FINANCING FOR DEVELOPMENT: THE IMPLICATIONS OF THE ZEDILLO REPORT FOR SOUTH ASIA

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August 18, 2001

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Foreword

Development goals are being broadened and redefined worldwide. This naturally raises the question of how to find finances for addressing the new challenges of development. In January 2001, the UN Secretary General, Mr. Kofi Anan set up a high level panel to address the questions relating to the financing needs of development. The panel was chaired by Mr. Ernesto Zedillo, former President of Mexico and had 10 other eminent persons as members. Dr. Manmohan Singh, former Finance Minister of India was a member of the panel. Dr. John Williamson was the Project Director of the panel.

In this first series of SANEI lectures, Dr. John Williamson spoke on the implications for South Asia of the report on financing for development as prepared by the high level panel. The lecture was hosted by The Bangladesh Institute for Development Studies, Dhaka on behalf of SANEI. The important issues raised in this lecture provide very useful background to those who are preparing for the international conference in Monterrey, Mexico which is being convened by the United Nations in March 2002, and others who would like to gain information on this important emerging area.

Isher Judge Ahluwalia
Director & Chief Executive
ICRIER

Financing for Development:
The Implications of the Zedillo Report for South Asia[1]

In March 2002 the United Nations will convene an international conference in Monterrey, Mexico, that will discuss the whole array of subjects concerned with the financing of development. This conference will be in the tradition of the Earth Summit in Rio de Janeiro in 1992, the 1994 Cairo Population Summit, the 1995 Beijing Summit on Women and the Copenhagen Summit on Social Development, and the 1996 Summit on Human Settlements in Istanbul. It responds to a wish that has been expressed by many developing countries for a long time, which have argued that discussing what needs to be done on the environment or population or whatever without any matching consideration of the financial means to attain the desired ends was a somewhat hypocritical exercise.

Considerable diplomatic effort has already been expended in preparing for this conference, in the form of meetings of a Preparatory Committee of UN Ambassadors and the discussion of a report of the UN Secretary-General (2000) that identified and discussed a large number of the relevant issues. The Secretary-General also convened a High-Level Panel charged with considering, within a more limited group and free of the constraints imposed by official positions, the range of issues involved. This Panel was chaired by the former President of Mexico, Ernesto Zedillo, and contained Manmohan Singh plus nine other

[1] A SANEI Distinguished Lecture to be delivered in Dhaka on 27 August 2001.

eminent persons from around the world, including Robert Rubin (the former US Treasury Secretary) and Jacques Delors (the former President of the European Commission). I had the honour of serving as the Panel's Project Director (which means in practice that I drafted what is called the Technical Report), and it is about this report, and its relevance to South Asia, that I propose to speak to you today.

Scope of the Report

The first thing that struck me when I was invited to serve as Project Director was the extraordinary breadth of the issues under consideration in the Financing for Development (henceforth FfD) exercise. The Secretary-General's report divided its discussion into six sections: "Domestic Financial Resources", "International Private Flows", "Trade", "International Development Cooperation", "Debt", and "Systemic Issues". The first section was in reality even broader than suggested by its title: it dealt with a whole range of internal policy issues that any developing country needs to confront, from governance through macro policy and public finance to the financial system. (Actually it is even broader than that, for it contains a couple of paragraphs addressed to the large industrial countries.) I was surprised (but gratified) to find that financing was deemed to include trade. "Systemic Issues" concern possible reforms to the system of international economic governance, in the international financial institutions (IFIs) and the relations of the UN and the IFIs, and needs for expanded cooperation in areas such as tax policy.

This broad coverage reflected a strategic bargain that lay behind the FfD exercise. Developing countries had traditionally resented the intrusion of international institutions into their domestic policy process: while many may have accepted structural adjustment programmes as the price of getting money, few welcomed them or owned them. For their part, developed countries resented the demands of developing countries to acquire an influence in the IFIs to which their economic weight did not, so they argued, entitle them. The strategic bargain was for both sides to acknowledge some legitimacy in the other's position. Developing countries recognized that it was reasonable for the international community to take an interest in whether they were pursuing the sort of best-practice policies that can reasonably be expected to nurture development, and developed countries recognized that the present form of the IFIs is not sacrosanct for all time.

