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UNCTAD can play part in realizing sustainable development agenda

The concept of interdependence – between countries and between policy areas – underlying the work of the United Nations Conference on Trade and Development (UNCTAD) can be employed to evaluate the implementation of the UN's 2030 Agenda for Sustainable Development. This evaluation, according to a recent UNCTAD policy brief, would examine the impact of the international environment on implementation as well as policy trade-offs and synergies at the national level.

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UNCTAD's role in follow-up of the 2030 Agenda

The concept of interdependence – both among countries and among policy areas – applied in the analytical work of the UN Conference on Trade and Development (UNCTAD) can help in assessing countries' implementation of the 2030 Agenda for Sustainable Development, says the UN body.

by Kanaga Raja

GENEVA: The United Nations Conference on Trade and Development (UNCTAD) concept of interdependence between countries and policy areas can be employed in the follow-up and monitoring of the implementation of the 2030 Agenda for Sustainable Development, according to UNCTAD's latest policy brief.

In its policy brief (No. 47, March 2016), UNCTAD said that the 2030 Agenda for Sustainable Development substantially increases the demand for evidence-based analysis and integrated and coordinated policy support in the area of expertise of UNCTAD.

"Its comprehensive and integrated nature mirrors the UNCTAD concept of interdependence between countries and policy areas," it added.

This concept can now be employed in the follow-up and monitoring process of the Agenda to assess the impact of the international environment on the effectiveness of national implementation strategies, and trade-offs and synergies in those strategies.

"Tailored policy support to member States should alleviate national implementation and reporting burdens, thereby facilitating the adoption of coherent national implementation strategies," said UNCTAD.

World leaders adopted the 2030 Agenda for Sustainable Development at the UN summit for the adoption of the post-2015 development agenda in September 2015, setting 17 Goals and 169 targets through which they have committed themselves and the international community to ending extreme poverty and achieving sustainable development.

The Addis Ababa Action Agenda that they adopted in July 2015 complements and supports the means of implementation of the 2030 Agenda for Sustainable Development.

The UN Statistical Commission established the Inter-Agency and Expert Group on Sustainable Development Goal Indicators to identify the indicators used to monitor progress towards the Goals at the global level.

"In addition to securing the financial resources required to bridge the investment gap identified in the Addis Ababa Action Agenda, the task ahead is to move from decisions to actions and put in place an appropriate monitoring and review system for the 2030 Agenda for Sustainable Development," said UNCTAD.

Moving from the Millennium Development Goals to the Sustainable Development Goals and the Addis Ababa Action Agenda has broadened the development agenda and substantially increased the demand for evidence-based analysis and integrated and coordinated policy support in the area of expertise of UNCTAD on trade and development and the inter-related issues of finance, technology, investment and sustainable development.

The six action areas of the Addis Ababa Action Agenda mirror the longstanding mandate and activities of UNCTAD, and two of the five areas of critical importance to the 2030 Agenda for Sustainable Development, namely partnership (Goal 17 and the means of implementation targets) and prosperity (Goals 8, 9 and 10), directly relate to its work programme.

These areas are also reflected in the targets of other Goals, just as other Goals are reflected in some of the targets related to prosperity and partnership.

"This is testimony to the comprehensiveness and integrated nature of the Goals that accord well with the integrated perspective of UNCTAD on sustainable development," said the policy brief.

UNCTAD's integrated approach is reflected in the concept of interdependence, with its two components concerning interdependence of economic, social and environmental conditions among countries, and interdependence among policy areas within countries.

Based on its universal membership, evidence-based policy support and a wealth of well-tested policy review tools, UNCTAD can now employ the concept of interdependence to evaluate both the impact of the international environment on country-level implementation efforts and the trade-offs and synergies across sectors and countries.

"This approach will be instrumental to maximize policy coherence and synergies at all levels in attaining the Agenda's economic, social and environmental Goals."

