Policy Brief No. 5

Governing Globalization: Issues and Institutions

Deepak Nayyar
and Julius Court

The United Nations University

WIDER

World Institute for Development Economics Research

UNU World Institute for
Development Economics Research
(UNU/WIDER)

Governing Globalization: Issues and Institutions

Deepak Nayyar and Julius Court

This publication is a policy-focused summary of the UNU/WIDER manuscript on *Governing Globalization: Issues and Institutions*, edited by Deepak Nayyar.

The manuscript has been prepared within the UNU/WIDER project on Governing Globalization: New Roles and Functions for the United Nations and Bretton Woods Institutions, directed by Deepak Nayyar, University of New Delhi.

UNU/WIDER gratefully acknowledges the financial contributions to the project by the Ministry for Foreign Affairs of Finland and the United Nations, Department of Economic and Social Affairs, Division for Social Policy and Development.

UNU World Institute for Development Economics Research (UNU/WIDER) was established by the United Nations University as its first research and training centre and started work in Helsinki, Finland in 1985. The purpose of the Institute is to undertake applied research and policy analysis on structural changes affecting the developing and transitional economies, to provide a forum for the advocacy of policies leading to robust, equitable and environmentally sustainable growth, and to promote capacity strengthening and training in the field of economic and social policy making. Its work is carried out by staff researchers and visiting scholars in Helsinki and through networks of collaborating scholars and institutions around the world.

UNU World Institute for Development Economics Research (UNU/WIDER)
Katajanokanlaituri 6 B
00160 Helsinki, Finland

Cover photograph: The United Nations
Camera-ready typescript prepared by Liisa Roponen at UNU/WIDER
Printed at Hakapaino Oy, Helsinki

ISSN 1455-9609
ISBN 92-9190-226-8 (printed version)
ISBN 92-9190-227-8 (internet version)

CONTENTS

FOREWORD		v
EXECUTIVE SUMMARY		vi
1	INTRODUCTION	1
	1.1 A changed world	1
2	GLOBALIZATION AND GOVERNANCE	4
	2.1 Towards global governance	4
	2.2 The logic of international organizations	5
	2.3 The importance of new world view	6
	2.4 Insights from public economics	7
	2.5 Principles of democratic governance	8
3	REFORMING THE EXISTING INSTITUTIONS	10
	3.1 United Nations	10
	3.2 The International Monetary Fund	13
	3.3 The World Bank	15
	3.4 The World Trade Organization	17
4	EMERGING ISSUES AND MISSING INSTITUTIONS	20
	4.1 Global macroeconomic management	21
	4.2 International financial architecture	21
	4.3 Transnational corporations	23
	4.4 Cross-border movements of people	24
5	CONCLUSION	26
6	LIST OF CHAPTERS	28

FOREWORD

The forces of globalization are causing rapid changes in trade and financial flows, and the movement of people across the world has become a major issue in need of urgent action. National economies have become closely interrelated, particularly through the adoption of the new information technologies. Although the institutions that attempt to regulate these processes have shown some evolution since their foundation fifty years ago, the United Nations system and the Bretton Woods institutions face both daunting and complex challenges.

This policy brief summarizes the results of a major UNU/WIDER project on these issues directed by Deepak Nayyar, which is now published as *Governing Globalization*: *Issues and Institutions*. This research has sought to identify the main ways in which the governance needs of the world economy and polity can be strengthened, in particular to better protect the interests of the poorer developing countries.

There has been an urgent need for a clear perspective on this important topic and this policy brief is sure to be of value to all those who are concerned with creating new and better structures of governance for the world economy.

Tony Shorrocks
Director, UNU/WIDER
June 2002

EXECUTIVE SUMMARY

A changed world

It is now more than fifty years since the United Nations system and the Bretton Woods institutions were created. However, the world has changed dramatically during the second half of the twentieth century. The technological revolution in transport and communications has eroded the barriers of distance and time. National economies have become ever more closely integrated through cross-border flows of trade, investment and finance. In the political realm, communism has collapsed and capitalism has emerged triumphant. The context has obviously changed. But thinking about development is also very different. And there is now a myriad of new actors—from transnational firms to NGOs—participating in the global economy and polity.

The concern is that the current system seems incapable of dealing with either the 'old' problems that persist or the 'new' problems that have surfaced. As we enter the twenty-first century, almost one-third of the people in the developing world, an estimated 1.2 billion, live in absolute poverty and cannot meet their basic human needs. The same number do not have access to clean water. And new problems have surfaced: the transition in the former Soviet Union and Eastern Europe remains grossly incomplete and has been accompanied by a large increase in mortality, poverty and inequality. The number of humanitarian crises, with their legacy of death, displacement and destruction, have risen dramatically over the past two decades. And some of the new problems are a direct consequence of globalization.

The UNU/WIDER study aimed to sketch the contours of institutions and governance that would meet the needs and challenges of the twenty-first century. Drawing on contributions from among the most distinguished economists, including Nobel Laureate Joseph Stiglitz, the study provides a comprehensive examination of the governance needs of the world economy and polity.

This policy brief is intended to outline suggestions and stimulate discussion at a time when the world community is thinking about, and is engaged in, a debate on global governance. The policy brief not only focuses on the reform of existing institutions, but also proposes new institutions that are needed. It articulates a powerful new worldview and vision that are critical for any efforts to develop legitimate and effective global governance rules for the first part of the twenty-first century.

Towards global governance

It is important to situate recommendations on global governance, through institutions and rules, in the wider context of globalization. Globalization is associated with increasing economic openness, growing economic interdependence and deepening economic integration between countries in the world economy. The process has brought about profound changes in the international context which have far reaching implications for development.

Why is governance of the world economy increasingly necessary? In short, because there is an increasing gap between the global challenges and the capacity of international institutions to deal with them. While economic activity has become international and global, the jurisdiction of national rules or laws has not. Externalities—non-market consequences of production and consumption processes—increasingly spill across national boundaries, yet there are no rules to deal with the consequences. A very large proportion of countries and people have remained untouched or have been marginalized by globalization. In a national context, the state could introduce corrective measures. However, the global economy remains almost ungoverned.

A new world view

In 1945, when the United Nations and Bretton Woods institutions were created, a vision about world peace and full employment was at the heart of the worldview. At the start of the twenty-first century, it is time to seek consensus on a new worldview. It must surely have the fundamental objective of ensuring decent living conditions for the ordinary citizens of the world. Poverty eradication is an imperative.

The new paradigm for world governance could derive some inspiration from the expected role of governments within countries. This would mean providing *global public goods*, such as world peace and a sustainable environment, as well as regulating *global public bads*, such as international crime whether trade in drugs, arms, people or organs. Rules and institutions of global governance could also draw some inspiration from the conception of political democracy so as to create a more democratic structure of world governance.

Governing globalization is a concrete starting point. The objective should be to make the market-driven process of globalization conducive to a more egalitarian and broad-based development.

Reforming existing institutions

It is clear that the world has changed considerably, particularly in the last decade, and that the present institutions for global governance—the UN, World Bank, IMF, and WTO—today operate on outdated political and economic foundations. They will need to be reformed before a crisis, perhaps induced by globalization, forces the changes required. Some important conclusions that emerge from the study are outlined below.

The United Nations

The legitimacy, effectiveness and credibility of the United Nations continue to erode. The UN suffers from a 'democratic deficit' that was an integral part of the original design but needs to be remedied now. The UN's moral authority is seriously undermined because its laws or principles are enforced selectively to suit the interests of the rich and the powerful.

The study also highlights a number of desirable institutional changes: (i) enlarging Security Council membership and circumventing the veto of the five permanent members in order to ensure the UN's credibility; (ii) full or partial independent financing of the UN, possibly through a version of the Tobin tax on international foreign exchange transactions or stock market transactions; (iii) establishment of a 'global people's assembly', modelled on the European Parliament, to run parallel to the General Assembly and serve as the voice of global civil society; (iv) creation of an 'economic security council' in the United Nations, to provide an institutional mechanism of governing globalization; (v) establishment of a high quality volunteer peace force to provide a prompt collective security response wherever humanitarian emergencies arise.

The International Monetary Fund

The major changes in economic realities over the last 50 years, combined with the repeated crises in the international financial system, make it clear that the role and governance of the IMF needs to be reviewed.

- First, the study argues that the time has come to redefine the role of the IMF towards a constructive role in managing and stabilizing the international financial system, not only through crisis management but also through crisis prevention. It would seem that the logic of international collective action—an integral part of its original design—has been forgotten.

- Second, governance in the IMF needs much more representation, transparency and accountability. It will need to become more representative of developing country concerns and restructure voting rights. There is a need for much greater transparency in the IMF, with disclosure of information and truly independent evaluation of operations.

- Third, IMF thinking and policies need to be reviewed. The practice of conditionality should be fundamentally reformed. It has become an infringement on national sovereignty and, at the same time, is an ineffective tool for changing economic policies. The IMF also needs to reconsider its perspective on capital account liberalization and capital account convertibility.

The World Bank

With 1.2 billion people still living in poverty, clearly the Bank's primary task should be to respond to the crisis of development. Its subsidiary task should be to provide scarce capital to countries and to sectors which do not have access to international capital markets.

- First, the Bank should redefine its role. It should give up its attempts to micro-manage economies through conditionality. Instead, it should seek to become a genuine partner in development through local participation in a relationship of equals.

