

ICRIER

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Foreword

Coming Out of the Slowdown



The world economic system appears to have come out of the economic slowdown faster than was earlier expected, no doubt owing to the combined fiscal and budgetary stimuli provided by all the governments. The actions required for the recovery were discussed in a series of meetings of the G-20 finance ministers and the Summit meetings of the Heads of Government. There was talk of coordinated action, but except for the agreement to strengthen the finances of the IMF, much of the action was taken by each country based on its assessment of its own needs.

The revised estimates of GDP growth of the IMF reflect the improved outlook for the global economy. The estimates indicate that different countries are expected to grow at different rates. The differing speeds of recovery will give rise to different issues becoming a matter of concern in a different sequence in each country and, consequently, the desire expressed at the G-20 meetings to have a coordinated exit from the stimuli may not be possible.

As we cast about to see what is happening around us, we observe different issues gaining priority in different countries. This issue of Regional Insights is reflective of these disparate concerns. While the guest article discusses the need for reform of the IMF, China appears to be taking some tentative steps to make the Renminbi an international reserve currency. With concerns about the declining value of the US dollar, the oil producers may need to look at whether oil should be priced exclusively in that currency. And a group of wise men led by Joseph Stiglitz and Amartya Sen tell us that the fixation on GDP as a measure of human welfare is misplaced; their advice is to also measure other elements that more directly measure well-being.

In presenting this varied fare, we hope that the reader will recognise in it the diversity that makes up this world.

This issue has been co-ordinated by Chetan Bhatia under my supervision. My thanks to him and all others who contributed to this effort.

Shrawan Nigam
Senior Consultant, ICRIER

Germany: Light at the End of the Tunnel

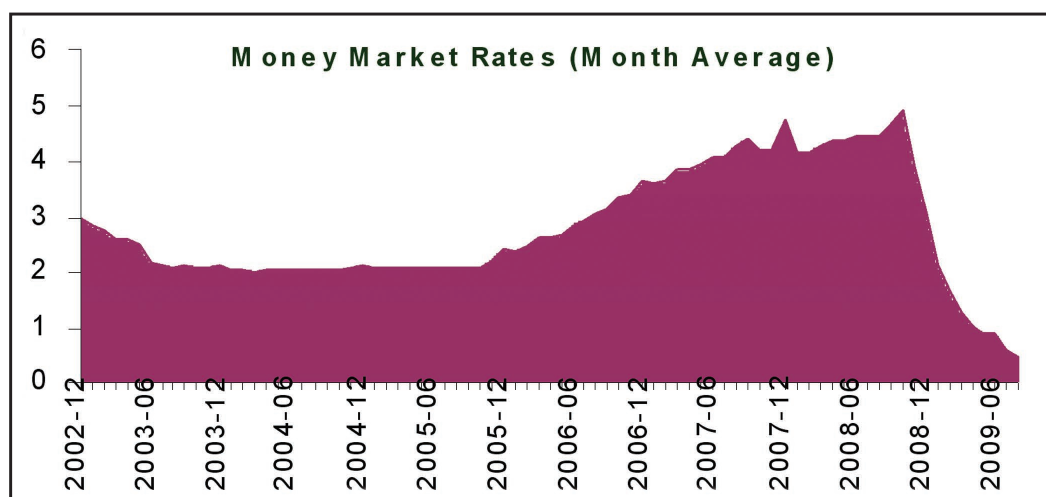


The financial crisis of 2008-09 surfaced in the US initially in the summer of 2007 and grew into a full blown crisis in September 2008 with the collapse of Lehman Brothers. It then rapidly spread across the globe. This 'Great recession of 2008-09' has been the most synchronised financial crisis that the World has experienced since the Great Depression. Germany was the first country in Europe to be hit by the crisis, with IKB Deutsche Industriebank, being the first bank to be declared in financial trouble in Europe as early as August 2007.¹

Apart from some hiccups in the financial sector, the real economy in Germany had been growing robustly until the early part of 2008. However, the collapse of Lehman Brothers in the US (September 2008) changed the overall scenario. The Lehman collapse led to an increase in risk premia in the credit markets across the world and, consequently, increased the money market spreads leading to the collapse of the overall credit delivery system across Europe, including Germany. This eventually had a series of repercussions on different parts of the economy. The transmission channel of the crisis in Germany (typical of any developed economy) was from the credit market or from the financial sector to the real sectors. There were various measures that were undertaken by the German authorities to overcome the crisis which included early bailouts of troubled banks along with other guarantees (400 billion Euros) for bank deposits and also refinancing in money markets. The overall stimulus provided by the German government has been estimated to be around 85 billion Euros.

This article, without getting into the details of how the financial crisis spread to different sectors in the German economy, would like to examine whether the recovery process has started after the financial crisis hit Germany.

Figure 1



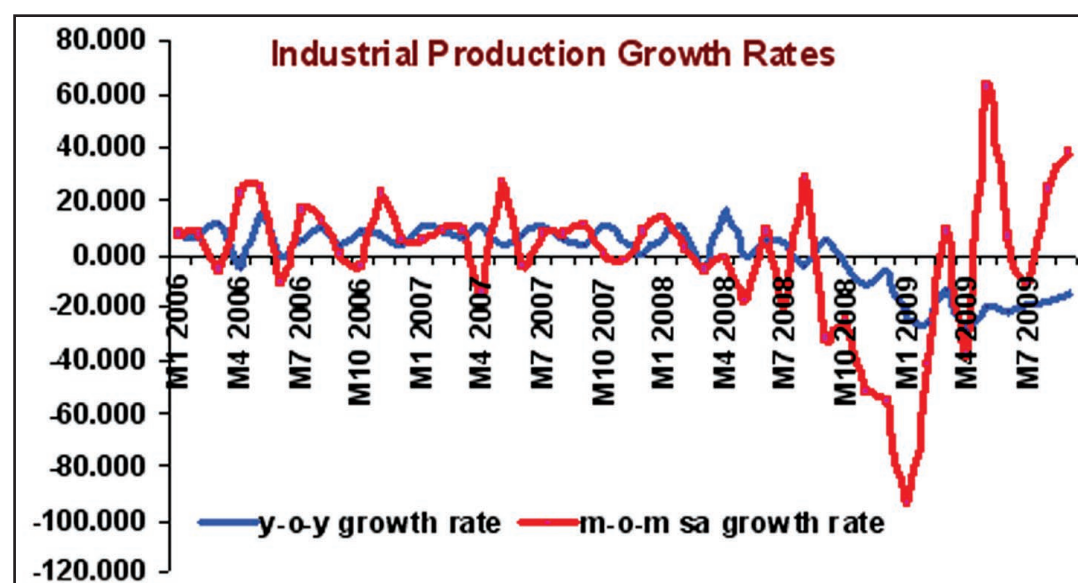
Source: Bundesbank (2009)

It may be worthwhile to begin by examining the credit market developments in Germany. When the crisis was at its peak, the money markets had frozen and the spreads increased with money market rates peaking to around 4.9 per cent in Germany during October 2008.

¹ IKB Deutsche Industriebank was the first bank in Europe to be bailed out following the financial crisis.

Commercial bank lending rates also rose to a high level of over 7 per cent. However, liquidity levels rose with the introduction of stimulus measures by the German government. This led to a fall in the commercial bank lending rate to around 1.8 per cent (May 2009). As can be seen in figure 1 above, money market rates too fell to 0.49 per cent in August 2009. It is apparent, therefore, that there has been a considerable easing of credit constraints in the economy since the credit freeze during the early stages of the crisis, which also led to a demand slump in the real sectors of the German economy.

Figure 2

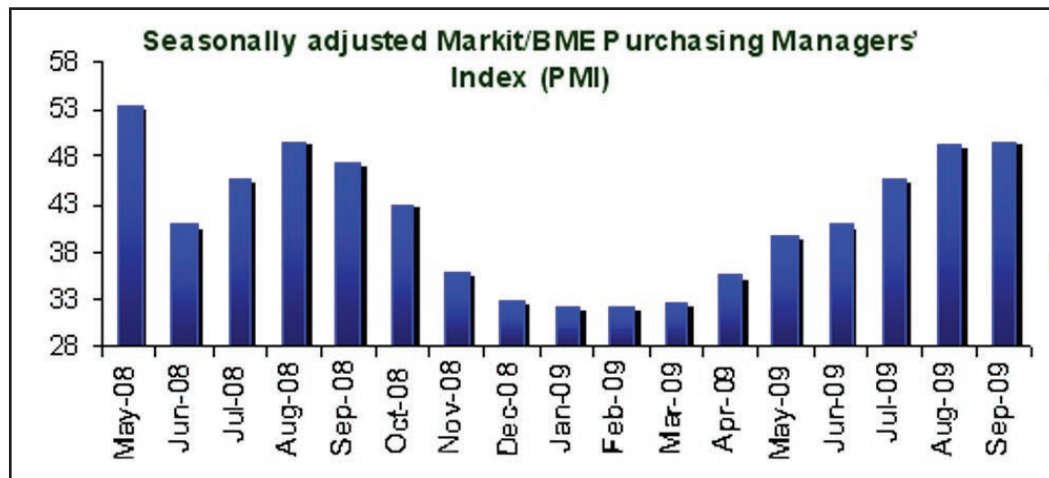


Source: IFS

The credit crunch had a simultaneous impact on the industrial sector with the contraction starting from the month of October 2008. The average contraction of the industrial sector during the core period of the crisis (October 2008-September 2009) was around 17 percent. The contraction which was visible from June 2008 became particularly severe from October 2008 onwards. A reversal seems to be taking place with a moderate pick-up in the orders received by overall industry with the seasonally adjusted month-on-month growth rate rising to 3.4 percent in the period May-July, 2009. From the de-seasonalized data for industrial production we find from May 2009 onwards (except July 2009) that the growth has been robust with average growth (May-September 2009) of around 14 percent. The other major indicator showing significant recovery signs in the industrial sector is the Purchasing Managers' Index (PMI).

The seasonally adjusted Markit/BME Purchasing Managers' Index (PMI) - a composite indicator designed to give a single-figure snapshot of operating conditions in the manufacturing sector also rose to its highest level in 13 months in the month of September 2009. Overall the rising trend seen in the orders placed, overall industrial production growth rates and the Purchasing Managers' Index (PMI) can be considered good signs of revival of the economy. Trends in confidence indicators also provide signs of recovery. Confidence indicators like GfK AG's sentiment index for October 2009, based on a survey of about 2,000 people, increased to 4.3 from 3.8 in September 2009. That's the highest reading since June 2008. German consumer confidence index also rose to a 16-month high in the month of September 2009.

