world order were obvious and calls for *structural changes* became stronger (Anell & Nygren, 1980:75). By borrowing money for imports, expansive developing countries increased their foreign debts faster than their repayment capacity and had to devote over a quarter of their export revenues to interest and loan repayments (Anell & Nygren, 1980:78). Added to this, productivity growth slowed down in most OECD countries, coupled with continued short-term price shocks (in gold, manufactured goods, oil, etc.) during the 1970s. Balance-of-payments constraints became binding. As a result, the governments of industrialised countries replaced the goal of full-employment growth with the twin objectives of containing inflation and restoring balance-of-payments equilibrium. They adopted cautious macroeconomic policies and espoused a stance of fiscal restraint. Consequently, the economic growth rates of the OECD countries fell to, on average, approximately one quarter of the previous per capita annual real rate. A growth crisis was on hand, aggravated by the fact that growth in real world trade fell to just over 3% per year – less than one half its previous rate (Levy-Livermore, 1998:19).

Remarkably, the growth rates of developing countries did not follow the trend set by those in developed countries. Faced with severe balance-of-payments pressures stemming from the price shocks combined with declining exports and generally weakening terms of

trades, most developing countries[19] have borrowed heavily to sustain their growth rates (Levy-Livermore, 1998:20). Banks in the developed countries, especially the US, extended loans to them since they were attracting an influx of petro-dollars. Until 1982, the foreign debt of developing countries[20] escalated; for the average non-oil developing countries, total foreign debt increased to a third of their GDP and over 150% of exports. At its Committee of Twenty (C20) meeting in 1976, the **IMF** recognised the emerging monetary disorder and allowed member countries to solve their problems to the best of their ability (Anell & Nygren, 1980:80). After this, fora such as the G7 (Russia was still excluded from the G8) were considered for coordination of international monetary policy. This was based on information exchange and consultation, and thus very different from any multilateral institutional binding form of rules and cooperation, and from what the IMF was originally designed to do (Varma, 2002:8). The only ostensibly positive aspect that came out of the decade after the oil shocks was the growth of international financial markets which resulted from OPEC countries who initiated large amounts of investment. Starting in the late 1970s, controls on capital movements were lifted in order to tap the now fast-growing international financial markets, which were further bolstered by new technologies, such as computerisation, and new instruments, such as derivatives. The IMF became the *guardian* of the stability of the international financial system and as a corollary of its mandate, it had to assist countries in financial distress.

The **World Bank** became the principal agency for assisting least-developed countries (LDCs) to get capital from the more developed, industrial countries and thereby continued its role as facilitator and promoter of investment and capital (Södersten & Reed, 1994:350). Until 1980, loans from the World Bank constituted project lending in the broad sense (Shihata, 2000:230): the financing of investment that enhances development (so-called programme lending); investment in specific sectors (sectoral lending), and lending to financial intermediaries which, in turn, provide equity participation to local enterprises. The World Bank thus stayed true to its mandate of being a primary financier of loans and other investments towards its member countries.

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[19] The group of low-income Asian countries is an exception.

[20] It was during this period that the developing countries put forward their proposal for a new international economic order (NIEO) in which they essentially requested a more even distribution of resources.

In another development, the Tokyo Round (1973-1979) of **GATT** was characterised by what was considered to be the first time that the institution comprehensively dealt with non-tariff issues affecting trade in goods, such as standards and technical specifications. It implied the proliferation of plurilateral agreements in areas such as subsidies, customs valuation and import licensing that apply only to those (chiefly the OECD countries) who sign up to them. Although developing countries could negotiate for a legal basis for receiving preferential treatment, they remained dissatisfied with their failure to achieve greater concessions (Nielson & Taglioni, 2003:24). Notwithstanding the fact that trade relations between the US, the European Community and Japan were strained, vital reductions in tariff and non-tariff barriers also proceeded (Irwin, 2001:326).

As far as **economic theory** is concerned, the theoretical developments in economics during the 1970s were still dominated by the neo-classical school as they replaced monetarism as the main rival to Keynesianism. Robert Lucas, in particular, made major contributions in this area and introduced his *surprise* supply function where output deviates from its natural level only in response to errors in price (inflation) expectations (Snowdon & Vane, 1999:11). With economic growth slowing down, and inflation and debt escalating, the focus of macroeconomics primarily turned to business cycle research in attempting to find new theoretical explanations. Although Robert Solow's neo-classical growth model was generally accepted until the early 1980s, the real business cycle approach challenged this conventional wisdom by assuming that the economy is subjected to random supply-side shocks (as opposed to demand-shocks). In this approach, the observed volatility in GDP is considered to be variations in the natural (trend) rate of output, and not deviations of output from a smooth deterministic trend. Subsequently, growth-centred approaches towards economic development still remained the dominant focus of the 1970s. Despite the fact that the literature in the 1970s paid much attention to the international dependence revolution[21] as well as the basic needs approach[22] (see Hunt,

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[21] The international dependence school of thought, dominated by Latin American thinktanks, argued for a change in *power* relations in and between countries as underdevelopment is the result of domination by the rich countries.

[22] This approach was developed by the Dag Hammerskjöld Foundation Report of 1975 and supported by the International Labour Organisation. This approach was predominantly concerned with provision of basic needs of people by increasing their participation in the economy and providing opportunities for the poor.

1989:260), these approaches were neither endorsed by the BWI nor included in their policy frameworks.

2.4.4 Debt crisis, structural adjustment and reformations: 1981-1993

Given the prevailing volatile circumstances in the **world economy** resulting from the growth crisis and stagflation, a debt crisis appeared to be inevitable. As tensions grew, the debt crisis was brought to a head by the inability of Mexico, Brazil and Turkey to meet their debt-service obligations by 1982 (when Mexico placed a moratorium on its debt repayments). Consequently, banks in developed countries became unwilling to extend further loans to all developing countries and attempted *rescheduling* as a way to deal with the debt crisis (Legrain, 2004:107). Unfortunately, the mistake most LDCs made was to either export their way out of the crisis, or adopt restrictive import regimes combined with deflationary government spending and macroeconomic policies or a combination of the two strategies in a stop-go manner. The result, which was generally evident in the LDCs during the 1980s, was rampant inflation, capital flight, low investment rates, drastic declines in living standards, and considerable increases in poverty. In addition, debt-service requirements have led to a net export of capital to the developed world by the end of the 1980s and 1990s. In fine contrast, the South-East Asian countries have continued, if not improved, their previous developmental performance and attracted large amounts of capital. Of significance, though, is the fact that the period from 1981 to 1993 has also been an era of substantial institutional adjustment and policy reform in most developing countries. Greater emphasis on open-trade regimes became apparent in many Latin American countries. Market institutions have generally been reinforced, especially in some African and Latin American nations (Kreinin, 2006:338). With changes taking place in the international payments regime, coupled with the recovery of the dollar (1981-1985) and the Cold War that ended in 1991, the OECD countries experienced a revival in growth combined with more trade liberalisation. This indicated that *liberal ideas* have been strongly in the ascendancy again since the 1980s.

This was the period during which the **IMF** and the **World Bank** enforced their stronghold within global economic governance through the advent of conditionality. In

fact, it has ensured infiltration into the domestic policies of developing countries, together with mechanisms for constant surveillance. By actually moving beyond its original mandate, the IMF started with development financing accompanied by structural reform/adjustment programmes (SAPs). Concurrently, the World Bank increased its role in providing loans for balance-of-payments support (rather than specific projects or sectors) to developing countries, together with specific conditionalities for policy reform. Notably, the IMF's agenda of anti-deficit and anti-inflationary policies collaborated with the World Bank's efficiency prescriptions for deregulation, privatisation, and liberalisation (Varma, 2002:9). Ahead of macroeconomic indicators and sectoral reform, the conditionality programmes of each have intensely extended into matters such as governance, corruption, and judicial reform.

The lengthy Uruguay Round (1986-1993) in Punta Del Este became one of the largest negotiating mandates on trade ever agreed (Nielson & Taglioni, 2003:24). This round of the **GATT** Treaty has helped, despite conflicts and divergent interests over agricultural products, financial services and intellectual property rights (TRIPS), to keep the world trading system both open and at least potentially subject to calculable rules (Hirst & Thomson, 2003:15). Moreover, if the widespread consensus of the 1950s and 1960s was that the future belonged to a capitalism without losers, securely managed by national governments acting in concert, then the later 1980s and 1990s have been dominated by a consensus based on contrary assumptions: that global markets are irrepressible and that the only way to avoid becoming a loser – whether as a nation, firm or individual – is to be as competitive as possible. Notably, these were also the principles on which the views of the IMF, WB and GATT were based (Varma, 2002:12). The notion of an ungovernable world economy is a response to the collapse of expectations schooled by Keynesianism and sobered by the failure of monetarism to provide an alternative route to broad-based prosperity and stable growth. Since the mid-1980s – in terms of **economic theory and thinking** – the new Keynesian school has, in fact, emerged as the main rival to the neo-classical approach. New Keynesian research mostly concentrated on explaining why prices and wages adjust only gradually, and in doing so have sought to re-establish a case for policy effectiveness and justify interventionist policies to stabilise the economy

(Todaro & Smith, 2003:127). Dominating the 1980s, this led to a neo-classical counter-revolution in development theory and policy, mainly arguing that poor resource allocation occurs due to incorrect pricing policies and too much state intervention. This counterrevolution favoured supply-side macroeconomic policies, rational expectations theories, and the privatisation of public corporations. In both developed and developing countries it called for freer markets and the dismantling of public ownership and government regulation of economic activities. It is argued, according to this neo-liberal (or neo-classical) view, that by permitting competitive free markets to thrive, combined with greater privatisation and less government regulations that cause price distortions, both economic efficiency and growth will be stimulated. Of great significance, though, is the fact that neo-classicists obtained controlling votes on the boards of two of the world's most powerful financial agencies – the World Bank and the IMF (Todaro & Smith, 2003:128). These developments were greatly impelled by the introduction of the Washington Consensus[23] (WC) in 1989. Viewed as a major contribution to structural reform and policy discourse at the time, the neo-classical principles that the WC tended to reflect became the *backbone* of the policies the World Bank and IMF applied toward their client countries (Stiglitz, 2003a:53). The WC essentially includes the rational expectations presumption of free market fundamentalism (Davidson, 2004:593). As a reform agenda, the WC's list of ten policies was directed at promoting economic growth. At the core of this list were fiscal austerity, privatisation and market liberalisation, which became the three pillars of Washington advice during the 1980s and 1990s.

Underlying the WC was the policy assumption that the needed level of resources for development financing would be provided by private capital flows and that attracting and retaining access to those flows should be a primary policy aim for developing countries. However, the WC has proven to be a failure in being a policy framework that attempts to increase and maintain private capital flows to emerging markets. On the basis of adverse developments and crises in numerous emerging economies during the 1990s and there-

[23] The WC was first presented in 1989 by John Williamson as an attempt to summarise the commonly-shared themes among policy advice by Washington-based institutions at the time (the IMF and World Bank). Originally, though, it was designed as market-orientated reforms for Latin American countries.

after, many scholars[24] started to question the WC and specifically its assumption that private flows can provide adequate resources for development in an economically unequal global landscape (D'Arista, 2004:22-24). Öniş and Şenses (2005:264) point out that "the Washington Consensus was based on the understanding that imperfect markets are always superior to imperfect states". This implies a lesser role for government given that it is, principally in WC-speak, confined to securing law and order, macroeconomic stability and the provision of physical infrastructure.

2.4.5 New uncertainties and opportunities after the Cold War: 1993-current

After the fall of the Berlin Wall in 1989 and the collapse of the Soviet Union in 1991 and especially after the opening up of China, another 1.7 billion people were brought into the capitalist world. Coupled with the effects of the WC, this set off the economic liberal push of the 1990s. In becoming more genuinely global than before, economic globalisation started to involve countries where roughly two-thirds of the world's population lives. The other third is not immune to it, but is still to a large extent isolated from it. By way of specifically faster and cheaper transport and communications technology, the **global economy** became quite a *techno paradise* where emails *zip* round the world instantly and with over 1 billion people using the Internet by 2005 (Internet World Stats, 2006:1). Just as the 20th century witnessed the global diffusion of industrial capitalism, so in the early stages of the 21st century post-industrial capitalism is taking place. World trade grew to record highs. In 2000, goods and services worth $7.8 trillion were traded internationally – $1300 for every person on earth. While the world economy is currently over six times larger than in 1950, the volume of world trade is nearly 22 times what it was then (Legrain, 2004:109). Cross-border trade has soared from 8% of world output (GDP) in 1950 to 25% in 2000. Although a wider range in products is traded than ever before, most significantly, however, is the growth in services. By 2004 approximately a fifth of world trade was in services. Furthermore, the growth in foreign investment is staggering. Whereas in 1985 companies invested a mere $50 billion abroad, by 2000 their foreign direct investment (FDI) totalled $1.3 trillion. Ending the downturn since 2001, global FDI inflows grew 6% in 2004 to $612 billion (UNCTAD, 2005:1). In

[24] See D'Arista (2004:24-30), Stiglitz (2003a:76-86), Held (2005:15), Davidson (2004:594-595).

becoming more prominent than ever before, multi-national corporations (MNCs) became arguably the *most dominant* participants in the world economy, accounting for 30% of global GDP and two-thirds of international trade – of which about half is trade within the same company and its ancillary networks (Muller *et al.*, 2001:8).

Although the end of the Cold War has created a more *fluid* global system, it also set off a new era of immense global uncertainty. First, there was the Mexican crisis of 1994-1995 when the drastic depreciation of the peso triggered a cycle of portfolio investor exits which induced fears[25] of global financial contagion (Michie & Smith, 1999:18, 41). This was followed by the East-Asian crisis of 1997-1998. The fragility of the affected East-Asian economies as well as the banking crisis experienced by the Japanese economy sent fears of global financial contagion throughout the world – yet again (not to mention the impact of the current global financial crisis). It became clear that these crises[26] and other related/similar uncertainties in the global economy could be ascribed to the general trend towards the liberalisation of global financial markets and, in particular, to the deregulation of capital controls which – in these cases – led to *overinvestment*.

Particularly after the Cold War, the world economy became, as a primary feature, settled into three largely self-contained regional centers (the TRIAD): the EU[27], which trades a mere 11% of its collective output with the rest of the world; NAFTA, which trades just over 8%, and Japan, 11%. The rest of the world is linked to at least one of these hubs through a tangled web of bilateral (or regional) trade agreements (Legrain, 2004:112). On the face of it, the real character of the international system will continue to be dominated by the TRIAD countries and their regional clusters or allies. Correspondingly, the pattern of foreign investment is uneven too. Most global FDI flows (85%) come from American and European companies, and 70% of them are invested in either the US or the EU (Hirst

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[25] The Mexican crisis also led to fears of systemic financial crisis in other emerging markets, as investors turned bearish on the markets. When this flight did occur, it was termed the *tequila effect*.

[26] Argentina also fell into crisis in 2001, but for slightly different reasons. Faced with a domestic recession, external deficits, and a declining value of the Brazilian currency, it could not maintain the peso fixed at 1 peso = $1. It finally adopted a floating exchange rate and also restricted the inflow of short-term funds (Kreinin, 2006:348).

[27] After many years of negotiation since 1951, the European Union (EU) was established under that name in 1992 by the *Maastricht Treaty,* and then launched the euro as its official currency in 2002.

& Thomson, 2003:57). One might add, though, that among the developing countries, China and India are exhibiting annual growth rates of 6% to 10% and are starting to play a significant role in international trade and attract vast amounts of FDI.

By furthering its efforts into development financing, supplemented by structural adjustment programmes (SAPs), the **IMF's** active involvement in country assistance during the 1990s was primarily in the form of its Enhanced Structural Adjustment Facility (ESAF). However, due to heavy criticism regarding its harsh impact on poor countries and its failure to promote economic growth and macroeconomic stability, the IMF later replaced the ESAF with the Poverty Reduction Growth Facility which takes shape through the Poverty Reduction Strategy Paper (PRSP) process. The PRSP process can be regarded as a way for the IMF, and the **World Bank**, to further micro-manage policy directions in developing countries, covering health, environment, and labour issues (Varma, 2002:9; Mosely *et al.*, 1995:65). In addition, the IMF made use of the enhanced Heavily Indebted Poor Countries (HIPC) initiative which, in essence, is based on the acceptance and continuation of debt management whereby a PRSP must be developed as a precondition for HIPC debt relief. The actual relief, though, will only be forthcoming once the strategy is implemented.

In corresponding with the expansion of the domains of both the IMF and the World Bank, the **World Trade Organisation** (WTO) was established in 1995 (superseding the GATT) as an intergovernmental negotiating forum. The WTO currently sets and regulates a code of international trade conduct, which contains three basic principles: the principle of nondiscrimination embodied in the most favoured nation clause; a general prohibition of export subsidies (except for agriculture) and import quotas, and a requirement that any new tariff be offset by a reduction in other tariffs. Distinctively, the functions of the WTO[28] are much wider than those of the GATT. Apart from overseeing rules pertaining to international commodity trade, it also deals with transactions in commercial services, intellectual property rights, and foreign investments (Kreinin,

[28] As Kreinin (2006:84) points out, the WTO is a global organisation that formulates ground rules for international trade and provides a framework for liberalising trade.

2006:141, 349). WTO negotiations under the Doha Round[29] (since 2002) were quite stymied, and needed a powerful initiative to push them ahead. As demonstrated in the Hong Kong ministerial meeting in December 2005, the strong trend towards bilateral and regional trade agreements appears to be permanent (WTO, 2005:33). WTO leadership is needed to minimise the trade-diverting effects of such arrangements. Opportunely, strong suggestions were made that *aid for trade* be expanded and directed towards helping developing countries, particularly LDCs, to build their supply-side capacity and trade-related infrastructure so as to benefit more from WTO agreements.

Significantly, the IMF, World Bank and WTO have strongly followed a neo-liberal[30] ideological approach, especially in the aftermath of the Cold War and after the acceptance of the Washington Consensus. The global spread of neo-liberal doctrines has everywhere reduced the ability of governments to autonomously formulate economic policies – a clear indication of the interwovenness of economies around the world and, more importantly, the *influence* of global institutions of governance (Wade, 2000:488). The waves of deregulation that have curtailed governmental powers virtually across the world since the 1980s have their origin in deep and intricate value shifts. In this regard, the proliferation of neo-liberal norms was propelled not only by the failures of socialism but also by the advocacy of the United States (Berger, 2000:52). In a position of unchallenged dominance in global financial and trade institutions, the US pushed for a rapid end to capital controls across the world and for making IMF and World Bank assistance dependent on recipient countries' acceptance of incisive limitations on the role of government in the economy[31].

Initially, in terms of **economic theory**, the upsurge of the neo-liberal orthodoxy as a commonly accepted framework for implementing the principles of market liberalism, primacy of individualism, outward orientation and state contraction in the majority of countries (including the G7) made the Washington Consensus seem very credible.

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[29] Note that the Doha Round is still inconclusive.

[30] The neo-liberal ideology (also known as pluralism) could be regarded as part of modernisation theory and due to its neo-classical nature, its central focus is the rule of the market or market fundamentalism.

[31] From this perspective, globalisation is, in effect, a process steered by politics: ideological change, the contingencies of the collapse of the socialist economy, and US power in the world *(Pax Americana)*.

However, during the 1990s the WC came under serious challenge as empirical evidence undermined the fundamental claim that full-scale liberalisation at all cost is associated with superior economic performance (Öniş & Şenses, 2005:265, Davidson, 1993:165). In this regard, endogenous growth theories such as the Lucas and Romer models re-emphasised the importance of savings and human capital investment for achieving rapid growth, hence suggesting an active role for public policy in promoting economic development through direct and indirect investment[32] in human capital formation and the encouragement of foreign private investment in knowledge-intensive industries (e.g. technology such as computer software and telecommunications). The problem with the WC, as argued by Rodrik (2003:56), was that it "listed what became regarded as *ten commandments*, with an implicit promise that a country that did these ten things would grow". Fading support for the WC is commonly attributed to its macroeconomic prescriptions. Maintaining fiscal discipline, which prohibited the adoption of anti-cyclical policies, was an unrelenting demand at the core of the WC (D'Arista, 2004:23). However, the most important criticism against this *one-size-fits-all* approach was what it omitted (e.g. limited government intervention) rather than what it included. This led to the emergence of new lines of thought in development theory, which included a number of adjustments to the original WC. By his own admission, Williamson (2000:195) repeatedly emphasised that, although the WC still amounts to a sensible reform agenda, it is incomplete. Whereas the WC mainly focused on so-called *first-generation reforms*, there was a growing need for *second-generation reforms*, which involves the strengthening of institutions that could augment possible benefits derived from earlier reforms. Hence, in response to the absence of vital institutional transformation (needed to complement market-orientated policies), the fear that financial liberalisation may result in too much volatility, and the waning *trickle-down effect*, a variety of adjustments on the WC – as articulated by different schools of thought – emerged during the latter part of the 1990s (Loots, 2006a:22; Rodrik, 2006:74-75).

One line of thought, known as the *Augmented Washington Consensus*, suggested that the existing WC's policy guidelines be enhanced with second-generation reform measures.

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[32] It includes *complementary investments* in education, infrastructure (providing public goods) and research.

This included better corporate governance, anti-corruption measures, more flexible labour markets, prudent capital account opening, financial codes and standards, and targeted poverty reduction strategies – to name but a few (Rodrik, 2003:44). Parallel to this school of thought, a so-called *New Consensus* also emerged, which mainly had contributions from the *Santiago Consensus* (since April 1998) and the *Monterrey Consensus* (since March 2002). In stressing the importance of market-based development, the Santiago Consensus also placed much emphasis on broadening the government's role with regard to a number of functions, including (Todaro and Smith, 2003:704; Smith, 1998:16): providing more macro-stability; improving infrastructure, public health, and education; facilitating technology transfer; managing coordination failure in the private sector, and regulating and supporting financial sectors; and lastly, ensuring the provision of basic public goods. The Monterrey Consensus made significant contributions to the debate by emphasising the importance of broader economic and human development – especially in developing countries (Loots, 2006a:24). It aims at ensuring sound macroeconomic policies and endorsing the UN millennium development goals, granting increased market access for developing countries, increasing FDI and aid flows to mobilise domestic and foreign resources for development, fighting corruption by means of good governance, ensuring peace and security, and attending to systemic issues such as the coherence between the international financial, trading and monetary systems in order to provide more assistance to development.

Complementary to the above consensuses, the *Post-Washington Consensus (PWC)* also stresses the importance of effective institutions (international and domestic) as a necessary ingredient for successful development as well as the formation of transparent and accountable states for the same purpose. It is believed that well-functioning governments are vital to market-orientated reforms. Importantly, the growing criticism directed towards the neo-liberal paradigm since the 1980s and 1990s put pressure on the BWI to respond positively to the PWC and similar consensuses. During the late 1990s and especially after 2000, the BWI noticeably shifted their policy focus from a hard-core neo-liberalism to this new synthesis. By 2001, according to D'Arista (2004:31), "they started to place increased emphasis on promoting financial stability and preventing

crises". Moreover, due to the renewed interest in poverty, governance, and institutional issues by the IMF, WB and the WTO, greater emphasis has also been placed on exploring how to attain the critical requirements for successful development. The PWC provided valuable guidance and focus in this respect (Williamson, 2000:200-201). In aiming to transcend the old consensus, the PWC places a high premium on the creation of democratic regimes where states and markets are considered to be complementary rather than substitutes. While this new emphasis is what mainly distinguishes the PWC from the early neo-liberal agenda, it (and other consensuses) inherently remains a *product* of the current hegemonic position of the neo-liberal paradigm (Öniş & Şenses, 2005:275).

2.5 Issues of debate: global economic governance and globalisation[33]

The contentious characters of both global economic governance and globalisation make debate something that is hard to prevaricate. Triggered by abrupt and often baffling changes in contemporary world economy, a critical dialogue has opened up that attempts to interpret the present form of the world economy, the kind of changes that are taking place, and the modes and effectiveness of contemporary economic governance. The debate is mainly divided between two schools of thought with almost diametrically opposed views: the globalists[34] and the sceptics (or traditionalists). A third perspective, that of the transformationalists, takes a different stance and often places itself in the middle. This section will focus on three primary issues of debate, thereby contextualising the arguments of each school of thought. It then outlines the view taken in the study.

The **first issue** of debate centres on the matter of whether globalisation should rather be understood as internationalisation (or even regionalisation). As indicated in section 2.2, *globalists* in general are proponents of a radical form of globalisation, whereas *sceptics* are more in favour of internationalisation and regionalisation – especially trilateral

[33] Note that although the issues of debate emphasised in this section encapsulate some of the most important contentious matters related to globalisation and global economic governance, it does not, of course, include all the various debatable issues that can be related to these two themes.

[34] Globalists are, in fact, divided between positive and pessimistic globalists. Whereas the former has a neo-liberal stance and focuses more on the opportunities created by globalisation, the latter is a neo-Marxist version of the globalist position, which accepts the account that a strong globalisation process has occurred, but thoroughly condemns it (Held, 2000:22, 89). Unless otherwise pointed out, the debate – when referring to the globalist perspective – chiefly emphasises the positive position.

regionalisation which essentially involves the TRIAD countries. Although this issue has to a large extent been dealt with, the transformationalist perception is still an important remaining constituent. This view recognises the evidence of new forms of intense interdependence and integration that are transforming the international economic system. According to Held (2000:90), *transformationalists* argue that "international economic relations have changed to such an extent that, whilst the traditional view of a coherent national economy that can be managed in the interests of domestic objectives is no longer viable, the ubiquity of market forces could also be challenged and resisted, though with great difficulty and only in new forms". They thus interpret this process of global change and transformation as a conditional form of globalisation that is constantly evolving (Held, 2000:90). In this sense, globalisation should not be understood as an inevitable or a fixed end-point.

The **second issue** of debate concerns the question of whether modern-day globalisation is unprecedented or not. *Globalists* believe that even though globalisation has been continuing for centuries, what is happening now is, in many respects, inevitable and historically unprecedented. They assert that globalisation is presently more genuinely global than before. Whereas globalisation was essentially driven by Europe and the Americas in the late 19th century, it now also involves Japan, the East-Asian countries, China, Mexico, India and more – countries where almost two-thirds of the world's population live (Legrain, 2004:108). As part of the Internet-led technology revolution, transport and communications are faster and cheaper, thus facilitating the expansion of globalisation even more.

In substantiating their argument, globalists contend that world trade is at record highs and that a wider than ever range of products is traded. Cross-border trade had risen to over 25% of world output (GDP) in 2000, which is significantly above the previous peak of 18% in 1914 (Obstfeld & Taylor, 1999:78). Products traded are now more technology-driven than before, not to mention the growth in services: telecoms, finance, insurance, software, and management consultancy. Cross-border services trade, which previously hardly registered in world trade figures, was the fastest growing component of world

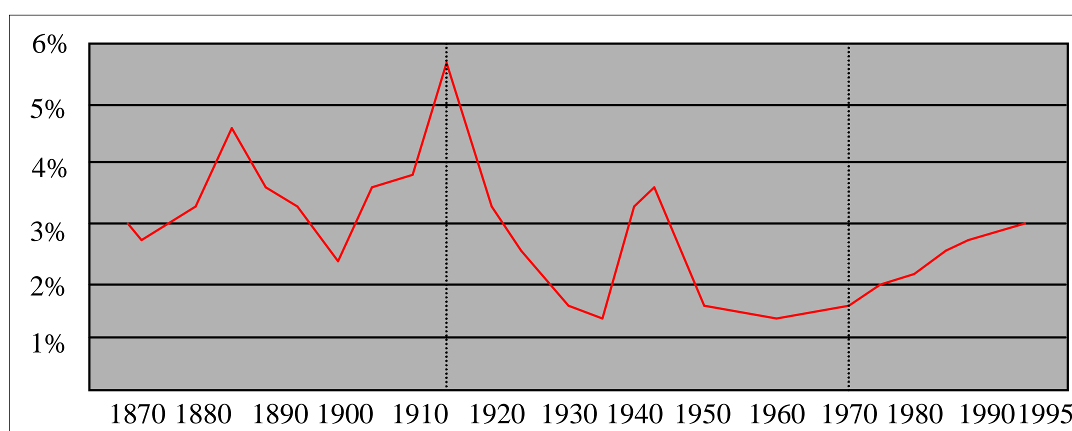
trade in 1997 (contributing 25% of the total) (Legrain, 2004:108-109). In addition, globalists argue that foreign investment is also unprecedentedly larger. Assets owned by foreigners increased to 56.8% of world income in 1995, compared to the earlier climax of 17.5% in 1914. Globalists assert that, although foreign investment was respectably substantial a century ago, it was limited in its impact (Hoogvelt, 2001:70).

Opposing these contentions, *sceptics* argue that globalisation is at any rate much exaggerated as a distinctively new phenomenon, and highlight continuities between the past and the present. They contend that the current highly internationalised economy is not unprecedented and does not necessarily involve a move towards a new type of economic system. Hirst and Thomson (2003:2) emphasise that "it is one of a number of distinct conjunctures or states of the international economy that have existed since an economy based on modern industrial technology began to be generalised from the 1860s". Sceptics claim that, despite increases in global flows of trade and investment, these are not substantially different to the economic and social interactions that have occurred between nations in previous historical times (Held, 2000:23). In a sense, sceptics argue, the current international economy is less open and integrated than the regime that existed from 1870 to 1914 (the *belle époque*). The exchange of goods and cultures dates back to early times. Even in the 19th century, open trading and liberal economic relations were customary worldwide. Thus, we are merely seeing a continuation and progression of earlier world trading links.

In the sceptical view, the pre-1914 system was genuinely international, tied by efficient long-distance communications and industrialised means of transport. The current technology revolution in communications and information, they argue, has further developed a perhaps more complex monetary and trading system, but did not create it. Sceptics also prefer to compare different periods in terms of their openness and integration in order to support their argument (Hirst & Thomson, 2003:27). In a study aimed at measuring financial openness, Grassman and Lundberg (1981:128) used the current account balance to GNP ratios of six leading countries (Great Britain, Italy, Sweden, Norway, Denmark and the US) and found no increase in openness between 1875

and 1975, and a decline in capital movements for these countries. Measuring it somewhat differently, Howell (1999:16, as shown in Figure 2.2) found that there was a decrease in openness among the G7[35] countries from a peak in 1913 (almost 6%), but with a gradual increase after 1970 – yet, only reaching 3% by 1995. Furthermore, although the net capital flows of the G7, as a percentage of world GDP (at purchasing power parity), increased from 0.34% in 1995 to 0.94% in 2000, there was a steady decrease in the five-year period after that, falling to 0.86% in 2005 (IMF, 2006:2-6).

Figure 2.2: International capital flows among G7 economies: percentage of GDP (1870-1995)



Source: Howell, 1999:17 "Asia's Victorian Financial Crisis", *IDS Bulletin*

In a study Turner (1991:17), comparing the pre-1914 Gold Standard period with the 1980s, found that current account imbalances and capital flows, measured in relation to GNP, were larger before 1914 than during the 1980s. Hence, sceptics contend that using gross figures for ratios of trade and capital flows relative to output confirms that *openness* was greater during the *belle époque* than even in the 1990s. All this, argue the sceptics, points to a similar or even greater degree of internationalisation during the earlier period, which – in their view – suggests that modern-day processes and developments are not unprecedented (Hirst & Thomson, 2003:28, 60).

[35] To clarify, whenever the study refers to the G7 countries it refers to the United States, Canada, Japan, the United Kingdom, France, Germany, and Italy. It deliberately excludes Russia (as the remaining constituent to the G8) in either the data referred to or in it not being a relevant role-player to a specific issue/subject. The G7 and G8 are not terms used interchangeably as they are, on purpose, referred to differently.

Transformationalists assert that new and different issues of economic interdependence in the present era are particular to it. In this view the world economy has certainly not remained unchanged. Due to fundamental re-organisations in the global economy, they argue that (Held, 2000:90):

- the world is in a new phase re the internationalisation of economic activity;
- the present era is one of unprecedented transformation in the patterns of international enmeshment – i.e. complex patterns of reciprocal interdependency and integration between economies, and
- the process of transformation designated by the term globalisation is a contingent and historically specific one.

As economies have become interdependent and technologies connected societies from around the world in an interwoven web of interaction, globalisation, according to transformationalists, has been progressing intermittently throughout the modern age. They argue that it's most recent manifestation signifies a strong qualitative shift towards an unprecedented higher level of international interdependency, integration, and cooperation (Bell, 2003:805). Transformationalists are specifically cautious of the apparent *essentialism* of the globalists and the sceptics. Instead they deliberately propose a *via media*, asserting that globalisation is a momentous phenomenon – one that is novel in many regards – but nothing also that is a long-term historical process, shaped by conjectural factors. Hence, transformationalists agree that globalisation represents a significant shift, but question the inevitability of its impacts.

To this end, it is necessary to highlight that, although the first two issues of debate mainly focused on globalisation, both have important implications for **global economic governance**. With regards to the first issue *vis-à-vis* the interpretation of globalisation, the *sceptical* understanding of internationalisation (as opposed to globalisation) reflects a world order dominated by nation-states (Castells, 1997:162). From a global economic governance perspective this involves a greater degree of emphasis to be placed by the IMF, World Bank, and WTO on supporting governments' efforts to govern cross-border economic activities more efficiently (thus respecting their sovereignty).

Conversely, the *globalist* position (and by and large the transformationalist view too) insists that globalisation reflects a world order that suggests a lesser role for states and a greater role for regional blocs and global competitiveness (Muller *et al.,* 2001:244). Hence, it is the governance of global economic activities, considered beyond the control and regulation of governments, which is at issue in this instance. According to transformationalists, there is a distinct need for new forms of supra-national governance which implies either a greater responsibility for the institutions of global economic governance in regulating cross-border economic activities, or an increased role for well-coordinated regional governance to perform this function, or even a degree of both.

Concerning the **second issue**, although the *sceptics* are challenging the unprecedented nature of globalisation, it is important to bear in mind that the pre-1914 era was structurally different from the contemporary era. It was characterised by the *Pax Britannica* system in which Britain owned nearly a quarter of the world, and the Gold Standard, with its unique automatic adjustment mechanism, was the monetary regime of the time. The 19th century was a world of unilateral and discretionary policy whereas the 20th century was a world of multilateral and institutionalised policy (Legrain, 2004:113). Thus, by comparison, the *globalists* (and, in this case, the *transformationalists*) perceive the existing world order to be in need of new forms of economic governance and rule due to the unprecedented nature of globalisation.

The **third issue** concerns the question of whether globalisation promotes global inequality or not, and the implications of governance. Although there clearly is some common ground between the three schools of thought about the fact that growing interdependence is associated with a more unequal world, they interpret and respond differently to it. In the *sceptical* view, national factors are considered to be equally (if not more) important as determinants of the pattern of global inequality (Gilpin, 1987:156). However, the prospect of moderating, let alone eradicating, the growing North-South divide by means of coordinated international intervention is decidedly utopian and a categorical mistake as it could undermine the principal basis of international order (Woods, 1999:53). In this respect, hierarchy (as headed by the most powerful states), and

thereby inequality, is a vital ingredient of the sceptic understanding of world order, and the basis for effective international governance.

Globalists take issue with this understanding, arguing that, although there has been – in certain respects – an erosion of old hierarchies, the problem of global inequality can be diminished, if not resolved, by means of concerted global action. Pessimistic globalists, in particular, consider neo-liberal economic globalisation as the primary cause of growing global inequality. Alongside world markets and international capital, Hoogvelt (2001:131) argues that the uneven nature of globalisation is creating a new social division which transcends the old core-periphery organisation of the world economy. Yet, optimistic globalists contend that governing the world economy in a manner that would create a less unequal world would require exceptionally strong cooperation involving all stakeholders, including MNCs, IGOs, governments, multilateral institutions of governance, and the transnational civil society (Held & McGrew, 2000:339).

Transformationalists argue that global inequality is illustrated most noticeably by the unprecedented transformation in the patterns of marginalisation of developing economies. This is resulting in a very uneven and complex relationship between territorial boundaries and transnational forms of economic activity that increase the divide between rich and poor countries. Transformationalists are very critical of the current system of multi-layered global governance and view its lack of democratic credentials and legitimacy as serious flaws which can divide nations and exacerbate inequalities (Held, 2000:175). In their view, the most effective way to minimise global inequality is to reform the system of **global economic governance**, in particular, in a manner that would make it more accountable to contemporary principles of democratic governance.

As far as the view taken in this study is concerned, all three positions make valuable contributions towards creating a framework for understanding the changing global economic landscape and the challenges at hand. Recognising both the globalist and the sceptic positions, this study mostly agrees with the assertions in the transformationalist account. Globalisation is a reality, whether people contest it in one way or another, or not

at all. Despite qualitative changes, especially in the post-Cold War era regarding speed and space, globalisation should be regarded as a historical process that is persistently evolving. In differentiating between historic globalisation (1000AD-1920) and contemporary globalisation (1920-today), one should recognise that the former led to the latter. Concurring with Kobrin (2002:46), the current/last wave of globalisation (which started around 1980 after the second wave (1945-1980)) entails a qualitative transformation of the international world economy, which is significantly different from that prior to the First World War. While the current global economy is relatively open, it has real differences from that prevailing before 1914. Among others, some of the most significant of these differences include:

- it has more generalised and institutionalised free trade through the WTO;
- industrial production has grown more than fifty-fold over the past century, with four-fifths of this growth since 1950 (Lechner & Boli, 2000:376);
- drastic increases in the scale of technology in many industries – in its cost, risk and complexity – have rendered even the largest national markets too small;
- national markets are fused transnationally rather than linked across borders;
- the explosion of transnational strategic alliances is a manifestation of a fundamental change in the mode of organisation of international economic transactions from markets and/or hierarchies to global networks;
- foreign investment is different in its modalities and destinations;
- the emerging global economy is digitally integrated and entails the migration of markets from geographic space to *cyberspace*, and
- a shift in power from nation-states to transnational economic actors and forces.

A brief word of caution, though, about making direct comparisons between separate periods would suffice. The author agree with Hirst and Thomson (2003:28) in that by using gross figures for ratios of trade and capital flows, it might disguise important differences between the two main periods in dispute (pre-1914 and post-1973). Even in light of this, though, Hoogvelt (2001:68), for example, compared the foreign trade portion[36] of 1913

[36] The foreign trade portion is measured by the ratio of the volume of world trade (expressed as the sum total of world merchandise exports and imports at current prices) to the volume of world output (GDP). Note: this comparison excludes world trade in services because it is a more contemporary occurrence.

(33%) with that of 2000 (43%), and found that current world trade is now at an unprecedented higher intensity level. As Table 2.1 indicates, the stock of FDI relative to GDP has also increased by two-thirds since 1913 and the ratio of world exports to GDP has increased almost three-fold since 1913.

Table 2.1: World stock of FDI and exports relative to world GDP (1913-2006)

	1913	**1950**	**2000**	**2006**
FDI relative to GDP	9.0%	4.0%	19.6%	12.7%
World exports relative to GDP	8.7%	7.0%	23.3%	30.9%

Source: Michie, 2003:152 *The Handbook of Globalisation*; data from World Bank, 2008 *World Development Indicators (WDI) Online Database*

The issue of global inequality and its underlying linkages is a serious cause for concern which lies at the heart of this study. For example, it is becoming increasingly evident that there exists a democratic deficit in so far as the institutions of global economic governance are unrepresentative of the world community. Globalisation is a process amenable to influence where economic and political role-players create the structure behind its dynamic and orientation. Given that, as Table 2.1 suggests, along with trade, MNCs have been a premier agent of globalisation in the latter half of the century, global governance by corporate capital is one of the most serious concerns because it reinforces the unevenness that has characterised economic progression since the start of industrialisation. The point of this example is that global inequality has serious implications for global stability and world order. In agreement with Abrahamsson (2003:xviii), the two most urgent challenges ahead are how to make globalisation more global and global economic governance more representative. Whether globalisation can be given a human face or whether it will generate a more unruly world, are *governance issues* which will dominate the global agenda long into the 21st century.

2.6 Conclusion

This chapter highlighted the fact that there exists a strong interrelationship, especially in the present era, between *globalisation* and *global economic governance*[37]. However, in recognising this, it is essential that the conceptual meaning and interpretation of globalisation and global economic governance be clarified. This was the first objective of the chapter. What became clear is that apart from distinguishing globalisation from internationalisation and regionalisation, it, as a *process*, also needs to be differentiated from the *condition* the world economy is asserted to be in – as this is a major source of conceptual confusion. Globalisation is specifically an interpretation of the changes that are taking place in the world economy, and not a description of the state the world economy is perceived to be in, i.e. a global economy. Hence, globalisation refers to the integration of national markets in the global economy. On the other hand, global economic governance exclusively refers to rules and guidelines created and used by international institutions (most notably the IMF, World Bank and WTO) and their members for the management and guidance of the global economy. Global economic governance is both a *reaction* to and an *originator* of global transformations.

For contextual purposes, this chapter also pointed out that, as world economic history experienced volatile periods that varied from high growth and vast amounts of capital flows and trade to inflation shocks and growth and debt crises, the BWI (and later the WTO) gradually **grew in global significance**. Although the way in which economic theory developed was mainly to explain changes in economic history, it also played a central role in shaping the ideological frameworks of the IMF, World Bank and WTO. As economic thinking progressed, so did the aims as well as principles and doctrines that determine how these institutions operate, cooperate with each other and interact/engage with their members – especially developing country members and their policy-making. This was especially the case since the 1980s when neo-classical views started to dominate the decision-making of these institutions. Notably, their advocacy of market principles and increased competitiveness marked a watershed endeavour: moving from reactively performing a function of bailing countries out of financial distress to becoming

[37] Note that how these concepts are defined in section 2.2 will be how the study interprets them throughout.

more proactive in setting the tone for the way (in terms of ideological approach) in which economies should be managed and policies formulated (Varma, 2002:7). They are regarded as being mainly responsible for the global spread of neo-liberal[38] doctrines – especially in the wake of the WC and the PWC (Stiglitz, 2003b:38). This, together with other economic governance issues, and coupled with the growing impact of globalisation on the world economy, added fuel to a heated **debate**. Arguing over various issues, including the interpretation of changes in the world economy, the unprecedented nature of globalisation and its implications for global inequality, globalists and sceptics vigorously opposed each other. By rejecting the polarity of the globalists and the sceptics, transformationalists emphasise that the consequences of contemporary global interactions are complex, diverse, unpredictable and in many cases uneven. This warrants serious study and concern. They recognise that global economic governance forms part of a global system of shared governance and view it as central to ensuring the stability of the world economy. They emphasise the necessity of new and/or (changes/reforms for more) progressive international structures for democratic accountability. This study concurs with this view as it emphasises (the most) the need for a vast improvement in global economic governance arrangements.

The debate about globalisation and global economic governance is extremely **vital** since it plays a key role in determining the **direction in** which the global economy is developing. More voices/participants should be encouraged to ultimately lead to more creative solutions for the concerns being raised. The debate has already, for instance, led to a growing recognition of the developing world's – especially **Africa's** – pleas regarding *global inequality* (which is arguably aggravated by globalisation) and to more efforts by developed countries to seek answers and provide more constructive assistance. Similarly, critics of the IMF, World Bank and WTO have, although with limited success, placed pressure on these institutions to start taking reform more seriously and show a

[38] The discourse of contemporary globalisation could be understood as a primarily ideological construction which supports the neo-liberal project: depicting its progression as moving from historic globalisation to contemporary globalisation and now, neo-liberal globalisation – i.e. the latest phase of contemporary globalisation, which by and large commenced as the Cold War ended (Held & McGrew, 2000:339).

willingness to adjust to contemporary global economic governance needs, which is primarily brought about by globalisation.

While this chapter laid the theoretical, historical and contextual foundation of the study, the next chapter draws attention to the essence of the deficiencies in global economic governance by specifically focusing on the institutional failures and criticism brought against its most central institutions: the IMF, World Bank and WTO.

Chapter 3

Deficiencies in global economic governance: An institutional critique

3.1 Introduction

"Justice comes in many forms, and economic or distributive justice is now one of the world's most important issues". Through this assertion Lawson (2003:104) emphasised the vastly increased need for improved arrangements for global economic governance. But why does this perception subsist, considering that there do exist some powerful institutions of global economic governance that have a strong influence over how the global economy is shaped? This, according to critics, is exactly where the problem lies. As principal institutions of neo-liberal globalisation, critics are claiming that the IMF, World Bank and GATT/WTO (or IGEGs) have failed to deliver prosperity, free trade, and economic growth (Öniş & Şenses, 2005:274; Stiglitz, 2003a:32-33). Evidently, in contrast to what their founders had hoped and promised, the IGEGs have not been very successful in providing solutions to the world's main financial and trade problems (Mikesell, 2000:406). This caused many requests for changes in their policies and structures and in some instances, even for their abandonment.

Both in the developing and the developed world, countries are becoming more and more concerned about the palpable imperfections in the world economy, and more specifically, the fundamental flaws in the system that governs it (Davidson, 2004:591). In pointing out that there have been 100 currency crises in the past 35 years, Stiglitz (2003c:54) also emphasised that something is wrong with the global financial system as "international financial crises or near crises have become regular events". 60 years after their creation, the IGEGs face a crisis of legitimacy that seriously impairs their credibility and limits their effectiveness (Buira, 2005:7). It may seem, therefore, that the institutional framework that is required to govern and remedy the global economy is, in itself, distressingly fragile. This appears to be the *essence* of the global **governance void**. It is thus concerns such as these that warrant – with renewed immediacy – an investigation into the nature and validity of the criticism leveled against the IMF, WB and GATT/WTO. What is evident is that while globalisation has produced institutional

changes, it has not necessarily produced the most effective or legitimate ones (Mortensen, 2000:176). It must be stressed, though, that the problem is not with globalisation *per se*, but with how it has been managed. A significant part of the problem lies with the IMF, World Bank and GATT/WTO, which help set up *the rules of the game*. In this way these three institutions have played a long and decisively dominant role in shaping the basic characteristics of the global economy.

The chapter critically examines the IMF, World Bank and GATT/WTO by specifically investigating the different types of criticism these institutions have been challenged with. The aim is to evaluate the merits of these criticisms (in section 3.3), firstly against the core objectives and decision-making processes of the IMF, World Bank and WTO (section 3.2), and secondly, against how these institutions defend themselves against their critics (section 3.4). The chapter will attempt to assess whether this critique constitute (and/or contributes to) compelling rationale behind the need for serious institutional reform in the seemingly tenuous architecture of global economic governance.

Before reflecting on the key aims of each of the IGEGs it would be beneficial to pause and briefly focus on three theoretical developments that are of late being pointed out in literature. Firstly, as the IMF, World Bank and WTO adjusted their ideological framework (during the late 1990s) in accordance with the thinking of the Post-Washington Consensus, their beliefs mostly came to fall into the category of neo-liberal institutionalism as a mode of international governance (Öniş & Şenses, 2005:280). In this perception, apart from recognising the vital role of the nation-state, it is assumed that formal international regimes, rules and institutions can, legitimately, govern international affairs. Proponents of *neo-liberal institutionalism* believe that these assumptions have become strong enough to meet the challenges of an increasingly interdependent global economy. Critics, though, strongly doubt this.

Secondly, this pungently relates to what Gill (2003:130) calls "disciplinary neo-liberalism"; and defines it as "a concrete form of structural and behavioural power,

combining the structural power of capital with *capillary power* and *panopticism*[39]". In being institutionalised at the macro-level of power, disciplinary neo-liberalism is an intriguing discourse of global economic governance. According to Gill (2003:131) it is particularly reflected in the policies of the IMF and World Bank (through conditionality that mandates changes in economic policy) and the regulatory framework of the WTO.

Thirdly, it seems as if the emergence of elements of a common perspective, or a *hegemonic ideology*, is intensifying in the current global economic order (Wade, 2002:233). The resolve of neo-liberalism and the growing worldwide acceptance of (or openness towards) market fundamentalism, especially since the 1990s, which essentially involves the policy prespriptions of neo-classical economics, are, according to Hoogvelt (2001:242), progressively becoming the *nucleus* of ideological convergence[40]. The commitment shown by most governments and a majority of international institutions of governance to this ideology (or variations of it), confirms this trend (Gilpin, 2002:242). Importantly, though, these pro-free-market perceptions both underpin, and are the result of, the structural power of capital.

3.2 Objectives and decision-making processes of the IMF, World Bank and WTO

This section attempts to identify the core focus-areas of the three central institutions of global economic governance. The object is to concisely identify each institution's operational character by clarifying what these institutions commit themselves to and how they make their governing decisions. Each institution is considered separately. Notably, this section also complements that which was discussed in chapter two regarding how the IMF, World Bank and GATT/WTO evolved over history. The reason for explicitly focusing on each institution's aims and decision-making is to be able to draw comparisons between what the institutions set themselves out to do, and what they actually have achieved (or what they are, at least, attempting to achieve). Significantly, this is the area of concern from which most of the criticism stems from.

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[39] Panopticism derives from the Greek word *panopticon*, which means *sees all* and relates to surveillance. It can be defined as a dystopia latent in modernity: the possibility of developing a system of control which reduces the individual to a manipulable and relatively inert commodity (Gill, 1995:37).

[40] It must be stressed that this is, particularly in light of the present global financial crisis, something over which most scholars and policy-makers are currently having a re-think – a case this study is also making.

3.2.1 The International Monetary Fund (IMF)

Being considered as the institutional nerve center of the monetary order, the mandate given to the IMF by its member countries includes the promotion of international cooperation on monetary and financial affairs through collaboration and consultation; and assuring members of temporary access to its general resources if need be (Kelkar *et al.*, 2005:48). In being primarily responsible for macroeconomic assessments, the IMF is the only international organisation whose mandate requires it to get involved in active dialogue with practically all countries (IMF, 2004:3). It has become the principal forum for discussing both, the global context of national economic policies, and, issues that are vital to ensuring the stability of the international monetary and financial system. The official responsibilities of the IMF are determined by its Articles of Agreement. As its most important constitutional instrument (since 1944), it states that the IMF's primary objectives are (Irwin *et al.*, 2004:181; O'Brien *et al.*, 2003:161):

- promoting foreign exchange stability;
- creating a multilateral system of payments between members;
- promoting international monetary cooperation;
- reducing the duration and severity of disequilibria in members' balance of payments, and to enhance current account convertibility;
- facilitating the expansion and balanced growth of international trade, and
- to assist in the correction of maladjustments in members' balance of payments;

Compliant with an amended Article IV, Section 3 of its statutes, the IMF was principally tasked to oversee the international monetary system. Its main focus of activities has, particularly since the 1990s, shifted from exchange rate surveillance to the stability and integrity of the international financial system (Smaghi, 2004:247). In attempting to better achieve its economic reform objectives, the IMF started to intervene more intensely in many countries. Apart from the structural adjustment programmes (SAPs), conditionality was further expanded when the IMF (together with the WB) insisted on stipulations on domestic governance and the institutional framework of economic policy-making (Woods & Narlikar, 2001:569). Accordingly, the IMF initiated major training and technical assistance activities to provide staff and tools to countries that struggle with the

policy reform challenges of an era of intense globalisation. Furthermore, the governance structure and decision-making processes of the IMF is the result of the agreements embodied in the quota regime[41], with the size of quotas determined by each country's relative economic weight in the world economy. Although each member receives a basic number of votes, a country's relative voting power in the IMF is decided by the size of its quota (Kelkar *et al.*, 2005:55). In effect, the IMF's quota regime functions as the basis for determining the required size of each member's capital contribution, the extent of access that each member country has to the IMF's resources, and the distribution of voting rights within the institution. The body that governs the IMF is the Board of Governors, which controls, but does not manage, it – a function performed, rather, by the Executive Board. Decision-making at the IMF is based on a rule that is not one country, one vote, but roughly 100,000 SDRs (Special Drawing Rights) to one vote. On this basis, the IMF is officially controlled, in terms of decision-making, by its wealthiest member states by means of weighted voting. Probably the most significant way for developing countries to have some meaningful influence in the IMF, is through the constituency system (Portugal, 2005:93). Accordingly, a group of countries – a constituency – join to elect an Executive Director, which then represents these country's interests through casting the constituency's votes as a unit in Executive Board decisions.

3.2.2 The World Bank (WB)

Although it was established to fill the financing disparities left by private capital markets, the World Bank is, at present, primarily responsible for structural and poverty assessments in member countries (Bird & Joyce, 2001:75). The very core of the World Bank's mission is to reduce global poverty and increase economic growth. It is therefore the World Bank's task to finance growth-enabling investment in poor countries. Roads, bridges, wells, communication systems, and health systems are all projects that are funded by the World Bank as part of its quest to reduce worldwide poverty (Guell, 2006:160). In addition, the World Bank is also concerned with debt relief, the transfer of financial resources and general economic development – particularly in the developing countries.

[41] See Appendix 3A for a detailed explication of how IMF quota formulas are used for calculations.

Due to the economic crises experienced by a number of countries during the 1980s, World Bank loans started to move beyond the financing of specific development projects and directed much of its efforts toward the contentious activity of policy-based lending – attaching conditions on loan disbursement. In being quite similar to the IMF's economic austerity conditions, this gave the World Bank influence over how loans were spent and, consequently, a prime position in ordaining the conditions of development policy discourses (O'Brien *et al.*, 2003:11). Today, through the International Bank of Reconstruction and Development (IBRD) and the International Development Authority (IDA), the WB officially offers investment loans and development policy loans. Whereas the former is meant for economic and social development projects, the latter provide fast disbursing financing to support countries' policy and institutional reforms (World Bank, 2006b:1-2). Both types of loans involve conditions and requirements for domestic economic restructuring. Its track record shows that the World Bank's main intervention has been long-term loans and technical assistance which is intended to enhance the financial sectors of various developing countries (Scholte, 2002:196). During the past decade and more the World Bank's policies and programmes have chiefly been aimed toward sector restructuring, privatisation and legal reform.

The World Bank's decision-making procedures are officially determined by *Article V, Section 3(b)*, which decrees that all matters will be decided by a majority of the votes cast by its 182 members. This is based on the 250 votes held by each member plus an additional vote for each share of stock held. Formal power at the World Bank rests in the hands of its member states, which are represented on the Board of Governors, who are the ultimate policy makers at the World Bank. This body delegates decision-making to the WB's Executive Board (EB): a 24-member body that decides on project proposals and reviews the World Bank's policies (Jacobeit, 2005:224). The president of the World Bank chairs both the Board of Governors and the Executive Board on which he has the casting vote in case of a tie. As the five largest shareholders of the WB, the US, United Kingdom, France, Germany and Japan each appoint an Executive Director and the rest are elected by the other member governments every two years. The reason why the developed countries hold a clear majority within the World Bank is because the amount of

stock depends on a member's relative economic and financial strength. Thus, as with the IMF, the WB is also controlled by its wealthiest member states through weighted voting.

3.2.3 The World Trade Organisation (WTO)

After the conclusion of the Uruguay Round (1986-1994) and with the signing of the Marrakesh Agreement, the WTO, in 1995, took its position in an environment of multilateral trade rules that dates back to the late-1940s. During these almost 50 years GATT made gradual progression towards achieving its aim of reducing trade barriers, i.e. liberalising trade flows between countries (Helleiner, 2001:251). It played a crucial role in building a new agenda that expanded the scope and changing nature of negotiations form merely focusing on bargaining over products to higher-level negotiations over policy harmonisation. However, as became evident through GATT's dispute settlement process, it mostly had to make a compromise between the desire to provide clear rules for trade arrangements and allowing for domestic autonomy.

Contrary to how the GATT Council took their decisions, the WTO upturned the unanimity principle as part of a modified dispute settlement procedure (Picciotto, 2003: 377). Achieving one of the WTO's key aims, this strengthened the rules-based nature of the trading system and gave eminence to the WTO as an international institution in terms of having a full-fledged enforcement mechanism. Hence, the WTO became a central institutional framework for the international cooperation of economic regulation, complementing the IMF's role in monetary management and that of the WB in development finance (Hockett, 2005:105). In effect, this realised the organisational *triptych* that was envisioned at Bretton Woods and now forms the basis on which these institutions aims to build greater coherence in global economic policy-making.

As a member-driven network organisation, the WTO extends the mandate of GATT by transforming the institutional basis of the world trading system: from shallow integration (trade liberalisation based on tariff concessions) to deep integration (dialogue over institutional practices, regulations and domestic policies) (Woods & Narlikar, 2001:569). The WTO's responsibilities significantly exceed those of GATT as it is geared towards

expanding the world trade order and also, as Stoll and Schorkopf (2006:27) stresses, "the establishment of a legal order for world economic relations". Accounting for more than 97% of world trade, the WTO's overriding objective is to help trade flow smoothly, freely, fairly and predictably (WTO, 2006:4). Furthermore, according to the Agreement establishing the WTO, the goals it desires to achieve include: raising standards of living, ensuring full employment, increasing real income, poverty alleviation, and expanding the production of and trade in goods and services in order to ensure an optimal use of the world's resources (Rodrik, 2005:126). Contributory to these objectives, the WTO believes what is required is more intensive trade liberalisation and the elemination of discriminatory treatment in international trade relations, which includes open non-discriminatory competition. Expanding trade is seen as a means to creating sustainable development, rather than an end in itself. Hence, Moore (2000:26) from the WTO emphasised that "the surest way to do more to help the poor is to continue to open markets". According to Wolf (2004:75, 73) the WTO "helps to provide the international public good of open markets" and "exists to facilitate, embody, and arbitrate over trade and trade-related agreements among its sovereign members".

With its distinctive legalistic nature, the WTO, at its founding, created a new set of binding commitments on members that reach into several areas of domestic legislation (Mortensen, 2000:178). Aiming to redefine the relationship between nation-states and the world trading system, this set is accompanied by efforts from the WTO which is based on three core strategies: its Dispute Settlement Body (DSB), the provision of a trade policy review mechanism (TPRM) and the development of a suite of mandatory codes. As a legal entity, the WTO governs the multilateral trading system by way of a framework of norms, rules and principles. Through rule-making, it aims at increasing and enhancing global policy-making within the context of the global trade regime. In also being a rule-supervisory institution, the WTO keeps a watchful eye over the implementation of agreements and dispute resolution (O'Brien *et al.*, 2003:136-137). Then, as a forum for discussion of trade policy-issues, the WTO aims to increase direct ministerial involvement and to make trade concerns an even higher priority to overall government policy-making. It also functions as a centre for the settlement of trade disputes where the

General Council acts as both the DSB and the trade policy review body (WTO, 2006:1). All these, however, are subject to the institution's highest decision-making body, the Ministerial Conference, which consist of member states and meets biannually. Notably, the WTO adopts the principle of one member, one vote and just about all its decisions are taken by consensus among all member countries and are ratified by members' parliaments.

3.3 Criticism against the governance of the IMF, World Bank and WTO

Particularly since the late 1980s, the World Bank, IMF and GATT/WTO (the IGEGs) found themselves accused of being unjust, unaccountable, ineffective and secretive. Resulting in an apparent crisis of legitimacy, the policies and functioning of these institutions were increasingly brought into question by the majority of their shareholders/members and other critics, demanding that they make remedial reforms. Although, admittedly, some reforms have been made, critics do not consider them to be adequately substantial (Woods, 2005:148). While a vast array of criticism[42] against the IGEGs exists, this section will, by and large, consider some of the most prominent ones. Notably, there is strong interplay between the different types of criticism. The section mostly involves all three institutions concurrently and is organised around criticism that affect their sovereignty and legitimacy as well as strategies and policies.

3.3.1 Questionable sovereignty

The criticism that is brought to the fore in this section questions the nature of the IGEGs' power and rule. From the outset, their thinking processes and principles are scrutinised as that gives insight into their underlying philosophies. The focus then moves on to these institutions' unwillingness to take sufficient accountability and also their susceptibility to external influence. Lastly, the IGEGs' proneness to move away from (or beyond) their original goals are leading critics to question their sovereignty.

[42] Although the study does not exclusively focus on the following criticisms due to a lack of space and scope, critics (see Stiglitz, 2003a; Varma, 2002; Held, 2004) also consider them very significant sources of poor global economic governance: the IGEGs moving away from their original intentions; their impervious attitude; lack of institutional coordination; insufficient adaptability; absence of law-binding agreements; unnecessary institutional complexities; misuse of the WTO's dispute settlement system; participation uncertainty (experienced by developing countries); the IGEGs made promises they cannot keep (unrealistic management); diminishing ability to solve global problems; and lack of adequate resources.