- Second, as with the IMF, greater representation and accountability are imperative. The need to restructure such a voting system is obvious. The study also calls for 'independent evaluation' of World Bank supported projects and programmes as a way to begin improving accountability to governments and people.

- Third, the Bank will need to re-orient its thinking about development which currently attaches far too much importance to markets and to openness. Simplified prescriptions, which emphasize more openness and less intervention, combined with a minimalist state that simply vacates space for the market, are not validated by either theory or history.

The World Trade Organization (WTO)

There has been a spectacular growth in international trade over the last 50 years. An increasing proportion of world output enters into world trade. Trade is more and more an arena for conflicts and claims from other spheres. The emerging multilateral trading system neglects developing countries and ignores the poorest among them. Reform is imperative. And, as an institution, the WTO is still young enough to permit debate and introduce change.

The study suggests some potential areas of reform: (i) prioritize development as a fundamental objective of the WTO; (ii) develop an efficient system of representative decision-making for the WTO—perhaps based on an executive board or group negotiations; (iii) do not overload the agenda (there is no reason why labour or environmental standards should be included); (iv) abandon the concept of the 'single undertaking'; (v) declare a 'standstill' on the ongoing process of deeper integration and reconsider, if not implement, a 'roll-back'; and, (v) strengthen 'trade-legal aid' arrangements for the poorest WTO members.

Emerging issues and missing institutions

The evolution or development of institutions for governance has simply not kept pace with the challenges of the twenty-first century. It is important to go beyond an analysis of existing institutions to identify institutional gaps and/or missing institutions. The policy brief highlights four areas where new institutions may have to be created.

Global macroeconomic management

The age of globalization has created a new world with an explosive growth in international finance. There is now a much greater instability in exchange rates (and interest rates) and the volatility is associated with a contagion across markets and borders. Yet, there is virtually no institutional framework for global macroeconomic management. There has to be some institutional mechanism for the consultation, surveillance and coordination of macroeconomic policies and it must extend beyond the G-7.

International financial architecture

The explosive growth in international banking and the staggering size of international foreign exchange markets as well as the frequency and intensity of the financial crises have led to a near-consensus on the need to reform the international financial architecture. A new institutional architecture should be designed to deal with crisis management and crisis prevention. The instability and volatility of exchange rates and capital flows are obvious problems. But it should also support the integration of developing countries into the world economy in a manner that promotes rather than hinders development.

Among the recommended reforms are: (i) institutional mechanisms that foster consultation, consistency and surveillance of national macroeconomic policies; (ii) a greater supply of emergency financing to assist in times of crisis (and available before rather than after international reserves are depleted); (iii) international agreement on standstill provisions, or orderly debt workout procedures, to play the same role as private sector bankruptcy procedures; (iv) giving countries the freedom to choose an exchange rate regime; (v) improving the institutional framework in which financial markets operate, including minimum standards in prudential regulations, supervision and accounting. It may, ultimately, be worth thinking about a World Financial Authority that would manage systemic risk associated with international financial liberalization, coordinate national action against market failure or abuse, and act as a regulator in international financial markets.

Transnational corporations

Transnational corporations have come to dominate cross-border trade, investment and technology. Their activities are often no longer governed by national rules or national policies. Therefore, the study also calls for an international system of governance for transnational corporations. There is a need for a discipline on restrictive business practices and an international regime of anti-trust laws. There is a critical issue about taxation of large international firms which is mostly untouched. The creation of an institution for this purpose, say a ‘world tax authority’, is not even on the distant horizon. A system of governance for transnational corporations would not have to begin from scratch. This could build on efforts by the UN Conference on Trade and Development, the experience of the European Union and initiatives by the OECD and the International Finance Corporation. It could also build on the attempts by the UN regarding the social responsibility of corporate entities in the sphere of labour standards, human rights and environmental concerns.

Cross-border movements of people

The almost complete absence of international institutions, or rules, in this sphere is a cause for concern. Globalization is creating demand for greater labour mobility across borders and for institutions to help manage this. Increasing disparity in economic opportunity is being accentuated by demographic factors (ageing in industrialized countries and population growth in developing countries). The result is a conflict between the laws of nations that restrict the movement of people across borders and the economics of globalization that induces the movement of people across borders. Trafficking people is the fast growing market for organized crime. As we enter the twenty-first century, the time has come to initiate a preparatory process which would work towards a new institutional framework that would govern cross-border movements of people. It is necessary to highlight two dimensions here.

First, there is a need to ensure rights and to eliminate abuse of actual migrants in their new countries of residence. The study calls for ratification of ILO conventions on labour standards to protect the rights of legal migrant workers (similar to the concept of *national treatment* in the WTO), with some provision for national obligations to create enforcement mechanisms. It also calls for protection for illegal migrants from exploitation and abuse and concerted action to curb the trafficking in people.

Second, we have to think of the potential migrants before they have moved. The aim should be that cross-border movement of people is governed at least in part by transparent and uniform multilateral rules rather than by diverse national laws and non-transparent consular practices alone. The equivalent of the *most-favoured-nation* principle, which makes for unconditional non-discrimination for people, could provide a basic foundation. And it is worth contemplating a multilateral framework for immigration laws and consular practices that governs the cross-border movement of people, similar to multilateral frameworks that exist, or are sought to be created, for the governance of national laws about the movement of goods, services, technology, investment, and information across national boundaries.

Conclusion

Global governance, then, is not so much about world government as it is about institutions and practices combined with rules that facilitate cooperation among key actors. This policy brief is intended to provide information and analysis, combined with recommendations for reform for a number of constituencies to which global governance matters. The policy brief argues that 'governing globalization' is necessary due to dramatic changes during the second half of the twentieth century. The policy brief is clearly not the end of the debate on the subject. It represents a modest beginning. The object is stimulate discussion and to highlight areas where further thinking is essential.

Historical experience suggests that crises are the catalysts of change. Last time, it was the aftermath of a world war and a worldwide economic depression that led to the foundation of the United Nation systems and the creation of the Bretton Woods institutions (the World Bank and IMF). The world need not wait for another crisis of such proportions to contemplate and introduce the much needed changes in global governance.

1 INTRODUCTION

1.1 A changed world

The United Nations and the Bretton Woods institutions were at the core of the institutional system for global governance that was created in 1945. Their roles and modes of operation reflected the context of the time and the worldview of their architects. The UN was set up in the quest for peace, human rights and development, motivated largely by the legacy of the Second World War. It was the devastation of the disastrous breakdown of the international monetary and trading system in the 1930s that led world leaders to create the Bretton Woods institutions. This juncture was also the beginning of the end of colonialism. It shaped the aspirations of the newly independent countries about economic development and national sovereignty. These countries wanted to improve the living conditions of their people through rapid industrialization and to participate in a more democratic world where the structure of governance treated nations as equal partners. In the pursuit of development, the role of the nation-state was perceived as critical everywhere.

During the second half of the twentieth century, however, the world has changed almost beyond recognition, not only in the sphere of economics but also in the realm of politics. The technological revolutions in transport and communications have eroded the significance of time and distance, facilitating a process of globalization. National economies have become ever more closely integrated through cross-border flows of trade, investment and finance. There has also been a profound change in the political situation, as communism has collapsed and capitalism has emerged triumphant. In both economic and political domains, the past decade has been particularly eventful. Even as some old problems persist, new problems have surfaced—many of them global in nature.

While the context has obviously changed, the perspectives on management of economies and development are now also very different. In 1945, the concerns of the industrialized countries were strongly influenced by memories of the great depression, which created the desire for full employment and a welfare state. The Keynesian consensus has vanished in the industrialized countries. The rise of monetarism has meant that macroeconomic policies have sought to maintain price stability at the expense of full employment, while the welfare state is being slowly eroded. The retreat of the state from the economy is matched only by the advance of the market.

The change is just as dramatic elsewhere in the world. In the post-colonial era, most underdeveloped countries adopted strategies to limit the degree of openness and of integration with the world economy, in pursuit of a more autonomous, if not self-reliant, development. The state was assigned a strategic role in development because the market, by itself, was not perceived as sufficient to meet the aspirations of latecomers to industrialization. Four decades later, by the early 1990s, most developing countries had begun to reshape their domestic economic policies so as to integrate much more into the world economy and to enlarge the role of the market *vis-à-vis* the state. Despite many voices of dissent, this approach, known as the *Washington consensus*, was widely accepted in thinking about development. The consensus lost some of its lustre as development experience during the 1990s did not live up to expectations and because of the repeated financial crises.

In 1945, the nation-state was the foundation of both the conception and the design of global governance. It was also the main actor. More than fifty years later, there are different players in the global economy and polity. For one, globalization has constrained the role of the nation-state. The autonomy of the nation-state is much reduced in matters economic if not political. For another, there are significant players apart from nation-states. Governments now share the stage with corporate entities (transnational corporations and international banks) and civil society. This myriad of new actors increasingly impacts upon global governance, thus providing another reason why the system of institutions and rules for global governance created then in 1945 is less compatible with the changed reality now.

