

*South Centre is an Intergovernmental Organization and Think Tank of Developing Countries*

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### EDITORIAL:

### Banco del Sur, Another Step Towards Decoupling

South Bulletin: *Reflections and Foresights* takes stock of on-going debates on major global policy challenges and delivers regular global flow of analysis and commentary to policymakers in the South.

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After much speculation and some hostile coverage in Western media the Banco del Sur – the Bank of the South (BdS) – is to be launched on December 5, 2007. It was thought that close US allies - Mexico, Colombia, Peru and Central America – might oppose its formation. This may have been mere wishful thinking. In fact, most of South America is now on board.

Because the initiative came from President Chavez, some doubted if the new bank would not simply become his political instrument. Paradoxically, this must be on account of the experience with the IMF. It is well known that the IMF cannot move without mandate from the United States. Presently its largest lending goes to Turkey and Pakistan, and this is not surprising. However, unlike the IMF whose governance is highly undemocratic, the BdS governance is based on the principle of *one country one vote*.

Of course, there are still many questions to be settled. There is the question of, for example, lending policies and rules, who may borrow, and at what terms, and whether BdS should act strictly as a development bank, or whether, like the IMF, it should also act as a bank of last resort for countries in balance of payments difficulties. These are weighty policy and operational matters. With time, these matters will no doubt be resolved and tested on the ground. Of course mistakes will be made in early years. But hopefully a robust system will emerge in not too distant future. After all, what BdS is attempting to do has never been tried. It is indeed quite revolutionary in its ambition and far reaching in its potential impact on the global financial architecture.

If the BdS grows to its potential, Latin American countries will be freed from IMF, the World Bank and Inter-American Development Bank conditionalities that chained their economies to the failed macroeconomic policies of the Bretton Woods institutions. "Decoupling" from the US-led global economic hegemony was so far only an idea, and applied mostly in the case of China, India and Brazil.

But now "decoupling" the whole of Latin America from volatilities of the Western credit system is a vision in the realm of reality.

There are, however, certain matters that must engage the new Bank in the interest of ensuring that it really does serve as a genuinely development bank.

First, the Bank must promote a new strategy of development, one that promotes innovation, production and employment, and, above all, one that serves the needs of the poor rather than accumulation by the rich.

Secondly, the new Bank should focus on regional economic integration of Latin America and the Caribbean states (if they should eventually join it). There are excellent banks in the continent that serve national priorities. Brazil's National Bank of Economic and Social Development (BNDES) alone lends \$30bn annually, four times more than the \$7 bn subscribed to the new BdS. There is Corporacion Andino de Fomento (CAF), the largest lender to the five Andean countries. They will no doubt continue their excellent work. But BdS needs to provide financial muscle to the integration of the continent as a strong regional economic bloc. (The IDB presently invests only 2% on regional integration – clearly not one its priorities.)

Thirdly, the Bank must move away from the Basel regulatory system which works to the detriment of development. Development lending is often a high risk operation. The minimum capital requirement of Basel unduly leverages attractiveness of "low risk" to "higher risk" financing. Basel regulatory arbitrage favours low risk lending and adds cost to development lending, which is one reason for scarcity of development capital in the South. Basel II's "Internal Ratings-Based Approach" creates even more bias against risk and cost of borrowing. The new Bank must of course be prudent in its lending, but it needs to balance the needs of development with the returns to capital for the lenders of capital. It must operate as a genuine bank for the people.

**Yash Tandon**

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## Using Indicators to Designate Special Products in the WTO Negotiations

By Luisa Rodriguez

The Special Products (SP) proposal was articulated by the G33. This group has insisted that the outcome of the WTO negotiations on agriculture should incorporate concrete, operational and effective provisions that would allow developing members to take into account concerns of food security, livelihood security and development more broadly.

According to this proposal and the existing negotiating mandates, the approach to identify SPs should be linked to three criteria—food security, livelihood security and rural development, and to the indicators.

This article examines the key concepts contained in the negotiating mandates that provide guidance on how to approach SP designation, it then highlights differing interpretations of these concepts, and finally presents the research findings on the use of indicators to identify SPs.

### Special Products and the approach to identify them

In the ongoing agriculture negotiations in the WTO, the majority of developing countries support a proposal on SPs, aimed at increasing the flexibility to achieve development goals related to food and livelihood security and rural development. Products designated as SP will be set aside from the full impact of the tariff cuts. According to this proposal, developing countries will undergo a tariff reduction in the vast majority of their agricultural tariff lines, reduce tariffs less than would have been required under the formula for some tariff lines, and exempt few tariff lines from liberalisation commitments.

Elements of this proposal were mainstreamed into WTO negotiating mandates. In this sense, products designated as SPs will be subject to a more flexible treatment in terms of market access commitments. Mandates also provide for information on the approach to identifying SPs: they indicate that developing countries will have the flexibility to self-designate an appropriate number of tariff lines as SPs based on criteria of food security, livelihood security and rural development needs and guided by indicators.

The use of the three criteria as a basis for the identifying SPs represents a fundamental link between trade negotiation outcomes and development goals.

As these criteria are broad and complex to define and measure, a list of 12 indicators was developed by G33, to measure

the contribution of each agricultural commodity towards achieving objectives implied by the criteria. These indicators can facilitate the decision-making process related to identifying SPs by providing guidance on relevant information to consider and allowing quantification of data.

### The self-designation principle

The self-designation principle mentioned in the negotiating mandates is one of the two controversial issues in ongoing discussions related to the designation of SPs. Although this concept is self-explanatory, its operationalization has been subject to differing interpretations.