Those of us who regard ourselves as liberal internationalists, sympathizing with the objectives of developing countries but regretting that so many of them jeopardize their prospects by being too tender on their populists, could only welcome this development. The challenge that confronted the Zedillo Panel was how to use the space that seemed to be opening up in order to develop an agenda that might be too bold to win immediate acceptance in an inter-governmental forum while avoiding being carried away in idealistic dreams that would invite ridicule. Judging by the lack of impact of the report so far, it is not clear that we hit the right note, but that does not imply that the agenda sketched by the Panel is not the right one for achieving the International Development Goals.[2] When we started work, I think it is true that most of us were not particularly focused on these, but, as our work progressed, we increasingly used them as a framework to guide our cost estimates and inform our policy recommendations. Our report may be viewed as an attempt to delineate what will be needed if the world is to achieve these goals, which have been widely endorsed by the international community.

Domestic Resource Mobilization

The Panel started where the Secretary-General's report did, with a wide-ranging though succinct discussion of the domestic policies that are needed if development is to succeed. This covers a broader range of subjects than the conventional wisdom of just over a decade ago that I attempted to summarize in my first rendering of the "Washington Consensus" (Williamson 1990). Macro discipline and competitive markets are certainly there, although the rationalization of the latter appeals to Amartya Sen rather than Adam Smith. But so are good governance, the sort of measures that empower the poor to take

[2] The International Development Goals for 2015 adopted by the UN Millennium Summit in September 2000 are: to cut in half the proportion of people living in extreme poverty, of those who are hungry, and of those who lack access to safe drinking water; to achieve universal primary education and gender equality in education; to accomplish a three-fourths decline in maternal mortality and a two-thirds decline in mortality among children under 5; to halt and reverse the spread of HIV/AIDS and provide special assistance to AIDS orphans; and to improve the lives of 100 million slum dwellers.

advantage of markets, the need for an adequate level of public expenditure and therefore for adequate tax revenue, and the importance of a diverse, well-functioning, competitive financial system. In the latter context, the report pointed in particular to the potential of a funded, defined-contribution pension system to raise saving with a limited adverse effect on incentives, but recognized that such a programme would need to be complemented by a tax-financed scheme to assure a minimum pension for all elderly persons.

The Panel also stressed that achieving this ambitious agenda is not simply a matter of political will. Many developing countries lack institutions capable of implementing much of this agenda. These countries will need to focus major national efforts on capacity building: developing a competent and corruption-free public service, nurturing a strong civic society and a vibrant and independent press, and promoting a strong indigenous private sector. Technical assistance as currently organised is not providing the help that it ought to be doing, and needs a new look by the international community.

Most of this seems to me to be highly relevant to South Asia. On the whole South Asia's record in terms of maintaining macro discipline has not been bad, although budget deficits have long been a source of acute concern in Pakistan and Sri Lanka, and now are in India as well. The institutional infrastructure for a market economy is still weak throughout the region, perhaps most particularly in regard to the ability to use the legal system to enforce financial contracts. One of the methods of empowering the poor that we commended, namely micro-credit, was largely pioneered here in Bangladesh. But even in Bangladesh, and certainly in the rest of South Asia, there is a long way to go to achieve universal access to micro-finance, especially among the poorest of the poor. And the record in terms of directing public spending toward education, health, nutrition, the rural sector, and other basic social programmes, which is surely the most important way of empowering the poor, is not good, to put it mildly. The financial sector is another weak area: while India has made remarkable strides in a few places, notably in modernising its equity market, the banking system remains problematic everywhere, nowhere more than in Bangladesh. The need for pension reform is already pressing in Sri Lanka, and the opportunity to raise savings by instituting funded, defined-contribution pension schemes is present in all the countries of the region. And all the five larger countries face a challenge in creating or restoring a competent and corruption-free public service.