3.3.1.1 Ideological stance in dispute

Given that choices of rules and institutional mechanisms can be considered as projections of power, critics assert that decision-makers such as the **IMF**, **WTO** and **World Bank** build institutional strongholds to ensure future gains from globalisation, at the expense of those who suffer from globalisation's uneven nature (Mortensen, 2000:187). Capital market liberalisation opens up new markets for the financial industry, even though it contributes to global economic instability. Hence, according to Stiglitz (2003c:121), there is a confluence here of ideology and interests as both serves to override economic analysis. Decisions are based, Stiglitz (2003a:216) assert, on "a curious blend of ideology and bad economics, dogma that sometimes seemed to be thinly veiling special interests". Despite the existence of contradictory evidence and theory, the IGEGs still stongly hold on to their neo-liberal beliefs – especially in light of continued reassurance of these convictions from those in financial markets (whose interests might, of course, be well served by capital market liberalisation).

Critics make a justifiable charge that the IGEGs, which may be held responsible for much damage under Washington Consensus (WC) reforms, are again put in the driving seat in a process set up to rectify it: the Post-Washington Consensus (PWC) (Öniş & Şenses, 2005:280-285). Also based on neo-liberal principles, critics argue that there do exist some striking limitations to the PWC. Firstly, through the PWC, the IGEGs have a new policy agenda, which, quite disappointingly, has a systematic bias towards domestic reforms as opposed to systemic or global reforms – including the three institutions themselves. Secondly, the IGEGs seem to recede from carrying out a balanced analysis of the globalisation process, especially regarding their approach towards the identification of the real causes behind developing country marginalisation as well as, for instance, financial vulnerabilities (e.g. the 2008 US sub-prime crisis) observable in developed economies. This is worsening the so-called, *credibility gap*, which exists between these institutions and particularly the development community at large (Picciotto, 2003:397). Hence, the fear that most critics have is that the IGEGs are being steered by a blinkered neo-liberalism (just packaged differently under the PWC) towards an eventual *cul-de-sac*.

In terms of their current neo-liberal ideological stance, the implications of increased **IMF-WB-WTO** *coherence*, according to critics, are posing a variety of problems. The main concerns in this regard are (Kahler, 2004:132-133; Varma, 2002:11):

- the proliferation of a tunnel vision and flawed model of development, based, mainly, on trade liberalisation as the vehicle to poverty reduction and growth;
- the *locking in* of liberalisation commitments through the WTO's dispute settlement mechanism;
- the permanent loss of the national sovereignty to pursue any chosen path of development based on national interests and needs, and
- it help create a policy-framework that favour creditors in industrial countries.

3.3.1.2 Inadequate accountability

Critics maintain that the supposed chains of accountability inherent in the governance structures of, in fact, all the IGEGs are, in practice, a long and imperfect one. This has resulted in an attenuation of accountability (Nye, 2001:3). Critics argue that although the IGEGs may be agents of states, they often represent only certain parts of those states. That is why critics of both the left and the right often portray the IGEGs as rogue agencies, pursuing their own ideological or bureaucratic goals rather than the legitimate ends of their member societies. Öniş and Şenses (2005:288) take the argument further by pointing out that "issues concerning how to make the IMF, the WB and the WTO more transparent and hence, democratically accountable in their operations, as well as problems arising from their power structure as dominated by developed country interests, receives only cursory attention by the intellectual proponents of the PWC as well as these institutions themselves". Critics assert that the **IMF's** evolution and its failures – especially in terms of its original objectives – are best understood when looking at its system of accountability. For instance, according to Stiglitz (2003c:119), one of the IMF's core missions in recent years has been to make central banks more independent, which means that they are less directly accountable to democratic processes. This, then, leads Stiglitz to conclude that "the IMF is becoming more accountable to people who are increasingly less accountable themselves … [and] has consistently discouraged public discussion of alternative strategies, … arguing that transparency could undermine its

effectiveness" – a view it apparently shares with member countries' central bankers. Even after the East Asian crisis calmed down, for example, the IMF refused to engage in processes of public evaluation. The IMF also tends to be a less heterogeneous organisation and is less open to self-criticism compared to the World Bank, critics argue (Öniş & Şenses, 2005:275). In the very limited cases where the IMF affianced in self-criticism, it tried harder to limit the extent of outside criticism than to actually understand the sources of its failures. The concern for critics is that this lack of accountability is getting worse.

While the roles of the IMF and the **World Bank** have expanded, their accountability has not. Their ever widening domain of advice and conditionality, for instance, has extended the purview of these institutions within member countries and directly affects a wider range of organisations, policies, people and groups – all to whom they ought to be accountable. Yet, what has been happening, critics argue, is that the IMF and the WB has continued to intrude into domestic decision-making, and, through the line of accountability they establish with the Central Bank or Finance Ministry, they increasingly override other agencies and local or democratic accountability (Schedler *et al.*, 1999:313). In underlining the accountability problem, this leads critics to ask: who makes specific policy decisions, by whose rules and under whose scrutiny?

In terms of the **WTO**, critics argue there is definitely significant room for improvement regarding accountability. They contend that even if all member states were represented in all decisive meetings, the problem of accountability towards the world's citizens – the ultimate stakeholders of governance – would still remain (Nanz & Steffek, 2004:326). Critics therefore argue that due to its secretive style of policy-making, the WTO inhibits informed public debate and critical reflection.

3.3.1.3 Lack of institutional autonomy

International institutions are shaped in the image of the powerful states. For this reason, critics claim that the World Bank, IMF and WTO are not value-free or apolitical. The context, for instance, in which globalisation are steered and governed, is offered by the United States in the sense that it is creating a world in the fashion of a real imperial

capital, which includes the institutions, laws and common values that globalisation (or Americanisation, some critics argue) makes necessary (Mortensen, 2000:187; Helleiner, 2001:33). The argument goes further in that corporate influence over US and other major powers' political decision-making can obviously carry profound spillover effects for rule-making in the global economy.

Trade liberalisation, for instance, is pushed forward by the demands for market access made by corporate exporters to their respective governments. In serving these interests, privatisation is essentially identical to what is called *policy capture*, where government policy instruments – as swayed by the IGEGs – are used for private objectives. In effect, the present institution-building process of global economic governance confers privileged rights of citizenship and representation to corporate capital, whilst constraining the democratisation process (Halabi, 2004:27). Hence, critical scholars accuse the IGEGs of deepening economic integration and promoting trade openness in order to serve the interests of the transnational business elite. What is concerning, though, is that misuse, in this respect, appears to be more pronounced in the **WTO** than in the GATT. The WTO's lack of institutional autonomy is an acute, but much overlooked, problem in its policy surveillance. One method of surveillance is through the TPRM. Being just advisory in nature, TPRM reports should not be the basis that gives the WTO the right to the initiation of cases, as it produces mistrust amongst members. Critics argue that this is exactly what occasionally happens due to the WTO being largely controlled by the most resourceful governments.

It is no secret that the **IMF's** decision-making process is determinedly influenced by the G7 countries as it is they that mainly drive its policy agenda – even if they have to act as a voting bloc, which happens quite often, according to critics. Although the G7 countries are still short of a voting majority, chances are small that the IMF would approve an issue if they are strongly opposed to it. That is why Portugal (2005:93) asserts that the G7 seemingly "act as a self-appointed steering committee of the IMF".

Critics are also concerned about the **WB's** lack of institutional autonomy. For example, the call for an advisory group to shortlist potential candidates for the new president of the WB in April 2001 raised eyebrows as the selection procedure that was followed excluded a great majority of members (Buira, 2005:32). This attracted many criticism concerning the legitimacy and independence of the governance of the WB.

3.3.1.4 Moving away from original intentions

The **IMF's** largest shareholders have tended to use it for goals that go beyond the purposes for which it was originally designed. While these goals might be seen as admirable international aims in the sense that they provide vital global public goods, such practice, according to Portugal (2005:77) "undermines legitimacy and accountability, while at the same time reducing the IMF's efficiency in its core areas". The **WB** and the IMF were neither created nor structured to undertake, or to be accountable for such a wide variety of activities as is currently the case. They were created to deal with a limited, clearly predetermined range of technical issues. It was intended that they should only deal with member countries via their Treasuries, Finance Ministries, Central Banks or similar agencies (Woods, 2005:156). While this is still the case, critics take issue with the fact that the WB and the IMF, through conditionality and loan agreements, are holding Central Banks and Finance Ministries officially accountable for policies that strictly lie outside their sphere of responsibility – such as health issues, for example.

3.3.2 Dubious legitimacy

Critics often doubt the legitimacy of the IGEGs, particularly due to the severe unfairness of their voting and quota systems (Stiglitz, 2003a:96). Together with other forms of democratic deficits and these insitutions' lack of effectiveness, critics feel duty-bound to critisise the validity of much of the IGEGs' authority and how they, unjustly, exercise it.

3.3.2.1 Deficiencies in the voting systems and quota restrictions

The number of basic votes (250) in the **IMF** has since 1944 never changed with successive quota increases. Consequently, the proportion of basic votes to the total has now declined to only 2.1% of the voting power (Buira, 2005:9). As indicated by Table

3.1, this caused the balance of power to shift very significantly, benefiting countries with large quotas, and detrimentally affecting small countries whose participation in decision-making was supposed to be protected by the IMF's Articles – as orginally intended.

Table 3.1: GDP, quotas and votes in the IMF as percentage of total votes

Group of countries	GDP (PPP) 2003 (% shares)	GDP 2003 (% shares)	Quotas 2003 (% shares)	Total votes (% shares)
G7 Countries	44.1	64.4	46.1	45.3
Other Industrial Countries	8.3	11.9	15.6	15.5
Total Industrial Countries	**52.4**	**76.3**	**61.7**	**60.8**
Africa	**3.4**	**1.5**	**5.4**	**5.7**
Asia	26.5	10.0	10.3	10.5
Middle East	3.7	2.6	7.6	7.7
Latin America and the Caribbean	7.6	4.8	7.5	7.7
Transition Economies	6.3	4.8	7.5	7.7
Total Developing and Transition Countries	**47.6**	**23.7**	**38.3**	**39.2**
Total	**100.0**	**100.0**	**100.0**	**100.0**

Source: Buira, 2005:10 *Reforming the Governance of the IMF and the World Bank*

Note: These quota calculations are based on Appendix 3A. These are not open source information to make it possible to update the percentage values presented in this table.

From Table 3.1 above it is clear that industrial countries has almost two-thirds of the votes and quotas, compared to that of the developing and transition countries combined. Notably, **Africa** has the lowest share with only 5.4% of the quotas and 5.7% of the votes. Critics furthermore argue that there exist clear biases regarding the calculation of quotas. For example, economic output is currently measured as GDP at market exchange rates and does not reflect the currency's true purchasing power at home (Kelkar *et al.*, 2005:57). The problem is that the non-tradable sector is being undervalued and also, the prices of tradable goods are not being equalised across countries due to the lagged effect of the exchange rate. As a result, GDP can be under- or overvalued when making cross-

country comparisons of incomes. Given that creditor countries command disproportionate voting power within the IMF's current quota regime; this *is leading to skewed crisis analysis* and resource distribution. Together with the reduction of basic votes in the IMF's quota regime, which has downgraded the say of smaller countries, critics argue that these are among the main reasons why the governance of the IMF suffers from a democratic deficit. An example of this is the substantial disparity that currently exists between the voting power and economic strength of smaller European countries (such as Belgium, Italy and Netherlands) and major emerging market economies (such as Brazil, China and India). Supporting this view, Wade (2005:ii) argues that "you know something is seriously amiss in global economic governance when Belgium, Sweden and Switzerland, with 0.004% of world population and 12% of world GDP, have the same share of IMF and WB votes as China and India, with 38% of world population and 19% of world GDP; and when the former do not even borrow from the organisations". Moreover, in being the basis for power relations between member countries, the IMF's quota regime, one could argue, indirectly prohibits countries to submit issues that are likely to be vetoed by the US, as decisions made by the Executive Board are mostly on the basis of consensus voting (Kelkar *et al.*, 2005:56). Importantly, this indicates how the skew distribution of voting power affects the nature and scope of matters on the IMF's agenda and their effectiveness in providing a more stable global financial environment. Critics argue that, especially with the US retaining veto power with 17.38% of the total votes (85% is required for a super majority), the IMF's quota regime has, inaptly, become a matter of political judgment and compromise.

The quota formulas of the IMF provide three basic functions in that it determines the degree of voting power, members' required contributions, and access to the IMF's resources. Notably, a member country's quota is the only policy instrument that is used for these three policy objectives. According to Buira (2005:11) "the logic of having only one formula for determining these different roles has often been questioned". Many critics therefore insist that the fundamental flaw of the IMF's current quota regime is the mismatch between objectives and instrument. Today the original formula is used in conjunction with four other variants of it. Critics argue that the formulas contain too

many variables of which some of them are not directly related to the functions of quotas and cause unwarranted distortions (Portugal, 2005: 85). A concern, though, is the lack of transparency in the determination of quotas due to a disturbing degree of discretion used in the selection of the formula to be applied and in adjustments to the results when guesstimating members' quotas. This, combined with the apparent *inertia* inherent in the IMF's quota structure, is indeed worsening its unrepresentative nature. In fact, it has been argued that the quota formulas discriminate against developing countries that have experienced a fall in aggregate calculated quotas. These are some of the reasons why developing countries have long been complaining about the quota formulas' bias. Critics assert that there exist a significant discrepancy between how quotas are formally calculated and how they are actually calculated by the IMF, where, in effect, the average actual quota is less than half of the average calculated quota (Kelkar *et al.*, 2005:60). Also, quota-increases in the form of *equiproportional* and selective quota adjustments, in practice, tend to be small. The Board of Governors – in which the developing countries has limited say – takes the final decisions on these matters.

Furthermore, one of the main factors causing a crisis of legitimacy is the unrepresentitive nature of the governance structure of the IMF and WB. Voting shares in the IMF, for instance, are in proportion to an outdated and imperfectly measured economic weight of a country. In using a system of *one-dollar-one-vote* rather than *one-man-one-vote*, the IMF purportedly is a commercial enterprise with shareholders (Stiglitz, 2003c:120). Only a small group of developed countries controls the institutions, and almost demeaningly regard the rest as minor partners. Since votes on their boards of directors are weighted by financial contributions, there exist a lack of representative democracy in the IMF and **WB** which are analogous to what Griffin (2003:802) calls, a "plutocracy". Considering that the developing world account for most of the world's population, half of global output in real terms (purchasing power parity), comprising of the most vibrant economies and the largest holders of international reserves, the limited recognition given to these countries is deplorable (Buira, 2005:7). What is fuming critics is that while these countries are playing an increasingly important role in the global economy, their influence in the IMF and the WB has not increased correspondingly (Helleiner, 2001:36). As a matter of fact,

in combination with the transition economies, their aggregate voting power has only fluctuated between 37% and 40%. In an empirical study done by Le Fort V (2005:116-125), cross-section regression analysis were used to determine the extent of representation distortions in the IMF's quota structure. The results indicate that economic growth, credit rating, population and dummies for the US and China all have negative signs and reflects under-representation. With faster growing countries continually not being recognised in the IMF's voting structure and with more populous countries appearing to be discriminated against, the study finds that the distortions will continue to increase.

Table 3.2: Governance structures and voting procedures of the IGEGs

Organisation	Representation	Voting	Majority	Veto right	Opt out right	Session right
WTO (statutes)	One state, one seat	One state, one vote	50% + 1 – 100%	No	No	Yes
WTO (reality)	One state, one seat	Trade weight, Consensus		Yes	No	Yes
IMF/WB loans (statutes)	Constituencies	One $, one vote	50% + 1 – 85%	No	Yes	Yes
IMF/WB loans (reality)	Constituencies	One $, one vote, consensus		Yes	No	Yes
IMF/WB codes and standards'	Constituencies	One $, one vote	50% + 1	No	Yes	Yes

Source: Varma, 2002:26 *Improving Global Economic Governance*

Note 1: 50% + 1 if not otherwise specified, two-thirds to amend treaties, three-quarters to authorise temporary opting out of existing treaties or permanent opting out of amendments, and 100% (consensus) to adopt new treaties.

Note 2: Opt out possible with approval of three-quarter majority of members.

According to its statutes, representation in the WTO is largely based on the *one-country-one-vote* rule. However, in reality, decisions are made through consensus and based on weighted voting power (in this case trade weight). That is why, although the WTO is governed by consensus, it awards the largest share of influence to the major trading powers (Kahler, 2004:136). As indicated by Table 3.2 above, this is also the situation with the IMF and World Bank: they have provisions for voting, but due to a mindset of

recognising the flaws of the voting system, consensus has in reality been propelled to override due process for the sake of avoiding a vote. This clearly demonstrate the marked *difference* between what the IGEGs declare in their statutes and what voting procedures they in most cases actually follow. Ironically, in all three institutions, voting power ultimately tends to underpin any process of consensus-based decision-making. Some critics even argue that consensus is just a public relations tactic for the domination of certain countries within these institutions (Varma, 2002:18). One problem with this form of decision-making is that it is subtly passive. In the WTO, for instance, *silence is taken to imply consent*, which presents an odd way to make decisions about issues with serious consequences for countries. Consequently, it fails to take into account the realities experienced by a significant number of developing country members.

3.3.2.2 Democratic deficit and unfairness

Global economic governance is argued to suffer an enormous *democratic deficit*. According to a report by the United Nations Development Program (UNDP), the economic and political frustration experienced by developing countries regarding the skewed distribution of global power has (even then) seldom been greater (UNDP, 2002:101). As the largest creditor of the IMF, the US has always favoured conditionality. Although, initially, European countries were against conditionality, they later changed their position as their situation changed. As partly being a reflection of the character of the **IMF**, this resulted in a growing distinction between countries that determine its policies, and countries that are subject to it. Over time conditionality increased and IMF resources declined – worsening the growing divide (Griffin, 2003:790). Moreover, making matters worse and making uniformity and transparency quite ridicule, countries that are strategically and systemically important to the IMF have access to its resources well beyond the limits established by the access policy.

According to Nanz and Steffek (2004:324), "there is wide consensus that the WTO is not among the most open or transparent international organisations, and that its democratic legitimacy is questionable". **WTO** rules, for instance, are specifically designed to serve global corporate expansion and the harmonisation process. By specifying the conditions

under which nation-states can protect or promote domestic firms, the WTO is delimiting the scope of government and redefining the role of the state in the domestic economy. That is why, in the eyes of critics, the WTO is seen as an institution that remains a projection of the asymmetrical distribution of resources and power in the global economy. As the central issue in the WTO's crisis of legitimacy, it seems to operate beyond the realm of democratic debate. Critics are particularly displeased about the WTO's unfair treatment of governments when compared to how it neglects to set rules for global competition (Picciotto, 2003:391). Currently, issues related to regulated competition and oligopolistic competition remains outside the scope of WTO governance – which should not be the case, critics argue.

Critics assert that liberalisation that has taken place under the WTO in particular, has been on an asymmetrical basis. This is continuing to occur in areas of interest to developed countries (often to the detriment of developing nations), such as services and intellectual property rights – all of which are hard-pressed by US and EU multi-national interests. Conversely, in areas of interest to developing countries such as textiles, agri-culture, movement of labour, the WTO allows barriers to remain in developed countries. Critics describe global trade negotiations within the framework of the WTO, in reality, as anything but consensus-driven, trust-based or balanced, in exchange of bargaining concessions (Mortensen, 2000:193). Negotiations, they assert, are about shifting the costs of trade liberalisation, and hence, the redistribution of the potential benefits and losses of globalisation – to the detriment of smaller role players, i.e. developing countries in particular. This underlines the regime imperfections of the WTO and the fundamental flaws in its bargaining system. Notably, the WTO's *legitimacy deficit* stems from the problematic nature of its procedures as it retains important characteristics of the *club model* of international cooperation that typified its predecessor, the GATT (Keohane & Nye, 2001:271). The club design aims at crafting *coalitions of the willing and able* among the powerful players. In addition, the infamous *green room* consultations at the Ministerial Conferences have become a synonym for secretive and obscure ways of international decision-making[43]. By preventing even ex-post reconstruction of the

[43] Green room consultations, which started in 2002, normally involve 10 to 25 out of the 147 members.

political debate, no records are kept of these meetings. Ultimately, according to Nanz and Steffek (2004:326), "the club system tends to privilege the concerns and interests of the key trading nations at the expense of marginalised stakeholders". The WTO is notorious for its lack of democratic legitimacy. Not just critical NGOs, but also in academic circles, the WTO has been identified with "the technocratisation and bureaucratisation of trade policy" (Bellmann & Gerster, 1996:45). It has, in fact, become a hated symbol of globalisation as it continues to impose unwarranted limitations on the legitimate exercise of sovereign discretion, particularly on developing countries (Wolf, 2004:75).

According to Held (2004:369, 371), due to power imbalances, **all three the IGEGs** are rarely fully representative of the states involved in them, which leads to a breakdown of symmetry and congruence between decision-takers and decision-makers. Kaul (2003:27) speaks about the *forgotten equivalence principle*. This principle suggests that those who are significantly affected by a global good or bad should have a say in its provision. Yet almost the opposite is happening as there is a breakdown of *equivalence* between decision-takers and decision-makers, between stakeholders and decision-makers, and between the outputs and inputs of the decision-making process.

3.3.2.3 Diminished effectiveness

Both the IMF and the WB have lost some of their effectiveness. Critics maintain that the IMF's surveillance is only effective over countries that resort to its financial support, i.e. developing and emerging economies, but has little if any impact on industrial countries and on systemic issues because the latter group is not much in need of the IMF's financial assistance. **IMF** resources – as a proportion of world trade – were allowed to fall from 58% in 1944 to below 4% at present, mainly due to developed countries that no longer resort to the use of IMF resources (Buira, 2005:25). Without sufficient resources, the IMF cannot perform its proper function. The support and direction it provides to countries during uncertain times is questionable, especially when the IMF act pro-cyclically in pursued of, what Stiglitz calls, "beggar thyself policies". Equally questionable, is its effectiveness in providing incentives to timely adjustment. Hence, the IMF's effectiveness in the management of systemic issues is a serious cause for concern and is considered by

most member countries to be weakening its legitimacy. Due to a series of financial crises (especially during the 1990s) that threatened to obliterate the economies of several emerging markets in Asia, Africa and South America, the IMF's ability to carry out its mandate has been ever since called into question. Accordingly, Stiglitz (2003c:54) indicates that "this much is clear: the IMF whose responsibility it is to ensure the stability of the global financial system, has failed miserably in its mission to stabilise international financial flows, arguably making matters worse". Critics such as Kelkar *et al.* (2005:48) therefore warn that the IMF "will lose relevance if it continues to ineffectively meet the needs of all its constituents". Apart from not being able to meet the needs of several emerging economies, the IMF also struggles with those of the G8 (G7 plus Russia). In fact, the very reason why the G7 came into existence in 1973 was due to frustration with IMF proceedings – even then. Also, one of the key reasons why the IMF battle to achieve international monetary cooperation is mainly because of the widely shared perception that its decisions fall in line with those taken at annual G8 (previously G7) meetings.

As far as the **World Bank** is concerned, its lending operations experienced a drastic decline during especially the past eight years and resulted in a sharp increase in net negative transfers. In effect, this dramatically limits the provision of capital and, its significant other, the transmission of knowledge (Stiglitz, 2003c:124). Also diminishing the World Bank's effectiveness, the increase in conditionality along with burdensome administrative procedures leading to delays of disbursements, are ever increasing the non-financial costs of loans. Furthermore, given that the distribution of WB capital shares are largely aligned with IMF quota shares, critics argue that the continued under-representation of developing nations is eroding the WB's effectiveness and legitimacy. As a result, several critics ask whether the WB is still needed (Zahrnt, 2005:690). Many of them see the world divided up into two groups, middle-income countries and lower-income countries, and insist that middle-income countries do not need the World Bank. Accordingly, both the lending and non-lending services of the WB should be provided privately and low-income countries (LICs) need grants, not loans. Critics argue that due to the **WTO** not being properly equipped to deal with the more complex problems of

governing globalisation, it is not effective enough (Mortensen, 2000:177, 186). More specifically, they assert that three problems concerning its effectiveness exist:

- the WTO is a weak enforcer of its rules which allows opportunism to flourish;
- it is a weak monitor, resulting in states not trusting each other and are thus hesitant to enter into new agreements, and
- it is a weak legitimiser which increases the risk of *system break-up* over the long term if the political acceptance that supports its purpose, disintegrates.

With a budget of only about 5% of the combined budget for the three IGEGs, the WTO secretariat is remarkably underfunded and understaffed in the light of its new responsibilities. Thus, as a constitutional system, many critics argue that the WTO is imperfect, chiefly for this reason (Blackhurst, 1998:176). The resource deficiencies put severe limitations on the role of the WTO in global economic governance, and, was it not for it's member-driven network, it might not have gained such a prominent position in the governance process. In fact, the lack of organisational resources within the WTO dispute settlement system (DSS) has presently become a major problem for the WTO. Furthermore, critics emphasise that the conventional wisdom that the WTO is very *effective* in resolving disputes should be questioned. In a study done by Iida (2004:211-214), the effectiveness of the WTO DSS have been examined in five areas: assuring a level playing field, actually solving disputes, balancing legislative and judicial functions, fending off unilateralism, and reconciling trade and nontrade concerns. It was found that in all of these accounts, the effectiveness of the DSS are either very limited or almost non-existent. Wolf (2004:76) concurred that "in practice, dispute-settlement remedies are of little use to small countries, unless the big players voluntarily submit".

Critics regard the lack of interagency cooperation among the IGEGs as a serious concern. Greater coherence amongst agencies that receive billions of taxpayers' dollars is desperately needed as its absence damages their collective credibility and effectiveness, which frustrates their donors and owners and gives rise to public cynicism (Moore, 2003:220). In addition, the ineffectiveness of the IGEGs is further illustrated by their inability to mount collective problem-solving solutions when there exist some

disagreement over objectives, costs, means, and more. This inertia often leads to a situation where the cost of inaction is greater than the cost of taking action.

3.3.3 Disputed strategies and policies

Critics often consider the high failure rate of several of the IGEGs' strategies and policies as their real *achilles heel* – and therefore dispute them (Varma, 2002:24). It is particularly the negative impact this has on developing countries that give credibility to the arguments of the critics. This section focuses on the rationale behind many of these arguments.

3.3.3.1 Failed policies and programmes

According to Stiglitz (2003a:158), the IMF's failed policies in the developing world stem from ideological *narrow-mindedness*, namely its commitment to free markets and antipathy to government intervention in the economy. Critics argue that due to large scale capital outflows normally resulting from a crisis, the current policy of **IMF** lending to countries after the Asian crisis, for instance, caused a deep recession and extensive currency depreciation. Furthermore, as the IMF's resources declined, especially during the 1990s, the balance between adjustment and financing in programmes supported by the IMF shifted in favour of more adjustment, increased conditionality, and eventually led to a high rate of program failures. Then, in comparison with Asia, whose per capita income grew by 320% from 1970 to 2000, Latin America – where a number of countries are pursuing orthodox policies and structural reforms – grew by only 40% during the same period (Buira, 2005:30, 32). Finally, this differing performance greatly diluted the confidence in the pro-market reform policies endorsed by the IGEGs.

A fundamental problem with both IMF supported programmes and of World Bank loans are their standardised approaches to the often too complex problems of distinct developing nations, thus neglecting country priorities. The problem is that they do not adequately recognise these characteristics. Hence, their lack of a plurality of approaches is yet another reason why the governance of both institutions are accused of being un-representative. Moreover, the World Bank's record in sponsoring successful programmes is inaptly poor. Even its internal performance evaluations identify more than half of its

projects as failing to achieve *satisfactory, sustainable* results (Calomiris, 2000:89-90). The problem is that the **World Bank** assign subsidised loans to member countries, but does little to ensure that the funds are used for the stated purposes. In the case of the **WTO**, critics assert that its trade liberalisation agenda, which involve reciprocal tariff reductions, is proving to be rather illusionary. Existing evidence, according to Finger (2005:801), suggest that in the event of the Uruguay Round testing the ability of trade negotiations to balance cross-issue gains and losses sufficient to ensure a positive net outcome for each member, the GATT/WTO were found wanting to actually do so.

3.3.3.2 Wrong remedial strategies and adverse effects on developing countries

In attempting to implement the WC-reforms (in view of the IGEGs' strong emphasis on fiscal discipline), the liberalisation of financial markets, and a free market *competitive* exchange rate has created severe economic problems for Latin America and much of East Asia (Davidson, 2004:595). In effect, the *wrong medicine* has been given. Even the **IMF** now admits that capital market liberalisation presents considerable risks for many developing countries. It is also now widely recognised – especially after the crises of the 1990s – that capital market liberalisation has contibuted to global economic instability and has been a major factor that led to crises being more frequent and deeper over the past quarter-century (Stiglitz, 2003c:113). Hence, the vigorous pursuit and prescription of such policies by the IMF is creating an *anomaly* in that it is in stark contrast to its mandate of enhancing global economic stability. Furthermore, transition economies that privatised the fastest got the most support from the IMF. But Argentina and Turkey, for instance, found themselves trapped in a vicious circle, resulting from being too conformist on key aspects of neo-liberal reforms such as early capital account liberalisation, which rendered them inherently crisis-prone (Öniş & Şenses, 2005:270-273). Ironically, countries that appeared to be privatising slowly (like Poland, Slovenia and Hungary) are countries that have had the most successful transitions. What is unsettling is that little risk is actually born by creditors, nor the institutions themselves. This implies that developing countries are left to bear most of the costs of such crises.

According to Stiglitz (2003c:113), East Asian countries were actually forced to adopt conditions for contractionary policies set forth by the IMF during the financial crisis. These bailout packages exacerbated the downward spiral within the region and created serious moral hazard. As a result, the IMF was doing exactly the opposite of what Keynes had originally intended. IMF conditionality furthermore put developing countries in a position where they struggled to meet their obligations and had to cut their already low levels of education and healthcare spending, but often to no avail. Another mistake of the IMF with regards to policy prescriptions to developing countries is its excessive emphasis on inflation and exchange-rate stability as if they were goals in themselves. They are merely means to ends. Although consensus exists that eliminating hyperinflation is essential for economic growth, there is no consensus that reducing inflation increases growth. Too tight monetary policy in Russia and other transition countries, for instance, is often blamed for its contribution to the high level of barter in those economies.

Zahrnt (2005:692) maintain that “the risks of participating in the **WTO** (especially for developing countries) rise as the uncertainty about efficiency and distributional effects of WTO agreements is becoming greater and as the costs of employing counter-measures in case of unexpected, adverse effects of WTO agreements is increasing”. This, therefore, give context to the alarming observation by D’Arista (2004:23, 32), that “more openness without an arsenal of safeguards and strong anti-cyclical fiscal and monetary tools left emerging economies unprotected against the erratic pro-cyclical behaviour of the liberal-ised global financial system”. With ideology reigning over experience, emerging economies were continually encouraged by the IGEGs to open their borders and engage in the global economy, and as a result, incurred mounting debts denominated in strong currencies (with very limited ability to use their own currencies in transactions outside of their borders). Thus, a concern for developing countries is that these episodes have increased the risks of participation in the WTO, IMF and **WB** to a fairly disconcerting level.

3.3.3.3 Growing intrusiveness and dominance over domestic policy-making

Going well beyond the subtly respectful strictures set out in the original Articles of Agreement, both the IMF and the World Bank, critics assert, now reach deep into policy-

making within member governments. In fact, according to Woods (2005:156) both institutions have embraced areas of policy it was unimaginable for them to affect prior to the 1980s. Conditionality, in particular, has increased dramatically. By using a sample of 26 countries, Kanpur (2001:47) established that there were six to ten performance criteria and conditionality measures in the 1980s as opposed to approximately 26 in the 1990s. In addition, both institutions had become involved in negotiations with borrowers on virtually all matters concerning economic policy-making and more (e.g. judicial reform, corporate governance, the rule of law, etc.).

Emphasising the growing intrusiveness of the **IMF**, Kelkar *et al.* (2005:50) argues that "as the IMF increasingly seeks to harmonise and coordinate strategies for crisis prevention and management, it is becoming a rule-making institution whose decisions impact international as well as national economic policy-making". What is more, an inherent imbalance exist in the IMF as critics argue that while it has expanded its conditionality to matters beyond its main areas of expertise, its mandate remains undeveloped and in need of improvement – particularly in key aspects such as international economic cooperation (Portugal, 2005:76). In the same way, the **World Bank's** candid reassessment of development has placed it in an arduous position as it increasingly recognises the vital importance of matters outside its core competence. Stiglitz (2003c:125) therefore construe that "if the core mission of the World Bank is not lending money, then its own governance structure makes little sense". In fact, ever since the World Bank came into existence it has continually added new tasks to its mandate. By now, critics argue, its mission has become so complex that it strains credulity to portray itself as a manageable organisation (Einhorn, 2001:22). The problem is that the World Bank takes on challenges that lie far beyond any institution's operational capabilities. This, then, leads to a lack of focus and application.

In parallel expansion to the domains of both the IMF and WB, the **WTO** has become the keystone for the formulation of international trade rules. However, critics have identified a trend towards the WTO not only deepening liberalisation in a given area but also subsuming regulation of that area into its own regulatory system (Lunde, 2000:15).

Notably, this signifies a movement of regulatory sovereignty away from national governments to a global system in the pursuit of a specific model of regulation, i.e. deregulation, which mainly meets the needs of multi-national interests. As liberalisation has advanced, the WTO has increasingly come to affect what were initially thought of as purely domestic regulatory decisions (Woods & Narlikar, 2001:570). However, three factors, in particular, have of late made the WTO more dominant in domestic economies:

- increasing *deep integration* as evidenced through the Uruguay Round's agreements on sanitary and phyto-sanitary standards, which accompanied further liberalisation of agriculture, and on technical barriers to trade;
- due to the WTO being a single undertaking, all members, including developing countries, have found themselves forced to make commitments, some of them onerous, and
- the dispute settlement system (DSS) has, unprecedentedly, become both more potent and more legalistic. For instance, no longer can a party to a dispute block the adoption of a panel finding or halt the unstoppable progress of cases. The effect and concern of the growing importance of the DSS and other WTO agreements is that they increasingly constrain national policy choices.

Picciotto (2003:391) emphasised that "it seems that the *pressure towards global homogeneity* tends to override local preferences as embodied in national laws, policies and regulations, yet it takes place through a network of technocratic governance institutions that seem to operate beyond the realm of democratic debate". This is what, as critics argue, increasingly makes the role played by the IGEGs in the global economy, **unjustly dominant** (Nye, 2001:3). Critics are worried about, what they call, *an agenda of convergence* that is pursued by arguably the most powerful agents in the global economy, the WTO, IMF and World Bank. The trade liberalisation measures within developing countries that have accompanied the IMF and World Bank's structural reform programmes and conditionalities, for example, have served to support the trade liberalisation aims of the WTO (Calomiris, 2000:90). Rowden (2001:38) calculated that between 1995-1999, 65% of all WB adjustment operations supported trade policy

reforms and between 1995-2001, under IMF loans, 36 countries were obligated to reform their trade regime in line with WTO accession requirements.

3.4 In defense of the IMF, World Bank and WTO

One can understand that the IGEGs find themselves in quite a dilemma, particularly regarding their efforts to balance the interests of both developing and developed countries. On the one hand the IMF, World Bank and WTO try to place the emphasis, through neo-liberal policies, on deriving mutual benefits from free markets. But this, on the other hand, may come at the cost of breaking collectively legitimated rules of, for instance, research independence or personnel selection; and *vice versa*. The dilemma, according to Wade (2002:217) is that "asserting legitimacy-protecting collective rules may cause the organisation to lose support of the hegemon, while doing what the hegemon wants may entail breaking the collective rules".

What is more, the IGEGs are in the ungainly position of reconciling fundamental tensions: between global economic integration and national sovereignty; between a few very powerful states and a multitude of weak ones; between believers in market fundamentalism and sceptics (Wolf, 2004:82). Hence, any international regime must be a compromise and for that, all three of them deserve acknowledgment.

Defending itself, the IMF (2006:1) argues that it is not true that the programmes it supports impose austerity on countries in financial crisis. An IMF programme reduces the extent of the *belt-tightening* needed and attempts to cause a quicker recovery of incomes than would otherwise be the case. The IMF's financial support, charging below market interest rates, reduces the adjustment the country would have to make otherwise. Accordingly, tighter budgets, for instance, are not always what the IMF recommends. In the Asian crisis all countries ran substantial fiscal deficits during 1998, reflecting the quick turnaround in the IMF's policy advice once the scale of the crisis became known. The IMF further claims that it does not follow a *one-size-fits-all approach* in terms of its advice. In a study of 133 IMF-supported programmes, the IMF's Independent Evaluation Office found that from 1993 to 2001 there was considerable variation in the scale of

fiscal adjustment programmed across countries. Evidently, not all programmes were austerity-orientated. At least 40% of programmes have focused on a widening of the current account deficit as a percentage of GDP, while about a third focused on an increase in the primary fiscal deficit and primary spending as a percentage of GDP (IMF, 2003:4).

When a country is facing a balance of payments crisis and the private sector, such as banks and other lenders and investors, are unwilling to lend to it, the country turns to the IMF for help. When the IMF, in turn, suggests corrective policies that will restore investor confidence and result in an inflow of capital, it should not necessarily be viewed as *favouring* bankers and elites. Restoring the banking system of such a country to normal functioning is critical to creating a safe environment for citizens and investors. Intervention, particularly in this regard, helps to prevent contagion, i.e. when an ongoing crisis in one country spill over to its neighbours and other countries.

The IMF claims that it is not being dominated by the G7 countries. Although most of its financial resources are provided by the G7, decisions on policy and country matters are made through consensus among IMF shareholders. Apparently, all members have the same opportunities for their views to be heard. With the developing countries having 37% of voting power in the Executive Board, they, as a bloc, has just as much power to veto important decisions that require an 85% or 70% majority as the US with 17% voting power or a coalition of developed countries. After all, the IMF (2006:6) claims, it is very seldom that divisions break down along *North-South* lines. The IMF does, however, admit that change is necessary to give more votes to countries that account for a larger share of the world economy. Political will by its members, though, is required to rebalance IMF quotas (McLenaghan, 2005:189). Furthermore, the IMF's EB has taken the position that its approach to assign a major role to GDP as the primary variable in quota calculations is consistent with the role of quotas in meeting the financing requirements of the IMF, which need to correspond with each member's ability to contribute.

The IMF maintains that it is not unaccountable. It is accountable to its shareholders, its 184 member countries. All its members has sufficient opportunity to provide input through the EB, which meets three times a week, and by means of the Annual Meetings where representatives from member countries (governors of the IMF) meet to discuss the outlook for the world economy and the role of the IMF. The view taken in the IMF (and to some extent in the WB) is that although consensus decision-making may sacrifice some transparency and accountability, it, importantly, serves to avoid conflict that damages other arenas of foreign relations (Kahler, 2004:150). In terms of transparency as a vehicle for fostering accountability, the IMF attempts to open up decisions to greater scrutiny and promotes transparency in its members' policies. Particularly through its website, the IMF try to convey large amounts of information on itself and member countries. In addition to these efforts, the IMF established the Special Data Dissemination Standards to provide markets with up-to-date and high-quality economic and financial indicators (Askari, 2004:59).

In being more open to self-criticism, the **World Bank** has, even more so than the IMF, vastly expanded its transparency in recent years. Its disclosure policies and documentation not previously in the public domain, are now frequently available on its website and other sources. An unprecedented step towards greater horizontal accountability was taken by the World Bank in 1993 when an Inspection Panel was called into existence by the EB. The Panel functions as a body where any group directly affected by the World Bank's operations may launch complaints (Woods & Narlikar, 2001:576). The World Bank also, in 1999, created a Compliance Adviser/Ombudsman with the aim of dealing with the concerns of people directly impacted by the International Finance Corporation and the Multilateral Investment Guarantee Agency financed projects.

Many of the World Bank's projects have been criticised on the basis that the focus is wrong (for instance, too much emphasis on large projects). Proponents of the WB argue that its projects should be judged not by their size but by their effects. In many regions, the WB's projects clearly have helped. Perhaps excluding **Africa**, most other regions that have received the most WB aid, experienced an increase in per capita income (Owen,

1994:100). Furthermore, although critics accuse the World Bank of increased intrusiveness into areas outside its mandate, the WB believes that these new practices move the human factors in development from the background to the center of attention. This result in greater awareness of significant uncertainties and ambiguities in the development process, and acknowledges that development is much more than a technical problem (Brunner, 2004:103). The World Bank's more comprehensive approach to development indicates that the orientation of the WB has changed quite dramatically in terms of how it deals with developing countries. In many countries, the World Bank has committed to placing the country in a central role in decision-making.

With regards to making adjustments, the World Bank, in fact, did make some important changes as it grew and learned from experience. It has played an increasing role in stimulating and coordinating research and development of new technologies that have proven to be especially relevant to developing countries, particularly with regards to agriculture (Owen, 1994:99). The World Bank also, ever more, coordinates the actions of other donor agencies and governments. These initiatives have helped to convert unrelated national and multilateral aid programmes for key developing countries into fairly integrated global efforts.

The **WTO** is an institutional hybrid that is, somewhat paradoxically, caught in the tension between ungovernable market and power dynamics, and the political need to attempt regulation of globalisation. Still, as Irwin (2000:353) argues, "the WTO is useful because it changes the political economy of trade policy in a way that tends to facilitate trade liberalisation as an outcome". Furthermore, as one particular site that attempts to govern globalisation, it is not surprising that those actors who operate within that specific site are held accountable for the costs of the globalisation (Mortensen, 2000:176). Moreover, although the WTO started to pay more attention to the issue of accountability, it, admittedly, has very few mechanisms of evaluation, compliance, and enforcement in place (WTO, 2006:11). Currently, the WTO has two mechanisms of accountability with respect to members: the TPRM and the DSS. The former attempts to improve transparency and understanding of policies through regular monitoring and constructive

debates, while the latter seeks to promote members' understanding of WTO disciplines. Its transparency improved after placing much more documents of major significance (such as minutes of Ministerial Councils, panel findings, summary reports, studies, etc.) on its website. Exceptions might still be documents on tariff renegotiations (Hoekman & Kostecki, 2001:183). Concerning developing countries, the WTO (2006:18) claim to have committees that look at these countries' special needs and also, that all its agreements contain special provisions for them, including:

- longer time periods to implement agreements and commitments;
- measures to increase their trading opportunities, and
- support to help them build the infrastructure for WTO work, to implement technical standards, and to handle disputes.

It must be pointed out that all three IGEGs have, in accordance with a number of criticisms mentioned in this chapter, started with reforms to make these institutions more accountable, transparent, democratic and effective. However, there is still considerable debate over to what extent these changes have been made, and whether it constitute real structural change to the architecture of global economic governance. Although further reforms are non-negotiable, there is less debate, though, over the need for, and logic behind, the existence of the IMF, World Bank and WTO.

3.5 Conclusion

Although the case for global economic regimes is strong, those that exist are, inevitably, highly imperfect. Today, more than 60 years after the establishment of the IMF, World Bank and GATT/WTO, effective governance of the global economy remains an outstanding issue yet to be addressed. After weighing up the criticism of the IGEGs against the touchstone of their goals, principles, and defense, the study find these institutions **disturbingly deficient** in terms of adequately performing their role as central pillars in global economic governance. Even by their own internal measures, they, as monopoly agents of governance, often fail to achieve their goals and are found wanting in terms of effectiveness – this, mostly to the detriment of developing countries. Still, as the IMF, World Bank and WTO began the new century with ever-grander visions, the

criticism have simply increased (Calomiris, 2000:87; Einhorn, 2001:28). Serious governance deficiencies have led critics to put forward powerful arguments that both question their viability and, call for fundamental reforms. Admittedly, some of the criticism brought against the IGEGs are, perhaps, debatable, such as: to whom they actually should be accountable; that not all decision-making are externally influenced; that there do exist valid reasons or restrictions why they are not, in some cases, sufficiently effective; and that changes in the global economy and governmental deficiencies requires of them to become more intrusive in domestic economies (mostly developing economies). These could be distinguished from less contentious but more **serious criticism**, such as: their economic logic in terms of ideology; the unfair quotas and voting structures; clear inherent democratic deficits; and the adverse effects that their policies have on developing countries. These are some of the most severe imperfections that remain integral to the global *governance void*. What is for certain is that, taken collectively, all of the criticism seriously damages the IGEGs' sovereignty, legitimacy, effectiveness, and public image, which is resulting in a serious lack of trust and ownership in these institutions. Surmounting these criticisms indeed pose a momentous challenge to the current institutional arrangements of global economic governance. Almost more importantly, though, are the underlying factors that have led to the IGEGs being criticised so extensively. These factors can be considered as the actual **root of the problem** in global economic governance and it is here where reform is most needed:

- the multiplicity of objectives (including the confusion of means with ends);
- ideological stubbornness and injudicious narcissism;
- varying degrees of resistance to change and an inherent inertia;
- lack of autonomy and a continuing biasedness towards developed country interests (particularly the G7), very often at the expense of developing countries' (especially **Africa's** (see section 5.5 in chapter five)) wellbeing and progress, and
- the absence of an institutional framework to discuss global economic policies and a corresponding regulatory regime to assess, coordinate and strengthen it.

Encouragingly though, according to Stiglitz (2003d:34), real reform has started to take place at the World Bank, while less reform has taken place at the IMF, and small amounts

of reform have even happened at the WTO. Yet, as a main issue of concern, current efforts to improve governance in the global economy are still heavily biased toward the interests of the firms, governments, and (the much lesser in number) peoples of the wealthiest of the world. While there are signs that larger and potentially more influential developing country role players may finally be admitted to global economic governance and decision-making councils, the smaller and poorer developing countries risk continuing exclusion (Helleiner, 2001:255). This, as critics rightly argue, still does not solve the global inequality problems and is, in fact, another illustration of the ongoing unfair nature of current global economic governance arrangements. As a result, there must be concern as to whether reforms in global economic governance will grant sufficient weight to the imperative of sustainable global economic development and the struggle against human poverty, which is arguably the primary trepidation regarding the way in which the global economy is currently evolving.

All of these criticisms indeed constitute sufficient **grounds for real reform** that goes beyond conferences and consternation. The IMF, World Bank and WTO have the responsibility to demonstrate a genuine commitment towards ensuring a comprehensive framework for global economic policy-making and the equality of countries; thus, designing an agenda which reflects the interests of all countries, and not just a select few. Reforms should at least include changes in their governance structures, policies, modes of operation, and their approaches towards solving broader global economic problems, i.e. long-term systemic challenges (and related factors). Hence, at issue then, is how these institutions can be altered to make a greater contribution to the solution of current global trade, development and financial problems[44].

With this chapter having considered the criticism against the IGEGs, the next chapter will deepen the investigation into the deficiencies in global economic governance by examining a number of contributing factors that make the task of global economic governance more problematic. These factors are significant because they, also, should be

[44] In chapter six more attention will be paid to the challenge that these three issues raises, that is: what kind of reforms should be made to make free trade fairer, economic development more sustainable, and lessen countries' (especially developing countries') vulnerability to global financial instability?

taken into consideration when reforming and remodelling the complete framework of global economic governance.

APPENDIX 3A: IMF quota calculations

Indicating the complexity of calculating IMF quotas, the current five formulas, used from the Eighth to the Eleventh Reviews, are (Dos Reis, 2005:208-209):

Bretton Woods: $Q1 = (0.01Y + 0.025R + 0.05P + 0.2276VC)(1 + C/Y)$

Scheme III: $Q2 = (0.0065Y + 0.0205125R + 0.078P + 0.4052VC)(1 + C/Y)$

Scheme IV: $Q3 = (0.0045Y + 0.03896768R + 0.07P + 0.76976VC)(1 + C/Y)$

Scheme M4: $Q4 = 0.005Y + 0.042280464R + 0.044(P + C) + 0.8352VC$

Scheme M7: $Q5 = 0.0045Y + 0.05281008R + 0.039(P + C) + 1.0432VC$

where: $Q1$, $Q2$, $Q3$, $Q4$ and $Q5$ = calculated quotas for each formula

Y = GDP at current market prices for a recent year

R = 12-month average of gold, foreign exchange reserves, SDR holdings and reserve positions in the IMF, for a recent year

P = annual average of current payments (goods, services, income and private transfers) for a recent five-year period

C = annual average of current receipts (goods, services, income and private transfers) for a recent five-year period

VC = variability of current receipts, defined as one standard deviation from the centred five-year moving average, for a recent 13-year period

For each of the four non-Bretton Woods formulas, quota calculations are multiplied by an adjustment factor so that the sum of the calculations across members equals that derived from the Bretton Woods formula. The calculated quota of a member is the higher of the Bretton Woods calculation and the average of the lowest two of the remaining four calculations (after adjustment).

Chapter 4

Factors contributing to the shortcomings in global economic governance: The broader context of the governance void

4.1 Introduction

Although credit can be given to the IMF, World Bank and WTO for, to an extent, adjusting their roles in response to changing global economic realities, the *vacuum* left by their deficiencies has accentuated the need for a more holistic approach to global economic governance. The importance of recognising and addressing fundamental problem-areas on a broad scale in this integrative process is crucial in ensuring that the redesign and/or reform of the architecture of global economic governance balances the interests of both the countries of the North and those of the South. Hence, it is essential to identify and accentuate problematic factors in global economic governance's broader framework (or external environment), as they also need to be considered in the redesign process. Adjustments in the past (*vis-à-vis* global economic governance) have not necessarily been in the right direction. According to Varma (2002:24), not enough emphasis was placed on global stability and development, whereas conditionalities and neo-liberal policy prescriptions by especially the IMF and WB were over-emphasised (usually under G7/8-direction). Currently, the problem is that overall global economic management is left to the markets and/or, in some cases, to *ad hoc* initiatives by consultative *fora* of the main developed countries, such as the G8. Hence, insufficient effort is made to ensure that the management of the global economy attends to basic realities/factors that concern developing countries, in particular, thus worsening the **governance void**.

Considering this, the aim of this chapter is to provide additional context to the problematic nature of the governance of the global economy. It attempts to identify key causes and sources of instability that specifically make the process of governing the global economy more complicated and, in many cases, less effective. It is important to note that these disquieting developments in the global arena contribute to an increasing *governance void*. The chapter thus investigates the way in which these developments/ factors impede the process of global governance, including global economic governance. Hence, the implications for global stability and world order are considered. The factors

are divided into three main categories: the asymmetry problem (section 4.2), the emergence of more non-state and private actors of authority in the global economy (section 4.3), and sources of specific uncertainties and imbalances (section 4.4). Notably, many of these factors (or concerns) are, to some extent, political in nature. In terms of the study as a whole, this chapter serves to emphasise the political and economic realities of global economic governance as part of its wider context, i.e. global governance[45].

At this stage it must be emphasised that literature presents two decisive parallel developments (and/or discourses) in global governance which serve as contextual background to the issues investigated in particularly this chapter. First, as also stressed earlier, Strange (1996:72) underscores an increasing governance void in the global economic order. This so-called "yawning hole of non-authority and ungovernance" could be attributed mainly to three reasons: a steady decline in the authority and legitimacy of nation-states in the face of a rapidly expanding global marketplace; mechanisms of regional governance that remain, in most cases, unimposing and toothless, and a significant degree of uncertainty with regard to the ability of the IMF, World Bank and WTO to provide a suitable and balanced institutional framework for governing and regulating the global economy. Secondly, Veltmeyer (2004:4) points out the increase in neo-imperialism, in particular after the 1990s. Neo-imperialism, which replaced old imperialism after World War II, is an imperialism in economic form (with political implications), i.e. the domination of developing economies by agents of economic power such as multi-national corporations (MNCs) and the institutions of global economic governance. In this sense, they are mainly agents of the G8 countries and, in particular, the US, to serve – as Sklair (2001:57) claims – the economic interests of the "elite transnational capitalist class".

Although they co-exist, the governance void and neo-imperialism seem to oppose each other in the global arena, creating an **unhealthy imbalance**. The former signifies the absence (or lack of) proper guidance in the global economic order, while the latter emphasises a strongly growing form of *agencies of rule* – other than nation-states – in the global economy. The fact that the co-existence of these two seemingly contradictory

[45] See chapter two (under section 2.2) for a definition and contextual description of global governance.

international developments is expanding underlines their key role in underpinning and worsening the prevailing governance uncertainty regarding the management and progression of the world economy. This also severely complicates global economic governance and seriously contributes to increased global instability and inequality through the imbalances (in terms of the global dominance of only certain role-players (e.g. MNCs and the G8), at others' expense (e.g. the developing economies)) being created.

4.2 The asymmetry problem

Although this issue raises significant debate, an increasing number of scholars agree that the role of governments in the global economy is declining due to globalisation, and more specifically, the uncontrollable nature of the forces that drives this process (Held, 2000:3; Bell, 2003:805; Held & McGrew, 2000:22). As a result of what some call "the retreat of the state", governments are not in a position (as they were in the past, it is argued) to provide proper governance to cross-border economic activities. Yet, as a social entity, the state is an active participant in the processes involving neo-liberal globalisation (Singer, 1999:207). For the sake of clarity, the issue under discussion is not about the extreme case of the demise of the state and/or the complete erosion of state power and capacity, but rather about a thorough restructuring of the state. In fact, nation-states remain militarily, economically and politically powerful, and are now in some respects larger, stronger, and more intrusive in social life.

However, it is obvious that the Westphalian[46] norm of sovereignty is, largely due to globalisation, no longer similarly operative. As stressed by Scholte (2001:22), both from a juridical and practical point of view, state regulatory capacities have ceased to meet the criteria of sovereignty as it was traditionally conceived. In this sense, contemporary globalisation (in particular, its third wave (1980-today)), which conceivably involves the qualitative transformation of the world economy, has brought an end to the traditional theory of sovereignty. For example, globalisation is viewed as displacing the role of the state as the institution creating the conditions of capital accumulation as well as the

[46] Originating from the Peace of Westphalia in 1648, this system is viewed as the organisation of humanity into sovereign, territorially exclusive nation-states – free from outside interference (Held, 2000:6).

regulation of international capital flows (Veltmeyer, 2004:16). Due to globalisation, national markets have also become increasingly fused transnationally rather than merely linked across borders (Kobrin, 2002:46). This complicates the process of governing such intensely integrated markets and puts territorially confined nation-states in a dilemma: they are forced either to collaborate with each other or to leave the governance of these markets to one or more, or a combination of, supra-national bodies/agencies over which they have no official control.

Those who agree that this change is occurring and recognise its new challenges describe it as the so-called *asymmetry problem*. It is believed that there is a profound and asymmetric shift from a state-dominated to a market-dominated global economy (Gilpin, 2000:108). Globalisation is disturbing the basic symmetry of political organisation (nation-states) and economic organisation (markets[47]) as the latter expand beyond the limits of government control and national territories. Hence, both the authority and the legitimacy of states are in decline. It is argued that the rapid interpenetration of economies is facilitated by a global drive for liberalisation of markets and a dramatic reduction of the commanding role of the government in national planning – something which is even regarded as *a crisis of globalisation* (Strange, 1996:72). Ironically, though, as Wolf (2002:15) points out, "the change seen over the past twenty years is market-driven globalisation unleashed, consciously and voluntarily by governments [themselves, as key agents of this change]". Nation-states are thus creating the contradiction of reducing their own economic authority and allowing markets to expand globally in a more unmanageable fashion. Consequently, globalisation is currently transforming the nature and form of economic and political power in favour of the former:

- state boundaries are steadily becoming less important as large and accelerating flows of capital, trade, technology and labour create an integrated global economy, and
- the growth of capital markets and the continued lowering of barriers to trade and investment are continually tying markets together.

[47] Alfred Marshall (1961:270) defined a market as "not any particular market place in which things are bought and sold, but the whole of any region in which buyers and sellers are in such free intercourse with one another that the prices of the same goods tend to equality easily and quickly".

However, the political institutions (or global polity) have lagged behind and as a result, the ability of states to govern the market has weakened (Griffin, 2003:790). For that reason, the sovereignty of governments is on the edge of transformation, as is their actual capacity to rule (Ohmae, 1995:59). The exclusive link between territory and political power has been broken due to the fact that borders – fundamental to the exercise of national power – are eroded as markets become more globally integrated. Hardt and Negri (2002:98) therefore argue that the state is becoming increasingly less important in both the regulation and the management of the global economy. In Held's (2000:3) view, globalisation is creating new economic, social and political conditions that are serving to transform state powers and the context in which states operate. The concern is that, as closed national economies dissolve into mixed, interdependent, and integrated cosmopolitan societies, there is growing uncertainty as to how and by whom such economies should rightfully be governed/regulated. Central to this concern, as Held and McGrew (2000:13) point out, is the fact that "the modern state is increasingly embedded in webs of regional and global interconnectedness permeated by quasi-supra-national, inter-governmental and transnational forces, and unable to determine its own fate".

It is important to note that the sustained neo-liberal globalisation of economic activity is considered to be reshaping the ordering principles of the modern world and revolutionising the ways in which people interact, thereby undermining the role of the state (Bell, 2003:803). This is due to the perception that imperfect markets are superior to imperfect states. As deregulation and other reforms have reduced the role of the state in the economy, markets have become one of the most important mechanisms in determining both international and domestic economic and even political affairs. In addition, Legrain (2004:154) argues that many of the economic policies on offer today are similar. With the increase in global interconnectedness, the scope of strategic policy choices available to individual governments (chiefly those in the developing world) and the effectiveness of many traditional policy instruments tend to decline (Öniş & Şenses, 2005:282). As a result, effective state intervention is being substantially eroded under neo-liberalism which, in turn, has a negative impact on the ability of states to readjust to a new agenda that could involve fresh thinking – as is required for decent policy reform.

It appears that the increase in the mobility of capital induced by the development of global financial markets is causing the balance of power between states and markets to shift, to the benefit of the latter. This, in turn, generates powerful pressures on governments to develop market-friendly policies, which include increased privatisation, labour market deregulation, low public deficits and expenditure, as well as lower (internationally competitive levels of) taxation. As pressures from the international economy progressively intrude on domestic societies, nation-states increasingly struggle to control active intervention by outside parties, which illustrates that state sovereignty is no longer absolute, but conditional (Sideri, 1999:126). In fact, the autonomy of states is compromised as governments find it increasingly difficult to pursue domestic agendas without cooperating with (and often seeking the consent of) other agencies, political and economic. This need for increased international collaboration regarding decision-making further adds to the governance uncertainty inherent in contemporary global economic governance.

In stressing the largely irreversible nature of current global processes, Ohmae (2006:vii) adds that "many of the core values supporting a world order based on discrete nation-states – liberal democracy as practi[s]ed in the West, for instance, and even the very notion of political sovereignty itself – have shown themselves in serious need of redefinition or, perhaps, replacement". In fact, the complex processes that together constitute globalisation's driving forces have created a new transnational arena for economic, social, and political interaction, in which the nation-state is no longer in a similar commanding position than was traditionally the case. Held and McGrew (2000:34) even contend that "the *decision signals* of global markets, and of their leading agents and forces, become a, if not the, standard of rational decision-making". So what are these key forces/processes that cause such evolution in the market?

The three most dynamic driving forces behind **globalisation**, namely increases in technological innovation (which is in line with endogenous growth models), international trade and foreign investment have been exceptionally instrumental in providing an irresistible motive for the geographic expansion of markets. There is no question that the cost, risk, complexity, and pace of technological development have increased

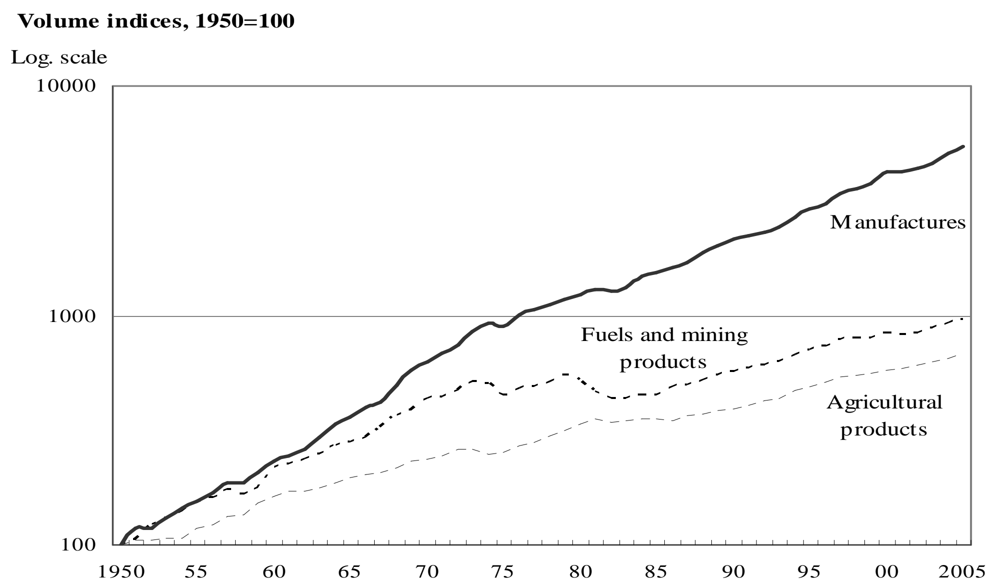
substantially over the past four decades. A technological revolution with momentous but uncertain consequences is facilitating and paralleling the considerable growth in global trade and investment. This, rather than the need for larger production runs, is the main motivation for the transnational integration of markets. For example, in the United States, research and development (R&D) expenditures increased almost six-fold between 1950 and 2000. In 2006 the top 1250 R&D-active companies in the world invested £249 billion in R&D, 7% higher than the previous year (compared to a 5% increase in 2005) and accounting for over 50% of global business R&D (DTI, 2006:1).

