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Reinventing Globalization: Fair is Feasible

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REINVENTING GLOBALIZATION:
FAIR IS FEASIBLE

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The financial crisis, which surfaced in the United States in September 2008, spread through contagion almost like a forest fire across the world. Its transmission to the real sector of economies was also rapid as it led to a sharp contraction of output and employment. The downturn moved quickly into a recession. And this recession could persist for some time, even if it does not turn into a depression. Cycles are embedded in the nature of capitalism. Yet, it is clear that this is the deepest crisis in capitalism since the Great Depression more than 75 years ago. There is, however, an important difference between then and now. Developing countries were not so connected with the world economy at that time. The focus then, it is no surprise, was on industrialized countries. Developing countries are much more significant and integrated into the world economy now. Hence, this time around, the global crisis has profound implications and serious consequences for development.

The origin, the spread and the persistence of the crisis are attributable to markets and globalization. It is an important conjuncture that could be the beginning of the end of market fundamentalism, just as it could be beginning of the decline of globalization as a virtual ideology. The belief in the magic of the market has been somewhat battered in industrial societies. It is not quite the same in the developing world. Of course, doubts and questions have surfaced. But the conceptual language of globalization dominates the discourse. Even so, the crisis provides an opportunity to rethink development. In doing so, it is essential reconsider the balance between the national and the global, the State and the market, public action and private decisions, or the real and financial sector of economies. This wider context sets the stage for the paper.

The essay starts from the premise that the uneven development brought about by globalization was not sustainable in terms of economics and not feasible in terms of politics. The global crisis only highlights the ever present risks associated with a deep integration of national economies into the world economy. More important, perhaps, it provides strong reason to question the belief that markets and globalization are the

road to development in the twenty-first century. The paper considers what needs to be done in the national and international contexts to reinvent globalization so that development outcomes improve the well-being of ordinary people. It argues that, in times to come, globalization is feasible if it is fair and creates opportunities for all.

Section I outlines the essential contours of the world of globalization which is constituted by unequal partners and asymmetrical rules. Section II analyzes the uneven development and the unequal outcomes in the world economy associated with globalization making a distinction between winners and losers. Section III considers a possible analytical construct to focus on what might make a reinvented globalization feasible. Section IV sets out the correctives that would need to be introduced at the national level which would make for a more egalitarian development. Section V explores how the rules of the game for the world economy need to be reshaped, through a different multilateralism, to create more space for the pursuit of national development objectives. Section VI discusses the logic and the possibilities of international collective action, with particular reference to the opportunities for cooperation among developing countries.

I. THE GAME, THE PLAYERS AND THE RULES

Globalization is about 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 in the world economy. Economic openness is not simply confined to trade flows, investment flows and financial flows. It also extends to flows of services, technology, information and ideas across national boundaries. But the cross-border movement of people is closely regulated and highly restricted. Economic interdependence is asymmetrical. There is a high degree of interdependence among countries in the industrialized world. There is considerable dependence of developing countries on the industrialized countries. There is much less interdependence among countries in the developing world. Economic integration straddles national boundaries as liberalization has diluted the significance of borders in economic transactions. It is, in part, an integration of markets (for goods, services, technology, financial assets and

even money) on the demand side, and, in part, an integration of production (horizontal and vertical) on the supply side.

The process of globalization is driven by market forces and technical progress, while international trade, international investment and international finance constitute its cutting edge. There are three sets of players in this game: national governments, international firms and multilateral institutions.

National governments remain the main political players but are no longer the main economic players. The autonomy of the nation state in the economic sphere has been eroded by globalization everywhere, not only in the developing world but also in the industrialized world. Of course, the nation state in the latter has far more space than the nation state in the former. In spite of the profound changes unleashed by globalization, however, it would be a mistake to underestimate the power of the nation state for it remains a crucial player in the political sphere. Even now, only nation states have the authority to set the rules of the game. Nation states in the industrialized world, as home countries, provide international capital with the means to set rules for the game of globalization. Nation states in the developing world, as host countries, provide their people with the means of creating space for development in a world of globalization. As players, however, nation states are most unequal, because political power is a function of economic strength and geographical size.

Globalization has placed a new set of players centre-stage: transnational corporations which dominate production, investment, trade and technology in the world economy, and international banks or financial intermediaries which control the world of finance. It would seem that the present conjuncture represents the final frontier in the global reach of capitalism to organize production, trade, investment, finance and technology on a world scale without any fetters except, of course, for tight controls on labour mobility. For this purpose, transnational corporations and international finance wish to set rules of the game which would enable them to manage the risks associated with globalization. In this task, nation states of the industrialized world provide the much needed political clout. The multilateral framework of the WTO, the IMF and the World Bank is, perhaps, the most important medium. And nation states in the

developing world simply fall into line. The power asymmetries are such that most of them have little choice.

The transformation of the GATT into the WTO represented a paradigm shift. The GATT system was simply about negotiating market access at the border for trade in goods. In sharp contrast, the WTO seeks to impose binding multilateral disciplines, with a common enforcement mechanism, on domestic economic policies. The regimes for trade-related investment measures, trade-related intellectual property rights and trade in services, lodged in the WTO, coincide closely with the interests of transnational corporations which are capital-exporters, technology-leaders and service-providers in the world economy. Similarly, in the guise of conditionality, IMF programmes of stabilization and World Bank programmes of structural adjustment in developing countries and transition economies, in effect, attempt to harmonize policies and institutions across countries, which is consonance with the needs of globalization. It would seem that, wherever cross-border transactions are dominated by international firms, governance is being moved as much as possible from national policies and rules to international institutions and rules. This is a consequence of the strong influence exercised by transnational corporations and international finance in their home countries. Their object is to reduce transaction costs and their bottom line is the balance sheet. And these rules are essentially about what governments can or cannot do. But there are no rules, even contemplated let alone negotiated, on what transnational corporations and international finance can or cannot do.

In a world of unequal partners, it is not surprising that the rules of the game are asymmetrical in terms of construct and inequitable in terms of outcome. The strong have the power to make the rules and the authority to implement the rules. In contrast, the weak can neither set nor invoke the rules. The problem, however, takes different forms.[1]

First, there are different rules in different spheres. The rules of the game for the international trading system, set in the WTO, provide the most obvious example. There are striking asymmetries. National boundaries should not matter for trade

[1] For a more complete discussion on rules of the game, see Nayyar (2002) and Nayyar (2003).

flows and capital flows but should be clearly demarcated for technology flows and labour flows. It follows that developing countries would provide access to their markets without a corresponding access to technology and would accept capital mobility without a corresponding provision for labour mobility. This implies more openness in some spheres but less openness in other spheres. The contrast between the free movement of capital and the unfree movement of labour across national boundaries lies at the heart of the inequality in the rules of the game.

Second, there are rules for some but not for others. In the WTO, for instance, major trading countries often resort to a unilateral exercise of power, ignoring the rules, because small countries do not have the economic strength even if they have the legal right to retaliate. The conditions imposed by the IMF and the World Bank, however, provide the more familiar example. There are no rules for surplus countries, or even deficit countries, in the industrialized world, which do not borrow from the multilateral financial institutions. But the IMF and the World Bank set rules for borrowers in the developing world and in the transition economies. The conditionality is meant in principle to ensure repayment, but in practice it imposes conditions that reduce restrictions on cross-border economic transactions and dismantle regulations on domestic economic activities through policies that are similar if not uniform across countries.