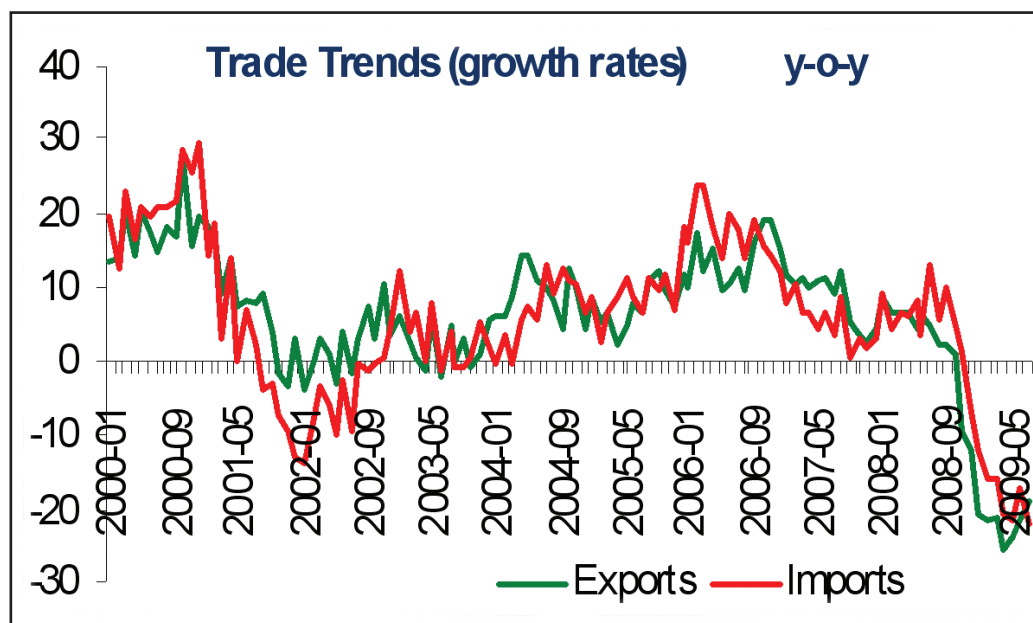
Figure 3



Source: Markiteconomics

The recovery story is also reflected in Germany's trade figures. This can be considered a significant development given that it is the second largest exporting country in the world after China. It is particularly noteworthy given the sharp decline in Germany's trade which had contracted by around 19.5 per cent as compared to previous year.

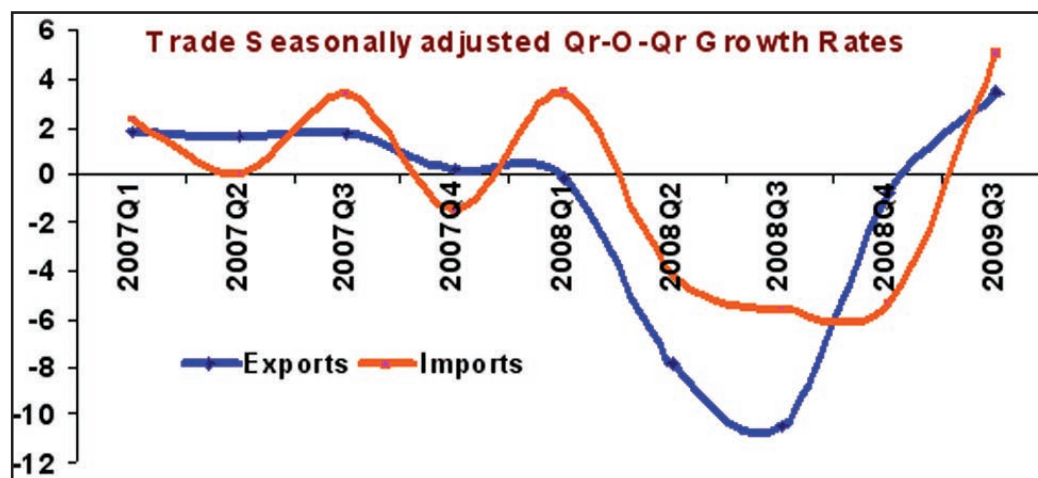
Figure 4



Source: Bundesbank

The year on year growth rates cannot provide a good trend of the inflection points in the data. However, examining the deasonalised quarter-on-quarter growth rates, we find a clear sign of recovery happening during the third quarter of 2009 (July-September) with both imports and exports registering growth rates of around five and 3.4 per cent respectively as compared to the contraction seen in the previous three quarters.

Figure 5



Source: German Federal Statistical Office

There are some green shoots also seen in the employment figures with unemployment rate falling to 8.1 per cent (November 2009) as compared to 8.2 per cent seen in October 2009.

Finally, we can provide a stronger basis for the recovery argument by looking at the most important aggregate indicator of the overall economy i.e. GDP growth rate. Germany's GDP has been positive for the last two quarters. GDP grew by 0.7 per cent during the third quarter of 2009 as compared to the previous quarter (2009Q2) based on seasonally adjusted data. In the previous quarter (second quarter of 2009) too, it had grown by 0.4 per cent. This was in contrast to the contraction seen in the earlier four quarters (2008Q2-2009Q1).

Dony Alex

Japan's Opposition Wins Election: What now for the Economy?



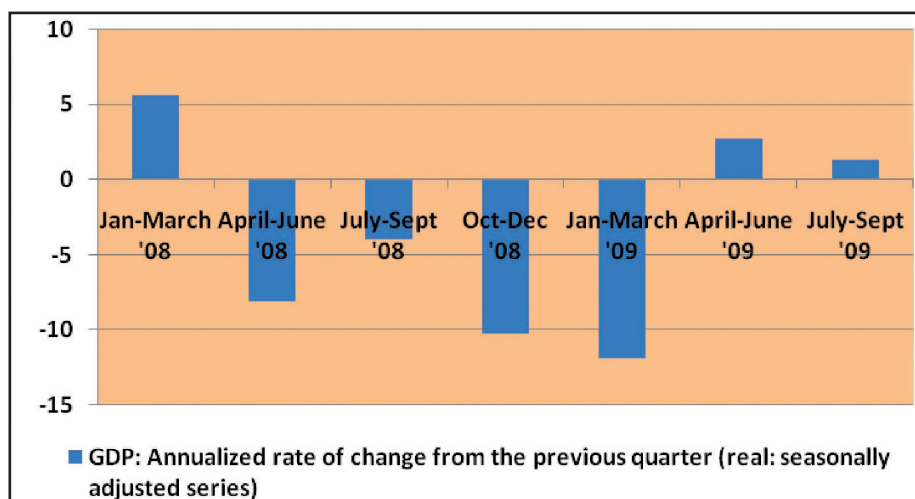
Voters in Japan have handed a landslide victory to the Democratic Party of Japan (DPJ) in the recent general elections, ending five decades of almost uninterrupted rule by the Liberal Democratic Party (LDP). The DPJ won 308 of 480 seats in the Lower House giving it majority control. Through a coalition with two smaller parties, the DPJ is expected to retain majority in the Upper House elections, due later this year, as well.

What does this historic change of guard mean for the Japanese economy struggling to cope with the worst economic recession since World War II? Indeed, winning the national elections was the easy part for the DPJ. The tough part for Prime Minister Yukio Hatoyama will be to deliver on the promises of 'change', particularly on the economic front. The latest data shows that with the aid of stimulus measures at home and abroad, Japan's economy has improved in recent months but only marginally. Rather the fact that China is projected to overtake Japan and become the world's second largest economy in 2010 is prompting speculation that Japan will be the next Switzerland – rich and comfortable, but of little global importance.

Although technically the Japanese economy pulled out of recession in the April-June quarter in 2009, Japan's GDP grew only 0.3 per cent in the July-September 2009 quarter, much slower than the 1.2 per cent expansion reported earlier. This translated to an annualised rate of 1.3 per cent, down from the previous estimate of 4.8 per cent. The Japan Cabinet Office has said that the main reason for the fall was that capital investment by companies – the amount they spend on new assets – was revised downwards for the quarter to a contraction of 2.8 per cent from the original estimate of 1.6 per cent growth, in the face of the stronger yen. The yen recently hit a 14-year high of around 84 to the dollar.

The severe downgrade in GDP figures is expected to intensify the ongoing dispute between the Bank of Japan and the Ministry of Finance over whether Japan's outlook can be described as positive. The central bank has consistently painted a more optimistic picture of Japan's prospects, leading the Financial Services Minister, Shizuka Kamei, to accuse it of being "asleep at the wheel, as usual".¹

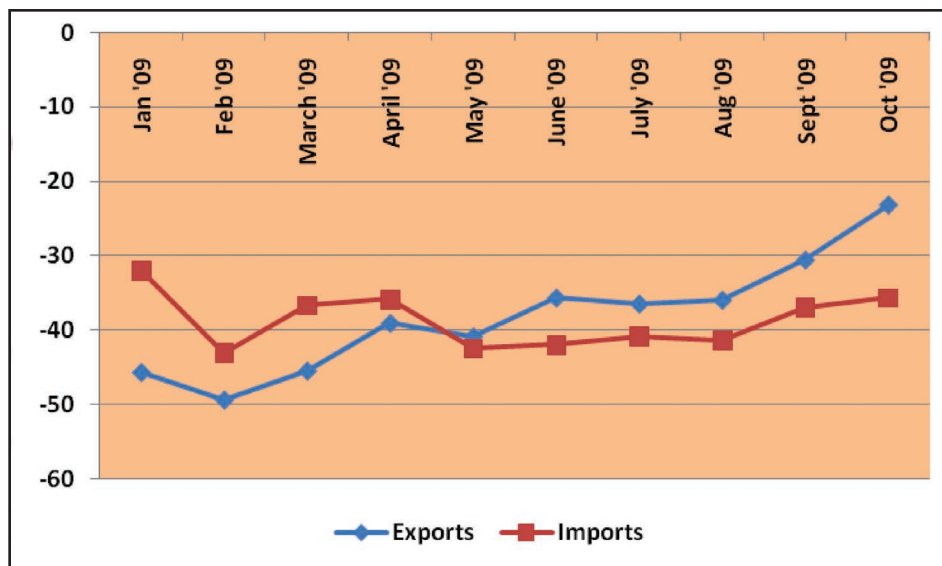
Japan's GDP: Annualised rate of change from the previous quarter (real: seasonally adjusted series)



¹ 'Ridiculous' revision of figures leaves Japanese recovery hopes in tatters, Times Online. Dec 9, 2009 <http://business.timesonline.co.uk/tol/business/economics/article6950348.ece>

Specifically, Japan's exports have been falling less in year-on-year terms after tumbling nearly 50 per cent in February 2009. In terms of volume, the exports to the United States and Asia are improving gradually, while exports to Europe remain weak.