Furthermore, as Yergin and Stanislaw (2000:215) highlight, "information technology – through computers [particularly the Internet] is creating a *woven world* by promoting communication, coordination, integration, and contact at a pace and scale of change that far outrun the ability of any government to manage". One example of this is the exponential increase in technology-driven collaborative agreements among leading MNCs from major industrial countries, in particular during the past decade and a half. By continually working towards increased global market access, these strategic alliances are creating a *network* of global economy and, notably, represent a change in the mode of organisation of cross-border economic transactions. Furthermore, Kobrin (2002:50-51) interprets the qualitative advances in information technology in particular by insisting that "we face a dual revolution as markets are migrating from geographic space to cyberspace (e.g. the exponential growth of e-commerce) and the morphing of products from real *atoms* to digital *bits*". Crucially, both are causing serious problems for the regulation of geographically defined markets and economic governance that is rooted in territorial jurisdiction.

More evidence of the substantial expansion of markets is the dramatic increase in international trade in various market segments. Figure 4.1 below merely illustrates the growth of three of these from 1950 to 2005: trade in manufactured goods has risen the most and increased sharply throughout this period; secondly, trade in fuels and mining products gradually increased before and after the volatile period of the 1970s, and thirdly, agricultural products also showed, apart from a few interruptions, a gradual increase for

the entire period (WTO, 2007a:3). Not only did aggregate international trade grow at an annual rate of 5.3% between 1989 and 1997 (nearly four times faster than global output (1.4%)), but world merchandise trade grew at 5.8% for the period 1990-2005. This is almost double the growth for the period 1973-1990 (Yergin & Stanislaw, 2000:220).

Figure 4.1: World merchandise trade by major product group (1950-2005)



Source: WTO, 2007a:2 *International Trade Statistics 2006: Selected Long-term Trends*

Coinciding with the growing intensity of globalisation, the net effect of global investment patterns, in particular since the 1980s, showed a dramatic increase. In fact, it was since the 1990s that capital flows for both industrial and developing countries increased sharply in volume (Dos Reis, 2005:197). Inflows of foreign direct investment (FDI) in 2005, for instance, rose by 29% to $916,3 billion after an increase of 27% in 2004 (with a peak in 2000) (UNCTAD, 2006:9). However, according to Epstein (2003:151), the likelihood that the positive impacts of FDI will materialise and be widely shared is significantly diminished by the neo-liberal policy framework that is dominant in most countries. Increased deregulation and *free* capital mobility are the main reasons for the lack of a democratic framework of multi-national investment regulation. With MNCs now already producing more than 25% of the world's GDP, the problem is that if this

situation persists, it will hamper future efforts to successfully govern/regulate cross-border investment.

Therefore, due to the current qualitative transformation of the world economy – caused mainly by globalisation's driving forces – a key concern is the geographic complications resulting from the asymmetry problem. With geographic space losing significance as the basis for the organisation of markets, the mode of organisation has unexpectedly changed: intergovernmental politics remains geographically grounded in sovereign territory while major sectors of the global economy are organised in terms of non-territorial electronic networks. Hence, as emphasised by Cutler *et al.* (1999:73), "geographically rooted economic governance has become more problematic as non-state or private actors are increasingly involved in authoritative decision-making". The result is increased **governance uncertainty**, leading to governments being locked in an array of global, regional, and multi-layered systems of governance and barely being able to monitor it all, let alone stay in command. All this has altered and compromised the capacity of states to provide the public good of a common structure of rights, duties and welfare for their citizens. In fact, these systems and institutions, according to Held and McGrew (2000:35), "undercut, circumscribe and delimit the kinds of entitlements and opportunities national states can offer and deliver". Consequently, the institutional nexus of the political good is being reconfigured, leading to more governance uncertainty.

As the search for new and appropriate forms of international governance is a priority on the global agenda, the world is witnessing a historic shift in the structure of global order (Veltmeyer, 2004:4, 16). Globalisation has ushered in a new post-capitalist form of development. The nation-state has retreated from the development process and been replaced by what Robinson (1996:380) conceptualises as the *internationalised state*. Accordingly, globalisation involves a structural shift towards a polycentric form of shared global governance, thus inviting a corresponding adaptation of the state. In this respect, the state's sovereignty and authority are being reconfigured in the context of a multi-layered system of global and regional governance. They are viewed as one level in

this very complex system of often overlapping and competing agencies of governance (Hall & Biersteker, 2002:66).

As evidenced in the growing membership of multilateral institutions, states are increasingly being transformed into **reflexive states**[48] with a new public philosophy of governance which recognises the changed global context of economic and political action. In addition, the involvement of states in regional forms of governance is continually being encouraged. Consequently, globalisation does prefigure a historic power shift from national governments to evolving systems of regional and global economic governance. The study would therefore concede that the contemporary world order might best be described as a *heterarchy*[49]. This certainly suggests that the world is currently witnessing not only a transformation in state power, but also the emergence of new forms of governance in the global economy. In fact, both the rising status of multilateral institutions of governance and regional governance (as part of a complex set of interconnecting relationships) have now become primary vehicles by means of which states (more accurately the G8) can exercise their power – indirectly. This power is, however, different from its traditional concept in that states now have to compromise their autonomy by sharing the function of governance with other agencies in a complex set of interconnecting multilateral relationships.

In explaining this transformation, Held (2004:366) points out that "while many states retain the ultimate legal claim to effective supremacy over what occurs within their own territories, this should be juxtaposed with, and understood in relation to, the expanding jurisdiction of institutions of global and regional governance and the constraints of, as well as the obligations derived from, new and changing forms of international regulation". Hence, one can argue that if sovereign states are the principal building blocks of a stable world order, as many critics maintain, then the issue of the state and the state system being in decline (and thus being severely transformed due to increased

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[48] In his description of the *reflexive state*, Held (2000:164) states that it "seeks to reconstitute its power at the intersection of global, regional, transnational and local systems of rule and governance".

[49] A *heterarchy* is a system in which political authority is shared and divided between different layers of governance and in which multiple agencies share in, and often compete for, the task of governance (Held, 2000:163).

liberalisation) is indeed cause for concern for the future governance of the global economy (Lawson, 2003:136). This is due mainly to two questions: what will take its place then (in terms of performing this central function in world order)? And how long will it take for this replacement or transformation to take place? Given that the state system has been the defining feature of international order throughout the modern period, its decline is most certainly worsening the **governance void** and is asking perturbing questions about the future building blocks and central role-players of, specifically, a new global economic order.

4.3 Uncertainty created by the emergence of new actors of authority and the rising centrality of non-state actors in the global economy

The growing interest in the idea of *governance without government* is an interesting – and quite momentous – discourse in global governance as it provides an important context for the asymmetry problem. For instance, the role which social organisations, rather than governments, can perform in resolving collective action problems that are currently at the top of global political and economic agendas are increasingly being recognised. In fact, according to Young (1997:5), "the general proposition that groups of interdependent actors can and often do succeed in handling the function of governance without resorting to the creation of governments in the conventional sense is now well established". Although there still is significant uncertainty regarding the conditions under which governance without government can succeed, one cannot deny the need and desire of various stakeholders to become engaged in processes involving the institutionalisation of global decision- and policy-making. Hence, the emphasis is shifting towards the growing acknowledgment of and deference for, new actors of authority not only in global economic governance, but also in global governance. In view of both the intensifying asymmetry problem and the fact that states still remain among the main players on the global stage, governments are indeed no longer the only main players. Held and McGrew (2002:73) thus argue that in light of increasing global interdependence, the structure of the world order is changing – in particular after the Cold War. From a governance perspective, one decisive implication of this is the following: as the demand for governance increases with the proliferation of complex interdependencies, rule systems

can increasingly be found in civil society or advocacy groups, non-governmental organisations (NGOs), business associations, MNCs, and other types of collectivities that are not regarded as nation-states. Also included among these is the amorphous collection of groups that together constitute the *anti-globalisation movement*. This movement mainly functions as a catalyst of resistance to neo-liberal globalisation. Some of the illustrious protests of this movement were the *Battle of Seattle* against the WTO in 1999; protests against the IMF in Prague in 2000; the European Union (EU) summit meeting in Gothenburg and the G8 summit meeting in Genoa, both in 2001. The sub-sections that follow will focus on the global civil society, multi-layered global governance, MNCs, and interdependent networks of global governance.

4.3.1 The global civil society – the rise of people power

In this knowledge era of the Internet, citizen groups of both advanced and developing countries (separately and/or in collaboration) are increasingly mobilising and coordinating public opinion and protest across national frontiers with relative speed and ease. People's renewed appreciation of the workings of the market and the value of mass participation in decision-making has led to a shift in the balance of confidence – a declining faith in the competence of government (Yergin & Stanislaw, 2000:218). Thus, with globalisation undermining the role of the state by reducing their legitimacy and authority in the eyes of the public, most of the growing number of civil society collectives are primarily performing two key functions: organising human behaviour and creating **new systems of rule** (Berger, 2000:45). Though they are not replacing states, they are often, quite unprecedentedly, exerting considerable pressure on governments, and operate independently and distinctly from them – transnationally. The globalisation of political and economic activity has therefore, particularly over the past two decades, been accompanied by the emergence of a new kind of *network politics* which seeks to make global markets and global institutions work in the interests of the world's peoples rather than *vice versa* (Held, 2000:154). This *governance from below* represents an alternative politics of protest and transnational mobilisation. One area, for instance, in which the expanding transnational civil society continues to have some notable success is in mobilising and organising resistance to the rule of global capital (e.g. the Stop the MAI

campaign[50]). The most positive aspect of this development is perhaps that governance from below is becoming a more, rather than less, significant channel whereby citizens and communities can hold the agencies of global governance to account for their actions.

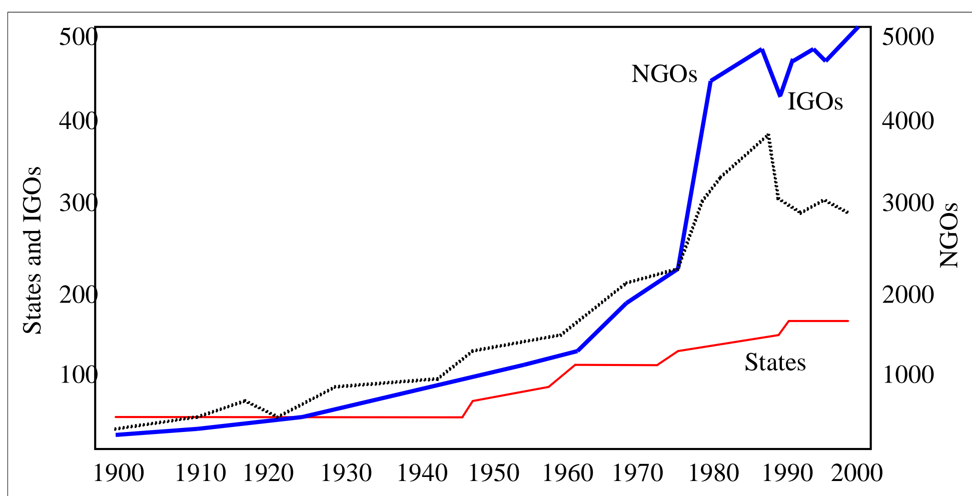
Due to this upsurge in the collective capacity to govern (i.e. *people power*), Held and McGrew (2000:185) are convinced that the world is in the early stages of undergoing a remarkable expansion of collective power. Although it currently is highly disaggregated and unfolds unevenly, it nonetheless is a relatively new development of rule systems that have become wider in functional scope and more extensive over space. Hence, driven by the continuing globalisation of national economies, combined with the advent of global interdependence issues (such as environmental pollution, climate change, monetary crises, HIV/AIDS and drug trade), new and intensified forms of transnational collaboration as well as new social movements – serving as transnational voices for change – are radically emerging (e.g. the World Social Forum). In this era of the empowered individual, citizens are, by collective will, demonstrating that they want to play a major role in rewriting existing laws, setting new precedents for participation, and shaking up hierarchies; all of which increasingly create powerful pressures that reverberate within international institutions and states.

Although it is made up of non-profit organisations and voluntary associations dedicated to civic, humanitarian, cultural and social causes, civil society is emerging as an independent international and counter-hegemonic force with a growing global presence. Though it is difficult to establish reliable statistics on NGOs, Held *et al.* (2001:8) calculate that they increased from a few hundred at the start of the 20th century to over 5000 at the start of the 21st century. As Figure 4.2 below indicates, the growth of NGOs – compared to that of inter-governmental organisations (IGOs) and states – experienced a much greater and more rapid increase during the 1980s, in particular, and thereafter. Among the more than 3000 civil society groups listed at the United Nations (UN), the

[50] This campaign (to stop the Multilateral Agreement on Investment (MAI)) was the first major movement, using the Internet and network politics, to successfully challenge the imperatives of neo-liberal globalisation. Negotiations on the MAI took place from 1996 to 1999 and sought to establish rules governing international investment by MNCs. Governments feared a public backlash against the loss of sovereignty implied by the MAI and negotiations ultimately collapsed by early 1999.

largest and most prominent organisations are Oxfam, Amnesty International, Greenpeace, and the International Committee of the Red Cross. Apart from the success they had with the MAI, the global civil society – in recent times – effectively promoted treaties to limit global warming, helped establish an international criminal court, persuaded the International Court of Justice to render an advisory opinion on the legality of nuclear weapons, and mounted a drive to cancel the foreign debts of the world's poorest countries (Falk & Strauss, 2001:214). While these efforts remain works in progress, these transnational forces have to date been essential in furthering them.

Figure 4.2: Growth of NGOs, states and IGOs (1900 to 2000)



Source: Held & McGrew, 2002:48 *Governing Globalisation*

NGOs appear to have been accorded some form of legitimate authority, which Hall and Biersteker (2002:14) call *private authority*[51]. In light of the growing recognition of degrees of order and institutionalised, patterned interaction within the international system, NGOs (among other private actors) mainly exercise their influence and private authority in three different ways. First, by having the authority to **set the agenda**, many NGOs enjoy notable success in their lobbying efforts with governmental decision-makers which, due to their tactical decision-making and policy preferences, results in growing popular support from all classes of citizens. In this regard, they provide citizens with a

[51] *Private authority* refers to a growing number of actors (other than nation-states) associated with global market forces that appear to have taken on authoritative roles and functions in the international system.

channel of access to global and regional decision-making forums. Secondly, NGOs exercise their private authority by virtue of their authorship, or expertise. By giving expert advice they attempt to influence policy preferences. They are often viewed as credible providers of technical information – for example the detailed information contained in Amnesty International's annual human rights report. Thirdly, with their emancipatory and normatively progressive social agendas, NGOs exercise their private authority in the form of a *moral authority* over public issues, something for which they are also valued as ostensibly objective or neutral non-state actors. Accordingly, they exert pressure on governments, international bodies and corporate empires to be more accountable.

4.3.2 Multi-layered global governance – who is in charge?

Figure 4.2 also indicates that by contrast to the slow growth in the number of states (as expected), IGOs showed remarkable growth during most of the 1980s by almost reaching 400. However, they have declined sharply since then to just below 300 in 2000 – a figure that is still significantly higher than before the 1980s. The UN, the International Labour Organisation (ILO), and the IGEGs are examples of international bodies created by formal agreements between nation-states. Significantly, the growth in IGOs is a critical contributory factor to an increasing trend toward **shared governance**, which means that the sovereignty and autonomy of national governments is ever more locked into a multi-layered system of governance (Held, 2000:173, 130). Thus, in the context of the reflexive state, nation-states are not so much losing power but having to adjust to a new context in which their sovereignty and power is shared and bartered among many other public and private agencies or centres of authority – above, below and alongside the state.

What Held calls "powershift" is best demonstrated by the emergent multi-layered system of global governance. Characteristically, this system has evolved into a complex polyarchy that depends upon a multiplicity of agencies with no single centre of authority. These agencies range from nation-states, governmental organisations and multilateral institutions to MNCs that meet (and attempt) to agree on global policies, rules and norms. Scholte (2001:24) views this system in which power is exercised at various levels as three distinctive layers or infrastructures of governance:

- *The suprastate (top) layer* is unique in that the global and regional governance bodies in this tier have some kind of autonomous legal personality. With membership increasing, the coverage and influence of most is expanding – globally. Some examples are the IGOs, regional groupings and the IGEGs.
- *The national or state (upper middle) layer* includes global national governments, and is sandwiched between the other three layers.
- *The transnational (lower middle) layer* encompasses representatives of the global civil society that exert their influence by means of their infrastructural power, i.e. political strategies whereby average citizens and communities gain a voice in global governance. This layer also includes constituencies that represent the interests of MNCs, such as the World Business Council, which have acquired a privileged position in the governance of the global economy.
- *The substate (bottom) layer* comprises local governments and sub-state authorities that seek to promote the economic, cultural and political interests of their locale. Their activities range from establishing local diplomatic missions abroad to efforts overseas to attract international investment. One formal body, for instance, that represents key global and regional forums is the International Union of Local Authorities.

The layers of multi-layered global governance (except the national layer) expanding in terms of crowdedness and participants becoming more influential in the global arena signal a new method of governance – from an exclusively state-based structure towards **complex multilateralism** (O'Brien *et al.*, 2003:206). Concurrently, the nature of governance and authority of the IGEGs is also going through a transitional phase. This is mainly due to the growing recognition of, and adjustment to, the demands of the other actors in multi-layered global governance, in particular the global civil society. The complexity of this transition (for instance, the need to accommodate these demands, and clashes of rival goals) creates substantial **governance uncertainty** because while it is clear what the transition mostly entails, it is not so clear where it is going. This uncertainty is exacerbated by the heterogeneous and at times contradictory character of global governance. According to Koenig-Archibugi (2002:62), "the interplay among

distinct governance arrangements is remarkably diverse, as the modalities of interaction range widely, from symbiosis to rivalry". Alas, it is mainly the inherent inconsistencies in complex multilateralism that have a crippling effect on global governance. Among many other examples, irregular decisions such as not to create and empower necessary independent bodies are often made, as well as the deliberate exclusion of many stakeholders from decision-making processes – something that conveys overwhelming power to merely a few.

4.3.3 Multi-national corporations (MNCs) – growing global powerhouses

Since 1973 when international production surpassed international trade the world became stunned by the enormous size and steadily growing importance of MNCs in world economic activities. Today the scope of these non-state actors' penetration in the global economy is certainly unprecedented as more than one-third of world output is part of an integrated global corporate production system under the governance of MNCs. There are currently more than 450 000 MNCs in the world and by 1996 the largest 100 (excluding financial institutions) held $1,8 trillion in foreign assets and $2,5 trillion in foreign sales (UN, 1998:39). This was more than the combined GDPs of India, China, South Korea, Malaysia, Singapore, and the Philippines at the time. The assets of the world's five largest MNCs also rival the GNPs of such middle-sized economies as Turkey, Indonesia, Saudi Arabia, and South Africa.

In pointing to the emergence of a new structure of global economic governance whose rules largely determine how countries, organisations and people participate in the global economy, many scholars recognise the central position of MNCs (Held, 2000:160; Mazarr, 2006:173; Hoogvelt, 2001:77). In view of the increasing rule of global capital, corporations of global and financial capital are considered to be at the forefront of this new structure (as part of the system of multi-layered global governance). In fact, it is perceived that their influence in multilateral institutions (such as the IGEGs), IGOs, and world economies will largely determine how this structure is arranged. According to Veltmeyer (2004:19), of Fortune's top 100 MNCs, 80% are based in the US or Western Europe and "have drastically increased their control of the world economy". As prime

units of **Euro-American imperialism**, most technological innovations, FDI, and international trade are under the direct control of these MNCs. Their success, Falk and Strauss (2001:215) argue, lies in the "expansion of international trade regimes, the modest regulation of capital markets, the dominance of the neo-liberal market philosophy, and the supportive collaboration of most governments, especially those of rich countries". And part of this success is the key role played by MNCs, especially since the 1990s, in taking over strategic sectors in developing economies. The concern, though, is that MNCs gain greater power at the expense of ordinary citizens. The growth of direct and equity investment flows by MNCs have become a central part of the mechanisms of a new resurgent imperialism that is built upon regulatory arbitrage (moving their business to countries that offer the most favourable regulations) and political dynamism (influencing domestic and global policy-making). This, in Veltmeyer's view, is a reflection of their centralised empire-building character and a means of securing US hegemony. Alas, these dynamics of political and economic power cause unnecessary uncertainty *vis-à-vis* arrangements within multi-layered global governance.

4.3.4 Networks of interdependence – at the increasing risk of exclusion

The formation of interdependent networks re-emphasises the multi-layered nature and, again, the complexity of global governance as it involves a plurality of actors and diverse levels of coordination and operation, including (Held, 2004:367):

- corporate and private networks, comprising various business actors involved in shaping compatible global policies (e.g. the elite networks found in the International Chamber of Commerce (ICC[52]) and the World Economic Forum) and strategic alliances between corporations and complementary partners (e.g. cross-border, cross-regional and cross-industrial suppliers);
- an increasing number of public agencies (e.g. central bankers) that maintain links with similar agencies in various countries, thus forming trans-governmental networks for the management of global economic issues;

[52] The ICC (2007:3) describes itself as having "unrivalled authority in making [voluntary] rules that govern the conduct of business across borders". The ICC has close links with governments and multilateral institutions – e.g. it has long been granted consultative status at the highest level with the UN.

- NGOs and leading role-players in global advocacy networks who perform a function in various domains of global governance and at different stages of the global public policy-making process, and
- public agencies, NGOs, multilateral institutions, and business actors collaborating in many domains in order to provide innovative approaches to social problems by means of multi-stakeholder networks. One ambitious example of this is the UN's Global Compact initiative. The aim is to promulgate nine core principles drawn from the Universal Declaration of Human Rights and for the actors to then cooperate with each other in exercising these principles in their various domains (e.g. MNCs acting on their social responsibility).

According to Mortensen (2000:189), networks involving multiple relationships have become the dominant organisational form in contemporary society. Coinciding with the rise of multi-layered global governance, global networks emerge in response to the dispersion of state authority and, in many cases, the *absence of governance* in specific domains. The **network morphology** is also a source of dramatic reorganisation of power relationships as the privileged instruments of power connect the networks. In Castells's (2000a:260) view of the network society, these networks "converge toward a meta-network of capital that integrates capitalist interests at the global level and across sectors and realms of activity: not without conflict, but under the same overarching logic". By reproducing itself, this structure continues to expand as competition proceeds, thus enhancing the global character of the world economy.

The fact that these meta-networks have the capacity to switch off non-essential functions, devalued territories, and subordinate social groups is cause for concern. Hence there is the risk that people, locales and/or activities are being excluded from this network because their structural meaning might become insignificant (e.g. some developing economies). It is feared that they could be subsumed in the unseen logic of the meta-network where value is produced and power is determined. As a result, this network society appears to be a type of meta-social disorder: an automated, random sequence of events, derived from the uncontrollable logic of markets, technology, and geo-political order.

Keohane and Nye (2002:7) maintain that as interdependence and globalisation have intensified, the systemic relationships among various networks have become more important. Consequently, *system effects* become more significant: intensive economic interdependence affects social and environmental interdependence, and in turn, awareness of these connections affects economic relationships. Thus, by implication, the expanding networks become a type of global institution that regulates relations in a particular field. Notably, the complexity, diversity and ambiguity of the interactions in and between the different types of global networks cause further **governance uncertainty** and place additional strain on the power relations between the various role-players in multi-layered global governance, thus creating additional problems for effective global economic governance, in particular.

4.4 Disconcerting sources of specific uncertainties and imbalances

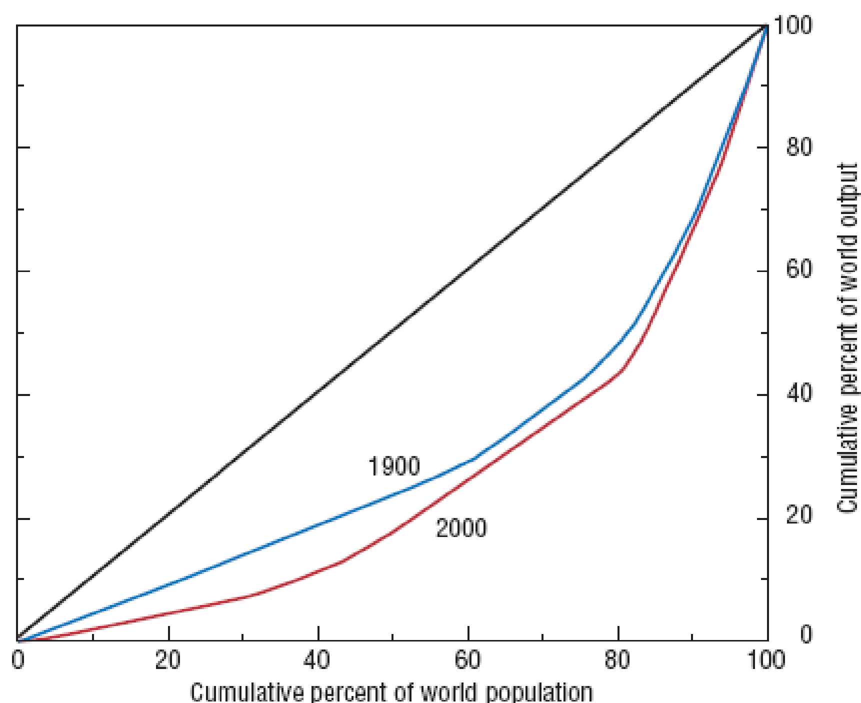
The perception of *the need for global governance* was excessively stimulated by a description of the world as being, in particular since the 1970s, increasingly inter-dependent. However, the end of the Cold War gave rise to global ramifications for the dynamics of interdependence (Rosenau, 2002:72). Problems such as global warming, financial crises, increased civil wars (e.g. Rwanda and Kosovo) and the growing divide between rich and poor are among the many problems[53] that have posed challenges to the global economic order. More people became convinced that many of these dislocations inherent in the vast degrees of interdependence should be addressed; thus amplifying the need for global governance and proper processes and structures to sustain it. However, very little of what was expected effectively materialised and as a result, increasing global uncertainties and imbalances have become global concerns, in particular since the 1990s. The gradual increase of these systemic risks – as exacerbated by globalisation – are transmuting the world into a **global risk society**. In view of that, this section will focus on some of the key issues within the sphere of global governance that have implications for the stability of the global economic order.

[53] Other significant global concerns for which there was not enough space here include rising energy prices (and the burgeoning Asian demand), environmental degradation and its economic impact, Japan's stag-nation, European unemployment, the US current account deficit and comparable surpluses in Asian countries, exchange rate misalignment of Far Eastern currencies (need to appreciate against the dollar), and the world's adjustment to the growing export markets of China (goods) and India (services).

4.4.1 Global inequality – the uneven playing field

By the late 1990s the US, EU and Japan had accounted for nearly three-quarters of the world's GDP. In 1996 already this TRIAD accounted for 66% of world trade flows and 65% of world stocks of FDI. It was also established that 86% of the world's resources are consumed by the world's wealthiest 20%. Furthermore, comprising only 15% of the world's population, the TRIAD accounts for between two-thirds and three-quarters of all economic activity (Held, 2000:110). As a result of this **triadisation** of the world economy, most of the remaining 85% of the world's population are virtually excluded from the globalisation process, signifying how uneven global opportunities are distributed between countries and people. In 1997, for instance, the income gap between the fifth of the world's people living in the richest countries and the fifth in the poorest was 74 to 1, up from 60 to 1 in 1990, 30 to 1 in 1960, 11 to 1 in 1913, 7 to 1 in 1870 and 3 to 1 in 1820 (UNDP, 1999:9). In Figure 4.3 the Lorenz curve clearly shows how world inequality increased in the 20th century, mainly, the IMF (2001:155) asserts, due to a large decline in the relative per capita income in the poor countries.

Figure 4.3: World Lorenz curve: 1900 and 2000



Source: IMF, 2001:155 "Fiscal Policy and Macroeconomic Stability", *WEO*

Identified at the summit meeting in Cancun, Mexico, (in the early 1980s), the global inequality gap is fast becoming the **primary obstacle** to a potentially prosperous future for the world as a whole. There are two major concerns. First, the fundamental inequalities and inequities in the distribution of the world's productive resources and fruits of development; and secondly, growing inequalities due to the concentration of power, property and income in the international system (Bowles, 2004:134). In this respect, it is specifically the continued domination of global markets by the major powers (the TRIAD – especially the US and EU) that delineate this concern. This includes the way in which they use IGEGs to their advantage and their use of imperialist power in market-opening strategies. With respect to this triangle of wealth, power, and technology, Castells (2000a:262) argues "the rest of the world becomes organised in a hierarchical and asymmetrically interdependent web, as different countries and regions compete to attract capital, human skills, and technology to their shores".

Looking at the broader picture, it is obvious that the structure of world economic activity is increasingly dominated by the OECD countries and the intensifying links between them. There is currently a significant concentration of trade and capital flows as well as an overwhelming proportion of technological capacity and industrial production between these countries. This takes place at the exclusion of much of the rest of the world from global markets, resulting in widening disparities between rich and poor nations. Countries such as the G8 concentrate resources to an even greater extent, particularly with respect to informational infrastructure, skills, and technology – key determinants of competitiveness (Castells, 2000a:265). Apart from the OECD countries gaining an enormous competitive edge, this situation is also leading to, in many cases, harmful competition among developing countries for investment and trade opportunities. Significantly, though, this is an indication of how globalisation is re-ordering developing countries into winners and losers – another dimension of the global inequality problem (Held & McGrew, 2000:26). In addition, it is increasingly recognised that equity is a **global public good** and that the lack of equity undermines global security and impedes global cooperation (Griffin, 2003:800). Although neo-liberals associate globalisation with growing global affluence in which global inequality and extreme poverty are considered

transitional conditions that will fade away with market-led global modernisation, it has certainly not materialised. With perhaps the exception of a few Asian countries (India, China and some South-East Asian countries), there is no convincing evidence to suggest that this *trickle-down effect* has, on a wide scale, effectively closed the gap between rich and poor countries.

Moreover, a key dimension of the exclusionary effects of global inequality, which is of great significance given the current era of vast technological advance, is the digital divide. As a reflection of other technological divides, the rapid diffusion of the Internet is proceeding unevenly throughout the globe. In September 2000 there were approximately 378 million Internet users around the world (6.2% of the world population). According to Castells (2002:260), this figure amounts to 42.6% North America; 23.8% Western Europe; 20.6% Asia (including Japan); 4.7% Eastern Europe; 4% Latin America; 1.3% Middle East, and 0.6% **Africa** (most of which South Africans). This contrasts sharply with each region's share of the world's population. The *digital divide* contributes strongly to existing sources of inequality that appears to widen the gap between the opportunities offered by the Information Age and its forlorn reality of social exclusion for many people that seem to be in a *race to the bottom*.

A major concern, then, is prevailing **global apartheid**, in which the minority of rich countries, or global elite, determines the rules and conditions for global competition and cooperation. An area that poignantly illustrates this is how this group benefits excessively from trade expansion and openness. Much of what is considered free trade is not fair trade and is therefore not a *level playing field*. Two well-known current concerns in this regard are subsidies that distort particularly the agricultural sector, and dumping, a rapacious form of price discrimination. Industrial countries spend approximately 1% of their combined GDP on subsidising (or protecting) the agricultural economy, which leads to higher-than-necessary prices for consumers and excessively high input-costs for competing farmers in developing countries (Kreinin, 2006:348). In the case of dumping, developed country monopoly companies typically sell their commodities in a developing

(country) foreign market at a price below that charged in their home (exporting) country, making it almost impossible for domestic firms to compete.

Another illustration of global apartheid is the way in which developing countries are ignobly excluded from most decision-making (e.g. at G8 meetings) and are given little say in establishing the rules and preconditions for global trade and development (Booker & Minter, 2001:31). The G8 is therefore often considered a kind of *global directorate* as it assembles the leaders of the world's most economically (and militarily) powerful states. Its veto or collective decisions determine to a large extent the priorities listed in the global agenda and the politics of global governance.

In the discussion on global inequality it is important to emphasise the significant role played by MNCs in aggravating it, in particular when considering that two-thirds of world trade is controlled by only 500 MNCs – mostly from developed countries (Öniş & Şenses, 2005:281). Creating the perception that *capital has priority, people are inciden-tal*, these **corporations** benefit tremendously from unregulated trade and large free trade areas since it makes them less answerable to local and national communities. Chomsky (2004:150) argues that investors and corporations have benefited the most from the liberalisation of trade and capital flows – of which by far the most come from developed countries. Stocks of both inward (67.7% in 1999) and outward (90% in 1999) FDI, for example, are highly concentrated in the developed economies, with the overwhelming share of FDI flows among them (Epstein, 2003:152). Furthermore, in the US, the 1990s was the first post-war period when the division of income shifted strongly towards inves-tors and owners of capital, and away from households and labour. This is even more true of developing countries where neo-liberal programmes have regularly reduced labour's share of national income. It is thus disturbing that corporate-led globalisation, through devices of intra-firm transfers, strategic alliances, outsourcing, etc., is concentrating wealth and power in the hands of those who are unaccountable to the public.

Unfortunately, it is expected that the gap in opportunities between the *haves* and the *have nots* as well as between those *included* and those *excluded* from the system of wealth and

power will remain, contrary to neo-liberal economic theory but consistent with reality (Chomsky, 2004:145). In the current liberal economic order the gross inequality within and between countries, characterised by a maldistribution of goods and resources, is breeding trouble that is culminating into conflict, with serious security implications for world order. While this situation is indeed morally outrageous and economically wasteful, many are now coming to terms with how potentially socially explosive the situation is. With the poor often left hopeless, poverty is increasingly undermining the fabric of many societies by means of confrontation, violence and civil disorder (Camdessus, 2004:422). Hence, rather than witnessing a new world order emerging along liberal idealist principles, many, according to Lawson (2003:112), are instead witnessing the rise of brutal "*new world disorder*".

4.4.2 Geo-political and -economic tension: a threat to global cooperation

The historical scars caused by the drawn-out Cold War has, even until the present, left an unwholesome heritage of political tension between the Western bloc, under US leadership, and the Soviet bloc. Apart from this, serious economic rivalries between the US, Japan and Western Europe developed in the West during this period. This pattern of Russia and China being the US's main **geo-political rivals**, and the enduring economic conflict (mainly over trade issues) among the TRIAD-countries are dividing the world into various camps, creating uncertain terrain, rife with tremulous and ambivalent interstate alliance formation (Callinicos, 2002:262). To make matters worse, many US policymakers see the potential that China might develop into an economic and military rival.

Developing countries bear in mind the fact that, although the colonial order may have passed, the post-colonial order throughout Africa, Asia and the Pacific was raised on its foundations. Accordingly, the damage caused by colonialism and the vast accumulation of wealth and progress it permitted in Western Europe and the US, still has its aftereffects. One prime example of this is the persistence of **neo-colonialism**, which Hoogvelt (2001:30) describes as "the continued economic control and domination over colonial resources even in the absence of direct political overlordship and administration". This indirect prolongation of the colonial system still takes place regardless of formal

recognition of political independence in emerging countries. Apart from being indirect, another key difference between this form of external domination and that which prevailed in the colonial times is that it is structural in nature, exercised predominantly through creating new constitutional structures that serve to lock in the power of market forces (Gill, 2003:167). By creating problems for global cooperation, this situation continues to create a sense of unease and *disguised mistrust* on the part of many developing countries towards the rich North and its global economic order, which is under US hegemony and on the G8 agenda. Many developing countries thus perceive globalisation as a project designed to serve the economic interests of this transnational capitalist class. Structural reforms, for instance, are viewed as programmes designed to open up developing economies to *free* market forces and global competition, advancing developed country interests and allowing them to dominate and wield forces in their favour. The fact that, although developing countries are dominated, they are also increasingly dependent on ex-colonial economic networks, complicates matters for developing countries and makes it difficult for them to respond counteractively (Castells, 2000a:268). While stimulating interdependency in the global economy, the new competitive paradigm – based on technological capacity – is underpinning dependency in an asymmetrical relationship which is, in fact, reinforcing historical patterns of domination.

Even though the northern regions dominate the world without (official) war, the world still remains conflict-ridden and increasingly in a state of **risk alert** (Mann, 2000:145). This becomes more apparent if one considers the following threats: conflict between potentially nuclear states such as Pakistan and India or even between Iran and the US; the instability of Russia and other smaller well-armed powers; the continuation of military regimes in the world; rising ethnic separatism (for example in Africa, Sri Lanka, Bosnia, Ossertia, etc.); nuclear weapons falling into the wrong (terrorist) hands, and the largely uncontrolled current spread of biological and chemical weapons through-out the world. Excluding the probability that militarism in all its variations will come to an end, these threats have become serious obstacles to the diffusion of transnational global networks that attempt to govern a largely unprotected global economy.

4.4.3 Westernisation, Islamic revolt and security threats

A key global concern pointed out by Held (2000:60) is that "culture flows are profoundly imbalanced, and dominant cultures are seen as threatening more vulnerable cultures". With the local becoming more globally integrated, it is essentially the imperial cultures of the West (primarily the US) that are engulfing cultures in much of the rest of the world in processes of homogenisation, the opposite of diversity. As a result, contemporary *global culture* does not draw, in any even or uniform way, on the vast diversity of cultures in the world, balancing and synthesising these. Carried by expanding global markets and driven by Western media and corporations, the new hybrid global culture is heavily weighted in one direction – from rich countries to poor. Such hybridisation has become a feature of globalisation, robbing cultures of much of their authenticity while making the search for the authentic almost an obligation. **Cultural imperialism** through increased Westernisation (or Americanisation) is thus fuelling the perception that globalisation is an extension and reproduction of existing economic inequalities between nations.

At the other end of the spectrum, forms of anti-Western and anti-American sentiment are developing, as manifested by the Islamic world's counteractive cultural assertion. With the total world Muslim population of over 1.2 billion (almost a quarter of the total world population), it is not surprising that their collective influence in opposing Western ideas and cultural influences have had ramifications that affected people globally (Huntington, 1996:213). As a source of serious global imbalance, the *friction* between the increasing global secular influence of the West and the continuing resistance by many of the 28 Muslim countries is showing ominous signs of build-up towards escalating global conflict, thus putting undue pressure on the global economy. Yet this situation is a natural consequence of the current Islamic resurgence and its reaction against what they call *gharbzadegi* or Westoxication of Muslim Societies.

The events of 11 September 2001 (or 9/11) and other fearful terrorist attacks are extreme examples of what can happen if these negative sentiments boil over and result in **extremist backlash**. Other such threats include possible biological or chemical attacks. However, the possible escalation and augmentation of this situation (and not merely in an

Islamist sense) poses an even bigger threat to the stability of world order and, by implication, the global economy. Many are convinced that *world disorder*[54] is on the rise and that this just adds to an already out-of-control global scenario, which is awakening fear and a renewed sense of insecurity in people (Brzezinski, 1993:8; Moynihan, 1993:76; Kaplan, 1994:61). This, and e.g., how the oil price reacts, affects people's participation (as consumers, investors, and workers) in the global economy.

The immediate and more identifiable concern, however, is growing Muslim anti-Westernism that has been paralleled by expanding Western concern with the *Islamic threat* posed chiefly by Muslim extremism. Regarded as a source of nuclear proliferation, terrorism, and often, unwanted migrants, Islamic fundamentalism is currently viewed as leading the way for other cultural groups that prefer to oppose Western influences. By overshadowing other sources of terrorism, Islamic revolt has thus become symbolic of much of the sentiment prevailing in other parts of the world (in particular in the East and the developing world) where there is an *outcry* for social coherence and moral community in a time of rapid global change. Yet, ironically, it is the West's democracy, especially in the neo-liberal period, that provides conditions under which forces of opposition and resistance can expand and prosper – and be mobilised against the system (Veltmeyer, 2004:186). This, at least in part, contextualises the global economy's volatile nature. Although there are multiple opinions on why there is an Islamic revolt against Westernisation, the view by Hoogvelt (2001:199) appears to be the most accurate. The author identifies its roots in mainly the **exclusionary effects** of Western globalisation that coincides with the West's blatant ignorance regarding these effects. The Islamic world's millions of people do not have much of a prospect of being incorporated into the new global system, and Muslim minorities in developed countries often find themselves excluded from the global system. Consequently, the contemporary Islamic crescent is driven by a politics of identity in response to exclusion. For them, this exclusion has a religious meaning and self-immolation becomes the way to fight against it. Perhaps the

[54] In sum, *world disorder* (or chaos) mainly refers to the breakdown of governmental authority and the break-up of states; the spread of terrorism and the proliferation of nuclear and other weapons of mass destruction; the intensification of ethnic, tribal, and religious conflict; the occurrence of massacres and ethnic cleansing; refugees multiplying into the tens of millions; the prevalence of financial market crises and other systemic risks; and the increase in international criminal mafias (Huntington, 1996:35).

most important **lesson** learnt from this situation is that it clearly illustrates what exclusion from modernity could cause. At present, the inherent danger and the risk of possible escalation is real, as is its potential to destabilise basic global economic activity.

As repeatedly emphasised by Washington and the EU (and the mass media), 9/11 ushered in a new era in which a new set of priorities, alliances and political relations are established (Veltmeyer, 2004:38). What makes this attack momentous is that it provoked an inter-state conflict, which marked the beginning of terrorism likely becoming a major source of international insecurity. October 7, 2001, therefore signalled the start of a major worldwide offensive against adversaries of the US under loose definitions of *terrorism* and *terrorist sympathisers*. Hence, the world is again (as was the case during the Cold War) divided and polarised, with alliances on the side of both the US and, in opposition this time, Iran. Accordingly, *Pax Americana*, under the Bush administration, moved from a more consensual and hegemonic leadership to one based on dominance and balance of terror. It is also becoming more evident that the current age of sacred terror is not just the age of Islamic terror. With religion – a core determinant of identity – becoming an increasingly sensitive issue as cultures are pressed to either adjust to or oppose Westernisation, more adherents of the great faiths and new, burgeoning cults are, according to Benjamin and Simon (2003:419), placing violence at the core of their beliefs. Given that religious violence is typically different from any other kind of warfare (e.g. for the true believer there is no compromise about the sacred), the threat of extremist attacks is not only more tenacious, but also quite contagious in terms of gathering global momentum.

By the same token, the **broader issue** of the *globalisation of organised violence* has serious implications for national and international security. Increased global disorder has rapidly been exploited by mushrooming crime[55] syndicates and other illegalities at the international level that thrive on the greater freedom of action as a result of reduced government control. With the privatisation of security and the availability of all kinds of surplus arms, states have lost their monopoly over organised violence (Held & McGrew,

[55] According to Castells (2000b:350), informational capitalism is characterised by the formation of a global criminal economy, and by its growing interdependence with the formal economy and political institutions. It includes an increasingly populated underworld of, very often, the socially excluded.

2000:12). National security has, paradoxically and out of necessity, become a multilateral affair. It is quite unprecedented that governments now have this common focus and purpose, which can only be realised if they join together and pool resources, power, technology, intelligence, and authority. As opposed to unilateralism, global and regional security institutions have become more significant as most nation-states are currently *signing up*, rather, to a host of multilateral arrangements and institutions in order to enhance their security.

The reality and concern, however, is that countries find it difficult to counter transborder networks of organised crime and violence. Drug smugglers, illegal weapon traders, terrorists, the activities of paedophiles, and illegal immigrants, for instance, do not recognise borders. Hence, coordinating national policies and military efforts to effectively combat these diverse threats are becoming an almost impossible task. Illicit trade in weapons, drugs, women and laundered money is escalating rapidly along with the international mafia network (e.g. links between American and Sicilian Mafia, Japanese yakuzas and Colombian cocaine cartels, the Russian Mafia and Chinese triads) (Abrahamsson, 2003:114). **Exploiting** the benefits of globalisation, organised crime, estimated to gross over $1.5 trillion a year, is rivalling MNCs as an economic power. The wealth of criminal organisations is used for corruption (as a very powerful instrument that, quite bizarrely, minimises their exposure to risk), in ways that undermine the foundations of good governance. Their networks are reaching deep and wide, increasing their ability to *criminalise* business, politics and the police – especially in countries with weak states. As a serious threat to human security, this has a severe destabilising effect in both rich and poor countries.

In addition, the rise in the number of civil armed conflicts, which are being fed by the global traffic in weapons, involving new actors and blurring political and business interests, are also a serious concern for global stability. In the power vacuum of the post-Cold War era, mercenary armies and military companies started to offer training to governments – and corporations. Accountable only to those who pay them, these hired military services are increasingly becoming a **severe danger** to the security of humanity

as a whole. Called *world society conflicts* or *new wars*, these civil armed conflicts burgeon due to increased disorder and illegalities, which, albeit with strong local dynamics, have a strong global presence (Abrahamsson, 2003:116). Apart from it simply being a source of instability in the world, the global impact of these wars is, by means of related flows of refugees and cross-border illegalities, to logistically sustain the warfare. They, in conjunction with terrorism, reinforce persisting global disorder and instability.

4.4.4 Social instability and governance uncertainty – a threat to capitalism

Social instability is often viewed as one of the most profound results of the weakening of traditional authorities, particularly the decline of the nation-state. According to Mazaar (2006:213), rising social instability has become one of the most obvious trends of the last 30 years. In its different forms, social instability can, among other methods, be measured in terms of crime (e.g. global illegal drugs trade), psychological distress, or bonds of trust and responsibility that become insecure. In addition, ferocious competition to replace traditional authorities in the social power structure, as well as the conflict between old and new values, is resulting in growing alienation and **social instability**. Accordingly, the struggle to find legitimacy for more individualistic authorities (including collective action groups/associations) is urgently becoming a key concern in the contemporary era – particularly since it has implications for how global governance should be re-structured and exercised.

Closely associated with social instability, **political instability** in both the developed and the developing world is taking the form of skepticism and even hatred towards governments and *old authorities* at unprecedented levels (Monbiot, 2004:75). The only difference is the effects: in the developed countries political instability leads to increased fragmentation of political parties and voters becoming more politically independent (non-affiliation with parties), while in many of the developing countries it may result in civil war. The advent of neo-liberalism has resulted in the final disembedding of the global system, which led to the political system losing vital parts of its social contract and consequently its legitimacy. With the erosion of citizens' confidence in the nation-state coinciding with its *retreat*, people's insecurity regarding which institutions will replace

many of its functions is mounting. Hence, combined with the fast change and uncertainty of the knowledge era, the decline of industrial-era authorities is starting to produce dangerous levels of social anxiety and unrest, giving rise to social tensions that threaten political stability and community cohesion. Ultimately and very significantly, the subsequent social disintegration is **threatening** the capitalist system.

The problem is that, currently, old authorities decay before appropriate new ones arise to take their place, creating a *governance disparity* (i.e. *void*). What is disturbing, though, is that pressing social problems are aggravated by the lack of appropriate governance solutions and social institutions whose response is slow and which are often corrupt and/or incompetent to provide answers for modern-day dilemmas. People tend to distrust social authorities. This trend then inflames the threat posed by extremist movements of anger and disaffection, and seriously complicates collaborative global governance because of the way in which it causes a rift between disparate groups of people. Huntington (2006:51) supports this view, pointing out that contact between people with different religious beliefs and other deeply-held values have often led to conflict. Two symbols, in particular, typically express these conflicts: the notion held by Islamic fundamentalism in especially Iran of the US as *the Great Satan*, and the erection by student protestors in 1989, in Tiananmen Square, China, of a replica of the Statue of Liberty. Lawson (2003:112) therefore emphasises that the high incidence of ethnic conflict appears to have made the current period less stable and less conducive to the maintenance of a peaceful world order than during the Cold War period.

In Gill's (2003:159) view, the present state of world order is one of disintegration/ integration: old economic, political and social structures are under stress or breaking down and social disorder and chaos characterise conditions in much of the world, while **new patterns of dominance** and supremacy are being reconstructed at the core of the system. This restructuring of power is occurring in a less consensual, more conflict-ridden and post-hegemonic world order, making fair global governance – the common need among especially developing countries – hard to attain.

4.4.5 Volatility of global financial flows – a prime source of global uncertainty

Over the past two decades in particular the world has, as Scholte (2002:189) points out, "experienced continual problems with heavy transborder debt burdens, major disruptive swings in foreign exchange values, a perpetual roller-coaster in the securities markets of global financial centres, and a string of crashes among global derivates players". This inordinately volatile nature of current global financial markets is among the main causes of economic fluctuations and insecurities that lead to excessive investor and country risk. For developing countries this is of particular concern because of the fact that volatility in capital flows contributes to a more volatile macroeconomic environment, which is mainly due to the *pro-cyclicality* of capital flows and their restricted market access (Dos Reis, 2005:197).

In reality, the more financial markets become integrated, the greater the associated **contagion effect** whereby an economic crisis in one region rapidly acquires global ramifications. Since the late 1980s many securities markets have meandered through highly unstable routes. More harmful instabilities came from dramatic speculative swings in foreign exchange values (e.g. the European exchange rate mechanism in 1992) and the swift withdrawals of cross-border investments, especially over the short term (e.g. the crises in Latin America, East Asia, and Russia in the late 1990s). In addition, the global derivatives market continued to suffer a series of catastrophes: the Metall Gesellschaft and Orange County affairs in 1994; Barings in 1995; Sumitomo in 1996, the East Asian meltdown and Long-Term Capital Management in 1998, the end of the IT boom, and the 2008 financial crisis, involving the failing a number of major US banks.

However, much of the origins of financial market instability can be traced to a couple of decades ago. The drastic increase in international capital flows (especially FDI) since the 1970s, together with the associated process of mergers and acquisitions as well as the restructuring of capital in terms of its shift towards developing countries, have moved the conditions of a **systemic crisis** from the North to the South (Veltmeyer, 2004:19). Significantly, this has led to an increase in the flows of short-term speculative capital to the developing countries, which coincided with a weakening of economic conditions in

this part of the world (e.g. slower growth and more crises and poverty) and an economic convalescence in the developed world. As a result, there is, even more so today, a greater concentration of ownership of the world's productive resources and a perturbing degree of volatility in international capital flows, which can largely be ascribed to increased financial market deregulation. The harsh reality is that no single country can today withstand the negative impact of excessive financial volatility and its accompanying economic insecurity, re-emphasising the fact that concerted global action is needed to prevent and manage this source of uncertainty.

Moreover, a fascinating point made by Chomsky (2004:147) is that the liberalisation of capital tends to undercut democracy. The free movement of capital creates a kind of *virtual Senate* with veto power over government decisions, which dramatically restricts policy options. With private interests prevailing, voters and speculators, in this sense, conduct moment-by-moment referenda on state policies in both rich and poor countries alike. As a result, countries increasingly have to compete for – in most cases – footloose and fancy-free capital under conditions of highly uncertain global economic governance arrangements, which, in the absence of proper regulation of international capital flows, **causes instability** in the global economy. In fact, with the world economy rapidly becoming more interdependent the sensitivity of the situation is heightened to such a degree that writers such as Harvey (2000:90) exclaim that: "the world's financial markets are on the boil in ways that make a snap judgment here, an unconsidered word there, and a gut reaction somewhere else the slip that can unravel the whole skein of fictitious capital formation and of interdependency". In view of that, the possible implications of the deficiencies of private capital markets are a central concern *vis-à-vis* global interdependency because of their potentially long-term destabilising effects (Bird & Joyce, 2001:78). This suggests that with highly volatile global financial flows being an acute source of global instability, the need for a progressive regulatory framework is presently becoming one of the principal and most sensitive challenges in global economic governance. The referred possible implications – which are known to have happened in the past – include:

- reduced global economic welfare;

- capital that is inefficiently allocated throughout the world;
- capital markets that become more unstable and that coincide with a high incidence of balance-of-payments crises;
- some governments (in the developing world, in particular) possibly become unable to pursue macroeconomic policies based on domestic needs, and
- poor countries are being deprived of external finance, affecting the quality of life of millions of people.

4.4.6 Reservations about the market – can it be trusted?

Many countries have a strong disbelief in allowing society's welfare and a country's position in the global system to be predominantly determined by the market. Due to its potential harmful effects, some developing countries have during the 1990s reacted with resentment against expectations towards them to rely almost wholly on the market (Gilpin, 2002:242). In defiance of free market ideology, Malaysia, for instance, imposed capital controls, and South Korea strongly opposed demands by the US to liquidate the *chaebol* form of industrial organisation. In addition, developing countries are generally concerned about the inability of the market to close the gap between rich and poor countries, following the removal of the demand for a New International Economic Order (NIEO) from the global agenda due to the shift in favour of a more neo-liberal policy – which made the market and private investment flows the preferred conduits through which the gap should supposedly be closed.

Polanyi (1957:181), a critic of the *market utopia*, warned against the "hazards of planetary interdependence" associated with global market expansion. In this view, a market system is considered a fragile arrangement that, especially when based on pure liberalist principles, can easily get out of control and lead to large-scale global economic instability – particularly as the profit-motives of market players get out of hand. The risk of market failure is, today in particular, a growing potential reality in light of increased market liberalisation (e.g. persisting neo-liberalism) and growing global economic interdependence. This, though, was planned because ever since the market gained a hegemonic position at the conclusion of the Cold War, the stage was set and the global

agenda pushed for a truly liberal global order. Sadly, this trend does little to beget a more secure and stable global economy.

In Barber's (2000:23) view, there is a brutal *Darwinian logic* about markets in that they are both nervous and greedy. They look for stability and transparency, yet they reward that which is often less than democratic. One prime example of this, and against which serious insurgencies are raised, is trade liberalisation in the West – particularly when considering how larger trading partners are exploiting smaller ones, benefiting at their expense. In addition, the current trend towards bilateral and regional trade agreements – as pushed by the WTO – is having serious negative trade-diverting effects that increase the cost of production. Even Keynes (1933:761), before the Second World War, questioned the value of free trade due to it having the capacity to create scope for unfair trade. He regarded a certain degree of national self-sufficiency as a precondition for international political stability, denouncing the "decadent international capitalism" of his time. However, with the asymmetry problem currently coming increasingly into effect as markets expand, governments and countries are becoming less self-sufficient and more dependent on each other, thus creating an underlying sense of **insecurity** in the global political economy as this is almost the *last line of defense* in trying to govern the market.

4.4.7 Contradictory international developments

Although globalisation and regionalisation are mostly complementary processes, there is also, quite often, a significant degree of conflict between **globalising and regionalising forces** and the interests concerned (Hoogvelt, 2001:230). This is especially illustrated in the case of regional trade integration versus global trade liberalisation: countries want to derive benefits from, and protect the welfare of the regional grouping (e.g. through trade and capital restrictions), but are expected to abide by globalising tendencies to avoid being isolated. This results in tension between global and regional governance. In this sense, according to Held and McGrew (2000:22), there is an acknowledgment of growing tensions between the rule-making activities (and authorities) of multilateral bodies, such as the WTO, and regional bodies such as the EU or African Union (AU). The WTO and other IGEGs attempt to promote *open regionalism*, emphasising the neo-liberal creed of

liberalisation, privatisation and open markets. This is often contradictory to the emphasis by regional bodies on *new regionalism* as a process from within, which is mostly endogenous to the respective region. One example reflecting this variance is the regions' use of tariffs and non-tariff barriers to trade to rather restrain the liberalisation trend, enabling local industries to become more globally competitive. The more these two spheres overlap and clash in terms of having divergent objectives, the greater the destabilising effect on the global economy. With the EU, for instance, representing the most advanced regional arrangement the world has seen, this danger is most evident in that Europe's integration process is viewed as possibly a threat to the global trade system (Hettne, 2000:159). What is more, its widening effect is signified by the fact that *Fortress Europe* is regarded as a good model or pretext for organising other regional trade systems such as NAFTA, the East Asian Economic Caucus and even the AU.

The countries of the North are exerting more pressure on those of the South to liberalise. This, however, presents a serious **contradiction** as neo-liberal regimes and policies are pressed in the wake of declining export prices (of coffee, metals, sugar, textiles, clothes and other goods produced in the developing world) and capital inflows that are drying up (Petras, 2004:49). In concurring that globalisation appears to increase poverty and inequality, even the World Bank (1999:46) stressed that the costs of adjusting to greater openness are borne exclusively by the poor – regardless of how long the adjustment takes. Making matters worse, developed countries have responded by raising protective tariffs at home and increasing export subsidies. Sadly, variations of this form of unfair trade are still the order of the day.

Furthermore, with neo-liberal economic reforms coinciding with increased emphasis on democratic regimes during the 1990s in particular, an embedded contradiction emerged more distinctly: these reforms essentially **undermine** effective democracy by allowing markets (which often generate inequitable effects) to overwhelm nation-states – the holders of power that represent the people (and are held accountable to them), and through which decision-making power is (directly or indirectly) exercised, by the people. It is therefore not surprising that several studies monitoring political attitudes, according to

Chomsky (2004:151), found that many people from countries around the world often have a *feeling of powerlessness*, stating that they have little/no influence on what government does. This tendency is rising sharply throughout the neo-liberal period. The above contradiction is further evident, according to Veltmeyer (2004:169), in that "the idea of democracy has served as an ideology, to obfuscate and camouflage the interior design (and *fascistic fist*) of the imperialist project". This suggests that, whereas democracy is commonly presented by the US and other rich countries as a system that promotes equity, it actually allows them to stay in control of how global order is evolving.

An interesting and relevant line of reasoning is Barber's (2000:21-24) view that the planet is caught between an allegorical Babel and Disneyland: paradoxically, it is falling brusquely apart and coming reluctantly together at the very same time – a sort of *creative chaos*. In describing the co-existence of two opposite forces, Jihad and McWorld, the author points out that the increasing struggle between them is creating a world that seems, to a significant extent, out of control. The description of *Jihad* (or holy war) is used to signify a retribalisation of large swaths of humankind by war and bloodshed as cultural conflict increasingly dominates a new post-Cold War world characterised by great divisions between humankind. It opposes the numbing and neutering uniformities of industrial modernisation and the colonising culture of McWorld. It is a defence of indigenous national or religious traditions around the world, producing a variety of movements. *McWorld*, therefore, signifies Western and corporate forces that are pressing nations into one homogeneous global *theme park*, linked by communications, information and commerce. Yet, ironically, there exists a powerful and **paradoxical interdependence** between Jihad and McWorld because while they oppose each other, they in a way need each other to become stronger. Jihad not only revolts against but abets McWorld, while McWorld not only imperils but re-creates and reinforces Jihad. They thus produce opposites and strengthen each other. Intriguingly, in opposing each other, they seem to work to the same ends (i.e. the demise of the state) – working in apparent tension, yet in covert harmony. Although they are operating with equal strength in opposite directions (Jihad is driven by parochial hatreds and McWorld by universalising markets), they, in effect, do appear to have something in common: *anarchy*.

This is exemplified by the fact that both are making war on the sovereign nation-state, the formal institution at the centre of the current world order. Governments are intimidated by market ideology and are in retreat as justice yields to markets[56] due to, on the one hand, McWorld's creation of global markets rooted in consumption and profit that are guided by the market's untrustworthy invisible hand, and on the other, Jihad that forges communities of blood rooted in exclusion and hatred, communities that discard democracy in favour of tyrannical paternalism or consensual tribalism. Neither McWorld nor Jihad aspires to re-secure the civic virtues fragmented by their denationalising effects, i.e. the confrontation between *global commerce* and *parochial ethnicity*. Nor do they service public goods or pursue equality and justice. It is therefore difficult to believe that the continuous clash between Jihad and McWorld will result in some overriding good. In fact, it is becoming more obvious that the threat of their turbulent interplay is creating a climate of instability and disorder, which amplifies the fear that the world does not have a sufficiently strong centre or axis (e.g. in terms of well-coordinated supra-national governance) – so to speak – and that mere anarchy is let loose upon the world.