Trade

The Panel took the view that trade is essential for rapid and sustained growth. It welcomed the recent trade liberalization by developing countries, but noted that much of the remaining protection in developed countries (notably in agriculture and clothing) is directed against the exports of developing countries. It suggested two approaches for achieving better market access by developing countries.

One is to initiate a new trade round at the forthcoming ministerial meeting of the WTO in Qatar next November. The Panel sketched what it saw as necessary elements of any agenda that would justify using the term "development round" to describe a new negotiating round. These are: finishing the business of the Uruguay Round; strengthening the rules of the WTO system (notably by bringing anti-dumping actions within WTO disciplines); liberalizing trade in agricultural products; reducing tariff peaks and tariff escalation; reforming trade-related intellectual property rights (TRIPs) as agreed in the Uruguay Round; legitimating limited, time-bound protection of infant industries; and taking a new look at liberalizing migration.

The second approach to improving market access was confined to the least-developed countries. The Panel called for generous financing of the "Integrated Framework" that has been created to build up their capacity of trade negotiation and promote their export diversification. It also urged the European Union to implement fully its "everything but arms" initiative[3] and called on all other industrial countries to at least match the EU initiative. And it suggested that industrial countries could implement immediately, so far as the least developed countries are concerned, all their Uruguay Round promises that are still outstanding (of which the important one is abolition of the Multi-Fibre Arrangement, the MFA).

The Panel also discussed the problems of countries that remain overwhelmingly dependent on primary commodity exports. It suggested reversing the 1980s' scaling back of the IMF's Compensatory Financing Facility and it endorsed launching a scheme for commodity risk management, which would essentially insure prices for a

[3] It should really be called "everything but arms, bananas, rice, and sugar, at least for now"!

number of basic crops a few months in advance on near-commercial terms. Those measures might do something to alleviate the cyclical problems that commodity producers face, but the Panel recognized that they would not address the problem of a secular decline in real commodity prices—a problem which, it argued, would be resolved only when development had proceeded far enough to avoid new producers entering already-crowded markets even when their prospect is merely that of scratching out a bare subsistence living.

Once again, let me briefly examine how relevant these suggestions are to South Asia. The first thing to appreciate is that, in sharp contrast to Africa, South Asia is not primarily an exporter of primary commodities. At least outside of South Asia, people are still frequently surprised to learn that Sri Lanka is not primarily an exporter of tea, nor is Bangladesh primarily a jute exporter. On the contrary, South Asia's exports in 1999 consisted 79% of manufactures, essentially the same as in East Asia (81%) and the industrial countries (82%), and far higher than in any other region of the developing world.[4] Pakistan's exports are primarily resource-based, in the sense that its industrial exports are predominantly of cotton goods and cotton is produced locally, but even this is not true of the other countries of South Asia. Hence the Panel's suggestions to help commodity exporters, and its emphasis on the need to include agricultural liberalization on the agenda of a new trade round, and its complaint about the EU's delay in liberalizing imports of bananas, rice, and

[4] And with the growing importance of software exports from India, the region's export profile is beginning to look even more modern than those figures would suggest.

sugar from the least developed countries, are all of limited relevance to the region.

In contrast, most of the other proposals are highly relevant. Bangladesh and Nepal, as well as Bhutan and the Maldives, are classified as least developed countries, and would therefore stand to benefit from the proposals to bolster the Integrated Framework, replicate “everything but arms” in other industrial countries, and accelerate the phase-out of the MFA. Anti-dumping actions are currently under way against exports of Bangladesh and India, and they are surely an important latent threat when the MFA is disbanded. Tariff peaks will be a big issue in the region’s major export product, namely clothing, after the MFA goes. TRIPs has emerged as the principal area where the Uruguay Round foisted damaging obligations on developing countries, and there is a clear need to seek a better balance between the incentive to innovate on the one hand versus affordable access to knowledge whose use would involve zero opportunity cost to society on the other. Migration is critically important in all five of the larger South Asian countries.

Private Capital Flows

The Panel took the view that developing countries also stand to benefit from the other main form of globalization, by tapping the international capital market. The report outlined the sorts of conditions that are needed to attract FDI, and also commended the Secretary-General’s Global Compact as laying out the requirements for foreign investors to behave as good corporate citizens.