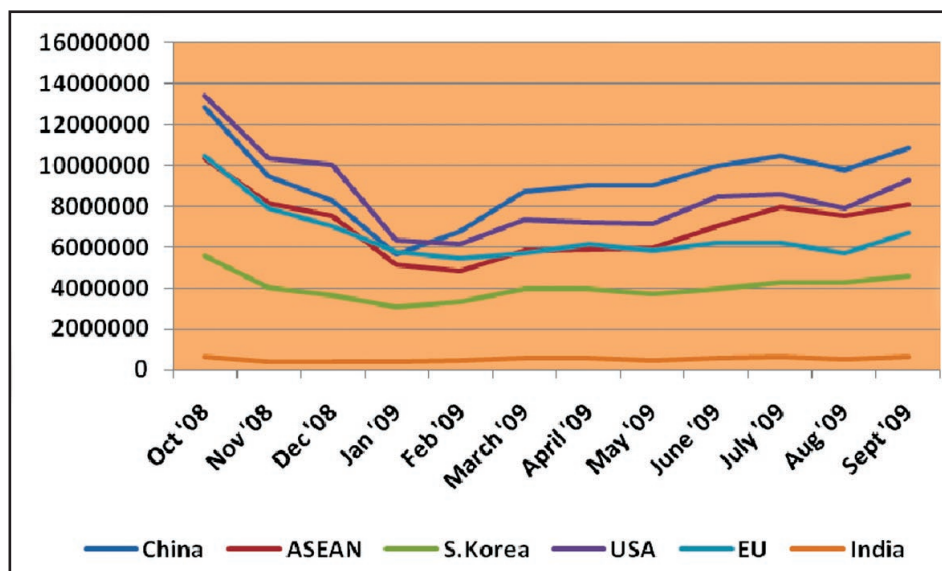
Japan's Exports and Imports: % Change over the Same Month in the Preceding Year



Source: Ministry of Finance, Japan

Total Value of Japan's Exports to Major Country/Region

(US\$)

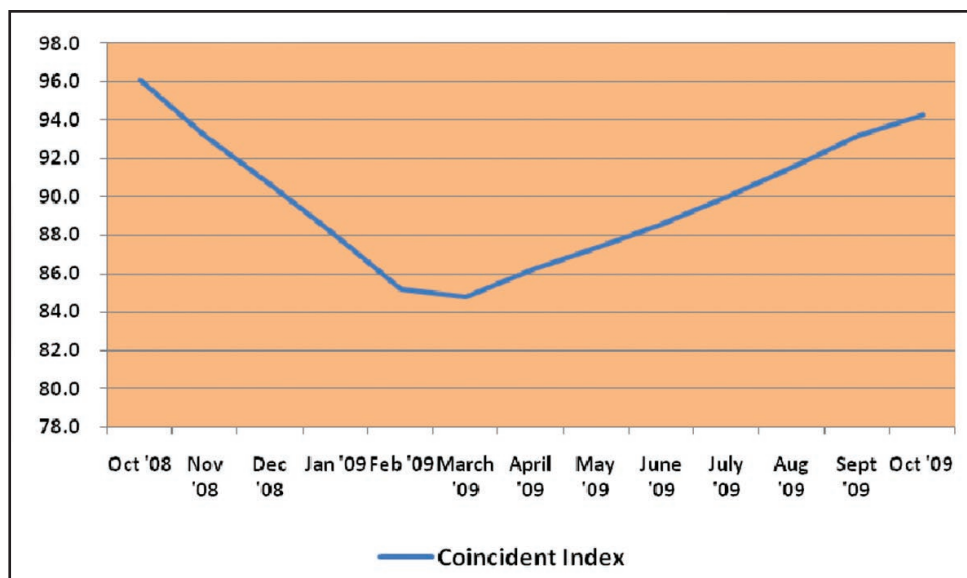


Source: Japan Statistics Bureau

The coincident index, a composite of eleven indicators, estimated by the Economic and Social Research Institute, has climbed to 94.3 in October 2009, the highest since November 2008. The coincident index is regarded as the broadest indicator of economic activity as it includes industrial production, manufacturing shipments, large industrial power consumption, retail sales, all industries' operating profits, sales in small and medium enterprises and effective job offer rate.

Coincident Index Graph

2005 average = 100

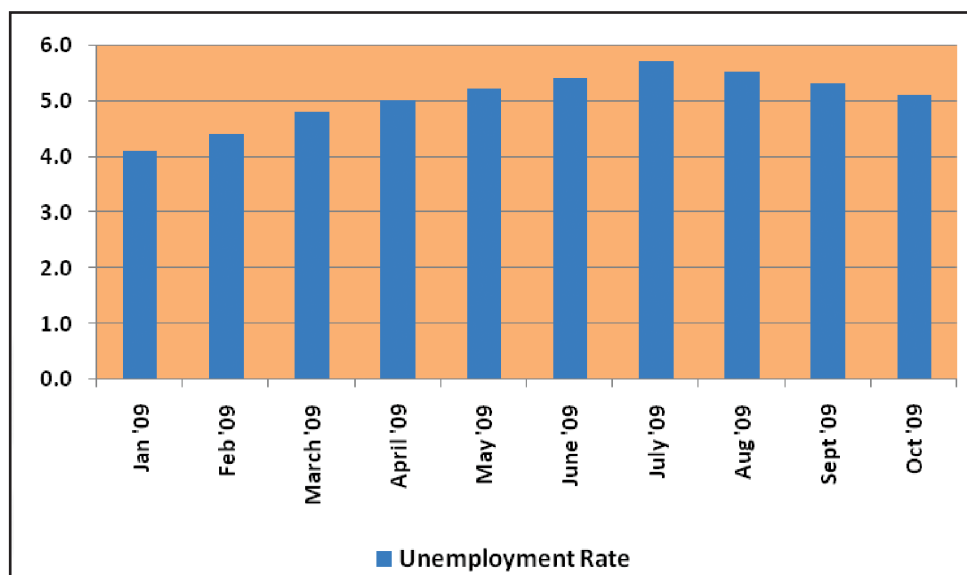


Source: Cabinet Office, Japan

Though these figures indicate some kind of economic recovery, what is worrisome for the government is that it has been weaker than previously estimated. The pressure on investment and jobs, therefore, remains.

Japan's unemployment rate has declined marginally to 5.1 per cent in October 2009 after registering a post-war high of 5.7 per cent in July 2009. The number of unemployed persons in October 2009 was 3.44 million, an increase of 34.9 per cent from the previous year. According to the Labour Ministry, the job-to-applicant ratio, a leading indicator of employment trends stands at 0.44, meaning there are only 44 positions for every 100 candidates. The proportion of college students with job offers has tumbled 7.4 per cent from a year earlier to 62.4 per cent. Further, the average monthly income per worker household is down 4.6 per cent in nominal terms and down 1.8 per cent in real terms from the previous year.

Japan's Unemployment Rate



Source: Japan Statistics Bureau

With regard to investment, the Bank of Japan's closely watched 'Tankan' survey of business sentiment released early December 2009 offered a downbeat picture for future capital spending. According to the survey, big companies plan to cut capital outlays by 13.8 per cent in the fiscal year ending in March 2010. This is a more pessimistic result than the 10.8 per cent cut projected in the previous survey in September 2009.

Household spending, a leading indicator of private consumption that accounts for nearly 60 per cent of Japan's GDP, grew 1.6 per cent in October 2009 from a year earlier. However, the average of monthly income per worker household is down 1.8 per cent in real terms from the previous year. In fact the average consumption expenditure per worker household is up only 0.6 per cent in real terms from the previous year. The worry is that the rise in overall figures is mainly due to government subsidies offered on energy-efficient cars and electronics and it will be difficult to sustain the momentum because of falling wages and rising unemployment.

Index of Consumption Expenditure Level: % Change from the Previous Month

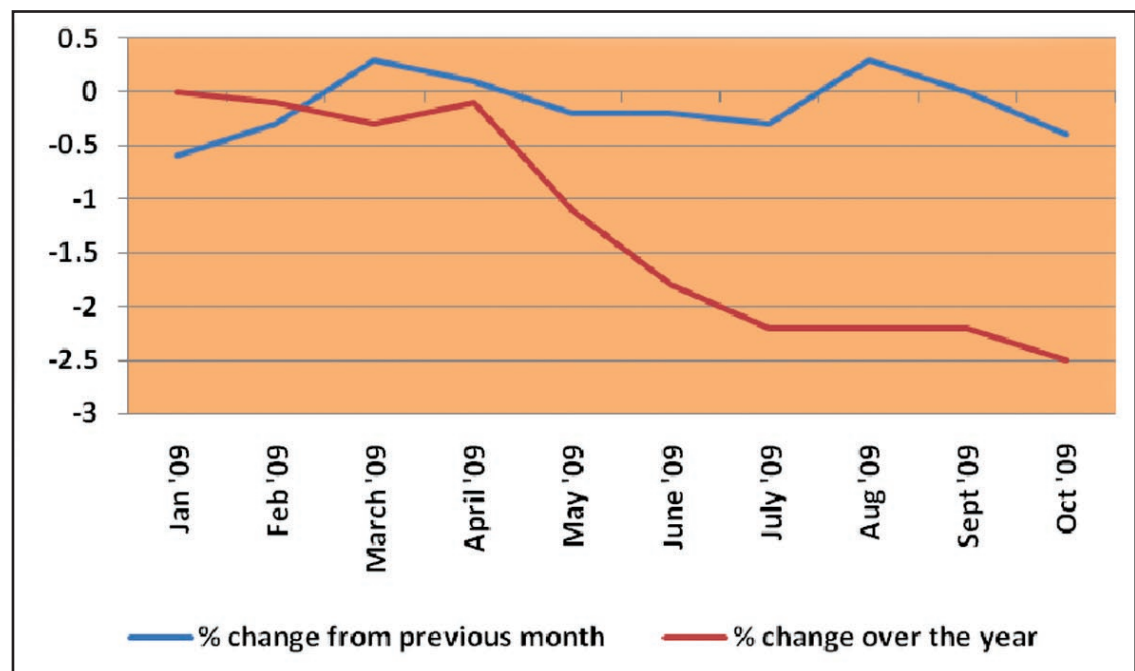


Source: Japan Statistics Bureau

In fact, sluggish domestic consumer demand is already weighing on prices. The key consumer price index (CPI) has fallen a record 2.5 per cent in October 2009 from a year earlier. Core CPI has now dropped for seven straight months and suggests that Japan is once again headed towards a prolonged period of deflation. It is expected that the Bank of Japan forecast that deflation is likely to linger until March 2011 will be extended. Though the big drop in CPI over the last few months stems mainly from lower oil prices, even the so-called "core-core CPI", excluding fresh food and energy, has fallen 1.1 per cent from last year.