According to the G33 interpretation, the self-designation implies that countries will select products that are important for them from the perspective of food security, livelihood security and rural development. In this context, indicators serve as methodological tools that may facilitate national assessments on whether certain crops meet the criteria. Hence, the designation will not be arbitrary.

In spite of this, other countries have insisted on the need to enhance predictability in the process of identification of SPs. To achieve this, they have suggested developing rules for the “self designa-

tion”, for instance:

*Defining how potential SPs candidates should comply with the criteria*, for instance requiring simultaneous compliance with the three criteria to designate a product.

*Testing the link between potential SPs and indicators*, by requesting countries to justify the designation through data and explanations, suggesting the type of data to be provided (i.e. verifiable, from international data sources).

*Excluding certain products*, because they are of export interest to (developing) countries.

*Defining a methodology to prioritize potential SPs candidates*, using benchmark scores for criteria and indicators.

*Defining how indicators should be used*, for instance defining quantitative targets for parameters mentioned in the list of indicators, to gauge whether a product complies with an indicator.

Some of the rules mentioned above were captured in recent documents prepared by the Chairman of the Committee on

### **FAO definitions:**

*Food security: When all people, at all times, have physical and economic access to sufficient, safe and nutritious food in order to meet their dietary needs and food preferences for an active and healthy life.*

*Livelihood security: The adequate and sustainable access to income and other resources in order to enable households to meet their basic needs. This includes adequate access to food, potable water, health facilities, educational opportunities, housing and time for community participation and social integration.*

*Rural development: process that affects the well-being of rural populations including the provision of basic needs and services i.e. access to food, health services, water supply, basic infrastructure (roads etc.) and the development of human capital through education.*

## Using Indicators to Designate Special Products in WTO Negotiations (continued)

Agriculture, for instance establishing a closer relationship between criteria, indicators and the selection of the products, testing the data, using data that is publicly available and negotiating quantitative parameters to use indicators. The Chairman does, however, recognize that these courses of action might prove to be complex.

### A cautious approach to rules on SP designation

Using rules for the self-designation process implies the possibility of negotiating partners questioning or refusing to accept whether a product can be designated as an SP. This would appear to be contradictory with the self-designation principle contained in negotiating mandates. Recent research would seem to suggest a cautious approach to the design of rules for the designation of SPs.

### UNCTAD - South Centre experience

In July 2007, UNCTAD and South Centre analyzed the availability and “workability” of data contained in international recognized sources, such as FAO and UNCTAD. The research findings suggest that:

- These sources provide data on only 30% of the indicators. These data sources do not provide information on indicators related livelihood security nor on the regional importance of products.
- Information is not equally available for all countries, for recent years and for all products. Small island countries are particularly affected by the lack of recent data.
- There is no universal understanding on how expressions such as “significant proportion” and “resource-poor farmers” should be interpreted. Not even organizations as FAO have provided guidance on the interpretation of these concepts. Interpreting these concepts entail using quantitative targets for parameters contained in the indicators. The number of tariff lines potentially designated as SPs is very sensitive to variations in these quantitative targets.
- Excluding products for which developing countries account for more than 50-80% of world exports from the designation implies excluding 8-34% of tariff lines at the 6 digit level.

In view of the above, two elements are worth taking into account when discussing the designation of SPs through indicators.

First, verifiable data from international sources is not enough to operationalize the designation according to the three criteria. National and regional data sources are needed to capture local realities, in particular the livelihood security dimension and the regional importance of products.

Second, quantitative targets are very important in the process of designating SPs using indicators. They have a direct bearing on the number of potentially designated products. These targets will depend on the interpretation given to different concepts contained in the list of indicators, as proposed by the G33.

### FAO - ICTSD experience

A methodological approach was developed by ICTSD and FAO to identify products that could potentially be designated as SPs in the WTO, using the indicators proposed by G33. This methodology was developed on the basis of several case studies conducted with developing countries during 2006 and 2007.

The approach used has several stages. In the first stage and prior to using the list of indicators, the development criteria underlying the SP proposal are analyzed in consultations with the national stakeholders. At this stage, the aim is to frame the analysis for the identification of SPs within the broader national strategy

for sustainable agricultural development and poverty alleviation, to go beyond commercial considerations.

In the second stage, the qualitative information (related to development plans and broad policy objectives) obtained during the first stage is completed with quantitative information obtained through the indicators. In this stage, indicators are used to assess the importance of products for food and livelihood security and rural development. For example, in this stage, indicators are specifically used to: identify the intended beneficiaries, for instance through their income level, their geographical context/location and their production capacity; and to identify the products on which the livelihoods of these beneficiaries depend upon (through their contribution to the economy, contribution to the consumption).

In the third stage, the list of products obtained is subject to prioritization and ranking, analyzing the direct or indirect impact of liberalization and issues such as substitute products and vulnerability to imports. The prioritization of products could be done using a methodology to rank the products on the basis of the score accorded to these indicators. However, the assessment of the “special-ness” of potential SPs is likely to vary from country to country, depending on the priority as-

### **Parameters mentioned in the list of indicators.**

*Most of the indicators contained in the list proposed by G33 contain expressions such as “significant proportion” or “a relatively low proportion”, “significant contribution”. Examples:*

*A significant proportion of the domestic consumption of the product in its natural, unprocessed or processed form, in a particular region or at a national level, is met through domestic production in the developing country Member concerned*

*A significant proportion of the total agricultural population or rural labour force, in a particular region or at the national level, is employed in the production of the product.*

## Using Indicators to Designate Special Products in WTO Negotiations (continued)

signed to each criterion under the policy framework and objectives. Hence, a ‘one size fits all’ methodology might not be appropriate.