And it pointed out that any desire to tap foreign savings to finance domestic private enterprise or government deficits requires other forms of capital inflow, in the form of portfolio investment or bank loans. It recognized the danger that such flows could precipitate crises if they were suddenly withdrawn, and therefore urged a cautious approach to capital account liberalization. It noted a couple of ways in which industrial countries still impede portfolio outflows and urged that these be removed. But it remained silent on the principal outstanding issue in the ongoing discussions on reform of the international financial architecture, namely whether and when and how to organize standstills on some or all debt service payments in the event of a capital account crisis.

International Development Cooperation

The report had much more substantive things to say about the role of international public finance. To begin with, it offered a taxonomy of the four vital roles which it argued need to be filled by international public finance, no matter how much private capital may dominate total financial flows to developing countries in the future. These are:

- In helping to initiate development in low-income countries, which it identified in the next few years with achieving the International Development Goals.
- In coping with humanitarian crises.
- In accelerating recovery from financial crises.

- In providing global public goods[5], of which it identified the principal examples as peacekeeping; the prevention of contagious diseases; research into tropical medicines, vaccines, and agricultural crops; the prevention of chlorofluorocarbon emissions; the limitation of carbon emissions; and the preservation of biodiversity.

The report argued that a primary aim of the Financing for Development conference should be to secure adequate mechanisms to fund these four roles on an adequate scale. In particular, every country that seriously pursues the International Development Goals should be assured that their achievement will not be thwarted by a lack of external finance.

It also tried to quantify what this principle would imply. It sought to do this without inviting the accusation that it believed problems could be solved by throwing money at them, by emphasizing that aid is worthwhile only where the policy and institutional environment is favourable, and that its estimates are conditional ones of how much it would cost if all countries create the appropriate environment. A summary of existing estimates, partial and incomplete though they are, suggested that a figure in the vicinity of $50 billion a year was the right order of magnitude for

[5] Pure public goods are both nonexcludable (the buyer cannot prevent others consuming them) and nonrival (one person's consumption of the good does not diminish that of others). These characteristics imply that no isolated, self-interested individual will have an incentive to pay for these goods: collective purchase is necessary. Similarly, no individual self-interested country has an incentive to pay for global public goods: collective international action is needed if they are to be supplied in appropriate quantity.

achieving the International Development Goals. A decent level of assistance in humanitarian disasters would require an extra $3 or $4 billion per year. And seriously addressing the need for global public goods might require an extra $15 billion or so, without allowing anything much for what is bound to be by far the most costly item on the agenda, namely limiting carbon emissions. Rough and ready as these estimates are, they suffice to make the point that international public finance needs a substantial boost in resources.

In turning to what might be done to increase the available sums, the Panel first considered how much was likely to be yielded by the HIPC Initiative. Even if this is financed entirely by additional ODA (official development assistance, i.e. aid), as has been promised, the impact will be quite modest compared to the needs just summarized. The official estimate is that the enhanced HIPC Initiative will reduce debt service by $1.1 billion a year from what would otherwise have been paid, and by $2.4 billion a year from what would have been due. But at best, this will offset only a small part of the estimated shortfall in ODA, and this suggests one reason why the question is still being posed as to whether debt relief has been pushed far enough. The Panel concluded that more will indeed need to be done to help the HIPCs in one way or another, but there was some disagreement as to whether a new debt relief agreement was necessarily the best way to bring that additional relief. If that were the path to be chosen, it would be important to make sure that the financing for it is truly additional, for it is easy to see ways in which otherwise the bill could in reality end up being paid by countries like Bangladesh (in the form of reduced aid flows).