Third, the agenda for new rules is partisan, but the unsaid is just as important as the said. The attempt to create a multilateral agreement on investment in the WTO, which seeks free access and national treatment for foreign investors, with provisions to enforce commitments and obligations to foreign investors, provides the most obvious example. Surely, these rights of foreign investors must be matched by some obligations. Thus, a discipline on restrictive business practices of transnational corporations, the importance of conformity with anti-trust laws in home countries, or a level playing field for domestic firms in host countries, should also be in the picture.

The process of globalization is already reducing the autonomy of developing countries in the formulation of economic policies in their pursuit of development. These unfair rules also encroach on the policy space so essential for national development.

The existing (and prospective) rules of the WTO regime allow few exceptions and provide little flexibility to countries that are latecomers to industrialization. In comparison, there was more room for manoeuvre in the erstwhile GATT, *inter alia*, because of special and differential treatment for developing countries. The new regime is much stricter in terms of the law and the implementation. The rules on trade in the new regime make the selective protection or strategic promotion of domestic firms *vis-à-vis* foreign competition much more difficult. The tight system for the protection of intellectual property rights could pre-empt or stifle the development of domestic technological capabilities. The possible multilateral agreement on investment, should it materialize, would almost certainly reduce the possibilities of strategic bargaining with transnational firms. Similarly, commitments on structural reform, an integral part of stabilization and adjustment programmes with the IMF and the World Bank, inevitably prescribe industrial deregulation, privatization, trade liberalization and financial deregulation. Taken together, such rules and conditions are bound to curb the use of industrial policy, technology policy, trade policy and financial policy as strategic forms of intervention to foster industrialization.[2]

At the same time, the consequences of integration into international capital markets also reduce degrees of freedom. Exchange rates can no longer be used as a strategic device to provide an entry into world markets for manufactured goods, just as the interest rates can no longer be used as a strategic instrument for guiding the allocation of scarce investible resources in a market economy. What is more, countries that are integrated into the international financial system are constrained in using an autonomous management of demand to maintain levels of output and employment. Expansionary fiscal and monetary policies – large government deficits to stimulate aggregate demand or low interest rates to encourage domestic investment – can no longer be used because of an overwhelming fear that such measures could lead to speculative capital flight and a run on the national currency.[3]

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[2] It must be recognized that such state intervention was crucial for development in the success stories among late industrializers during the second half of the twentieth century. For a convincing exposition of this view, see Amsden (1989), Wade (1990) and Chang (1996).

[3] For an analysis of this issue, see Nayyar (2002a).

In sum, the existing global rules encroach upon essential policy space. And the problem is compounded by the rapid, sometimes premature, integration into international financial markets. Therefore, latecomers to industrialization in the contemporary world of globalization find it difficult to emulate countries that preceded them, in East Asia and elsewhere, because their policy space is so constrained. Indeed, the industrialized countries had much more freedom and space in policy formulation at comparable stages of their industrialization.[4]

II. UNEVEN DEVELOPMENT AND UNEQUAL OUTCOMES

During the second half of the twentieth century, economic growth in the world economy was rapid, particularly when compared with the preceding fifty years, but this growth was unevenly distributed over time and across space. In view of the fact that growth rates witnessed a discernible change in the trend *circa* 1980, it is appropriate to compare the period from 1951 to 1980 with the period from 1981 to 2005.[5] Growth in GDP and GDP per capita during 1981-2005 was much slower than it was during 1951-1980. This was so for the world economy, for industrialized countries and for developing countries.[6] Growth in GDP was in the range 4-5 per cent per annum during 1951-1980 and in the range of 2-3 per cent per annum during 1981-2005 almost everywhere, except Asia where it was 6 per cent and 4 per cent per annum respectively. Growth in GDP per capita slowed down considerably even in the industrialized countries, from 3.5 per cent per annum during 1951-1980 to 2 per cent per annum during 1981-2005, but the slowdown was more pronounced for developing countries, from 2.2 per cent per annum to 0.8 per cent per annum. In Latin America and Africa, during 1981-2005, growth in GDP per capita was less than 0.5 per cent per annum, while Asia fared better at more than 1.5 per cent per annum.[7] In sum,

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[4] See Bairoch (1993) and Chang (2002). See also Maddison (1995).

[5] Such periodization serves an important analytical purpose. It may seem arbitrary but it is not. For evidence on growth rates in the world economy during the second half of the twentieth century, which establishes that 1980 was a turning point, see Nayyar (2008). See also, United Nations (2006).

[6] The evidence on growth rates in GDP and GDP per capita cited in this paragraph draws upon earlier work of the author (Nayyar, 2008).

[7] It is worth noting that China and India were the exceptions. In both countries, growth rates in the second period were much higher than the perfectly respectable growth rates in the first period.

growth did not accelerate. It slowed down. This growth was more volatile as compared with the past, particularly in the developing world.[8]

Available evidence also suggests a divergence, rather than convergence, in levels of income between countries and between people. Economic inequalities increased in the late twentieth century as the income gap between rich and poor countries, between the rich and the poor in the world's population, as also between rich and poor people within countries, widened.[9]

The incidence of poverty increased in most countries of Latin America, the Carribean and Sub-Saharan Africa during the 1980s and the 1990s. Much of Eastern Europe and Central Asia experienced a sharp rise in poverty during the 1990s. However, East Asia, South-East Asia and South Asia experienced a steady decline in the incidence of poverty during this period. But most of this improvement is accounted for by changes in just two countries, with large populations, China and India.[10]

The employment situation during the last quarter of twentieth century provides a sharp contrast with the preceding quarter century, during which full employment was almost the norm in industrialized countries. Unemployment in the industrialized countries increased substantially beginning in the early 1970s and remained at high levels thereafter. In the developing countries, employment creation in the organized sector continued to lag behind the growth in the labour force, so that an increasing proportion of workers were dependent upon low productivity and casual employment in the informal sector. The employment situation is much worse, everywhere, as the financial crisis and economic downturn in 2008 led to a sharp contraction in output which has meant much higher levels and rates of unemployment not only in the industrialized countries but also in the developing world.

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[8] For evidence on the volatility of growth in the world economy during the period 1975-2000, see World Bank, *World Development Indicators 2003*. For evidence on the volatility of growth in developing countries during the period 1980-2000, as compared with the period 1960-1980, see UNCTAD, *Trade and Development Report 2003,* p.59.

[9] It would mean too much of a digression to enter into a discussion of this proposition here. The argument is developed, with supporting evidence, in Nayyar (2006). See also, Cornia and Kiiski (1999), Bourguignon and Morrison(2002), Atkinson (2003), Milanovic(2005) and United Nations(2006).

[10] For supporting evidence, see World Bank, *World Development Report* and *Global Economic Prospect*s, several issues.