Global challenges: old and new

As we enter the twenty-first century, some old problems persist and may have intensified. Almost one-third of the people in the developing world, an estimated 1.2 billion, live in absolute poverty and cannot meet their basic human needs. The same number do not have access to clean water. As many as 840 million people suffer from malnutrition. And, more than 850 million adults remain illiterate. Most of the people living in such deprivation live in the developing world. But, one-eighth of the people in the industrialized world are affected by, or live in, poverty. (The evidence cited here is drawn from UNDP [1999] *Human Development Report 1999: Globalization with a Human Face*, New York: Oxford University Press.)

And new problems have surfaced for which there are no systemic solutions. The transition in the former Soviet Union and Eastern Europe remains grossly incomplete and has been accompanied by a large increase in mortality, poverty and inequality. Many of these new states remain economically fragile and politically unstable. Elsewhere, nation-states have fractured as they have slipped into ethnic strife or civil war. The number of humanitarian crises, with their legacy of death, displacement and destruction, have risen dramatically over the post-war era and the response of the international community has been *ad hoc*, inadequate or simply not forthcoming. There is still no system in place to take care of, let alone prevent, complex humanitarian emergencies.

Some new problems are a direct consequence of globalization. The rapid integration of international financial markets, combined with the explosive growth in portfolio investment flows and short-term capital movements, has led to a volatility in capital flows and an instability in exchange rates. The management of these is complicated and failure can result in massive economic crises which (as events in Indonesia show) can easily acquire political dimensions. A large proportion of both countries and people have remained untouched or have been marginalized by the process of globalization. Exclusion has had social consequences as some of those deprived have turned to crime, drugs or violence. Environmental destruction continues. The accent on deregulation has possibly accelerated the overexploitation and degradation of common property resources. It need hardly be stressed that this list of problems—old and new—is illustrative rather than exhaustive.

The key questions

The world economy and polity are fundamentally different since the United Nations system and the Bretton Woods institutions were created more than 50 years ago. Thus, the governance needs of the world—in terms of institutions and rules—must also have changed. The institutional framework has, of course, evolved over time. However, the underlying construct, which was based on the worldview of its architects, has remained the same. It should come as no surprise, therefore, that there are no systemic solutions for the old problems that persist and the new problems that confront the world.

This UNU/WIDER study sought to sketch the contours of institutions and governance that would meet the needs and challenges of the twenty-first century. It particularly focused on a number of questions: Is the institutional framework created *circa* 1945 adequate, or even appropriate, for the economy and the polity of the contemporary world? Do we need to redefine the role of, or adapt the existing institutions to meet the needs of our times? If there are gaps, do new institutions need to be created?

Reflecting the main questions in the study, this policy brief is divided into three sections. The *first* section situates the discussion in the wider context of globalization, which now affects the living conditions of people. The *second* section suggests how key existing institutions—the UN, IMF, World Bank and WTO—need to be modified or restructured to meet the present and future needs of global governance. The *third* part points to emerging governance needs and suggests areas where new institutions may have to be created.

The brief is intended to put forward suggestions and stimulate discussion at a time when the world community is thinking about, and is engaged in, a debate on global governance. It is based on a comprehensive examination of the governance needs of the world economy and polity. Drawing upon contributions from among the most distinguished economists in the profession, including Nobel Laureate Joseph Stiglitz, the study not only focuses on the reform of existing institutions, but also analyses issues of emerging significance to suggest that new institutions are needed. It emphasizes that a powerful new worldview and a long-term vision are critical for any efforts to develop legitimate and effective global governance rules for the first part of the twenty-first century.

2 GLOBALIZATION AND GOVERNANCE

2.1 Towards global governance

It is important to situate our analysis of governance, through institutions and rules, in the wider context of globalization. For the process of globalization in the world economy has brought about profound changes in the international context which have far reaching implications for development. The need for governance is greater than before. But the task has become more difficult.

The world economy has experienced a progressive international economic integration since 1950. However, there has been a marked acceleration in this process of globalization during the last quarter of the twentieth century. There are three manifestations of this phenomenon—international trade, international investment and international finance—which also constitute its cutting edge. But there is much more to globalization. It refers to the expansion of economic transactions and the organization of economic activities across political boundaries of nation-states. More precisely, it can be defined as a process associated with increasing economic openness, growing economic interdependence and deepening economic integration between countries in the world economy.

Globalization, however, is not new. A similar phase began a century earlier than the current phase, *circa* 1870, and gathered momentum until 1914 when it came to an end. In many ways, the world economy in the late twentieth century closely resembled the world economy in the late nineteenth century. (The supporting evidence cited here draws upon Nayyar, Deepak (1995) 'Globalization: The Past in Our Present'. *Indian Economic Journal*, 43 (3): 1-18.) The parallels between the two periods are striking in terms of integration of the world economy, with comparable levels of integration in international trade, direct foreign investment and international finance. In the late nineteenth century, the missing dimension was international transactions in foreign exchange given the regime of fixed exchange rates under the gold standard; these are now massive. The missing dimension in the late twentieth century is labour flows, given the present regime of restrictive immigration laws and consular practices; there was almost unrestricted movement of people across national boundaries then.

There are two reasons why governance of the world economy is necessary now. First, national laws are applicable to resident individuals or registered firms but their jurisdiction does not extend to individuals or firms across national boundaries. This was probably sufficient in a world where economic space coincided, broadly, with political space. As a consequence of globalization, however, economic space extends much beyond political space. Yet, rules or laws do not. Second, rational economic behaviour by individuals (utility maximization) and firms (profit maximization) leads to externalities—unintended consequences of production and consumption processes. In a world economy characterized by ever increasing openness and integration, such externalities are much more prone to spillovers across national boundaries.

While globalization may have created some opportunities for the developing world, it is associated with an exclusion of a significant proportion of people and countries from economic opportunities. Markets exclude people as consumers or buyers of goods and services if they do not have sufficient incomes, which can be translated into purchasing power. Markets excluded people as producers or sellers if they have neither assets nor capabilities which can be used to yield an income.

And this is the problem with increasing globalization and the lack of governance. In a national context, the state may introduce correctives to pre-empt exclusion or interventions to limit the adverse effects of exclusion. The reason is simple: governments are accountable to their people. However, markets are not and globalization is a market-driven process. In the changed international context, the increased openness, interdependence and integration attributable to globalization have made it more difficult for governments to intervene (particularly through economic policies) and combat such exclusion without any increase in global governance. Instead, there seems to be an increasing gap between the global challenges and the capacity of international institutions to deal with them.

It is also clear that rules have developed to very different degrees in the different spheres. The contrast between the free movement of capital and the unfree movement of labour is the most striking. There are also striking asymmetries in the rules for the international trading system, being progressively set in the WTO. National boundaries matter less for trade flows and capital flows but are clearly demarcated for technology flows and labour flows.

Overall, however, what emerges clearly is the very limited nature of global economic governance. The momentum of globalization is such that the power of national governments is being reduced without a corresponding increase in effective international cooperation or supra-national government, which could regulate this market-driven process. In sum, national economies are much less governable while the global economy is almost ungoverned.

2.2 The logic of international organizations

International organizations (IOs) are mechanisms for transnational cooperation and collective action. Institutionalization serves to anchor international cooperation, be it through formal intergovernmental organizations such as the UN and Bretton Woods institutions or the various groupings of countries such as in the G-7, G-22 and G-77. International organizations can lower transaction costs for members and produce information; they encourage members to think about their future; create linkages across issues; and serve as agents that both create and diffuse ideas, norms and expectations. Their organizational structures and administrative apparatus provide a durable negotiating forum for direct interaction among members. IOs have been a successful institutional mechanism of global cooperation in part because they enjoy economies of scale by pooling activities, assets and risks. While IOs reflect the disproportionate influence of their more powerful members, they also bind the latter's actions to some degree.

In this context, it is important to make three sets of distinctions. First, there is a distinction between rule-setting or rule-making institutions such as the WTO or the IMF and development-oriented institutions such as the UNDP or UNICEF. Second, there is a distinction between treaty-based inter-governmental organizations, which constitute the United Nations system and informal consultative groups of countries within, or even outside, the United Nations system. Third, there is a distinction between inter-governmental organizations and non-government or private sector institutions.

The United Nations system and the Bretton Woods institutions are, almost inevitably, the focus of attention. There is a new set of actors on the stage who, unlike governments, do not approach problems from the perspective of national interest. It is also necessary to recognize the importance of these new actors. These are transnational corporations, international coalitions of NGOs and issue-networks among people across borders. These groups are shaping a whole set of standards, rules and norms. In the private sector, these range from the International Standards Organization to the International Organization of Securities Commissions. But there is also the International Union for the Conservation of Nature on environmental issues. This has led to the emergence of coalitions-of-the-willing on important issues. Therefore, the needs of global governance in the twenty-first century extend beyond cooperation among nation-states.

2.3 The importance of new world view

In 1945, when the UN and BWIs were created, a vision about world peace and full employment was at the heart of the worldview. At the start of the twenty-first century, it is time to seek consensus on a new worldview. This can only be based on a vision about the future economy, polity and society in the world, which should provide the core of a new development agenda. It must surely have the fundamental objective of ensuring decent living conditions for the ordinary citizens of the world. The eradication of poverty from the world is an imperative.