Consumer Price Index: % Change

2005=100



Source: Japan Statistics Bureau

To tackle this gloomy economic scenario, the DPJ panacea is to reorient public spending from wasteful mega infrastructure projects to directly boosting consumer demand. Guided by the philosophy of “Putting People’s Lives First” and “Improving People’s Lives Will Improve the Economy”, the aim is to realise economic recovery by increasing the disposable income of households with tax cuts and enhanced welfare measures. Some specific measures that the electorate has been promised are financial incentives to boost Japan’s low birth rate, free high school tuition, eliminate highway tolls, create a more robust pension system, improve health care, and raise minimum wages.

These measures are expected to cost some US\$77 billion in the fiscal year starting April 2010, rising to US\$185 billion in the fiscal year ending March 2014. Given that government debt in Japan is already the world’s largest and public-debt-to-GDP burden is fast spiralling towards 200 per cent, the question is whether this is fiscally sustainable. Already Japan’s debt service obligations took up a fifth of the entire budget for 2008. With tax revenue plunging, the government is likely to take on additional debt this year to make ends meet. According to Japan’s Chief Cabinet Secretary Hirofumi Hirano, the government may have to issue more than US\$500 billion in government bonds if it is to fulfil election campaign promises.

The new Finance Minister Hirohisa Fujii has said that improving the economy will be his top priority even if it is at the expense of Japan’s precarious fiscal health. In his words, “Of course, government finances are important, but my principle is that the economy comes before government finances.” Already, the Bank of Japan is facing mounting pressure to loosen its policy as deflation tightens its grip on the nation’s economy. Calls to adopt new easing steps such as purchasing long-term government bonds have grown louder in recent weeks after the government declared that the nation’s economy was in deflation -- a decline in the general level of prices for goods and services - for the first time since 2006.

In addition, the new Japanese government is signalling a change in the currency intervention policy. The finance minister has said that he sees benefits in the strengthening of the yen and that he does not favour intervention to weaken the currency to help exporters. This is a major shift in Japan's policy, which in the past has encouraged a weaker yen to boost Japan's export competitiveness. The idea is that in Japan's resource poor economy, a strong yen lowers costs for manufacturers and consumers gain greater purchasing power.

In fact, the recently unveiled US\$81 billion economic stimulus plan highlights the balancing act the DPJ coalition is struggling with. The government is keen to prevent the economy from going into a "double-dip" recession but also faces a potential "debt trap". Heavy government borrowing in tandem with the downward demographic trend in Japan projects an extremely difficult economic outlook in the longer-term. So far, Japanese households have indirectly bankrolled government debt through their low-yield savings. But the average household savings rate has plunged in recent years from over ten per cent to just two per cent. And, the decline in savings has come not via higher spending but via reduced incomes. Besides, Japan's rapidly ageing society cannot forever sustain financing of government spending.

The latest United Nations forecast estimates that there would be 77 elderly dependents for every 100 workers by 2050, compared with just 33 per 100 now. Prime Minister Hatoyama's government needs to take bold but necessary steps to open up immigration policies and slow down the decline in working population. This will also lower the price of domestically consumed services, thereby further raising consumer purchasing power. Unless there is fundamental structural reform in Japan the elections will remain momentous only in political terms.

Sanjana Joshi

Guest Article

Globalisation and Reform of the IMF



(Shigeo Kashiwagi is Senior Fellow at the Policy Research Institute, Ministry of Finance, Japan. This contribution is an abridged version of his original article published in Japanese in May 2009.)

At the G20 summit in April this year, leaders declared, “We believe that the only sure foundation for sustainable globalisation and rising prosperity for all is an open world economy based on market principles, effective regulation, and strong global institutions.” The key question is whether they will be able to take action in line with this message. Until the outbreak of the current crisis, the world economy was globalising at a rapid pace. Unfortunately, now the movement towards globalisation seems to be going into reverse. Global trade has shrunk for the first time in twenty five years, and the flow of capital has also decreased.

The biggest concrete result of the London summit was the agreement it reached on reform of the IMF. Why was this a topic of discussion? And does the fact that it was relatively easy to reach an agreement on this issue mean that it will be easy to implement it and that we can hope that the IMF will contribute to preventing the reversal of globalisation?

The first reason for the calls to reform the IMF is the need to secure additional resources for it so that it can play an appropriate role in supporting countries hit by crises. What is particularly essential is to provide financial support for emerging market economies that have been powering global growth in recent years. In order to restore global confidence, it is essential to secure a proper flow of capital. The second reason is the need to make the IMF’s lending system easier to use; this is in response to the fact that recent years have seen a decline in the use of IMF resources. It has been variously pointed out that the loan application procedures are time-consuming, that the amounts of loans fall short of borrowers’ requirements, and that the policy conditions imposed on borrowers are too strict.

In line with such observations, the IMF moved in advance of the London summit to expand its lending limits and to create a new system of “flexible credit lines,” allowing countries with strong economic fundamentals and sound policies to set up provisional credit lines that they can draw on immediately. It also decided to overhaul its lending system. The IMF nevertheless needs to undertake bold reform so that it can offer appropriate support for globalisation among its member countries. Another reason for IMF reform is to monitor the implementation of macroeconomic policy pledges that countries have made in the face of the current global crisis and construct an early warning system that will be effective in predicting and forestalling future crises.

Leaders have pledged various measures in order to overcome the current crisis, but the surveillance of implementation is a task that can only be handled by an international institution like the IMF. In fact, the existence of this sort of international institutional framework is a major difference between now and the 1930s, and this is the basis for assertions that it will be possible to avoid the worst-case scenario in the face of the current crisis. Of course, it is also necessary to reform the weighting of quotas within the IMF as a part of the reform of global governance so as to reflect countries’ voices more appropriately in discussions concerning global issues. It is thought that countries’ voices within the IMF should basically reflect their shares of the world economy.

But implementation of the IMF reform measures may not be easy, and we can expect to see various twists and turns in the road ahead. What are the key points to watch in connection with this process?

First of all, we should note that agreement has yet to be reached concerning the details of the enlargement of the IMF's resources. The orthodox approach would be an ordinary capital increase in the form of hikes in the member countries' subscriptions, but the task of sorting out the countries' conflicting interests in this connection is likely to take considerable time. So the London summit participants agreed on a US\$500 billion increase in the IMF's resources in the form of loans from specific countries, with market borrowing to be considered, if necessary, as a supplement.

Of the US\$500 billion, half has already been found in the form of concrete commitments from Japan (US\$100 billion), the EU, Canada, and Switzerland. It is expected that other countries, such as the United States and China, will also make concrete offers, but the amounts and timing remain uncertain. One hopes that other Asian countries with ample foreign reserves will do their share in promoting global economic stability by actively extending similar loans. At the same time, there is concern on whether the IMF's newly established lending facility will actually lead to increased lending.

The financial crisis has led to an increase in the number of countries applying for IMF loans but, in most cases, the applications are being made after fund shortages have emerged, implying that the countries' domestic economies have already started to feel adverse effects. In today's world, where global flows of funds have expanded greatly, even countries whose domestic economies are performing well can find themselves suddenly facing a shortage of funds if some external factor causes a large outflow of capital. In order to ward off such occurrences, the IMF should set up a precautionary system allowing countries meeting certain conditions to receive loans immediately on the basis of agreements reached in advance.

The IMF has set up the "flexible credit line" facility, which would seem to meet this description, but the poorer countries cannot use it, and even countries that are eligible may be reluctant to apply for credit lines lest outsiders take their submission of an application as a sign that their economies are fragile. Of particular interest is whether applications will be forthcoming from the emerging market economies in Asia, which have been keeping their distance from the IMF following the 1997-98 Asian currency crisis. Their response will be instrumental in determining the future effectiveness of the IMF in Asia.

An additional area in which problems exist is the IMF's responsibility for monitoring the economic policies of its members. The track record so far shows that even if the IMF offers fine advice to member countries about their policies, inasmuch as the recommendations are not binding, they have no effect unless the country receiving the advice can summon the political will and decisiveness required for implementation. In order for the IMF truly to serve as a major force in blocking the reversal of globalisation, it is necessary to ensure that countries accept its advice regardless of whether they are developing or developed or whether they are recipients of IMF lending or not. This point presents a difficult challenge for the major advanced countries, including Japan, and it also represents a crucial test for the IMF, whose effectiveness has been called into question.

The final problem I would note is in the area of the IMF's governance. Though the need for governance reform is accepted and there is agreement on the general principles

involved, it will be difficult to achieve prompt concrete implementation. The IMF has been considering this matter even before the current crisis struck, and it has reached a degree of agreement. In the spring of 2008, it conducted an ad hoc adjustment of quota shares, and it has been agreed that future capital increases should be conducted in such a way as to make countries' quotas reflect their economic strength. In this respect, the IMF deserves high marks by comparison with other international institutions set up under the leadership of the victorious Allies after World War II, such as the United Nations Security Council, where the original governance structure has remained fundamentally unchanged.

At the London summit, it was agreed to seek further reform of the IMF's governance, including the adjustment of quota shares, in order to strengthen its relevance, effectiveness, and legitimacy. Achieving this will require co-operation and political commitment by the countries involved. It will be important in this connection for countries whose relative economic weight has declined to be willing to accept decreased shares, and for countries seeking larger shares to be ready to accept greater responsibility and burdens accompanying their increased voices within the IMF.

Japan, which rose from the position of a defeated country receiving assistance to the status of an advanced country, and whose quota share within the IMF has risen accordingly, has a duty to tell other countries about its experience. It is to be hoped that Japan will show leadership in encouraging other Asian countries to play a more forward-looking and constructive role.

The road to reform of the IMF is unlikely to be a smooth one. There is a constant tendency for participants in international gatherings like the London summit to shunt off all the difficult problems to international institutions and minimise their own countries' burdens. The successful implementation of the agreements reached in London will depend on whether the national governments of the countries involved can refrain from dismissing these issues as somebody else's concern and take action in a responsible manner as the IMF's shareholders. The response of Japan and other Asian countries will be of particular importance in this connection.