It would seem that, in some important respects, the world economy fared better in the golden age of capitalism than it has in the age of globalization. It is obviously not possible to attribute cause-and-effect simply to the coincidence in time. But it is possible to think of mechanisms through which globalization may have accentuated inequalities. Trade liberalization has led to a growing wage inequality between skilled and unskilled workers not only in industrialized countries but also in developing countries.[11] As a consequence of privatization and deregulation, capital has gained at the expense of labour, almost everywhere, for profit shares have risen while wage shares have fallen.[12] Structural reforms, which have cut tax rates and brought flexibility to labour markets, have reinforced this trend. The mobility of capital combined with the immobility of labour has changed the nature of the employment relationship and has reduced the bargaining power of trade unions. The object of managing inflation has been transformed into a near-obsession by the sensitivity of international financial markets, so that governments have been forced to adopt deflationary macroeconomic policies which have squeezed both growth and employment. The excess supply of labour has repressed real wages. Financial liberalization, which has meant a rapid expansion of public as well as private debt, has been associated with the emergence of a new rentier class. And the inevitable concentration in the ownership of financial assets has probably contributed to a worsening of income distribution.[13] Global competition has driven large international firms to consolidate market power through mergers and acquisitions which has made market structures more oligopolistic than competitive.

Globalization has, indeed, created opportunities for some people and some countries that were not even dreamed of three decades ago. But it has also introduced new risks, if not threats, for many others. It has been associated with a deepening of poverty and an accentuation of inequalities. The distribution of benefits and costs is unequal. There are some winners: more in the industrialized world than in the developing

[11] For evidence in support of this proposition, see UNCTAD (1997). In addition, see Wood (1994). Stewart (2003) also suggests that trade liberalization, (associated with globalization) provides an explanation for rising inequality and cites supporting evidence.

[12] Some evidence on the increase in profit shares in industrialized countries and the decrease in wage shares in developing countries is reported in UNCTAD (1997). Stewart (2003) develops a similar argument that globalization may have led to an increase in inequality through an increase in returns to capital as compared with labour.

[13] This argument is developed in UNCTAD (1997).

world. There are many losers: numerous both in the industrialized world and in the developing world. It is, perhaps, necessary to identify, in broad categories, the winners and the losers.[14]

If we think of people, asset-owners, profit-earners, rentiers, the educated, the mobile and those with professional, managerial or technical skills are the winners, whereas asset-less, wage-earners, debtors, the uneducated, the immobile and the semi-skilled or the unskilled are the losers. If we think of firms, large, international, global, risk-takers and technology-leaders are the winners, whereas small, domestic, local, risk-averse and technology-followers are the losers. If we think of economies, capital-exporters, technology-exporters, net lenders, those with a strong physical and human infrastructure, and those endowed with structural flexibilities are the winners, whereas capital-importers, technology-importers, net borrowers, those with a weak physical and human infrastructure, and those characterized by structural rigidities are the losers. It needs to be said that this classification is suggestive rather than definitive, for it paints a broad-brush picture of a more nuanced situation. But it does convey the simultaneous, yet asymmetrical, inclusion and exclusion that characterizes the process of globalization. It is not surprising, then, that the spread of globalization is uneven and limited both among people and across countries.

In retrospect, it is apparent that globalization has been associated with simultaneous, yet asymmetrical, consequences for countries and for people. There is an inclusion for some and an exclusion, or marginalization, for many. There is affluence for some and poverty for many. There are some winners and many losers. Joan Robinson once said: "There is only one thing that is worse than being exploited by capitalists. And that is not being exploited by capitalists." Much the same can be said about markets and globalization which may not ensure prosperity for everyone but may, in fact, exclude a significant proportion of people.

It would seem that globalization has created two worlds that co-exist in space even if they are far apart in well-being. For some, in a world more inter-connected than ever before, globalization has opened door to many benefits. Open economies and open

[14] For a more detailed discussion, see Nayyar (2003).

societies are conducive to innovation, entrepreneurship and wealth creation. For many, the fundamental problems of poverty, unemployment and inequality persist. Of course, these problems existed even earlier. But globalization may have accentuated exclusion and deprivation, for it has dislocated traditional livelihoods and local communities. Everybody sees the world through the optic of their lives. Therefore, perceptions about globalization depend on who you are, what you do and where you live. Some focus on the benefits and the opportunities. Others focus on the costs and the dangers. Both are right in terms of what they see. But both are wrong in terms of what they do not see.

On balance, it is clear that there is exclusion of countries and of people.[15] Too many people in poor countries, particularly in rural areas or in the informal sector, are marginalized if not excluded. Too few share in the benefits. Too many have no voice in its design or influence on its course. There is a growing polarization between the winners and the losers. Such uneven development is no surprise in a world of unequal partners and asymmetrical rules. And, for some time now, critics have argued that these mounting imbalances in the world are ethically unacceptable and politically unsustainable.[16] But this was simply not recognized by ideologues with a strong belief that markets and globalization are the road to development and prosperity.[17] The economic crisis that surfaced in late 2008 has led to some recognition of the reality that such unequal outcomes in development are not sustainable. It has also shaken the belief system of those who thought of globalization as a magic *mantra*, as market fundamentalism has taken a beating, although doubts have surfaced far more in industrialized countries than in developing countries. Even so, the crisis provides an opportunity for introducing the much needed correctives.

[15] For a detailed discussion, as also evidence, see Nayyar (2003) and Nayyar (2006).
[16] For a critical perspective on the implications of globalization for development, see Stiglitz (2002), Nayyar (2003) and Kaplinsky (2005). See also, Soros (1998) and Baker, Epstein and Pollin (1998). This particular proposition is set out, as also explained, in the Report of the World Commission on the Social Dimension of Globalization (2004).
[17] See, for example, Sachs and Warner (1995), Bhagwati (2004) and Wolf (2004).

III. POSSIBLE ANALYTICAL CONSTRUCT

It is clear that *outcomes* of globalization, which are so unequal between countries and among people, are neither desirable in the sphere of economics nor sustainable in the realm of politics. But that is not all. It has been suggested that, in terms of international economic integration, beyond a point, the *process* of globalization is neither feasible nor sustainable in the wider context of a world with nation states and democratic politics.[18] This proposition is based on a simple analytical construct, which is the standard trilemma from open economy macroeconomics.

The original trilemma argues that it is not possible for countries to maintain, simultaneously, independent monetary policies, fixed exchange rates and open capital accounts. This open economy trilemma is sometimes described as the 'impossible trinity' because it is possible to maintain only two of the three. If an economy chooses capital mobility and fixed exchange rates, it must give up autonomy in monetary policy. If an economy wants fixed exchange rates and autonomy in monetary policy, it must do without capital mobility. If an economy wishes to have autonomy in monetary policy with capital mobility, it cannot have fixed exchange rates. These possible alternatives are, in fact, observable in the world economy at different points in time. From the late nineteenth century until the Great Depression, the Gold Standard combined fixed exchange rates with capital mobility but countries sacrificed monetary policy autonomy. From the mid 1940s until the early 1970s, the gold exchange standard created at Bretton Woods combined fixed exchange rates with monetary policy autonomy but (more or less) ruled out capital mobility. In the period since the mid 1970s until now, the present era of globalization, most countries sought to combine monetary policy autonomy with capital mobility abandoning fixed exchange rates for a regime of floating exchange rates.