Such a consensus must be built on a depth of understanding which recognizes the complexity and diversity of development. This thinking should not be limited to the sphere of economics. It must extend to the realm of politics. In this new global message, the concern for efficiency must be balanced with a concern for equity. For efficiency and growth are means not ends. They need to be combined with economic stability, full employment, poverty eradication, reduced inequality, human development and a sustainable environment. In pursuit of these objectives, the new paradigm for world governance could derive some inspiration from the expected role of governments within countries. It could also derive some inspiration from the conception of political democracy so as to create a more democratic structure of world governance.

Governing globalization is a concrete starting point. Markets and globalization, orthodoxy believes, are necessary to ensure prosperity for everyone. This is a debatable proposition. In any case, it is clear that markets are not sufficient and may, in fact, exclude a significant proportion of people. The endeavour should be to make the market-driven process of globalization conducive to a more egalitarian and broad-based development pattern. The object of such a design should be to provide more countries with opportunities to improve their development prospects and more people within these countries to improve their living conditions. It would have to be supported by a new institutional set-up. This would mean providing *global public goods*, such as world peace and a sustainable environment, as well as regulating *global public bads*, such as international crime whether trade in drugs, arms, people or organs. It will be necessary to reform existing institutions and to introduce new rules or create new institutions. Some of these would require a system to correct for the failures of unregulated or liberalized international markets and other initiatives will be needed to build up missing markets.

2.4 Insights from public economics

In markets and societies at the national level, it is the role of governments to provide *public goods* such as road signs, street lights or public parks, and also to regulate *public bads* such as pollution or unfair competition. The logic of markets is exactly the same at the global level. But it is not obvious who would provide such goods at the global level. There is no world government that would provide international *public goods* and regulate international *public bads*. Yet, the openness, interdependence and integration associated with globalization mean that the functions of governments, in providing *public good*s and regulating *public bads*, will somehow have to be undertaken at the global level.

In a world where the pursuit of self-interest by nations means uncoordinated action or non-cooperative behaviour, sub-optimal solutions, which leave everybody worse off, are a likely outcome. International *public bads* are likely to increase while international *public goods* would not be provided. Such outcomes can be prevented only by evolving institutional mechanisms for cooperation between nation-states, which facilitate coordinated action and cooperative behaviour.

The economic characteristics of *public goods* (non-excludable and non-rival in consumption) are the same, irrespective of whether the *public goods* are local or global. The obvious examples are global security, global economic stability, global environment, global health and, of course, knowledge. The provision of such *global public goods* is a central part of the logic for international collective action. But the rationale for collective action across countries goes further, for it can address any form of market failure. The provision of *global public goods* requires institutions that ensure a contribution from all countries to meet international obligations. The United Nations was created to provide global security and world peace. The WHO was established to promote global health. Their success is determined by their ability to elicit the requisite cooperation from nation-states. The provision of *global public goods* requires the strengthening of existing institutions in some areas and the creation of new institutions in other areas.

Global public bads are more than simply the analogue of *global public goods*, where negative externalities spill over across national boundaries. The obvious examples are environmental degradation or international crime. *Global public bads* also have distributional implications. Chemical factories might yield profits for producers in one country, but acid rain for residents across the border in another. The gainers and the losers, then, are in different countries. Those who gain may not be in a position to, or may not wish to, make compensation payments to those who lose. The regulation of *global public bads* necessarily requires internationally agreed but nationally implemented rules that enforce restraint on the part of economic agents in all countries, whether individuals or firms. But it also requires funds for the needed compensation payments. Such international rules, even when funds are available, would have to be supported by mechanisms for enforcement and dispute settlement.

The institutional framework for the provision of *global public goods* and the regulation of *global public bads* could extend to public-private partnerships. In other words, market institutions or commercial mechanisms may be a useful complement for public action. It should also be possible to forge cross-border coalitions between nation-states and interest groups in civil society for this purpose. However, such institutional mechanisms would materialize only when the costs and benefits of unilateral self-insurance within countries are compared with the costs and benefits of international collective action across countries. This calculus is necessary both for the provision of *global public goods* and for the regulation of *global public bads*.

2.5 Principles of democratic governance

Governance is largely about rules and institutions that regulate the public realm. It is not just the inequitable outcomes that are important for assessing governance, it is also the ways the rules were constructed and enforced that matters. In order to offer some ideas as to the first steps toward appropriate change in global governance, it is helpful to look at principles of democratic governance.

A democratic system seeks to provide for equal participation of the rich and the poor, or of the strong and the weak, in political processes. Such systems are characterized by voice, transparency, accountability and fairness. In terms of these attributes, the existing arrangements for global governance are, to say the least, undemocratic. Developing countries account for more than 80 per cent of world population and contribute almost 50 per cent of world output. Yet, their influence in multilateral institutions that govern the world economy is at best limited and at worst marginal. In thinking about structures of governance, it is useful to make an analytical distinction between the nature of representation and the decision-making process in the system.

In terms of representation, the existing system does not provide for equal opportunity. The principle of one-country-one-vote in international institutions such as the United Nations and the WTO is not the same as the principle of one-person-one-vote in a political democracy, but it is clearly more representative than the principle of one-dollar-one-vote in multilateral institutions such as the IMF or the World Bank. The problem, however, also extends to *exclusion* from representation in arrangements such as the P-5 or the G-7 or OECD, which make decisions that are of profound importance for global governance. Furthermore, representation is incomplete. As a rule, most international institutions are inter-governmental organizations. In a more democratic set-up, there should be representation not only for the state but also for civil society, corporate entities and people at large.

In terms of decision-making, the existing system is even less democratic. If voting rights conform to some principle of equality between countries, voting decisions based on majority rule are, in theory, democratic. Yet voting rights are not equal between countries. Even where they are, international institutions are most reluctant to use voting as a means of decision-making. The right of veto in the Security Council of the United Nations is explicitly undemocratic. But decision-making by consensus, as in the WTO, can also be undemocratic, if there is bilateral arm-twisting or a consensus is hammered out among a small sub-set of powerful players, while most countries are silent spectators that are in the end a part of the apparent consensus. Of course, the reality is that not all countries are equal partners in the world. The essential corrective, then, is to create institutional mechanisms that give poor countries and poor people a *voice* in the process of global governance. Even if they cannot shape decisions, they have a right to be heard. More important, however, democracy is not only about majority rule, but also about protection of minority rights. The concerns of poor countries and poor people should, therefore, constitute an integral part of any democratic design for global governance.

In this context it is important to stress that for countries at vastly different levels of development, there should be some flexibility in the application of uniform rules. It is, in principle, possible to formulate general rules where application is a function of country-specific or time-specific circumstances, without resorting to exceptions. This implies a set of multilateral rules in which every country has the same rights but the obligations are a function of its level or stage of development. In other words, rights and obligations should not be strictly symmetrical for member countries. There is a clear need for positive discrimination or affirmative action in favour of countries that are economically poor or politically weak. It is also possible to specify conditions under which countries can depart from, or even opt out of, multilateral rules. It is important to recognize that, in democratic situations, *exit* has as much significance as *voice*.

There is, also, the issue that the enforcement of rules is asymmetrical. In the Bretton Woods institutions, enforcement is possible through conditionality. Such conditionality, however, is applicable only to developing countries or transitional economies that borrow from the IMF or the World Bank. In the WTO, enforcement is possible through retaliation. But most developing or transitional countries do not have the economic strength, even if they have the legal right, to retaliate. The reality, then, is that countries that are poor or weak conform to the rules whereas countries that are rich or strong can often flout the rules. There is no enforcement mechanism yet that can be imposed on the powerful players who circumvent the rules. The enforcement of rules, for the rich and the powerful, must therefore be central to any institutional design for global governance.

3 REFORMING THE EXISTING INSTITUTIONS

An assessment of the activities of the United Nations system and the Bretton Woods institutions over five decades is obviously difficult. Most would agree that the performance of these institutions presents a mixed picture with some important successes and some major failures. As highlighted above, the world has changed considerably and new global problems have surfaced, but the evolution or development of institutions for governance has simply not kept pace. The capacity of the old institutions is no match for the complexity of the new challenges, and changes are urgently needed to close the institutional gap. Based on historical and institutional analyses in the project, this section suggests various reform measures for the main international organizations: the United Nations, International Monetary Fund, World Bank and World Trade Organization.

3.1 United Nations

The United Nations system spans a wide range of activities such as peacekeeping, disarmament, refugees, famine prevention and human rights, development, labour, health, education and culture. Changes in the world, particularly during the past decade, have eroded the legitimacy, effectiveness and credibility of the United Nations. The process of globalization has given rise to new problems and governance needs but the UN system has yet to adjust. The responsiveness of the United Nations to issues of our times has been limited to global meetings such as the Earth Summit or the Social Summit; these are useful fora for public concern but insufficient as solutions to the problems at stake.

World peace is seen as a critical pubic good and the UN is judged mainly in relation to peace and security issues. It is clear enough the UN did not respond well to the challenges of the 1990s. The UN performance in Bosnia and Rwanda were widely perceived as dismal failures. The bypassing of the Security Council over Kosovo reinforced the impression that the UN peace and security role was being eclipsed. There is still no system in place to take care of, let alone prevent, complex humanitarian emergencies.

The moral authority of the UN, however, is seriously undermined because its laws or principles are enforced selectively when it suits the interests of the rich and the powerful. The UN is hamstrung by a range of problems from inadequate resources to political disagreements. And the real problem, often, is that the United Nations is a watchdog without teeth. The problem is compounded by the fact that there is a democratic deficit in the UN system. It was an integral part of the original design and it has not diminished with the passage of time.