The obvious alternative way of bringing additional resources into the picture would be for the industrial countries to increase ODA. Most of them endorsed the UN target for giving 0.7% of GNP in aid many years ago, but only 5 small countries (the largest being the Netherlands) achieve the target, and the largest industrial country is at the bottom of the league table with ODA of a mere 0.1% of GNP. Actually achieving the target would increase ODA by some $100 billion per year (a near tripling), so the Panel indeed called for the target to be achieved. But it was not under the illusion that its call would reverberate around the White House and the US Congress so as to result in a prompt septupling of the US aid budget. Hence the report also called for the launching of a Campaign for the Millennium Goals that might track the progress being made towards achieving the goals, highlight shortfalls, and identify remedial actions. The hope is that such a campaign could combine the enthusiasm that the debt campaigners brought to bear in their successful campaign for HIPC with the professional expertise of the key international agencies and the financial support of private foundations, and thus achieve a revival of public support for ODA in key industrial countries like the United States.

Even if the sums raised for ODA were to increase enough to meet the cost of achieving the International Development Goals, it is not clear that it would be proper to use those funds to meet the growing need to finance global public goods. And if ODA does not increase much, then the world will need to think about ways of supplementing ODA in financing development. Hence the Panel also addressed the possibility of raising what are known as "new and innovative sources of finance", i.e. of imposing some form of international taxation. In the end the Panel could not agree to *recommend* establishment of an international tax designed to generate revenue for financing the supply of global public goods, but it did recommend that the Monterrey conference should *consider* whether to establish such a tax.

It also considered the form that such a tax might take. The leading candidate here has long been the Tobin tax; that is, the longstanding proposal of Nobel laureate James Tobin to impose a "small" tax on all transactions in the foreign exchange market. This is a cause that has attracted astonishing support from some of the anti-debt crusaders, perhaps particularly the church-based ones, in a number of developed countries. Vijaya Ramachandran, who was the member of our Panel's Secretariat whose e-mail address was released to the public, received between 1,000 and 2,000 e-mails in support of the Tobin tax, and virtually none on the vast range of other issues that we were charged with discussing. The attraction is presumably that this is seen as a way of extracting resources for worthy ends from people who are pursuing the unworthy activity of speculating in the foreign exchange market.

The only serious intellectual attempt that I know of to come to grips with the Tobin tax was at a conference inspired and in part organised by the late Mahbub ul Haq in 1995 (reported in ul Haq, Kaul, and Grunberg 1996). The Overview to that volume developed the view that the tax would kill two birds with one stone: raise revenue for international good causes at the same time as it curbed speculation. My own view at the time was that it was an imaginative way of raising revenue but essentially irrelevant so far as curbing speculation is concerned[6], and I have never seen any persuasive evidence that the latter view was in error. I became less sanguine about the potentiality of the tax in raising revenue when I came across the new literature on the micro structure of foreign exchange markets (Lyons forthcoming). But I suppose that one might still be able to get maybe $10 billion a year from the tax, assuming one could get universal agreement among the main financial centres to impose it[7]. In any event, after reviewing the arguments the Panel decided to sit firmly on the fence and called for further rigorous study.

The Panel also looked at alternative forms that international taxation might take. It noted proposals such as to tax use of the "global commons" (the high seas, Antarctica, outer space), and then focused on the possibility of taxing carbon dioxide emissions. The attraction of this is similar to that claimed for the Tobin tax, in that it would kill two birds with one stone. Specifically, it would discourage carbon emissions (that is, help supply an important global public good) at the same time as raising revenue. A carbon tax could be either a supplement or an

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6 This is because the speculative threat to a currency is determined by the stock of short-term assets that can be withdrawn, not the flow in and out that would be penalized by a Tobin tax. There is no reason why someone holding assets for 24 hours need go through the foreign exchange market every day; they can perfectly well roll their claims over once a day. The vast bulk of transactions in the foreign exchange market are very short-term (reversed within a few minutes), and are not what I would have described as speculative.

7 I thought Peter Kenen had made the case reasonably convincingly in the Tobin tax volume that such limited agreement was all that would be needed, though this did not convince all members of the Panel.

alternative to the Kyoto approach of setting limits for national emissions. Most economists will like the fact that it is a more market-friendly approach than Kyoto. The specific form of tax that the Panel suggested was an internationally agreed minimum rate of tax on the consumption of each fossil fuel, with the tax rates calibrated to reflect each fuel's propensity to add to global warming. Developing countries could be subjected to the same obligation to ensure that each fossil fuel bears a minimum tax rate (and therefore, implicitly, that it is not subsidized), but excused the obligation of paying the receipts from a base rate of tax over to the international community.