4.5 Conclusion

It is clear that a number of factors with a variety of facets are hampering both the process of global economic governance and that of global governance in the contemporary period, thus making the **governance challenge** monumental. The chapter considered a number of uncertainties and imbalances that are key sources of instability in the global economy and thus of particular concern for its governance arrangements. One crucial issue is the asymmetry problem and how it implicates some of the other factors identified. On the one hand, it gives scope for the emergence of new actors of authority on the international scene, allowing a more distributed form of (multi-layered) global governance, while on the other, governments are engulfed by the market, having gradually less control (in terms of market intervention) over something that is highly volatile and prone to failure. The net effect of all this is that it creates rising governance uncertainty, which is an unhealthy scenario for the global economy.

[56] This is taking place due to the growing global influence of the *liberal modern project*. What was once appreciated as protecting the public interest is now excoriated as heavy-handed regulatory browbeating.

Hence, countries are gradually coming to terms with a major concern, namely that the neo-liberal ideology of liberalisation, deregulation and privatisation is eroding national governance at such a rate that sufficient mechanisms for effective global governance that could fill this **governance void** are not in place. Nor are there other appropriate institutionalised forms of governance. This is a cause for concern that seriously hinders the current transitory phase. An even wider and unnerving context of this concern is that most governments[57], which are also vital to a stable world order, are to a large extent unable to deal with many of the problems/factors mentioned in this chapter. In addition, while many such governments are engaging in collaborative arrangements to counter this effect, a serious *contradictory concern* pointed out by Kahler and Lake (2003:24) is that the more economies become integrated, the more this drains political authority from states (shifting it to supra-national institutions, NGOs and MNCs), thus threatening national democratic processes.

It must be noted that the asymmetry problem is not – at this stage – a cause for major concern for certain (rich) countries in that they use the neo-mercantilist practice of *new imperialism* to derive benefits from how most of the other countries are adversely affected by this problem. Accordingly, some state policies (e.g. those of the US and some of the other imperial members of the G8) dictate and direct economic exchanges and limit the market's role to a subsidiary one – all to the advantage of the imperial economy (Veltmeyer, 2004:49). This, then, gives impetus to the perception that neo-imperialism is viewed as the projection of state power under conditions of a renewed form of US-led imperialism. Hence, with both effects co-existing – the governance void, indicating the lack of a proper governance structure in the world economy, and neo-imperialism, indicating too strong, but inadequate, forms of selective governance (e.g. the G8 and MNCs) – there is an increasing imbalance, which seriously incites global instability and erroneous governance. Importantly, the added concern is that this is worsening the global economy's exclusionary effects, particularly as regards **Africa** and its marginalisation.

[57] The emphasis here is on most of the governments outside the G8 (mainly the developing world) – those on whom the governance void has a much greater effect due to their increased *defenselessness* against global governance uncertainty and global inequality concerns. This is in contrast to the imperial members of the G8 that are *guilty* of exercising neo-imperialism and using it to their benefit (Veltmeyer, 2004:4).

Another crucial issue is the precarious mixture of **global inequality** and social exclusion. The widening disparities between rich and poor countries are a very serious concern for global economic stability – a concern that is receiving unsatisfactory attention. In fact, the most serious challenge for the global economy in the coming years is to make globalisation compatible with domestic social and political stability (Rodrik, 2000:323). This means that it should be ensured that global economic integration does not contribute to domestic social disintegration, which includes not only the worsening gap between rich and poor, but also the rise of civil strife and military conflict. In fact, the divide between the welfare states in the North and the developmentalist states in the South is threatening to evolve into a large-scale global catastrophe. A concern for developing countries, in particular, is the fact that trade and capital liberalisation are collaborating to promote global interdependence in such a way that both are presenting them with a dangerous level of vulnerability (Varma, 2002:3). Salient features of the global economy such as increased volatility, contagion, and exclusion (or marginalisation) are not only putting them in an *adverse position* (e.g. in the case of Africa), but also pose serious challenges to the current institutional arrangements of **global economic governance** with regard to providing greater protection for developing economies.

The dominion of global corporations together with the powerful role played by the G8 in global governance are aggravating concern about global inequality (Leech & Leech, 2005:260). The concern with the G8, in particular, is that their strong influence in the IMF, WB and WTO together with the growing emphasis on multi-layered global governance are creating vexing **governance uncertainty** and are dividing the world between superior leaders (the G8) and subjected followers (the rest, but mainly the developing countries) – whereby the latter have very little control over the direction of global governance or their inclusion/exclusion in the relevant decision-making processes. Given the internationalisation of the state and the transition towards a multi-layered system of global governance, the world is moving rapidly towards an *apolar world order*, with increasing elements of disorder, beset with various imbalances and instabilities. As has been pointed out by Gill (2003:160), the advent or occurrence of global structural change during the post-Cold War period in tandem with an increase in global imbalances and

uncertainties has produced a type of *institutionalised chaos*, which is propelled by the restructuring of global capitalism. While it is accelerating changes in production, finance and knowledge which rise to new patterns of change, it is particularly the upsurge in the structural power of globally mobile capital that entailed alarming instabilities. This emerging world order can, in contrast to the 1950s and 1960s, be recognised as being ridden with deepening **social inequalities** within and between countries, harsh economic conditions for most parts of the world, and a lack in global security structures. These changes entail great benefits for the strong countries, largely at the expense of the weaker ones. This, according to Mazaar (2005:236), is in fact the result of a world that has moved from a history of periodic authority crises into an era involving a persistent crisis of authority. In this view, the contemporary era is but a continuation of the struggle between different groups personifying different kinds and degrees of authority. It is now just more intense, more brisk, and more constant than previously.

The **great irony** of all this is that the more liberal the world becomes, the less free (and more insecure) it appears to be due to the resultant binding hold of global instability and inequality. Liberalism was at its brink in the world just prior to World War I. Since World War II the world has, again, become gradually more liberal, thus coinciding with more/further *chaos* and creating scope for greater imperialistic dominance. It is clear that if all the factors or sources of global instability are not well managed and sufficiently taken into consideration in a holistic global governance approach, more disorder will be the order of the day. Their global effects are undeniably increasing exponentially, thus necessitating radical remedial action by means of a coherent approach. Apart from pointing them out, the chapter has brought attention to the inherent danger of the *non-governance* of these factors for the global economy.

In the following chapter, while still examining problem-areas germane to the focus of this study, the attention is turned to concerns pertaining to global inequality of which Africa's marginalisation is, perhaps, the most significant part. In effect, Africa's diminishing role in the global economy and the implications of it losing ground in global decision-making will be investigated.

Chapter 5

Africa's marginalisation: Debates, evidence and the linked role of global economic governance

5.1 Introduction

As the post-Cold War era is gaining momentum and a global shift of focus is transpiring, many low-income countries are seriously concerned about the major powers that are slowly withdrawing from developing world socio-economic concerns (Saxena, 2001:330). With the problems in the Middle East capturing global attention, this confirms the fears of many Africans that the end of the bipolar confrontation could reinforce Africa's marginalisation and isolation in the world economy. Whereas Africa[58] was intensely tied into global processes and structures, initially by colonial intervention and later by Cold War ideological links, it has in recent times, according to Deng (1993:33), become predominantly dislodged from this earlier interdependency. In fact, it is argued that the September 11 attacks and their aftermath drove home to Africa its marginalisation and its lesser global significance in a new era dominated to a large extent by concerns over global terrorism and instability in the Middle East (Nnaemeka, 2003:601). More specifically, it is becoming apparent that the way in which contemporary globalisation and global economic governance is progressing has made these two processes prime catalysts of Africa's intensifying marginalisation over especially the past two decades. Globalisation has deepened global economic integration among the rich developed economies at the virtual exclusion of relatively poor regions such as Africa. Global economic governance has promoted policies (not without mechanisms of coercion) that have adversely affected African economies.

It is disturbing to note that the rise of global economic inequality coincides with the marginalisation of regions not considered attractive trading partners and/or *efficient* recipients of investment. Africa ranks among these regions. According to Soludo (2001:50), it is "caught up in a vicious web of social exclusion, poverty, technological backwardness and deficient institutions". Africa is therefore faced with the immense task

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[58] Although referring to Africa as a whole, the intent is not to generalise but to convey a collective view of Africa. The study recognises that there is considerable variation among African countries.

of becoming not only an active participant, but also a respected competitor in the global economy. In taking up this challenge, it is important to identify the extent of, and find a strategy to counter the continent's marginalisation. This chapter investigates the first-mentioned issue (chapter seven will consider the strategy) and aims to examine the sources and severity of Africa's marginalisation. While there is some consensus over the consequences of the continent's marginalisation, its causes have elicited polarised debate. In investigating both the debate and the evidence of Africa's marginalisation, this chapter attempts to answer the extent to which the continent has been marginalised within the global system. First, the debate will shed light on the sources of Africa's marginalisation and, secondly, the evidence attempts to quantify the comparative extent to which it is marginalised. The evidence will thus provide a valuable perspective on Africa's comparative position in the world economy, which is essential for future strategising. In seven sub-sections, the evidence will focus on economic growth and poverty; trade performance and trade restrictions; foreign investment in Africa; globalisation and technology advancement; debt and aid; the level of human development and the progress made in reaching the Millennium Development Goals (MDGs); and finally, Africa's governance performance. Prior to all the above, however, a section will attempt to clarify and delineate what is meant by Africa's marginalisation. Before concluding the chapter, one section is devoted to investigating the nature of the link between global economic governance and the continent's marginality in general as well as evaluating the implications of Africa's marginalisation for the developed world, in particular. As a whole, the chapter provides a comprehensive account of Africa's underdevelopment, which could be regarded as both a cause and an effect of its marginalisation.

5.2 Defining and interpreting marginalisation

Young (2000:35) defines marginalisation as *"exclusion from meaningful participation in society ... due to a lack of accommodation, which is proving to be one of the most dangerous forms of oppression"*. It also means to relegate to an unimportant or power-less position within a society or group (Merriam-Webster, 2008:1). According to Held (2000:90), marginalisation is "the way unevennesses in economic developments are made manifest by pushing certain economic actors out of the heart of economic development

and into subsidiary and subordinate peripheral positions". The words *exclusion*, *oppression*, *relegate* and *pushing* seem to paint a clear but demoralising picture of how marginalisation is the direct and/or indirect result of maltreatment and exploitation for no legitimate reason. Mullaly (2007:252) argues that marginalisation commonly results in severe material deprivation and that individuals often face marginalisation due to dominant discourse(s) within the structures of society. It can even lead to the extermination of groups. Marginalisation is unjust because it obstructs the opportunity to exercise capacities in a socially defined and recognised way, while inhibiting economic and human progress. The New Partnership for Africa's Development (NEPAD) recognises the reality of Africa's marginalisation by underlining "Africa's peripheral and diminishing role in the world economy" (Gibb *et al.*, 2002:10). In addition, the study identifies the **marginalisation of Africa** as the continent's continuous omission from full-scale participation in the global system as well as the structures of global economic governance, for reasons pertaining to Africa's failure to properly integrate itself into the global economy; its deliberate and/or unintentional exclusion from mainstream global economic activity, and its restricted prominence and involvement in processes relating to the governance of the world economy. Although this chapter examines Africa's marginalisation from an economic perspective, the intention is not to restrict it to merely economic marginalisation, but to contextualise this specific emphasis in the broader concept of marginalisation. Furthermore, whether marginalisation – as will be observed in the following sections – is the result of intentional or unintentional actions (or even non-actions) by whomever, it is still considered marginalisation because it involves a calculated decision. The crux of the concern is not only Africa's marginalisation from the rest of the world, but the marginalisation of Africans in the development of Africa.

5.3 Debating the causes of Africa's marginalisation

The debate involving Africa's marginalisation has, over the past three decades, become intense as the search (or hunt) for its root causes is reaching extreme proportions. With this thorny issue moving up agenda lists, it has become evident that while perceptions in this regard vary, these are mainly divided into two camps known as the *externalist* and the *internalist* explanations. It is disappointing to note that at times the debate runs the

risk of giving rise to some form of *blame game*. It is important not to lose sight of the fact that the intent should be to pay attention to how opportunities for Africa to participate meaningfully in the global economy are negatively affected, and how such opportunities could constructively contribute to Africa's de-marginalisation. This is the underlying purpose and focus of this section.

5.3.1 The externalist explanation

This explanation essentially holds the industrialised countries responsible for Africa's underdevelopment. It is argued that ever since its birth, capitalism – a world market and system of value production that underpins the current global system – has been a globalising system in which political and economic power has played a key role in gaining advantages, exploiting inequalities, and crushing competition. Its strongly non-egalitarian nature originally manifested when the Industrial Revolution in the North was tied up with the exploitation of Black bodies and when the triangular trade between Africa, Europe and the Americas became an *unequal exchange of unequals*. With the latter still characterising trade between Africa and the North, Africa has, as Gibson (2004:5) argues, "become marginal and marginalised partly through its centrality and integrality to the birth and development of modern capitalism".

Cognisant of the many vibrant economies that existed in Africa prior to colonisation, the externalist view impugns the dark shadow cast by colonial rule and the slave trade over the continent's history as this period signalled the **start** of its marginalisation. Lasting for almost 400 years since the late 15th century, the slave trade had serious debilitating effects, leading to Africa's underdevelopment. During the colonial period, as Africa was leisurely opened up to the competitive "commercial winds of the world", its economy underwent a deformation that resulted, according to Saxena (2001:427), in three constituent sectors: the subsistence sector; the indigenous monetary sector, and the foreign enclave. The latter occupied only 2% of the African population, while 75% to 90% of the population toiled ceaselessly for subsistence survival. The warped pattern of colonial development eventually left the continent with a situation characterised by a lack of regular

production of marketable surplus; a lack of specialisation on a significant scale, and static technology. This culminated in an underdeveloped continent with three basic features:

- unevenness of productivity between sectors;
- disarticulation of the economic system, and
- foreign domination (e.g. structural adjustment programmes (SAPs)).

It is also believed that the *colonial hangover* undermined the **enabling capacity** of African countries. One such example is state weakness in Africa, which has its origins in the inter-state system established by the colonial powers (Herbst, 2000:71). This system continues to provide little incentive for states to develop the capacity to mobilise financial and human resources in order to augment defences against external threats. Another example of such undermining is African countries' discontent with the industrialised nations which, after making significant reforms, did not realise their commitment to devote 0.7% of the GNP per annum to development assistance in Africa (Mwakikagile, 2004:101).

Many Africans view neo-liberal globalisation as simply the **latest form** of capitalist penetration into Africa, which reinforces the continent's marginalisation within the global system. Varma (2002:11) argues that, as many African countries are classified as least developed nations, the benefits of trade liberalisation have yet to be seen as they continue to be marginalised from the international trading system and have experienced a decline in their share of world trade. The externalist explanation therefore blames the developed nations and their trade and aid policies towards Africa. For decades African governments have pointed to the developed countries that continue to protect agricultural exports, a sector in which the continent ought to be best able to compete internationally (Cheru, 2002:91). In addition, the intermittent dumping of surplus agricultural products on markets in Africa ruins prices for local farmers. With aid, the major concern, according to Collier (2007:121), is that "it exacerbates the problem of breaking into global markets for new exports". Aid has a *Dutch disease* effect in that it causes a country's currency to rise in value against other currencies which, like natural resource revenues, tends to make (other) exports non-competitive. This is a concern for African economies because aid

tends to retard the growth of, in particular, labour-intensive export activities, which are required for export diversification. The externalist explanation believes that this suits the rich nations as African nations can at best only remain primary producers of raw materials for the developed world and continue to be a *dumping ground* for cheap manufactured goods.

The externalist view also argues that Africa's economies are **made more vulnerable** and prone to crisis and economic collapse due to external shocks such as unsustainable levels of debt service repayments to creditor countries and institutions, declining commodity prices, soaring interest rates, and Western protectionism. A classic example of the latter is in the field of trade. In working towards increased trade liberalisation, Africa has been stung by the unfair trade practices of many developed countries. In fact, this has more than offset the crucial role which trade is supposed to play in facilitating African economic and social development. Western subsidies have depressed prices and resulted in massive export losses for African producers (Robinson, 2005:1). These losses, in turn, have made many African economies more vulnerable by trapping them in a cycle of poverty and dependence on foreign aid.

The externalist explanation also criticises the narrow idea held by the Bretton Woods institutions[59] that economic reform was not only necessary but also sufficient to address the problem of Africa's slow growth (Gibb *et al.*, 2002:24). However, it was painfully recognised in the 1980s that this approach was risibly inadequate, due to the dismal failure of policies to generate economic growth. Instead of stemming Africa's economic decline, harmful and unsuitable **policy conditions** put many of the continent's economies at a disadvantage.

5.3.2 The internalist explanation

By basically blaming the victims, this predominantly *Northern* or *developed world* perspective criticises why Africa finds itself marginalised from most of the rest of the

[59] The links between these institutions and Africa's marginalisation will become clearer in section 5.5 – especially regarding the role SAPs played in (economically) peripheralising many African economies.

world, identifying the **continent itself** as the main culprit for its underdevelopment. It argues that African countries were better off during the first decade of independence (in the 1960s) than they are today. Mwakikagile (2004:98) asserts that "besides the former Belgian Congo and a few other hot spots, they had less chaos then than they do today". As part of Africa's decolonisation process, before the 1980s, domestic policies hostile to foreign-owned firms, the private sector, the export sector and foreign capital were regarded as part of the continent's Africanisation process. The subsequent retreat of the foreign-controlled private sector led to sharp reductions in capital inflows as well as the shrinkage of production and export volumes (Collier, 1995:543). It is also argued that in and after the 1980s the reversal of government policies through SAP reforms largely failed because these policy reforms have not gone **far enough**. In addition, policy discrepancies such as higher rates of corporate taxation and policy disparities such as the neglect of infrastructure for the productive sector impede African economies from becoming more efficient. Reform has proved to be insufficient because, although slightly narrowed, the gap between Africa and the advanced economies still continued to exist as Africa was unable to compete with economies that place a higher value on export success and foreign investment inflows. Africa was thus not in a position to benefit from globalisation. In the end, according to this perspective, Africa's mainly poor economic performance and the exploitative practices of African elites should be blamed for structural adjustment not reaping the benefits it should have.

A serious concern regarding foreign investment interest, in particular, is Africa's **high-risk environment** which, in itself, is to a large extent responsible for the continent's marginalisation. This is a serious constraint on Africa's economies which makes them not only more volatile and unpredictable than other regions, but also more vulnerable. The risk of doing business on the continent is too high, mainly because of the unusually high common risks. Reflecting not only on why there is a lack of investment attractiveness but also on the general vulnerability of Africa's economies, the most prominent risks include:

- *Erratic policy changes.* Although all governments occasionally make adjustments to their economic policies, such changes are predictable because a policy rule is being followed. In Africa, however, too many policy changes generate

undue risk because the policy rule itself is subject to change (Mwakikagile, 2004:104).

- *Defective policies.* Indiscriminate state interference and inappropriate macro-economic and trade policies have, as Cheru (2002:94) argues, exacerbated inherent food insecurity in many African countries. High export taxes, restrictive exchange rate regulations, and overvalued national currencies (making export products less attractive and less competitive in world markets) have historically damaged rural economies, thus undermining agricultural productivity.
- *Poor governance.* African countries have suffered severely from political instability and ravaging dictatorships which have, in most cases, led to large-scale economic mismanagement. Based on a system of patronage and personal accumulation, governance in many African countries was (and is, e.g. Zimbabwe) characterised by the state's inability to provide a political environment conducive to economic growth and development. As a result, governance in Africa has very often been unaccountable, non-transparent and undemocratic, and led to corruption growing out of control, thus undermining development. On the Corruption Perception Index of Transparency International, developing countries are scoring worse than industrialised countries, with Africa ranking at the bottom of the list (Luiz, 2006:633). Being a disincentive for foreign investment, corruption also raises transaction costs, increases uncertainty and insecurity, and emasculates government actions. Poor governance can also be attributed to the prevalence of civil war and conflict that have plagued many African countries. Easterly and Levine (1997:1205) assert that ethnic fractionalisation and conflicts, to a large extent, account for Africa's growth tragedy and underdevelopment. The internalist view believes that, although the majority of African countries co-exist with the 21st century, their reality is 14th century civil war, plague and ignorance.
- *Vulnerability to world price fluctuations.* Due to Africa's high dependence on a few primary commodities for export, its economies are more susceptible to dramatic movements in world prices. As a result, trade restrictions effectively increase exposure to external shocks, thus limiting options to counteract.

- *Weakening of agencies of restraint.* Contract enforcement is the foundation of reliable business relations. However, in Africa, both civil legal systems and audit systems have too often been less than incontrovertible (Collier, 1995:551). Weak agencies of restraint have a direct and an indirect impact on Africa's marginalisation. Directly, weak judiciaries and accountancy practices result in a rudimentary financial system. Indirectly, they make the high-risk environment even riskier by means of weak systems of policing and weak central bank management, resulting in macroeconomic policies that are prone to abrupt changes.

It is obvious that much of what is mentioned above is the result and/or cause of the broader problem, namely Africa's long catalogue of **mismanagement** – particularly in its economy (Gibb *et al.*, 2002:9, 24). In this respect, the internalist view mainly blames the continent's high debt burden; a deformed public sector; under-utilisation of human resources; vast unemployment; concentration of ownership in the hands of a few, and large-scale income and social inequalities for marginalising the majority from economic activity. The weakness of the state in Africa is considered the underlying dilemma *vis-à-vis* its problem of mismanagement. The inability to establish and maintain an institutional framework for the effective regulation of political and economic activity is chiefly to blame as political reform is regarded as a prerequisite for sustainable economic reform. Partly explaining the lack of economic growth, a key problem with state weakness in Africa is the non-mobilisation of the resources needed for the development of governance institutions that ought to be accountable and responsive to the delivery of public goods and services in return for resources provided by citizens. Many African countries are believed to be dominated by a neo-patrimonial mindset that subverts depersonalised practices (such as predictability of administration and uniform application of rules), leading to personalised spheres of power and influence, and the comprehensive use of patronage.

Efforts at promoting economic development in Africa by making states act collectively have consistently failed, predominantly because heads of state **refuse to sacrifice** any degree of sovereignty. This is also regarded as a *failure of the state* because – as in the case of the Lagos Plan of 1980 – many African governments afterwards ignored their

policy commitments, i.e. commitment to collective action. This was followed by increased globalisation in the 1990s, making much-needed political reform significantly more difficult. Another failure of the state has been the high dependence of African nations on foreign aid to fuel their economies. African governments made the mistake of pursuing economic development strategies that were more externally than locally based.

As far as the internalist explanation is concerned Africa only has itself to blame for **not transforming** the enabling mechanism of *human capital development* into a competitive edge (Saxena, 2001:425). More needs to be done to improve workers' skills. In fact, the combination of a lack of available African technical and managerial skills, as well as corrupt bureaucratic and political set-ups undermine any development initiative from the top. Hence, without an adequate middle-rung productive machinery, very little is contributed towards building links to the existing domestic resource base. In addition to a lack of skilled labour (plus Africa's brain drain) and the low levels of education, the lack of infrastructure and poor transportation and communications are regarded as part of the reason why Africa is responsible for its own underdevelopment.

Another capacity issue is the fact that Africa is marginalising itself from the global economy by **not keeping up** to date with technology. Although the continent is an excellent platform from which to launch initiatives to close the gap between itself and the developed world, more needs to be done in terms of comprehensive investment and development skills development, especially in the technology sector. According to the internalist explanation, this is potentially the cause of Africa's ultimate marginalisation (Luiz, 2006:637). Being able, at least, to follow and keep pace with technological progress elsewhere by utilising what is on offer in current advanced economy production processes, for instance, has significant value and could stem the gap from widening. However, as a player on the world stage, Africa is presently not even in a position to be a follower because it is not in the game, i.e. not even close to employing full production capacity.

5.3.3 Finding the balance

While there is some degree of exaggeration due to the emotive nature of the issue of Africa's marginalisation, both perspectives are valid and find significant **common ground**. They agree on the following key areas: the importance of good governance (economic and political); capacity-building (human and production); improving living standards; capital inflows and its productive use; a free and fair international trading system, and more say in how global economic governance is exercised. The debate over Africa's marginalisation has also led to both sides starting to **accommodate** each other's views. Institutions such as the World Bank and the majority of Western donors now give recognition to the influence of exogenous factors, such as debt structures and terms of trade, on the performance of African economies (Cheru, 2002:91). Similarly, African policy-makers now realise the debilitating effects of poor domestic policies and institutional failures as they are facing a crisis of the state in Africa as well as a growing demand for democracy by its own people. Although no real consensus regarding an alternative development route for Africa is emerging, it is encouraging to see a growing willingness by parties on different sides of the debate to **work together** towards the common goal of eradicating underdevelopment in Africa.

5.4 Significant evidence of Africa's marginalisation

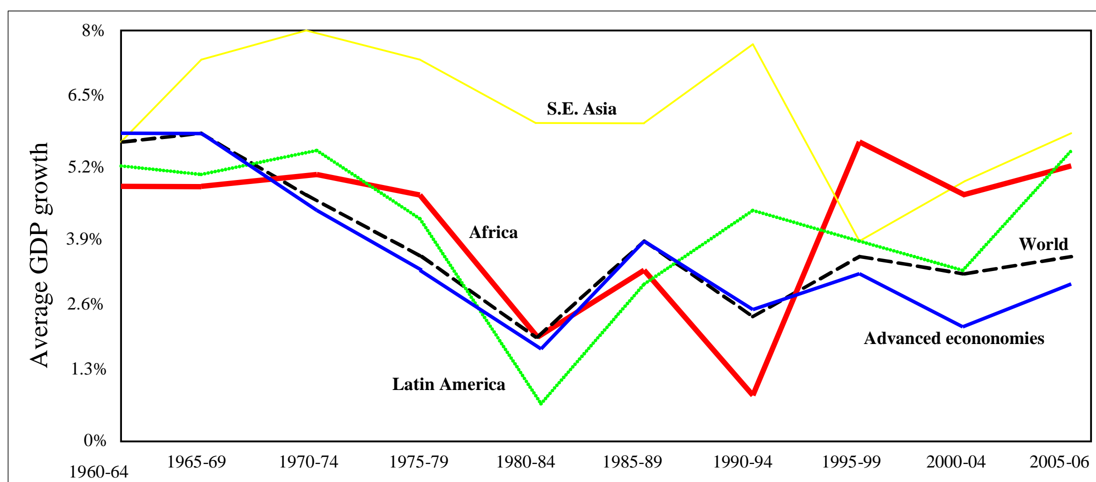
As the prime cause of the widening gap between Africa and most of the rest of the world, the challenge of its marginalisation is fast becoming an exponentially worsening reality. Contrary to most other economies that have become more globally integrated, Africa's economies have turned inwards as its shares of world trade, production and investment are increasingly less significant in the way in which the global economy is progressing. While there is less debate on the consequences of Africa's marginalisation, there is still considerable ambiguity regarding its extent, in particular when compared with other regions. Hence, this section aims to quantify the nature and proportional extent of Africa's marginalisation by examining selected evidence[60] from recent and historical data.

[60] While most of the relevant data are included, it is hardly possible to cover literally all related aspects.

5.4.1 Africa's growth performance

Although Africa's economic growth between 1995 and 2006 remained constant at just over 5%, most African countries have been growing from a very narrow base with a high dependency on a limited range of predominantly primary products being produced and exported. Figure 5.1 also reveals why current growth levels have to a degree been met by some scepticism in that, for the preceding 20 years, African growth levels have been highly volatile, ranging between 5.4% and 0.8%. It also shows that Africa was for the last period (2005-06) somewhat behind its main competitors in South-East Asia (5.6%) and Latin America (5.4%) in terms of GDP growth.

Figure 5.1: Comparative GDP growth rates (1960-2006)



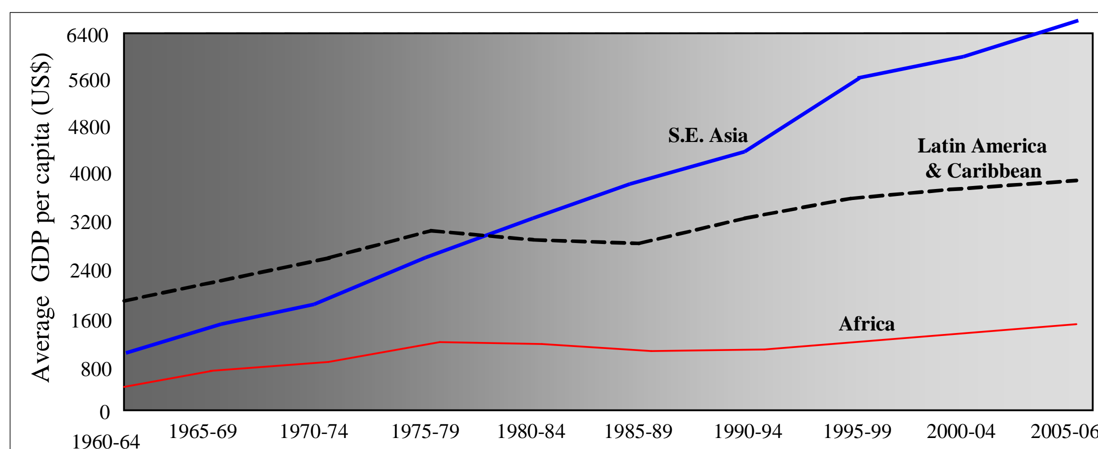
Source: Data from World Bank, 2008 *WDI Online Database*

Note: Growth rates based on 5-year moving averages.

The gap between Africa and South-East Asia and Latin America (and the Caribbean) is further evident in Figure 5.2, indicating that the difference in GDP per capita between Africa and these regions are progressively more disconcerting. For the period 1960-2006, Africa's GDP per capita has never broken through the US$1000-level, while for South-East Asia there has been a steady increase to about $7200 for the period 2005-06. For Latin America and the Caribbean it has also grown gradually since particularly 1990 to the highest level of $3228 for the period 2005-06. While the present highest ever amount of $986 is somewhat encouraging, more than 20 African countries, for example, still have

a per capita income of less than that in 1975 (Gibson, 2004:3). This also explains Africa's high poverty levels.

Figure 5.2: Africa's GDP per capita in comparison with other developing regions (1960-2006)



Source: Data from IMF, 2007:217 "Spillovers and Cycles in the Global Economy", *WEO*; World Bank, 2008 *WDI Online Database*

For Thompson (2000:42), the resultant human toll defines the real marginalisation: "hunger is the greatest manifestation of consumption shortfalls in Africa; grain, meat and overall calorie consumption are well below required minimums; and one-third of children under five are underweight". Figure 5.3 shows that there was a persistent increase in extreme poverty for Sub-Saharan Africa[61] (SSA), whereas the other regions experienced decreases. Although extreme poverty for SSA significantly decreased after 2001 to 41.1% of the population, it is not yet sufficient for what is required to reach the Millennium Development Goal (MDG) target[62] of 22.3% by 2015 (UN, 2007:6).

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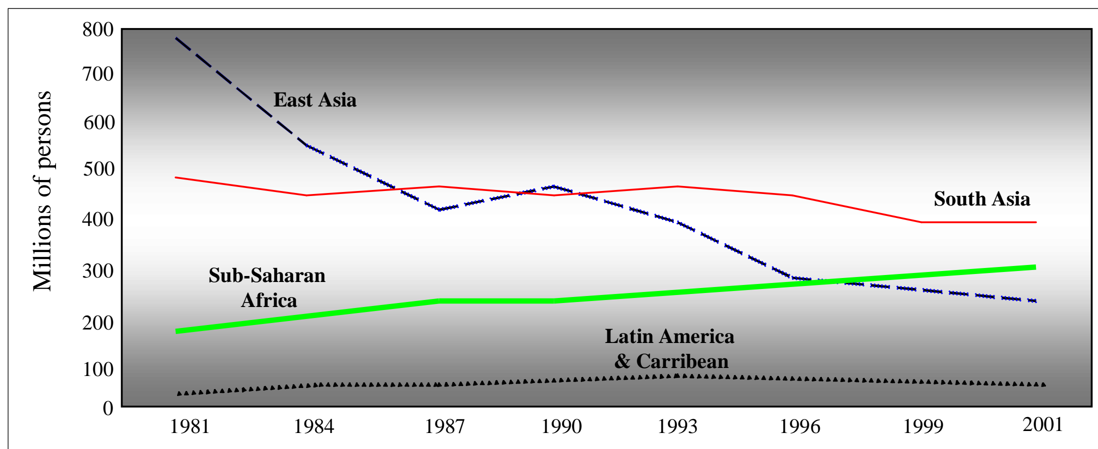
[61] Consisting of 48 (out of 53 African) countries, SSA is fairly representative of Africa (yet not fully).
[62] Alarmingly, Africa remains behind other regions *vis-à-vis* overall progress towards the MDG-targets.

Figure 5.3: Regional incidence of extreme poverty (1981-2001)

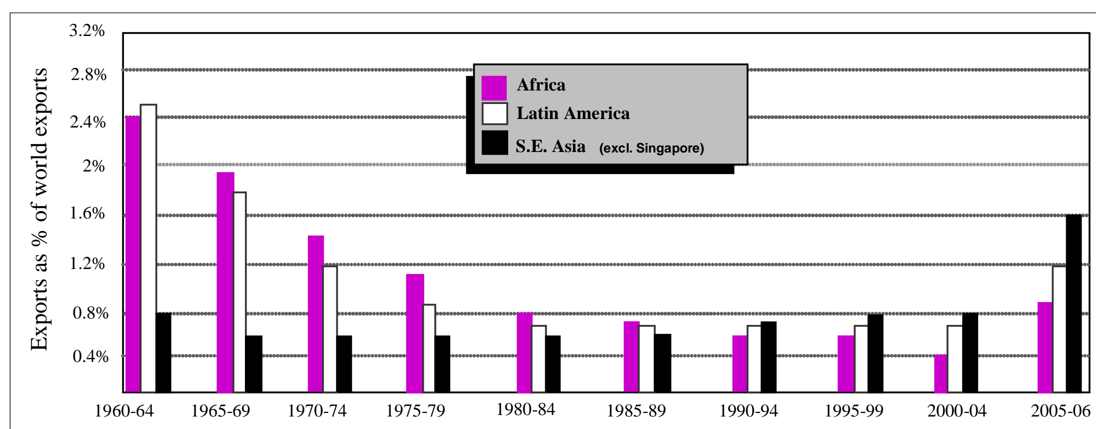


Source: Goldin & Reinert, 2006:29 *Globalisation for Development*

5.4.2 Africa's trade performance

Unlike other regions, Africa's export volumes have, on average, grown less rapidly than GDP – in terms of rates of increase. For example, between the eight-year averages of 1989-96 and 1997-2004 Africa's real GDP growth increased by 90%, while growth in export volume decreased by 2% (IMF, 2007:218). With Africa's share of world exports is falling gradually, it is rapidly falling behind other regions. Figure 5.4 illustrates the inverse situation: between 1960 and the mid-1980s Africa's share of world exports was more than that of Latin America and South-East Asia (excluding Singapore), but fell considerably behind these regions after the mid-1980s. This is in part explained by Africa's exports that grew at 2.8% per annum between 1970 and 1979, falling to -2.4% (1980-1992), and recovering to only 4.3% average growth between 1993 and 2006 (World Bank, 2008). When comparing the latter figure with a relatively poor region such as South Asia's 14.1% (1993-2006), the export gap between Africa and other developing regions becomes even more disturbingly evident. This raises the question: *why is there this export gap?*

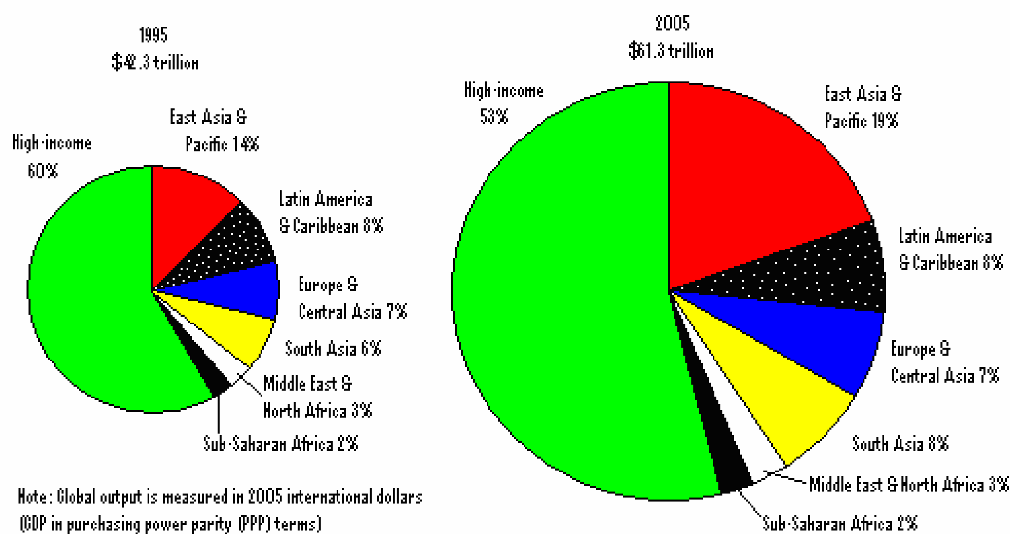
Figure 5.4: Average regional exports as percentage of world exports (1960-2006)



Source: Data from World Bank, 2008 *WDI Online Database*

One explanation is the continent's meagre output levels that are not improving in comparative terms. Figure 5.5 indicates that, between 1995 and 2005, Africa made no real progress regarding its percentage share of global output – remaining at 2% for SSA and 3% for North Africa and the Middle East. East Asia and the Pacific's share increased by far the most (from 14% to 19%), followed by South Asia. Latin America and the Caribbean as well as Europe and Central Asia have also remained at 8% and 7%, respectively. These regions and Africa have made no actual progress in terms of catching up with the leading regions. The only difference is that Africa is the region that remains trapped at the bottom of the scale.

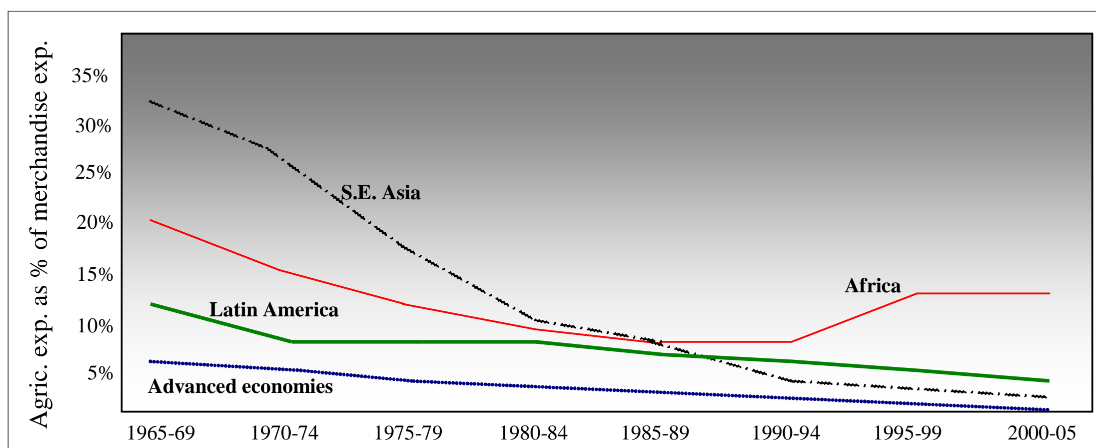
Figure 5.5: Changes in regions' shares of global output (1995 and 2005)



Source: World Bank, 2007a:185 *World Development Indicators 2007*

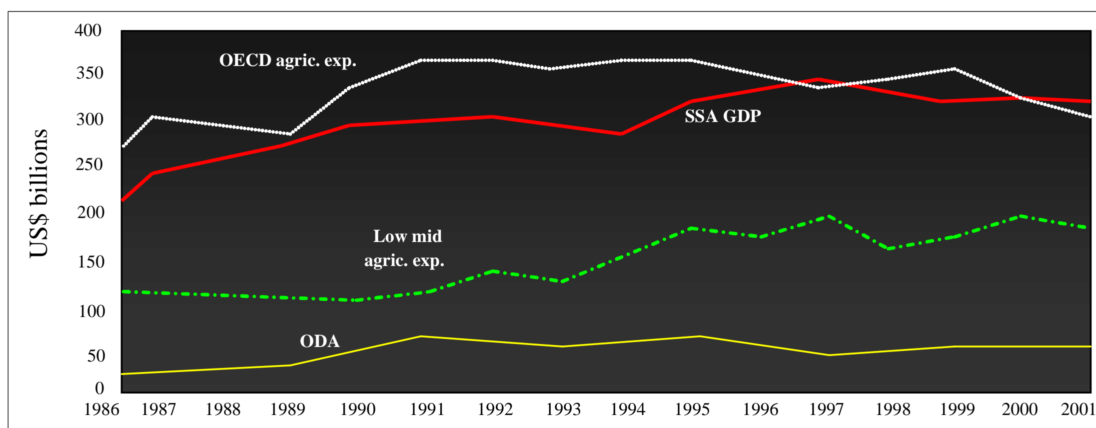
Although Africa inherited small markets and production scales, this is no excuse for not making meaningful progress. It is now clear, especially in light of Asian industrialisation, that its factor advantages – cheap unskilled labour and inputs for primary production – are no longer an acceptable basis for being globally competitive (Collier, 2007:11). Stren and Halfani (2001:473) claim that Africa lacks the capacity and infrastructure to compete economically, and has become "completely marginalised". Lower stocks of human capital, in particular, are resulting in Africa not being in a position to make use of opportunities for manufactured export growth. Its production efforts are mainly geared towards agricultural export growth which, compared to manufactured and service exports, offers fewer export earnings. Figure 5.6 illustrates how Africa's agricultural exports as percentage of merchandise exports are, especially after 1994, considerably higher than those of Latin America, South-East Asia and the advanced economies, whose percentage values continued to decline. Taken into account the continent's susceptibility to extreme weather conditions, this increased dependence on agricultural exports pose a significant risk to export earnings. Furthermore, the share of primary commodities in Africa's exports also remained highly concentrated – 83% in 1970, 76% in 1992, 70% in 2002 and 77% in 2006 (WTO, 2003:47; WTO, 2007b:4, 44).

Figure 5.6: Agricultural raw material exports as percentage of merchandise exports (1965-2005)



Source: Data from World Bank, 2008 *WDI Online Database*

Figure 5.7: OECD agricultural subsidies (1986-2001)

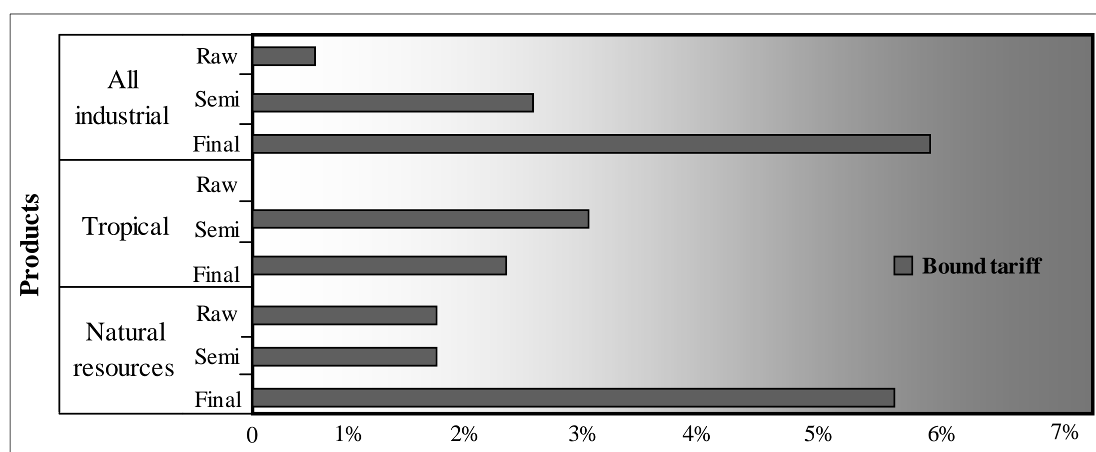


Source: Goldin & Reinert, 2006:63 *Globalisation for Development*

The extent and adverse impacts of agricultural subsidies further explain why Africa battles to escape marginalisation. Figure 5.7 indicates that between 1986 and 2001 total OECD agricultural subsidies – concentrated mainly in the US, EU and Japan – ranged between US$300 billion and US$375 billion. Put into context, this is for nearly the past 22 years more than the entire GDP of SSA. In addition, OECD agricultural expenditures have about doubled the entire agricultural exports of developing countries and nearly

quintupled the amount spent on Official Development Assistance (ODA). Goldin and Reinert (2006:63, 146) conclude that in the overall “subsidy war” of global agricultural trade, “developing countries simply do not have anywhere near enough resources to compete”. This uneven playing field becomes even more pronounced given that, in 2002, the US, EU and Japan spent between 0.9% and 1.4% of their GDPs on agricultural subsidies, while spending only between 0.1% and 0.3% on external aid for developing countries. In addition, as Figure 5.8 points out, the rates of tariffs levied by developed countries on developing-country exports are considerably high in terms of overall averages. Given Africa’s high trade-to-GDP ratio, this is very harmful to its economies (see Appendix 5B).

Figure 5.8: Import tariffs on developing-country exports to developed countries



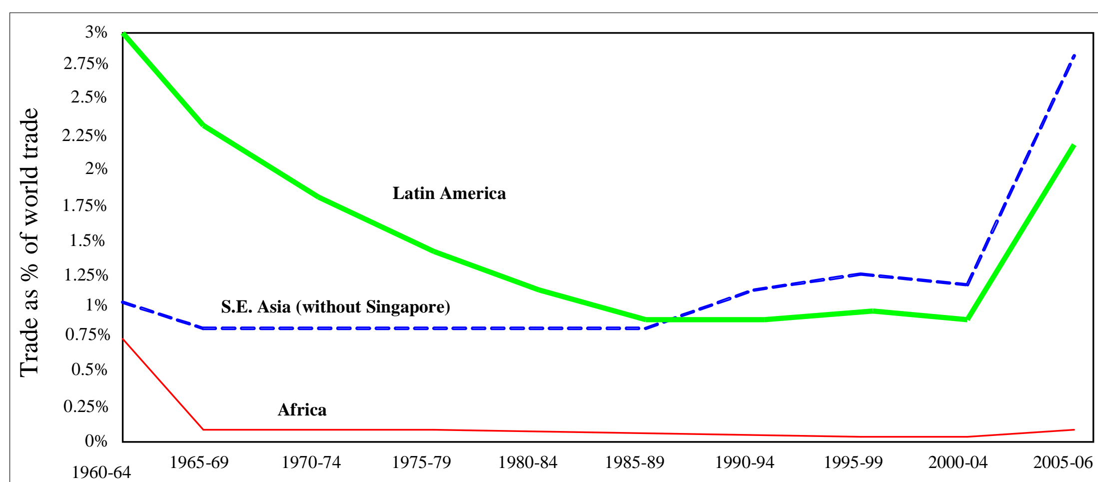
Source: Goldin & Reinert, 2006:62 *Globalisation for Development*

Typical of marginalisation, this is occurring in sectors in which developing countries (notably Africa) have the most interest in exporting labour-intensive goods, i.e. food, textiles and clothing, and wood products. Goldin and Reinert (2006:62) argue that this is the result of tariff escalation, which “prevents developing countries from capturing more value added domestically and from vertically diversifying their exports … and inhibits basic and deep learning processes required for long-term productivity gains”.

All this provides perspective on the bigger trade picture, i.e. Africa’s minuscule share of world trade. Measured in terms of world imports and exports of goods and services,

world trade has been growing at an average of 5% between 1960 and 2006. Figure 5.9 illustrates how Africa's (average) share in world trade over this period (0.09%) is far below those of South-East Asia (1.19%) and Latin America (1.59%). Alarmingly, the major difference between the regions is obvious after 2000 when the latter two regions' shares of world trade increased sharply whereas Africa's share increased only marginally. In doing very little to close Africa's *trade gap* with the other regions, this improvement is still very far off the share of advanced economies that never fell below 24% over 46 years. One of the main reasons for the persisting trade gap, according to Loots (2006a:16), is Africa's general lack of export diversification. It remains highly concentrated in primary commodities, most notably agricultural exports, a sector that makes a one-third contribution to African GDP, absorbs one-third of the labour force and provides a livelihood to about 70% of the poor on the continent.

Figure 5.9: Developing regions' share of world trade (1960-2006)

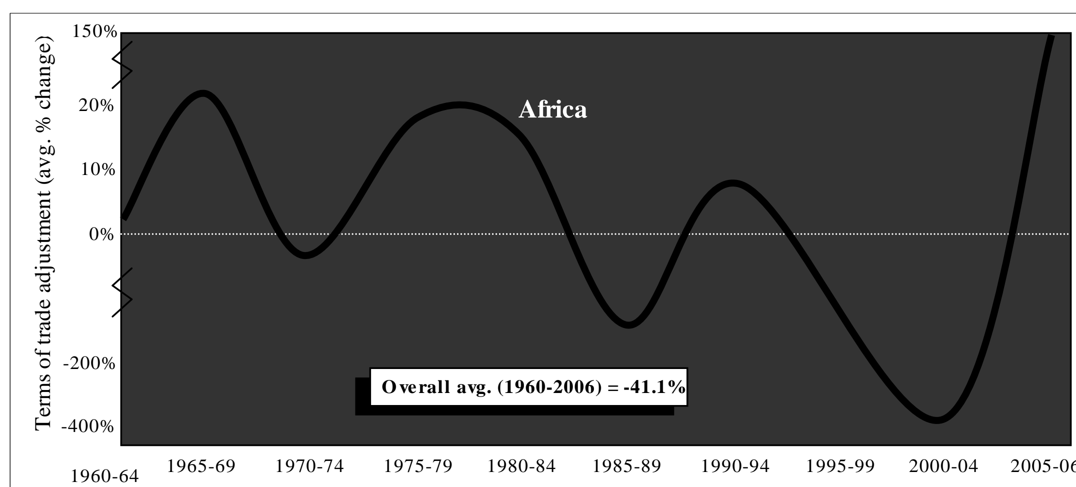


Sources: Data from World Bank, 2008 *WDI Online Database*; ADB, 2007:117

Indicating the amount of imports afforded by export earnings, Africa's terms of trade have on average, between 1960 and 2006, declined by 41.1%. This dramatic weakening of Africa's terms of trade explains, to a large degree, its marginalisation: it has been a victim of conditions beyond its direct control (Luiz, 2006:626). Although Africa's terms of trade experienced an improvement during the commodity price booms of the 1970s, a reversal took place since the 1980s due to increased price volatility in primary

commodity exports. Linking each period's percentage change, Figure 5.10 also depicts how Africa's terms of trade opportunely improved by 156% for the period 2005-2006 (mainly due to sharp increases in oil prices and robust demand, particularly from China, for industrial raw materials), after its lowest of -394% for 2000-2004. Interestingly, with Africa's wealth in terms of the value of export earnings having decreased sternly – as reflected, on average, by its weakened terms of trade – living standards did not improve significantly as average GDP per capita remained below US$1000, suggesting a similar trend and revealing Africa's rather unhealthy high dependence on strong export earnings.

Figure 5.10: Africa's terms of trade adjustment (1960-2006)



Source: Data from World Bank, 2008 *WDI Online Database*

5.4.3 Foreign direct investment and business environment

As far as investment – or the lack thereof – is concerned, Africa's marginalisation is even more entrenched within the global economy. According to Collier (2007:83), the continent has almost completely bypassed the vast increase in FDI over the past 25 years. While there has been a marked increase in direct private investment into developing countries in general and in particular since the 1990s, to over $200 billion per annum, Africa's share decreased to insignificant proportions. In the global competition for international capital, Africa is almost totally neglected, having attracted only 0.7% of the world stock of FDI in 2000 compared to over 70% for OECD countries (Gibb *et al.*, 2002:12). Table 5.1 shows that, in real terms, Africa's net inflows of FDI gradually fell

from nearly 7% of total net inflows of world FDI for 1970-1974 to a current level of less than 2%. This is considerably less than any of the other regions. UNCTAD (2001:35-36) further estimates that for each dollar of net capital inflow to SSA from the rest of the world, about 25 cents went back as net interest payments and profit remittances abroad, more than 30 cents leaked into capital outflows and reserve build-up, while 51 cents made up for terms of trade losses. This suggests, in Luiz's (2006:628) view, a net transfer of real resources from SSA to the rest of the world. Although worldwide FDI inflows grew spectacularly between 1980 and 1999, from $55 billion to over $860 billion, SSA's share, on average, remained well below 1%. This is in stark contrast with the developing countries' average share that rose from 15% to 24% over this period. In 2000 real per capita inflows of FDI into SSA were less than a third of those in 1980 (despite a five-fold increase in nominal terms) – a real example of Africa's marginalisation. Another cause for concern is the fact that Africa experienced a net capital flight and lost attractiveness as a market for FDI, especially in comparison with other developing regions.

Table 5.1: Real net FDI inflows, US$ (1970-2005)

Country groups	Net inflows of Foreign Direct Investment (FDI) 5-year periodic average as % of total net inflows of world FDI						
	1970-1974	1975-1979	1980-1984	1985-1989	1990-1994	1995-1999	2000-2005
Africa	**6.7%**	**4.4%**	**3.8%**	**2.3%**	**1.8%**	**1.4%**	**1.8%**
S.E. Asia	5.3%	5.5%	5.9%	3.8%	7%	4.1%	2.3%
Latin & Caribbean	10.7%	11.9%	12%	4.8%	7.9%	10.3%	7.1%
Advanced economies	73.3%	75.1%	75%	85.6%	70.1%	70.3%	72.6%
Rest of world	4%	3.1%	3.3%	3.5%	13.2%	13.8%	16.2%
Total	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**

Source: Data from World Bank, 2008 *WDI Online Database*

It can been deduced from Table 5.2 that one of the main explanations for Africa not being a popular investment destination – apart from its own lack of domestic savings for investment – is its failure to provide a business environment that is conducive in attracting FDI. By regional comparison in Table 5.2, SSA's figures for 2005 were the worst in most categories. Areas of specific concern include the high cost percentage of per capita income when starting a business (215%); the number of days required for

dealing with licenses (251); workers who are being fired too rapidly; too many procedures and days required for enforcing contracts, and insufficient protection for investors. It is also noticeable that SSA's figures were in most cases higher than the average of even those in low-income countries. In nearly all the cases it was higher than the world average.

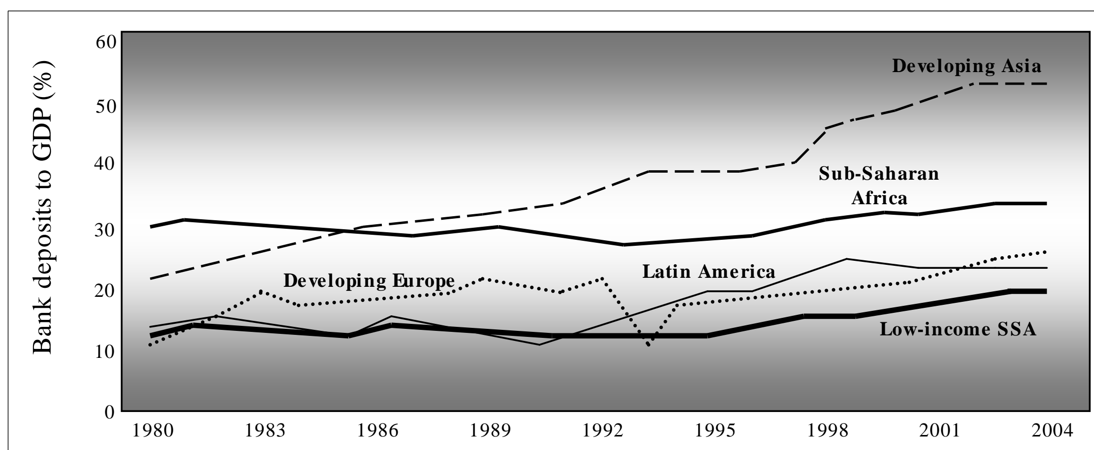
Table 5.2: Regional comparison of business environments (January 2005)

Regions	**BUSINESS ENVIRONMENT**										
	Starting a business			**Registering property**		**Dealing with licenses**		**Hiring and firing workers**	**Enforcing contracts**		**Protecting investors**
	Number of procedures	Time required (days)	Cost % of p/c income	Number of procedures	Time required (days)	Number of procedures	Time required (days)	Rigidity of employment index 0 to 100 (=very rigid)	Number of procedures	Time required (days)	Disclosure index 0 to 10 (=more disclosure)
Latin A. & Carib.	12	66	58.8	7	79	16	210	41	35	470	4
South Asia	8	35	39.7	7	124	16	195	39	30	386	5
SSA	**11**	**64**	**215**	**7**	**118**	**20**	**251**	**53**	**36**	**439**	**5**
Low income avg	10	60	168	7	114	19	231	50	36	421	5
High income avg	7	24	9.4	5	47	16	157	34	24	282	6
World average	10	48	77.3	6	86	18	209	41	32	394	5

Source: World Bank, 2006a:276 *World Development Indicators 2006*

Furthermore, banks' core business of financial intermediation – mobilising deposits and lending them to borrowers – is, according to Guide and Pattillo (2006:142), less pronounced in SSA than in other low-income countries. Figure 5.11 shows that bank deposits in low-income SSA in 2004 were only 19% of GDP, compared with 38% on average in other regions; private sector loans were only 13% of GDP, thus making financial intermediation more difficult. This is an important concern for African countries and impedes the creation of a more favourable investment environment, and one that needs to be addressed through appropriate financial sector reform.

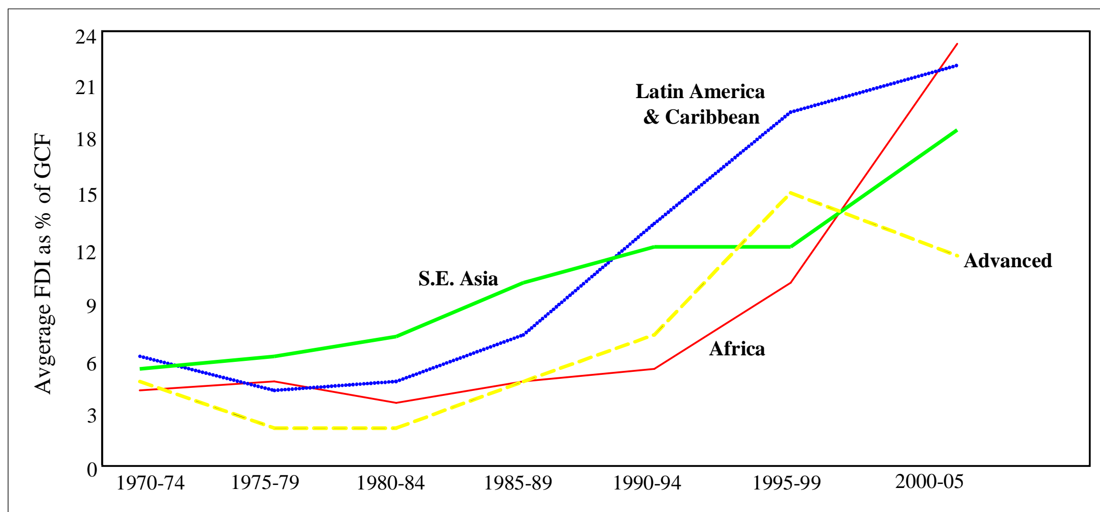
Figure 5.11: Lacking depth: bank deposits are the lowest in low-income SSA (1980-2004)



Source: Guide & Pattillo, 2006:138 "Financial Sector Reform in Sub-Saharan Africa." *Journal of Social, Political and Economic Studies*

A key question that arises is what was the impact of the FDI that Africa did receive? One meaningful indicator thereof is net inflows of FDI as percentage of gross capital formation (GCF). Figure 5.12 shows a significant increase in this percentage for Africa after 1990, which intensified after 1995. It increased from an average of 4.7% for 1985-1989 to 23.8% for 2000-2005. Considering that this is a reflection not only of the increase of investment as a percentage of Africa's GDP but also of how FDI contributes towards improving total GDP, it highlights the positive impact of FDI inflows on supporting domestic investment on the African continent as well as the need for its intensification. Africa's overall average percentage from 1970 to 2005 was only 8%, still significantly behind South-East Asia (10.3%) and Latin America and the Caribbean (11%). Importantly, the lack of FDI also plays a significant part in Africa's deficient integration into the global economy, making it very hard to effectively participate in, and reap the benefits of, globalisation.