The United Nations is the core of any international system of governance. Therefore, it is essential to contemplate reform that would make it more credible, more legitimate and more effective. It must act in accordance with its charter. It must be democratic in achieving representation and making decisions, through participation, transparency and accountability. It must move towards political independence in relation to the powerful geopolitical actors. Some institutional changes are obviously desirable.

Security Council reform

Created to reflect the geopolitical realities of 1945, the magnitude of change in the global setting since then makes reform of the Security Council imperative. These changes have to be recognized rather than ignored or wished away. The failure to make progress on this symbolic issue reduces the legitimacy of the UN and tinged the whole project of UN reform with doubt. First, there should be expansion of Security Council membership, at least to take account of the fundamental changes in the composition of international society since 1945, particularly de-colonization and the far greater role being played by non-Western countries. Second, it is imperative to circumscribe the veto powers of the Permanent Members of the Security Council. These countries have a privileged status that is neither remotely democratic nor reflective of current power relations.

Independent financing

It is necessary to seriously explore the prospect for various alternative modes, at least partial, of independent financing. Success here would both contribute to the overall effectiveness of the UN system and also be understood as a loosening of the reins of political control now exercised by the strongest member states. The financing pressures on the UN in recent years provide a rationale for restructuring UN financing arrangements. Also, the weakness of political will in humanitarian emergencies suggests that an enhanced UN role in the future depends in part on a financing structure that is independent from P-5 control. It is important to realize that the issue of financing is less about money than political control. It makes plain why the resistance of some governments is so intense, and why only a mobilization of even stronger counter-pressures of civil society in those same countries is likely to make independent financing a feasible project. Some version of the Tobin tax, say on international foreign exchange transactions or stock market transactions, and some charges on the use of the global commons, are possible means of such independent financing.

Volunteer peace force

To enable more reliable UN responses, especially in the setting of humanitarian challenges of small or medium scale, the establishment of a high quality UN volunteer peace force would be of great benefit. It would allow the organization to respond without expecting member states to expose their citizens to loss of life. It would tend to depoliticize such undertakings, and yet provide the UN Security Council with a mechanism to extend rapidly collective security responses to situations of severe humanitarian emergency.

The character of such a force, and its administrative relation to the UN system would have to be worked out in great detail. It would be an expensive undertaking if done in a professionally responsible manner. The coordination of control between the Security Council and the Secretary-General would be an important concern. Despite practical obstacles, the case for a UN volunteer force drawn from many countries seems strong at this point. Resistance from P-5 governments is likely to persist, but it might dissipate in due course, given the disenchantment with alternative approaches.

Global people's assembly

Despite the rhetoric, it is clear that the UN is not democratic enough. Structurally, international organizations will always face a democratic deficit. One country one vote (as in the UN) might seem more democratic than one dollar one vote (as in the Bretton Woods institutions) but both violate the notion of democratic equality inherent in one person one vote. Modelled somewhat on the European Parliament, a 'people's assembly' would give the peoples of the world more meaningful opportunities for participation in the UN system. This new organ could be structured to be a parallel body to that of the General Assembly and would be the voice of global civil society.

An economic security council

The creation of an economic security council has become essential as a means of governing globalization. Its creation would acknowledge the increasing importance of the economic dimensions of world order as well as the insufficiency of current institutional arrangements for economic governance at the global level. The Asian financial crisis of 1997, particularly in Indonesia, illustrated how rapidly economic vulnerability can result in massive suffering for large proportions of the population.

An economic security council would address the economic and social consequences of developments in the world economy. It would ensure that the United Nations provides an institutional mechanism for consultations on global economic policies and also, wherever necessary, the international regulatory authority. An economic security council would need to balance concerns of influence and representativeness. It would also need to ensure access for private sector representatives and certain NGOs in the formal workings of the new organ. But the existence of practical and political obstacles is no reason to bury an idea, whose realization could bring great benefit to the global public good.

3.2 The International Monetary Fund

The IMF was created to manage the international monetary system based on the gold-exchange standard active when currencies were not convertible. The world has changed then. The IMF has adapted to the change from a regime of fixed exchange rates to a regime of floating exchange rates, just as it has attempted to cope with the move from capital controls to capital mobility. It has had more success with the former than it has had with the latter. But it is no longer able to manage the international financial system.

Arguably, the most important development in the global economic system over the past several decades has been the liberalization of international capital markets that got underway in the 1970s. There has been a marked increase in the volatility of capital movements and asset prices, and its spread (or ‘contagion’) across markets and national borders. Volatile financial markets generate economic inefficiencies, create financial risk and raise the cost of capital. Exchange rate fluctuations in particular have been highly destabilizing. Developing countries are especially vulnerable owing to their dependence on foreign capital and their external indebtedness.

The recent string of crises has provoked impassioned calls for a fundamental overhaul of global financial governance. The IMF has been increasingly marginalized in managing capital flows and exchange rates even as they become more and more volatile. There is an enormous and increasing discrepancy between the scale and pace of financial movements and the institutional framework to regulate it. Reforming the IMF is an important part of redesigning the governance of world economy in the twenty-first century. Some changes in the role, policies and governance of the IMF are suggested below.

Redefined role

Given the massive change in context, the time has come to redefine the role of the IMF. This means defining a constructive role in managing and stabilizing the international financial system, not only through crisis management but also through crisis prevention. The sustainability of the exchange rate, of the current account deficit, of short-term debt and of outstanding portfolio investment, is relevant in thinking about the objectives of a reformed international financial system. However, the pre-occupation with the instability and volatility of capital flows associated with financial crises is so great that there is a tendency to understate the importance of managing exchange rates and current account deficits. The world, it seems, has come a full circle from a time when we thought only about current account macroeconomics to a time when we think only about capital account macroeconomics. But the adjustment problem, and for some countries even the liquidity problem, is not yet *passe*. Therefore, even as it adapts to its new role, the IMF must continue to perform its old functions. In doing so, it is necessary to change the structure of governance and the mode of thinking.

Better governance: representation, transparency and accountability

Governance in the IMF needs much more representation, transparency and accountability. If the IMF is to become the legitimate institution for governance in the world economy, it will need to become more representative of developing country concerns. The representation embodied in voting rights that are based on quotas is far too unequal between member countries. The lenders are the principal shareholders in the IMF but the borrowers are the principal contributors to the income of the IMF. There is a clear need to restructure voting rights so as to make them more representative and less unequal. A better combination of quota-based votes and basic votes would seem to offer a reasonable solution; at present, the share of basic votes is so minimal that these have little impact.

There is almost no transparency in the IMF. Indeed, its operations and programmes are shrouded in secrecy. The absence of public scrutiny means that there are almost no checks and balances. It is high time that the IMF practices what it preaches about transparency. This calls for a disclosure of information. The office for independent evaluation of operations must be given adequate resources and its independence ensured.

The accountability of the IMF is limited, at best, to finance ministries and central banks, which, in turn, have close connections with the financial community. The IMF has almost no accountability to governments in totality, let alone people at large, when things go wrong. Accountability is an imperative without which the IMF could continue to pursue the interests of a subset of the international community, often to the detriment of the general interest of peoples and governments or the collective interest of the world economy.

Rethink conditionality

There are at least four separate conditionality problems. First, the whole idea goes against the issue of government ownership. Second, regarding content, evidence of overkill has accumulated and has led to mounting criticisms of the IMF's analysis and approach. Third, conditionality has expanded into areas that have no direct bearing on the macroeconomic adjustments needed or loan repayment. It has thus become an infringement on national sovereignty. Fourth, conditionality is an ineffective tool for changing economic policies. Clearly, the practice of conditionality should be fundamentally reformed.

Ultimately, loans should go to those countries that have good policies in place, i.e. to make conditionality *ex post*. As far as 'good policy' countries are concerned, it makes eminent sense for the IMF (and World Bank) to provide automatic approval of a programme prepared by a 'good policy' recipient country. This would strengthen ownership and largely eliminate conditionality. The issue here is determining the criteria to be used for evaluating the recipient as a 'good policy' or a 'bad policy' country. The criteria must be restricted to a small set of macroeconomic performance measures that are less fundamentalist than current indicators.

A problem with *ex post* conditionality is that it will steer resources away from 'bad policy' countries, often the most needy. Such countries require a different type of assistance that should be provided by the World Bank. The relative importance of its role as a 'gatekeeper' for other (larger) external sources of finance in the poorest countries should, in any case, be reduced in favour of the World Bank and the regional development banks, which adopt longer-term perspectives and, accordingly, can better promote local ownership of government programmes.

Review its position on macroeconomics and liberalization

The IMF needs to reconsider its thinking in macroeconomics. There is now ample evidence to suggest that its stabilization programmes lead to adjustment through changes in output rather than through changes in prices. The outcome is beggar-thyself policies where current account deficits are reduced or inflation is restrained through a contraction in output and employment.