In addition to exploring mechanisms for increasing ODA and perhaps instituting some form of international taxation, the report revisited the potential role of the SDR. It did not take up the ideas that have been discussed in recent years for allowing special SDR issues to finance IMF crisis lending, because it did not identify a great likelihood of the IMF facing a liquidity shortage. Instead, it went back to the logic that was originally used to justify inventing the SDR, which is the desirability of being able to satisfy the trend increase in the demand to hold international reserves without the need for some countries to run current account surpluses or to borrow and other countries to build up short-term debts. It pointed to the large collective reserve accumulation by developing countries in recent years as tantamount to reverse aid, and urged a resumption of SDR allocations.

The report then turned to a consideration of questions concerning how ODA is spent. It made three points. The first is that aid should be distributed among aid recipients in a way calculated to maximize its impact in reducing poverty. That means giving it to countries that have a lot of poor people and that have in place the policies and institutions that will make aid effective in reducing poverty, and scrapping the past tendency to give aid for export promotion or to promote foreign policy objectives.

The second suggestion arises from a concern about the escalating costs of complying with donor requirements. Donors have in recent years increasingly imposed a host of requirements on aid recipients concerning governance, official procurement practices, anti-corruption measures, macroeconomic discipline, the environment, social spending, gender equality, human rights, child labour, and so on. Worthy as each of these causes is individually, collectively they impose a crippling burden on the fragile political and administrative systems of most aid recipients. The "common-pool proposal" (due to Ravi Kanbur and Todd Sandler 1999) is intended to provide an escape from this dilemma. They envisage each potential aid recipient elaborating its own development strategy, programmes, and projects, primarily in consultation with its own population but also in a dialogue with donors. The country would then present its plans to the donors, who would put unrestricted financing into a common pool of development assistance to the extent that they judge the country's intentions merit their support. This, together with the government's own resources, would finance the overall development strategy. Tying would be abolished; the transactions costs of receiving aid would fall sharply; and recipient countries would get the responsibilities of ownership.

The third suggestion is to reduce the cost of servicing IDA loans. The interest rate on these is already nominal, so the suggestion made by the Panel was to lengthen the maturity to 99 years and the grace period to 40 years. The objective was to ensure that poor countries do not again become unable to service their debts and thus require a repeat of the HIPC Initiative. Since the Panel reported, President George W. Bush has advanced an alternative proposal with the same objective: he proposed that half of all IDA loans should be given as grants. That has one advantage and one disadvantage as compared to the Panel's proposal. The advantage is that it would enable the World Bank to finance NGOs, rather than being restricted to entities for which the government is prepared to give a guarantee. The disadvantage is that the Bank would have to make an extra—and highly divisive--decision every time it approved an IDA operation, namely whether to make a credit or a grant.

So much for the proposals made by the Zedillo Panel. What would they imply for South Asia?

Consider first the issue of extending the HIPC Initiative by giving deeper debt relief. "Drop the Debt", the successor organisation to Jubilee 2000 in campaigning for debt relief, has suggested that all multilateral claims on HIPCs should be cancelled, and that this should be paid for by the Bank drawing on its reserves and the IMF drawing on its gold holdings. The latter suggestion seems to me an excellent one (though to my regret it was not endorsed by the Panel), but the former one would almost inevitably be at the expense of South Asia, which does not at present contain any HIPCs. If IDA lending were curtailed as repayments to IDA declined, then Bangladesh would be among the victims. If the Bank curtailed IBRD lending to match the lower level of its reserves, then India and Pakistan would be hit. The same would be true if the IBRD raised its interest rate to replenish its reserves, or if the market raised the margin at which the Bank could borrow. It is only if one believes that the Bank sits on more reserves than it needs, to satisfy the egotistical whims of its managers, that this proposal offers a free lunch. Drop the Debt has partially acknowledged these problems by proposing to extend the number of HIPCs to include Bangladesh and Pakistan. But it has not proposed including India, which has been too prudent a borrower to qualify as highly indebted, and which would therefore be even more disadvantaged through the mechanisms described above. The bottom line is that South Asia has a strong interest in ensuring that any expansion of HIPC is fully financed by additional ODA, as called for by the Panel. If that were satisfied, then an expansion of HIPC that involved increasing the number of countries covered could be strongly advantageous to those countries of the region that were included.