The derived construct is described as the political trilemma of the world economy.[19] The three nodes of this derivative are globalization, the nation state and democratic politics. In this characterization, globalization describes a substantial integration of national economies into the world economy, the nation state refers to sovereign

[18] This hypothesis is developed, at some length, by Rodrik (2000). See also, Rodrik (2002).
[19] For a detailed exposition and discussion of this trilemma, see Rodrik (2000 and 2002).

jurisdiction in terms of laws and institutions, while democratic politics is about electoral democracy, political freedoms and political mobilization. As in the original trilemma, it is possible to sustain only two of the three. If a country wants to stay with the nation state and democratic politics, it cannot sustain deep international economic integration. If a country wants to combine globalization with the nation state, it needs to sacrifice democratic politics. If a country wishes to have democratic politics in a world of globalization, it would have to do without the nation state.

The underlying reasons are not obvious. The essence of the Rodrik hypothesis is that deeply integrated national economies would conflict with the regulatory and jurisdictional discontinuities created by heterogeneous national laws and institutions, while harmonized laws and institutions that eliminate the significance of national borders conflict with the foundations of democratic politics where governments are accountable to their people. The basic idea could be illustrated with a caricature description of reality in the past. From the late 1940s to the mid 1970s, the golden age of capitalism, the multilateral economic system made it possible for countries to stay with the nation state and democratic politics by limiting the degree of international economic integration. From the late 1970s until now, the age of globalization, the 'Golden Straitjacket' which harmonized, policies, institutions and laws across countries, made it possible for countries to combine globalization with the nation state politics but democratic politics was progressively sacrificed.[20] It is possible to contemplate a future, however unlikely, where it may be possible for countries to combine democratic politics with globalization, by dispensing with the nation state and opting for a world government or global federalism.

There are two basic problems with the trilemma a concept. For one, it depicts a caricature world with strong structural rigidities. For another, it creates a binary world with either-or choices. Hence, if there are three possibilities, it is possible to attain

[20] Golden Straitjacket is a phrase used by Friedman (1999) to describe how Governments everywhere compete with each other to harmonize policies and earn the confidence of international firms and international markets. The following quotation (p.87) is so explicit that the phrase needs no further explanation: "As your country puts on the Golden Straitjacket, two things tend to happen: your economy grows and your politics shrinks....(it) narrows the political and economic policy choices of those in power....(so that) it is increasingly difficult to find any real differences between ruling and opposition parties....political choices get reduced to slight nuances...to Pepsi and Coke...but never to any major deviation from the core golden rules"

only two of the three at a time. It is, at best, an analytical abstraction that highlights conflicts or trade offs between three stipulated objectives. And it might be appropriate in the limited context of open economy macroeconomics as an analytical construct that highlights conflicts between policy objectives, or instruments, even if it does not quite capture reality. But there is a problem of transitivity in moving from economics in the original trilemma to politics in the derived trilemma. Each of the three nodes, international economic integration, the nation state, or democratic politics, may represent a range rather than a single unique point, which means that there may be choices within each. What is more, trade offs may be a continuum rather than binary choices, which means that it may be possible to have more of two and less of the third. In other words, there could be more choices within and between the three nodes whereas the trilemma only allows choosing two from three. The fundamental problem with such an analytical construct is that it suggests a false precision which is deceptive if not misleading. Of course, in reality, there are conflicts between objectives or desired states. And, wherever there are conflicts, there are bound to be trade offs. Hence, there are choices to be made. But these should not be reduced to: "pick two, any two".

The ideologues, who think of globalization as prescriptive, must recognize that there is something to learn from a historical perspective. Globalization in the late twentieth century, as much as the earlier era of globalization during the late nineteenth century, represents neither the end of history nor the end of geography. It is not the end of history, now as it was not then, because markets and globalization are not forever. It may have been a world war then and it is the economic crisis now that has created doubts about the wisdom and necessity of deepening economic integration in the world economy. And there was life after globalization then as there will be now. It is not the end of geography, because nation states cannot exist in a vacuum and most must strive to improve the economic conditions of their people to whom governments are accountable. There is, then, a strategic economic an political role for the state which must be recognized and performed.

It is clear that the nation state is a reality that has not withered away. There has been an erosion in its economic space but not in its political space. This reality has been brought home by the global economic crisis. At the same time, democratic politics is

an aspiration that is on the rise everywhere. The spread of market economy has been associated with the spread of political democracy. There are fewer authoritarian regimes and more democratic regimes. And, even authoritarian regimes are more accountable to their people as compared with the past, in part because of the changed world in communications technology associated with globalization. In sum, the nation state is a reality embedded in history that has emerged stronger from the global economic crisis. Democratic politics, which has gathered both momentum and strength in the recent past, is almost a prior. In contrast, the degree of international economic integration is a matter of strategic choice in terms of speed, sequence and engagement. It depends on choices made by the nation state where, ultimately, governments can decide only in accordance with preferences of people. And if it produces unequal outcomes, globalization is unsustainable in terms of both economics and politics.

The global economic crisis carries a clear message. Deeper integration of national economies into the world economy does not promise salvation or prosperity for all because it excludes a large number of countries and a significant proportion of people. What is more, it has accentuated the vulnerability of the excluded. It has also put employment and livelihoods at risk everywhere. The time has come to question the wisdom and necessity of the quest for an ever increasing and deepening international economic integration. It was an integral part of the virtual ideology of globalization, which is now open to serious question. Indeed, it is worth contemplating a *standstill* on new initiatives for deeper economic integration, just as it is also necessary to reconsider and *roll-back* some of the existing arrangements that constrain policy space for countries which are latecomers to development. [21] The recent crisis in the world economy provides an opportunity to reinvent globalization so that it is conducive to outcomes in development which improve the well-being of people. It

[21] It is worth noting that the phrases *standstill* and *roll-back* were first used during the 1980s with reference to protectionism. The argument outlined above is most applicable to the institutional framework for the multilateral trading system. It would be desirable to hasten slowly in creating new disciplines for deeper economic integration in the WTO. There is a clear need for a *standstill* on new issues sought to be placed on the agenda for multilateral trade negotiations. Similarly, there is need for a *roll-back* on the TRIPS agreement in the WTO. Of course, these are just examples. There are several other domains, such as capital account liberalization, where a *standstill* is imperative and some *roll-back* is desirable.

must provide space for the pursuit of national development objectives. It must be inclusive of countries and people, so that it provides economic and social opportunities for all. In the ultimate analysis, globalization is feasible if it is fair. This needs correctives at the national level and in the international context.

IV. NATIONAL CONTEXT: INTRODUCING CORRECTIVES

The discourse on theory and policy in development has become narrower with the passage of time. Therefore, it is necessary to redefine objectives by shifting the focus to people, to redesign strategies by introducing correctives, and to rethink development by incorporating different perspectives, that would make for more egalitarian economic development and a more broad-based social development. A systematic, let alone complete, analysis of such alternatives would mean too much of a digression.[22] Even so, it is necessary to reiterate the objectives and to outline what needs to be done.