The IMF should rethink its perspective on capital account liberalization and capital account convertibility. There is no evidence of an association between capital account liberalization and economic growth. In contrast, there is substantial evidence that premature liberalization and integration into international financial markets are fraught with danger and can put development at risk. Developing countries should not give away their autonomy on this matter unless the international financial system is radically improved. It is now generally agreed that such liberalization should be gradual, should emphasize longer-term flows, be extremely cautious with shorter-term and volatile funds (such as short-term credits and portfolio flows), and should be preceded by the development of strong prudential regulation and supervision, as well as consistent macroeconomic policies. Moreover, it is also accepted that any international agreement in this area should include safeguard mechanisms that would allow a temporary use of capital controls under specified conditions.

3.3 The World Bank

More than fifty years after its creation, the World Bank also needs to redefine its role. The World Bank was set up to provide financing for reconstruction and development projects. Similar to the IMF, the World Bank has gradually shifted its emphases and objectives. But, the reality is that progress has stalled. It is estimated that 1.2 billion people still live in poverty. The Washington consensus policies of the 1980s and 1990s failed to generate sustained growth in most poor countries and often exacerbated an unequal income distribution. There is little chance of most developing countries meeting the Millennium Summit targets to reduce poverty to half by the year 2015. Some changes in the role, governance and policies of the World Bank are suggested below.

A redefined role: partnership in development

Clearly, the Bank's primary task should be to respond to the crisis of development. Its subsidiary task should be to provide scarce capital to countries and to sectors which do not have access to international capital markets. The benefits may be more related to access in bad times than to reduced borrowing costs. The pursuit of these objectives, however, requires a change of mindset. The World Bank should cease to be a moneylender. It should transform itself into an institution more concerned with development. Thus, the focus of its activities should be on development in poor countries and for poor people, as a partner in—and not a manager of—development through local participation.

Governance: representation, transparency and accountability

The representation, as in the IMF, is asymmetrical and unequal. A very large proportion of the voting rights are vested in a very small number of industrialized countries as they are the principal shareholders in terms of paid-up capital. In contrast, a large number of developing countries and transitional economies are vested with a small proportion of the voting rights even though they are the principal stakeholders, interest payments from whom provide most of the income of the World Bank. The need to restructure such a voting system is obvious. It is a necessary condition for change. The accountability also is limited, once again, to finance ministries and central banks.

Moreover, in the World Bank, there is a difference between what is said and what is done, just as there is a difference between the thinking arm and the operational arm. The Operations Evaluation Department exists, but learning from experience is not yet incorporated into management and executive board decisions. The independent evaluation must also begin in borrowing countries to assess projects and programmes supported by the World Bank. This would be the beginning of accountability to governments and to people.

Promoting local ownership: reforming conditionality

There is an obvious need to promote local ownership of country programmes. For this purpose, the World Bank must give up its attempts to micro-manage economies through conditionality. Similar to the IMF, this will require radical reform in the sphere of conditionality. Conditionality is characterized by over-kill and over-reach, and, quite often, it does not work. The World Bank should, instead, seek to become a partner in development though local participation.

The World Bank now frames its activities in terms of a poverty reduction strategy programme (PRSP) under local national leadership. However, doubts remain about implementing the PRSP framework. So far, there has been little noticeable change in the

World Bank's country operations. While this process is undoubtedly difficult, it is inherently feasible and should be a matter of the highest priority. Translating the framework into practice, and achieving genuine donor coordination in the process, would have a massive impact.

Re-thinking policies and institutions conducive to development

It is perhaps just as important that the World Bank re-orients its thinking about development which currently attaches far too much importance to markets and to openness. Simplified prescriptions, which emphasize more openness and less intervention and which advocate a rapid integration into the world economy, combined with a minimalist state that simply vacates space for the market, are not validated by either theory or history. Economic theory recognizes and economic history reveals the complexity of the development process. The degree of openness and the nature of intervention are strategic choices in the pursuit of development, which should not be prescribed irrespective of the time and space, for they depend upon the stage of development and must change over time.

Generating and disseminating knowledge

It is increasingly recognized that what separates developed from less developed countries is not just a disparity in capital endowments, but gaps in knowledge. The production and dissemination of knowledge about development and about policies or institutions that are most conducive to development is an important function of the World Bank. This function has been distorted, if not subverted, by the Washington consensus. Washington consensus policy prescriptions became increasingly influential as these were adopted by the World Bank, to begin with in its research agenda and subsequently its policy menu. The dominance in ideas soon turned into a propagation of ideology as the World Bank acquired a near-hegemonic status in thinking about development. The time has come to question this knowledge-hegemony. This process can begin the moment developing countries and transitional economies seek to influence and to shape the research agenda of the World Bank. This is neither implausible nor unreasonable because research budgets are supported by the income stream rather than the share capital of the World Bank. More competition is as desirable in the sphere of knowledge generation as in any other. It would help generate a better understanding of which policies and institutions are truly conducive to development.

3.4 The World Trade Organization

There has been a spectacular growth in international trade over the last 50 years. An increasing proportion of world output enters into world trade. An increasing proportion of world trade is made up of intra-firm trade. Trade flows have moved much beyond the simple world of goods, just as trade barriers have moved much beyond the simple world of tariffs. Trade is more and more an arena for conflicts and claims from other spheres.

Trade was one of the three pillars at the Bretton Woods conference, but no formal institution was set up at that time. Nevertheless, the international trading system has evolved considerably since its inception as the General Agreement on Tariffs and Trade (GATT) in 1947 to its latest incarnation as the World Trade Organization (WTO). The GATT was designed to deal with 'shallow' integration, focusing on lowering the barriers associated with cross-border trade in goods. The current WTO system is much more expansive seeking harmonization or 'deeper' integration. Deeper integration seeks to achieve a harmonization of domestic economic policies spanning a wide range of issues including investment, competition, technology, government procurement, taxation and labour standards. The process is no longer confined to cross-border transactions in tangible goods and currently extends to transactions in intangibles, such as services. It now comprises a vast and complex array of agreements forming its substance and mandate.

But the system has not kept pace with the changing reality and the increasing complexity of world trade. The WTO received an unprecedented jolt at the Seattle Ministerial Meeting in late 1999. There remain deep disagreements between the developed and developing countries on issues relating to labour standards, investment and competition policy. As the Seattle meeting demonstrated, integration that is not aligned with economic or political realities, and is unresponsive to the principles of equity and democratic functioning, can throw the whole WTO process into an impasse. While there is an apparent consensus, or less disagreement, after the Doha Ministerial Meeting in 2001, the future remains far from clear.

The WTO is still young enough to permit more fundamental debate as to its rules system, its decision-making systems, the role and composition of its secretariat, and the capacity of all its current or prospective members to benefit from it. The formal voting structure and dispute settlement system in the WTO both allow, in principle, for greater input from its smaller and poorer members, and create the potential for more equitable outcomes for them. But developing countries will need to get their collective act sufficiently 'together' to realize the opportunities. Some suggestions for change and reform are set out below.

Development as a fundamental objective of the WTO

To begin with, it is essential to situate the institutional role of the WTO in the wider context of development. For trade is a means not an end. Economic development, which improves the living conditions of the people at large, is a fundamental objective. The WTO should, therefore, recognize, rather than ignore, the differences in levels of income and development between countries. This gap has widened during the second half of the twentieth century. The eradication of poverty and the creation of employment should thus be WTO objectives as much as trade liberalization and trade expansion.

A democratic and effective decision-making system

Whereas the WTO's formal voting structure (in principle one-country-one-vote) allows for greater developing country power than in the international financial institutions, its governance does not incorporate a permanent executive board or an equivalent body. An efficient system of representative decision-making will need to be devised. Decision-making in the WTO continues the *Green Room* tradition of the GATT in which the main players exercise disproportionate influence behind closed doors while a large number of member countries are spectators outside and are often presented with a *fait accompli*. Given the large number of member countries and the complex mandate of the WTO, an efficient system of representative decision-making, based perhaps on group negotiations or an executive board, would have to be contemplated.

Do not overload the agenda

The agenda for new rules in the WTO needs careful scrutiny, for it is shaped by the interests of the industrialized countries while largely neglecting the needs of development. The proposed multilateral agreement on investment should not, in fact, be lodged in the WTO. The issue of labour standards, of course, is simply not in the domain of the WTO. And there is no reason why environmental standards should find a place either. There is a strong temptation to place issues or lodge agreements on a wide range of matters in the WTO, essentially because it incorporates an enforcement mechanism and provides a legal right to retaliate. Consequently, there is a real danger that the WTO may be turned into an overloaded elevator which is neither functional nor safe.

Abandon the concept of the 'single undertaking'

It is necessary to abandon the concept of the *single undertaking* as the binding rule for future negotiations. The concept of 'single undertaking' means member countries are required to agree on (and abide by) the *entire* set of rules that is multilaterally negotiated within the WTO and to continue to do so in all its future negotiations and activities. Given the vast differences in levels of development between countries, there should be some flexibility for joining in, or opting out of sub-agreements in the WTO. The modality of plurilateral agreements should be taken out of its present limited context and used more liberally, whenever there is a lack of unanimity among the member countries or presence of strong reservations on the part of some, on the proposed disciplines on new issues calling for deeper integration. This modality is ideal in situations where it is neither feasible nor desirable to subject all countries, irrespective of levels of development, to a uniform discipline modelled on systems in a few industrialized countries and sometimes, as in Trade-Related Intellectual Property Rights (TRIPs), on the system of one country alone. Of course, member countries should continue to subscribe to a core of principles and practices that can be easily specified.