The age when the G7 or G8 countries could reach agreements just among themselves and, thanks to their overwhelming strength, turn them into global agreements is now clearly over. In recent years, the participants in both the G8 summits and the G7 meetings have been conducting "outreach" programmes, giving some emerging market economies the opportunity to make their opinions heard. In this respect, the G20 can be expected to play a major role. But it is simplistic to think that the G20 can solve every problem; we must keep its limitations in mind.

Like the G7, the G20 is a forum in which countries exchange opinions unofficially. Global decision making needs to take place in officially recognised international forums like the UN General Assembly and annual meetings of the IMF and the World Bank. The role of both the G7 and the G20 is to give countries the opportunity to conduct unofficial exchanges before the formal decision-making process. Also, it is rash to think that the G20 can completely replace the G7 and G8. The G7 will probably continue to play a major role as a forum for discussing and reaching decisions among developed nations sharing the same sorts of economic systems and conditions. A group with as many participants as the G20 may not necessarily be able to discuss matters efficiently and effectively.

In the period to come, we are likely to see the G7, G8, and G20 all continuing to play their respective roles, co-existing and overlapping as forums for international exchanges of opinions. What is crucial in this connection, as in the case of countries' voices within the IMF, is that the new participants recognise that the right to take part in such gatherings is accompanied by the need to accept certain responsibilities with respect to the world economy.

Henceforth, we need to reform global governance from a broader perspective, not just with reference to the numbers of countries participating in particular meetings. In order to prevent a reversal of globalisation and achieve stability for the world, we may need to create an institution that can take a comprehensive approach. The existing IMF-World Bank system was created at the Bretton Woods conference hosted by the United States in 1944. Some are now calling for a "new Bretton Woods" gathering to redesign the system. This may be desirable, but we cannot be too sanguine about the prospects of its realisation in the near future.

The marked decline in the relative leadership strength of the United States has made it difficult to achieve the sort of US-led solution to global problems that was seen previously, as in the case of the original Bretton Woods conference, where America, along with Britain, exerted overwhelming leadership. Even if the world economy gets over the current crisis, there will remain a number of difficult problems needing to be addressed from a medium to long-term perspective. And these difficult problems all concern Japan; our country cannot turn its back on them. As the world's number two economic power, Japan needs to feel a sense of responsibility and play a leading part in addressing these matters.

Since it will be difficult or impossible to resolve global issues without the United States – though its leadership strength may have decreased – Japan should approach the issues on the basis of firm US-Japan co-operation. Japan should recognise that it needs to contribute proactively in dealing with these global concerns. Also, in future, Asian presence in the world economy is certain to grow, and it will become impossible to ignore the opinions of Asian countries. Japan, while playing its own leadership role, should encourage its Asian neighbours to speak up from positions of responsibility concerning global issues and should play a major part in conveying Asian opinions to the rest of the world.

Shigeo Kashiwagi

American Clean Energy and Security Act: Some Concerns



The debate on the link between trade and climate change has become intense in the recent past. Even more intense is the debate on the recent unilateral climate change policies proposed by the US and the European Union and the probable impact of these measures on global trade.

In this context this article attempts to briefly discuss the proposed US climate change bill, the American Clean Energy and Security Act and the concerns associated with it.

Background

The 2007 Climate Change synthesis report by IPCC finds that global warming is unequivocal as is evident from observations of increases in global average air and ocean temperatures, widespread melting of snow and ice and rising global average sea level. The report further argues that greenhouse gas increases as a result of anthropogenic activity over the last 50 years have led to this increasing global temperature. On the basis of this report and other scientific estimates, there seems to be an emerging global consensus that the rise in atmospheric temperature needs to be limited to around 2 degrees Celsius. In order to limit the rise in atmospheric temperature to this level, the report suggests that compared to 1990 levels, industrialised countries might have to reduce their emissions by 25 to 40 per cent by 2020 and 80 to 95 per cent by 2050.

Given these concerns, it is essential to have a multilateral agreement to ensure that economies do indeed bind their emissions and engage in mitigation and adaptation actions. The UNFCCC and the Kyoto protocol are the international frameworks that deal with climate change. The Kyoto protocol, which for the first time defined binding targets for Annex 1 (Industrialised) economies, will come to an end in 2012. Countries have been negotiating on the contours of an agreement that would have to come after 2012. Many had hoped that the Copenhagen Conference would yield such an agreement. But, it now seems that Copenhagen will only be the first step towards such an agreement. The text, which was the outcome of the conference, neither sets a date for emissions to fall nor does it contain binding emission reduction targets for Annex 1 economies. Further, though the text emphasises the collective commitment of developed countries to pool resources for developing countries to engage in adaptation and mitigation actions, there is no specific action plan on how this will be done. This text is, therefore, more a framework for future discussions and is only the first step towards a legally binding ambitious agreement. Such an agreement would take a great deal of negotiations and time to come through.

Given the fact that there might not be an immediate multilateral deal, many economies have been proposing unilateral climate change measures. Concerns arise when such action plans include border carbon adjustment measures to deal with concerns over carbon leakage and the loss of competitiveness of domestic goods due to stringent domestic emission norms. Such measures have been proposed by both the EU and the US.

The US American Clean Energy and Security Act (ACESA)¹

The American Clean Energy and Security Act (ACESA), otherwise known as the Waxman Markey Bill, has been passed by the House of Representatives and is currently being debated by the Senate. The objective of the bill is to steadily reduce US GHG emissions

¹ The American Clean Energy and Security Act discussion draft WRI Brief of the Waxman-Markey discussion draft, John Larsen, Alexia Kelly and Robert Heilmayr, 4/20/09

such that the emissions in 2012, 2020, 2030 and 2050 do not exceed 97 per cent, 80 per cent, 58 per cent and 17 per cent of the emissions in 2005. The manner in which the bill proposes to do this is by a cap and trade system with binding limits on carbon emissions. The draft sets both a non-binding economy-wide GHG emission reduction goal as well as a mandatory cap on certain greenhouse gases. Domestically, the bill aims at distributing allowances through auctions. The bill also has options for the covered entities to satisfy a certain percentage of their emission reduction compliances using offsets, both domestic and international. In order to address leakage and competitiveness concerns, the bill proposes an Output-based Rebating (OBR) model of providing rebates to carbon-intense manufacturers. Sectors are presumed eligible if they meet 5 per cent energy or GHG intensity threshold and 15 per cent trade intensity. Each sector is rebated at 85 per cent of sector average direct and indirect emissions cost. Rebates are phased out beginning in 2020, unless presidential review determines that other countries have not yet taken substantial action and leakage concerns persist. If, by January 2018, no multilateral agreement is in place, the president shall establish an international emission allowance system in place. Under this system, the president will determine whether in each eligible industrial sector, more than 85 percent of United States imports of covered goods with respect to that sector are produced or manufactured in countries that have met at least one of the following criteria:

1. The country is a party to an international agreement to which the United States is a party that includes a nationally enforceable and economy wide greenhouse gas emissions reduction commitment for that country that is at least as stringent as that of the United States
2. The country is a party to a multilateral or bilateral emission reduction agreement for that sector to which the United States is a party
3. The country has an annual energy or greenhouse gas intensity, for the sector that is equal to or less than the energy or greenhouse gas intensity for such industrial sector in the US

The international reserve allowance programme in order to reduce the direct and indirect costs of complying with the bill would allow the sale, exchange, purchase transfer and banking of international reserve allowances for covered goods that are imported with respect to the eligible industrial sector. It would ensure that the price of purchase of international allowances is the same as the auction price for domestic allowances. It would also establish by then a methodology which would calculate the extent of emissions that every importer of the covered good must submit.

Concerns regarding the act

The provisions in the proposed bill that are worrying the global community are two. First, the international reserve allowance programme which would mandate the importers of commodities produced outside the economy to purchase allowances and second, the output rebate program which would rebate carbon intensive goods that are being produced for exports.² The question is whether these measures are being proposed out of genuine concerns regarding carbon leakage or whether they are yet another form of raising protectionist barriers in international trade.

² The American Clean Energy and Security Act discussion draft

Questions could be raised on the legal compatibility of these measures under GATT articles 1 (MFN treatment), 2 (members to be committed not to impose additional customs duties as well as “all other duties or charges of any kind”) and article 3 (National treatment). But article XX of the GATT, which provides for exceptions under certain conditions that affect exhaustible natural resources or health, might provide the loophole for the imposition of such measures. Past WTO disputes, though not precedent setting, do indicate that it might be possible to argue that the measures are compatible under article XX but it would finally be the way the bill is drafted and implemented that would determine whether, or not, it is indeed compatible under the WTO.

More importantly, the basic tenet of the UNFCCC is that of differentiated responsibilities for developed and developing economies, given the historical nature of emissions. This formed the basis for the Kyoto protocol requiring the Annex 1 countries to bind their emissions while developing countries retained the flexibility not to do so. The proposed US border carbon adjustment measures, by not differentiating between developed and developing economies, might be violating this spirit of differentiated responsibilities. Further, if the motive behind these measures is indeed to prevent carbon leakage, then there are other ways to deal with this such as transferring relevant technology faster and cheaper to developing countries, investment in more clean development mechanism projects and offering more financial help to developing countries for their mitigation and adaptation efforts.

The US is not a party to the Kyoto protocol. With the change in US administration, there does seem to be a more positive attitude towards engaging in a multilateral deal, which is evident from its active role in Copenhagen. But it is essential that the policies that the US have in the domestic and international arena should not be conflicting. What is needed right now, given the seriousness of the issue of climate change, is the willingness on the part of the US along with emerging economies to engage proactively to arrive at a legally binding multilateral agreement which would also have substantial policies on technology transfer and financial support. Domestic policies, such as the proposed measures within ACESA, would only lead to an environment of suspicion and cross retaliation. A multilateral agreement might be difficult but not impossible, if the right set of incentives and the right spirit of engagement is there.