The research findings of the FAO–ICTSD experience suggest that, when discussing the designation of SPs through indicators, *three* elements are worth taking into account.

First, measuring development needs related to food security, livelihood security and rural development criteria require not only a quantitative analysis of the indicators but also a qualitative analysis, taking into account policy objectives and development plans.

Second, there is also need to factor in other elements such as vulnerability to import displacement, imported substitute products and unfair competition.

Third, there is merit in factoring in the size of economies and agroecological conditions when interpreting quantitative parameters contained in the indicators. ICTSD and FAO used complex formulae to do this.

### Conclusions

Although several negotiating mandates have captured principles and elements of the G33 proposal on SPs, divergences persist on the interpretation of key concepts related the identification of such products, like the self-designation principle and certain parameters contained in the list of indicators.

According to the interpretation of the proponents of the SP proposal, the self-designation implies that countries will select

products that are important for them from the perspective of food security, livelihood security and rural development. In this context, indicators serve as methodological tools that may facilitate national assessments on whether certain crops meet the criteria. Hence, the designation will not be arbitrary.

In spite of this, other countries have insisted on the need to enhance predictability in the process of identification of SP and have suggested creating rules for the self-designation. This implies the possibility of negotiating partners questioning or refusing to accept whether a product can be designated as an SP.

Recent research would suggest a cautious approach to the design of rules for the designation of SPs. Restricting the source of information that can be used; having strict quantitative targets per indicator for all developing countries and excluding qualitative factors (like policy objectives, development plans, vulnerability to import displacement, imported substitute and unfair competition) can lead to “one size fits all” methodology that may render SPs ineffective, in terms of providing policy flexibility to meet development needs.

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## Strategic Implementation of WIPO’s Development Agenda: An Institutional Perspective

By Xuan Li

The process leading to adoption of the Development Agenda by the WIPO General Assembly on 28 September 2007 in Geneva can be described as a historical success. As many as 45 proposals were adopted, ranging from technical assistance to norm-setting, from flexibilities to technology transfer, and from assessment to institutional matters. The full implementation of WIPO Development Agenda implies significant changes in global knowledge governance. The general consensus is that there is a real opportunity to revolutionize the global governance of intellectual property law and policy towards a fair and efficient outcome. Some fundamental changes in ideology and operation in knowledge governance are inevitable. Actions on reforming knowledge governance must be undertaken. But the pertinent question is: *How?*

### Systemic Structure and the WIPO Development Agenda

System structure is decisive in influencing productivity and implementation effectiveness. Global knowledge governance can be viewed as a system. Considering that the greatest beneficiaries of the implementation of the WIPO Development Agenda are those on the ground, the national level approach

must be brought into the system. Thus, current knowledge governance system can be broadly classified into three components: first, the international governance; second, the national governance; and third, the interface/transmission between the international and national levels. To explore some concrete solutions, this essay will start with the diagnosis of symptoms arising from the systemic structure and sources of institutional obstacles in the system that prevents good knowledge governance.

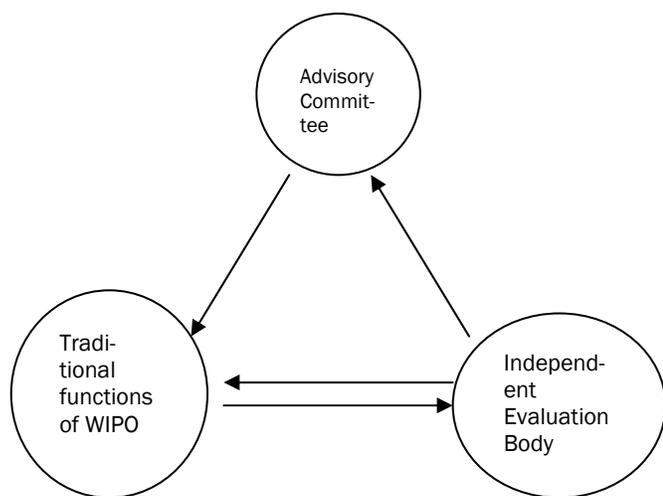
In terms of the first two components, both have similar underlying structural shortcomings although the symptoms of those shortcomings may vary. *At the international level*, the WIPO itself, as a result of being the sole UN agency dealing with IP affairs and having little or no institutional backup to ensure the IP regime reflects its multiple stakeholders’ varied interests at equilibrium, is a major source of a biased policy outcome in the favor of multinational corporations’ interests. *At the national level* for many developing countries, inadequate awareness and superficial instruction from domestic leadership and lack of methodologies to build a proper national

## Strategic Implementation of the WIPO Development Agenda (continued)

knowledge governance system represent some of the constraints. Both institutional failures originate from the conflicting roles played by both WIPO and states: in practice, each acts as a referee and athlete of IP simultaneously and without a proper supervisory mechanism.

The third institutional limitation comes from the linkage between the national and international levels. In practice, the two levels often lack efficient communication and coordination between them. The milestone cheered among Geneva delegates circles may not necessarily be echoed in the capitals in the same fashion. An institutional reason is be-

### Possible WIPO Institutional Reform



hind this possible disconnect: some delegates who were deeply involved in WIPO negotiations in the past years might come from Ministry of Foreign Affairs (MFA), whereas intellectual property affairs at the national level are often administered by an Intellectual Property Office (IPO) or some other agency which may operate quite autonomously of the MFA. This type of information asymmetry is likely to become more pronounced when more agencies are involved.