Figure 5.12: Net inflows of FDI as percentage of gross capital formation (1970-2005)

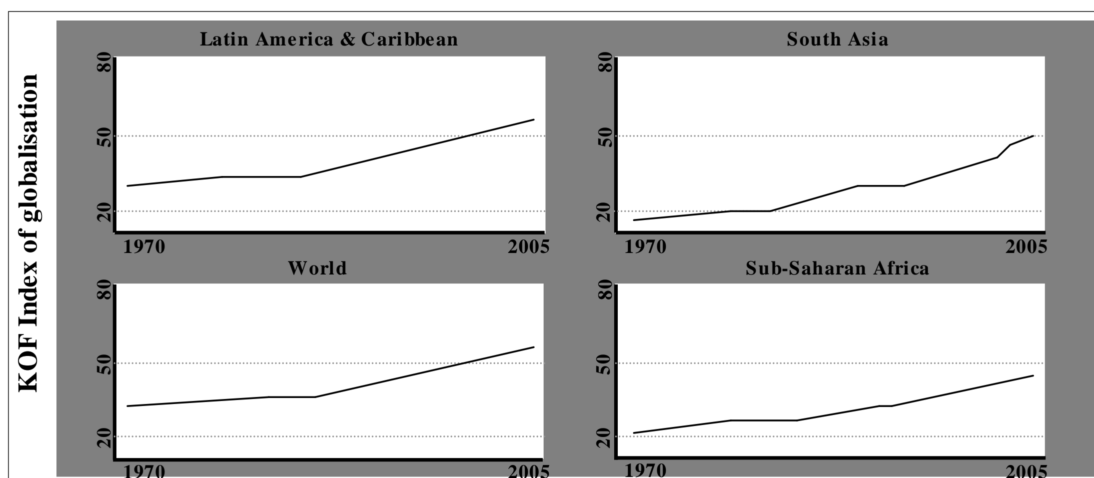


Source: Data from World Bank, 2008 *WDI Online Database*

5.4.4 Africa's performance as regards globalisation and technology

With world trade and investment being two fundamental components of globalisation, the impact of globalisation on Africa's economic development has mainly been negative. Contemporary (or neo-liberal) globalisation, as described by Saxena (2001:432), is when "the world-scale operation of the economy envisages a degree of world-wide uniformity and harmonisation of wants". This implies that, should what Africa supply and demand not correlate with this increasing homogenisation of wants – as effected by globalisation, it will find itself more and more excluded from the global economy; i.e. the discipline of the market. In essence, this encapsulates the impact of globalisation on Africa. The rule of the market forces countries and regions to either adjust to global patterns of supply and demand (production and consumption) – something Africa is unfortunately not very good at – or be excluded from it.

Figure 5.13: Development of globalisation across regions (1970-2005)



Sources: KOF Index of Globalisation, 2008:4 *Development of Globalisation Across the World*

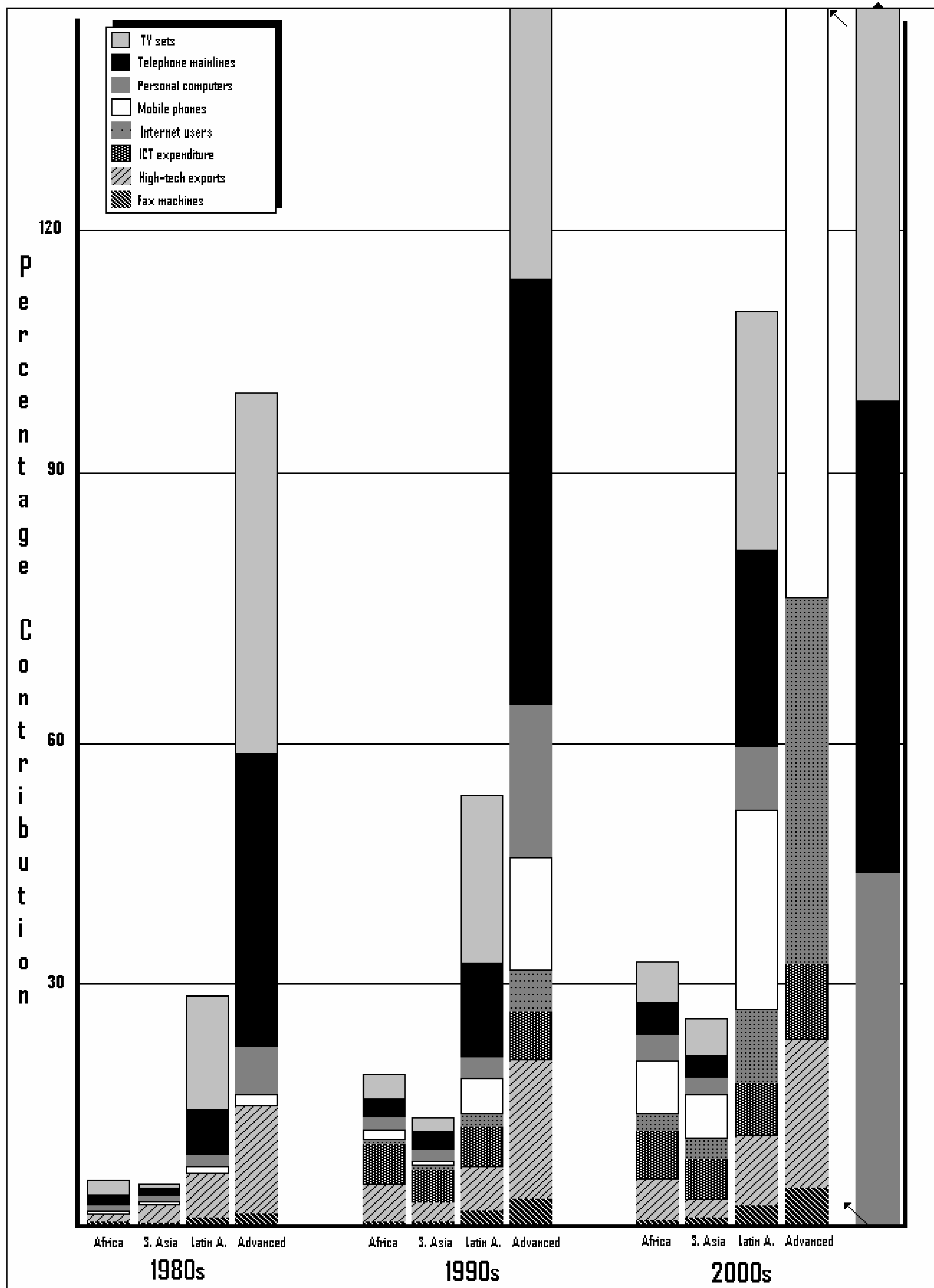
Giving a weight of 36% to economic globalisation, 38% to social globalisation, and 26% to political globalisation, the KOF Index of Globalisation, as illustrated in Figure 5.13, provides evidence of how SSA is clearly the least globalised region in the world with an average index value in 2005 of only 47. This is clearly behind South Asia, Latin America and the Caribbean as well as the world average. Leading Africa's languid progress in 2005, its best performers were Tunisia (index value of 64), Nigeria (67), Botswana (68), and South Africa (69). Importantly, Africa's low comparative value essentially suggests that globalisation actually perpetuates Africa's marginalisation.

Another fundamental component of globalisation is technology. This is where Africa is, perhaps, the most marginalised. According to Figure 5.14 (see also Appendix 5A), the digital divide between Africa and, in particular, Latin America and the advanced economies has increased dramatically since the 1980s. Only South Asia (with the exception of India) remained, on average, behind Africa in terms of technological advancement. Figure 5.14 is compiled by denominating eight different *types* of technologies into a percentage value for each decade (period: 1980-2006), which is then consistently compared among the four regions. In the **1980s** there was a considerable gap between Africa and Latin America, the main differences being telephone mainlines and

television sets, both as percentage of the population. Apart from the latter two, the main difference between Africa and the advanced economies was high-tech exports as percentage of manufactured exports (1.8% versus 14.1%). These differences increased further throughout the **1990s**. However, the difference in the number of Internet and mobile phone users as percentage of the population increased extensively (0.25% and 0.46% versus 6.8% and 13.2%). Another significant difference for the 1990s was the number of personal computers being used as percentage of the population. For Africa it was 0.83% and for the advanced economies this figure amounted to 18.95%.

Percentage values for the **2000s** reveal the actual disparity between Africa and these two regions where all the differences in technology usage escalated. A notable difference between Africa and Latin America was the larger increase in the use of personal computers – a basic requirement for building productive capacity – as a percentage of the population (2.2% versus 7.6%). Figure 5.14 illustrates that the seemingly *smallest* difference between Africa and the advanced economies was in information and communications (ICT) expenditure as percentage of GDP (6% versus 7.4%), which is of course explained by the high value of the advanced economies' GDP. All the other differences between the two regions parted at an exponential rate. Note that the entire bar on the right is supposed to be on top of the bar for the advanced economies, reflecting the true *digital divide*.

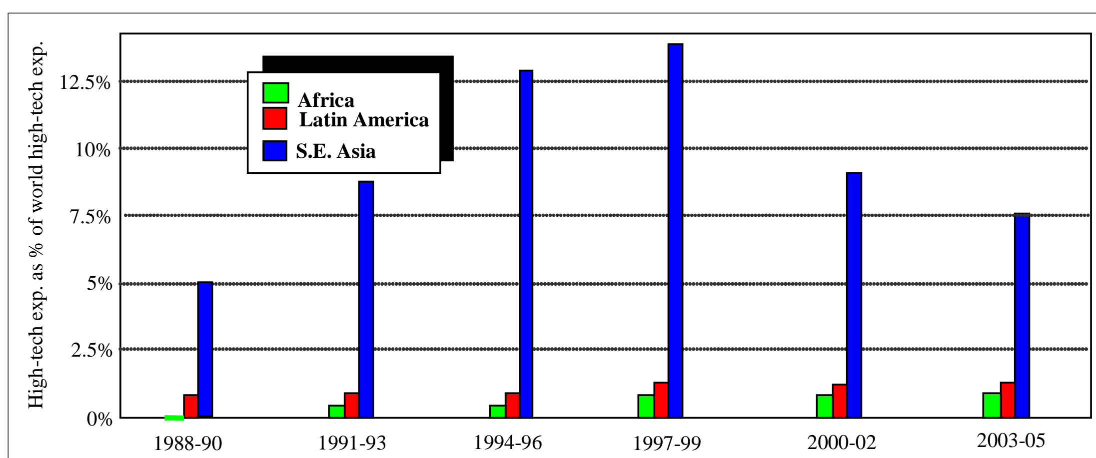
Figure 5.14: Digital divide between Africa and other regions (1980s-2000s)



Source: Own contribution; data from World Bank, 2008 *WDI Online Database*

ICT technology, in particular, has become a key indicator of a country's ability to integrate itself into the new global economy. With telecommunications currently the fastest growing sector in world economy, Africa only accounts for less than 1% of this market (Coyle, 2001:45). In fact, overall technological advance has for decades been a growing determining factor of competitive advantage in the evolving global market-place. According to Lim (1994:836), when comparing the relative contributions of technological progress and factors of production to growth in real per capita GDP in developed countries between 1960 and 1985, 75% was due to technology. For developing countries this figure was, on average, 14% and for Africa the contribution of technological progress was a disquieting 0%. A similar trend manifested itself from the late 1980s to 2005 *vis-à-vis* high-technology exports. Figure 5.15 reveals how Africa completely lagged behind other developing regions in terms of expenditure on these exports as percentage of world high-technology expenditure. Its highest percentage was a mere 0.2% for 2003-2005, which largely explains why Africa is not globally competitive.

Figure 5.15: Developing regional comparisons of high-technology exports (1988-2005)



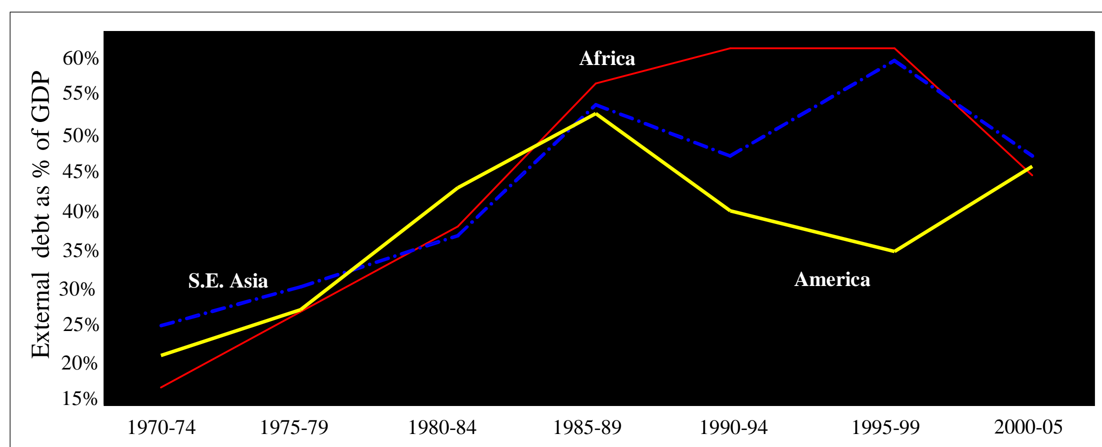
Source: Data from World Bank, 2008 *WDI Online Database*

5.4.5 Debt and aid

Another area of concern for Africa is the plunder caused by debt and debt-servicing that has overwhelmed the continent. Edoho (1997:13-14) argues that, since 1982, Africa's

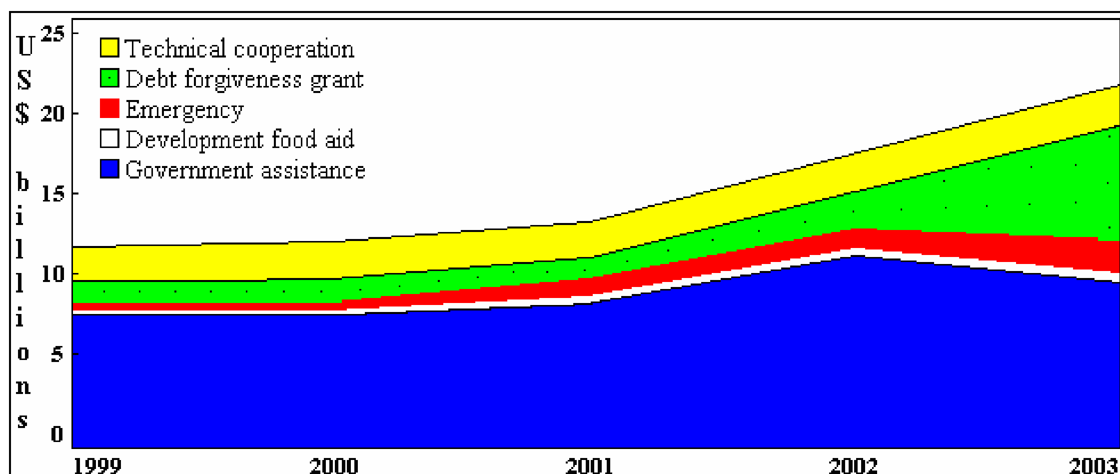
debt service ratios have risen more rapidly than in any other continent. According to Loots (2006a:19), Africa is the only developing region not to have successfully overcome the debt crises of the 1980s, thus constituting a serious threat to sustainable growth and development. Figure 5.16 indicates the sharp increase in external debt during the 1980s, which still increased gradually until 1999 to as high a percentage of GDP as 60.5%. The continent started to reduce this figure to 44.5% only in the 2000s. At an overall average of 43% for the whole period (1970-2005), it is still higher than that of both South-East Asia (41%) and Latin America (37%).

Figure 5.16: External debt as percentage of GDP (1970-2005)



Source: Data from World Bank, 2008 *WDI Online Database*

Figure 5.17: Breakdown of aid flows to SSA, excluding Nigeria (1999-2003)



Source: Goldin & Reinert, 2006:123 *Globalisation for Development*

Linked to the concern about debt, Africa also has, as Figure 5.17 suggests, become more dependent on aid, especially after 2001; thus making its economies more vulnerable. Loots (2005:11) points out that Africa's *aid-dependence* was higher in the early 2000s (3.4% – aid as percentage of GDP) than shortly after World War II (2.5%). Collier (1995:543) even goes so far as to claim that aid and migrant's remittances now constitute African economies' main form of participation in the global economy.

5.4.6 Africa's progress in human development and the MDGs

Over a period of 55 years, as indicated in Table 5.3, Africa did make significant progress in terms of human development as its HDI-value improved from 0.181 in 1950 to 0.442 in 1980 to 0.455 in 1995 to 0.507 in 2000 and 0.613 in 2005 – an overall progress of 238%. While this may seem relatively impressive, there has not been a corresponding improvement in African's living standards as GDP per capita improved with only 142% over this period. Also, continually lagging behind most other regions, Africa's HDI improvement is yet some distance from catching up with its main competitors; it is in 2005 at a level that East Asia was before 1995 and where Latin America was even before 1980.

Table 5.3: Comparative HDI-values of different regions (1950-2005)

Regions/years	Regional HDI averages (Weighted by population of countries pertaining to each region)				
	1950	**1980**	**1995**	**2000**	**2005**
Australia/NZ	0.856	0.864	0.933	0.938	0.953
North America	0.864	0.889	0.934	0.944	0.956
Latin America	0.442	0.683	0.802	0.803	0.803
East Asia	0.306	0.614	0.746	0.788	0.804
China	0.159	0.559	0.650	0.732	0.777
South Asia	0.166	0.407	0.449	0.593	0.611
Africa	**0.181**	**0.442**	**0.455**	**0.507**	**0.613**

Sources: IMF, 2001:162 "Fiscal Policy and Macroeconomic Stability", *WEO*; UNDP, 2006:283 *Human Development Report 1999: Globalisation With a Human Face*

A further major concern for Africa is the fact that, as the 2008 Millennium Development Goals Report found, the whole continent remained *off track* to meeting most of the world's shared goals, particularly that of fighting poverty. In fact, it was found that SSA is not on track to achieve any of the MDGs. This is highly disappointing, especially in light of significant progress that other developing regions made towards achieving these goals. Table 5.4 provides a brief regional overview as to the progress in achieving the MDGs. It is clear that Africa, in terms of both Northern and Sub-Saharan, is significantly behind South-East Asia and Latin American and the Caribbean. Table 5.4 shows that apart from poverty, the other most notable areas of concern for Africa is employment, low primary schooling (and education in general in SSA), improving maternal health, halting and reversing the spread of HIV/AIDS and tuberculosis, access to improved drinking water and slow progress in developing a global partnership for development.

Table 5.4: Selective regional progress in the MDGs (2007)

Goals and Targets	Africa		South-Eastern Asia	Latin America and Caribbean
	Northern	**Sub-Saharan**		
GOAL 1: Eradicate extreme poverty and hunger				
Reduce extreme poverty by half	low poverty	very high poverty	moderate poverty	moderate poverty
Productive and decent employment	large deficit in decent work (youth and women), moderate productivity	very large deficit in decent work (women), very low productivity	large deficit in decent work (women), low productivity	small deficit in decent work (women), moderate productivity
Reduce hunger by half	very low hunger	very high hunger	moderate hunger	moderate hunger

GOAL 2: Achieve universal primary education				
Universal primary schooling	high enrolment	low enrolment	high enrolment	high enrolment
GOAL 3: Promote gender equality and empower women				
Equal girls' enrolment in primary school	close to parity	almost close to parity	parity	parity
Women's share of paid enrolment	low share	medium share	medium share	high share
Women's equal representation in national parliaments	very low representation	low representation	low representation	moderate representation
GOAL 4: Reduce child mortality				
Reduce mortality of under-five-year-olds by two-thirds	low mortality	very high mortality	low mortality	low mortality
Measles immunisation	high coverage	moderate coverage	moderate coverage	high coverage
GOAL 5: Improve maternal health				
Reduce maternal mortality by three-quarters	moderate mortality	very high mortality	high mortality	moderate mortality
Access to reproductive health	moderate access	low access	moderate access	high access
GOAL 6: Combat HIV/AIDS, malaria and other deseases				
Halt and reverse spread of HIV/AIDS	low prevalence	high prevalence	low prevalence	moderate prevalence
Halt and reverse spread of tuberculosis	low mortality	high mortality	moderate mortality	low mortality
GOAL 7: Ensure environmental sustainability				
Reverse loss of forests	low forest cover	medium forest cover	high forest cover	high forest cover
Halve proportion without improved drinking water	high coverage	low coverage	moderate coverage	high coverage
Halve proportion without sanitation	moderate coverage	very low coverage	low coverage	moderate coverage
Improve the lives of slum-dwellers	moderate proportion of slum-dwellers	very high proportion of slum-dwellers	moderate proportion of slum-dwellers	low proportion of slum-dwellers
GOAL 8: Develop a global partnership for development				
Internet users	moderate usage	very low usage	low usage	high usage

Source: UN, 2008:47

Note: The progress chart operates on two levels: the words in each box indicate the degree of compliance with the target, while the colours show progress towards the target according to: ■ already met the target; ■ progress sufficient to reach the target if prevailing trends persist; ■ progress insufficient to reach the target if prevailing trends persist; □ no progress or deterioration.

5.4.7 Africa's governance performance

Table 5.5: SSA's governance indicators (1998, 2002 and 2006)

Governance indicator	Year	Percentile rank (0-100)	Governance score (-2.5 to +2.5)	Average: ranks and scores (all indicators)
Voice and accountability	2006	32.7	-0.58	**2006** Rank = 30.3% Score = -0.65
	2002	30.6	-0.65	
	1998	29.6	-0.69	
Political stability	2006	35.6	-0.5	
	2002	32.6	-0.61	
	1998	32.8	-0.62	
Governance effectiveness	2006	27.2	-0.77	**2002** Rank = 30.5% Score = -0.66
	2002	27.8	-0.72	
	1998	29.2	-0.7	
Regulatory quality	2006	27.4	-0.74	
	2002	30.1	-0.66	
	1998	31	-0.62	
Rule of law	2006	28.8	-0.74	**1998** Rank = 30.4% Score = -0.67
	2002	29.5	-0.71	
	1998	29.1	-0.74	
Control of corruption	2006	30.3	-0.65	
	2002	32.3	-0.6	
	1998	30.4	-0.64	

Source: Data from World Bank, 2007b *World Development Indicators 2007*

More positively, perhaps, Table 5.5 shows how SSA's governance has steadily improved in several critical areas from 1998 to 2006. The most notable areas are voice and accountability and political stability. There are, though, two main areas of concern, i.e. regulatory quality and governance effectiveness. Why the lack of progress in specifically these two indicators (actually the control of corruption as well) is somewhat troubling is that they are arguably most critical for attracting foreign investment. Without trust in SSA's regulatory environment and the effectiveness of its overall governance, very little investor confidence is build, which inhibits prospects for broadening Africa's growth base.

Lastly, while Africa's marginalisation is not homogenous, the evidence here clearly suggests that – as a region – it is playing an increasing peripheral role in the way in which the modern-day global economy is advancing. Yet, the main concern is that it is not only being marginalised within the global system, but also facing marginalisation within the developing world. However, although internal and external factors indicate that Africa's

challenge of de-marginalisation is now considerable, it is not impossible. Still, from the evidence it is clear that although there are some positive signs as regards progress or potential for progress, it is far from being sufficient, thus underlining the need for more efforts in the area of economic policy reform and strategy formulation all over Africa.

5.5 Africa's marginalisation and global economic governance – is there a link?

In short: yes. One key area illustrating this link is the way in which the IMF and the World Bank practically forced Africa into a new system of (neo-liberal) rules. This not only further marginalised the continent from meaningful participation in the global economy, but left its people in a marginal and desperate condition[63]. Hoogvelt (2001:181) contends that structural adjustment programmes (**SAPs**) and debt peonage have given the IMF and World Bank a stranglehold over states and economies, particularly in Africa. Shatz (2002:61) points out that African studies now generally accept that Africa's 20-odd years of experience with structural adjustment have failed. The failure of World Bank and IMF policies in Africa has moved the continent from "crisis" to "tragedy" (Leys, 1994:46). For instance, for the majority of Africa's people the delivery of basic services now comes at a price they can no longer afford. Education, health, security, and the basic determinants of welfare can no longer be met. The central structural adjustment policy of privatisation has not only put basic resources, such as electricity and water, out of reach of the multitude, but public transport and health care, once subsidised by the state, have now also become too expensive. This has resulted in job losses and deteriorating health conditions in a situation of increasing poverty (Gibson, 2004:2). Moreover, Choussudovsky (1997:153) argues that good governance – the so-called *logical result* of structural adjustment and democratisation – has meant that African people's lives and political life are dictated from the outside, undermining national independence. Aid, for instance, has been deliberately used as a leverage to improve governance which, in turn, is supposed to create an enabling environment for economic reforms (Hoogvelt, 2003:192). As a result, Africans regard the imposition of the neo-liberal paradigm as a form of recolonisation of the continent which, in fact, results in its further

[63] This is not to suggest that conditions for quality of life were necessarily more favourable before the SAPs. It merely highlights the role of global economic governance in further marginalising Africa.

marginalisation. It is argued that SAPs, in particular, amount to the pillage of what remains of Africa's economic wealth. Ironically, this reflects elements of authoritarianism, which qualifies as bad governance. This type of conduct is also illustrated by Africa's exclusion from the process involving the planning and designing of SAPs and other supposed *cure-all* neo-liberal policy prescriptions, which primarily take place in Washington (Gibson, 2004:1). All this attests to how the continent is further marginalised by the institutions it depends on for financial and technical assistance.

Demonstrating the negative impact of IMF/World Bank SAPs on, in particular, SSA-countries – shortly after their introduction – was the simultaneous economic deterioration of nearly all the countries in the region, including those relatively free from internal turmoil. Accordingly, as further evidence of Africa's marginalisation, Ghai (1991:14-17) asserts that (only) between 1980 and 1988:

- per capita incomes, in the region as a whole, declined by 30%;
- rates of investment in all SSA countries drastically deteriorated, and
- an annual loss of US$6.5 billion for the region occurred, even without taking into account capital flight. Put into context, this total amounted to:
  - 33% of total annual imports;
  - 45% of export earnings;
  - 11% of the region's combined GDP, and
  - 60% of gross capital formation.

Hoogvelt (2001:184) asserts that structural adjustment has "oiled the financial machinery by which wealth is being transported out of Africa, thereby removing the very resources which are needed by dynamic adjustment to the new global economy". The relation between commodity specialisation and debt illustrates this: both the IMF and the World Bank have used their leverage on Africa's indebtedness to require that production be concentrated on commodity exports. Forcing prices downwards, this led to SSA's terms of trade being lower in the late 1990s than in 1954 and food production per head, by then, also less than it was in the early 1970s. The vulnerability of many African countries was further aggravated by, on the one hand, forced privatisation by the SAPs, resulting in

foreign investors benefiting excessively, as well as the under-capitalisation of the emerging stock markets, which exposed them to speculants. On the other hand, imposed devaluations increased foreign debts in local currency, while interest rate liberalisations led to governments having to pay higher interest rates on domestic debt, and total production being undermined. Thus, as Griffin (2003:805) points out, with the benefit of hindsight it is obvious that the sequence of economic reforms has been far from optimal and that developing countries – mostly African – have been placed in a seriously disadvantageous position.

In response to the failure of the SAPs, even in 1989, the Economic Commission for Africa (ECA) initiated the African Alternative Framework to Structural Adjustment Programme for Socio-Economic Recovery and Transformation (AAF-SAP). Being on the whole concerned with *adjustment with transformation*, AAF-SAP stressed the need for capital investment for economic growth in Africa (Loots, 2006b:4). While it conceded to the demands of the SAPs agenda, AAF-SAP was not endorsed by the IMF and the World Bank, which reflects their lack of appreciation of local initiatives.

Africa's marginalisation by the institutions of global economic governance is also obvious in it having been given **minimal say** in their decision-making structures. Africa's under-representation has been grossly unfair, especially given the number of people it represents (about a seventh of the world's population). Hence, as Held (2004:371) argues, a breakdown of symmetry and congruence between decision-makers and decision-takers affects the credibility of general decision-making in the IMF, World Bank and WTO. These institutions are dominated by the major economic powerhouses, i.e. mainly the G8. Varma (2002:15) insists that the system for allocating IMF quota shares marginalises developing countries from effectively participating in decision-making processes relating to how the global economy is governed. Africa's actual quota share is now a mere 5.3%. Furthermore, 43 African countries are represented by only two Executive Directors on the **IMF** Board, accounting for less than 5% of the votes. By contrast, 24 industrial countries hold eleven seats on this Board, while the US has 17.5% of the voting share,

giving it veto power (Arrighi, 2002:23). A similar representation ratio is also reflected in the IMF's other governing bodies.

The **World Bank's** voting structure is also highly in favour of the richest countries: the US has 15% of the votes, Japan 11%, Germany 7%, Great Britain 5% and France 4%, each having an Executive Director on the Executive Board. Conversely, the 47 SSA member nations have a combined total of only 7% of votes and two Executive Directors to represent it. A case in point is that, although developed countries account for a mere 17% of the votes in the UN, they account for over 61% of the votes in the World Bank and IMF. Even the **WTO**, which is seemingly a more egalitarian forum for African countries to make their voices heard, offering a *one country, one vote* structure, is dominated by the advanced economies as, in fact, not all votes are equal. Luiz (2006:638) argues that, "industrialised countries are able to dictate the agenda of the WTO and the outcomes because they are better organised and have more resources which give them more voice". In addition, Amuwo (2008:3) argues that nowhere is globalisation's marginalisation effect more debilitating and pernicious to the interest of Africa than the extremely unfair trade practices institutionalised under the auspices of the WTO. The multilateral trading system of the WTO is hostile to Africa in the following main areas (Bello, 2006:4):

- by getting African states to sign the Marrakech Accord of 1994, thus giving teeth to the Uruguay Round that favours the developed countries, the WTO took from these states their right to employ a variety of critical trade measures for development purposes;
- the use of TRIMS and TRIPS not only obstructs the industrialisation of Africa, but also deepens its technological dependence on developed countries' firms;
- the WTO does not recognise the *special and differential* status enjoyed by developing countries under GATT, practically forcing these countries to liberalise trade (and investment) which is considered the only route to development;
- agricultural standards towards Africa have been unfair: while insisting that developing countries should withdraw subsidies from their farmers, developed countries have been allowed to regularly increase theirs, and

- the WTO systematically protects the trade and economic advantages of the rich nations (especially the US) by denigrating the developing countries' right to take activist measures to achieve development, which, again, dilutes their right to *special and differential treatment*. Inaptly, the WTO raises inequality into a principle of decision-making, while clearly undermining basic fairness.

Lastly, two seemingly contradictory developments are a cause for serious concern for future relations between Africa and the institutions of global economic governance as both issues could contribute to the further marginalisation of the continent. First, although global economic governance cannot impose its regulations on an unwilling state, increasing effort is put into binding the developing world – especially Africa – to **global regulations** by means of conviction and, in theory, mutual cooperation (Halabi, 2004:33). Neo-liberal policy prescriptions increasingly strengthen markets at the expense of governments. The economic discipline of global markets is thus used to pressurise African countries, in particular, to abide by universal norms, rules, practices and trends – economic and political – that, asymmetrically, mainly benefit the rich countries. Secondly, as Hoogvelt (2001:195) asserts, "what is currently emerging is a system of global economic governance with methods and instruments geared to containing and managing symptoms rather than removing causes, attesting to a process of **disengagement** from the periphery of the world economy". While Africa does not want this system to contribute to its marginalisation, it realises that it certainly needs these institutions to play a key role in its de-marginalisation, i.e. eradicating its causes, not merely the symptoms.

5.6 Is its marginalisation a problem only for Africa?

A critical dimension of Africa's marginalisation is the risk implications – for the rest of the world – of the ongoing degeneration and underdevelopment it causes on the continent. Although Africa is still heavily dependent on external assistance, it is, reciprocally, also of significance to many global economies as it is fundamentally linked to them. It is therefore important to ask whether the further marginalisation of Africa is only of major concern for Africa or whether it also has growing adverse implications for the rest of the world – in particular the developed world? The answer to this question is a

cautious yes because it is not perfectly clear in which ways the rest of the world is affected. There is no doubt that Africa's role in the global economy is indeed valued by most of the rest of the world. Notably, this does create the risk of non-performance due to its interdependence with global economies.

According to Saxena (2001:328), many Western countries depend heavily on Africa for natural resources and markets as it, among other resources, accounts for 99% of the world's cobalt, 54% of gold, and has significant gas and oil reserves along with largely untapped agricultural potential. The US, for instance, depends heavily on Africa for oil and various mineral resources which are essential for its industries. With Europe, Japan and leading developing countries such as China, India and Brazil as important trading partners, Africa is economically and strategically of great significance to many of the foremost economies in the world. This is also specifically emphasised by the key role played by a number of African countries in advancing the interests of the G20 (Arrighi, 2002:29). In addition, just as the economic significance of Africa to the rest of the world can hardly be exaggerated, so too can the impact and risk of its gradual disintegration due to marginalisation.

Importantly therefore, as Collier (2007:3) emphasises, "the 21st century world of material comfort, global travel, and economic interdependence will become increasingly vulnerable to large islands of chaos", of which Africa comprises the greatest part, with 70% of the people in what the author calls the "Bottom Billion" being Africans. As the problem of Africa's marginalisation and underdevelopment continues to grow, the continent diverges from an increasingly sophisticated global economy, thus making integration more difficult and the threat of it contributing to an escalating global risk scenario a greater reality. This is mainly due to the rising potential of Africa becoming economically and politically unstable as a result of increasing vulnerability to external shocks and influences, as well as internal turmoil and collapse. Reducing this vulnerability is a key challenge and opportunity for especially the institutions of global economic governance to, as partners, become more significantly and intently involved in Africa's de-marginalisation. It can therefore be resolutely construed that Africa's

marginalisation is without doubt also a problem for the rest of the world, thus reiterating the importance of collectively defeating this challenge for the better of all.

5.7 Conclusion

A number of countries and regions suffer from marginalisation. What makes Africa's experience unique is that it involves all the countries located on one continent, making it an *easy target* for exclusion. More specifically, Hoogvelt (2001:187) asserts that there is a new relationship between the new world order and Africa: "a relationship of exclusion, rather than of continuing incorporation". Given the impact of globalisation, Africa's marginalisation reflects a clear **peripheralisation** and divergence from an increasingly integrated global economy. In fact, according to Collier (1995:556), "Africa is currently more marginalised within the world economy than at any time in the past half century". The danger of this problem escalating to such an extent is that it may prove to be irreversible and, therefore, underpin the continent's further underdevelopment.

The chapter has demonstrated that Africa is **grossly underdeveloped** and that its marginalisation from the global economy is a harsh (and worsening) reality for which more answers need to be found via debate, cooperation and investigation. It provides valuable perspective on the challenge facing the continent in terms of economic development as well as some encouraging areas on which to build for the future. While many of the aspects and issues involved are debatable, it is a **necessary debate**. The most important aspect concerning the debate on the causes of Africa's marginalisation is that it highlights areas where drastic change through reform is needed, on the part of both Africa and the rest of the world. This chapter attempted to remould the debate into a format for *constructive criticism* that could provide valuable guidance for the continent's rebuilding process. Hence, some key areas of concern to which more attention should be paid by both sides in terms of reversing Africa's marginalisation, include:

- addressing the weaknesses of capitalism, making it a more equitable system that affords less competitive and less globalised countries the opportunity to be included into the global economy;

- redesigning reform efforts in Africa, in terms of both a more inclusive planning process and the proper implementation of reform initiatives;
- eradicating mismanagement by strengthening the state system (and its accountability), resulting in better mobilisation of resources and delivery of public goods and services;
- improving Africa's high-risk environment by eradicating corruption and poor governance in order to create conditions that are more attractive to FDI, and
- rectifying the unrepresentative inequalities in voting power evident in the decision-making structures of the institutions of global economic governance.

The evidence highlights mainly **six findings**. First, capital inflows are playing an increasingly central role in Africa's efforts towards improving economic growth and capacity building. With Africa becoming more dependent on it, it is vital that FDI should not result in a net transfer of real resources from Africa to the rest of the world. Secondly, export growth and diversification – especially in manufactures and services – are essential, not only in making Africa more competitive in the global economy, but also for improving living standards (i.e. GDP per capita) and overall productivity. Thirdly, and particularly in Africa's case, technological progress is playing an increasingly meaningful role in becoming more globalised, i.e. more integrated into the global economy. In view of this and, for example, telecommunications being the fastest growing sector in the world, the need for technological advance calls for more research, development and investment in technology as well as the development of technology skills to improve the productive capacity of African workers. Fourthly, the scandalous amount of OECD agricultural subsidies, along with tariff escalation (recurring in sectors in which developing countries have the most interest), still create a blatantly unfair global playing field. Fifthly, from the KOF Index of Globalisation it is clear that SSA is the least globalised region in the world and that globalisation actually perpetuates Africa's marginalisation. Lastly, it is evident that **global economic governance** has contributed significantly to Africa's marginalisation. IMF/World Bank SAPs played a decisive part in Africa's economic deterioration. So also did Africa's under-representation in these institutions' decision-making structures and the unfair trading regime under the auspices

of the WTO, unjustly constrict its economies. Reform of the IMF, World Bank and WTO is long overdue and must be speeded up.

Importantly, this reflects a **positive relationship** between the *governance void* and *global inequality*. It is not only the inadequacy of current global economic governance arrangements and the contributory factors that are creating this governance void, but also the unfair treatment by the IGEGs of many developing countries such as those in Africa; which is resulting in more global inequality and marginalisation. Reciprocally, as global inequality is worsening, it creates more and more uncertainty as to what regulations, guidelines and policy measures – i.e. governance arrangements (on a supra-national and/or domestic level) – are necessary to put an end to it. This effect is then also, due to the asymmetry problem and a lack of global leadership, further worsened by the current (and increasing) ambiguity regarding where the different spheres of authority begin and end and which is more dominant. The result is more global governance uncertainty and more global inequality, and the concern is that this is to the detriment of mainly the developing countries that struggle to become globally integrated.

Then, the chapter also highlighted the fact that the concern over Africa's marginalisation stretches beyond the continent. With uncertainty surrounding the Middle East and its oil reserves escalating, and China's interest in Africa growing by the day, the competition for Africa's mineral riches and resources are increasing rapidly. Hence, the strategic significance of Africa in the global economy is causing its marginalisation to be a major concern, also, for the rest of the world. Besides ethical and humanitarian concerns (e.g. poverty and health), this is an even more significant reason not to let Africa waste away. In addition, allowing Africa to fade a way increases the risk of it becoming a source of serious instability in the global economy – a risk that the developing world cannot take.

In addressing Africa's marginalisation, the key is to view the present *crisis* as, what Gramsci (1971:47) calls, "an interregnum", a turning point. The need to catapult itself out of underdevelopment and onto a sustainable path of de-marginalisation should become Africa's single most important focus. The continent cannot afford to linger on this issue

and should thus collectively, either by means of separate regional initiatives and/or the African Union, take drastic action to put itself on the global economic map. While initiatives by NEPAD and African Renaissance are the right steps in this direction, more should be done to speed up Africa's re-integration into the world economy. As developing countries such as China, India, South-East Asia and Latin America have demonstrated in the recent past, it is possible to rise above serious impediments and move forward. Africa will need to become *a global partner that adds value*. Becoming more globally integrated yet more self-reliant will be critical to Africa's de-marginalisation strategy. By mainly examining the extent of Africa's marginalisation, this chapter has concluded the study's investigation into a number of problem-areas that can be linked to either the governance void or global inequality or both. What stands out is that each of these problem-areas is a significant threat to the future stability and progress of the global economy.

The next chapter will be the first to address potential solutions by investigating how global economic governance can be reformed in order to improve it and to create a system that is more inclusive towards developing countries, particularly those in Africa.

Appendix 5A: Digital divide between Africa and other regions

Countries	DIGITAL DIVIDE							
	1980s							
	Items as average percentage							
	Fax Machines	**High-tech exports**	**ICT expenditure**	**Internet users**	**Mobile phones**	**Personal computers**	**Telephone mainlines**	**Television sets**
Africa	0.011%	1.8157%	0%	0%	0.0049%	0.0921%	1.0413%	2.1548%
South Asia	0.0011%	2.8943%	0%	0%	0.0039%	0.0213%	0.4455%	1.0457%
Latin America	0.0706%	5.3348%	0%	0%	0.0874%	0.4881%	8.2937%	14.247%
Advanced ec's	0.3429%	14.13%	0%	0%	0.7039%	5.5832%	38.3187%	40.4821%
	1990s							
	Items as average percentage							
Africa	0.1104%	4.0685%	4.3812%	0.2455%	0.4549%	0.8307%	2.1327%	4.5264%
South Asia	0.0818%	1.6621%	2.2874%	0.1241%	0.1875%	0.3442%	1.44%	3.2731%
Latin America	0.4334%	5.1748%	4.0229%	0.8277%	2.2179%	3.0784%	16.3845%	20.1038%
Advanced ec's	2.7948%	16.29%	6.2298%	6.8276%	13.1806%	18.945%	51.4574%	51.09%
	2000s							
	Items as average percentage							
Africa	0.176%	4.2428%	6.039%	1.8427%	8.1807%	2.201%	3.5904%	6.2681%
South Asia	0.2187%	1.665%	4.7935%	2.0075%	5.4504%	1.8265%	3.3434%	5.1815%
Latin America	1.0436%	8.4973%	6.2124%	10.282%	26.1006%	7.6185%	20.3662%	28.3179%
Advanced ec's	4.8%	21.57%	7.3921%	41.6089%	68.1761%	47.409%	56.7475%	78.047%

Source: Data from World Bank, 2008 *WDI Online Database*

Note: Items as average percentage, either as percentage of the population (e.g. items one, four, five, six, seven and eight from left to right) or as percentage of manufactures (e.g. item two) or as percentage of GDP (e.g. item three).

Appendix 5B: Regional comparison of trade-to-GDP ratios

Regions	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Africa	72.1	73.0	72.1	72.9	69.1	75.4	75.6	76.2	76.9	80.3	81.3	82.9	85.5
S.E. Asia	104.3	102.2	111.1	129.6	121.8	133.5	175.8	172.3	177.2	188.6	195.4	194.7	182.7
Latin America & Car.	89.5	89.9	91.6	88.9	85.2	89.2	86.8	82.8	85.7	89.1	90.0	79.3	78.1
Advanced econ's	40.9	41.6	43.5	43.7	44.0	48.3	48.1	46.8	47.0	49.8	52.2	n/a	n/a
World avg.	42.0	42.4	44.1	44.5	44.9	49.2	48.8	48.2	48.8	51.9	54.2	n/a	n/a

Source: Data from World Bank, 2008 *WDI Online Database*

Note: Although Africa's trade-to-GDP ratios were already well above 60% during the 1990s, they increased to exceptionally high levels of above 80% since 2004. In contrast to further increases for Africa in 2006 and 2007, the trade-to-GDP ratios of Latin America and the Caribbean decreased significantly to below 80%. The export-driven South-East Asian economies have, of course, abnormally high ratios. Interestingly, the closeness of the advanced economies' trade-to-GDP ratio's and that of the world average, especially over this last 14 years, is a reflection of how dominant the rich countries are in world trade. For Africa it is a concern that even though it predominantly exports primary products, and given that its economies are very adversely affected by tariffs, quotas and subsidies, it is highly dependent on trade – and, in particular, export earnings and manufactured imports.

Chapter 6

Remodelling global economic governance

6.1 Introduction

Today's world is dramatically different from that in the mid-20th century when the IGEGs were created. Not only have more developing countries become more globally significant, but the forces that drive globalisation have intensified global economic interdependence. Although this has, on average, created a more prosperous world, it has also increased global inequality and introduced new kinds of *global risks* (e.g. in trade and finance) that have heightened the vulnerability of the world economy. As a result of this new reality, the need for change in the governance and management of the global economy has become paramount. In fact, in a survey conducted by the Washington Post (2006:3) it was found that the IGEGs along with the G8 and the UN-system "have run out of forward momentum" and that "the stalling of international institutions is striking – and troubling". Bradford & Linn (2007:1) point out the inadequacy of the current international system of institutions to fulfil tasks required in the 21st century. Thus, the need for reform and a re-thinking (and remodelling) of particularly the present structure of global economic governance has reached a critical stage.

"Today we have globalisation without representation", according to Derviş (2005:xi). The absence of appropriate checks and balances, guiding principles at the global level, and a level global playing field have eroded global economic governance of the legitimacy and sense of ownership that is required to draw the cooperation and allegiance needed from the international community. The transformation of the world economy has *not been matched by a parallel evolution* of the mechanisms and institutions of global economic governance. In fact, the need for strong institutions of global governance, the centrality of human development, and the necessity of more participation by the developing countries in global economic decision-making are among the most urgent concerns for the global citizenry as globalisation continues to shape and reinvent the global economy. This chapter addresses global economic governance needs for the 21st century, complemented with the needs of low-income countries (LICs) – especially

Africa. Concomitantly, it suggests ways to bring about reform of the IMF, World Bank and WTO and therefore also the global economic system itself, with a view to de-marginalising Africa and advancing the economic development of the entire developing world. More specifically (and as key themes throughout), the chapter attempts to demonstrate how global economic governance could, via reform, become more instrumental in addressing two critical areas of concern in the global economy:

- ensure that Africa and other LICs benefit more from what is on offer in the global economy, resulting in better quality of life conditions. This implies enhancing – for the LICs – the opportunities and reducing the threats of globalisation, and
- build a more integrative global system that helps Africa de-marginalise to ensure that economic liberalisation, in particular, also works for the developing world.

While the chapter does not construct a *rating-list*, it does attempt to prioritise the reform agenda by emphasising key areas/issues where structural reform is most needed. The underlying and central focus of the chapter is economic development: how it can be brought about/enhanced, how to create an enabling environment (global and domestic) that would stimulate it, and how it can serve as a platform for global integration and de-marginalisation, by means of a reformed and improved system of global economic governance that would primarily benefit Africa, and the rest of the developing world. This chapter first addresses the question *does the world need more or less (global) governance?*, which is critical in determining the direction of change in governance on the global level. Secondly, it considers guiding principles for reform and reform alternatives (or proposals) for the WB, IMF and WTO, respectively. Thirdly, it explores the prospect of a more integrative governance framework, and also (lastly), a number of diverse issues and concerns that involve Africa, and which directly affect this framework.

6.2 Does the world need more or less (global) governance?

The issue of reform hinges on this fundamental question; i.e. should the global governance function be primarily in the hands of the state, or should the emphasis shift to supra-national institutions? Before addressing this question, it is necessary to examine the patterns of association between terms that provide significant context for answering it:

governance, good governance and global governance. *Governance* is broader than the notion of government. It is the sum of the many ways individuals and institutions, public and private, manage their common affairs (Commission on Global Governance, 1996:2). In principle, it is a continuing process whereby diverse or conflicting interests may be accommodated and cooperative action taken. For Rosenau (1995:14), this also relates to *global governance* in that “all governance refers to mechanisms for steering social systems toward their goals”. Given the growing need for integrating economic and social welfare into the bundle of goods of any well-governed society, *good governance* should include improvements in governmental institutions and sound development management (Weiss, 2000:802). In Ul Haq’s (1999:28) view, “the concept of good governance has so far failed to match the radicalism of the notion of human development”. It is therefore becoming clearer that in order to make economic development the central goal in all governance, a more **humane governance** is required. This entails providing global public goods to the global society on the local level by means of mechanisms of global governance and a strengthened state system, which needs to be well coordinated in order to effectively engender equitable socio-economic development – the end result and minimum requirement of sound political, economic and civic governance.

Global governance invokes, especially in the post-Cold War era, shifting the location of authority and the site of control mechanisms to the supra-national level. With the main challenges being international cooperation, consent and adherence as prerequisites for legitimacy, the global system is fast approaching a crossroad where it will have to decide whether to follow a global governance route with the emphasis more on supra-national institutions or a route with the emphasis more on states as the decisive role-players. The fact is that the international community is facing an *inescapable conundrum* in that the climate for governance has changed: the time of absolute and exclusive sovereignty has passed, which questions the basis – unquestionable national sovereignty – on which world organisation was built in 1944, and contemporary global problem-solving increasingly requires supra-national decision-making. It therefore appears, particularly with global problems escalating and the growing widespread acceptance of international norms (e.g. human rights and core labour rights), that **more global governance** is

inevitable. But is this what the world really needs? Of course it would be presumptuous to claim the answer to this question here, but it is necessary, at least, to consider some of the rationale behind it. For further context, it would be useful to briefly consider some key theoretical paradigms (see Appendix 6A). Given that international institutions have a natural tendency to expand in terms of their authority and jurisdiction, the Liberal-democratic internationalism theory stresses the fact that the need to ensure that they are more democratic (through reform) also increases. What has become critical, as argued by the Commission on Global Governance (1996:337), "is the need to balance the rights of states with the rights of people, and the interests of nations with the interests of the global neighbourhood". Although this study does not agree with the Radical communitarianism theory of *demarchy*[64], it concurs with the principle that democratic global governance should be organised along **functional** (e.g. trade, finance, environment), as opposed to territorial lines, and that such functional authorities should be directly accountable to the communities and citizens whose interests are directly affected by their actions (Held & McGrew, 2000:411).

Moreover, in opposing a centralised management of power – as this study does – this theory endorses the idea of a proliferation of diverse, overlapping and spatially differentiated self-governing communities of fate in which there would be multiple sites of power but no sovereign or centralised structures of authority whatsoever. This could result in a major shift in power in favour of the disadvantaged, causing a radical change in the overall pattern of global society. Importantly, this theory conceives democracy as inseparable from the achievement of social and economic equality and the establishment of the necessary conditions for self-development. It is a *bottom-up* theory of the democratisation of world order that promotes *humane governance* as the basis for engendering global development and international cooperation. This study, however, distances itself from the exclusive model proposed by Cosmopolitanism because of its mis-appreciation of reform of current global governance arrangements. This theory requires the subordination of regional, national and local sovereignties to an overarching

[64] *Demarchy* is subversive of existing forms of global governance and stresses the creation of alternative forms of global social, economic and political organisation based on communitarian principles. It seeks to facilitate and encourage the active participation of the people in decision-making (e.g. global civil society).

legal framework. The theory considers this the *ultimate triumph of democracy*. All three theories – as is the case with globalisation – have encouraged a revival of liberal international thought, which has led to a growing emphasis on the global need for improved governance arrangements that deal with global concerns. Both the liberalism of progress and the liberalism of fear emphasise the need for international institutions.

To qualify this *need for global governance* (and the issue of whether it is what the world *needs*), it is necessary to ask what the most favourable conditions are under which to exercise global governance?; i.e. in terms of global economic governance, what kind of international economic structure and pattern of development is most conducive to improving quality of life conditions and long-term stability? It is apparent that the institutional framework necessary for effective global governance will have to transcend national borders and prove its legitimacy by being democratic, accountable and able to accommodate diverse role-players by balancing equally legitimate interests. Strong cooperation and coordination at the supra-national level – with no overriding central authority – are basic requirements at the core of such a framework. If this is to be the case and all these are the ultimate goals toward which the global community will be working collectively, then it appears that the world needs *more global governance*. Anything less than this would presumably not be what the world needs; stopping short of achieving all these goals would spell disaster for the global system. It appears that the option of governments (or even *regional governments*) – instead of supra-national institutions – becoming the decisive role-players in world order is dwindling by the day as globalisation is causing markets to burgeon across borders as these are becoming too difficult to regulate and manage. Even the option of smaller international institutions that only become mere instruments of coalitions of nation states, allowing markets to dictate and supposedly solve global problems facing humanity, seems too great a risk.

The reality is that *globalisation has institutional requirements*. And, for the same reason – excessive global uncertainty – market liberalisation cannot persist without the existence of institutional mechanisms which can modify, compensate or accommodate societal pressures. In fact, as Mortensen (2000:179) argues, “if the global market is left unregula-

ted, it will, in time, undermine its own momentum". Hence, a supra-national governance framework (i.e. *more global governance*) is indeed necessary on condition that it ensures the efficient functioning – and proper governance – of global markets across borders – and the delivery of global public goods on an equal and fair basis. The securing of good governance at the global level is, in fact, the remedy proposed by both the advocates and the opponents of globalisation. The question then becomes what should such a global governance framework be, and more germane to this study, what would be the nature and composition of an appropriate supra-national economic governance structure[65]? The following sections will addrress this question. Admittedly, there still are some questions that are essential to this examination, but fall – by and large – outside the scope of this study. Some include: *governance for whom, and for what?* As global governance increases, answers to these questions and others will become crucial in order to establish sufficient legitimacy and accountability. However, the issue at hand is how to transform and strengthen the existing system of global economic governance structures.

6.3 The need for reform: guiding principles and structural change

As the first step in examining possible components (or role-players) of a global economic governance framework/structure, reform of the WB, IMF and WTO is an absolute and indisputable necessity. However, before considering proposals for structural reform for each institution, this section attempts to establish some guiding principles for reform that reflect their true intent. Any reform agenda must be based on a clear and interconnected set of principles that should be balanced according to their relative significance. For a reform of global economic governance, mainly eight standard principles are advanced:

- *The principle of fair representation* that allows developing countries to have a greater say and influence in voting and decision-making structures and processes;
- *The principle of ownership* that ensures that developing countries participate more closely and effectively in the formulation and initiation of programmes in their countries, thus taking greater cognisance of local (country-specific) conditions;

[65] While it is only a suggested structure for global economic governance (see section 6.4) – with the emphasis on *economic* – it ought to form part of an overall global governance structure. The latter, though, is a broader topic that falls outside the scope of this study. Importantly, more research in this area is critical.

- *The principle of independence* that ensures that the IGEGs and their decision-making are not inappropriately influenced by any country(ies), especially the G8;
- *The principle of facilitating and building partnerships between developed and developing countries* to foster new patterns of assistance and cooperation that deliver on promises and are mutually beneficial without any form of exploitation;
- *The principle of good governance (internal focus),* including sufficient effectiveness, accountability, legitimacy and transparency on all levels – decision-making and operational. Importantly, it must also show a willingness to adjust to 21st century conditions and requirements as regards global economic governance;
- *The principle of global leadership and effective use of power (external focus);* i.e. a responsibility that allows them to strengthen their governance through a clear division of labour to play a more decisive role in human development (WB leadership), the global financial system (IMF leadership), and the global trading system (WTO leadership) to improve the delivery of basic global public goods to all;
- *The principle of critical reflection;* their becoming more critical of the impact of their in-country operations and programmes, resulting in constant improvement;
- *The principle of a global responsibility for human development;* making poverty reduction and pro-poor growth key foci in all programmes and decision-making.

6.3.1 Reforming the World Bank and establishing development as a central focus

The WB has a long history of adapting to changing global circumstances. Yet most of this transformation was in expanding its mission and agenda, while mostly neglecting what is actually required, i.e. real structural reform. The WB's strategy of incrementalism has attracted much criticism as piecemeal reforms have been found wanting and 21st century-demands have been growing. Globalisation is failing for most of the world's poor and a major reason for this is that there has not been a corresponding change in how the global economy is governed. The WB needs to become even more responsive to the concerns of the developing countries. First, in being a public institution the WB has an obligation to become more open and **transparent**, especially to the LICs. Its decision-making and research should be made more public, thus encouraging public debate. The fact is that secrecy engenders suspicions. This limits an institution's legitimacy and

undermines the political sustainability of its policies because it raises the question of whose interests are really being served (Stiglitz, 2003a:229). Secrecy also undermines democracy. The difficult issue, for instance, of *a voice for Africa* still awaits a convincing response. Critics argue that the WB's legitimacy is undermined by it promoting *insider* financial and corporate interests instead of addressing the needs of the voiceless poor. This has led to an acutely growing demand for a more **representative** governance structure and broader engagement of borrowers, as originally intended by the WB's founders. The pressing issue for the WB (and the IMF) is how to rebalance members' changing economic and demographic weights to reflect countries' true current *status*. One suggestion is that of *double majority voting* which would particularly benefit **Africa**. This can be defined as a majority of shareholder votes, on the one hand, and a majority of developing country votes, on the other (Jakobeit, 2005:229). As a compromise and a way out of the current impasse, double majority voting should not only be restricted to operational matters (projects, programmes and personnel) but also be used on many more issues at the WB. This would create an incentive for borrowers (who now, due to a lack of influence, see no point in debating institutional issues) to build coalitions. Furthermore, to engender more change in the present voting and capital structure of the WB, it could also: (1) strengthen the principle of ownership by giving developing countries a greater say in the formulation and initiation of WB programmes in their countries, and (2) increase the number of basic votes of the 149 developing countries, restoring them to their original level, and thereby increasing their relative weight from 40% to 43%. To build consistency, the ratio of basic votes to total votes should be maintained in future to prevent *vote erosion* of the past decades.

Two further suggestions for fairer representation in the case of both the WB and the IMF include: Europe could strengthen its position on both Executive Boards if they were to consolidate the current eight chairs into a single European chair, giving them a combined voting share of over 25% and veto power along with the US. With a lesser number of seats, this would also make decision-making more effective. Secondly, as an incentive for the Europeans, the US could withdraw its right to veto in both institutions. This would make it the respected global leader it is supposed to be instead of its current *hegemonic*

ruler status. Both sides would gain in terms of their key shared objective: making the WB and IMF more effective instruments of global development and financial policy (Bradford & Linn, 2007:126). Emerging market economies – especially those in Asia[66] – would also benefit, having a stronger voice and vote in these institutions. These five proposals for change would give real content and meaning to governance reform in the WB and IMF, thus creating more opportunities for multilateral bargaining, coalition building, and more democratic global economic governance, which is needed for the 21st century.

In addition, the WB needs to become **less dependent** on its shareholder governments. WB directors, in particular, should be appointed on merit for fixed terms coupled with an unequivocal promise of independence from the governments that appointed them. Eradicating further doubts about its independence, the WB should not elect Americans only to be its presidents. This sensitive issue needs urgent attention. In becoming more independent, the WB should ensure that both borrowers and non-borrowers become more aware of their ownership in the WB. One consideration for this is to have a rethinking of the framework for the IDA[67] (International Development Association), separate from any reconfiguration of IBRD (International Bank of Reconstruction and Development) shares, which would have little impact on decision-making in the IDA.

Another dimension of the WB's struggle to gain legitimacy is the issue of **accountability**. As a first initiative of this kind, the World Bank Inspection Panel offers (since 1993) a possible recourse to people affected by WB projects to try to hold the institution (and indirectly their own government) to account. It enhances the power of the Executive Board, as well as that of a wide group of affected *stakeholders* in the WB's work. However, with the Board retaining the power to permit investigations by the Inspection Panel to proceed or not, it remains a rather questionable mechanism of horizontal accountability. The Inspection Panel needs to have a greater say and become more independent. It should also be complemented by another horizontal check on WB officials – an alternative model of accountability, the Office of the Compliance Adviser/

[66] The WB needs to revitalise its role in low-income yet fast growing emerging markets such as China and India, to not become irrelevant as a lending agency and to promote pro-poor and equitable growth policies.
[67] The WB's facility for low-cost loans and grants to the poorest countries, funded by donors' contributions.

Ombudsman (CAO) (Woods, 2005:161). Created in 1999, the CAO is tasked with dealing with environmental and social concerns related to WB operations. Having to report to the President of the WB (although being independent) and having no formal power, the CAO will need to increase its authority in order to be a credible instrument of accountability. Horizontal accountability will, importantly, also need to be reinforced by forms of vertical accountability such as member governments and organised global and local interest groups to hold the WB and other global governance institutions to account.