Implement a 'standstill' and a 'roll-back'

It would be desirable to hasten slowly in creating disciplines for deeper economic integration through the WTO. It is worth contemplating a *standstill*. A formal step is for the WTO to declare a standstill on new issues sought to be placed on the agenda for multilateral negotiations in the WTO. Issues such as labour standards and a global investment regime should be deferred for the time being. A declaration of a standstill would make it possible to conduct a collective assessment of how integration efforts so far have affected member countries, particularly those of the South and, among them, the poor and the least developed countries.

It is also necessary to reconsider, if not *roll-back* some of the existing agreements in the WTO, such as the unequal agreement on trade related aspects of intellectual property rights. This was signed at a time when most governments and most people did not understand its economic implications. But it has profound implications for development in countries that are latecomers to industrialization.

Strengthening of 'trade-legal aid' arrangements for the poorest

The formal voting structure and dispute settlement system in the WTO both allow, in principle, for greater input from its smaller and poorer members. In reality, however, the capacity of many, perhaps most, developing countries to participate effectively in the WTO system is very much in doubt. The WTO is a member-driven organization and the continuous WTO process involves at least 45 meetings per week in Geneva. If delegates from member countries are not actively involved in its day-to-day activities, their interests are ignored.

The requirements for effective participation (the number of meetings and complexity of the issues) place an enormous strain on resource-constrained smaller and poorer countries. The most important institutional reform that WTO needs is institutional arrangements to off-set weak negotiating capability of developing countries. Some form of financial support would allow these members to engage experts to help them to formulate their position on complex issues.

4 EMERGING ISSUES AND MISSING INSTITUTIONS

As the world has changed, new global problems have surfaced, and the evolution or development of institutions for governance has simply not kept pace with the challenges of the twenty-first century. An emerging institutional gap is discernible in a very wide range of symptoms. There are areas such as organized crime, global climate change, portfolio investment flows and illegal migration, where better regulations are necessary to cope with cross-border consequences. National authorities are manifestly unable to operate alone. Yet, no international authorities or coordinating bodies have been created. The analysis in the UNU/WIDER project pointed in particular to a number of areas where institutional innovations are the most pressing.

4.1 Global macroeconomic management

The perspectives on global macroeconomic management have undergone profound changes during the second half of the twentieth century. The *age of globalization* has created a new world with an explosive growth in international finance as a consequence of the domestic deregulation of financial sectors and the introduction of capital account liberalization. There is now a much greater instability in exchange rates (and interest rates) and the volatility is associated with a contagion across markets and borders. In this world, developing countries and transitional economies are more spectators than participants but are not immune from the consequences. It is time to develop a capital account macroeconomics and think about global macroeconomics. Moreover, the object of macro-management should extend beyond managing inflation to restoring full employment and stimulating investment.

At the turn of the century, it is clear that the problems of global macroeconomic management are, to say the least, complex. Yet, there is virtually no institutional framework for this task, which is left almost entirely to the market. The G-7 does provide an institutional framework for consultation about, if not coordination of, macroeconomic policies. This is simply not enough, in part because it is driven largely by G-7 (if not just G-1) interests and in part because it needs much wider representation. Clearly, global macro-management cannot be left to the market and it must extend beyond the G-7. There has to be some institutional mechanism for the coordination of macroeconomic policies.

It is also necessary to evolve a suitable institutional framework for consultation and surveillance as there is a long list of concerns. It is essential to deal with international volatility and contagion. It is just as important to reflect on the management of exchange rates in a world where there are no fundamentals but only conventions. These issues in global macroeconomic management are important not only for the industrialized economies but also for the developing countries and transitional economies. And, in so far as global macroeconomics is not simply about managing financial flows or exchange rates, it is also important to think about the macroeconomic objectives of internal and external balance in the short term and macroeconomic policies that are conducive to economic growth and productivity increase or employment creation in the long term.

4.2 International financial architecture

The frequency and intensity of the financial crises have led to a near-consensus on the need to reform the international financial architecture. There are, however, more fundamental reasons for reform and change. The existing institutional framework for the governance of the international monetary system, embodied in the IMF, was created a long time ago. Since then fixed exchange rates have been replaced by floating exchange rates and capital controls have given way to capital mobility. This has been juxtaposed with an explosive growth in international finance. The expansion in international banking has been phenomenal, the international market for financial assets has experienced similar growth and the size of international foreign exchange markets is staggering.

But that is not all. Interdependence and openness, combined with volatility and contagion, have made the governance of international financial markets far more difficult. The conception and design of the architecture should, of course, be concerned with crisis prevention and crisis management. But it should also support the integration of developing countries into the world economy in a manner that promotes rather than hinders development.

First, there is a need for institutional mechanisms that would facilitate consultation, consistency and surveillance of national macroeconomic policies. This would be conducive to international collective action that would address problems arising from market failure and negative externalities which spill over across national boundaries. For the industrialized countries, some global consistency of their macroeconomic policies would enhance their collective ability to minimize both inflation and unemployment. For the developing countries, collective lines of defence in the face of financial boom-bust cycles could enhance their ability to cope with contagion.

Second, there is a need to increase the supply of emergency financing in times of crisis so that it is made available before rather than after international reserves are depleted. Moreover, such financing should include countries facing contagion. The effectiveness of emergency financing may be limited if the negotiation process is too cumbersome or if it is perceived to postpone adjustment which is judged as inevitable. Most important, perhaps, markets may decide that intervening authorities are unable or unwilling to provide finance in quantities required to stabilize speculative pressures. Nevertheless, the very existence of emergency financing could perform a stabilizing role.

Third, there is a need to create an international sanction for standstill provisions, or orderly debt workout procedures, in the realm of international finance. This is essential because capital flight, with its chaotic effects on exchange rates, interest rates and economic activity, does significant damage to debtor countries. It is also bad for creditors. Such standstill provisions would play exactly the same role as national bankruptcy procedures play within economies. The preventive suspension of debt service, combined with rescheduling, under an international agreement would ease, if not resolve, the worst problems associated with capital flight.

Fourth, countries should have the freedom to choose an exchange rate regime and should have autonomy in capital account liberalization. The need for prudence in capital account liberalization where it has not been introduced, and the need for capital controls (whenever the need arises) where it has been introduced, is clear enough.

Fifth, there is an emerging consensus that there is a need to improve the institutional framework in which financial markets operate, whether through principles of sound corporate governance or through common minimum standards in prudential regulations, supervision and accounting. There is, in general, broad agreement on the need for regulation and supervision to ensure financial stability. There is less agreement on a more elaborate institutional framework for governance. In a world of open financial markets, however, only an international institution that has power to regulate, intervene and enforce can effectively regulate the risks to which economies are exposed. The proposed Financial Stability Forum is but a first step.

It may, ultimately, be worth thinking about a World Financial Authority that would manage systemic risk associated with international financial liberalization, coordinate national action against market failure or abuse, and act as a regulator in international financial markets. Such an authority would have powers of regulation and surveillance. And it would supervise the inspectors. It would also have the ability to coordinate with central banks and the IMF when interventions may be needed from an international lender of the last resort. This interface between national regulatory structures and international regulatory norms would need an institutional framework.

4.3 Transnational corporations

The last quarter of the twentieth century—*the age of globalization*—has witnessed the phenomenal rise of transnational corporations. Transnational corporations, which have come to dominate cross-border trade, investment and technology, constitute both the driving force and the cutting edge of globalization. Until the mid-1990s, the economic activities of transnational corporations were governed largely by national rules or national policies.

It would seem that, wherever cross-border economic transactions are dominated by transnational corporations, governance is moving from national policies and rules to international institutions and rules. This is a consequence of the strong influence exercised by transnational corporations on rules through their influence in home countries. Their object is to reduce transaction costs and their bottom line is the balance sheet. But these rules often affect what developing governments can or cannot do and reduce degrees of freedom in formulating development strategies. The problem is that there are no rules, even contemplated let alone negotiated, on what transnational corporations can or cannot do.

The time has come to consider the creation of an international system of governance for transnational corporations because the economic space of their activities extends way beyond the geographical space of nation-states. In this context, it is important to emphasize that international regimes of discipline should be concerned not only with the rights but also with the obligations of transnational corporations. There is a need for a discipline on restrictive business practices of transnational corporations. And, in a world where the economic activities of large firms transcend national boundaries, an international regime of anti-trust laws is also necessary. Indeed, an institutional framework for global governance of transnational corporations would have to incorporate regulatory norms that interface between corporate policies and international obligations.

Such an endeavour would not have to begin from scratch. It is possible to build upon the earlier work in UNCTC and UNCTAD on restrictive business practices and on a code of conduct for transnational corporations. These proposals were reasonably balanced but did not provide for any enforcement mechanism. Similarly, there is much to learn from the European Union experience on competition policy. There is, in addition, considerable work on corporate governance in the Organization for Economic Cooperation and Development (OECD) and the International Finance Corporation (IFC). The OECD bribery provisions also constitute a code of conduct. Interestingly enough, arbitration practices in the corporate world follow UN systems. And there is a framework for the settlement of disputes between transnational corporations and governments in the International Centre for Settlement of Investment Disputes (ICSID). The United Nations is also attempting to engage the corporate community in terms of a commitment to principles in the sphere of labour standards, human rights and environmental concerns. This patch-work of informal arrangements could provide a starting point.