In the national context, the near obsession with economic growth, economic efficiency and price stability as objectives is misplaced and must change. These are simply means. It is the well-being of people that is an end. Thus, full employment and poverty eradication should be the basic objectives. And it is essential to strike a balance: economic growth with social progress, efficiency with equity, stability with growth, expansion with inclusion, growth with development, productivity increase with employment creation and so on. These are not either-or choices. There are strong interconnections and complementarities. The fundamental objective, then, must be to ensure decent living conditions for people, ordinary people. In the pursuit of this objective, the importance of public action cannot be stressed enough. Therefore, it is imperative that the ends are not lost sight of in the concern for means. And there are two forgotten essentials that should form an integral part of any attempt at redesigning strategies of development. First, it is not quite recognized that economic growth is necessary but not sufficient to bring about a reduction in poverty. It cannot suffice to say that the outcomes of economic policies should be moderated by social policies. Second, it is often forgotten that the well-being of humankind is the essence of

[22] For a more detailed discussion, see Nayyar (2007).

development. Thus, distributional outcomes are important. So are employment and livelihoods.

At the micro level, in redesigning strategies, it is necessary to introduce correctives and interventions that prevent or minimize the exclusion of people from development. At the meso level, in rethinking development, it is important to recognize the importance of initial conditions and the significance of institutions. At the macro level, it is essential to create space for the pursuit of national objectives, by reconsidering the balance between domestic and external factors, the relevance of politics in economics and the role of good governance, in the process of development. It must be stressed that the developmental role of the state is critical across the entire spectrum of what needs to be done. For this purpose, it is imperative to restore the moral authority of the state which was eroded by the virtual ideology of market fundamentalism associated with globalization in a prescriptive mode. The reason is simple enough. If governments do badly, it is not possible to dispense with them or replace them with markets. Governments must be made to perform better.

Markets and globalization have a logic of their own, which leads to inclusion for some and exclusion for others, or affluence for a few and poverty for many. Given this reality, it is necessary to introduce correctives that prevent exclusion and interventions that limit the adverse effects of exclusion.[23] The object of correctives should be to foster inclusion. The inclusion of poor people requires the spread of education and an increase in social consumption. It also requires a substantial investment in physical infrastructure, particularly in rural areas and backward regions. The integration of people who are excluded by markets, into economy and society, requires one fundamental corrective. Such people must acquire capabilities, through education or training, which would give them access to markets as producers or sellers which, in turn would yield an income so as to provide them with access to markets as consumers or buyers. The object of interventions should be to curb exclusion. The extent of exclusion can be limited by providing public goods and services to regions or groups that are vulnerable, marginalized or excluded. For the people who remain excluded despite such interventions, it is essential to widen and

[23] For a detailed discussion, see Nayyar (2003).

strengthen safety nets such a anti-poverty programmes or social security. Even at the micro level, the role of governments is vital in every sphere.

It is obvious that initial conditions are important determinants of development. It should also be recognized that initial conditions can and should be changed to foster development. This is an unambiguous lesson that emerges from economic history.[24] In countries that are latecomers to industrialization, state intervention creates conditions for the development of industrial capitalism through the spread of education in society, the creation of a physical infrastructure and the introduction of institutional change. This role has always been recognized. The building of managerial capabilities in individuals and technological capabilities in firms is also an important, even if less recognized, dimension of initial conditions, for such capabilities determine technical efficiency in the short run and competitiveness in the long run.[25] This has been recognized for some time. Globalization, however, led to a widespread disillusionment with the economic role of the state and a strong belief in the magic of the market. Hence, orthodoxy neglects the importance of initial conditions. There is an irony in this situation. In the context of globalization, such a role for the state is more necessary than ever before. Indeed, creating the initial conditions is essential for maximizing the benefits and minimizing the costs of integration with the world economy.

The debate on development is, in large part, about policies. The time has come to move beyond policies to institutions.[26] Orthodox economics has sought to harmonize the role as also the form of institutions across the world irrespective of space and time. This is a serious mistake, since one-size-does-not-fit all. There are specificities in space. Institutions are local and cannot be transplanted out of context. There are specificities in time. Institutions need time to evolve and cannot be created by a magic wand. The blueprints for economic liberalization over the past 25 years have simply not recognized this reality. Yet, the role of the state is crucial in almost every dimension of institutions. In an economy, the state seeks to govern the market through rules or laws. It does so by setting rules of the game for players in the

[24] For a fascinating historical analysis of the development experience of latecomers to industrialization, see Amsden (2001) and Chang (2002).
[25] See Lall (1990).
[26] See for example, North (1990) and Chang (2002a).

market. In particular, it creates frameworks for regulating markets. But it also creates institutions, whether organizations or entities, to monitor the functioning of markets. The development of such institutions, which cannot always develop on their own, may need some pro-active role for the state, as catalyst if not leader. Of course, there are institutions that may develop through markets, as in standards or for safety, but these depend on social norms. Much remains to be done so as to improve understanding of institutions and of institutional change in the process of development, which could be the difference between success and failure at development.[27] Such understanding needs not only theory but also history. However, the theory must be non-ideological just as the history must be non-selective.

Globalization came to be associated with a belief system that national political objectives, domestic economic concerns or even national boundaries should not act as constraints. In such a world, domestic economic concerns mesh with, or are subsumed in, the maximization of international economic welfare and national political objectives melt away in the bargain. The time has come to rethink the relative importance of the external and the internal in the process of development, in terms of markets and in terms of resources. It needs to be recognized that the domestic market is critical in the process of development and that external markets are at best complements but cannot be substitutes for the domestic market even in smaller countries. Of course, the validity of this argument depends in part on the size of a country. Even so, domestic markets are, at one level, constitutive of development because it means that ordinary people have purchasing power and are, at another level, instrumental in the process of development because they can drive processes of growth. Similarly, it is important to rely more on domestic resources for investment and think of external resources as complements rather than substitutes.

In every society, economy and polity are closely inter-twined. It is the interaction of economics and politics which shapes outcome for people. Therefore, it is essential to explore the interplay between economics and politics in the process of development.[28] There is, then, need for a political economy that extends beyond econometric analysis

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[27] Chang (2007) makes an important contribution to our understanding of institutional change and economic development.
[28] This is stressed by North (2001) in a short essay on understanding development.

at a micro level, even if it is the fashion of our times. This is easier said than done. But a beginning could be made by exploring the relationship between markets and democracy, democracy and development, and development and empowerment.

The essence of the tension between the economics of markets and politics of democracy must be recognized. In a market economy, people vote with their money in the market place. But a political democracy works on the basis of one-person-one-vote. The distribution of votes, unlike the distribution of incomes or assets, is equal. One adult has one vote in politics even though a rich man has more votes than a poor man, in terms of purchasing power, in the market. This tension may be compounded by a related asymmetry between economy and polity. The people who are excluded by the economics of markets are included by the politics of democracy. The rich dominate a market economy in terms of purchasing power. But the poor have a strong voice in a political democracy in terms of votes. Hence, exclusion and inclusion are asymmetrical in economics and politics. It is only the state that can mediate in the process. The reason is important even if it is not obvious. Governments are accountable to their people whereas markets are not. In a democracy, however, governments are elected by the people. But even where they are not, the state needs legitimation from the people most of whom are not rich or are poor.[29]

The relationship between democracy and development is also complex. But it is important to reject the view that latecomers to development cannot afford the luxury of democracy. Indeed, thinking ahead, it is clear that democracy is going to be conducive to the process of development. The reason is straightforward. The essential attributes of democracy, transparency and accountability, provide the means for combining sensible economics with feasible politics.[30] The economic priorities of the people will be reflected more and more in the political agenda of parties if there is a transparency in the system. The agenda of political parties will be reflected more and more in the reality of economic development if there is accountability in the system.