As still the second poorest region of the world, South Asia is a major recipient of aid, and would therefore stand to benefit from any impact that the Panel's recommendations for increasing aid, and for a Campaign for the Millennium Goals, may have. Similarly, it would expect to benefit from any financial pickings that may come from a Tobin tax or a carbon tax. But whereas the ancillary benefits of a Tobin tax would be irrelevant for the region (even if they were realized, about which I have expressed my scepticism), any impact that a carbon tax might have in mitigating climate change would be highly positive for the region. The Maldives, in particular, risks being completely inundated, except perhaps for one island, by the second half of this century, while the estimates I have seen are that Bangladesh stands to lose around 13% of its already crowded land area on present trends.

A resumption of SDR allocations would also enable the countries of the region to build up their reserves without sacrificing real resources or increasing commercial borrowing. This would be particularly welcome in Bangladesh, given its current inadequate level of reserves. But it would be important to recognize that SDRs come on relatively hard financial terms; their interest rate is the average of the short-term rate on the four currencies that compose the SDR basket, not near-zero as on much of Bangladesh's current borrowing. Any country that allowed its reserves to fall below its cumulative allocation would therefore need to build up the capacity to service the resulting debt.

The proposal to distribute aid according to the two criteria of the prevalence of poverty and the presence of conditions that make aid effective in reducing poverty is one that would benefit South Asia. It will not surprise you to learn that poverty is still acute in the region, but those who have been berated by people like me in my World Bank days for doing too little to improve policy may be surprised to learn that I think the second condition would also work to South Asia's advantage. I do not intend to withdraw any of the things I said on this topic in the past: I continue to believe that the region could grow significantly faster if its politicians displayed more courage in implementing the policy reforms that they know to be needed when they are in office, and in supporting what they know to be needed when in opposition. But the fact is that policies in South Asia are on average a good deal better than in the other two main aid-receiving areas of the world, namely Sub-Saharan Africa and the economies in transition, which is why South Asia grows so much faster than they have been doing. As a matter of fact, a recent World Bank study that asked what Africa would need to do to achieve the goal of halving poverty by 2015 argued that three things were needed: a more efficient allocation of aid among countries, to focus it on those countries with much poverty and good policies; another $10 billion a year of aid; and action to improve policies—at least to the average level in South Asia! (Collier and Dollar 2000).

For all their shortcomings, I also believe that the governments of South Asia could relatively quickly organize themselves to take advantage of the common pool proposal if that were an option. And since all the countries of South Asia are still borrowers from IDA, the region would certainly benefit from an easing in IDA's terms. I admit that I would prefer this to take the form of grants rather than longer maturities, so that IDA could finance BRAC rather than just the government of Bangladesh.

Systemic Issues

The Panel urged a number of changes in existing international institutions, starting with the WTO. It argued that this was ridiculously underfunded, and therefore unable to offer all the services to its members (e.g. to help small and poor countries contest anti-dumping actions brought by the rich and powerful) that would be desirable. It also called for a proper governing structure that would enable all countries to be represented, at least indirectly, in the negotiation of future trade accords. It acknowledged the concerns that have surfaced in many industrial countries about labour and environmental standards, but argued against further expanding the WTO's responsibilities to cover these issues. It argued that it would be preferable to strengthen the ILO to deal with labour issues and to consolidate the various international organizations that have responsibility for environmental issues into a Global Environment Organization.