By categorizing the institutional obstacles related to the WIPO Development Agenda into international, national and interface types, some ideas to improve the picture could be tentatively tabled as follows:

#### Reform at the international level

To vigorously implement the adopted proposals, major reform in WIPO is a must, given its inadequate management system since its founding about 37 years ago. At the policy level, a proper conceptualization of how WIPO should incorporate the work of dealing with both IP and development needs should be crafted and adopted. At operational level,

the merits of setting up **two separate bodies** to differentiate the role of referees and athletes of WIPO should be studied seriously:

First, a **WIPO Advisory Committee** to set out direction and targets. One type of advice may include the establishment of WIPO Standing Committees on IP and Technology Transfer and a systematic introduction of Exemptions and Limitations, perhaps towards a treaty on access to knowledge and technologies and implementation of TRIPS flexibilities, etc.

Second, an independent **WIPO Evaluation Body** to conduct assessment on whether targets are met. The function of existing WIPO bodies could shift to focus mainly on the aspects of implementation. Such a system is thus structured in **Figure 2**.

#### Reform at the national level

More efforts are needed to raise the awareness of both the top leadership and at the grassroots on the importance of such reforms. Strong national leadership is crucial in this regard.

There could be two parallel institutions at the national level – one with an advisory function to ensure the direction and objective of policy choices, and the other with the function of evaluation to ensure that any implementation is in line with proposed national objectives. The role of a national IPO could be limited to implementation of policies rather than policy making itself. The national leadership should be closely assisted by the qualified National Advisory Committee and Independent Evaluation Body, and both would report directly to the top leadership instead of the IPO.

National governments should try to strengthen coordination and coherence among their different monitoring agencies/ministries concerned with IP and development, such as the Intellectual Property Office, Ministry of Public Health, Ministry of Agriculture, MFA, etc.

#### Interface between international and national levels

A lot can be done to improve the coordination and coherence among different developing countries and between some developed countries and developing ones. The format of communication could be flexible to ensure prompt and accurate flow of information between Geneva-based delegates and capital decision makers.

It would be highly desirable that more efforts at international cooperation and exchange between international bodies and national ones be made to provide technical assistance to developing countries for gradually enhancing their capacities in both participation of international rule-making as well as administration of national policies. Such elements would contribute to the realization of an optimal result of any reform plans.

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## Aid for Trade: Twenty Lessons from Existing Aid Schemes

By Darlan Fonseca

Following from the widespread acknowledgment that developing countries need support to benefit from trade liberalisation, debates on 'aid for trade' (AFT) have attracted much attention over the past years. This is not surprising since current AFT initiatives seem unprecedented in their purported geographical scope, thematic coverage and, possibly, resources involved. Aid for trade is discussed under the overarching framework of the World Trade Organization (WTO) but also in the context of regional and bilateral trade talks such as the Economic Partnership Agreements (EPAs) currently being negotiated between the European Union (EU) and the African, Caribbean and Pacific (ACP) countries. Precisely because of this level of ambition, and the possible thematic and geographic scope, the actual operationalisation of AFT initiatives to deliver incremental trade-related aid is a complex exercise that presents many challenges for all involved.

While potential donor and recipient countries discuss issues surrounding the demand side and the supply side of AFT, it is important to have clear ideas on what is already working (and what is not) at the multilateral, regional and national levels. To make concrete proposals for moving forward with AFT, donors and recipients have to take stock of existing programmes and identify financing gaps and needs for improvements of delivery mechanisms. Therefore, the current study aims to inform the ongoing debates by highlighting lessons learnt from existing trade-related aid schemes. These lessons are informed by an exploration of the European Commission (EC) trade-related assistance (TRA) (in the framework of ACP-EU relations) as a significant example of regional and bilateral schemes, as well as the multi-agency Integrated Framework (IF) and the International Monetary Fund (IMF) Trade Integration Mechanism (TIM) as major multilateral aid schemes.

The analysis provided may be beneficial in assessing whether existing trade-related aid mechanisms can play a key role in channeling AFT, as there is no need to reinvent the wheel. Indeed, a comparative assessment of existing aid instruments on the one hand and AFT mandates and objectives on the other will be a precondition for the identification of possible gaps in thematic and geographic coverage between the two as well as to extract best practices in delivery mechanisms and procedures. It is also hoped that this study will be useful in terms of translating some elements of the overall debate on aid effectiveness into the language of trade, as a first step in bridging the two separate worlds of

the ministries of trade and ministries for development cooperation, as these two often lack sufficient exchange of information and interaction, both in developed and developing countries.

By pointing to strengths and weaknesses in the functioning, institutional set-up, scope and monitoring of existing instruments, this study identifies lessons on how to operationalise the delivery of AFT and points to some best practices towards increased aid effectiveness. While many lessons could be drawn, the conclusions of this study present twenty lessons deemed particularly relevant in terms of underlying principles, improving the demand and supply of AFT during design phases, as well as improving its management and delivery.

*“AFT should be aligned to the trade priorities endogenously set by developing countries and rooted within their overall national development priorities.”*

### Twenty Principles and Lessons from Existing TRA Facilities

#### Underlying Principles of AFT

1. AFT should be based on a partnership approach whereby the parties choose aid and trade as instruments to achieve common objectives and do not consider aid as donor compensation (or conditionality) for trade liberalisation by the recipient country.
2. AFT should be aligned to the trade priorities endogenously set by developing countries and rooted within their overall national development plans.
3. Any AFT initiative should concretely reflect full ownership of the interventions by all relevant stakeholders in the beneficiary countries.