[29] The discussion in this paragraph draws upon Nayyar (2003a).
[30] For a more detailed discussion, see Bhaduri and Nayyar (1996).

The problem is that democracy, while conducive and necessary, is not sufficient to actually produce development. We know that from experience. Development may or may not be provided from above by benevolent governments. It must be claimed from below by people as citizens from governments that are accountable. The empowerment of people, then, is an integral part of any process of change that leads to development. A political democracy, even if it is slow, provides a sure path for two reasons. It increases political consciousness among voters to judge political parties for their performance. At the same time, it increases participation in the political process when it leads to mobilization on some issues. This highlights the significance of Amartya Sen's conception of development as freedom.[31] Expanding freedoms for people at large constitute development. But the same expanding freedoms, which empower people, are instruments that drive the process of change in development.

Governance is critical in the process of development. The real issue is not about more or less government. It is about the quality of government performance. This has two dimensions.

The first dimension is more obvious. It is about redefining the economic role of the state in a changed national and international context. In the earlier stages of development, the primary role is to create initial conditions. In the later stages of development, the role is neither that of a promoter nor that of a catalyst. It is somewhat different and spans a range: functional intervention to correct for market failure, institutional intervention to govern the market, or the strategic intervention to guide the market.[32] In this era of markets and globalization, surprisingly enough, the role of the state is more critical than ever before and extends beyond correcting for market failures or regulating domestic markets. It is about creating the initial conditions to capture the benefits from globalization, about managing the process of integration into the world economy in terms of pace and sequence, about providing social protection and safeguarding the vulnerable in the process of change and about

[31] For a lucid analysis, see Sen (1999).
[32] Cf. Nayyar (1997) See also, Bhaduri and Nayyar (1996). For a discussion on the economic role of the State with reference to industrial strategy, see Shapiro and Taylor (1990).

ensuring that economic growth creates employment and livelihoods for people.[33] In sum, governments need to regulate and complement markets so as to make them people-friendly.

The second dimension, good governance, is less obvious. It is, however, more concrete and less abstract. Governance is largely about rules and institutions that regulate the public realm in civil society. A democratic system seeks to provide for equal participation of the rich and the poor, or the strong and the weak, individuals as citizens in political processes. The basis for good governance is a democratic political system that ensures representative and honest governments responsive to the needs of people. This involves more than simply free and fair elections. It extends to economic, social and political institutions required for the functioning of market economy and political democracy. A vibrant civil society, empowered by freedom of association and expression which can voice diversity in views, is just as important for good governance in so far as it provides checks and balances when governments do not act as they should. In sum, good governance, where governments are accountable to citizens and people are centre-stage in the process of development, is essential for creating capabilities, providing opportunities and ensuring rights for ordinary people. Governance capabilities matter. Indeed, the quality of governance is an important determinant of success or failure at development.[34] The moral of the story is not less government but good governance.

V. INTERNATIONAL CONTEXT: REINVENTING MULTILATERALISM

The present set of institutions and rules for managing the world economy were established more than sixty years ago with the foundation of the United Nations system and the creation of the IMF, the World Bank and the GATT. Since then, the world has changed almost beyond recognition, while the institutions have changed

[33] See Report of the World Commission on the Social Dimension of Globalization (2004).
[34] A striking illustration of this proposition is provided by the wide diversity in economic performance across states in India, despite common policies, similar institutions and the economic union. It is worth highlighting the most telling example. During the period from 2004-05 to 2008-09, Bihar, among the poorest states in India for a long time, has recorded the highest rate of growth in output, at more than 11 per cent per annum, across states in India. This is attributable, in significant part, to good governance. There are several such examples that would emerge from a comparison of economic performance across countries in the developing world.

little or have adapted slowly. National economies have become ever more closely integrated through cross-border flows of trade, investment and finance, while the technological revolution in transport and communications, which has eroded the significance of barriers implicit in distance and time, has transformed reality so that economic space no longer coincides with geographical space. It is clear that the institutions that were put in place so long ago are no longer either adequate or appropriate for the world economy.[35] And we should not have to wait for a crisis of enormous proportions, similar to that which followed the Great Depression and Second World War, to rethink the institutions and rules for managing the world economy. Indeed, the financial crisis and economic downturn of 2008 provide a window of opportunity for change. Existing rules or institutions need to be changed or adapted. Missing rules or institutions need to be introduced or created. The time has come to redesign and reinvent the multilateral system such that it fosters international cooperation and is conducive to national development. In this context, it should be recognized that there might be a trade-off between policy coherence in the international context and policy space in the national context, so that it is essential to strike a balance.

It is clear that, during the first quarter of the twenty-first century, development outcomes would be shaped, at least in part, by the international context. It is also clear that unfair rules of the game in the contemporary world economy would encroach on policy space so essential for development. This situation needs to be corrected. The correctives should endeavour to make existing rules less unfair, introduce new rules where necessary and recognize that even fair rules may not suffice. But this endeavour cannot succeed without more democratic structures of governance in the world economy. In this process, interestingly enough, the role of nation states would be critical.

In reshaping unfair rules, it need hardly be said that the nature of the solution depends upon the nature of the problem. Where there are different rules in different spheres, it is necessary to make the rules symmetrical across spheres. Where there are rules for some but not for others, it is necessary to ensure that the rules are uniformly

[35] For a detailed discussion on this theme, see Nayyar (2002).

applicable to all. Where the agenda for new rules is partisan, it is imperative to redress the balance in the agenda.[36] The object should be to enlarge rather than restrict policy space.

There is a clear need for greater symmetry in the rules of multilateral trading system embodied in the WTO. If developing countries provide access to their markets, it should be matched with some corresponding access to technology. If there is almost complete freedom for capital mobility, the draconian restrictions on labour mobility should at least be reduced. The enforcement of rules is also asymmetrical. In the Bretton Woods institutions, enforcement is possible through conditionality. Such conditionality, however, is applicable only to developing countries or transition economies that borrow from the IMF or the World Bank. In the WTO, enforcement is possible through retaliation. But most developing countries do not have the economic strength, even if they have the legal right, to retaliate. The reality, then, is that the countries that are poor or weak conform to the rules, whereas countries that are rich or strong can flout the rules. There is no enforcement mechanism, yet, that can be imposed on the powerful players who circumvent the rules. And the hegemonic powers, often, simply ignore the rules. The enforcement of rules for the rich and the powerful is, therefore, essential. In addition, the agenda for the new rules needs careful scrutiny for it is shaped by the interests of industrialized countries while the needs of development are largely neglected.