Swapna Nair

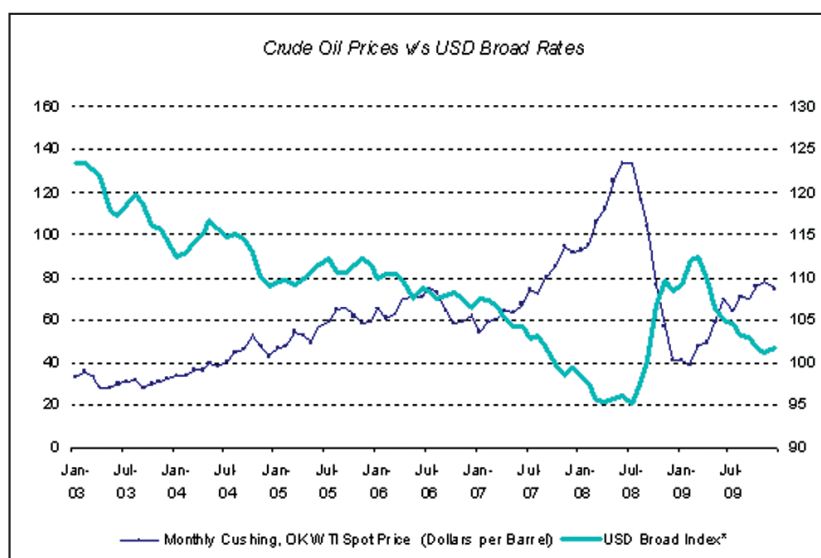
Will Saudi Arabia and Kuwait Favour a Dollar Switch?



Generally, a depreciation of the US dollar is expected to result in a rise in exports for those countries whose currencies are pegged to the dollar and a fall in exports for those whose currencies rise against the dollar. However, due to the inelastic supply response of oil, which is itself a result of the production-sharing agreement under the Organisation of Petroleum Exporting Countries (OPEC), dollar depreciation produces a perverse outcome for oil exporters like Saudi Arabia and Kuwait.

The Link:

The correlation between oil prices and the dollar has been strong and negative. The coefficient of correlation for the two stands at around -0.9 for monthly data running from January 2003 to December 2009. Therefore, oil prices rise when the U.S. dollar depreciates against a basket of currencies.



* The broad index is a weighted average of the foreign exchange values of the U.S. dollar against the currencies of a large group of major U.S. trading partners.

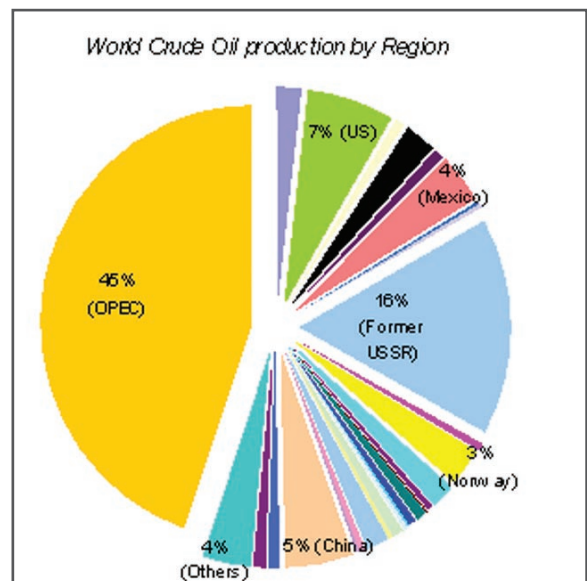
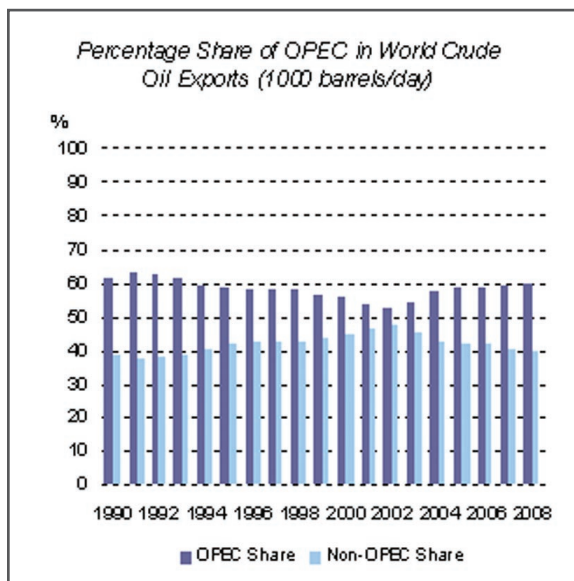
Data Source: US Federal Reserve, *Energy Information Administration-US Dept. of Energy*

What could be the possible explanations for this?

1. Oil is mostly traded in dollars (other than for exceptions such as Iran and Venezuela who have been pushing for other currencies such as the Euro). Given this, even when the local currency's value remains constant against other currencies, a depreciation in the US dollar (implying lower real value of dollar revenues) would have to be compensated for by an increase in dollar-denominated oil prices.
2. Like gold, whose demand increases when confidence in the dollar wavers, the speculative demand for oil would push up its price.
3. The chain of causation can also run from oil to the dollar. A rise in oil prices can affect production in a large energy-importing economy such as the US, leading to bigger trade deficits and a consequent depreciation of the dollar.

The OPEC angle:

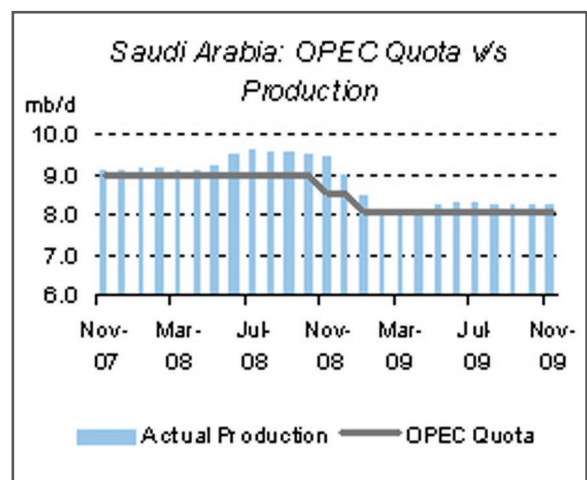
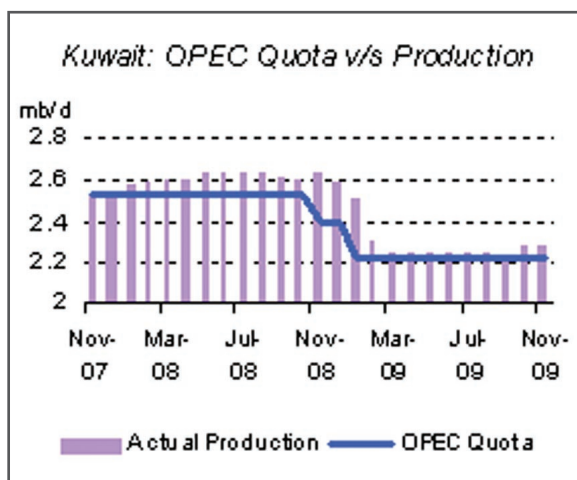
OPEC accounts for 60 per cent of the world's crude oil exports. This predominance and the fact that outside OPEC, individual producers are mostly small and in any case fragmented (illustrated in charts below), allows it to behave like a typical cartel which controls supplies.



Source: www.opec.org

Kuwait and Saudi Arabia are both OPEC members. Given this, they are more or less obliged to comply with OPEC production quotas. In January 2009, OPEC made a cut of 2.2 million barrels a day (mb/d) in the overall production of its members. It has maintained that level since. Saudi's quota went down from the November quota of 8.477mb/d to 8.051 mb/d, i.e. a 5 per cent fall. For Kuwait, the new quota is 2.222 mb/d or a fall of 7.38 per cent from the previous quota.

Therefore, when the dollar depreciates and the real value of the oil-related dollar revenue of OPEC members decreases, they lower supply and push up prices.



Note: mb/d is million barrels per day.

Data Source: International Energy Agency, Bloomberg.

Can there be a switch from dollar denomination of oil prices?

The three existing oil markets – the West Texas Intermediate crude, North Sea Brent Crude and UAE Dubai crude – are all dollar-denominated. In the March 2008 OPEC conference, members had noted that oil prices were moving against market fundamentals and was being influenced both by the weakness in the US dollar and the significant flow of funds into the commodities market (as stated earlier, the speculative demand for oil rises when the dollar wavers).

Recently, speculation has been rife that secret meetings are being held by certain Gulf States to replace oil trading in dollars with the Yen or the Euro. However, this is unlikely to happen. During one of the OPEC meetings, Iran had suggested that oil be priced in a basket of currencies, but this did not meet with much support, especially from strong US allies such as Saudi Arabia. Because such a switch can also have serious foreign policy repercussions on many of the countries in the Middle East, the possibility of a widespread political consensus on the issue is unlikely. The US has already placed several restrictions on its nationals from directly or indirectly trading, financing or facilitating any goods or services from Iran (which already uses other currencies to trade in oil) that would benefit their oil industry. The professed objective of these sanctions was to curb Iran's terrorist activities. However, today, there is heightened awareness in the West regarding the rest of the region's, especially Saudi Arabia's, involvement in such activities. Given this, sanctions detrimental to the region may not be difficult to place.

What can we expect in the future?

Given the negative correlation oil prices share with the dollar, a weak dollar may in fact augur well for the oil exporters' current accounts.

According to IMF estimates, in 2008, (the year of record high oil prices as well as a weak dollar), Saudi's exports of oil and refined products (measured in dollars) jumped by 36.8 per cent compared to 9 per cent in 2007 and resulted in a current account surplus of \$134.2 billion¹ (28.6 per cent of GDP) compared to \$93.5 billion (24.3 per cent of GDP) in 2007. Kuwait's total oil and gas exports rose by 39.9 per cent in the fiscal year of 2008 as against 7.9 per cent in 2007. Its current account surplus rose to \$70.6 billion in 2008 from \$50 billion (44.7 per cent of GDP for both years) in the previous year.

The strength of the US dollar is dependant on the strength of its current account. The current account deficit stood at 4.9 per cent of the GDP at the end of 2008. While this deficit is sizeable, since October 2009 it has shown a declining trend. This is only to be expected as savings would have risen and domestic consumption contracted, following the economic downturn. The current account deficit is projected to shrink to 2.2 per cent of the GDP by the end of 2010 (IMF). A similar trend holds true for the merchandise trade balance as well.

But US domestic consumption will eventually get back on track. This consumption would be met through increased imports. If the US fails to generate any significant increase in demand for its exports by then, the current account deficit will again widen. Such a deficit can become unsustainable, especially in light of the fact that the US has already incurred a huge budget deficit in its efforts to contain the financial crisis. This will make a sharp downward adjustment in the dollar necessary.