4. Capacity building in the context of AFT should include both long-term and short-term interventions with a focus on participation and endogenous change.

#### Improving Demand & Supply of AFT during Design Phases

5. Multi-stakeholder involvement towards a large consensus around the projects to be implemented, with adequate balance between inclusiveness and efficiency, can boost the credibility of the AFT initiative.
6. AFT objectives must match existing delivery instruments and actually available resources; donors should avoid re-labeling existing aid and raising unrealistic expectations.
7. Recognition that trade can make a vital contribution to development should be matched by a broad scope of AFT programmes and the policy decision by donors to support trade reforms in developing countries with substantial levels of predictable funding.

## Aid for Trade: Twenty Lessons from Existing Aid Schemes (continued)

8. The broader the scope of interventions the more important the proper articulation, definition, timing and reporting of AFT initiatives.

9. AFT interventions should integrate regional priorities without losing focus on national-level interventions.

10. AFT country and regional interventions should be designed through thorough diagnostic analyses.

### **Improving the Management & Delivery of AFT**

11. Given the possibly large amounts disbursed and numbers of donors, beneficiaries and projects, AFT should be subject to regular evaluation and improvement through formal monitoring and review processes.

12. A solid institutional architecture is fundamentally important, especially with regard to the wide scope of activities carried out under the AFT initiative.

13. Several different types of stakeholders need to be closely involved in the programming, delivery and evaluation of AFT.

14. Country-level and sub-regional-level management plays as important a role as global level governing bodies.

15. With regard to the multi-actor and multi-level dimension of the AFT initiative, effective coordination has to be ensured (going beyond solely the exchange of information).

16. Complementarity and coherence of AFT interventions should be guaranteed through joint programming and each donor's role defined on the basis of expertise and comparative advantages.

17. AFT resources must be commensurate with objectives and made predictable as well as timely and effectively available.

18. Support under the AFT initiative should not lead to indebtedness in the recipient countries.

19. Modalities for AFT disbursement must be flexible and user-friendly to ensure the timely and effective delivery of aid (e.g. use of budget support and locally owned management procedures).

20. Adequate procedures for timely and efficient delivery of AFT may require improvements both on the donor side and on the recipient side.

Several of these principles and best practices cut across experiences in the three trade-related approaches analysed,

suggesting that some of these lessons lie at the heart of the effectiveness of TRA delivery. The relevance of these lessons is strengthened by the fact that many of them reflect elements of the Paris Declaration on Aid Effectiveness, widely recognised as a qualitative benchmark for aid delivery. Moreover, these principles coincide in part with the lessons identified in the recommendations prepared by the WTO Aid for Trade Task Force. More than a simple coincidence, the commonalities enhance the legitimacy of the elements identified in these recommendations and highlight the importance of rendering these elements fully operational.

*“Country-level and sub-regional management plays as important a role as global level governing bodies.”*

A number of fundamental questions remain to be answered before any assistance is implemented under the AFT umbrella. Firstly, yet to be determined is whether the AFT initiative will constitute a source of funding or whether it will function as a mechanism coordinating access to funding, but not having any funds of its own. In addition, there could be significant variations in the amount of aid available depending on how AFT programmes are defined and classified. To what extent AFT commitments will be additional to current spending and which categories of existing aid can be classified as AFT are still ongoing discussions. Even assuming that there are additional resources available, these will of course not be endless and will definitely not be made available at one time. Hence, a kind of prioritisation of interventions or prioritisation of countries and sectors will be required. Those choices will have an enormous influence on the actual operationalisation of AFT and will determine its architecture and functioning, thereby influencing the validity of the lessons elaborated here.

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## Role of Low-Income Countries in the Governance of IMF and World Bank

By Aldo Caliarì

At the 2006 Annual Meetings of the World Bank and the International Monetary Fund, in Singapore, these institutions adopted a two-stage plan for reforming the quota formula that determines voting power of member countries. The move followed more than five years of wrangling over different proposals for reforming the way that the vote of the members is weighed, beginning with the call by the Monterrey Consensus (2002), to enhance the participation of all developing countries in the decision-making of the two institutions.

The direction of the reforms, however, seems dangerously centered on aligning the voting power with the role and weight of members in the global economy. This concern reflects the anachronistic distortion that grew over time in a voting power structure that largely reflects the geopolitical and economic world of the 1950s, and begs for some correction. The concern coincides with a no small “realpolitik” factor in the seriousness with which the institutions took governance reform: the threatening possibility that middle-income nations awash in capital, especially those in Asia, may leave the Fund to set up their own regional institution for financial support.

But it is worth recalling that there was more than the mere dislocations between economic size and voting power to the demands for reform and democratization of the Bretton Woods Institutions. The ethical imperative that those affected by a decision should be able to have a say on it played a big part. From this perspective, however, it is likely that the Singapore agenda for governance reform will bring, ironically, retrogression rather than progress. This is because every measurement of growth trends in the developing world shows an increasing gap between middle-income and low-income economies. Alongside the impressive dynamism emerging economies exhibited in the last two decades, low-income countries (“LICs”) only kept falling further behind. A reform along the lines of “aligning representation with economic power”, therefore, would increase the voice of some middle-income countries but would sideline, and probably reduce, the voice of low-income countries in the Fund.

To make matters worse, because of a steady stream of early repayments by several middle-income Fund members over the last two years, this happens at a time when low-income countries represent the largest portion of countries with outstanding Fund programs. For this same reason, LICs are the members where the Fund still enjoys the largest clout, especially if compared to middle-income countries who have “emancipated” from the Fund.