But that is not all. There are some spheres where there are no rules, such as environmental sustainability, international financial markets or cross-border movements of people. Climate change is on the agenda, even if there is little progress. The time has come to introduce some rules that govern international financial markets, which would also manage systemic risk associated with international financial liberalization and coordinate national action against market failure or abuse. It is also perhaps necessary to think about a new international financial architecture not only for crisis management and crisis prevention but also for international

[36] The following discussion on the rules of the game in the world economy draws upon earlier work of the author (Nayyar 2002 and 2003).

reserves and institutional governance.[37] Similarly, it is worth contemplating a multilateral framework for consular practices and immigration laws that would govern cross-border movements of people, akin to multilateral frameworks that exist, or are sought to be created, for the governance of national laws, or rules, about the movement of goods, services, technology, investment and information across national boundaries.[38] The essential object should be to create a transparent and non-discriminatory system, based on rules rather than discretion, for people who wish to move, temporarily or permanently, across borders.

Rules that are fair are necessary but not sufficient. For a game is not simply about rules. It is also about players. And if one of the teams or one of the players does not have adequate training or preparation, it will simply be crushed by the other. In other words, the rules must be such that newcomers or latecomers to the game, for example developing countries, are provided with the time and the space to learn so that they can become competitive players rather than push-over opponents. In this context, it is important to stress that, for countries at vastly different levels of development, there should be some flexibility, instead of complete rigidity, in the application of uniform rules. Indeed, uniform rules for unequal partners can only produce unequal outcomes. Thus, we should be concerned with the desirability of the outcomes and not with the procedural uniformity of 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. It 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 across countries. And there is a clear need for positive discrimination or affirmative action in favour of poor countries, particularly but not only the least developed countries, that are latecomers to development. This principle should be incorporated in the conception and design of the new multilateralism.

[37] There is an extensive literature on this subject which has addressed the entire range of issues for some time. See, for example, Nayyar (2002b) and Eatwell and Taylor (2002). The Stiglitz Commission, constituted in the aftermath of the financial crisis, provides an analysis of what went wrong and what needs to be done (United Nations, 2009).

[38] For a discussion on the rationale for such a multilateral framework to govern cross-border movements of people, see Nayyar (2002c). The World Commission on the Social Dimension of Globalization (2004) makes a similar proposal.

The reshaping of rules is easier said than done. Much would depend upon structures of governance. The existing arrangements for global governance are characterized by a large democratic deficit.[39] In terms of representation, the existing system is less than democratic. For one thing, representation is unequal, in part because of unequal votes in multilateral institutions such as the IMF or the World Bank, and in part because of exclusion from representation in arrangements such as the P-5 or the G-8 or even the OECD. For another, representation is incomplete in so far as it is confined mostly to governments, with little that could be described as participation by civil society or corporate entities, let alone people or citizens. In terms of decision-making, the existing system is even less democratic. Where some countries have more votes than others and yet other countries have no votes, the system is obviously undemocratic. Even the principle of one-country-one-vote, however, does not ensure a democratic mode of decisions. Much also depends on how decisions are made. The right of veto in the Security Council of the UN is explicitly undemocratic. But decision-making by consensus rather than a vote, 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.

It is difficult to imagine more democratic structures of governance in a world of such disparities, economic and political, between countries. But democracy is not simply about majority rule. It is as much about the protection of rights of minorities. 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. In addition, wherever existing rules constrain autonomy or choices in the pursuit of development, there is a need for the equivalent of an escape clause. Such a provision to opt out of obligations embedded in international rules, without having to forsake rights, could provide countries that are latecomers to development with the requisite degrees of freedom in their national pursuit of development objectives. It is important to recognize that, in democratic situations, *exit* has as much significance as *voice*.

[39] The democratic deficit is analyzed, at some length, in Nayyar (2002).

VI. INTERNATIONAL COLLECTIVE ACTION: LOGIC AND POSSIBILITIES

The logic of international collective action was recognized more than six decades ago. It was an integral part of the conception of the Bretton Woods institutions that were created at the end of World War II and in the aftermath of the Great Depression. The recognition of its significance diminished with the passage of time. In fact, with the advent of markets and globalization, by 1980, it was almost forgotten. There is an irony in the situation. In the mid 1940s, our understanding of collective action, the circumstances under which public, as opposed to private, action is necessary and desirable, was somewhat underdeveloped in terms of economic theory even if it was shaped by actual experience in the Great Depression. In the late 2000s, in terms of economic theory, our understanding of collective action, is far more complete. Markets, by themselves, may not lead to efficient, or otherwise desirable, outcomes. And such market failure may occur when there are public goods (or bads), externalities, and incomplete or imperfect markets. In market economies, it is the role of governments to provide public goods such as street lights or public parks, as also to regulate public bads such as pollution or unfair competition. But there is no world government that would provide international public goods such as world peace or a sustainable environment, and regulate international public bads such as international crime or trade in drugs, arms, people or organs. Similarly, rational economic behaviour by individual (utility-maximization) and firms (profit-maximization) leads to externalities in production and in consumption so that the whole is different from the sum total of the parts. In a world economy characterized by ever increasing openness and integration, such externalities are much more prone to spillovers across national boundaries.[40] More than six decades later, actual experience of market failure that straddles geographical borders is also much greater. There are several examples: recurring financial crises, impending climate change, trafficking of people, trading in human organs, growing narcotics trade, and so on. Clearly, the logic of international collective action is far stronger. Indeed, given the interdependence in the contemporary world economy, the need for international pubic action to address problems arising from market failure is greater than ever before. Yet, the effort is much less.

[40] For a more detailed discussion on international public goods and international public bads, see Nayyar (2002).

The recent global economic crisis is at least a prompt if not a wake-up call. It has, perhaps, led to a much needed recognition of the logic of international collective action, which had been almost forgotten. Its significance is now widely accepted. But it would seem that the willingness and the ability of governments to coordinate, in terms of implementing such collective action, is not quite there. Both have to be created. The former needs economic persuasion and political acceptance. The latter needs creating institutional mechanisms and rethinking national sovereignty. The domains where this is necessary and desirable are many: global macroeconomic management, international financial markets and climate change are the obvious examples but there are several others such as international migration or international crime. But the institutional mechanisms that exist are neither adequate nor appropriate.

Consider, for example, the attempt to co-ordinate macroeconomic policies after the financial crisis in late 2008. The G-8 may provide a forum for consultation but it cannot provide an institutional framework for the coordination of macroeconomic policies. The reason is simple enough. It cannot suffice in part because it is driven largely by G-8 (if not G-1) interests and in part because it needs much wider representation. The G-20 is wider in its membership but narrower in its jurisdiction, for its concerns are limited, despite recent attempts to make it larger than life at Washington DC, London and Pittsburg. Similarly, the conference on Climate Change at Copenhagen in December 2009 floundered, in part, because of the absence of an institutional mechanism for consultations and negotiations. The outcome, such as it was, which was shaped by informal consultations between the United States on the one hand and Brazil, China, India and South Africa on the other, was not endorsed because most countries were not part of the process. The least developed countries are almost always marginalized or ignored. This time around, even the EU was left watching on the sidelines.