While temporary downswings may boost the current account surpluses of Saudi Arabia and Kuwait, a permanent downward revision will undermine the real value of their dollar reserves. In the immediate future, a sharp downward revision of the dollar is not very probable. Given this scenario, Saudi Arabia and Kuwait are unlikely to strain their relationship with the US by switching over from petrodollars. Rather than globally undermining the dollar, what would be more feasible is a strategy where by they pull out or divert more of their investment from US to other markets.

Parvathi Jayamohan

¹ All \$ figures are in US dollars.

The Barefoot Approach to Rural Development in Africa

Facilitating Sustainable Development and Effective Aid



Development assistance will continue to become an increasingly important aspect of Indian foreign policy in the years ahead. The main objectives of aid are to facilitate economic development and strengthen foreign relations. Directing limited resources for foreign aid as effectively as possible is crucial for the Government of India.

The Indian Technical and Economic Co-operation (ITEC) Civilian Training Programme, administered by the Technical Co-operation Division of the Ministry of External Affairs, has been engaged in capacity building and human resource development since 1964. The ITEC Programme funds the training of thousands of participants from developing countries annually in IT, management, rural development, government, renewable energy, and other specialties. One course, however, is particularly unique – the training of illiterate and semi-literate rural women to become solar engineers at Barefoot College.

Barefoot College has been training rural, uneducated, African women to become solar engineers at its campus in Tilonia, Rajasthan since 2004. Participants from twenty African countries, including Ethiopia, Kenya, Tanzania, Mauritania, Uganda, Malawi, Benin, Rwanda, Sierra Leone, and Mali have participated in the Barefoot solar engineering course. The women are trained to build solar electrification systems, including several types of circuits (e.g. a charge controller, an inverter circuit, etc.), in just six months. After completing the course, the equipment the women build is shipped to their villages where it is used to electrify the houses in their community. The participants in the course leave with the ability to install, maintain, and repair the equipment, ensuring sustainability.

The Barefoot philosophy of teaching involves only practice and no theory; trainees need no educational qualifications. Additionally, Barefoot solar engineers learn without verbal language, other than learning the English names of essential parts (e.g. capacitor, resistor, etc.). Instead, Barefoot solar engineers learn by seeing and doing. They construct solar electrification units that are able to power two light bulbs for four to five hours with a 40-watt panel or light bulbs, a fan, and cell phone with a 75-watt panel.

Barefoot College does not award certificates of any kind. Instead, trainees' validation comes from their community as a result of their abilities. According to the Barefoot philosophy, certificates are only useful for getting jobs in cities, which is not what is intended for the trainees. Rather, those who become solar engineers are meant to stay in their village and work for their community. Barefoot only trains women because, their experience suggests that women show a greater commitment to the community and are more likely to remain in and work for the community.

The Barefoot approach functions at the grassroots, community level. A central element of the Barefoot model is community involvement; interaction and listening to the community is an important part of its approach. The community chooses the participant/s to be trained, the participants have roots in and work for the community, the community has a financial stake in the project, and the community determines what type of electrification systems are required (i.e. 40-watt or 75-watt solar panels). Community involvement and ownership in the solar electrification projects is essential for the sustainability of the projects.

Commercial solar electrification of rural villages has not been as sustainable as the Barefoot approach because the systems require expensive repair and maintenance work to be done by a technician. By building capacity within the village, the community can repair and maintain the systems themselves. Typically, as a part of the Barefoot solar electrification process, villages donate the space (e.g. a small structure/room) to be the solar “workshop” of that village where repair work can be done, while increasing their stake in the project. Training a villager to maintain and repair electrification equipment is substantially more sustainable (i.e. cost-effective for the community) than merely transferring the technology and expecting villagers to pay technicians to maintain and repair the equipment. Moreover, the Barefoot approach can be replicated with the founding of training centres in Africa; Barefoot alumni have already started centres in Ethiopia and Sierra Leone.

In March 2010, a new, six-month ITEC course will begin on the Barefoot College campus in Tilonia. More than thirty participants from the Democratic Republic of the Congo, Chad, Tanzania, Kenya, Namibia, and Sierra Leone will train to become solar engineers. Many participants will be leaving their community for the first time in their lives. ITEC funds the transportation costs, course fees, and a modest stipend for course participants. The participants' communities and their governments, as well as several international development organisations (e.g. the UNDP, the Asian Development Bank, etc.) share the cost of the equipment that is used to solar-electrify the participants' villages. Initially, participating governments have been sceptical of the feasibility of training rural, uneducated women to become solar engineers; the programme, however, has had remarkable success.

Empirical findings suggest that rural electrification can have substantial economic and socio-cultural impacts.¹ Research has also shown that access to electricity increases worker productivity with the use of power tools.² Electrification enhances the ability to communicate with cell phones, radios, etc. as well.³ The majority of Sub-Saharan Africans live in rural areas where electrification levels are frequently below 5 per cent.⁴ Not only are households in need of electricity, but also schools and hospitals. Solar electrification provides a solution to rural, off-grid communities.

In addition to training participants to build solar electrification systems, Barefoot College is capable of training participants to build solar cookers. Solar cookers are expensive to ship, however, and funding to transport them to Africa is currently unavailable. Research indicates indoor air pollution (IAP) exposure because of cooking with traditional fuels (i.e. biofuels) to be "dramatically high".⁵ Furthermore, exposure to IAP has been found to significantly affect health risks.⁶ Increased use of solar cookers would reduce exposure to IAP.

Barefoot College's work addresses several Millennium Development Goals simultaneously. Rural electrification helps reduce poverty by enhancing opportunities to engage in income-generating activities (e.g. cooking at night rather than during daylight or craft making at night, etc.), while providing employment opportunities for the solar engineers.⁷ Barefoot helps to develop a global partnership for the sustainable development of the least developed countries.⁸ The training of solar engineers helps ensure environmental sustainability by integrating renewable energy practices into country policies and programmes.⁹ Barefoot's courses empower women and promote gender equality.¹⁰ Rural electrification can also help children complete their schooling¹¹ by allowing them to do schoolwork or take classes at night.

The Barefoot course, funded by ITEC, is a unique opportunity and approach to rural development, capacity building, and aid. The Government of India should continue to pursue and support such innovative, cost-effective, high-impact approaches to facilitate sustainable development as part of its foreign policy in order to strengthen its relationship with African countries. While it is not realistic for India to match other countries' (i.e. China's) aid to Africa monetarily, India could play a greater role in African development by focusing on low-cost, high-impact assistance to facilitate sustainable development using innovative approaches.

Michael Dickerson

¹ Barkat, Abul et al. 2002. Economic and Social Impact Evaluation Study of the Rural Electrification Program in Bangladesh. Dhaka: Human Development Research Centre. Pg 284.

² Kirubi, Charles et al. 2008. Community-Based Electric Micro-Grids Can Contribute to Rural Development: Evidence from Kenya. World Development. doi:10.1016/j.worlddev.2008.11.005. Pg. 11.

³ Jacobson, Arne. Connective Power: Solar Electrification and Social Change in Kenya. World Development. Vol. 35 (1): pg. 157.

⁴ Karekezi, Stephen and Waeni Kithyoma. 2002. Renewable Energy Strategies for Rural Africa: Is a PV-led Renewable Energy Strategy the Right Approach for Providing Modern Energy to the Rural Poor of Sub-Saharan Africa? AFREPREN. Pg 1.

⁵ Duflo, Esther et al. 2008. Indoor Air Pollution, Health and Economic Well-being. MIT: Poverty Action Lab. Pg. 17.

⁶ Smith-Sivertsen, T. et al. 2004. Reducing Indoor Air Pollution with a Randomized Intervention Design – A Presentation of the Stove Intervention in the Guatemalan Highlands. Norsk Epidemiologi. Vol. 14 (1): 137-143

⁷ Goal 1 and Target 1B

⁸ Goal 8 and Target 8B

⁹ Goal 7 and Target 7A

¹⁰ Goal 3

¹¹ Target 2A

Book Review

Time to Move beyond GDP

A Review of the Report on Measuring Economic Performance and Social Progress



“GDP is an attempt to measure what is going on in our society, which is market production. It is what I call GDP fetishism to think that success in that part is success for the economy and society,” says Joseph Stiglitz, Chair of the Commission on the Measurement of Economic Performance and Social Progress. In 2008, French President Nicolas Sarkozy, dissatisfied with the available tools of economic assessment and concerned about the increasing gap between the information contained in aggregate GDP data and what counts for common people’s well being, created the Commission, co-chaired by Joseph Stiglitz and Amartya Sen.

The recent financial crisis has exposed the inadequacy of the tools that economists have relied upon for so long to assess societal well-being. GDP had failed to account for the public health impact of environmental degradation and the social costs of joblessness. Neither could GDP foretell the recent global financial crisis that broke out with such force that it swept away banks, jobs and homes. In the recent massive property market bubble in the US, the price of assets, properties and shares moved so unrealistically that it created a false illusion of success. GDP was measured using market prices, and given the overpricing of assets, particularly real estate, it sent out misleading signals of societal well-being. What we measured was wrong and, therefore, what we did was wrong.

The other more popular alternative to GDP, the Human Development Index (HDI) measures the average achievements in a country in three basic dimensions of human development: a long and healthy life, knowledge and a decent standard of living. But this composite index, too, may not be comprehensive enough to capture all the facets of human development. Data limitations pose a constraint on its estimation and different methodologies may be used to address these constraints.

There is, thus, an urgent need to adopt new assessment tools that incorporate a broader concern for the well-being of people than mere economic growth.

The Commission, which submitted its report on 15th September 2009, has highlighted the need to broaden the coverage of statistics in the light of the recent crisis. The authors argue that ‘those attempting to guide the economy and our societies are like pilots trying to steer a course without a reliable compass’. The main message of this report is that the time has come for our measurement system to shift emphasis from measuring economic production to measuring people’s well-being and sustainability. But that does not in anyway undermine the importance of GDP and production measures. In fact, the Commission recognises that there is no single measure that can encompass everything. It, instead proposes a dashboard of dozens of indicators, which can be used to construct composites indices that capture what they want to measure (human security, safety, material well-being, health etc) Additional information required for the production of these relevant indicators of social progress and the measurement tools pose a great challenge.

The report looks at three issues in developing alternative metrics. The first identifies the limits of GDP as an indicator of economic performance and social progress, including problems with its measurement. GDP takes no account of depreciation or non-market activities; it ignores distribution issues and does not adequately capture improvements in the quality of goods and services. The commission repeats the old demand of finding an appropriate measure to estimate the environmental cost of production as GDP does not include environmental degradation.