Summing up, the focus on economic weight in the reform of governance would perpetuate and compound a situation

whereby those who borrow are disenfranchised from influencing the policies of the Fund.

The first stage envisioned in the Singapore resolution already awarded quota increases to four countries: China, South Korea, Mexico and Turkey, all deemed to be substantially under-represented. Out of these four countries, three are OECD countries, and the fourth—China—certainly not one likely to need to resort to the Fund anytime soon, nor one whose weight in economic governance matters goes unnoticed.

There were hopes that the second stage, which promised to enhance the voice and participation of low-income countries, would do more for them. But the direction of the reforms is not promising.

*“The focus on economic weight in the reform of governance would perpetuate and compound a situation whereby those who borrow - LICs - are disenfranchised from influencing the policies of the Fund.”*

In terms of the reform of quota formula, several reports emanating from both the Managing Director and the Executive Board, state that the intention of the exercise is to find a formula that captures the relative position of members in the world economy. It is unfortunate that the Board apparently is no longer considering the possibility of adopting different quota formulas for different objectives. In fact, a key reason for the inadequacy of the current quota formula is its attempt to reach three objectives, determining voting power, contribution to the Fund and access to Fund resources, with only one formula. The reform would have offered an opportunity –now apparently lost—to reexamine whether different quota formulas for different purposes made more sense than the single quota formula.

An Executive Board paper prepared for the last Annual Meetings notes “significant convergence” among members on the use of four of the variables used in the current formula: GDP, openness, variability and reserves. This article will not address the certainly dubious claim that these variables will bring much improvement to the overall position of developing countries as a whole. On the specific issue of their potential benefit to LICs, however, the choice of variables is clearly biased against them.

Firstly, the proposed variables are all “supply” variables, this is, variables rather correlated with the capacity to supply Fund resources rather than variables measuring the need for them. But there are additional problems. The “openness” variable is so correlated with GDP that its inclusion in addition to a GDP variable is tantamount to overstating a factor based on economic size.

Moreover, the way that openness is counted would likely continue to treat trade within currency unions as international trade. This approach has the effect of overstating the openness figures for European Union member countries.

## Role of Low-Income Countries in the Governance of IMF and World Bank (continued)

A possible variable that could measure demand is the “variability” one. Some analysts claim there is an emerging consensus on including not only long- but also short-term capital flows volatility in this measure. This would represent some progress. The inclusion of short-term capital flows would benefit lowest income countries subject to sharp fluctuations but had, in the past, been resisted. However, there is still a bias inasmuch as a capital account shock of the same absolute size will affect a smaller economy more strongly than a bigger one. A measure of variability as a proportion of GDP would be a more adequate measure. Several developing country officials echoed the critique of the current measure of variability and the call for a corrected one.

A more promising emphasis for low-income countries seems to be on the other component of each member’s vote: basic votes. Indeed, an important shortcoming of the single quota formula is that, in order to exercise the voting power given by it, member countries would have to contribute the respective amount of capital. For cash-strapped countries this is bound to be a problem. Basic votes, on the other hand, are not tied to capital contributions. The specific purpose of these votes, of which each member statutorily received an equal number (250) when the Fund was established, was to increase the weight of smaller members. As put by a commentator, basic votes take into account the risks and disadvantages unique to being small: market and exchange rate risks are higher, less ability to take advantage of scale economies, reliance on outside markets to make production viable, large impact of actions of large neighbors, low diversification, etc.

Progress has been made towards an amendment to, at least, double basic votes. However, this is not enough to redress the consistent erosion that basic votes as a proportion of total voting power have suffered since 1945. Basic votes represented over 11 percent of total votes but, after a number of increases in capital, which only affect the quotas, the share of basic votes in total votes has dropped to slightly above 2 percent. To reinstate the basic votes to their original share in total votes, at least a quadrupling is required.

It has been agreed, also, that the amendment of the Articles of Agreement will also add a clause to index basic votes with successive future quota increases, so the share is maintained constant. It is important to ensure that this clause is effectively put in place, but it is also important that the share is the original one, not the one resulting from a mere doubling of basic votes.

In the best case scenario, basic votes and quota reform will only go so far in redressing the imbalances that the poorest

countries face in their participation in the Fund. For example, no matter how many votes LICs have, only two Executive Directors are from LICs. As another consequence in the drop of middle-income country users is that the proportion of programs in African LICs as a share of total number of Fund programs has gone up. In this regard, it is interesting to note there are only two out of 24 Executive Directors serving African LICs and able to voice their concerns at the Board.

The proposals to require a double majority for decision-making, e.g. a weighted majority plus a numerical majority of member countries, would go a long way towards producing an immediate and significant increase in the capacity of smaller countries to influence decisions. An interesting feature of this

proposal is that it could be implemented without changes to the Articles of agreement, on a pilot basis. Some members have voiced technical legal obstacles to the implementation of this proposal but analysts claim the obstacles are more political than strictly legal. They refer to the World Bank delving into governance matters, a field where it had initially interpreted it had no jurisdiction, and the rise of policy-based conditionality, forbidden by the Articles of Agreement. These two cases are clear examples of how far the Bretton Woods Institutions can go in reinterpreting their constitutive agreements, present the political agreement of their main shareholders. Likewise, it is argued that the provisions in the Articles of Agreement that forbid Executive Directors from splitting their vote would make this double majority modality unworkable. But members could agree to

state how many countries in their constituency are for “yes” or for “no” and the Secretary of the Board could take note of it for tallying purposes. This is not very different from the function the Secretary plays today where it already interprets the direction of the vote of each member in tallying the votes.