UNCTAD said that accompanied by supportive statistical work, this evaluation could be done in collaboration with other stakeholders and comprise three steps: a global assessment; an assessment of the impact of the international environment on national implementation in all countries; and an assessment of policy trade-offs and synergies at the national level, focusing on those countries that face serious capacity and resource constraints in assessment and implementation.

The first step recognizes that a universal and comprehensive agenda requires an evaluation of the distance from the 17 Goals globally and of the collective implications of actions at the national level.

It could be dealt with through aggregation from national and regional levels to the global level, as well as through the use of the global metrics that are being identified by the Inter-Agency and Expert Group of Sustainable Development Goal Indicators.

International environment

The policy brief underlined that while primary responsibility for the implementation of the 2030 Agenda for Sustainable Development lies at the national level, the comprehensiveness and universality of the Goals makes a supportive international environment an important determinant of effective implementation, and that such an environment takes the form of supportive global trends, international policy frameworks, multilateral rules and effective partnerships.

UNCTAD said that this environment may be reflected in seven channels:

(1) The trade channel: While trade integration generally improves efficiency of production, the contributions of trade to investment and ensuing enhanced production, technology upgrading and productivity growth are more important for sustainable development.

Exporting increases market size and generates economies of scale that make firms more productive and invest to further expand productive capacity. Export earnings also allow financing of imports of capital equipment that embody advanced technology, as well as goods required to address basic needs, such as medicine.

"These links between trade and investment catalyze structural transformation, employment creation and skills development, directly supporting the accomplishment of Goals 8, 9 and 10."

(2) The investment channel: Implementing the Goals in developing countries requires an investment push of an estimated $3.3 trillion to $4.5 trillion a year, with current levels of investment leaving an annual gap of $2.5 trillion.

UNCTAD said that while foreign direct investment (FDI) flows can boost investment in developing countries beyond domestic investment, a dominance of mergers and acquisitions over greenfield investment would make FDI contribute little to building productive capacity.

(3) The finance channel: Financial integration confers benefits when it helps to finance imports of capital goods for the creation of productive capacity and reduce pressure for macroeconomic adjustment to temporary shocks. It can also make domestic financial markets more efficient.

However, cautioned UNCTAD, "financial integration increases vulnerability, as cross-border private capital flows tend to be highly volatile and associated with global financial cycles with often adverse consequences for macroeconomic stability, the sustainability of foreign-currency denominated debt and income distribution."

The balance of these effects is country-specific, it said, adding that benefits are more likely to occur in countries with strong financial regulation and a high level of financial development.

"The finance channel would be strengthened by bringing the level of official development assistance to internationally committed levels and reorienting such assistance in line with the strategies of recipient countries to implement the Goals."

(4) The technology channel: Expanding the digital revolution into production processes promises universal benefits by reversing the slowdown in productivity growth that has plagued the world economy over the past few years.

"Its development benefits will add to those derived from enhanced technology transfer, especially when innovation-based investment raises productivity growth and allows workers operating new machinery and software to demand higher wages, with resulting higher aggregate spending further boosting investment and the prosperity of society as a whole."

Innovation could also enhance the environmental sustainability of creating productive capacity, said UNCTAD. "If the recent substantial decline in the cost of producing solar and wind energy continues, there will be massive investment in renewable energy that would substantially transform the global energy sector. It could also transform the world economy itself, for example, by triggering major productivity increases and accelerating growth in the real economy, irrespective of how the digital revolution is going to move forward."

(5) The regulatory channel: Norms governing international trade have increasingly been set through bilateral and regional agreements. These often spur global trade less than multilateral agreements, as they are less about market access and more about regulatory convergence and standards that reshape global value chains.

Further, their norm-setting is non-inclusive and distorts international competitiveness by providing different trading partners with different conditions, often at the expense of lower-income countries that see their preferential margins in international markets erode.

According to UNCTAD, international investment agreements govern FDI but are often perceived as paying insufficient attention to inclusive growth and the Sustainable Development Goals.

"Trade and investment agreements may also unduly hamper domestic policies and regulation set in the public interest."