The report also reviewed the complaints against the Bretton Woods institutions, such as the limited role the IMF plays in influencing the macroeconomic policies of the major countries, the content of conditionality, and their voting structure. It welcomed the Fund's recent effort to cut back conditionality to its macroeconomic core and the recognition of the importance of ownership, and suggested more dialogue with the UN and the use of panels of "wise men" as possible ways of reconciling ownership with lending only in the presence of a supportive policy environment.

The Panel also made two important proposals for new international institutions. One was for an International Tax Organization (ITO). It was envisaged that such an organisation could compile statistics, identify trends and problems, present reports, offer technical assistance, and provide a forum for the exchange of ideas and the development of norms for tax policy and tax administration. It could engage in surveillance of tax developments in the same way that the IMF maintains surveillance of macroeconomic policies. Going further, it might engage in negotiations with tax havens to persuade them to desist from harmful tax competition. Similarly, it could take a lead role in restraining the tax competition designed to attract multinationals—competition that often results in the lion's share of the benefits of FDI accruing to the foreign investor. More ambitiously, an ITO might sponsor a mechanism for multilateral sharing of tax information, like that already in place within the OECD, so as to curb the scope for evasion of taxes on investment income earned abroad. Perhaps most ambitious of all, it might in due course seek to develop and secure international agreement on a formula for the unitary taxation of multinationals, as well as develop international arrangements that would provide for emigrants to pay taxes to their home countries.

The Panel also argued that the absence of any apex institution with political legitimacy able to guide the evolution of the international economic system constitutes a major lacuna in existing arrangements. It discussed the possibility of correcting this by creating an Economic Security Council within the UN, small enough to be effective (which rules out adapting the existing Economic and Social Council). Rather than offer its own blueprint, however, the Panel urged the UN to convene a global economic governance summit on a one-time basis, which might then convert itself into an Economic Security Council if it concluded that would be useful.

How would this raft of proposals impact South Asia? The proposals to reform the WTO are motivated very much by a concern to strengthen the position of the weaker countries; thus, while India may not have that much to gain from them, the rest of South Asia would. The suggestion for treating labour standards in a strengthened ILO and environmental issues in a consolidated GEO should reduce the danger often perceived in South Asia that these concerns will be used as a pretext for protectionist restrictions. But do not mistake this for an argument that labour and environmental abuses should not be subjected to effective international disciplines. The intent is to avoid overloading the WTO with yet more extraneous issues that it is ill-equipped to handle, not to divert what civil society in the developed world cares about into ineffective channels.

I see a strong interest of all the five large countries of South Asia in an ITO. At the moment there is not a strong interest in the ability to collect tax on assets that are held abroad, but this is likely to become a factor over time. But all are already at risk of losing tax revenue through tax degradation as countries compete with one another for multinationals by offering tax incentives. All host enough multinationals to make the loss of tax revenue through transfer pricing a real risk. Above all, all five are sufficiently important sources of migrants (and increasingly of migrants who have received expensive educations at national expense) to give them an interest in being able to levy taxes on their emigrants.

South Asia has an interest in the creation of an Economic Security Council to the extent that this could indeed be expected to achieve the objective of improving the evolution of the international economic system. It also has an interest in being appropriately represented within any such body. India would be sure of being represented in its own right, but the smaller countries also have an interest in securing some system of constituency representation that would give them a say, rather than membership being limited just to the larger countries on the model of the G-20.

Concluding Remarks

Those of us who live in Washington are bracing ourselves for another round of confrontations between the police and anti-globalization protesters in a few weeks time. These battles increasingly strike me as either misguided or mislabeled. There is a historical precedent for stopping globalization in its tracks: it already happened once, in 1914. This suggests rather strongly, at least to me, that the aim should be to influence the form rather than the fact of globalization, to make sure that globalization does not exclude large swathes of humanity from its potential benefits. That is very much what the Panel was trying to do. It made the case for free trade being reciprocal, meaning that the industrial countries should allow free access to the products in which low-income countries have a comparative advantage. It argued that we need to provide properly for ODA and global public goods, not to turn the clock back to a day when countries thought only of themselves. It took the view that the multinational institutions need to be reformed, not abolished. I hope you will agree that this was the right way to try to point the world.

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