According to his last report before leaving the institution, the now former Managing Director, Mr. Rodrigo Rato, said that agreement on the new formula should be reached by the 2008 Spring meetings at the latest. The new Managing Director, Mr. Strauss-Kahn, promised to bring the governance reform process to completion. He might well do it by following the “emerging consensus.” But he should know that if the outcome of the reform process fails to increase the voice of the members that make most use of the Fund today, chances are the undemocratic nature of the institution he presides will remain as incontestable as ever.

*“If the outcome of the reform process fails to increase the voice of the members that make most use of the Fund, chances are the undemocratic nature of the institution will remain as incontestable as ever.”*

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## A Bank of Their Own

By Mark Weisbrot

*"Developing nations must create their own mechanisms of finance instead of suffering under those of the IMF and the World Bank, which are institutions of rich nations . . . it is time to wake up."*

That was Lula da Silva, the president of Brazil – not Washington's nemesis, Hugo Chavez – speaking in the Republic of Congo just two weeks ago. Although our foreign policy establishment remains in cozy denial about it, the recognition that Washington's economic policies and institutions have failed miserably in Latin America is broadly shared among leaders in the region. Commentators here – Foreign Affairs, Foreign Policy, the editorial boards and op-ed contributors in major newspapers – have taken pains to distinguish "good" leftist presidents (Lula of Brazil and Michele Bachelet of Chile) from the "bad" ones – Chavez of Venezuela, Rafael Correa of Ecuador, Evo Morales of Bolivia and, depending on the pundit, sometimes Nestor Kirchner of Argentina.

But the reality is that Chavez (most flamboyantly) and his Andean colleagues are just saying out loud what everyone else believes. So official Washington, and most of the media, has been somewhat surprised by the rapid consolidation of a new "Bank of the South" proposed by Chavez just last year as an alternative to the Washington-dominated International Monetary Fund (IMF), World Bank and Inter-American Development Bank.

The media has been reluctant to take the new bank seriously, and some continue to call the institution, pejoratively, "Chavez's bank." But it has been joined by Brazil, Argentina, Bolivia, Ecuador, Uruguay and Paraguay. And just two weeks ago, Colombia, one of the Bush administration's few remaining allies in the region and the third-largest recipient of U.S. aid (after Israel and Egypt), announced that it wanted in. Et tu, Uribe?

The bank, which will be officially launched on Dec. 5, will make development loans to its member countries, with a focus on regional economic integration. This is important because these countries want to increase their trade, energy and commercial relationships for both economic and political reasons, just as the European Union has done over the last 50 years. The Inter-American Development Bank, which focuses entirely on Latin America, devotes only about 2 percent of its lending to regional integration.

Unlike the Washington-based international financial institutions, the new bank will not impose economic policy conditions on its borrowers. Such conditions are widely believed to

have been a major cause of Latin America's unprecedented economic failure over the last 26 years, the worst long-term growth performance in more than a century.

The bank is expected to start with capital of about \$7 billion, with all member countries contributing. It will be governed primarily on a one-country, one-vote basis.

How ironic is it that such an institution would be called "Chavez's bank," while nobody calls the IMF or the World Bank "Bush's bank?" The IMF and World Bank have 185 member countries but the United States calls the shots; it has a formal

veto in the IMF, but its power is much greater than that, with Europe and Japan having almost never voted against Washington in the institution's 63-year history. The rest of the world, i.e., the majority and the countries that bear the brunt of the institutions' policies, has little to no say in decision making.

Politically, the new bank is another Declaration of Independence for South America, which as a result of epoch-making changes in the last few years is now more independent of the United States than Europe is. The most important change that has brought this about – other than the populist ballot-box revolt that elected left-of-center governments in Argentina, Bolivia, Brazil, Ecuador, Uruguay and Venezuela – has been the collapse of the IMF-led "creditor's cartel" in the region. This was the main avenue of U.S. influence, and there's not much left of it. Of course the U.S. government still has some clout in the region, but without the ability to cut off credit to disobedient governments,

its power is vastly reduced.

The need for alternative regional economic institutions, for both development lending and finance, is becoming increasingly accepted by most of the world. Ten years ago, in the wake of the Asian financial crisis, there was a whole series of proposals, even books by prominent economists, on how to reform "the international financial architecture." The current crisis triggered by the collapse of subprime-mortgage-backed securities may provoke another such discussion. But the fact is, a full decade after the Asian crisis, the rich country governments have made no significant movement toward reform. New leaders of the IMF and the World Bank were appointed in the last few months, and by tradition, these have to be a European and an American.

That tradition was honored, despite calls from a majority of the member countries and scores of NGOs and think tanks to open up the search process. For the World Bank, the Bush administration even managed to add insult to injury by ap-

*"With reform at the top blocked, positive changes will have to come at the regional, and of course, most importantly, at the national level. Latin Americans are doing their part, and the world will surely thank them for it."*

## A Bank of Their Own (continued)

pointing Robert Zoellick, a neoconservative in the mold of his intensely disliked predecessor, Paul Wolfowitz, to run the beleaguered institution. Without even the smallest symbolic changes, it is hard to imagine more substantive changes, e.g., in the voting structure, taking place in the foreseeable future.

With reform at the top blocked, positive changes will have to come at the regional, and of course, most importantly, at the national level. Latin Americans are doing their part, and the world will surely thank them for it.

Not everyone is happy to see the old order challenged. An insider at the Inter-American Development Bank told the Financial Times: "With the money of Venezuela and political will of Argentina and Brazil, this is a bank that could have lots of money and a different political approach. No one will say this publicly, but we don't like it."