The report strongly favours looking at income and consumption trends along with production.

It emphasises the need to track households' income and consumption, and not just economy wide trends as happens now. This is a relevant suggestion given that in OECD countries, real household income has grown at a lower rate than GDP per capita. The household perspective entails taking account of payments between sectors, such as taxes going to government, social benefits coming from government, and interest payments on household loans going to financial corporations. The commission suggests that when assessing material well-being, income and consumption should be looked at jointly with wealth. Measures of wealth are central to sustainability and, therefore, deserve prominence. Further, it recommends that to get a better sense of inequality, the entire distribution of income, consumption and wealth be given more importance than just the mean.

Conventional measures of GDP attribute poor economic performance (less income and growth) to a society that chooses to limit its consumption of material goods and enjoys more leisure. In its second section, the report turns its focus on improving measures of "quality of life" or "well-being". This is a multidimensional concept; which incorporates both objective conditions (income, consumption and wealth) and subjective measures. The Commission recommends steps to improve measures of people's health, happiness, education, personal activities and their environmental concerns. It focuses on getting reliable measures of social connections, political voice and insecurity that determine life-satisfaction. However, these subjective notions are tricky to measure and the commission does not come up with any one indicator that can capture all these aspects. Here, the report seems to be more appraisal-oriented than prescriptive. It does not give a very clear methodology on how to go about including these.

The final issue the report raises is that of sustainability. One of the more innovative features of the Stiglitz Commission's report is the way it calls for the inclusion in our metrics of different aspects of sustainability, not just environmental. Economic activity is sustainable if future generations can be as well off as the current one. Their well-being, in turn, depends on the stock of capital – physical, natural and human – that we pass on to them. Finding a single measure to assess sustainability is again a complex issue. Sustainability assessment requires a well-identified dashboard of indicators. One of the distinctive features of the components of this dashboard should be that they are interpretable as variations of some underlying stocks. The Commission proposes a stock approach to measuring sustainability by creating a monetary index of sustainability. Such an approach suffers from the absence of markets on which valuation of assets could be based. The report argues that environmental aspects of sustainability deserve a separate follow-up. However, the difficulty arises in turning these general principles into new tools of measurement.

Overall, the commission raises more questions than it answers. Though it is a comprehensive assessment of the limitations of existing data, its findings have made a very modest contribution to an old debate. GDP has been lambasted for years but we have still not found a suitable, globally acceptable alternative to it that would provide correct insights about societal well-being to the common man and to economists. The Commission proposes various dashboards of indicators but it does not come up with a quick and easy way to tabulate a new measure of well-being. The report needs to give more assistance on how to create a broader set of indicators that accurately capture both well-being and sustainability. However, it cannot be denied that the report is timely in the light of the recent financial crisis. Maybe this time, policymakers will realise the heavy price paid for their "GDP fetishism" and broaden the metrics to look beyond measures of market production. They will, hopefully, turn the crisis into an opportunity and work towards resolving this age-old problem with GDP statistics. With the political weight of Sarkozy behind this report and leading academics at the helm of it, the task will hopefully be taken with greater earnestness this time round.

Data Indicators

The Data Indicator section presents interesting and relevant economic data on the region. The objective is to pick up two different related economic variables in each issue and highlight trends and patterns that could be further researched into.

International trade has been affected by the global financial crisis in multiple ways, with decline in consumer demand and protectionist tendencies being two of them. Given this background we decided to calculate Hirschman Indices which would give us an indication of the extent of geographical concentration of exports and Tariff dispersion Indices which would give us an idea of the extent to which a country's tariffs are spread out thereby giving an indication of how protectionist it is in terms of its imports.

Hirschmann Indices

Countries	Hirschman Index-2008
Russia	0.213
Germany	0.214
South Africa	0.219
India	0.220
Thailand	0.227
France	0.228
United Kingdom	0.247
Pakistan	0.250
United State of America	0.256
China	0.264
Australia	0.311
Sri Lanka	0.316
Bangladesh	0.334
Saudi Arabia	0.532
Japan	0.567
Nepal	0.700
Canada	0.780
Mexico	0.803

Data Source: IMF Direction of Trade Database

We have calculated Hirschman indices for 18 economies. Economic theory argues that a more diversified export structure in terms of geographical destinations protects an economy from being affected adversely by shocks that impact their trading partners. Canada, Nepal and Mexico are the countries with the highest scores indicating that their markets are the least diversified. The results for Nepal and Mexico are intuitive since at a lower stage of development diversification is difficult. The fact that Canadian exports are also non diversified is an interesting result. On a slightly more detailed analysis we find that the markets for Canadian goods are mainly developed countries. Whether this is by choice or does it represent a more fundamental issues such as lack of competitiveness is something which needs to be looked into.

Trade Dispersion Indices

Countries	Latest Data Available	Agricultural Products (AG)			Non-agricultural Market Access (NAMA) Products		
		% of Non AV Lines	Simple Average	Tariff Dispersion	% of Non AV Lines	Simple Average	Tariff Dispersion
Japan	2008	3.03	11.02	9.48	0.18	3.38	4.19
United State of America	2008	18.95	11.61	34.24	1.75	3.60	4.28
Bangladesh	2007	0.00	19.92	10.59	0.00	3.75	6.90
Canada	2007	9.49	4.92	9.37	0.00	3.77	3.80
Australia	2009	0.00	1.39	8.65	0.00	3.89	4.00
European Union	2008	29.00	8.21	7.53	0.00	4.22	4.03
Saudi Arabia	2008	1.87	4.23	4.48	0.00	5.34	2.68
South Africa	2007	10.63	8.61	9.59	0.36	7.83	9.94
China	2008	0.55	15.22	10.79	0.09	8.80	4.78
Thailand	2007	32.66	25.34	17.65	5.08	9.29	12.19
India	2008	0.14	34.49	28.76	6.76	9.37	7.72
Sri Lanka	2007	4.85	22.27	12.12	0.84	9.49	8.80
Russia	2001	26.97	10.06	5.07	8.11	10.26	5.19
Nepal	2008	6.88	12.89	9.53	0.29	12.35	9.34
Mexico	2007	3.24	23.37	36.84	0.01	13.43	7.96
Pakistan	2007	4.66	14.54	10.47	0.02	15.22	14.15

Data Source: WTO Tariff Database

The tariff dispersion index is a single number that measures how widely spread out are the tariffs in a schedule or part thereof. In other words, a high tariff dispersion index indicates that there is a lot of variation in the tariff schedule. Economists generally believe that a uniform tariff (with low dispersion) is more economically efficient. An alternative measure is to consider the difference between the maximum tariff and the minimum tariff. We have calculated tariff dispersion indices for select economies for both agriculture and NAMA. We have also looked at the percentage of non ad valorem tariff lines. A crucial issue that is being negotiated within the Doha round of trade negotiations is the conversion of non ad valorem lines to ad valorem lines. It can be seen from the above table that the extent of non ad valorem lines is higher in agricultural products rather than in non agricultural industrial goods. Further developed countries such as United States, European Union, Thailand seem to be the economies that have a high percentage of such tariff lines. Specific duties are generally not preferred since they are more opaque than ad valorem and can discriminate between exporters on the basis of their value.

In terms of tariff dispersion in agricultural commodities, it can be seen that countries such as US, Mexico and India have the highest tariff dispersion indicating that they might have high tariff peaks on certain commodities. In the case of US it seems to be on tobacco and oilseeds and for India on grape wine and spirits. For Mexico it can be seen that there are various high bands of tariffs raising the question whether the tariff structure is randomly high or whether there is a logic to it. Regarding industrial goods it can be seen that Thailand and Pakistan have the highest tariff dispersion. For Thailand the tariffs seem to be high for the motor vehicle sector. Thailand has been in the process of phasing out these high tariffs but this data shows that tariffs in this sector are still relatively high. For Pakistan the high tariffs are in the sector of motorcycles which again seems to be a point of concern in WTO negotiations.

Though much more research and analysis is needed before we can make further conclusions what seems to emerge primarily is that protection within agricultural sector is much higher than that in the industrial sector.

About ICRIER

ICRIER – established in August 1981 – is an autonomous, policy-oriented, not-for-profit, economic policy think tank. ICRIER's main focus is to enhance the knowledge content of policy making by undertaking analytical research that is targeted at improving India's interface with the global economy. ICRIER has nurtured its autonomy by establishing an endowment fund, income from which enables it to pursue its priority research agenda. ICRIER receives other financial support from a number of sources including the Government of India, multilateral international institutions, bilateral agencies and the private sector.

A medium-term strategy that spells out ICRIER's vision and focus areas can be found on its website www.icrier.org. ICRIER has formulated a code of conduct for undertaking research.

To effectively disseminate its research findings, ICRIER organises workshops/ seminars/ conferences to bring together political leaders, policy makers, academicians, industry representatives and media persons to try and generate a more informed understanding on issues of major policy interest. ICRIER invites distinguished scholars and policy makers from around the world to deliver public lectures on economic themes of interest to contemporary India.

ICRIER's founding Chairman Dr. K.B. Lall, led the organisation since its inception till 1992 when he handed over the Chairmanship to Mr. R.N. Malhotra (1992-1996). Mr. Malhotra was followed by Dr. I.G. Patel who remained Chairman from 1997 until his demise in July 2005. ICRIER's current Chairperson is Dr. Isher Judge Ahluwalia. Amongst ICRIER's founding members are Dr. Manmohan Singh, Dr. C. Rangarajan, Dr. M.S. Swaminathan, Dr. Jagdish Bhagwati, Dr. R. J. Chelliah, Mr. Muchkund Dubey, Prof. Deepak Nayyar etc.

ICRIER's highly qualified in-house team of about 50 researchers is led by Dr. Rajiv Kumar, D.Phil in Economics from Oxford University and Ph.D from Lucknow University. The team includes several Ph.Ds from reputed Indian and foreign universities. In addition, we have around 25 external consultants working on specific projects. ICRIER's office is located in the prime institutional complex of India Habitat Centre, New Delhi.

Regional Insights Team



About Us

ICRIER started the Regional Insights initiative in 2008.

The rationale is that research on India's relations with other countries will have to take on board the increasing demand being placed on India for a major role in international discussions on evolving a new global social, economic, financial and environmental architecture. In this context, each researcher has adopted a country/region. The Team will track and monitor developments in the major countries, regions, economic blocks and India's neighbours.

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ICRIER was established in August 1981, and it has successfully completed 28 years as an autonomous, premier policy-oriented, not-for-profit research institution.