If the IGEGs are to have a significant impact on poverty, inequality will need to be at the heart of any strategy. As it adapts its **approach towards LICs**, in particular, the WB's structural adjustment frameworks have to become more distributionally favourable (Cornia & Court, 2001:31). This means that it should allow more time for institutional development ahead of reforms, include distributional concerns in the design and regulation of privatisation (e.g. in the way WB-teams are using Poverty Reduction Strategy Papers), and set up new, permanent mechanisms that would support the poor during periods of structural reform (e.g. social funds that protect the poor from macroeconomic shocks). Local economic and political institution building should become a prime vehicle for creating conditions that are more conducive to equitable and pro-poor growth, thus also increasing developing country ownership in the World Bank. Although it has long recognised the importance of education, living within one's budget constraints, and macroeconomic stability as prerequisites for successful development, the WB is now also coming more to terms with the importance of establishing a strong technological basis that includes support for advanced training (Stiglitz, 2003e:122). The World Bank should emphasise this aspect and promote trade and openness in the context of encouraging exports rather than advise LICs to merely reduce trade barriers on imports.

In further adapting its approach, the World Bank is slowly starting to address an issue that has been growing in prominence over the past 10-15 years: the **provision of global public goods**. As much ambiguity still surrounds this issue, the World Bank would strengthen its development initiatives if it were to extend its mandate for providing and financing global public goods, i.e. as a global leader and initiator, not as the sole provider

and financier. Birdsall (2006:40) defines *global public goods* as "those goods (or *bads*) that no single nation has a sufficient incentive to produce (or limit) in optimal (from a global standpoint) amounts, but which have benefits (or costs) for all nations". Examples include technological advances in health and agriculture, while *bads* include global warming. Although WB involvement in providing and financing (e.g. trust funds managed outside the purview of its budget) global public goods is still fairly limited, it has, with its deep range of expertise, the ability to make a significant contribution. A Global Public Goods Trust Fund should be initiated and managed by the WB, which can be financed (among other sources of finance) by some portion of its annual net income. To enhance ownership in the WB, low- and middle-income borrowers should have at least 50% of the votes in such a Trust Fund, with the middle-income countries having more power to set the agenda in return for financing that they would provide by paying higher interest charges on their loans than they otherwise would (Birdsall, 2007:54). And, in the broader picture, this Trust Fund should also be linked with the build-up of a stable and equitable system of development finance for all developing countries as well as finance for development-related scientific research, especially in health and agriculture.

This should be viewed as complementary to the reality that public assistance is being greatly outpaced by private capital flows as the WB now openly recognises that it increasingly finds itself marginalised in its capacity to finance development. In 2000, private net inflows to emerging markets exceeded net official inflows by nearly $170 billion and in 2006 by $68 billion (World Bank, 2008). It is cause for concern that only in the poorest countries the WB still has an impact as regards financing development. Hence, to further bolster the initiatives mentioned above, the WB should adopt a strategy – collaborating with the private sector – whereby its development funds complement private capital flows, and *vice versa*, to assist development in the broader developing world.

Economic theory now recognises that development is more than just efficient resource allocation and the supply of capital; it also involves a *transformation of society*. Conditionality by the IGEGs has created impediments to effective transitions due to it making it difficult for developing countries to focus on priorities. Broadly considered,

conditionality has failed without being replaced. While the World Bank has attempted to refine conditionality, it should rather be substituted with, for example, *selectivity*. This means, according to Stiglitz (2003a:242), "giving aid to countries with a proven track record, allowing them to choose for themselves their own development strategies, ending the micro-management of the past". Given selectively, evidence suggests that aid can have significant impacts both in reducing poverty and in promoting growth. This presents an opportunity for the WB to play a leading role in the coordination of aid, which is infamously fragmented, duplicative, and cluttered with a large number of donors tripping over each others' bilateral and multilateral efforts. For this, a reformed and credible World Bank is needed to reduce the risk of control by one institution for donors.

Moreover, with debt forgiveness coming increasingly under scrutiny, without the forgiveness of debt, many developing countries simply cannot grow. Large proportions of their current exports go to repaying loans to developed countries. Despite the moral issues and arguments, debt relief needs to go further in that not only the poorest of the countries receives this benefit. As a form of **development assistance**, the WB has a crucial role to play here to make the case of debt relief (and lower criteria) on behalf of other developing countries, thus levelling the playing field to enhance global competition. Although it makes sense that the LICs need grants, not loans, a need for loans (e.g. for infrastructure projects) remains, which requires the role of a *credit cooperative* that should be filled by the World Bank. The World Bank is therefore needed, even for middle-income (and occasionally high-income) countries in the case of countercyclical lending and funding for critical sectors such as health and education. To enhance its **lending effectiveness** and relevance for these groups of countries, the World Bank should consider to sharply expand the range of financial products and instruments now available to borrowers. Two examples are (1) risk management products and instruments to hedge against commodity risk, and (2) borrowing in local capital markets to strengthen them and to lend in local currency, thereby reducing currency risk for borrowers. Another innovation could be to create a new loan product (without much conditionalities) that would reduce hassle costs for borrowers and administrative costs for the WB. Savings from the latter, Birdsall (2006:29) argues, would yield greater social returns if deployed in the financing of global

public goods. An innovation that would particularly benefit LICs is to add a degree of *differential pricing* among IBRD borrowers, tied strictly to per capita income and not to credit rating. Moreover, especially for LICs, it is critical that the WB continue to change its approach in favour of more active participation in a development programme by the borrowing country to improve its effectiveness. This would ensure a more cooperative relationship between itself and recipient countries, and be central to building the sense of participation and ownership that the developing world requests for enhanced legitimacy.

In addition, the **internal evaluation** department does not fill the need for the credible, fully independent assessment of WB programmes and aid effectiveness. Well-targeted evaluations of WB-supported programmes that are fully and visibly independent would improve the credibility of its efforts. The WB needs to take leadership in ensuring truly independent evaluation of the impact of WB and other aid-supported programmes. This will provide evidence for further improvement (or alternative strategies) of programmes. In addition, for the WB to become more **effective** as regards its development efforts, it should consider scale and distance. Its headquarters in Washington and its staff of international professionals limit the effectiveness of its operating role in local ventures such as micro-credit lending. Following a wholesale (instead of retail) approach to development via smaller organisations in the field is more appropriate for *hands-on tasks*. This will help fill the need of making the WB's programmes more country-specific.

According to Einhorn (2001:33), the World Bank is now clearly due for a "managerial" cycle to follow its visionary one. Taking on ever more grandiose ambitions has resulted in the WB losing focus. In addressing its internal management, the WB should narrow its **focus** and raise its profile of core competencies, i.e. becoming a global leader in mainly two areas: as a development agency and in the delivery of global public goods. The WB's *mission creep* has led it further away from tasks on which it is even feasible to have accountability. If it reverses this trend, not only will it become more effective, but it will also be better able to create accountability for results achieved in especially LICs; this would raise the legitimacy of its governance and give credibility to its leadership. There is also a need for re-organisation in the WB. One suggestion is putting finance ministers

in the lead to strengthen the hand of those policy-makers who see the WB as a key role-player in expanding the global economy. This will simplify the WB's role as a partner with the WTO and the IMF in expanding global prosperity (Einhorn, 2001:34). Another suggestion is for the World Bank to transform its Development Committee into a decision-making body and provide it with more effective control over the activities of the WB and the IMF (Camdessus, 2005:16). Its purposes would be, *inter alia*, to review the transfers of real resources to developing countries. The change would strongly signal the high priority given to the involvement of governments in development decision-making.

As a **long-term lender**, the World Bank has an enormous task. Camdessus (2005:11) argues that this should include reintroducing grants in the panoply of its instruments for development, and working hard to progressively bring market financing to the emerging countries. Given the need for development and more rapid progress towards the Millennium Development Goals (MDGs) – complementing some good work the World Bank is already doing in this area – this role should be enhanced by:

- the WB concentrating more on investment in infrastructure and technology;
- shifting more of its attention from nation-states to cities (especially mega-cities) where many of the most critical unfinanced needs (and initiatives) are;
- intensifying its cooperation with regional development banks (RDBs), yet retaining the responsibility of taking the lead on development issues and projects;
- continuing with technical assistance and developing local financial markets, and
- working towards real solutions for corruption (which undermines development) by helping to create conditions and an environment in which political leaders experience the benefits of basic ethical requirements of business or official life.

The WB should embrace and enhance its contemporary role as a **global development agency** by taking leadership in coordinating and participating in global development activities and policy dialogue, involving development partners from around the world (Pincus & Winters, 2002:24). With its expertise the WB could simultaneously combine its role as a knowledge bank and promote a market in development thinking and practice to generate ideas and projects beyond the boundaries of the Washington Consensus.

6.3.2 Reforming the IMF and the global financial system

The IMF is not a private bank; it is a public institution that has a basic responsibility as regards openness and **transparency**, in particular. There should be no place for secrecy, especially due to the fact that the leaders of the IMF, WB and WTO are not directly elected by the public and therefore have no direct accountability to the public (as of yet). As Stiglitz (2003a:229) argues, “there can be democratic accountability only if those to whom these public institutions are supposed to be accountable are well informed about what they are doing – including what choices they confronted and how those decisions were made”. If they want to perform a global governance function, these institutions need to recognise the global citizens’ basic *right to know*. Apart from being transparent about its discussion papers and other documents, the IMF needs to disclose the expected poverty and unemployment impact of its programmes. Countries should know the likely consequences of what it recommends and be able to hold the IMF to account if it systematically errs in its analyses – if, for example, the increases in poverty are greater than it forecasted. The institution should be held accountable not only for its outputs (including the quality of its decisions), but also for the inputs and the process in decision-making. As the most noticeable gap in the transparency of the IMF, the decisions taken by the Executive Board (e.g. the minutes of Board meetings) should be published; more votes on issues should be taken and recorded so that they can be publicised and governments be held accountable by their citizens for their part in those decisions. In addition, the selection of the Managing Director must be transparent and unprejudiced.

Although the work of the IMF has since 1996 been evaluated by itself, the Office of Internal Audit and Inspection, and external, independent evaluations by outside experts, the actual weakness of **monitoring and evaluation** in the IMF to date has been that all too often reviews and reports are ignored and not followed up (Woods, 2004:410). There needs to be sufficient reform subsequent to any evaluation and the entire process be made public to enhance better absorption of lessons for improvements. Moreover, the horizontal **accountability** of the IMF – the capacity of other actors to ensure that it works effectively, fairly and within its jurisdiction – must be further enhanced and become fully independent. For instance, monitoring and evaluation should also include audits at

country level. Vertical accountability needs to be updated to take account of its changing role in a globalising world economy – particularly as regards its relationship with NGOs and the global civil society. In view of growing public demand, this form of accountability requires an improvement in the voice and participation of developing countries, in particular. To secure broad-based participation and ownership in the process of strategy development and implementation (what the IMF wants), more participation by developing countries at Board level is required. Meaningful participation by developing countries in the processes of priority-setting, policy-making, and implementation and monitoring in an ongoing way is vital. This implies that representative reform within the IMF requires overhauling not just the voting structure but also its decision-making processes, which qualifies as mere *basic requirements* for vertical accountability.

The **voting structure** of the IMF's governance is arguably most in need of real reform due to its palpable unfairness. Apart from not accurately reflecting countries' relative economic strength, the problem with the IMF's current weighted voting system is that it causes a member's voting power to be incongruent to its voting weight, allowing the G8 countries to dominate decision-making even more than their unfair voting margin suggests. As in the case of the World Bank, it is suggested that the IMF adopt a double majority voting system in which an initiative would need to be approved by a majority of the weighted votes and by a majority of members in order to pass. This will enable a fairer representation of countries' voting weights and a greater *symmetry of interests* and preferences of both developed and developing countries (Strand & Rapkin, 2005:237). In order to access the potential effects of a **double majority voting** system, two renowned indices can be considered – the Shapley-Shubik and Banzhaf indices – which are often used in the analysis of voting power to determine the relative influence of individual actors in a voting system. For example, in a voting game with n countries (and country i):

$$[q; w1, w2, w3, \ldots, wn]$$

As shown below, a country's Banzhaf voting power value is simply the number of times it is a *critical* actor divided by the total number of times all countries are critical actors.

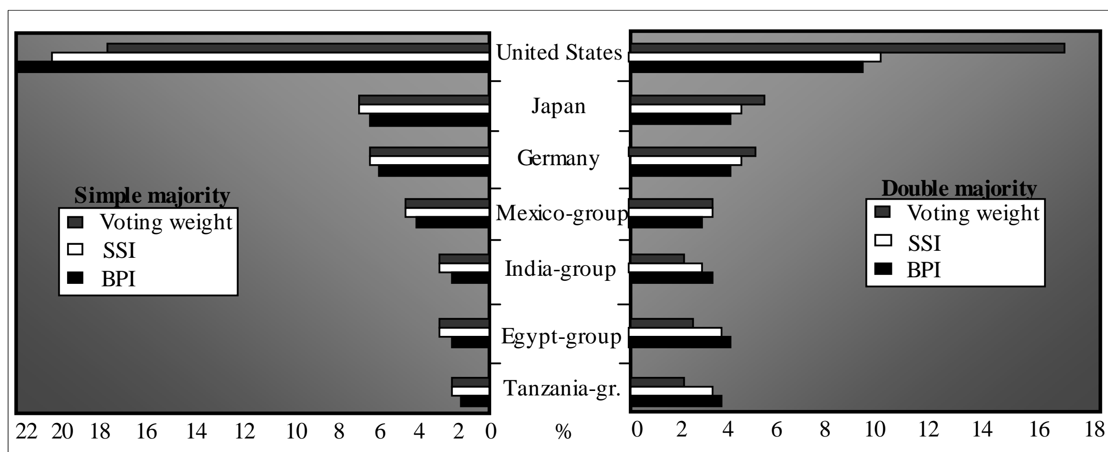
$$BPIi = \frac{BPi}{\sum BPk}$$

The Shapley-Shubik index below assesses countries based on their abilities to serve as *pivotal* members of winning coalitions. This index divides the number of times (i.e. orderings) a country is pivotal by the total number of possible orderings, and multiplies it with the votes (value/influence) added to coalition S by country i.

$$SSI = \frac{(n - s!)(s - 1)}{n!} [v(S) - v(S - \{i\})]$$

Results for both indices sum to 1 and can be expressed as percentages. Both should effect greater congruency in the overall balance between relative voting power and voting weight; hence more equitable representation. Strand & Rapkin (2005:242) have simulated a double majority voting procedure for the IMF's Executive Board, using the two index measures above. Results show that the change from simple majority to double majority voting rebalances the gaps between voting weights and power, thus increasing the voting power of developing countries and decreasing that of the developed. This result in a fairer distribution of voting power and still gives more voting power to the creditor nations.

Figure 6.1: Voting weight and power in the IMF – simple and double majority rules



Source: Strand & Rapkin, 2005:242-243

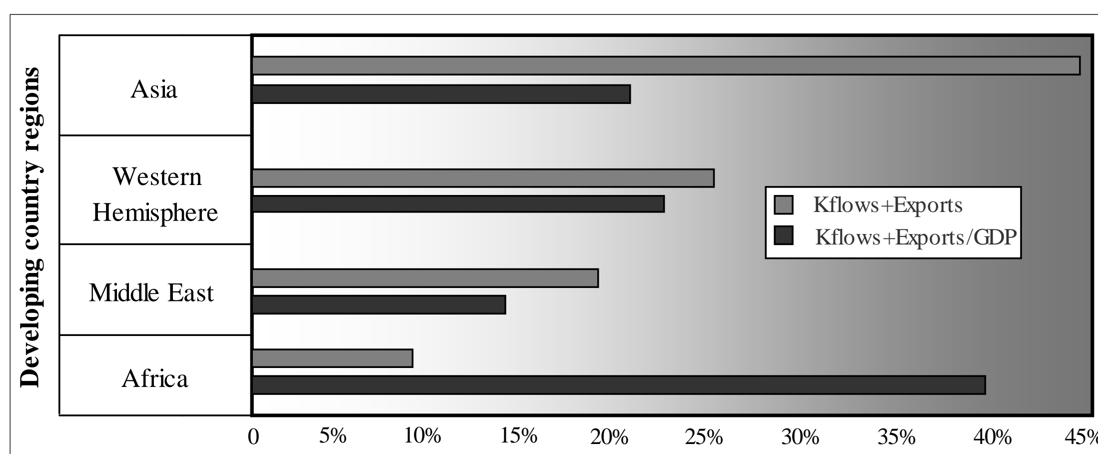
Note: Being headed by specific representatives, the voting groups in Figure 6.1 consist of: **Mexico**, El Salvador, Guatemala, Honduras, Nicaragua, Spain, Venezuela; **India**, Bangladesh, Bhutan, Sri Lanka; **Egypt**, Bahrain, Iraq, Jordan, Kuwait, Lebanon, Libya, Maldives, Oman, Qatar, Syria, United Arab Emirites, Yemen; and **Tanzania**, Angola, Botswana, Burundi, Eritrea, Ethiopia, Gambia, Kenya, Lesotho, Liberia, Malawi, Mozambique, Namibia, Nigeria, Sierra Leone, South Africa, Sudan, Swaziland, Uganda and Zambia. Note also that in total there are about 15 voting groups being representing on the IMF's EB.

As Figure 6.1 shows, two African constituencies (e.g. Egypt and Tanzania voting groups) would have significantly more voting power under both indices, while that of the US (and especially the other G8 countries) decreases considerably. Double majority voting would therefore give developing countries a greater voice and would require the US and other large vote holders to rely on others more for coalition building than they currently do. For a full overhaul of the IMF's voting regime, this method could be complemented by either significantly increasing basic votes to a set percentage, and/or by a switch to a purchasing power parity (PPP)-based version of GDP. GDP at PPP would give a truer reflection of a country's economic strength and would lessen its disparity with voting power. It should also be used in the IMF's **quota formula** calculations to make resource allocation fairer. Corporate governance principles that protect the rights of minority shareholders should also be introduced by the IMF to help separate political power from economic power. Lastly, while the IMF mostly makes decisions based on consensus, achieving consensus is becoming more difficult due to the polarisation between major creditors and others, making it even more critical for the IMF to adopt a truly representative voting system.

In addition to voting reform, the IMF needs to initiate reform concerning its quota formula by including capital flows volatility as an additional variable. This will capture macroeconomic volatility associated with capital accounts shocks as well as countries' vulnerabilities to balance of payment crisis, thus providing the IMF with a better indication of the amount of resources potentially required to stabilise a given country (Dos Reis, 2005:195). A suggestion is to measure and include not only capital flows volatility as a share of GDP, but also volatility in exports as share of GDP. Although the latter already forms part of the current quota formula (as current receipts) of the IMF, it is in absolute terms. One problem with the IMF's quota calculations is that it does not capture coun-

tries' macroeconomic vulnerability to capital and current account shocks. As Figure 6.2 shows, measuring volatility (1990-2003) in absolute terms rather than as a proportion of GDP makes a significant difference in how volatile capital flows and exports of different regions are perceived to be. It even affects the regional ranking among developing countries, revealing that Africa appears, in the latter's case, to be the most vulnerable region.

Figure 6.2: Volatility of net capital flows and exports (1990-2003)



Source: Dos Reis, 2005:207

Table 6.1 indicates that Africa will thus benefit the most from this proposed change in the quota formula. From 1990 to 2002 **Africa's** total volatility of capital flows and exports (measured in absolute terms in the middle-column vs. share of GDP on the right) rose by 24 percentage points, while that of the US declined by over 21 percentage points. It must be borne in mind that although significant, this change represents only a fraction of the whole formula. Moreover, Knight *et al.* (2000:23) contend that "the increasing adoption of floating exchange rates and the surge in international capital flows in the 1990s have led to numerous calls for IMF reform". It is thus clear that the time for curtailing reforms is over. *Ad hoc* responses and half-hearted gestures to reform, its reluctance to admit its policy mistakes and its efforts to defend its stance of institutional infallibility have cost the IMF much of its credibility. Fundamental change based on transparency and a healthy dose of self-examination will assist greatly in transforming the IMF into the effective and legitimate global governance institution for which it is supposed to be appreciated by all.

Table 6.1: Variability of net capital flows and current receipts (1990-2002)

	Variability	
	Current receipts + Net capital flows (US$ billions, share of total)	(Current receipts + Net capital flows)/GDP (in percent, share of total)
Developed economies	62.5%	9.1%
Major industrial	44.5%	0.8%
Of which US	21.4%	0.1%
Other industrial	18.0%	8.3%
Developing economies	29.6%	67.2%
Africa	2.9%	26.9%
Asia	12.9%	14.7%
Middle East	6.0%	10.2%
Western Hemisphere	7.7%	15.5%
Transition economies	7.9%	23.7%

Source: Dos Reis, 2005:205

In addition to reforming its governance structure, the IMF needs to adjust its approach towards stabilisation and structural adjustment frameworks, placing more emphasis on eradicating inequality and poverty. Whereas efforts in these two areas during the 1980s and 1990s have tended to cause rises in inequality – where **SAPs** had major impacts on the poor – a change of approach should mainly involve efforts to (Cornia & Court, 2001:31):

- choose reasonable *stabilisation targets* for inflation and the budget deficit;
- choose a realistic pace for adjustment; often gradual – but irreversible – measures are politically and technically more feasible than more ambitious ones;
- reduce deficits by increasing progressive taxation rather than by reducing pro-poor public expenditures;
- generate sufficient external financing to even out consumption;
- proactively establish adequate and inexpensive social insurance mechanisms;
- rely more – whenever possible – on devaluation and/or other export promotion measures rather than on monetary and fiscal expansion;
- include distributional concerns in the design and regulation of domestic financial regulation and privatisation;
- support policies (including capital controls) to diminish the output volatility caused by financial shocks, and
- improve country surveillance in developed economies – as the 2008 sub-prime crisis in the US has shown – to be equally as intense as in emerging economies.

A reversion to capital controls appears inevitable if countries prefer to assign fiscal and monetary policy to achieving growth. For example, capital controls to support the currency have enabled China to reflate its economy, create new employment opportunities and in this way offset part of the social costs of privatisation. International action – led by the IMF – to curb destabilising short-term capital flows could mitigate output volatility and enhance the scope for evading drastic recession-induced increases in poverty and inequality (Cornia & Court, 2001:32). Capital account liberalisation is increasingly perceived to have caused growing income inequality in many developing countries, making it difficult to reduce the output volatility associated with financial contagion. With exchange rate policy and financial regulation regarded as weak points in emerging economies, all this stresses the need for cooperative international action and IMF leadership with respect to regulatory mechanisms for global financial markets.

Policy-makers, both nationally and in institutions such as the IMF, are increasingly realising that greater care must be taken in assessing the appropriate **regimes for capital inflows** in developing countries. Efficient allocation of capital flows and the extent to which these lead to continued improvements in economic performance will depend heavily on the efficiency and development of the global financial system (Wilson, 2004:178). The IMF, in its recommendations, must emphasise the importance of meeting certain preconditions before countries' capital accounts are fully opened, particularly in view of the risk that a move to capital account convertibility may not improve welfare and may increase vulnerability to financial crises. This underscores a more *pragmatic approach* – with the IMF as the torch-bearer – towards capital account liberalisation. It is important, though, that the IMF should clarify its role in this liberalisation process.

As one of the truly *new* aspects of the global economy, the growing and unprecedented influence of global capital markets increasingly requires actions to strengthen the **global financial system**. Hence, fundamental reform of this system – led by a reformed IMF – is needed to minimise future crises and the risk of contagion that avoids both moral hazard and excessive macroeconomic adjustment in crisis countries (Knight *et al.*, 2000:27). Key reforms therefore include (Stiglitz, 2003a:236):

- *Becoming more aware of the dangers of capital market liberalisation.* Instead of resisting them, the IMF should reinforce interventions by banking and tax systems that attempt to reduce the hazardous externalities imposed by short-term capital flows on those not directly party to these transactions (the borrowers and lenders).
- *Improved banking regulation.* In terms of both design and implementation, this is needed in both developed and less developed countries to curtail short-term lending, in particular. The mistake of too much financial sector deregulation and the excessive reliance on capital adequacy standards must be rectified and adapted to the circumstances and capacities of each country. In addition, the banking system should supply capital to finance enterprise and job creation.
- *Enhanced risk management.* No matter what reforms occur to the exchange rate mechanism, countries will still face extensive risks, especially the less developed. While insurance markets against these risks should be developed, the IMF, World Bank and the developed countries should provide loans to the developing countries that mitigate these risks, for instance by having the creditors absorb the risks of large real interest fluctuations.
- *Improved safety nets.* International assistance for developing countries, especially in agriculture and small business, is essential for building safety nets to enhance the capabilities of the vulnerable within these countries in order to absorb risks. A lack of unemployment insurance programmes exemplifies weak social safety nets.
- *A debt-relief framework.* Such a framework will enable governments to negotiate the rescheduling and reduction of repayment obligations. For LICs and middle-income countries this will offer recourse to a mechanism that limits creditor claims which, more often than not, jeopardise their long-term economic prospects.
- *Improved response to crises.* First of all the IMF needs to warn its members of the outbreak of financial crises in a timely manner. The 1997-98 crises taught the need for a restoration of balance: the concerns of small businesses and workers have to be balanced with those of creditors; and the impacts of policies on domestic capital flight have to balance the excessive attention paid to foreign investors. In addition, Appendix 6B offers an alternative framework for IMF

intervention in the format of a decision-tree, clarifying options for moving from crisis to solution.

Moreover, the IMF should continue being centrally involved in **policy advice** to its member countries. Sensitivity to country conditions and expertise will, however, become more critical in future. In fact, the IMF should develop an ongoing working relationship with a country to help it solve its problems, and to build *policy credibility*. While this involves continuing policy assistance instead of *once-off* advice, it should be a two-way relationship that encourages contributions from both sides. This is important for enhancing ownership in the IMF and helping the acceptance of its advice as impartial. The focus of the IMF's work – outside crisis situations – must be to help markets work better and to avoid the build-up of unsustainable imbalances, such as the current global current account imbalances. Crockett (2004:54) suggests that one way in which it can do this is by setting a standard in its area of expertise, macroeconomic policy. The IMF has developed useful standards of data transparency and could perform a similar function in the areas of monetary and fiscal policy guidelines, complementing countries' efforts. Another key leadership/coordinating role for the IMF is to assist in the dissemination and implementation of standards developed by other role-players in the global financial system. While building a stable and efficient financial system is a complex and time-consuming task, it is necessary to follow a cooperative approach and be sensitive to differing institutional structures across countries.

Just as the introduction of more stability into the global financial system – a global public good in itself – enjoys high priority in the IMF, the strengthening of **ownership** should also be given precedence. The IMF is the one international institution that needs to raise its profile in terms of credibility and participatory governance. In building a relationship of trust with country authorities and enhancing ownership on the basis of giving as much flexibility and empowerment to these authorities as possible, it desperately needs, among other things, to: (1) promote flexibility in programme design by basing its conditionality on attaining broad outcomes rather than on detailed policy actions (*outcomes-based conditionality*) and allowing more flexibility in the timing of disbursements linked to

structural reforms (*floating tranches*); (2) devote more effort to provide technical support for capacity building in low- and middle-income countries. In terms of its conditionality, the IMF should seek to minimise its interventions and aim for greater consensus and commitment (Bird & Joyce, 2001:81). The idea is to streamline conditionality, based on the principle of *less is more*. Programme conditionality might be reformed to even follow a sliding scale; governments that follow a recognised economic reform agenda and have a good track record of economic policy could receive light conditionality, with this becoming heavier only when governments are disinclined to formulate their own programmes or in case where past promises have not been kept.

IMF programmes should include more country-driven strategies, making poverty alleviation the focal point of economic policy, together with a renewed emphasis on rapid growth led by the private sector. The IMF should give more recognition, though, to the role of **global corporations** in the intensification of movements of short-term capital and the often destabilising impact on the global financial system. In cooperation with member countries, the IMF should initiate and strengthen the design of a counteractive strategy, comprising a global regulatory framework for MNC behaviour and involvement in countries – in particular vulnerable host LICs. With privatisation now a *given* in many countries, regulation is increasingly the key entry point for equity concerns. The IMF should assist countries to establish various regulatory mechanisms and subsidies to ensure that service delivery to the poor can be deployed, thus increasing the relative effectiveness of privatised utilities. In addition – especially during times of crises – the IMF should also play a **role** in encouraging ongoing communications between a debtor and its private sector creditors and the establishment of standing creditor associations. Introducing collective actions clauses in sovereign debt instruments, for instance, will further strengthen the IMF's *coordinating role* in bringing debtors and creditors together.

6.3.3 Reforming the WTO and the global trading system

As the WTO has outgrown the processes appropriate to an earlier time, there is con-sensus among its members that they need a process with a greater degree of internal **transparency** and inclusion to accommodate a larger and more diverse membership

(Walden, 1999:8). It is unacceptable that the terms of many trade agreements are still negotiated – and the agenda set – behind *closed doors*, with little public debate about specific provisions. Procedural reforms are needed to reveal deliberations about trade issues. Small groups of countries, involving all members, should be chosen to reflect the various interests of both large and small trading countries, ensuring an open and transparent process in which the views and voices of all are heard. Similarly, the deliberation process must accommodate the active involvement of role-players other than trade ministers alone; e.g. science ministers for intellectual property matters, environmental ministers for when trade policies affect the environment, and the global civil society. For more *transparency*, the WTO should also disclose all contacts between governments and written submissions relating to trade negotiations. For more **inclusion**, developing countries must participate more in rule-making. While each country has a single vote at the WTO, in practice, the US, Europe and Japan dominate proceedings (Stiglitz, 2003a:225). This has to change. A reform which aims to counterbalance the asymmetries in the global trade network bargaining system and provide insulation from the politics of decision-making on trade and foreign investment issues is urgently required.

More opportunities for developing countries should be created by the WTO for their concerns to be heard in order to, at least, achieve significant concessions. Although interests might not fully coincide, China's joining of the WTO will certainly make the developing countries' voice more powerful. Reforming the WTO will require a more *balanced trade agenda* – more balanced in treating the interests of the developing world and the concerns (e.g. environment) beyond trade. Reforming the global trading system has until now been approached as purely a matter of bargaining, from which the poor and the weak, the developing world, have nearly always emerged as losers. Yet, ironically, as Stiglitz and Charlton (2005:xii) argue, "both the North and the South as a whole could benefit from a fair and development-oriented [trade] agenda". *Developed countries* – the most powerful actors within the WTO – must do their share to help integrate developing countries into the world trading system, mainly by reforming their own trade policies in ways that open trading opportunities to the developing world. They have a responsibility, especially in view of their key role in the politics of global trade negotiations, to build the

global trade architecture in ways that enhance the participation of the developing world, thus unlocking the potential of fair trade as a prime engine of growth and poverty reduction. This implies – at the very least – drastically reducing subsidies and tariffs.

Another reform requirement for a fair trade regime would be a *new body* within the WTO responsible for **assessing** the impacts of proposed trade provisions on development and developing countries. It should also objectively consider the consequences of alternative proposals for all member countries. Such a body could, for instance, attempt to assess the impact of supposed non-trade-distorting agricultural subsidies in a world characterised by capital constraints. It could also provide guidance on whether a proposed regional or bilateral trade agreement is consistent with the principle that *trade diversion* should be limited, and be less than the amount of *trade creation*. An expanded WTO secretariat might also include an independent body to assess countries in crisis, to adjudicate and approve the imposition of trade restrictions (i.e. safeguard measures), and to investigate dumping charges, phytosanitary conditions and countervailing duties. In helping LICs to strengthen their institutional capacity, the WTO will also need to adjust existing structures in order to increase its scope of **technical assistance**[68] and expand its capacity to provide financial assistance to these countries. In fact, all existing and future WTO agreements should be appraised (as regards implementation and other costs). This would condition the phasing in of these agreements in the developing countries on the provision of commensurate financial assistance (Rodrik, 2005:146). The WTO should also allow developing countries to require additional compensation when a dispute settlement panel rules in favour of a complainant from this group. Furthermore, with developing countries often disadvantaged in expensive and complex legal proceedings, the WTO should consider an expansion of existing legal assistance schemes to ensure institutional fairness. The WTO should, in fact, also provide expanded legal and fact-finding assistance to its developing country members in prospective dispute settlement cases.

[68] As a progeny of the Integrated Framework for Trade-Related Technical Assistance, the Financing Facility for Trade-Related Capacity Building should develop a budget of about $250m to support a coordinated program of training and other activities to enhance representation among developing countries at the WTO.

There is wide consensus about the critical role of international trade in the promotion of **economic development** and poverty alleviation. However, while the WTO has indicated its commitment to this, the infancy of its initiatives concerning development through trade is revealed in its making promises more than showing results (Stiglitz & Charlton, 2005:56). Little has come of the promise that a *rules-based system* of world trade would protect the weak countries from unilateral acts by the large trading powers, and it has not lessened the risk of isolation from world trade against which these countries were warned just prior to the creation of the WTO. For its legitimacy's sake, the WTO needs to become more accountable and independent. This will require it to become **less dependent** on the US and other advanced economies' financial contributions. The *legitimacy* of the WTO is also suffering due to the absence of a clear set of **trade principles**. A lack of discussion, let alone agreement, on such principles has deprived the WTO's members of any means of collectively choosing a set of policies from among competing proposals. The WTO needs to **guide** the world trading system toward commonly agreed values to make the global trading environment more predictable and a more open forum for the settlement of disputes. In fact, a truly economic development round of trade negotiations is required, based on principles and values such as (Held, 2005:17):

- *Any agreement should be assessed in terms of its impact on development* (items with a negative effect on development should be excluded from the agenda). Impact analysis is supposed to be driving the prioritisation of trade issues on the WTO agenda, not the momentum of special interest groups as is now the case.
- *Any agreement should be fair.* Benefits derived from welfare gains in the multilateral trading system should be equitable, making social justice pivotal. While fairness has complex implications for trade agreements, the norm should be that, *if in doubt*, a larger share of the benefits should accrue to the poorer countries.
- *Any agreement should be arrived at fairly. Outcome fairness* requires fair procedures and a transparent bargaining process. Procedural fairness needs to deal with the asymmetry of power and that of information among WTO members. Unlike power disparities, informational disadvantage can be relatively easily remedied.
- *The agenda should be limited to trade-related and development-friendly issues.* The WTO should follow a more conservative approach regarding the growth of its

mandate. Issues must be highly relevant to trade flows and there must be significant rationale for collective action. Development-friendliness is non-negotiable.

There is a strong need for more **flexibility** in policy proposals at the trade rounds. In the Doha Round it was proposed that multilateral disciplines in competition policy be introduced, but this would limit the ability of governments and local firms in the developing world to take advantageous actions. Although the WTO should serve as a device for commitment to good policies, such commitments ought to be part of voluntary plurilateral arrangements instead of compulsory elements of the WTO's *single undertaking*. In fact, reform of the WTO should include a move away from agreements which enshrine compulsory rules under the single undertaking. The WTO could differentiate between core and non-core disciplines and apply compulsory commitments to the former, while allowing the latter to be passed over by developing countries on development grounds (Hoekman, 2003:87). Such flexibility and differential treatment would facilitate the design of trade agreements that are more likely to promote economic development.

A key *lacking element* of the global trading system is that of developing countries' persisting limited **market access**. In making this system fairer, these countries would gain tremendously in areas such as agriculture, intellectual property, unskilled intensive services, and others if they be given more market access. What matters, for instance in market access, is not only the average tariff, but also the *structure of tariffs*. For example, higher tariffs on more processed food than on less processed have an inhibiting effect on the ability of developing countries to increase their manufacturing capacities. Because developed countries gain more from liberalising their markets than developing countries do from liberalising theirs (due to lesser adjustment costs and competition from open developing markets), the WTO needs to provide more assistance to developing countries in making the required adjustments, giving them longer time to adjust. It is thus suggested that reform of the *global trading system* – under the leadership of the WTO – include provisions for **special treatment** of developing countries:

- all WTO members committing themselves to providing free market access in all goods to all developing countries poorer and smaller than themselves. Developing

countries should thus expect free access to all markets with (1) a larger GDP, and (2) a larger GDP per capita;

- the promise of market opening not be undermined by technical provisions such as rules of origin (where preferential liberalisation is inhibited by complicated rules);
- developed countries committing themselves to the elimination of agricultural subsidies, and the elimination of all tariff peaks and tariff escalation for the LICs;
- built-in *opt-out rights* for developing countries and an end to single undertaking;
- a review of existing agreements that have been negotiated to the detriment of developing countries (e.g. TRIPS), and attending to areas such as commodity prices;
- the General Agreement on Trade in Services (GATS) agreement should be rebalanced, with more focus on developing country interests and less emphasis on the interests of the developed world and especially influential MNCs, and
- restricting the use of anti-dumping measures in developed countries when exports originate form developing countries (due to the consumer costs of anti-dumping).

The above proposals appear much less radical if trade is regarded as a means to development, rather than an end in itself. To enhance the **fairness** of the global trading system, reciprocity should not be the key feature of these negotiations, as they have been in the past. Apart from increased market access, provisions should also be included in trade agreements to compensate for a lack of skilled labour and ownership of physical capital in developing countries. Their disproportionate position is reflected in how what they export and import differs from that of developed countries. Decisions at the WTO and in trade agreements on which goods and services to liberalise, and distinguishing between those that are subject to restrictions on subsidies, can make a *significant difference* for the general trade equilibrium. If the developed countries is serious about promoting development in the developing world, developing countries should be given the opportunity to gain significantly from increasing production (without impediments) in markets in which they have a natural comparative advantage, and developed countries should be restricted from protecting themselves in sectors that are of greatest concern to the developing world. As Rodrik (2005:141) contends, the exchange of reduced policy autonomy in the developing world for improved market access in the developed world is

a bad and unfair bargain as far as development is concerned. For trade liberalisation to benefit the developing countries on a sustainable basis, it has to be carefully managed by the WTO, which should become an institution that manages institutional diversity rather than imposing uniformity.

It must also be pointed out that in view of the deepening consolidation of corporate power in the global economy, a new anti-trust investigation agency should be established under the auspices of the WTO to investigate threats to the public interest posed by monopolistic abuse (Sen, 2002:257). A **Global Anti-Trust Mechanism** will assist in making the WTO more independent and would help dissipate allegations and suspicions of it being influenced by corporate interests. It will better enable the WTO to guard over corporate interests in global trade being furthered at the expense of human development.

Held (2005:16) contends that the WTO "need to move their **agenda** away from a narrow set of policies concerned with market creation and supervision to a broader range of policies that encourage different national economic systems to flourish within a fair and equitable rule-based global market order". In the end, the aim with reform in the global trading system is to ensure that international trade agreements are beneficial in managing cross-border global public goods (or positive externalities) to facilitate a fair (as possible) distribution of global benefits. At the very core, the basic idea is to allow the trade dimension of globalisation to better help poor people. Putting development first establishes a *more balanced trade agenda* to steer the multilateral trading regime in the right direction.

6.3.4 Threats to the reform of the IGEGs and the global economic system

One of the key issues that often dampen the enthusiasm for genuine structural reform in global economic governance is the **lack of commitment** by national leaders – especially those of the developed world – to change involving economic sacrifices. This lack of political will and, at times, even social or individual will slows down decision-making and processes that entail putting structures required for change in place. Among the concerns posing the largest stumbling block is the **role of the US**. The clear and present danger is that the US and its developed country following will support new rules that mainly/only

protect living standards in their own countries while overlooking the pressing need to address the widening income and technology gap between North and South (Moshirian, 2005:310). There is a real risk that the deeper reforms of voting and representation will be prolonged or even deserted due to those in control of the IGEGs not willing to surrender control. The US will not easily give up its effective veto. It is even possible, although unlikely, that this could result in no global governance instead of more or less.

Other threats to global economic governance reform involve dealing with **trade-offs**. It is unavoidable that decision-makers in the IGEGs (and domestic policies) will be confronted with competing/conflicting reform alternatives. This might lead to the stalling of processes geared towards structural change. These trade-offs could even incur costs borne by parties that are supposed to benefit from reform. For example, at the heart of transparency and evaluation are choices and trade-offs as to which kinds of information are collected by whom and how, since for obvious practical reasons not all information on all governance activities can be collected and released (Woods, 2004:411). Monitoring particular activities entails opportunity costs, which need to be taken into consideration. Increased transparency also involves costs that are, as in the case of the IMF, borne by the borrowing members via increased loan charges.

A key prerequisite for the future success of global economic governance is that it complements, rather than **undermines**, countries' – in particular developing countries' – national development strategies. This not being the case, it will further erode the credibility and legitimacy of the IGEGs, which is likely to result in further tension between the developed and developing worlds. With the growing prominence of China, India and other leading developing countries in the global economy, this is highly likely and could fragment and derail the drive towards better global economic governance. With fears in the developing world that more global economic governance will only be a parallel development to the Americanisation of the world economy, resulting in more sacrifice of local cultures and uniqueness, the IGEGs will need to ensure that the opposite occurs and that the developing countries tangibly experience the benefits of global citizenship.

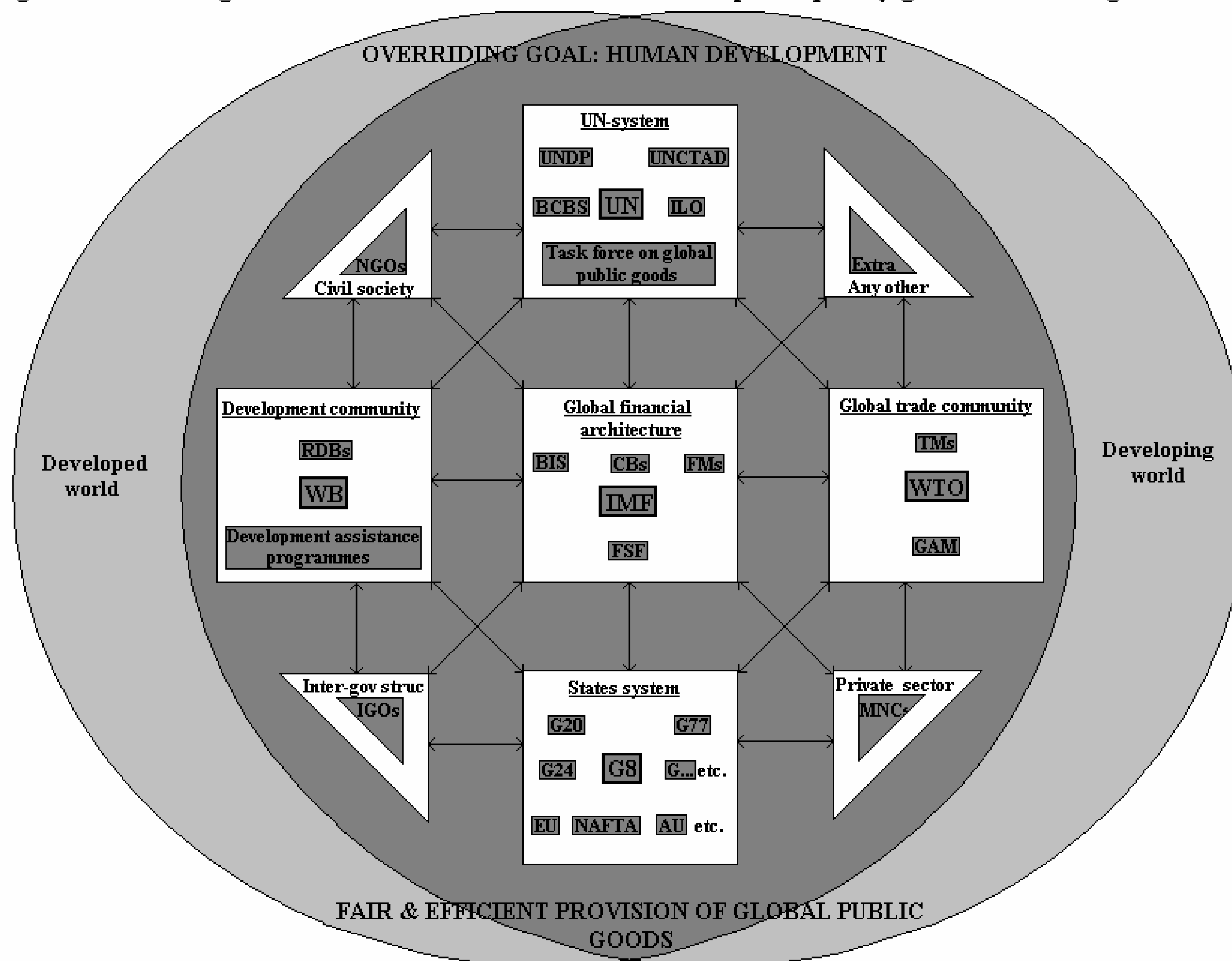
6.4 Building a more participatory and integrative governance framework

Globalisation has engendered fragmentation of both authority and control at all levels and cannot be expected to produce supra-nationalist global polity architecture. With more pronounced competition between sites of governance, Mortensen (2000: 192) argues that "contradictions and incoherence have come to dominate the relationship between different sites and levels of global economic governance". There is the need for more autonomous and *interlocking* multilateral institutions forming the backbone of a democratically networked and coherent global economic governance framework that efficiently links up with other significant role-players in global governance. It must be a non-hierarchical pluralistic structure with no *control at the center*; rather multiple actors performing separable yet complementary functions at different governance sites, addressing specific issues. The challenge is to establish a legitimate global economic polity that can make the (globalising) global system work for maximum human welfare – hence, making globalisation functional, to civilise it. Given that, as Helleiner (2001:247) asserts, "there is now broad consensus that the global economy is undergoverned", it has become necessary to not only put in place an adequate system of economic governance, but also ensure that such a system is sufficiently integrated to provide the required economic guidance to the overall global system; e.g. to involve enough role-players to assist in decision-making. The task is to build *a new consensus* on global economic engagement, i.e. real socio-economic development, more global financial stability and fair trade based on increased international cooperation and the sharing of mutual benefits.

As perhaps the most pronounced example of how global economic governance could be remodelled, the present study proposes a framework (Figure 6.3) for more inclusive and participatory governance. Note that this is merely a broad and sketchy framework that serves as a starting-point for investigation, debate and design in this direction and not – as expected – the final product. The first and most important aspect to point out is as, Figure 6.3 shows, that the *space* where concerned role-players in global economic governance should interconnect is where the interests of both the developed and developing worlds meet. The idea is that this *shared space* must grow to create an increasingly **mutually beneficial** global environment for both the North and the South in order to enhance par-

ticipation and cooperation among various institutions and role-players – whose interests are represented in this framework – in the global economy. It also reflects the importance of cooperation between the developed and developing world in both providing and receiving global public goods, with economic development as the primary goal aimed for.

Figure 6.3: An integrative framework for more inclusive and participatory global economic governance



Abbreviations: Bank of International Settlements (BIS), Central Banks (CBs), Finance Ministers (FMs), Financial Stability Forum (FSF), Basel Committee on Banking Supervision (BCBS), International Labour Organisation (ILO), Regional Development Banks (RDBs), Trade Ministers (TMs), Global Anti-Trust Mechanism (GAM), African Union (AU) and Etcetera (etc.).

Source: Own contribution

Note: Although several sources (e.g. Buira, 2005:21-26; Bird & Joyce, 2001:89-92; Dos Reis, 2005:202) stressed some of the components of this framework, it is compiled based on the author's own views and understanding regarding the creation/building of a more integrated global economic governance system. Also note that although the UN, BIS, ILO, BCBS, etc. is not part of the analysis in this study, they had to be included in this framework as they ought to form part of it.

As the central pillars in the global economic governance framework and leaders in their governance sites (see Figure 6.3), the **IMF**, **WB** and **WTO** must *coordinate* more closely to ensure that their policies are cohesive and support each other. For instance, financial problems cannot be solved without attending to development concerns (especially in the developing world) and without a thorough investigation of trade problems and solutions. There is a very close link between finance, development and trade in this globalising world. Furthermore, a reformed **UN**[69], through its agencies, can and should play a key facilitating role in *nudging* the world economy in the direction in which a majority of its members already agree, i.e. intensifying efforts towards global integration with growing emphasis on actively encouraging appropriate political or quasi-political processes toward improved global economic governance (Helleiner, 2001:249). Importantly, the interactions and interdependence between individual institutional reforms and broader governance reforms need to complement each other. Notably, this is the *nexus* of global reforms that should define the reform agenda and exploit **synergies**.

Given the **G8**'s key role in setting the agenda and priorities in global economic policies, it needs to cooperate more with the other Gs (e.g. G20, etc.) on realigning this agenda to incorporate more developing country concerns and initiatives. This, together with the variety of **regional groupings** on and between the continents (due to increasing regionalisation), should form part of the *state system* in Figure 6.3. It is essential that the LICs, in particular, be included in this system. In the triangles there are the *fringe* role-players, which are becoming more influential in global economic policy-making, i.e. the global civil society (mainly NGOs), MNCs, IGOs (from both the North and the South), and other[70] **emerging actors** related to this framework. To a significant extent their interests and concerns also need to be accommodated in the way the global economy is governed.

Although difficult to illustrate, the idea is that literally all role-players should be directly linked to each other through the sharing of mutual interests in how the global economy is governed. Each role-player should be allowed to have its own mechanisms of account-

[69]Although the UN does not form part of the study's analysis, it cannot be neglected from this discussion.
[70]Other/new role-players to cover areas where governance is missing yet needed – to fulfil overriding goals.

ability (towards their interest groups/members) – for example, internal and/or external evaluation processes – which is then *peer reviewed* by the other role-players according to an explicit criteria. If the proposed system is made more inclusive, poor people – even without significant structural change in the IMF, WB and WTO – can then at least gain some influence over global public policy. Since global decisions affect people of all nationalities, individuals of any nationality should have an equal weight in shaping those decisions. Turning this into meaningful human development should be what the *institutional re-engineering* of global economic governance is about. Lastly, at the risk of oversimplification, it is not suggested that this framework be a panacea for the deficiencies in global economic governance, nor is it suggested that this is a perfect model for guaranteeing positive results. It is essential that this framework should regularly adjust to new/changing needs in the global economic governance sphere. It has significant value in illustrating the need for increased cooperation between role-players in a changeable format – bringing the interests of the developed and developing worlds closer – to improve global economic governance. This merging of interests should primarily be progressed by *reform* and improving the efficiency of providing *global public goods* to all.

6.5 Africa and other pressing concerns affecting global economic governance

The following sub-sections briefly emphasise highly critical areas of concern that urgently need to be addressed by a reforming global economic governance system. Notably, dealing with these concerns would be in the best interest of particularly developing countries, and more specifically **Africa**. As a supplement to preceding discussions, it offers more clarity and direction as to what approach to follow or priorities to set in each case.

6.5.1 Contributing to Africa's de-marginalisation

One benefit of giving Africa a greater and more equitable say in global economic decision-making is a better design of policy prescriptions, i.e. policies that are geared more towards addressing the needs of the poor. Many of the other reforms proposed (e.g. in trade and finance) will also help Africa to have a better chance of competing in the global economy. This should be sufficient to, at least, lay a basis for de-marginalisation – a responsibility shared by Africa itself. In addition, policy conditionality also needs to be

guided and moderated to ensure that instead of damaging African economies, it complements African initiatives towards capacity building and good governance – economic and political. Conditionality should be redesigned to be *retrospective* rather than prospective. This would eliminate the tendency of governments to make promises which they fail to keep, and would replace it with a strong incentive for them to build good reputations.

6.5.2 Dealing with globalisation

It is critical that reform of global economic governance helps to make globalisation fairer, and be more effective in raising the living standards of the poor, in particular. The disenfranchisement and separation between rich and poor caused by globalisation will need to be dealt with urgently in its decision-making structures. This will also lay the foundation for a *gradual, but guided* process of global integration, which would allow (and not overwhelm) traditional institutions and norms to adapt and respond to new challenges while preserving cultural identities and opportunities for the private sector at the local level. Globalisation imposes significant new burdens on international agencies with respect to managing transnational forces in ways which enhance *global social justice* and human security. Hence, if the WB, IMF and the WTO do not take the lead in efforts to reform, *worse* globalisation and *worse* global economic governance will ensue. First of all, fairer participation is needed because globalisation is creating a new set of requirements for regulation and enforcement which requires the cooperation of the *have-nots*.

6.5.3 Strengthening the state system

Despite burgeoning markets, states remain the primary agents in global, regional and domestic decision-making. For this reason, governments have a responsibility to make markets work better by swiftly responding to market failures and ensuring that they are efficient. For instance, for liberalisation to work, governments need to take actions to promote exports and new enterprises. States will also be required to become more effective in linking up with relevant global role-players. As *network states*, they should join forces more with regional groupings, the IGEGs and the private sector to enhance their ability to facilitate the effective functioning of cross-border markets. IGOs should also be strengthened to complement states' networking efforts. Furthermore, in assisting their econo-

mies to integrate better globally, governments (especially those in the developing world) should produce welfare-enhancing outcomes – mainly by emphasising human capital development and the transfer of technology. Lastly, the US will need to take a step back and allow other countries to have their fair share in global economic decision-making. In currently being an *elephant in the room*, it is an opportunity for the US to play a more complementary role towards building a mutually beneficial global system. Together with other developed countries, its first step could be to help reform the IMF, WB and WTO.

6.5.4 Incorporating the global civil society

Given that successful mechanisms of governance are more likely to evolve out of bottom-up than top-down processes due to it evoking the consent of the governed, the global civil society should be allowed to help global economic governance generate acceptable and shared instruments of control/regulation. It already plays a role in governing the world polity. With non-governmental actors increasingly exercising authority legitimately in the public realm, global economic governance will have no choice but to give decent recognition to their voice. Apart from being more involved in the *decision stage* of the policy process, NGOs can also help governments formulate policy options. NGOs are often better placed than elected officials to raise issues on the policy agenda due to their close proximity to small communities of people sharing specific interests. With their unique expertise, NGOs also have an important role to play at the level of implementation.

6.5.5 Corporate interests

Just as important as the need is to cooperate with them, so is the need for MNC activities to be regulated within a supra-national governance framework. The role-players in the proposed framework should, collectively (e.g. through a form of *network accountability*), hold MNCs accountable for their dealings in host nations to ensure that public interest prevails over corporate interest. With increasing pressure on MNCs to adopt *corporate social responsibility programmes* to promote sustainable development, this would help to make value-based initiatives such as the Global Compact[71] a success (Legrain,

[71] The Global Compact is an initiative by former UN secretary-general, Kofi Annan, involving business, governments, NGOs, the UN, the OECD and the EU. It is not a regulatory instrument or code of conduct. It utilises the power of transparency and dialogue to disseminate good practices based on universal principles.

2004:205). By giving capitalism a more human face, this is an opportunity for large companies to use their money, power and global reach to step in where governments fail to act – i.e. to give something back to the community. Instead of repeatedly arguing about corporate interests being secretly served, MNCs should be invited to participate (without voting power) in discussions about global economic regulation and management to ensure more transparency regarding their involvement in global economic governance.

6.5.6 Diverse issues that are significant to the governance of the global economy

Environmental concerns are starting to increasingly affect nearly all governance decision-making at both the global and the domestic levels. Important linkages between the environment and the global economy are raising concerns about how to prepare and deal with potential crisis situations. One such link, for instance, is how environmental degradation can lead to poverty and *vice versa*. It is thus essential that global economic governance be comprehensive enough to be in a position to manage any threat to human development, including that posed/caused by environmental risks.

Given, for instance, the relationship between international security and eradication of poverty, the world is in need of a *global security agenda* that enhances economic stability. Such an agenda should also be guided by global economic governance processes. Currently, it demands mainly two (missing) items of governments and institutions: first, an open acknowledgement that the ethical and legal issues posed by the global polarisation of wealth, income, and power cannot be left to markets to resolve and, secondly, there must be a multilateral commitment to the rule of law to ensure robust execution of international law enforcement. With the International Court of Justice having played a very limited role in extending the rule of law to global affairs, what is needed, at least, is a system of permanent international courts to perform this judicial function.

6.6 Conclusion

The chapter has shown that, for global economic governance to become more effective and legitimate, a two-pronged strategy of reform is necessary, i.e. individual institutional reform and broader governance reforms. Proposals presented made the case for a more

integrative global economic governance system that needs, at its core, a truly reforming WB, IMF and WTO to take up reliable leadership positions and serve the interests of the entire global community. In essence, by placing more emphasis on human development and reform of the global financial and trading system, **critical guidance** can be provided for the non-exclusionary integration of the global economy. In view of escalating globalisation, this is essential for eradicating the marginalisation of regions/countries (e.g. Africa). Stiglitz (2003a:226) argues that "the most fundamental change that is required to make globalisation work in the way that it should is a change in governance". Reform of the IMF, WB and WTO and the creation of a more inclusive framework for global economic governance should result in creating a governance system that is more effective and legitimate – the key lacking requirements of the current archetypical. Reforms that are congruent in their politics and content are needed. This is possible although there are no easy solutions and various reforms often compete. The **overriding question**, especially in case of conflicting challenges, must be: *what is best for economic development?*

As Weiss (2000:806) argues, for the IGEGs "the need for critical scrutiny of standard preconceptions and political-economic attitudes has never been stronger". It is crucial that they pursue an economic agenda that *calibrates* the freeing of markets with poverty reduction programmes and the immediate protection of the vulnerable throughout the world. A challenging reality, though, is that the dominant role of the US is arguably the most serious *stumbling block* in the way of structural change. If it remains intransigent, chances for real reform are slim. The US should rightfully ask itself what it has actually gained from being the only country with a veto power over major decisions. The US needs to combine its pre-eminent place of power with **collaborative global leadership**. Notably, although some of the proposals for reform could be considered ambitious, they are not impossible – only the appropriate decision-making is necessary. For instance, even in the case of no change in the voting arrangements of the IGEGs, one could have more African seats; their voice would be heard even if their votes were not counted. **Africa** will no doubt benefit significantly from having a greater say in particularly the design of policies to be prescribed/recommended by the IGEGs, ensuring that more (African) country-specific conditions are taken into consideration. With these institutions'

membership comprising several African countries, this will enhance ownership in and the legitimacy of the IGEGs. It will also establish human development as central foci in all decision-making. The *primary goal* of the WB, IMF and WTO must be to take leadership in creating favourable conditions for global socio-economic development, which should be based on true **participatory governance**, i.e. pro-poor growth and poverty reduction, a stable global financial environment, and an equitable global trading regime.

What is required for the proposed global economic governance framework to be successful is a better balance between *competition* and *cooperation* where role-players interact on the basis of horizontal coordination, serving the interests of both the developed and developing worlds by providing **global public goods** in a free, fair and more stable global economy. Making development the overriding priority and by agreeing on its long-term benefits for all, actors in this system will find it easier to place genuine cooperation ahead of competing interests, i.e. **the new TINA** (*there is no alternative*). The underlying aim should be to find ways to creatively pool role-players' collective strengths.

While there will always be room for improvement as regards the governance of the global economy, **fundamental reform** (or overhaul) of the IGEGs – the first required step – is now more critical than ever. The reality is that globalisation is constantly changing the nature of the global economy and asks for a parallel evolution of *innovative* global economic governance. The drive towards increased modernisation is in need of strong political will. This drive needs to guide the reform debate toward the persistent search for new/improved mechanisms of global governance that, above all, result in global prosperity and benefit all. In essence, what is needed and what the **remodelling of the global economic governance system** is about is creating a *new partnership*: collective effort by the developed and developing countries and multilateral institutions to govern/manage the global economy in such a way that opportunities are created for the developing world – especially Africa – to not just receive from but also contribute to a truly globalising and prospering global economy.