Apparently, these institutions that preach the virtues of international competition are not so enthusiastic when it breaks into their own monopolistic market.

### Mark Weisbrot is Co-Director of the Center for Economic and Policy Research in Washington DC

*Note: On 23 October 2007, the same weekend as the fall meetings of the IMF and World Bank, the Center for Economic and Policy Research hosted a press breakfast and public event in Washington, DC with the Finance Minister of Venezuela, Rodrigo Cabezas; the Finance Minister of Bolivia, Luis Arce; and the new Minister of Political Economy of Ecuador, Pedro Paez, on the Bank of the South. Audio and video files of the events are available at <http://www.cepr.net/content/view/1334/>.*

## South in News

Democratic Republic of Congo to take over from Argentina as the **new Chair of the G-24** for 2008. Syrian Arab Republic and Brazil will be the First and the Second Vice-Chair respectively.

2–3 November 2007: The **2nd NAM Business Forum** took place in Havana, Cuba followed by the International Trade Fair from 5–10 November.

17–18 November 2007: **Meeting of G-20** Finance Ministers and Central Bank Governors to be held in Cape Town, South Africa. G-20 is an informal forum that brings together industrialised and developing economies to discuss key issues in the global economy.

5 December 2007: New date for the launch of the **Bank of the South**. Its members are: Argentina, Brazil, Bolivia, Colombia, Ecuador, Paraguay, Uruguay and Venezuela.

## South Centre News

### Work Opportunities

South Centre is looking for an economist/senior economist and two research fellows for its Innovation and Access to Knowledge Programme. Last date for applications: 14 December 2007. *Only nationals of countries members of the Group of 77 and China are eligible for these positions.*

### Upcoming Events

5 December 2007: « The Implementation Game: Developing Countries, the TRIPS Agreement and the Global Politics of Intellectual Property » *Fifth South Innovation Perspectives Seminar, Palais des Nations, Geneva.*

5 December 2007: « Enhancing a development agenda in climate change for developing countries » *Side-Event to the 13<sup>th</sup> Conference of the Parties, United Nations Framework Convention on Climate Change, 13:00-15:00, Room: Wave (Grand Hyatt), Bali, Indonesia.*

### New Publications

Intellectual Property Quarterly Update 2007 (Third Quarter): *This issue examines the use of the August 2003 Decision of the General Assembly of the WTO to enable the import and export of pharmaceuticals produced under compulsory license by Rwanda and Canada.*

For more information on the above, visit the South Centre website at: <http://www.southcentre.org/>



**SOUTH BULLETIN :**  
Reflections and Foresights

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### CALL FOR CONTRIBUTIONS

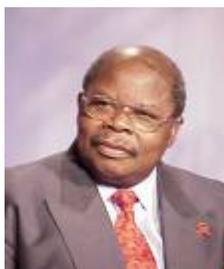
**We welcome your analysis and commentaries (of up to 2000 words) on ongoing and emerging issues to be published in the South Bulletin.**

**Send them to: Vikas Nath at [nath@southcentre.org](mailto:nath@southcentre.org)**

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## GUEST EDITORIAL: Benjamin Mkapa

### Owning a Stake in the Globalizing World: *It can be done, play your part*



The pace of global change is increasing immeasurably, but the divide in the participation and in influencing the pace as well as the content of the change between North and South, is also increasing. I know of the discourses and negotiations that are taking place on many fronts on new and old issues including aid, trade, finance and development. And I have noticed that in all these fora there are efforts either to divide us or to stress the divisions between the ranks of the South. Those efforts take various forms and categorizations: some are imagined, some are not so imagined, some are imagined politically, others are not so imagined politically, some are failing while others are modest successes.

The effect of this is either to persuade us that we cannot unite or to make us stress our own perceived divisions. The best illustration of this is the fact that we now have decided to turn to the Millennium Development Goals as being really the *nirvana* of development for the South and for the least-developed countries, instead of considering them as a minimum, an absolute minimum of (belated) development goals. The full consequence of the observations I have made is to ask ourselves whether in this process of vast and fast globalization, do we have any stake or ownership? And how much political will we are mobilizing not only to consolidate this stake but to pursue it as vigorously and in-depth as the developed countries of the North have decided and do.

This really means we go back to the roots of the South Commission as well as the rationale behind founding the South Centre. If we do have commitments, is this a commitment to affirm, assert ourselves and rest our stake or is it a commitment to mitigate the impact, the obvious impact where South simply becomes the agenda-takers at every fora? Do we have the will and can we mobilize this will? Are we really resigned to being soft governments of the South? We need to be proactive in defining the stakes, in analyzing them, and in strategizing in the pursuit of discourses as well as in negotiations.

*This is the challenge that we have to face, and urgently too.*

In addition to the traditional issues, there are now the new issues such as those of climate change and new forms of energy. Again, are we going to lie back? Are we in the South going to be just supplements to those in the North who are determining the pace and the direction of change? I think it is not too late to mobilize ourselves. Mobilize ourselves we must, because if we do not, then we will be asked to contract out our stake even further.

My founding President, who was the first Chairman of the South Centre Board, used to say "*it can be done, play your part*". I think that more of us can play our part, more than what we are doing now. It can be done if everyone plays his or her part. Let us resolve that more of us will do our part so that we can identify our stake, but above all, own a part of this process of a globalizing world in which we have an equitable share.

*Mr. Benjamin Mkapa is the former President of Tanzania and the Chairman of the South Centre. The above is an excerpt from the address delivered by Mr. Mkapa, at the Eighth Meeting of the Council of Representatives of the South Centre on 4 October 2007 in Geneva.)*