But, there is the critical issue of taxation of large international firms which is mostly untouched. So far, there is no institutional mechanism for exchange of information. The creation of an institution for this purpose, say a World Tax Authority, is not even on the distant horizon.

4.4 Cross-border movements of people

The movement of people across national boundaries is not new but is becoming an increasingly important issue at the start of the twenty-first century. While there has been a marked acceleration in the other dimensions of globalization during the last quarter of the twentieth century, this does not apply to labour flows. However, there is an increasing tension between the laws of nations that restrict the movement of people across borders and the economics of globalization that induces the movement of people across borders. For a number of reasons, this is likely to be a crucial area for international institutional innovation in the future.

Pressures for international migration are not surprising in a world where income disparities between countries are vast, while the spread of education combined with the revolution in transport has led to a significant increase in the mobility of labour. The reach of the electronic media is enormous—people get much more information about other parts of the world. Globalization has set in motion forces which are creating a demand for labour mobility across borders, and market institutions, legal and illegal, have developed which make it much easier for people to move across borders. The pressure for change will be reinforced by demographic change. Rapid population growth in developing countries will lead to increased pressures to move. The ageing of the population in the industrialized countries may make the import of labour an economic necessity, which could even lead to selective relaxation of immigration laws and consular practices.

The implications of these pressures and the institutional gap are already being felt. There has been a rapid growth in illegal migration; during the last decade, 30 million people were trafficked in Southeast Asia alone. This has been facilitated by the development of illegal networks facilitating the illegal movement of people—now said to be the fastest growing criminal market.

In terms of governance, there are hardly any international rules or international institutions that govern cross-border movements of people. The solitary exception is, perhaps, UNHCR, which provides for the protection of refugees. For the cross-border movement of people other than refugees, however, there are no international institutions or rules, let alone governance. Such cross-border movements are governed entirely by national immigration laws and consular practices. As we enter the twenty-first century, the time has come to initiate a preparatory process. It should, perhaps, begin with an exchange of information on surpluses and shortages between labour-exporting and labour-importing countries, which might ultimately provide the basis for the creation of an ‘international labour exchange’. This cannot suffice. It is also essential to work towards a new institutional framework that could govern cross-border movements of people. It is necessary to highlight two dimensions of governance needs in this sphere: *actual migrants* and *potential migrants*.

Actual migrants

There is a need to ensure rights and to eliminate abuse of actual migrants in their countries of residence after they have moved. Among such migrants, it is necessary to make a distinction between legal migrants and illegal migrants. There are some similarities in the problems faced by them, but there are also important differences. For the former, the essential objective should be to ensure a respect for their rights. For the latter, the fundamental objective should be to eliminate exploitation and abuse. Thus, the institutional solutions would need to be somewhat different.

For migrant workers who have been admitted to their countries of destination in accordance with the laws of the land, there must be some equivalent of the WTO concept of *national treatment*. This, in turn, requires a universal acceptance and ratification of ILO conventions on migrant workers. In this context, it is essential to highlight a striking asymmetry. There is so much emphasis on labour standards, which are sought to be lodged in the WTO. There is so little concern about rights of migrant workers, which are written into obscure ILO conventions. Yet, it should be clear that labour standards and migrants’ rights are two sides of the same coin. Both should remain in the ILO where the rights of workers are a fundamental concern.

The cross-border movement of people, attributable to market forces despite immigration laws, is also a reality. But the plight of illegal immigrants, everywhere, is a cause for serious concern. The working conditions are exploitative and the living conditions are abysmal. This is not simply a matter of enforcing the law. There is often collusion between intermediaries and employers while governments turn a blind eye to this reality. Such tacit approval of illegal migration to meet labour shortages must be replaced by an explicit recognition of the need for labour imports which should be met through legal channels even if such imports are seasonal or temporary. At the same time, there is a clear need for concerted action to curb the trafficking in people that is organized by international criminal and smuggling syndicates. Such trafficking in people is a gross violation of human rights which is an example of international *public bads* that need to be regulated through concerted joint action by countries of origin and destination. In this task, the ILO should play a critical institutional role.

Potential migrants

We also have to think of potential migrants before they have moved so that the cross-border movement of people is governed at least in part by transparent and uniform multilateral rules rather than by diverse national laws and non-transparent consular practices alone. Thus, it is necessary to develop institutions, or rules, that govern the cross-border movement of guest workers who move temporarily, as also for professionals or service providers who move temporarily for a specified purpose. Such labour flows have increased significantly in the recent past and are likely to increase further. It is, therefore, important to develop a set of transparent rules for the temporary movement of guest workers or service providers across national boundaries. In doing so, the equivalent of the *most-favoured-nation* principle, which makes for unconditional non-discrimination, could provide a basic foundation.

To begin with, regional arrangements such as the EU, which build on other forms of economic integration, could yield feasible solutions, but regional arrangements are difficult to replicate and do not always constitute building blocks. Sooner rather than later, therefore, it is worth contemplating a multilateral framework for immigration laws and consular practices that governs the cross-border movement of people. This would be akin to multilateral frameworks that already exist, or are sought to be created, for the governance of national laws, or rules, concerning the movement of goods, services, technology, investment and information across national boundaries.

5 CONCLUSION

Global governance, then, is not so much about world government as it is about institutions and practices combined with rules that facilitate cooperation among sovereign nation-states, NGOs and firms. The policy brief has argued that greater efforts at 'governing globalization' are necessary due to dramatic changes during the second half of the twentieth century. Globalization has meant an increase in international interactions across national borders without an adequate development of the rules and institutions to manage these interactions. Without reform of existing institutions and development of new institutions, it is difficult to see how the international community can solve the challenges that face it in the first part of the twenty-first century. The fundamental objective of the conception and the design for governing globalization should be based on a new worldview that puts the priority on ensuring decent living conditions for all people.

This policy brief was intended to provide information and analysis, combined with recommendations, for reform for a number of constituencies to which global governance matters. More specifically, it targets the following groups:

- Academics: it provided a comprehensive analysis of the current state of knowledge on issues of global governance for teachers, researchers and students in economics, political science and international relations.

- Policy-makers and diplomats: it identified key issues for those in national governments, particularly those in the Treasury or the Foreign Office, and international organizations, that are working to make the process of governing globalization more legitimate as well as more effective in reducing poverty around the world.

- Journalists: particularly those writing about the world economy and the world polity.

- NGOs: many of which are increasingly concerned about problems associated with global governance, the policy brief could serve as an advocacy tool for improving the nature of global governance.

The policy brief is clearly not the end of the debate on the subject. It represents a modest beginning. The object is to stimulate discussion and to highlight a number of areas where further work is required. Historical experience suggests that crises are the catalysts of change. Last time, it was the aftermath of a world war and a worldwide economic depression that led to the foundation of the United Nation systems and the creation of the Bretton Woods institutions. The world need not wait for another crisis of such proportions to contemplate and introduce the much needed changes in global governance.

LIST OF CHAPTERS
Governing Globalization: Issues and Institutions

Editor: Deepak Nayyar

Part I **CONTEXT**

Chapter 1 Introduction
Deepak Nayyar

Chapter 2 Nationalism and Economic Policy in the Era of Globalization
Amit Bhaduri

Part II **ISSUES**

Chapter 3 Global Macroeconomic Management
Lance Taylor

Chapter 4 Transnational Corporations and Technology Flows
Sanjaya Lall

Chapter 5 Capital Flows to Developing Countries and the Reform of the International Financial System
Yilmaz Akyüz and *Andrew Cornford*

Chapter 6 Cross-Border Movements of People
Deepak Nayyar

Part III **INSTITUTIONS**

Chapter 7 The United Nations System: Prospects for Renewal
Richard Falk

Chapter 8 The Bretton Woods Institutions: Evolution, Reform and Change
Jong-Il You

Chapter 9 Globalization and the Logic of International Collective Action: Re-Examining the Bretton Woods Institutions
Joseph E. Stiglitz

Chapter 10 From GATT to WTO and Beyond
S. P. Shukla

Part IV GOVERNANCE

Chapter 11 Reforming the International Financial Architecture: Consensus and Divergence
Jose Antonio Ocampo

Chapter 12 Developing Countries in Global Economic Governance and Negotiation Processes
G. K. Helleiner

Chapter 13 Processes of Change in International Organizations
Devesh Kapur

Chapter 14 The Existing System and the Missing Institutions
Deepak Nayyar

POLICY BRIEFS

PB1 Forests in Global Warning, by Patrick Humphreys and Matti Palo, January 1998 (available only in PDF from www.wider.unu.edu)

PB2 Social and Economic Policies to Prevent Complex Humanitarian Emergencies: Lessons from experience, by Jeni Klugman, March 1999

PB3 Access to Land and Land Policy Reforms, by Alain de Janvry and Elisabeth Sadoulet, April 2001

PB4 Inequality, Growth and Poverty in the Era of Liberalization and Globalization, by Giovanni Andrea Cornia and Julius Court, November 2001

Policy Briefs are distributed free of charge. Please address your orders and inquiries to:

UNU/WIDER Publications
Katajanokanlaituri 6 B
00160 Helsinki
Finland

Telephone (358-9) 6159911
Facsimile (358-9) 61599333
E-mail: publications@wider.unu.edu