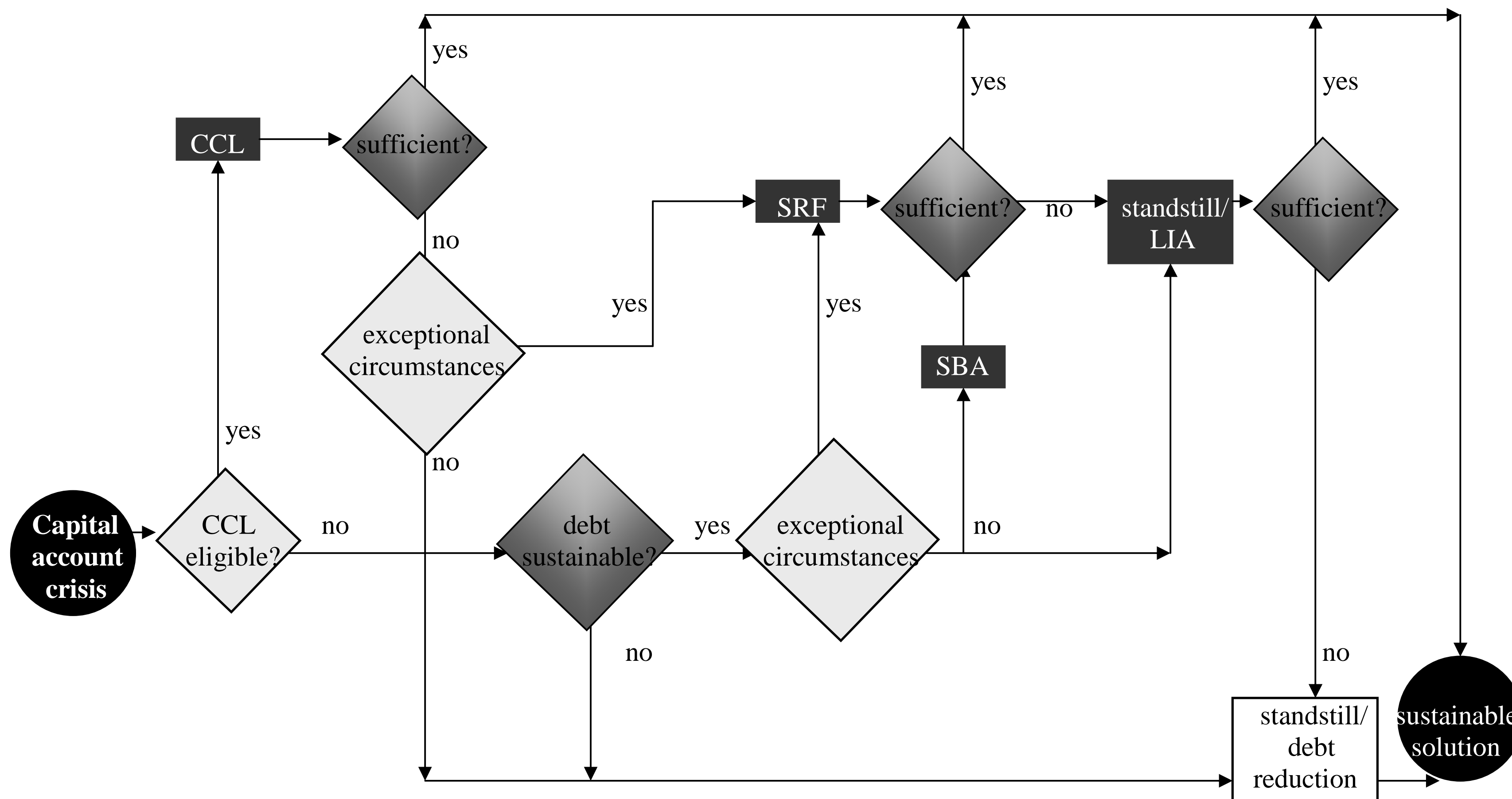
This chapter has not only laid emphasis on how the IGEGs can be reformed, but also proposed how the system of global economic governance can be remodelled. The next chapter shows what reforms Africa, on its part, should make.

Appendix 6A: Models of global democracy – a summary and comparison

	Liberal internationalism	**Radical communitarianism**	**Cosmopolitan democracy**
Who should govern?	The people through governments, accountable international regimes and organisations	The people through self-governing communities	The people through states, associations, international organisations, all subject to cosmopolitan law
Form of global governance	*Polyarchy* – pluralistic fragmented system, sharing of sovereignty	*Demarchy* – functional democratic governance, devoid of sovereignty	*Heterarchy* – divided authority system subject to cosmopolitan democratic law
Key agents/ instruments, processes of democratisation	Accelerating interdependence, self-interest of key agencies of power in creating more democratic/cooperative forms of global governance	New social movements, impending global ecological and economic crises	Constitutional and institutional reconstruction, intensification of globalisation and regionalisation, new social movements, impending global crises
Traditions of democratic thought	Liberal democratic theory – pluralism and protective democracy, social democracy, reformism	Direct democracy; participatory democracy, civic republicanism, socialist democracy	Liberal democratic theory, pluralism and developmental democracy, participatory democracy, civic republicanism
Ethic of global governance	Common rights and shared responsibilities	Humane governance	Democratic autonomy
Mode of governance transformation	*Reform* of global governance	*Alternative structures* of global governance	*Reconstruction* of global governance

Source: Held & McGrew, 2000:417 *The Global Transformations Reader: An Introduction to the Globalisation Debate*

Appendix 6B: Chronology of crisis-resolution – a framework for IMF intervention



Abbreviations: Contingent Credit Line (CCL), Lending into Arrears (LIA), Standby Arrangements (SBA), Supplementary Reserve Facility (SRF)

Source: Haldane & Kruger, 2004:220 "The Resolution of International Financial Crises: An Alternative Framework"

Chapter 7

A proposed African response towards structural adjustment

7.1 Introduction

While it might be true that, as Cheru (2002:34) asserts, "the state of Africa is a scar on the conscience of the world", the fact remains that, ultimately, it is up to Africa to abandon its current state and improve its own well-being. This is the reverse side of the proverbial coin, which requires of Africa to assume more responsibility for its own development. The continent needs to enhance reform and make adjustments that will facilitate its de-marginalisation in order to reap more of the benefits of globalisation and have a greater say in global decision-making in general, and global economic governance in particular. To this end, a strategy is required to ensure appropriate change, including structural, welfare-enhancing policy reforms and a feasible and collective vision (regarding regionalisation and global partnerships) for the future.

The idea of developing an agenda for African recovery in the post-independence period dates back to 1979 when Africa initiated a New International Economic Order (NIEO). As this received little recognition outside the continent, state capitalism in Africa was soon replaced by first-generation neo-liberal reforms underpinned by the Washington Consensus. This developed into second-generation reform measures encapsulated in the Augmented or Post-Washington Consensus (PWC) and, in 2002, the Monterrey Consensus. From this practical confusion of reforms proposed and adjusted by the IGEGs African leaders continued with initiatives for recovery, including the formalisation of the African Union (AU) in 2002, the Millennium Partnership for the African Recovery Programme in 1999 and various other plans, which finally consolidated into the NEPAD-initiative in 2001. Being the first African initiative to receive wide international support, NEPAD – emphasising structural change (based to a large extent on second-generation reforms) and regionalisation – brought new hope for halting Africa's marginalisation in the globalisation process. Unfortunately, due to NEPAD's weakness of being remarkably short on details and delivery mechanisms (Luiz, 2006:641); it has not sufficiently delivered on its promises. Hence, questions as to what adjustments to make and how to

re-strategise development efforts are slowly starting to surface throughout the continent. Given the increasing globalisation of the world economy, the current period could be the last window of opportunity for Africa to start closing the gap between itself and most of the rest of the world, to ultimately defeat underdevelopment and stagnation.

This chapter aims to balance the importance of country-specific **reform deepening** with that of regional integration in Africa as well as the building of global partnerships with key external role-players. It attempts, in particular, to contribute towards a strategy for the continent's de-marginalisation, with the eventual aim of it leading to an improvement in Africa's standing in the global economy and for it to become a respected participant in global decision-making. As a central focus, the idea is to promote a collective strategic approach to African countries' efforts to address both their development needs and Africa's need for deeper integration in the world trading and financial system. The following sections will first investigate an African reform strategy that includes three specific key areas: economic development, the financial sector and trade[72]. The way forward in terms of Africa's regionalisation efforts is then considered, followed by emphasis on the importance of building global partnerships to strengthen Africa's own labours.

7.2 Deepening African reform: building a strategy for reversing marginalisation

Underlining the critical need for reform, Collier (2007:178) points out that most African countries "are resource-rich but policy-poor". However, much of the reason why many African economic reform efforts have been unsuccessful can be linked to either wrong/ non-implementation or implementation without a strategy in mind. The three focus-areas of this section attempt to assist in the building/formulation of such a strategy to *improve reform success* and to promote a collective continental reform approach for Africa. Equally important is the fact that selective country-specific reform is necessary, which implies that countries test and employ those reforms that are of particular benefit to their progress – especially economic. Hence, a *fine balance* needs to be maintained, guided by country discretion and continental vision. The reforms suggested also attempt to enhance

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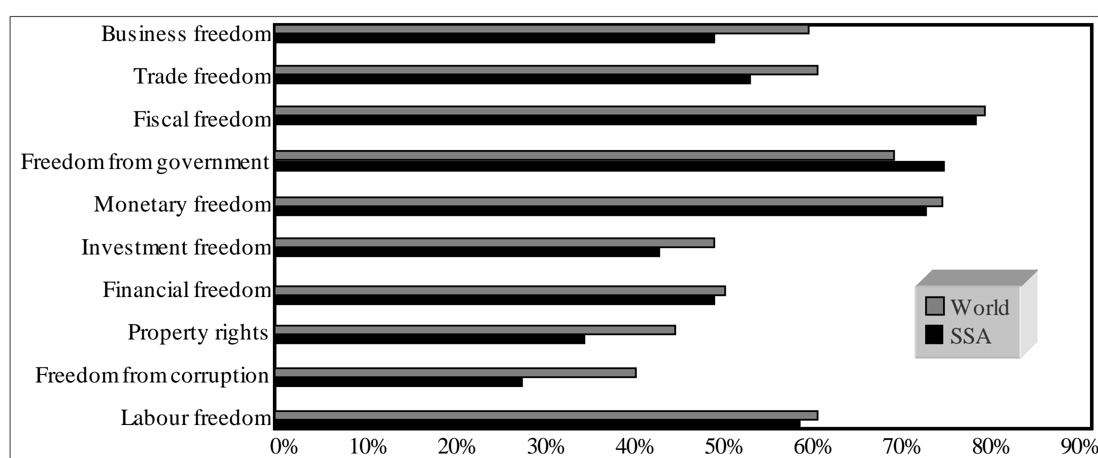
[72] The study concedes that a myriad of reforms are required (with some already materialising) in Africa, but will not be able to focus on them all. Reforms stressed under this section are not only some of the most critical but also correspond in terms of issue – for cohesion – with those emphasised in chapter six.

Africa's ability to attain all the MDGs, especially goal one, the eradication of extreme poverty and hunger, and goal eight, developing a global partnership for development. Despite the need for reform deepening, it should be noted that some African countries have already successfully implemented many of these and other reforms. With most African countries freer today than in the mid-1990s, Figure 7.1 illustrates that SSA is in half the cases close to being as free (or freer, in one) as the world – mainly due to reform.

Figure 7.1: Freedom scores (2007)



Source: O'Grady, 2008:6 "The Real Key to Development: 2008 Index of Economic Freedom", *The Wall Street Journal*

Lastly, the following reform proposals emphasise both so-called *sustainable growth factors* (e.g. macroeconomic stability and production transformation) and *framework conditions* (e.g. quality institutions, infrastructure and education). Concurring with Rodrik (2003:3), structural reform in Africa cannot work without these two ambits complementing each other. The proposed reforms have these key overarching objectives:

- enhancing economic growth and human development in Africa;
- stimulating investment (foreign and domestic, private and public) in Africa;
- developing Africa's trade capacity, diversity and policy effectiveness;
- promoting, through benefit-sharing, a culture of learning and adjustment in Africa
- human and physical (e.g. infrastructure, institutions, etc.) capacity building, and
- expanding and strengthening Africa's relations with external partners.

7.2.1 Economic development-specific reform[73]

Economic reform attempts to enhance development effectiveness (more favourable conditions for development) and to improve Africans' *enabling capacity* to participate more meaningfully in their respective economies. The idea is to promote an environment complementary for the IGEGs', especially the **WB's**, development initiatives in Africa.

Goal 1: Improving macroeconomic management

Since structural change is a function of economic growth (Loots, 2006a:22), it is critical to consider what determinants of macroeconomic stability are important for sustainable growth. In view of this, ensuring broad macroeconomic stability not only includes low inflation and fiscal deficits, but also stability in key relative prices (e.g. real interest rates and real exchange rates), sustainable current account deficits and private sector balance sheets, and smooth business cycles. It is vital that African countries maintain a prudent macroeconomic stance and strictly avoid policy reversals, thus preserving a stable and predictable economic climate, particularly for building investor confidence (Anyanwu, 2006:63). Coherence and transparency are key requirements for macroeconomic policy reform, especially given thoughts about increased policy coordination among African countries. Apart from stimulating growth, macroeconomic policy – to positively affect development – needs to ensure that income distribution becomes more equal. Without declining inequalities, growth would be unsustainable and poverty would remain too high.

Firm fiscal policy reform must establish a *virtuous* set of debt dynamics, which suggest that fiscal deficits cannot be financed by money creation. African governments' debt should not be increasing as a proportion of GDP as it should ideally be falling; any fiscal deficit should be financed by government borrowing from the private sector and not by monetary expansion (Knight *et al.*, 2000:19). Fiscal spending by African governments should give higher priority to poverty-related projects such as rural infrastructure to create an *enabling environment* for the poor. In the case of exchange rates, Murray (1999:23) suggests that all countries (especially African countries) should move towards

[73] While many of the reforms highlighted in the following sections are well documented in literature, it is worth pointing out that the aim is to emphasise *reform deepening* of first-, second- and third-generation reforms. The latter include, among others, further trade liberalisation and anti-corruption policy measures.

a system of flexible exchange rates, anchored by a credible monetary policy. This could help reduce countries' vulnerability to capital volatility. During periods of large capital inflows, letting the real exchange rate appreciate via an appreciating nominal exchange rate rather than via higher domestic prices under a fixed or pegged rate (e.g. the African Franc-zone) reduces the likelihood of persistent overvaluation when circumstances change and domestic assets are less attractive. Globally, flexible exchange rates also provide a public good because the need for an ultimate provider of international liquidity is reduced *pari passu* with the extent of floating, thus reducing the likelihood of financial crises, calls for emergency bailouts, and the degree of moral hazard in the system.

In the move towards a fully independent monetary policy and flexible exchange rates, the role of a nominal anchor becomes critical. This suggests that African countries will need to become stricter (and more explicit) as regards **inflation targeting**: lowering and narrowing their target ranges to ensure a stable rate of inflation that will, in particular, promote development (and assist the poor) through price stability. This, together with a credible monetary policy also makes capital account liberalisation much easier by freeing capital mobility without excessive exchange rate risk, thus smoothing out the external adjustment process. It is important to underline that macroeconomic stability on its own is a necessary but not sufficient condition for African economic growth and development – it needs to be complemented by reforms in other critical areas as well.

Goal 2: Microeconomic management that promote competitiveness and collaboration

Comprehensive microeconomic reform in Africa is needed to – at least – provide more effective business services and lower costs (Gelb *et al.*, 2007:45). Of importance here is performance monitoring by means of comparative assessments of *de jure* constraints (e.g. doing business) and investment climate surveys that provide an idea of how firms view the *de facto* severity of constraints and how they impact on firms' performance. This will help identify and mitigate factors shaping business costs to improve the capacity of African firms to compete. Many African countries lack a powerful business sector and it is therefore crucial that a strong and undivided pro-business constituency that takes collective action be built up across Africa. For this, reforms need to take into account the

political economy of Africa's mostly small economies and ensure that especially barriers for new entrants (such as licensing and credit and asset registries) are reduced. Building a unified business forum that includes high-level business-government consultative *fora* (e.g. Investor Councils) across the continent is paramount for enhancing the global (market) competitiveness of African businesses and getting into a position to benefit from globalisation. Competition in both the private and public spheres – as in East Asia – needs to become a hallmark of African development. While it might require a review of fiscal arrangements, reforms should include performance-based incentives in areas such as ports management, customs, tax administration, and clearance or transit time.

Importantly, true African progress will only be realised by **close partnership** between government and business. As Gibb *et al.* (2002:101) argue, "the single most important ingredient for Africa's success in both political and economic terms is the creation of wealth through employment across the broad spectrum of its [Africa's] population". This can only be achieved by sustainable growth that is, in turn, predicated on improving conditions for commercial activity. This is why Africa should rely less on global assistance and more on putting in place the conditions that will allow investment to come to it, because private investment is what actually reinforces sustainable growth, not global assistance. Among others, Mozambique and Tanzania are African economies that give testimony of how vital partnerships between business and government are for successful turn-arounds, based on market-orientated reforms. Although Africa has been guilty of the opposite in the past, it is critical that such partnerships lead to increased private sector competition that enhances market access and the competitiveness of domestic firms.

Goal 3: Institutional and public sector management – good governance and the APRM

Continued improvements in Africa's governance systems are fundamental. Government institutions have to be modernised and upgraded further. African governments should be accountable for their actions, allow the rule of law to prevail, and respect private property rights. Efforts to increase the **effectiveness** of public institutions should be stepped up, particularly if these are to serve as true partners of the private sector. The fact is good governance underpins economic progress and is a necessary condition for development.

According to Neto and Jamba (2006:161), the basic idea behind good governance is “to establish institutions and regulatory systems that are capable of running effective markets”. For this reason, transparency and stability in economic interaction are key aspects of good governance. Even democracy, which makes governments accountable, is an essential component of economic development through its basic credo: freedom – of choice, from servitude and from constant economic dependency.

Africa needs to strengthen **democratic governance** by enhancing, at least, the following enabling mechanisms (Cheru, 2002:54): the rule of law (anti-corruption measures) and constitutional legitimacy; a functioning and active civil society; respect for the rights of different nationalities; a climate of political reconciliation, and commitment to an open and equitable economic regime of growth. Democratic government helps to guarantee political rights, protect economic freedom and foster an environment where peace and development can flourish. This requires that African governments be strengthened, equipped and monitoring systems employed to better perform their task of good governance. Accordingly, one (such) instrument, the *African Peer Review Mechanism* (APRM), should be refined and play a more decisive role in benchmarking the quality of a country’s policy implementation to international standards. It identifies four substantive areas, namely democracy and political governance; economic governance and management; corporate governance, and socio-economic development. The purpose of the APRM is “to provide a clear framework to guide the design and implementation of the assessment in each of these areas” (NEPAD, 2003:4). While it contains standards for key objectives as well as extensive indicative criteria, the APRM needs to become more specific in terms of assessments or measurements of each objective. The establishment of an appropriate national structure, the financing of the process, and the organisation of a participatory and all-inclusive self-assessment system need specific attention. Moreover, it is a good surveillance mechanism for guiding continent-wide development and gaining international credibility as well as attracting investment interest. To make it excellent, however, it requires the **full support** of all African countries[74] as well as a realisation that mutual accountability – its essence – is in the best interest of every African.

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[74] Currently only 27 countries have signed up for the APRM and 13 of them have had reviews launched.

Goal 4: Better management of external finance, aid and external debt

It is imperative that African countries lead the process that would translate development commitments into action. While the Abuja Conference in 2006 is an important step in this direction, more initiatives are required for the monitoring of the implementation of their own commitments and those of the donors. Ensuring that the international community meets the financing gap will also require the involvement of various role-players such as the Africa Partnership Forum, civil society organisations and community-based organisations to, through monitoring implementation, have a significant impact on the delivery of development-financing commitments at community level. Recipient governments could then direct aid to priority sectors with greater potential of improving people's well-being. This will enhance coordination among African countries as well as mutual accountability on the part of both Africa and donor countries. In addition, **aid effectiveness** could be further improved by better donor coordination by African countries. Aid agencies should be encouraged to harmonise standards and focus on ensuring that the money goes to projects and programmes prioritised in national budgets.

Frameworks for handling high, sometimes volatile (and possibly increasing) levels of aid need to be improved. In helping it to attain the MDGs, official development assistance (ODA), in particular, has a crucial role to play – as part of the *big push* that Africa needs – to alleviate poverty on the continent (Sachs *et al.*, 2004:4). For donors, the key is to increase ODA without increasing Africa's dependence on it. For African governments, it is critical to ensure that the current weak relationship between ODA per capita and growth in Africa is strengthened by creating conditions and developing capacities that enhance the complementariness of poverty alleviation and growth. Hence, the importance of a good policy environment and human capacity development is paramount. Better coordination, and the untying of aid from donors' special interests, will also make a significant difference in making aid to Africa more effective (UNCTAD, 2001:52). By paving the way for private sector growth and international integration (with effective aid attracting foreign capital), aid – and development assistance in general – need to support the transformation of African economies. As in the 1980s, aid money should not postpone much-needed reforms, but rather serve as an *incentive* for their implementation.

Furthermore, debt relief has a principal role to play in the provision of adequate external financing in Africa. African countries should make a stronger case for the suspension of debt payments by all African Heavily Indebted Poor Countries (HIPCs) without additional subsequent interest obligations until final agreement is reached on debt reduction, to be extended subsequently to non-HIPC countries found eligible for debt relief. This could help make a significant contribution to growth and poverty reduction provided it is combined with additional official financing to fill the external resource gap. External financing is critical for **closing Africa's resource gap** and raising investment levels so as to meet targets set for GDP growth and poverty alleviation (e.g. for attaining the MDGs) – if it is managed correctly. Evidence from Greenhill & Blackmore (2002:24) shows that debt relief to African HIPCs did result in substantial increases in spending on health and education, which suggests that debt relief[75] could certainly contribute to poverty alleviation in Africa and help build a more attractive investment environment. Equally important, however, African countries' external debt overhang needs to be dealt with urgently as it hampers funds to be allocated for poverty reduction. Debt-service-to-export ratios are still too high and need to be reduced to an average of at least 10%.

Goal 5: Becoming tech-wise and using technology for development

Globally, technological diffusion (now) involves more than the acquisition of machinery and product designs. It requires continuous incremental technical changes in order to improve productivity and efficiency. African countries need to broaden their scientific and **technological infrastructure** to develop the capacity to understand, access, apply, adapt and manipulate technology for development production. More specifically, African countries need to enhance their capacity to produce and trade in technology-intensive goods in order to break the core-periphery pattern of international trade. Moreover, information and communications technology, for instance, can provide powerful new tools both for addressing people's basic needs and for enriching the lives of poor people and communities in unprecedented ways. Hence, every African country needs to have an *e-strategy* and place emphasis on competitive suppliers for a communications infra-structure (this presents a highly constructive opportunity in which the developed world

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[75] Debt relief includes the rescheduling and/or cancellation of debt service, and/or debt stock cancellation.

could provide assistance). With most of its economies either under- or undeveloped, Africa can benefit considerably from the use of even the most basic of technologies – especially due to it becoming more affordable as new technologies are replacing old ones. Areas that will particularly benefit from this include agriculture, energy, manufacturing, mining, fishing, transport, education, health and infrastructure. African economies, which are mainly built on primary industries, may benefit disproportionately from the deployment of basic technologies by increases and growth in these areas. In fact, with technology promising to be one of the most effective and sustainable solutions for Africa's food security problems, the continent need to undergo a fast-track industrial revolution. This has become a minimum requirement in today's *high-tech network age*.

For the African economic renaissance to move beyond excited rhetoric and academic interest, African leaders must face the reality of the continent's technological needs and do everything necessary to **close the technology gap** it has with the rest of the world. Basic technologies have a crucial role to play in the continent's sustainable development. Their deployment needs to form part of any technology policy and be accommodated by reform efforts. Gibb *et al.* (2002:122) argue that currently the biggest hurdle to the deployment of technology in Africa is inappropriate government policies. Through reform, governments need to create an enabling environment that allows policy-makers to design policies which balance market needs with those of society. This will assist in more engineers and scientists being trained (and the *brain drain* halted) in order to prepare Africa's capacity to absorb technology flows. This also requires fundamental reform in African education that gives priority to developing technology-related competencies.

Goal 6: Human capital development and productivity growth

In this era of ever-increasing globalisation and global competition, it has become paramount – particularly for Africa – to enhance human capacities. There is an increasing tendency towards the global assimilation of scientific knowledge and the diffusion of technology, which has resulted in a qualitative shift towards knowledge-intensive production. Cheru (2002:78) estimates that "in the last fifteen years, the role of education has become even more important in economic growth and social transformation as the unpre-

cedented pace of scientific and technological advances transforms the global economy". Knowledge has arguably become the crucial factor in building global competitive strategies and has significantly altered the educational and skills requirements of work and the workplace. Vocational-orientated school reforms – strictly on educational grounds – should be further enhanced in all African countries to accelerate **human capital development**. It should be designed to have a significant impact on the employment prospects of graduates, and on reducing the pressure for expansion of upper secondary and higher education. Through good fiscal management (i.e. in national budgets), rural areas, in particular, should receive sufficient formal assistance and resources to overcome educational disparities (including the gender gap) with urban areas. Linking the world of school with the world of work has to be a minimum requirement for reforming African educational systems. Expanding vocational and technical education should not only result in more employment in the labour market, but also in significant increases in workers' productivity and successful self-employment. Technological progress must undoubtedly be incorporated into existing national human resource development strategies in Africa.

Furthermore, **business skills** are in short supply in Africa, and efforts to strengthen them to close the *productivity gap* between smaller domestic and larger, often minority or foreign-owned firms, are essential. Gelb *et al.* (2007:47) point out that labour skills are a more frequent concern to firms in Africa than labour regulation, which suggests a need for improved worker training and general skills development to enhance productivity. This underlines the need to address the *skills gap* in order to address the productivity gap. Fundamental to economic development, African educational (and fiscal) reform and skills development programmes must reflect the new requirements for global competitiveness. With labour in abundance in Africa, one can only imagine how the continent's productivity will be affected if skills are drastically improved. Appropriate education and entrepreneurial ingenuity are among the most critical keys to the Africa's future progress.

7.2.2 Financial sector reform

The need for Africa's financial sector to be strengthened is immutable. Financial infrastructure reform – as emphasised in this section – is primarily aimed at attracting

more foreign investment; i.e. creating a more favourable investment environment through financial and regulatory reforms, thus complementing the work of the **IMF** in Africa.

Goal 1: Financial infrastructure reform

In concise terms, the key areas of financial infrastructure reform include timely and accurate disclosure of financial data; more effective risk proofed payment and settlement systems; strengthened supervision and regulation; high-quality accounting and auditing practices; stronger corporate governance and insolvency laws, and more effective market discipline (Knight *et al.,* 2000:16). A basic step is for African countries to strive to undertake the reforms necessary to – by making the areas above top priority – implement the international standards and best practices being formulated in various *fora*. The Financial Stability Forum's standards and codes, the Basle Committee's core principles for banking supervision, and the IMF's codes of transparency for fiscal policies and for monetary and financial policies are among the most significant guidance platforms for financial infrastructure reform. Importantly, although the adoption of such standards are voluntary, market participants' recognition that a country is implementing such codes and standards is becoming increasingly decisive in the formulation of a country's **reputation** as a well-managed destination country for international capital flows. Clearly therefore, aligning African financial reforms with such principles will help make it a more attractive investment destination and enhance the effectiveness of its financial system.

African governments have indeed a serious responsibility to improve their legal, judicial, and regulatory environments, particularly as they cannot afford to discourage private investment. As also became clear in chapter five, outdated legal and weak judiciary systems cannot be tolerated in view of increased privatisation of state-owned enterprises (Anyanwu, 2006:63). Important for reform, though, is that this needs to be **balanced** against the fact that liberalisation is a necessary condition for making African economies more competitive and attractive to foreign investment. Financial reform, therefore, needs to perform the dual function of helping to establish a responsible and judicious environment, based on strong and reliable rule of law, while enhancing the competitiveness of African financial institutions, rooted in the attraction of capital.

Together with sound macroeconomic management, African economies will be able to turn financial market globalisation to their advantage by benefiting considerably from less expensive access to capital (Knight *et al.,* 2000:15). This will help build a stronger market discipline which, along with strengthened prudential oversight, will serve to improve the stability and resilience of domestic financial systems. Stiglitz (1998:33) argues that “without a **robust financial system** – which the government plays a huge role in creating and maintaining – it is difficult to mobilise savings or to allocate capital efficiently”. While Africa’s corporate governance needs to be improved, it also needs to simplify business regulations by reducing restrictions on new business ventures by locals and foreigners (e.g. the streamlining of licensing, customs procedures and labour market laws and rigidities). African countries would greatly benefit from increased capital inflows, new enterprise and jobs, and a more business-friendly environment.

Goal 2: Intensifying banking reforms

A key step in strengthening the financial systems of African countries is adequate reform in the banking sector. Although the promotion of microfinance and efforts to enhance enterprise financing are modest attempts by African banks to, in part, address problems[76] with mobilising deposits and lending them to borrowers, more robust banking (system) reforms are required, such as:

- following a harmonised approach to regulation in the context of low restrictions to market entry that would allow financial firms to benefit from economies of scale and scope in larger markets;
- eliminating distortions, such as the forbearance practice of bank supervisors, to improve banking soundness and facilitate greater inter-bank activities, and
- reducing the excessive use of costly monetary instruments (e.g. high reserve requirements) to spur development of the banking sector. African countries could benefit from alternative instruments (e.g. leasing) or alternatives to collateralisation (e.g. group guarantees and reversible equity stakes) to overcome bottlenecks created by weak property rights.

[76] This is a problem (mainly due to a lack of depth in terms of bank deposits and private sector loans) that was pointed out in chapter five. The need to urgently address this problem through banking sector reform is critical for the attraction of particularly foreign investment into Africa.

Moreover, implicit and explicit guarantees made by governments to, or on behalf of, domestic banks must be eliminated. Directed lending by domestic banks to preferred domestic firms and guarantees on foreign loans to private borrowers should also end at once. With most African countries' banking sectors remaining weak and vulnerable to crises (Knight *et al.,* 2000:17), one of the most pressing reforms is the recapitalisation and restructuring of the banking sector, as well as a fundamental strengthening of regulation, prudential supervision, disclosure and **market discipline**. To accelerate this process, a promising suggestion is for African countries to allow foreign banks more scope to enter the domestic banking sector and to acquire under-capitalised or else troubled domestic banks. Foreign banks can inject the capital needed to return domestic banks to viability, thus potentially lowering the burden for African taxpayers. They also bring with them strong accounting standards, disclosure requirements, and risk management and management expertise that are required by supervisors and private investors (Gavin & Hausmann, 1997:46). Foreign entry also encourages competition, thus instilling stronger market discipline and greater resilience to shocks, by forming asset pools that are more diversified across countries, industries and asset classes. Simultaneously with recapitalisation, significant steps must also be taken to improve bank regulation and supervision according to the Basle Committee's Core Principles for Effective Banking Supervision and its other, more detailed, standards.

Goal 3: Capital market deepening

Capital markets can only operate efficiently if investors are convinced that they have reasonable access to financial information about the fundamental condition of debtor governments and firms. Thus, the rules on disclosure and governance, again, are critical for a positive African investment climate. Capital markets trade standardised instruments whose values depend critically on enforceable and transparent regulations governing accounting and auditing practices, bankruptcy and corporate governance. For African countries, for instance, to issue debt in their own currency and develop markets for domestic currency-denominated instruments, their capital markets need to be further deepened and expanded. **Sophisticated capital markets** are inseparable from economic

progress. Hence, there is a need to promote and deliberately support African domestic capital markets and put in place supportive infrastructure for the markets.

One suggestion is that African governments adopt a **sub-regional approach** to the support and development of capital markets, so as to strengthen their catalytic role in mobilising savings. Regional integration – together with further macroeconomic and structural reforms – could help African capital markets develop and overcome the impediments related to size and liquidity (Anyanwu, 2006:65). African governments should support developing African regional and continental stock exchanges because this will facilitate the development of more efficient and competitive markets throughout Africa. Multiple listings and cross-border trade in securities, for example, could be an option in setting up sub-regional stock markets. In addition, it is of critical importance that African stock markets be made more effective. In this regard, four essential requirements that are geared towards attracting more investment include: (1) a set of substantive legal rules that meets a set of clear, well-functioning, and reliable securities laws; (2) improved trading infrastructure; (3) increased participation by local institutions, and (4) increased market liquidity combined with promising future listings.

7.2.3 Trade reform

With Africa in desperate need of gaining at least some competitive edge in the global economy, transforming its trade is arguably the area that holds the best promise for realising this goal. Deepening African trade reform would facilitate the continent's global integration and promote, in cooperation with the **WTO**, a fair global trading system.

Goal 1: Trade diversification and gradual liberalisation

In an Economic Report on Africa, the ECA (2007:41) called for the need of a "third way" in the form of "strategic" trade policies aimed specifically at diversification and development. As with Asia, African governments should put diversification ahead of **aggressive export promotion** of unprocessed primary products. The ECA report pointed out that African economies have since the late-1990s become less diversified and more specialised in the production and export of a limited range of primary commodities,

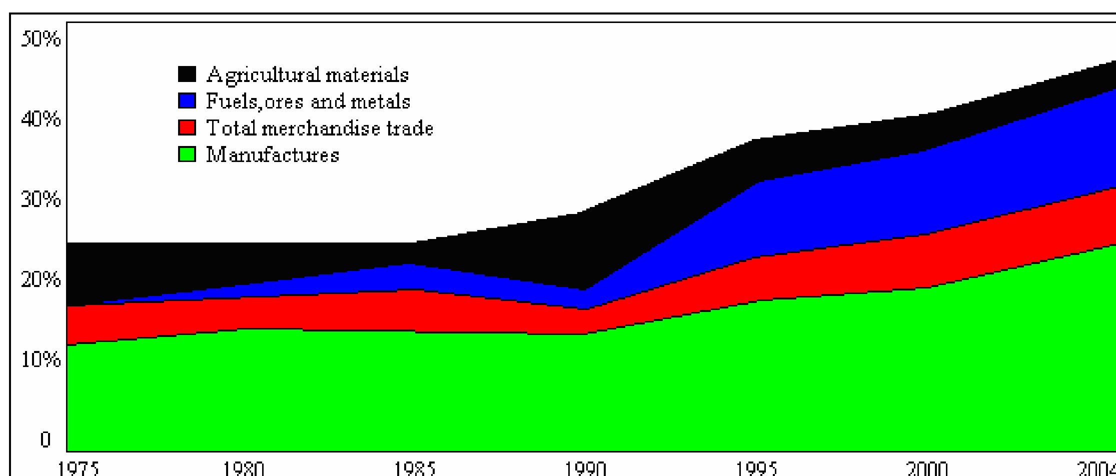
notably oil, gas and minerals. It is vital for an economy to attain a state of *deep diversification* before reaching the turning point towards greater specialisation. ECA evidence indicates that the benchmark turning point should be a per capita income level of approximately US$9000, which is significantly higher than the African average.

Since economies become more diversified as investment ratios rise, increased investment is key to reversing, in a sense, this trend towards specialisation. In Africa's case, the pattern of investment is a crucial determinant of diversification as total public and private sector investment has a positive impact on diversification only where public investment *crowds in* private sector activity. The ECA (2007:55) report also found that rapid trade liberalisation may well slow down diversification. Hence, with African countries needing to diversify more, protective tariffs and other barriers to trade should be maintained for longer periods than in the case of when a country pursues an export-driven growth path. This, though, is not to suggest that there should be little/no trade liberalisation. On the contrary, trade liberalisation should remain a high priority for African countries, but be **gradually implemented** so as to complement efforts – of equally high priority – to diversify exports, while still balancing the latter with a healthy degree of specialisation to ensure that Africa continues, at least, to produce what it is good at producing.

Indicating trade among developing countries (or *South-South trade*) as a share of total developing country trade for the period 1975-2004, Figure 7.2 shows a significant increase, particularly since 1990. Thus, not only has the developing countries' share in global trade increased, but they are trading more with each other. This is important to African trade because of more markets opening up, minimising problems with market access. However, with over 75% of Africa's exports still primary commodities dominated by crude oil, natural gas, precious and base metals and agricultural produce (specifically cocoa, coffee and tea), the concern remains the relatively low levels of manufactures and total merchandise trade (Siddiqi, 2006:24). As became clear in chapter five, this makes the region more vulnerable than other regions to a deceleration of global demand. Africa's trade diversification should primarily focus on these areas to ensure not only an increase in export earnings and competitiveness, but also the enhancement of the

continent's **production capacity** (also through the utilisation of more skilled workers) to ensure sustainable growth regarding exports' contribution to economic growth and development.

Figure 7.2: Growing trade between developing countries (1975-2004)



Source: World Bank, 2006a:329 *World Development Indicators 2006*

The benefits of trade are well-known: providing access to foreign exchange, expanding markets, increasing FDI, facilitating the transfer of technology, and stimulating domestic productivity that leads to employment being created and an increase in domestic incomes. However, these can only fully materialise in Africa if sufficient trade diversification takes place. The ECA (2008:133) argues that African countries' over-reliance on primary commodity exports is, in a sense, *self-destructive*, mainly due to these exports' very low income elasticity of demand and hence less opportunity for rapid export market expansion. Diversification of exports and production structure is essential for Africa to move into the export of new and dynamic products in world trade (Loots, 2005:1). To help overcome the continent's marginalisation, Collier (2006:204) found that Africa would particularly benefit from diversifying exports into **labour-using manufactures and services** due to its low-wage differential advantage to the developed world. By reducing Africa's dependence on traditional commodity exports, it will, in particular, assist in protecting African countries against vulnerability to external shocks resulting from terms of trade instability. To diversify and improve productive capacities requires not only

sufficient domestic reforms (e.g. maintaining macroeconomic stability, a regulatory environment conducive to export promotion, support for the private sector, promote the adoption of ICTs, and develop adequate social, institutional and physical infrastructure), but also assistance from development partners through human and financial resources to help African countries attain their diversification objectives. The following areas will help *fast-track* Africa's integration into the multilateral trading system:

- more technical assistance and capacity-building in trade and export development to help bridge the gap between resource needs and resource availability;
- more meaningful (duty and quota free) market access to the region's countries that will serve as an incentive to diversify and, hence, boost productivity, and
- increasing financial support for regional infrastructure development projects – a major constraint to rapid export market promotion – to reduce transport costs.

Reflecting its economies' high dependence on trade, Africa's trade-to-GDP ratio is currently more than 80% (World Bank, 2008). Together with the fact that the elasticity of trade in African countries is significantly higher than in other developing regions (which implies that a dollar earned by trade has on average a larger impact on growth than in other developing regions) (Loots, 2006a:21), this stresses the importance of expanding the continent's limited range of export products. Africa, therefore, has no luxury in viewing trade diversification as a mere option; it is a must in today's global economy.

Goal 2: Making trade policy more effective

Trade policy should be dynamic and vary from sector to sector: it should target specific potential export growth areas in each sector and build the necessary capacity. This requires the support of other policies to, for instance, create more *fiscal space* for African governments to invest more, backed by a return to more **sector-orientated policies** with less emphasis on the *macroeconomic-stability-above-all-approach.* In essence, African governments need to adopt more proactive policies in the realm of trade, finance, industry and research. They should also be complemented by greater flexibility in African economies to enable policy-makers to switch focus, for example, from exports in oil and gas to growing and processing foods or setting up clothing factories.

While vital for promoting trade and export market development, donor support, for instance, will only be maximised if African countries make more efforts to mainstream trade effectively into their national development strategies (Dupasquier & Osakwe, 2007: 96). This requires involving all relevant stakeholders in the design and implementation of trade policies, and ensuring that trade and other macroeconomic and social policies complement each other, market access impediments are removed, and trade capacity is strengthened. In particular, productivity needs to be improved (Cheru, 2002:134). No trade can take place where production is non-existent. African trade expansion needs to be accompanied by coherent national and sub-regional policies to remove the main obstacles to productivity and export growth, both of which are essential for development. It is critical that reform of African countries' trade policies **address** the following impediments that are among the main reasons for Africa's marginalisation in world trade:

- high transaction costs[77] (e.g. excessive internal transport and freight costs for land-locked African countries as exports must clear customs at road/rail border posts);
- supply-side constraints (e.g. inadequate and underdeveloped industrial capacities);
- weak basic infrastructure (e.g. deficiencies, from rural roads to regional highways, rail networks and port services), and
- a small skills base (e.g. lack of investment in human capital and technologies).

Given the real danger of trade liberalisation harming an economy during conditions of income inequality, trade policy needs to be complemented by, for instance, an appropriate **redistribution policy** of taxes on owners of capital and subsidies to labour, to ensure that both broad classes of factors of production can benefit from international trade (Salvatore, 2004:134). Stiglitz and Charlton (2005:216) point out that there is considerable evidence that poorly implemented liberalisation, particularly in the service sector, can have negative effects on the poor. Carefully managed *implementation*, effective regulation, and substantial assistance are therefore critical for making African trade policy more effective and must form a central part of the continent's reform agenda.

[77] In some African countries, 60% of export-receipts are spent on transport costs (Siddiqi, 2006:25). Overall, Africa's freight costs average 15%, three times more than the average figure for Latin America. Only in SSA, 15 countries' competitiveness is undermined due to cost problems *vis-à-vis* being landlocked.

To make African trade policy more effective, a *fine balance* is needed between (1) liberal trade policies, devoid of the uncontrolled opening up of African economies to external markets, and (2) policies that protect domestic markets. The key is for the former to be selective in terms of allowing foreign competition, i.e. to the extent that it ensures a level playing field, and for the latter to facilitate in the capacity building of local industries, with both, in effect, stimulating African economies to become more mature and be better able to compete in the global market place (preferably on the basis of fair competition).

Goal 3: Enhancing the complementary relationship between trade and aid

It is important to appreciate the potential complementary relationship between trade and aid, also known as *aid for trade*[78]. In fact, the WTO has recently initiated the Aid-for-Trade (A*ft*) initiative, which is recognised for its vital role in Africa's export development. However, as the ECA (2008:134) argues, it is taking too long to become fully operational. All involved parties have a responsibility to speed up its implementation so that valuable time is not lost in increasing African countries' capacity to take advantage of existing opportunities in the multilateral trading system. Importantly, regarding the A*ft* initiative in Africa, a number of traditional capacity-building programme problems must be **avoided**: the lack of ownership of these programmes by recipient countries, the lack of sufficient and predictable funding, and the tendency to focus more on donor priorities than on those of recipients. Moreover, Goldin and Reinert (2006:69) point out that trade policy experts now recognise that, without aid-assistance, developing countries will be unable to exploit the market access that is available to them.

In principle, it is important to add that, as Collier (2007:162) emphasises, "aid needs to be accompanied by African trade liberalisation or it could even increase poverty". Aid without trade liberalisation could be disastrous. Since aid often ruins export competitiveness (because more aid means less need for exports, thus exporters earn less), trade liberalisation is critical for making new export activities competitive. Trade liberalisation also increases the demand for imports by making them cheaper without the need to appreciate the exchange rate, thus reducing the taxes imposed on imports. This

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[78] Note that the *aid for trade* debate is a dramatic paradigm shift from the earlier *trade not aid* debate.

provides an opportunity for aid to be used more for buying imports. In Hoeffler's (2004:1131) view, an economy would benefit more if aid is kept in its original foreign exchange value (dollars, euros, etc.) and is directly used for spending on growth-orientated imports such as infrastructure. While this does not suggest that aid should not be used for building schools and such like, the emphasis should be on spending it on imports. If aid inflows coincide with increased African trade liberalisation, it will help make African exports more competitive and the spending of aid money more effective.

7.3 Regionalism: a catalyst for change and empowerment

There is no doubt that cooperation between African countries is necessary for increased coordination as regards guiding change/reform on the continent, with human progress as the central foci. Greater cooperation resulting in increased regionalism could, invaluably, in turn, **reinforce** African structural change/reform. As the EU has shown, regionalism promises to be of great benefit if tailored to local needs. According to Kaplan (2006:86), the EU (and other, established regional organisations) have redefined international relations, sovereignty, and development, showing how a centralised, multi-country bureaucracy might play a significant role in shaping state behaviour, standards of governance, and even societal evolution. In Africa, each regional grouping should have a mandate to raise governance standards, merge economies, establish one set of rules for doing business, and integrate transportation systems. This new dynamism would not only unleash the caged entrepreneurialism of Africans but also draw MNCs from around the world[79]. Hence, as the ECA (2004:46) underlines, "revitalised regional integration offers the most credible strategy for tackling Africa's development challenges, internal and external. Why? Because of the many weaknesses that overwhelm the limited capacities and resources of individual countries. Collective efforts, with dynamic political commitment to integration, can help overcome the daunting challenges".

In view of growing emphasis on the African Renaissance, an approach to economic regionalism that all sub-regions in Africa could naturally work more towards is that of *new regionalism*. This is an expression of regional identity similar to nationalism, i.e.

[79]The ECA (2004:35) estimated that FDI is worth five times more than foreign aid to the developing world.

extended nationalism (Thompson, 2000:43). However, this approach should entail more than mere *trade blocs*: trade integration should be complemented by the harmonisation of economic policies while investment diversion should be as much a concern as trade diversion. The emphasis should be on both economic **cooperation and competition** to stimulate regional trade and facilitate greater involvement in the globalisation process. Given questions regarding the extent to which a *single global logic*[80] will determine national development, Africa's regions should use the new regionalism approach not only to be shaped by world order but also, reciprocally, to reshape that world order. Regional interactions cannot be structured by a single market, especially not those in Africa. As is the case with recognising the complementary role of civil societies, new regionalism validates political interaction as co-equal with economic exchange relations in building regional cooperation. In this sense, the state's crucial role is recognised in regionalism, i.e. as – unlike the market – a planner, individually and collectively. The state is viewed as a vital actor in shaping regional relations and in responding to global exigencies. In contrast to the asymmetric relations between market and state, as engendered by contemporary globalisation and its underlying theories, new regionalism encourages supportive government involvement in economic planning and functioning. In this regard, the Southern African Development Community (SADC) sets a good example for the rest of Africa. In view of the fact that political cooperation is contingent upon economic coordination, SADC has ensured that **state coordination** remained central, particularly with respect to its ambition to ameliorate economic disparities. Since 1992, it has placed much emphasis on *development integration*, with the goal of cooperation, not simply for trade and economic growth, but to enhance its people's quality of life, and support the socially disadvantaged by means of regional integration. State agency is also reflected in the successful attraction of investment (from 111 corporations) to the state-run Beira Corridor[81] (involving 22 countries) of port, rail, road and oil pipeline development for landlocked neighbours. Apart from state decisions that designate such

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[80] This refers to the current drive, rooted in neo-liberalism, toward a single global market where policies that promote globalisation are encouraged, with excessive emphasis on global competitiveness to keep pace.

[81] NEPAD has identified mega projects to play a key role in facilitating regional integration. E.g. in 2005 Angola signed a 14-year deal with an Italian company to construct a 1,350km rail network, and German company Thormalehn is building a 4,000km railway between Sudan and the Kenyan port of Mombasa.

strategic investments[82], appropriate technology is promoted and selected subsidies (e.g. in seed and food supply) are provided for the most vulnerable who have no margin for *belt-tightening*. It is therefore necessary to advocate economic policies which acknowledge the regional impact of domestic economic decisions. SADC's approach to regionalism is a practical means of working collectively to overcome economic marginalisation by **transforming structural weaknesses** and trying to turn strengths into advantages, while at the same time gradually integrating into the global economy.

The continent is in need of strategies aimed at accelerating the process of regional economic integration and peace consolidation (Ayissi, 2001:16). Intra-African integration requires both economic and political commitment (complementing each other) to be truly successful. One such strategy, according to the ECA (2008:30), is more coordination, at national level, between relevant ministries and institutions (e.g. Ministries of Finance and Economic Development, central banks, and national planning bodies) to enhance the coherence in policy design and formulation, and to ensure that policies have the desired economic impact. Greater coordination, especially in dealing with sectoral issues, will enhance **policy effectiveness** and increase policy's impact on development. It would also ease the task of collectively dealing with systemic issues/risks that affect Africa as a whole, such as the management of commodity price risks as well as vulnerability to external shocks; prevention and management of currency and banking crises; and ensuring that countries facing severe economic crises have better access to credit.

Importantly, policy coordination should coincide with *deep economic integration*. In the view of Gelb *et al.* (2007:45), accelerating deep economic integration in Africa and improving infrastructure would help to widen economic space (e.g. increased market size), raising potential returns for investors relative to entry costs, as well as raising the level of competition. Hence, making Africa more competitive and enhancing its investment attractiveness should go hand in hand with efforts to deepen regionalisation. Moreover, apart from reducing the incidence of domestic policy reversals (thus

[82] There is a need to initiate more cooperation in infrastructure development projects such as telecommunications, transportation, power generation, and water supply to boost trade and attract investors to Africa.

improving the credibility of economic policies in Africa), an important benefit of deep forms of regionalisation is that it enhances the effectiveness of **WTO negotiations** in ways that are not sufficiently appreciated (Zahrnt, 2005:695). First, it extends the *zone of agreement* in WTO negotiations because intra-regional convergence enables the bridging of internal disagreements, owing to highly developed institutions for decision-making, a deliberative culture, trust and collective identity. Secondly, regionalism enhances bargaining power to gain concessions from the WTO (and other international agencies[83]) and offers a way to cope with the complexity of WTO negotiations as fewer participants and policy proposals in WTO negotiations enable more purposeful discussions. Third, it attenuates concerns stemming from uncertainty about efficiency and distributional effects of agreements by enabling the region to better counteract adverse, unexpected outcomes through exemptions, renegotiations, and violations of WTO rules. Therefore, particularly in Africa, deep regional integration (that *glue* nations together), as well as free-trade agreements with the ambition to significantly deepen the level of integration over time, should be intensified and be made a central goal in all regionalisation deliberations. This will facilitate the task of **regional governance** by developing mutual understandings of collective priorities within a certain region, which should, in turn, complement global economic governance by helping to clarify the interests and concerns of greater numbers/groups of countries. African regional development banks could, in terms of regional governance, play a vital *linking role* between Africa's regions and the IGEGs.

Another particular benefit of regionalisation is how it aids in making liberalisation a **gradual** process (as proposed under section 7.2.3). Success in achieving regional integration will create the necessary conditions for progress towards fuller economic integration at the level of markets and enterprises (Cheru, 2002:147). Once production bottlenecks are removed and output has increased, the pressure to find outlets for excess production capacity will grow, leading to eventual liberalisation. Hence, liberalisation is not the immediate aim, but rather a natural *outcome* of efforts to regionalise.

[83] Regionalisation, through increased bargaining power, could certainly enhance Africa's say in the IGEGs.

Table 7.1: Merchandise exports within the African regional bloc (1990-2004)

Regional groupings	Percent of total bloc exports								
	1990	1995	1998	1999	2000	2001	2002	2003	2004
CEMAC	2.3	2.1	2.3	1.7	1.1	1.4	1.5	1.4	1.3
CEPGL	0.5	0.5	0.6	0.8	0.8	0.8	0.9	1.3	1.2
COMESA	6.6	7.7	8.7	7.4	5.7	6.4	6.4	6.6	6.7
CBI	10.3	11.9	13.9	12.1	10.6	9.0	12.3	11.4	13.2
EAC	13.4	17.4	19.0	14.4	16.1	13.7	13.3	14.0	14.6
ECCAS	1.4	1.5	1.8	1.3	1.1	1.3	1.1	1.0	0.9
ECOWAS	7.9	9.0	10.7	10.4	7.9	8.5	10.9	8.6	8.5
IOC	4.1	6.0	4.7	4.8	4.4	5.6	4.3	6.1	4.3
MRU	0.0	0.1	0.1	0.4	0.4	0.3	0.2	0.3	0.3
SADC	4.8	8.7	10.4	11.9	9.3	8.6	9.5	9.8	9.5
UDEAC	2.3	2.1	2.3	1.7	1.0	1.4	1.4	1.4	1.2
UEMOA	13.0	10.3	11.0	13.1	13.1	12.7	12.2	13.8	13.9

Source: World Bank, 2006a:333 *World Development Indicators 2006*

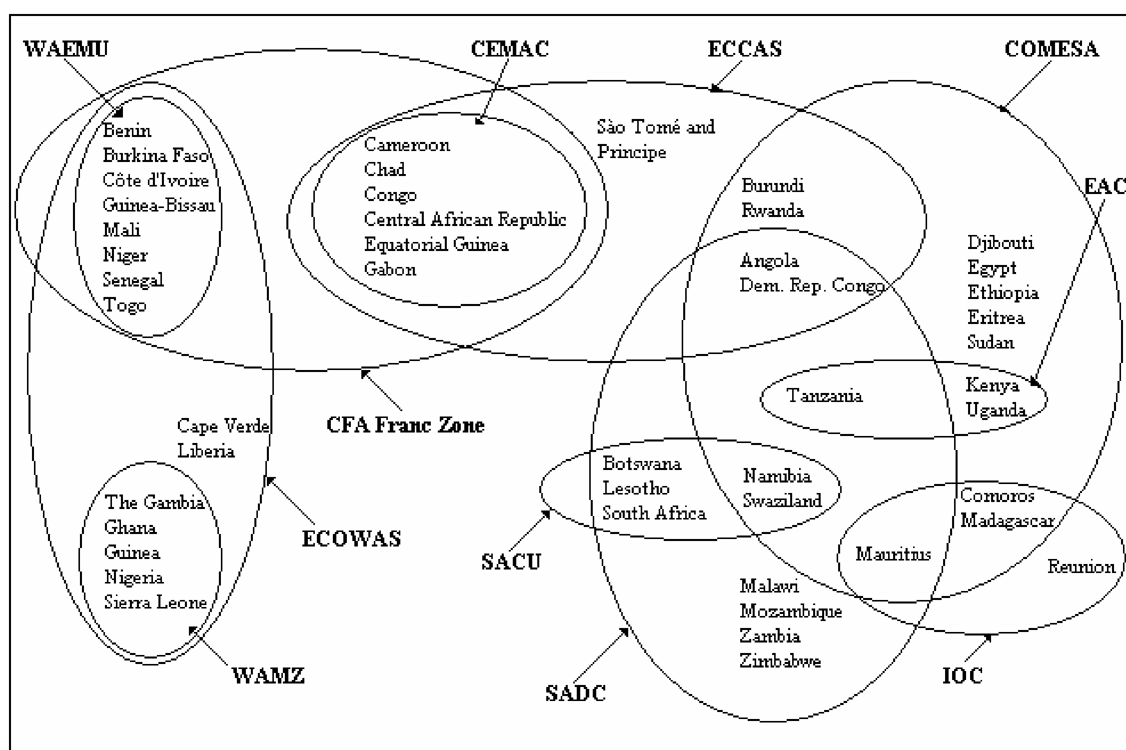
Note: For Table 7.1 and Figure 7.3 see the official List of abbreviations and acronyms.

Table 7.1 indicates how very few of the sub-regions in Africa have shown significant change from 1990 to 2004 in terms of export growth. In fact, in three cases (CEMAC, ECCAS and UDEAC) there has been a decline. Siddiqi (2006:25) further points out that Africa's low intra-regional trade – representing just 10% of Africa's total trade – is a cause for concern and an area that needs to be addressed urgently if trade is to contribute towards building stronger regional ties in Africa. More specifically, different duties, restrictive border practices, poor transport networks and civil strife are impediments that need to be eradicated in order to expand African cross-border trade. The above figure of 10% contrasts with that of 66% in Western Europe, 50% in Asia-Pacific and 40% in North America. The way forward for Africa cannot avoid going through intra-regional[84] trade first. Becoming true global partners first requires going through a regional phase. In this sense, Africa's regionalisation should **complement** its efforts to globalise. Increased intra- and interregional trade in Africa, particularly when stimulating export diversification, can be instrumental in enhancing the continent's global competitiveness.

[84] Africa must eradicate regional disparities where one country dominates the other countries in the region.

An area of hidden potential that needs urgent attention is export processing zones (EPZs). Although EPZs mostly have a poor record in Africa, experience elsewhere suggests that this need not be the case given real political commitment to coordinate all necessary service providers to make them work (Watson, 2001:18). EPZs have the potential advantage of encouraging clustering, the *thickening* of markets, and critical mass to validate transport and infrastructure investments, which is a critical consideration for Africa's sparse economies and essential for enhancing their competitiveness (Gelb *et al.*, 2007:46).

Figure 7.3: The African galaxy – overlapping regional groupings



Source: Yang & Gupta, 2005:9 *Regional Trade Arrangements in Africa*

Moreover, as is clear from Figure 7.3, Africa's regional trading arrangements are often overlapping and complex in nature. The problem is that these African integration initiatives are creating dynamic difficulties with various organisations having overlapping memberships (Appleyard *et al.*, 2008:416). As a result, internal inconsistencies, conflicting regulations and rules, and different strategies and objectives impede the expansion of domestic markets and discourage both domestic and foreign investment.

Considering the intensification of political problems, it appears that these simultaneous integration endeavours may well be a case of too much of a *good thing*. For African regionalisation to become more effective and value-adding, these regional groupings need to be **simplified**. At the risk of oversimplification, though, it would make sense to minimise Africa's current regional organisation into, at most, five groups representing North, East, West, Central and Southern Africa. One example, to avoid further unnecessary duplication between the West African Economic and Monetary Union (UEMOA) and the ECOWAS Secretariat, as Kaplan (2006:91) suggests, is that ECOWAS (with its security apparatus) be merged with the UEMOA economic team and have non-UEMOA countries join UEMOA's customs union and currency, concentrating all resources in one body, i.e. a West African Union. Although it could take time to implement due to a multitude of factors to be considered, similar thought processes could be advanced for Africa's other four main regions as well. The harmonisation of aims, strategies, regulations and trade agreements and policies will be key challenges.

Importantly, a number of **priorities** for regional integration that are particularly relevant to Africa can be identified (Cheru, 2002:150; Jefferis, 2007:100; Quattara, 1999:40):

- *Cooperation before integration.* In the process of intensifying regional integration, the emphasis should first be on building strong cooperation, concentrating on achievable goals with tangible short-term (mutual) benefits: e.g. strong coordination of policies by member states should forgo formal economic integration, helping countries to balance autonomy needs with cooperation needs.
- *Addressing the capacity gap in policy analysis and management.* Neglecting to build strong institutions and managerial skills at the national level for the implementation of complex economic and trade treaties is a serious concern. A regional network approach is necessary whereby existing expertise is shared among member countries and human capacity is built through good mentoring.
- *Integration with national plans.* Sub-regional programmes and projects need to be integrated with national plans and budgets. To enhance national ownership of the regionalisation process, national level reforms should be sensitive to regional dimensions of economic reforms (e.g. regional impact of devaluations).

- *Greater involvement by the private sector, civil society and NGOs.* Efforts towards regional economic integration will be more effective if they build from the realities of African and enlist the support of political constituencies (i.e. the private sector, NGOs, Chambers of Commerce, etc.) whose interests are directly served by the removal of barriers to trade and investment to enhance regionalism.
- *The need for a strong intergovernmental coordinating body.* Improved coordination between governments, regional organisations, and donor agencies – particularly when facilitated by a coordinating and monitoring IGO – will ensure the most efficient use of financial and human resources that can be mobilised from sources both within and outside Africa. This will help to overhaul regulation impediments (e.g. outdated customs procedures) and restrict corruption.
- *Sufficient convergence monitoring.* It is vital to keep track of change in the degree of convergence within regions to ensure that corrective actions are taken early, preventing divergence – especially re macroeconomic indicators and policies.
- *Strong, efficient regional institutions.* Such institutions should be authorised to develop appropriate policies independent of national interests without, however, losing sight of each member's particular situation. They should have sufficient human and material resources to assist members with policy implementation.
- *Regionalism cannot be a substitute for poor national economic management.* Participating countries need to deal effectively with their own economic, political and social problems (e.g. fiscal discipline, corruption and human development).
- *Regionalism should facilitate regional governance.* Regionalisation in Africa should contribute meaningfully to both sub-regional and over-all regional governance by e.g. the AU and the ADB. A complementary relationship between African regional governance and global economic governance is required.

Successful economic integration in Africa will be contingent on the implementation of policies that elicit the correct response from markets and that will **stimulate** regional production and demand. Policy changes/reforms should not only facilitate sound economic and public management, and increase private sector activity, but also encourage specific investments in human resource development. With closer economic

integration, each African country has an interest in ensuring that appropriate policies are followed in its partner countries, thus increasing policy coordination within a regional context. Efficient regional cooperation allows the economies of Africa to overcome the disadvantage of their relative small size and, by providing access to **larger markets**, to realise economies of scale. In addition, strengthening regional organisations could prove to be the only feasible way to tackle the problems that plague fragile states in Africa. It can invigorate development prospects by transforming business climates. It can change societal dynamics by empowering people, unshackling them from the restrictions imposed by ineffectual governments. It can reduce the intensity of inter-group rivalries by creating a supra-national umbrella under which all groups are forced to compete on equal footing, thus strengthening Africa's competitiveness in the global economy. As Kaplan (2006:95) emphasised, "development is a complex process that can succeed only when societal dynamics create a self-propelling momentum for [collective] positive evolution". Decades of searching for a way to jump-start this process in various places in Africa have proved fruitless because previous attempts targeted individual states and bolstered their status and with it the frictions, maladministration, and corruption they nourish. Reconsidering how to harness people and institutions to drive development and what can and cannot be achieved with existing structures suggests that regionalism may offer the only effective way to guide Africa's mostly troubled regions to a true AU.