The democratic deficit in the international context is obvious from these examples and so are its consequences. Decisions are difficult to reach. And even if decisions are reached among a small group of countries, such decisions are neither effective nor credible. The democratic deficit must be reduced if not eliminated. Therefore, more

inclusive representation is essential. If complete representation makes the number of countries so large that international negotiations are difficult or cumbersome, it is important to create institutional mechanisms that are seen as representative in terms of voice and credible in terms of outcomes. The quest for policy coherence in the international context is, in effect, a search for institutional mechanisms that would facilitate consultation and support coordination among countries for the purpose of international collective action. Of course, this is easier said than done. But it is time for a beginning.

The much needed 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. In principle, it is possible to contemplate cooperation among nation states to create rules and norms for the market that transcend national boundaries, just as the nation state created rules and norms for the market within national boundaries. In practice, however, a recognition of the benefits of such cooperation might not be motivation enough. Cooperation among nation states is far more likely to materialize, much like stable coalitions, if and when the costs of non-cooperation cross the threshold of tolerance. In either case, the nation state is the most important player in the game. Therefore, it is not possible to imagine good governance in the world without nation states, just as it is not possible to have good governance in countries without governments.

There is another window of opportunity at this juncture in time. And that window of opportunity is about the possibilities of cooperation among developing countries, which has so far been in the world of rhetoric rather than reality, words rather than substance. But this sub-set is an integral part of the logic of international collective action. What is more, the world has changed. In 2005, developing countries accounted for 81 per cent of world population and 22 per cent of world income (almost 45 per cent of world GDP in PPP terms). But that is not all. In the same year, 2005, developing countries accounted for 34 per cent of world exports, 33 per cent of world manufactured exports, 25 per cent of world manufacturing value added and 30 per cent of the stock of inward foreign direct investment in the world economy. It would seem that developing countries are much more integrated with, and far more

significant in the world economy, than they were 25 years ago.[41] It needs to be said that much of this significance is concentrated in a few developing countries: China, Hong Kong, India, Indonesia, Korea, Malaysia, Singapore and Thailand in Asia; Argentina, Brazil and Mexico in Latin America: and South Africa in Africa. In 2005, these twelve countries accounted for 60 per cent of the population and 68 per cent of the income in the developing world. These twelve countries also dominated the engagement of developing countries with the world economy in international trade, international investment and international finance.[42] Even so, it is plausible to argue, though impossible to prove, that this changed situation represents the beginnings of a shift in the balance of economic and political power in the world.[43] This, in turn, opens up two possibilities.

First, in the international context, where the distribution of economic and political power is so unequal, the increased economic significance and political influence of developing countries provides an opportunity to reshape rules and institutions even in a world of unequal partners. Developing countries as a group with mutual interests are more likely to be heard than single countries by themselves. There will always be some conflict of interest but there will always be areas where it is possible to find common cause and accept trade-offs. This is already visible in the WTO where solidarity among developing countries has enabled them to voice their concerns even if they have not yet been able to shape outcomes in negotiations.

At the same time, the large emerging economies - Brazil, China, India and South Africa - taken together, may be able to exercise significant influence through multilateralism, whether institutions or rules, in the global context. The United Nations, the World Bank, the International Monetary Fund and the World Trade Organization are among the most important multilateral institutions. In the United Nations, China alone is a permanent member of the Security Council with a right to veto. And it is also a member of the P-5. But India, Brazil and South Africa are engaged in knocking at the door, seeking permanent membership of the Security Council, with or without a veto. There can be little doubt that if and when there is an

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[41] The evidence on the significance of developing countries in the world economy, cited in this paragraph, is from Nayyar (2009).
[42] For more detailed evidence on this concentration, see Nayyar (2009).
[43] This hypothesis is developed, at some length, elsewhere by the author. See Nayyar (2009).

increase in the number of permanent members of the Security Council in the United Nations, these three countries would have the strongest claim to permanent membership. In the World Bank and the International Monetary Fund, China, India, Brazil and South Africa are permanent members of the Executive Boards. Given the democratic deficit in these institutions, which is embedded in unequal voting rights, China, India, Brazil and South Africa together could influence decisions or even reshape rules. So far, however, there is limited, if any, coordination among them for this purpose.[44] They have neither articulated collective voice nor exercised collective influence. The situation in the World Trade Organization is different. India and Brazil have been long standing advocates of developing countries in the WTO. China has a low profile possibly because of its recent accession. South Africa is not quite part of the strategic alliance among developing countries. But India and Brazil, along with United States and the European Union, are now members of the *Quad* which is the principal institutional mechanism for resolving differences and finding solutions. In sum, it would seem that China, India, Brazil and South Africa have a considerable potential for articulating a collective voice in the world of multilateralism. Coordination and cooperation among them carries a significant potential for exercising influence on multilateral institutions, which could reshape rules and create policy space for countries that are latecomers to development. Such coordination and cooperation, which is in the realm of the possible, has not yet surfaced in a substantive sense.[45] Even so, it is possible to discern beginnings. Brazil, China, India, and South Africa, together with Mexico, constitute the Outreach-5, who have been invited to the G-8 Summit in recent years. There is a hint of discontent about their status as observers peripheral to deliberations and decisions. And the Outreach-5, acting together, are now seeking a place at the high table with the G-8. The Climate Change Conference in Copenhagen saw an attempt at coordination among the four countries who have now chosen to describe themselves as BASIC. Even so, it is important to recognize that once these countries become major players, there is a danger that they might opt for the pursuit of national interest rather than the spirit of solidarity among developing countries or the logic of collective action.

[44] There is, perhaps, a modest beginning in the G-20, where India, Brazil and South Africa, with some participation from China, have made an attempt to coordinate their stance on reform and change in the IMF. But this is no more than a beginning. It has not influenced, let alone shaped, outcomes.

[45] The implications and consequences of the emerging significance of Brazil, China, India and South Africa in the wider context of the world economy are analyzed, at some length, in a recent paper by the author. For a detailed discussion, see Nayyar (2010).

Second, outside the world of multilateralism, there is a possibility of international collective action by developing countries for developing countries. In this context, it is interesting to note that, during the period from 1996 to 2005, the share of developing countries in international foreign exchange reserves held by central banks went up from less than two-fifths to more than two-thirds. Developing countries consciously built up foreign exchange reserves after the financial crises through the 1990s because the IMF was perceived as a difficult and unpredictable lender of the last resort. This outcome was thus shaped by the quest for self-insurance. That is the good news. The not so good news is that it has not been put to use in terms of development because these reserves are placed largely in fiduciary deposits in industrialized countries or to buy Treasury Bills of governments in industrialized countries. Clearly, there are alternative uses for these scarce resources which can support development. But institutional mechanisms need to be developed for this purpose. For example, developing countries can begin to think of regional institutions, as alternatives, or at least complements, to multilateral financial institutions which are caught up with belief systems that are simply not appropriate and are exceedingly difficult to change. New institutions, different in conception and design, could make a new beginning. But that is not all. If we think of channels of transmission in the world economy, developing countries are, together, an important potential market for exports and an alternative source of finances for development. The possibilities of regional arrangements in the developing world, which could be inter-regional, intra-regional or sub-regional, are also important because it is about pooling markets and pooling resources for development.

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