7.4 Enhancing Africa's global significance through building global partnerships

Although Africa's increased emphasis on regional integration has elicited much praise (and aid) from donors, its number of global partners could be increased, and current relationships strengthened. Opportunely, as Rodrik (2005:136) points out, "integration with the world economy is an outcome, not a prerequisite of a successful growth strategy". This, and given the fact that no country is (no longer) an island, stresses the importance of building global partnerships – especially from a regional perspective (and the associated possibilities of increased bargaining power due to regionalism). Africa's efforts *vis-à-vis* building global partnerships (as part of its global integration strategy) should be based upon equity, balance and mutual benefit. Besides increased regionalism, Africa has to make building global partnerships top priority in order to globalise and to

establish a **complementary relationship** between African regionalisation and globalisation. Concurrently, the developed world has begun to realise the potential benefits of supporting African continental and regional associations, at least in the area of security, where the West has an obvious self-interest. However, to ensure long-term sustainability, the partnerships between Africa and the global community need to go beyond security matters and primarily include creating mutual economic benefits.

The fairly recent Africa Growth and Opportunity Act (AGOA) by the US Government and Everything but Arms (EBA) Initiative of the European Community hold the promise of improving market access by means of tariff and non-tariff barrier reductions and, increasing investment from the US and Europe in African countries (that are resulting in increased exports from Africa) as firms seek to take advantage of the new opportunities created by these initiatives (Anyanwu, 2006:65). It is also expected that these initiatives should help address widespread concern over the size of budgetary outlays devoted to protect agriculture in developed countries. Mlambo and Oshikoya (2001:35) estimated that the **elimination of restrictions** on agricultural trade alone (including subsidies) could lead to an income gain for developing countries of up to US$400 billion by 2015. Both AGOA and EBA are designed to ensure that products from Africa enter the US and EU markets duty free. In practice, however, a number of constraints, of which the most hazardous are the rules of origin,[85] have seriously restricted African exports. While AGOA recently added a special waiver that resulted in African apparel exports increasing by over 50%, EBA has not made any change. In fact, in Collier's (2007:169) view, EBA has been totally ineffective. On the whole, a lack of coherence in European policies represents one of the largest obstacles to successful development cooperation with African partner countries. However, one EU-initiative that seems rather promising is the EU-Africa Partnership on Infrastructure, which aims to enhance development by securing the *regional interconnectivity* of the African continent by providing infrastructure from transport networks to water, energy and telecommunications networks and infrastructure-related services. Notably, this underlines the importance of more effective collaboration between Africa and its global partners. What is needed is one simple scheme/initiative,

[85] E.g. if a Kenyan garment manufacturer uses cheap Asian cloth, imports of these garments are prohibited.

which is exactly the same across the OECD, with more generous rules of origin, pan-African coverage, and a clear time horizon. The details of the scheme need to be sufficiently flexible, making room for adjustment until it works. The intention should be two-fold: to get Africa into new export markets and to create new investment opportunities for interested companies in Africa.

China is a good case in point. Yanshuo (2007:15) points out that an increasing number of Chinese enterprises are seeking opportunities in specifically Africa's infrastructure construction industry. Anyanwu (2006:68) estimated that annual infrastructure investment requirements in Africa are about 5% to 6% of GDP, implying investment needs of over US$250 billion[86] during the next ten years alone. Given the strong interest of China, this could lead to increased competition among prospective investors – a situation from which Africa can benefit strongly if it *manages it wisely* and without affronting any parties involved. Chinese firms are often willing to invest in complementary infrastructure in Africa without foregoing the burden of implementing Western standards and comforts (Mogae, 2007:71). Western firms also have a number of added constraints in terms of having to go through various stages of approval (e.g. in the EU) before being able to invest elsewhere. Moreover, Chinese President, Hu Jintao, already confirmed that China will help African nations build 30 hospitals, 100 rural schools, 30 anti-malaria centers and 10 special agricultural technology demonstration centers over the next three years. Willing to take larger risks than most of their Western competitors, enterprises have become the main part of China's investment in Africa and both sides are starting to gain from this cooperation mode, representing a new type of strategic partnership between Africa and China. In fact, against the backdrop of economic globalisation, Africa's close (and growing) connection with China is becoming a vital stimulus for the **integration** of the continent's economy with the global economy. Given that Africa's economic growth exceeded that of the world average over the past decade and the fact that Africa possesses abundant natural resources, there are ample qualifications for further trade and investment cooperation between China and Africa. If African countries can productively use the income earned from better prices by the

[86] It could be even more, given all the investment opportunities presented by the 2010 Soccer World Cup.

Chinese for their raw materials, then their own competitiveness should increase. Such investment will further generate employment, reduce poverty, raise skills and productivity, and increase revenues. Furthermore, *Sino-African trade* currently contributes over 20% to Africa's economic growth, with China becoming Africa's third largest trade partner (after the US and France) in 2006 as bilateral trade volume surpassed $55 billion (Broadman, 2006:51). Sub-Saharan countries, in particular, have benefited significantly in terms of developing their markets from the rise in Sino-African and Indo-African trade. The same can be said of trade between Africa and Latin America (especially Brazil). Clearly, there are significant gains to be realised from the reductions in tariff barriers to South-South trade. Stiglitz and Charlton (2005:216) estimated that in both agriculture and manufacturing the **gains** to developing countries from liberalisation of trade between themselves are greater than those from liberalisation of trade with the OECD (mainly because of extensive use of non-tariff barriers by developed countries). As a last note on China, although fears have been voiced that Chinese influence will undermine human rights, good governance and democracy, based on anecdotal evidence, the prerogative still lies in African hands to prevent this from taking place. In fact, dealing with such matters (and the lessons learned from it) brings a new (and necessary) maturity level to Africa's collaborations with global partners.

It is particularly vital that Africa's international development partners continue to facilitate the establishment of a *more open and equitable trade regime* in order to help address the problems of quality and lack of knowledge of export markets and appropriate technology from which a number of African countries suffer as a result of diversifying their exports. The phasing out of tariffs on especially processed products and all forms of exports subsidy as well as reducing restrictions on labour-intensive manufactures will provide **substantial support** for Africa's efforts to diversify exports. In addition, Africa's development partners should consider more direct measures such as enhancing existing guarantee schemes for private sector investment in Africa. Given the negative risk perception about the continent, these could be instrumental in providing additional incentives for private investors. On their part, African countries could design innovative

financial instruments – apposite to local conditions – such as the *securitisation scheme*, as these could also serve to provide additional security for potential investors.

Overall, it is essential that Africa's inward strategies regarding reform and regionalisation complement – and be complemented by – its outward strategy concerning the building of partnerships with key global role-players. Crucially, furthermore, in cooperation with global partners, African leaders must ensure that the aim of this **complementary relationship** is to make globalisation work for the poor. With policy being crucial for poverty alleviation, globalisation – although also restricting policy – creates new opportunities and spaces for policy engagement (Goldin & Reinert, 2006:229). This (policy-making) is where African nations and the IGEGs should take hands and join forces to ensure that global economic governance, ultimately, becomes more effective in guiding/managing globalisation so that it assists in putting the poor in a better position to be able to benefit more from its opportunities. In cooperation with the rest of the world, especially the IMF, WB and WTO, Africa should also contribute significantly to the provision of *global public goods*. To help exterminate the perception that Africa always expect others to help and that it always wants more (the *beggar-mentality*), it is critical that African governments meaningfully collaborate with other global role-players on the provision of such goods. In fact, they have a responsibility, first to their own people, to take the initiative and/or be a central driving force in ensuring that substantial benefits are derived from global public goods – and that global public bads are rigorously eradicated.

Lastly, two brief points need to be underlined: (1) While a number of African countries have, on their own, strong linkages with global partners (e.g. the Association agreements signed between the European Community and North African countries and South Africa), a fine balance, once again, needs to be struck between country and continental interests so as to ensure that benefits from these linkages, eventually, enhance the welfare of the whole of Africa. (2) It is also important that, in order for Africa to strengthen and widen its partnerships with the global community, especially the US and EU, it needs to heed their concerns. In this regard, Zimbabwe, in particular, is viewed as a test case for Africa

(Gibb *et al.*, 2002:150). They would be reassured if they saw Zimbabwe's neighbours making a much greater effort to distance themselves from *Mugabe-style* government.

7.5 Conclusion

This chapter explored ways to reverse Africa's marginalisation and examined key areas of reform that must be either undertaken quickly or deepened as a precondition for the continent's potential insertion into the global economy. Strengthening the **capacities** of African countries to manage the cold currents of globalisation in ways that promote democracy and human development remains the most critical contemporary challenge. In the words of former Botswana President, Festus Mogae (2007:72), "in the end no matter how many suitors she may attract, be they handsome or otherwise, it is Africa's own responsibility to achieve her full potential". This requires appropriate action (e.g. internal capacity building and skills retention) and change (e.g. structural reform to make African economies perform better). It is up to *African governments* to ensure that the necessary actions are taken and reforms implemented, because if, for instance, public investment in human capital and technology transfers is insufficient, the market will not fill the gap. Analysis by UNCTAD (2001:50) indicates that without sufficient reform deepening and a major re-orientation of domestic policies, it would be impossible to change the fortunes (i.e. to de-marginalise) of the African region. Duffield (1992:152) warned that "without reform Africa's position in the new world order could well crystallise during [and after] the 1990s into a permanently dependent welfare annex of the West." It should be noted that an overall continent-wide **reform strategy** does not make domestic country-strategies redundant; rather it gives impetus to the need for a domestic reform plan which feeds into this overall strategy, as, for instance, outlined by the NEPAD vision.

By setting specific *goals*, the chapter aimed to promote an African economic reform strategy based on **reform complementaries**, addressing key areas of weakness in Africa as emphasised in chapter five while underscoring the importance of ensuring that the reforms reciprocally benefit from each other. This strategy not only reflect Africa's prime challenges, but also underlines the importance of reform sequencing by giving specific **priority** – as a basis (and minimum requirement) – to the following areas of reform:

- Reforms that facilitate **good governance** (economic and political) and that strengthen (in terms of technical and resource capacity) institutions, governments and key decision-making *fora* (in business, etc.). Moreover, an aspect that has been seriously lacking in Africa and that needs to be remedied is the fact that it is necessary for Africa to experience more of the benefits and value of lawful conduct. This is a key reason why Africa has often fallen back into corruption and lawlessness – it is easier and the benefits of the opposite are not guaranteed.
- Reforms that enhance Africa's **investment attractiveness**, including sufficient standards to provide a secure investment environment and adequate financial sector reform to bring it in line with international standards and best practice.
- Reforms that make **trade diversification** a leading force in Africa's economies, enhancing their competitiveness. Otherwise the benefits of free trade and privatisation will be dissipated in rent seeking, and not be directed towards wealth creation. Trade expansion requires the removal of key obstacles to productivity. Not only need Africa's production become more diversified, its productive capacity in new product areas also needs to be efficient enough to (1) compete globally and (2) create new employment opportunities (particularly for the poor).
- Reforms that encourage the **use of technology** and promote human capital development, including vocational and technical skills development. This may include incentives/subsidies to the private sector to use more complex technology to increase productivity and to train workers on how to use it. Here, for example, supposedly outdated, more affordable technologies (in advanced economy terms) could still be used as highly beneficial in much of Africa's production.
- Reforms that facilitate increased economic **cooperation** and policy **coordination**, which result in African regional integration that is mutually reinforcing.
- Reforms that create more *links* with the **global community**, strengthening Africa's bargaining power in specifically the areas of trade, global decision-making (e.g. in the IGEGs) and setting global economic development priorities.

Importantly, as Easterly (2002:51) underlines, although African countries should seek to introduce structural change by implementing international best practice guidelines,

structural change is always an unfinished task. Structural reform is a dynamic and flexible process and requires constant adaptation to changes in both the internal and external environment. More specifically, Loots (2006a:22) asserts that "sustainable structural change can only be achieved through continuous policy adaptations and improvements in education [i.e. human capital development] to facilitate the process of adjustment to new conditions". Ultimately, successful policy reforms also require **successful implementation** – one of Africa's biggest hurdles to overcome. Together with effective regulation and substantial assistance, *carefully managed* implementation is a crucial constituent to any reform agenda. African governments are tasked with this responsibility and should be held more accountable. In fact, this underlines an important growing need for civil society to play a role. Forging a partnership with civil society to **build consensus** on reforms, and to provide checks and balances in policy-making, implementation, and appropriate change, is essential. African governments should actively encourage the participation of all the segments of civil society in economic policy debates. As evidence increasingly shows, according to Quattara (1990:20), adjustment efforts work best when reforms enjoy the *wide support* of the population, especially the intended beneficiaries. It is vital that the people of Africa need to be involved in setting the *priorities* for the reforms, and be kept fully informed of *progress* in order to develop a sense of participation in the nation- and region-building process which, in turn, promotes the transparency and accountability of public affairs.

It must also be emphasised that, in terms of policy reform and liberalisation, Africa should follow a **gradual, sequenced approach**. Cheru (2002:30) argues for "the guided embrace of globalisation with a commitment to resist", suggesting that while fully exploiting investment and trade opportunities made available by economic globalisation, the necessary measures, such as capital controls and expanded South-South trade, should be taken to shield Africa's economies from the ill effects of market shifts. As Rodrik (2005:137) points out, no country has developed simply by opening itself up to foreign trade and investment. The *trick* has been to combine the opportunities offered by world markets with a domestic investment and institution-building strategy, which serve as a stimulus for domestic entrepreneurs. Nearly all of the outstanding cases – East Asia,

China, India since the 1980s – involve partial and gradual opening up to imports and foreign investment. The onus is on African countries to *initiate* alternative formulations and conditions under which they will engage in global economic exchanges. Importantly, sufficient economic (and political) reform is, in essence, a prerequisite for both the successful integration of African economies and building long-term partnerships with the global community. African governments need to move **beyond rhetoric** in their commitment to *regional integration* in order to gain access to the economies of scale that other players take for granted. The courtship of Africa by various emerging economies (e.g. China and others) is in the end also a challenge to the complacency of traditional partners. In addition, domestic reform alone is not sufficient. The history of international integration bears ample evidence – in Europe, in the Americas and in Asia – of the importance of sub-regional and regional approaches to reform. In light of growing global interdependence, states cannot achieve all their objectives alone – they need regional and global partners. It is thus critical that Africa's regional integration becomes increasingly *instrumental* in the continent's global integration. Clearly, therefore, for Africa to de-marginalise effectively, a more regionally and globally integrated Africa is required.

In the end, **commitment** of African leadership is one of the most critical conditions for ensuring the success of economic and political reforms. Sound economic management and sufficient political will (without conflict) need to complement each other in order for Africa to succeed in becoming more globally competitive and advanced, particularly in terms of human progress and quality of life. Concurring with Goldin and Reinert (2006:132), it is imperative that policy change is driven by a country's *own* initiative, capacity, and political readiness rather than by foreign assistance. By specifically focusing on Africa, this chapter has investigated critical areas where reform deepening is not only most needed due to the severe extent of the continent's marginalisation, but also where it will more effectively make a significant contribution to it becoming more globally competitive – both as a region and as individual countries. The following chapter will conclude the study by emphasising key findings, recommendations and contributions that have emerged from the study as a whole.

Chapter 8

Conclusion

8.1 Introduction

The world economy, its governance processes and its driving forces, are in a process of change. Of course this is nothing new – they have been changing throughout history. However, the contemporary era[87] of globalisation has introduced and fuelled significant new dimensions to how the global economy operates and what it tends to respond to most. Technological advancements, rapidly growing volume of trade and capital flows, and the unprecedented expansion of cross-border markets have created a much more interdependent and networked global economy that has served to deepen/intensify capitalism and, regrettably, also global inequality. Hence, renewed questions are being asked about what kind of **global economic order** is required within which global economic activity can be governed better, as uncertainty and disorder are becoming serious causes for concern, given the increasing inadequacy of current global economic governance arrangements. Africa suffers the most from global inequality, and faces a future marred with increasing exclusion and thus worries about catching up with the rest.

Key **questions** arising, therefore, are what changes (and/or reforms) are needed to create a global economic governance system that benefits the whole global community more equably and, for Africa, what changes are necessary to turn its underdevelopment around and make it more globally competitive. Having identified and attended to these questions, the study – while not claiming to present the full answers – has introduced and re-oriented first steps that can be taken by both global economic governance and Africa towards creating a more just and *mutually beneficial* global economic order. The study had two main aims: (1) to examine the severity and relatedness of the governance void and global inequality, and (2) to investigate reform alternatives regarding the change/adjustment required in both global economic governance and Africa. The first aim – the focus of chapters three, four and five – was achieved by pointing out, very clearly, the deficient dispositions of both global economic governance (in terms of the

[87] According to Albrow (1997:61), the current "global age" involves a *new global consciousness*: an era distinct from the modern age that present a different set of challenges which are more global in scope.

IGEGs' eroding credibility and significant contributory factors that are worsening the governance void) and Africa (in terms of its proportionately diminishing contribution to the global economy). The second aim – the focus of chapters six and seven – was achieved by accentuating specific areas of reform and the kind of change that is required. Ultimately, the function of these aims and their attainment was to help make global economic governance and Africa – both **central concerns** regarding the current progression of the global economy – more credible and value-adding role-players in a rapidly globalising world economy that is in need of better governance, and a competing Africa to restore some balance. This concluding chapter will delineate the rationale, findings, recommendations and contributions of the study.

8.2 Rationale: challenges of a new global reality

To be clear, the two central concerns (also see Figure 8.1) of this study in terms of how the global economy is moving forward in view of the impact of globalisation are (1) the governance void and (2) global inequality, of which Africa's marginalisation forms a significant part. As the source of global governance uncertainty, the **governance void** is the result of a number of factors, in particular: clear deficiencies in the governance of the IGEGs, the asymmetry problem, uncertainty created by the emergence of new, non-state actors of authority in the global economy, geo-political and -economic tensions, security threats, social instability, and excessive financial market volatility. While the global economy is in a *transitory phase*, moving towards a higher/more sophisticated level of operation, it does require a corresponding improvement in global economic governance. As the recent sub-prime crisis in the US and the consequent global financial market meltdown is once again revealing, the success of capitalism in this globalising world economy is directly dependent on sufficient global economic governance arrangements and an adequate global economic regulatory environment that adhere to specific standards and prohibitions regarding capital and trade liberalisation. With governments on their own being decreasingly able to regulate the market, the onus is shifting towards supra-national governance, and more specifically global economic governance, to take up more responsibility *vis-à-vis* this function (which includes doing what is necessary and possible to ensure that global economic development coincides with the eradication of

global inequality). The latter’s current inadequacy, however, necessitates drastic reform and restructuring – something that has been lacking for too long and has, in itself, now become a disconcerting source of global instability. Figure 8.1 summarises and illustrates how critical global concerns that have been emphasised in this study could be categorised; firstly as root concerns, then serious concerns and thirdly, resultant concerns.

Figure 8.1: A categorisation of global concerns emphasised in the study

Root concerns	Serious concerns	Resultant concerns
- Developed world dominance - Reckless liberalisation -Inherent weaknesses of capitalism -The IGEGs’ inertia -A crisis of authority (globally) -Absence of an integrative global economic governance framework	-Global inequality -Unfair trade and trading practices -Footloose capital -Global financial market instability	-An apolar world order -Africa’s marginalisation and its reform debate -The governance void -The global risk scenario -The democratic deficit and the global economic governance reform debate -A crisis of legitimacy -Global contradictions -Policy incoherence

Source: Own contribution

The concern about rising **global inequality**[88] is that it is “intertwined”, with the rise of global informationalism, the network age as well as social exclusion throughout the

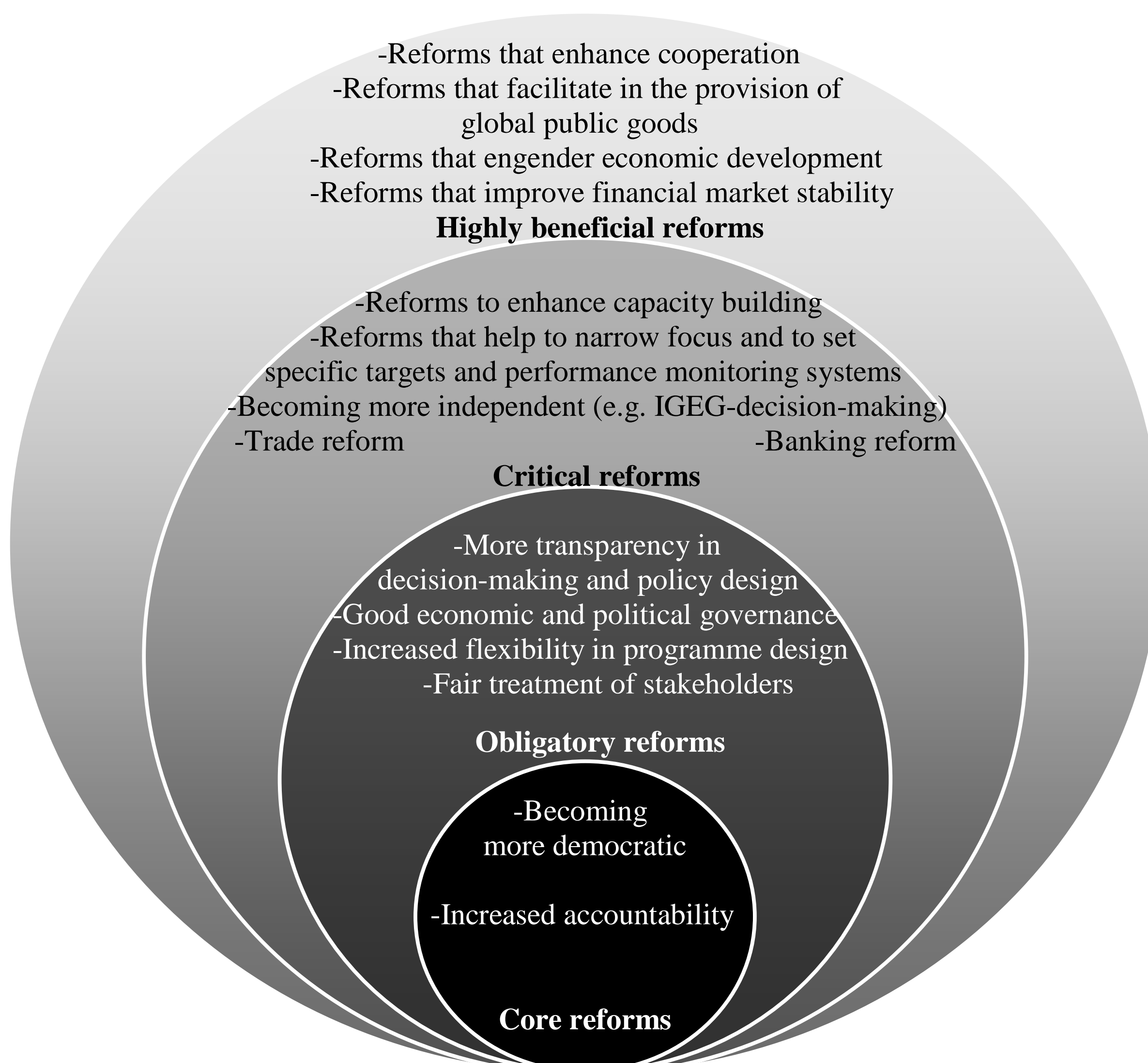
[88] To briefly put it into perspective: at present, the world’s richest 20% of countries claim an 82% share of global exports. The poorest 20% of countries get a mere 1% share (Gibb *et al.*, 2002:55). Similarly, the richest 20% attract two-thirds of the world’s FDI. By contrast, the poorest 20% attract only 1% of FDI.

world (Castells, 2000b:348). It is an *uncomfortable truth* that in this age of instant communication and global integration there are enormous inequalities separating human beings, with billions barely subsisting, billions working in incredibly difficult conditions, and a small elite commanding a mind-boggling degree of wealth. As Derviş (2005:136) rightly points out, "hunger in itself – despite also fostering violence and being implicated as an international security threat – is a weapon of mass destruction: it kills 24 000 people a day and 11 children every minute". As the world's poorest continent (yet potentially the richest in terms of natural resources), **Africa** remains at the *heart* of the challenge of overcoming exclusion and building a process of all-inclusive globalisation. Today, as Gibson (2004:11) underlines, the majority of Africa's population is significantly worse off than it was 25 years ago as a result of SAPs and debt repayment. While domestic issues, particularly supply-side constraints, are also to be blamed, the disadvantageous position of Africa within the regulated world economy has contributed to a severe diminution of potential benefits. All too often Africa has shared the burden but not the benefits of globalisation. The enhanced and enforced liberalisation of the African market has not been accompanied by adequate access to developed country markets. As a result, Africa entered the 21st century being marginalised from the global economy yet highly dependent on it. The fact is, ultimately, the human significance and the long-term broader socio-economic *systemic* importance of what happens in the poorest countries are as critical as what happens in the middle- and high-income economies. As Keohane (2001:1) thus stresses, "interdependence and lack of governance make a deadly mixture", which suggests that inertia in addressing this risk severely worsens the governance void. It is therefore clear that there exists a *dangerous* **positive relationship** between the governance void and global inequality. As global economic governance remains undemocratic and governance uncertainty mounts, global benefits are increasingly more unequally shared (or often not even shared at all); as global inequality is escalating and spiralling out of control, the less able current global economic governance arrangements are in eradicating it, thus heightening uncertainty and the governance void. The concern is that it is an ever worsening situation as globalisation continues to open up new cleavages between the developed and developing world and the need intensifies for it to

be governed by more coordinated multilateral and supra-national action. Yet, frustratingly, neither problem can be solved without fundamental reform.

Moreover, the fact is that we live in a partially globalised world. Currently, many view **globalisation** as a highly uneven zero sum game – countries gain at others' expense (Luiz, 2006:644). The future of globalisation remains uncertain, but the neo-liberalism that drives it tends to neglect the mechanisms for distributive justice and social protection as well as public policies which could hinder the functioning of the free market. In fact, the freer the markets are, the greater is the burden on the regulatory institutions, and i.e. the IGEGs, to provide democratic and legitimate governance. The way in which globalisation is spreading today increases both social polarisation and the risk of political violence. Such a situation affects the developed countries, but, above all, the poorest countries which are struggling to break free from the dominant economic and political structures that reflect the policy orientations of the major commercial and financial powers (De Senarclens & Kazancigil, 2007:275). While this situation is unsustainable, the fault, though, lies not with globalisation but rather with its current practice, which presents the very real danger of poor countries resorting, in desperation, to primitive methods of *de-globalisation* (e.g. higher tariffs and quotas, exchange rate controls and debt repudiation), thus ending up being further marginalised and impoverished. With *global inequality* then reaching extreme proportions, this could well become one of the most serious threats ever to global capitalism. There can therefore be no denying that globalisation has *institutional requirements*. Clearly, reformed IGEGs together with complementary policy reform in both the developing and developed worlds are thus urgently necessary to close the gap between the rich and poor countries. By distinguishing between core reforms, critical reforms and highly beneficial reforms, Figure 8.2 provides context as to how the study interprets the need for reform. This includes areas of reform in the developing and developed worlds as well as in global economic governance. Core reforms are fundamental reforms that must occur to build integrity and give credibility to other reforms. Critical reforms are reforms without which structural policy reform (in the developed and developing countries, and the IGEGs) cannot be regarded as a success. Highly beneficial reforms could be recognised for the considerable value they add.

Figure 8.2: Contextualising the areas of reform considered in the study



Source: Own contribution

It must be pointed out, however, that a major **obstacle** regarding the probability of remedial change in the global economy (particularly with respect to duly addressing *global inequality*) and its *governance* is the role of the **US**. Geopolitically, the US had ceased to be the guardian of the liberal trading order and in fact had become aggressively protectionist, blaming the newly industrialised countries, including Japan, for their enormous trade deficit (Hoogvelt, 2001:226). With the Cold War and Soviet threat belonging to the past, there is much less incentive (and strategic interest) for the US to

maintain the exceptionally favourable trading and currency status of its 'allies', hence lessening the chances of it making adjustments and stepping down from its hegemonic pedestal in world affairs – especially from its dominant influence in the IGEGs. The recent change in US presidency with Barack Obama at the helm, it would seem, inspires and holds the only hope for such (needed) change.

Notably, the *governance void* and *global inequality* have in common the fact that, aggravated by globalisation, both are serious sources of global instability that threaten to allow and cause disruption to particularly global trade and financial markets. Clearly, these two **dangers** cannot be allowed to continue/worsen if globalisation – currently the primary driving force behind change in the global economy – is to remain the *friend* of capitalism instead of its *enemy* and/or destructor – particularly not in light of the potential benefits[89] that globalisation has to offer the global economy (as a whole). The study identifies appropriate (or reformed) global economic governance as the *initiating* and *primary* instrument whereby both dangers could be addressed and, actually, be turned into catalysts for the true triumph of capitalism, thus benefiting everyone. This, of course, will not materialise if there is not sufficient reform and/or adjustment, also, on the part of both the developing and developed worlds, most notably Africa and the US. With the global economic landscape having changed dramatically since the mid- to late-1940s when the IMF, WB and the GATT (later the WTO) were founded, especially in light of a more interdependent global economy and heightened systemic risk and financial contagion, a global economic governance system needs to be prepared to proactively deal with potential future global economic crises – now, rather than when it is too late.

8.3 Findings: global economic governance and African reform – the need for change

Globalisation is rearranging the architecture of world order which means that the task and responsibility at hand for global economic governance is mounting by the day. There is a pervasive tendency in which major shifts in the location of authority and the site of control mechanisms are under way – globally. In many cases these shifts have transferred

[89] One such benefit is, for instance, international trade – one of the key driving forces of globalisation – in that it can have a significant positive effect on economic growth and development (Stiglitz & Charlton, 2005:11). Further, if international trade is fair, the positive effects can become truly global in scope.

authority from the political realm into the economic (e.g. MNCs and the escalating impact of global trade and financial market volatility) and social (e.g. citizens being more thoroughly empowered to engage in collective action[90]) realms. However, two points have become clear: (1) significant structural change in the mandates, functioning and country composition of the IGEGs is vital to reflect the changing balance among the world's economies and to effectively address the growing challenges facing this increasingly integrated and rapidly transforming global economy, and (2) each IGEG is no longer able to deal effectively with its primary mandate without strategic guidance and well-defined relationships with other institutions and role-players that address related issues outside its primary mandate, mission, and capacity. It is therefore critical that an appropriate *integrative system* of democratic global economic governance be put into place to be better able to address not only crises, but also collective everyday concerns arising on the global economic landscape. Accordingly, specific reform requirements and priorities as to improving current global economic governance arrangements and the creation of a more inclusive global economic governance framework are desperately in need of being implemented. Importantly, such a framework must have economic development as central focus. Hence, considering all the IGEGs, the study finds that the critical areas where reform is most needed in **global economic governance** are:

- *Entrenching good governance.* This means, first, for the IGEGs to become fully democratic and representative by adjusting their **voting** structures, being less dependent on their shareholder governments, becoming more inclusive in terms of their approach (i.e. giving more recognition to smaller role-players in global economic governance – e.g. NGOs and LICs), and, particularly in the case of the WTO, ensuring more meaningful participation for developing countries in rule-making in order to establish a more balanced trade agenda. Secondly, becoming more **accountable** to all member governments and the people they represent through a system of *network* evaluation and monitoring that includes both internal and external evaluation within a more integrative framework of global economic

[90] In this instance, the role of the Internet can be identified in the *skill revolution* as being instrumental in enabling citizens to identify their needs and wants more clearly, and its ability to help facilitate the popular trend towards *sub-groupism* – the fragmenting and coalescing of groups into new organisational entities – that has created innumerable sites from which authority can emerge and towards which it can gravitate.

governance. Thirdly, becoming more **transparent** in terms of decision-making and agenda- and priority-setting as well as to encourage public debate on such issues. Importantly, good governance will significantly contribute to the strengthening of ownership by the developing countries in the IGEGs, thus laying the foundation for building a relationship of trust – a vital requirement for cooperation – among all the role-players in global economic governance.

- *Substituting conditionality with selectivity.* This suggests, for instance, giving aid to countries with a proven track record, measured against a specific set of agreed-upon criteria/targets. As a built-in incentive, this will provide countries the freedom to choose their preferred development strategies (more appropriate to their own policy-priorities) and put an end to the micro-management of the past. It will also promote much more **flexibility** in programme design and policy proposals (if needed); depending on how fast the targets are attained.
- *Narrowing their focus, yet becoming more network-orientated.* In taking up their responsibility in terms of providing **global public goods**, each IGEG needs to specialise and build priorities around a specific area of concern. In its focus on economic development, the World Bank needs to make the eradication of poverty and human development top priority. The IMF, in enhancing the stability of the global financial system, should make a concerted effort to reduce countries' vulnerability to the dangers of capital market liberalisation (e.g. regarding the imposition of capital controls and improving banking regulation). Furthermore, in order to take necessary action, the IMF needs to recognise that just as much as the developing world's financial vulnerability is a source of global instability, so are MNC short-term capital flows. In ensuring a more just world trading order, the WTO should help to increase developing countries' market access and promote a fair and equitable rule-based global trade regime (that benefits the US the most[91]), including special treatment for the developing countries. Importantly, the IGEGs also need to become more network-orientated in their **approach**, implying that, as primary mediators in a more integrative framework of global economic

[91] The WTO should thus require of the US to give up the rights of its special position as *primus inter pares*.

governance, they should strongly promote cooperation and *benefit-sharing* (especially concerning global public goods) among all the role-players.

- *Expanding capacity to provide technical and financial assistance.* The IGEGs need to adjust and expand existing structures and **resources** to be better able to provide in the technical and financial needs of developing countries – particularly those (members) that pose a threat to the stability of the global economy. More financial resources will also enhance their capacity to provide stability in global product (e.g. oil) and financial markets (e.g. financial crises).
- *Developing a complementary relationship between global economic governance and regional governance.* In a world of (increasing) competing mega-regions this is a key challenge that needs to be urgently addressed – especially in light of the possibility of a mega-region on the rise in the East (Woods, 2000:394). Building a complementary relationship should involve, for the IGEGs, becoming sufficiently **adjustable** to balance the interests of all the regions and, for the mega-regions, to promote fair interregional competition and cooperation (with the IGEGs).
- *Remodelling global economic governance.* The importance of **building** a more integrative and inclusive system of global economic governance that has at its core institutions (e.g. the IGEGs) that are structurally reformed and that strive, above all, to promote economic development, create a fair global trading system and build a more stable global financial system. The complete system of global economic governance must become more participatory and open to remedial change.

Note that the study is not arguing that international cooperation and institutions (and their reform) are the only workable option for the future of world order. It underlines, though, that for the global economy to continue to successfully integrate and ensure the true success of globalisation, fundamental change on a supra-national level – i.e. global economic governance – is required. There is no doubt that globalisation does create potential gains from cooperation, but globalisation depends on effective and legitimate governance. Governance arrangements to promote global cooperation and help resolve economic and political conflict must be developed if globalisation is not to stall or go into reverse. The time is now right for a paradigm shift in which globalisation is framed not

simply around trade and investment growth – as ends in themselves – but a globalisation that embraces *economic and human development* (especially poverty reduction) as its *raison d'être*. In light of the positive relationship that exists between the governance void and global inequality in that they reciprocally aggravate each other, which is a serious global concern as it is being intensified by continuing globalisation, there is even more emphasis/pressure on global economic governance to adjust and become more effective, democratic and inclusive – appropriate to contemporary governance needs.

A major concern for **Africa** is its limited ability to participate in and affect the process of globalisation – the very process that primarily determines who are included and who are excluded from the global system and that has an extreme effect, either positive or negative, on all economies around the world. Although globalisation has the potential to support the continent's economic recovery, it is essential that the conditions under which Africa participates in this process need to be fundamentally changed. This means, in particular, that Africa should have a much greater say in the design of reform policies, it should stop being marginalised by a world trading system that is heavily in favour of the rich countries, and it should be allowed to have a more meaningful influence in the decision-making processes of **global economic governance** via increased voting power (especially given the large number of people it represents).

Moreover, given that globalisation perpetuates the divide between the rich and the poor countries by *rewarding* the profitable and *punishing* the unproductive/excluded/underdeveloped, the onus rests squarely on African countries (and other developing countries) to themselves – either individually or collectively (AU or sub-regions) – make the required alterations in their economies and policy frameworks to put themselves in a better position to also start enjoying the rewards of globalisation. It must be emphasised, though, that in reality this will never materialise in full if there is no corresponding adjustment on the part of developed countries to do away with restrictions on trade and capital flows originating from the developing countries. In the case of **Africa's** de-marginalisation a number of reforms – as *engines of progress* – should be high on the

agenda of African states and the continent's sub-regions. Hence, the study considers the following to be the most critical **reform (deepening) priorities** for African countries:

- *Improving economic management.* The key aspect *vis-à-vis* good macroeconomic management – apart from creating economic stability – is ensuring that policy reversals are strictly avoided due to their negative impact on investor confidence. The key priority with sound microeconomic management is to reduce business costs[92] in order to create a more favourable investment environment. In addition, one of the most significant microeconomic challenges is to create more linkages between sectors. A strengthening of the linkages between sectors such as agriculture, industry and the service sectors of African economies is necessary to develop a robust domestic private sector, thus specialising in more production-orientated enterprises and not mere petty commerce. Furthermore, to mainly reduce vulnerability to financial crises, financial sector reform is urgently needed in most African countries, including more effective banking regulation and broad-based financial infrastructure reform. In addition, capital markets must be deepened and their sophistication enhanced to attract more foreign investment, in particular. Importantly, a key concern in improved economic management must be the reduction of poverty and making income distribution more equal. It is of no use for Africa to have unprecedented economic growth levels, but no real economic development is taking place on a broad basis – particularly in rural areas. Lastly, the APRM needs to be further refined and sufficiently implemented.
- *Effective capacity-building.* In light of the asymmetry problem, it is essential that African state capacity be enhanced, especially with respect to increasing and mobilising resources at their disposal and improving technical and analytical expertise in the public sector (in cooperation with the IGEGs, for instance). Playing a more complementary role towards the market, African states should make the peoples of Africa owners and successful free-marketeers. In cooperation with developed country states, this is vital for widening the winner's circle of those benefiting from globalisation. It is also essential that African countries' institutional capacity be improved, especially the institutional setting of policy to

[92] For example, registering a business in Canada takes three days, in Africa it takes, on average, four weeks.

ensure not only effective policy reform, but, even more important, its implementation. Overall, building state capacity will also, in particular, help to strengthen democratic governance. Furthermore, given Africa's (abundance, yet) lack of skilled labour, it would work immensely in its favour to emphasise human capacity-building. Education, skills development and enhancing entrepreneurial ingenuity should be, together with building up resources for funding, at the top of African policy-makers' agendas. However, the need for a parallel improvement, i.e. in reducing unemployment, is central to human capital development.

- *Expanding Africa's narrow growth base and enhancing productivity.* For too long African countries have depended on the income generated from only a limited, mostly primary, range of products being produced. In nearly all the high-growth African countries, even, the emphasis is on one or two products as growth drivers. It is critical that African countries explore opportunities to expand production, particularly in manufacturing, and extend the range of products they produce in order to widen their growth bases. This also implies becoming more efficient in production by using more technology and skilled workers to raise productivity levels. Closing Africa's productivity gap with the rest of the world is arguably its most critical determining factor as far as catching up and becoming more globally competitive are concerned.
- *Trade diversification.* Diversifying Africa's trade capacity goes hand in hand with expanding its production. In this case the emphasis is on producing a greater variety of products and services, mainly to answer foreign demand and to raise export earnings. Hence, it is critical that African countries strategise their efforts – based on good foreign consumer-demand research – regarding new product and service areas in which they want to venture new exports. Being able to produce their manufactured needs themselves would also lower import costs.
- *A guided embrace of globalisation.* African states should pursue a strategy of *managed openness*, which involves seeking to influence the sequencing, speed and scope of the engagement of their economies with and adjustment (through reform) to globalisation. African trade liberalisation, in particular, must be gradual in order to support export diversification and, to a limited/managed

degree, protect its economies against the cold winds of global competition. Policy sequencing, in the sense of gradually introducing policy reforms and adjustments, should form the basis of Africa's approach towards *embracing* globalisation.

- *Advancing African integration.* Improving the prospect of Africa's future economic prosperity – especially *vis-à-vis* enhancing its global competitiveness – lies, to a significant extent, in effectively managing African integration into a re-regulated global economy. Africa's sub-regions need to restructure unnecessary overlapping and ensure that they are more complementary towards overall AU-integration. To intensify regional integration, macroeconomic convergence must be a high priority. Key policy indicators on which target bands need to be decided within each African sub-region include the debt/GDP ratio, the external balance as a percentage of GDP, the fiscal deficit as a percentage of GDP, and inflation. This should be underpinned by increased African inter- and intra-sub-regional trade to increase market size, and investment to build investor confidence. Importantly, intensified regional integration would also strengthen Africa's efforts regarding collective bargaining. Encouragingly, there has already been increasing collaboration between African ministers of trade, for instance, with the issuing of joint statements and the assumption of shared negotiating positions at WTO ministerial meetings. This is a step in the right direction for Africa and should be reinforced by collaborative agreements in areas such as investment opportunities (e.g. interregional infrastructure development such as decent transportation systems, especially for landlocked countries) and development initiatives.

One aspect that can be observed from the above is that the reforms are *reciprocally dependent* in that, to be successful, they need each other to create a positive and virtuous cycle out of which Africa can launch its de-marginalisation. Notably, this underlines the importance of widespread African reform, not selective reform. Moreover, globalisation has the potential to support Africa's economic recovery. But for that potential to be achieved, the conditions under which Africa participates need to be fundamentally changed. As Gibb *et al.* (2002:20) assert, for globalisation to be compatible with the recovery of Africa's economy, the regulatory procedures and policies governing world

trade, for instance, need to be re-structured to end the blatantly discriminatory practices which damage not only Africa and her peoples, but other developing economies as well. Importantly, any African reform/recovery strategy must be in line with the basic economic requirements of globalisation. It will **require of Africa** to make a distinct break with the past (i.e. colonialism, the neo-colonial policies of the western capitalist states, and recent corrupt rulers) and work towards a new 21st century approach, thus finding a way to progress within the framework of the existing global economic environment – without expecting change on the outside first. Favouring Africa, it is clear that a productive, competitive, united and vital Africa is a matter of profound global significance.

Importantly, on their part the **developed countries** need to show full cooperation in helping to eradicate undue restrictions *vis-à-vis* African (and other developing countries') trade and investment. They need to be part of the wider process of reform – addressing global economic and political insecurity – by making necessary reforms themselves. A key question for them is to what extent can they afford to have an unstable developing world? The role of particularly the US and the EU is critical in eradicating tariffs, quotas and subsidies. It is time for the US, in particular, to recognise that it must seek a world order based on cooperation and legitimacy if it wants to be more secure. Concurring with Derviş (2005:242), the possibility of Africa as a peaceful and growing region will only happen if the world community is willing to finance a new and major *big push* that substantially increases investment in the continent over a sustained period of time[93]. Africans will have to be able to work with donors in a framework that is legitimate and combines effective conditionality with local leadership and peer review. In addition, the UN, in cooperation with the AU, will have to intervene much more rapidly and decisively whenever local or national governance breaks down and millions of lives are threatened. Apart from aid and giving more consideration to Africa as regards investment and trade opportunities, one form of assistance that can benefit Africa enormously is the availability of affordable technology. Putting technology in the hands of *upskilling* Africans will improve productivity, entrepreneurship, small business development as well as commercial agriculture – among other critical growth areas.

[93] The UNDP (2007:9, 116) estimated that the cost of eradicating poverty is but 1% of global income.

Importantly, it appears that the only way to develop the sharing of mutual interests between developing and developed countries as well as other role-players in global economic governance is by accentuating **reform complementaries**, i.e. promoting a complementary relationship between reforms on the part of specifically Africa (and other developing economies), the advanced economies and the IMF, World Bank and WTO. One example is for African countries to continue with trade liberalisation, knowing that the US and EU are visibly reducing subsidies and the WTO is doing everything within its powers to create a fair global trading system. For this to materialise, two requirements are particularly relevant: **(1)** the sharing and prioritising of a core set of values, principles and goals that delineate how they *transact* with each other (see section 8.4), and **(2)** complete transparency coupled with the development of a credible monitoring system within the framework of global economic governance similar, for instance, to the APRM. These requirements can significantly *level the playing field*.

8.4 Recommendations: towards a new partnership with shared goals and principles

Former US President Bill Clinton said “we are stuck with a global economic system that doesn’t work for half the world. [We need to] propose a plan to embrace the other half, to move to a future of shared benefits and shared responsibilities” (Stiglitz & Charlton, 2005:3). Derviş (2005:119) argues that “embedded liberalism” must be replaced by “embedded globalisation”, suggesting that there will only be progress towards better global governance if it is grounded in democratic values and practice, respectful of cultural diversity, avoidant of the dangers of gigantism and bureaucratism by leaving what can be decided locally to local levels of public policy, and able to gain the allegiance of majorities across the globe. As the global economy is becoming more interdependent, there is a growing need for collective action to both create more global prosperity and address global risks. According to Rosenau (2000:185), there is an “upsurge in the collective capacity to govern”: despite the rapid pace of ever greater complexity and decentralisation, the world is “undergoing a remarkable expansion of collective power”, an expansion that is highly disaggregated and unfolds unevenly but that nevertheless amounts to a development of more universal systems of rule that currently are more in favour of the rich countries. However, this requires **democratic globalisation**, involving

the full participation of the entire global community in decision-making. Making this a reality – based on true multilateralism (as opposed to unilateral action by, for instance, the US) – should be central to global governance arrangements, and in particular global economic governance. Given that governance is about reconciling tensions, beliefs are important in reaching *equilibrium solutions*. In light of this, a new partnership between the developed and developing worlds in which more goals, values and principles of mutual/global concern are shared is necessary to restore credibility and make **global economic governance** more effective in addressing critical economic concerns to progress towards a point of equality where benefits and responsibilities are truly shared.

Without such a **new partnership** the probability of a more inclusive globalisation is low. Encouragingly, small steps have been taken as the international community took on specific commitments at the Monterrey conference in Cancun and the conference on sustainable development in Johannesburg. It is essential that commitments such as those be put into practice and that, for instance, the MDGs be achieved to significantly advance in fostering global economic development. Ultimately, the key to achieving this is to clarify and work towards completing a framework of shared goals and principles. Given the current increasing focus on, and attention to, global systems of rule, it is essential that a measure of coherence be, especially at this early stage, brought to the multitude of jurisdictions, rules and guidance frameworks that are proliferating on the world stage. Without attempting to cover all related areas, a number of key **value-based goals and principles** of common/global interest *aimed to reinforce complementary reforms* and to build consensus as regards priorities for a global agenda for change can be identified. The study recommends that, primarily under the guidance of an integrative framework of global economic governance and with the cooperation of both the developed and developing countries, these should at least include:

- *Ensuring that the opportunities and benefits of globalisation are shared much more widely.* This will require a levelling of the playing field through appropriate capital and trade rules, which implies a careful management/guiding (on primarily a supra-national level) of economic liberalisation. The aims would be to make capital flows safer (i.e. less footloose) and trade flows fairer (i.e. more to the

benefit of developing countries) without significantly inhibiting both liberalisation and the enhancement of a global regulatory environment for capital and trade.

- *Entrenching participatory democracy and good governance.* Democracy requires a respect for human rights, a strong civil society, and power-sharing. This should be complemented by the rule of law and the benefits of the market economy, thus paving the way for deepening interdependence, increasing global integration and strengthening multilateral institutions. This will lead to improved governance (economic and political, local and global), rooted in accountability, fairness and transparency. A *slimmer*, perhaps, yet more effective state is required, able to provide the private sector with a solid framework in which the rule of law could prevail, on a level playing field.
- *Enhancing the global partnership for economic development.* This means collectively eradicating poverty and hunger as well as raising living standards through appropriate human development by means of education and skills development. While the MDGs provide good direction in this regard, poverty reduction and economic development should become the epicenter of global policy frameworks.
- *Making economic development sustainable.* In essence, this means capacitating the poor and equipping them with enabling mechanisms such as good skills and technology to help them leapfrog onto much higher levels of productivity. As a first step, though, policy reform is required to create *environments* within the developing world that stimulate progress as the means to achieve economic development. This is important to ensure, at least in the long-term, a closing of the gap between rich and poor countries. Furthermore, with rising economic growth and international trade exerting increasing pressure on finite global resources and the environment, sustainable economic development also means that the needs of the present should be met without compromising those of the future.
- *Ensuring a complementary relationship between regionalisation and globalisation.* This can only achieved by means of governance coordination; i.e. ensuring that regional and inter-regional governance arrangements, cooperation and dialogues assist global economic governance in addressing global/mutual concerns. It would also enable countries to deal, to a degree, with the asymmetry problem.

- *Provision of global public goods – a demand created by globalisation*. Since the market tends to produce sub-optimal levels of public goods, collective action is needed to satisfy this demand. Global economic governance will not only need to take up this responsibility, but also be at the forefront of identifying deficiencies, and collaborate with key role-players in (and build relationships among) civil society, the corporate world, the state system and regional governance.

While being modified by suggestions such as the above, the standards and principles now being formulated at the international level must be turned into more precise standards in individual developed and developing countries and implemented systematically. Moreover, the suggested new partnership needs, in particular, to support sustainable growth and development in **Africa**. International support should be focused on those African countries that show a strong willingness to break clearly with the past, and that are ready to implement far-reaching economic (and political) reforms as well as performance monitoring systems (e.g. the APRM). Good supra-national governance will be required to harmonise and create a complementary framework for goals and targets already set (and new ones to be set/adjusted) by African regional governance, the IGEGs and the G8, respectively, to achieve this. It is certainly in the interest of the international community to have democracies spread and market economies develop in Africa.

8.5 Contributions of the study

Martin Luther King Jr. said "human progress is neither automatic nor inevitable". This, together with Plato's disquiet about "who guards the guardians?" has been the underlying **motivating factors** behind the concerns addressed in this study. The majority of people of Africa are trapped in a desperate situation from which there appears to be little escape. In the absence of a credible and appropriate governance framework, the IGEGs, the supposed *guardians* of the global economy, have very little accountability – except, it appears, to a small number of rich countries. The prime common denominator between these two *motives* is that both ask for drastic and urgent steps for adjustment/reform, requiring some degree of cooperation and the building of a mutually beneficial global scenario where Africa enjoys the benefits of more participatory global economic

governance and fair treatment (by the developed countries) and the IGEGs become more effective and receive the (necessary) recognition (i.t.o. authority and legitimacy) as well as the benefit of true ownership in them by the entire global community. Importantly, complementary reforms in both spheres will contribute significantly towards creating a more secure global economy – a primary (and growing) global need in this 21st century. Hence, in the context of all this, the study has made a number of contributions.

First, it contributed to a better understanding of the meaning of, and interrelationships between, global economic governance, globalisation and Africa's marginalisation. In this sense, it has also put forward an ideological stance with the emphasis on the transformationalist point of view together with second- and third-generation reforms and a strong accent on better (as opposed to less) global economic governance without the centralisation/concentration of global economic authority, as a frame of reference to be recommended for use by the IGEGs in order to re-evaluate their own ideological stance.

Secondly, by calling attention to a number of serious threats to the stability of the global economy (e.g. the asymmetry problem and factors contributing to a global risk society) as well as significant global developments that are increasingly affecting it (e.g. the network economy and the global civil society), the study gave impetus and direction as to key factors that need to be considered in order to make supra-national governance in the global economy more effective. Ultimately, the intention with this is to improve decision-making in how the world economy is governed/steered/managed, thus attending to the growing vulnerabilities of the global economic system. Apart from global financial instability and trade inequalities, among others, one such vulnerability is Africa's marginalisation, arguably the most illustrative example of global inequality for which the study brought recent evidence to the fore that clearly demonstrates the extent of Africa's underdevelopment, and that the situation is rapidly worsening with growing negative implications for the global economy. Hence, as a result of this, the study has called into action drastic steps (reforms) to be taken to assist in Africa's de-marginalisation, as this appears to be the last window of opportunity for the continent to catch up with most of

the rest of the world. Notably, the study contributed towards identifying how global economic governance is (and has been) significantly worsening Africa's marginalisation.

Thirdly, in view of the above and given the conspicuous deficiencies in global economic governance as well as the severity of Africa's marginalisation, the study proposed that global economic governance be reformed and remodelled into a more integrative system that adheres to contemporary principles of democratic governance and that is more network-orientated with a reformed World Bank, IMF and WTO at its core. As a better design – in the study's view – than current arrangements, it offers greater analytical clarity to what the roles and focus-areas of each of the IGEGs could be. Notably, the intention with this is to contribute towards building a framework of global economic governance that would be better able to address two central concerns identified in this study, namely the governance void and global inequality, in order to contribute towards creating a more secure and equitably prosperous global economy.

Fourthly, the study contributed towards constructing and prioritising an African economic reform strategy as a form of incentive for African countries to either start implementing or deepen these policy reforms[94] to effect structural change that mainly enhances their enabling capacity; thus facilitating economic development and, eventually, their competitiveness in the global economy. In helping to re-focus reforms *vis-à-vis* areas where they are most needed, the study also brought further perspective on addressing one of Africa's most troublesome present-day conundrums: balancing country interests with regional interests – including both sub-regional and overall continental interests.

Lastly, the study has, in essence, made a case for a less polarised world, characterised by true and more democratic globalisation. In view of increasing global inequality, the global economy cannot be allowed to continue along the same path, as the present *status quo* is unsustainable. The contemporary *growth regime*[95] that embraces only a globalised

[94] While they cannot *put on the switch*, they can create the right conditions for growth and development.
[95] This refers to the aftermath of the post-World War II Fordist-Keynesian settlement and the resultant virtuous cycle of capitalist production and consumption, which is now – since the later-1980s – carried forward by the contemporary hegemonic neo-liberal mode of regulation.

social minority and excludes the majority can primarily be altered if economic globalisation is made fairer by means of more effective and democratic global economic governance. The point is that the challenge of *better* (economic) globalisation is largely answered by addressing the challenge of *better* global (economic) governance.

In closing, while to an extent falling outside the scope of the study, a number of key areas where **further research** is required can be identified. These areas underline that concerns within the sphere of the *global economic order* are becoming increasingly interrelated and under scrutiny as the global community's awareness of them is growing and they, in terms of effect, become more globally significant. They include among others:

- The undue risk created by global financial integration as well as new mechanisms of regulation and management (e.g. in light of possibilities created by the technology revolution and increased international coordination among countries).
- The impact that globalisation might have on consumer and investor behaviour and thus what the implications are for a possible worsening of the global risk scenario.
- The direction of change in world order, and more specifically, whether it might entail a concentration of power in the global economy, which is a major concern regarding global inequality and a possible exploitation of the governance void.
- Investigating the creation of a 21st-century multilateral institution that stands central in global economic governance that includes countries representing 80% of the world's people and 80% of the world's GDP to assist in the balancing of the interests of the poor as well as those of the rich countries, and in the process also relieving some of the *workload* (in terms of urgent issues/concerns that require attention) on particularly the IMF and World Bank.
- How to better address the inadequacies of capitalism and make it more pro-poor.

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SUMMARY

The study has investigated the problematic nature of global economic governance as well as Africa's underdevelopment and marginalisation from mainstream global economic activity. It has called attention to a number of conspicuous institutional inadequacies within current global economic governance arrangements, most notably problems with accountability, institutional autonomy, ideological obstinacy, voting inequalities and effectiveness in the IMF, World Bank and WTO. Evidence of Africa's marginalisation has shown that the continent is exceedingly peripheralised within the global economy and that the role of global economic governance in this cannot be disqualified or ignored. These findings, together with a number of critical contributory factors, have laid the foundation for investigating the reforms required to improve global economic governance and eradicate Africa's marginalisation; thus attempting to address the pressing concerns of the *governance void* and *global inequality*. As far as global economic governance is concerned, the study proposed that both specific institutional reform and overarching system-reform be implemented. In the former's case, key areas of reform include: greater transparency; becoming more representative and democratic as well as independent and accountable; increasing ideological and policy flexibility, and enhancing their effectiveness through narrowing their focus. In the latter's case, a remodelling of the system of global economic governance is required to make it more integrative and participatory. The underlying aim in both cases is to make it more Africa-inclusive – thereby suggesting that global economic governance should be redesigned to be more in favour of the developing countries than is currently the case.

As far as Africa is concerned, structural reform – to varying degrees – across the continent is required in particularly the following areas: macro- and microeconomic management; public sector management; banking and financial infrastructure development, and trade policy effectiveness. The reforms are aimed towards building capacity, enhancing Africa's competitiveness in the global economy, and to promote intra-African cooperation and partnerships with key global role-players. The importance

of improving global economic governance and diminishing Africa's marginalisation is particularly underlined by the fact that contemporary globalisation is accentuating the inherent weaknesses of capitalism as it is making the global economy more interdependent and, alarmingly, more vulnerable and crisis-prone. Sufficiently addressing, therefore, the governance void and global inequality is a challenge that is central to ensuring a global economy that respond positively to guided liberalisation, that is less risk-inclined, and that provide more equal opportunities for progress.

Keywords:

Global economic governance, globalisation, Africa's marginalisation, policy reform, democratic deficit, governance void, global inequality, economic development, capacity building, export diversification and participatory governance.

OPSOMMING

Die studie het die problematieke aard van globale ekonomiese bestuur sowel as Afrika se onderontwikkeling en marginalisering van hoofstroom globale ekonomiese aktiwiteite ondersoek. Dit het die aandag gefokus op ‘n verskeidenheid opmerkbare institusionele tekortkominge binne die raamwerk van huidige globale ekonomiese bestuursreëlings, veral probleme met verantwoordbaarheid, institusionele outonomiteit, ideologiese obstinaatheid, kiesingsongelykhede en effektiwiteit in die IMF, Wêreld Bank en WHO. Bewyse van Afrika se marginalisering het aangedui dat die kontinent buitengewoon geperiferiliseer is binne die globale ekonomie en dat die rol van global ekonomiese bestuur hierin nie gediskwalifiseer of geïgnoreer kan word nie. Hierdie bevindinge, tesame met ‘n aantal kritieke bydraende faktore, het die fondasie gelê vir die ondersoek van hervormings wat nodig is om globale ekonomiese bestuur te verbeter en Afrika se marginalisering te ontwortel; en dus te poog om die dringende bekommernisse van die *bestuursgaping* en *globale ongelykheid* aan te spreek. Ten opsigte van global ekonomiese bestuur het die studie voorgestel dat beide spesifieke institusionele hervorming en oorkoepelende sisteem-hervorming geïmplimenteer moet word. In die geval van eersgenoemde sluit sleutel-areas van hervorming in: groter deursigtigheid; om meer verteenwoordigend en demokraties te raak sowel as onafhanklik en verantwoordbaar; groter ideologiese- en beleidsbuigsaamheid, en ’n verbetering in hul effektiwiteit deur hul fokus te vernou. In die geval van laasgenoemde is ‘n hermodellering van die stelsel van globale ekonomiese bestuur nodig om dit meer insluitend en deelnemend te maak. Die onderliggende doelwit in beide gevalle is om dit meer Afrika-inklusief te maak – wat voorstel dat globale ekonomiese bestuur geherontwerp moet word dat dit die ontwikkelende lande meer bevoordeel as wat tans die geval is.

Sover dit Afrika aanbetref is strukturele hervorming – in verskillende mates – regoor die kontinent nodig in veral die volgende areas: makro- en mikro-ekonomiese bestuur; openbare sektor bestuur; bankwese en finansiële infrastruktuur ontwikkeling, en handelsbeleid effektiwiteit. Die hervorminge het ten doel om kapasiteit te bou, Afrika se mededingendheid in die globale ekonomie te verbeter, en om intra-Afrika samewerking

en vennootskappe met sleutel global rolspelers te bevorder. Die belangrikheid van om globale ekonomiese bestuur te verbeter en om Afrika se marginalisering te verminder word veral geonderstreep deur die feit dat kontemporêre globalisering die inherente swakhede van kapitalisme aksensueer soos wat dit die globale ekonomie meer interafhanklik en, kommerwekkend, meer kwesbaar en krisisgeneigd maak. Die behoorlike aanspreek van die bestuursgaping en globale ongelykheid is gevolglik 'n uitdaging wat sentraal is tot die versekering van 'n globale ekonomie wat positief reageer tot geleide liberalisering, wat minder risiko-vatbaar is, en wat meer gelyke geleenthede vir vooruitgang bied.