UNCTAD said that financial reforms agreed at the international level may insufficiently take account of developmental needs by prescribing overly complex implementation requirements and encouraging too little the proliferation of financial products and organizations that support investment in productive capacity.

(6) The fiscal channel: Fiscal revenues are a prime source of finance for public investment, said UNCTAD. But their international origin has been limited by so-called "tax optimization" strategies of transnational corporations that declare profits in tax havens.

According to UNCTAD estimates, investment-related tax avoidance schemes cost developing countries some $100 billion annually – about twice the amount of FDI that went to Africa in 2015.

"Decisive multilateral action in this area would help augment public revenue available for the investment push needed to attain the Sustainable Development Goals," UNCTAD stressed.

(7) The institutional channel: Unresolved institutional deficiencies regarding sovereign debt workouts and the provision of official international liquidity in periods of balance-of-payments difficulties raise questions about the development orientation, coherence and consistency of the international monetary and financial architecture.

"These deficiencies, combined with the close inter-linkages between the trade and finance channels through the balance of payments, tend to reduce support from the global economic architecture to sustainable development."

UNCTAD said addressing these channels in an integrated way from the perspective of sustainable development will make it possible to develop a forward-looking assessment of the support from the international environment to the effectiveness of national implementation strategies and of the collective implications of national measures for global processes.

National policy coherence

"The inter-related nature of the Sustainable Development Goals also requires policy integration and coherence at the national level. Related assessments of trade-offs and synergies require a normative basis against which national policy frameworks can be evaluated and which allows checking the collective consistency of policies with shared objectives."

Developing a set of options and country-specific recommendations would promote national capacities and address vulnerabilities, said UNCTAD, citing one example of potential policy trade-offs or synergies relating to the growth-distribution-environment-trade link.

It said that technological progress is generally considered the main source of sustained economic growth. "But employing new technologies to attain economic goals could harm social inclusiveness by widening gaps in employment and income opportunities between workers with different skill levels. Economic growth could also face trade-offs with environmental sustainability through increased pollution and the depletion of non-renewable natural resources."

Distributional concerns are often addressed through redistributive policies or social safety nets. While necessary and desirable especially in poor countries, such policies may be fiscally unsustainable.

According to the policy brief, some schools of thought consider redistributive policies inimical to innovative entrepreneurship. But targeted innovation policy can also create synergies between economic and social Goals.

Developed countries can deploy new technologies in traditional industries that employ lower-skilled people or other disadvantaged groups. Related examples in developing countries include pro-poor innovation and agricultural innovation, as the associated productivity growth would disproportionally favour the worse off.

Innovation can provide synergies with environmental Goals, for example, by reducing the use of input, thereby decoupling environmental effects and economic activity, and by favouring economic transformation towards high-technology products that tend to reduce both resource use and pollution.

"Trade may add further synergies, as enhanced trade in green products could provide the necessary incentives for innovation and investment towards green structural transformation."

UNCTAD said that deploying specific technical standards and environmental regulation could further facilitate attaining environmental Goals; it could also generate employment and foster social achievements, though it would also tend to increase trade costs, with potentially adverse economic effects.

According to UNCTAD, this example also points to the need for evidence-based analysis and the exchange of experiences to understand whether the cause of trade-offs and synergies is rooted in national policies or in global processes and rules. Such an assessment would aim at identifying corrective action that is appropriate in a country's specific circumstances and stage of development.

"Given the likelihood of competing explanations based on different theoretical models, analysis and impact assessment would need to be complemented by peer review processes and debate as to what action should be taken, including in light of other countries' earlier experiences."

Role for UNCTAD

The policy brief said that the longstanding experience of UNCTAD in providing evidence-based analysis and integrated and coordinated policy support, technical cooperation and multi-stakeholder dialogues is a powerful vehicle to help ensure effective implementation and monitoring of a comprehensive and integrated approach to the 2030 Agenda for Sustainable Development and the Addis Ababa Action Agenda.

"As such, UNCTAD is ideally placed to play a central role in a follow-up and monitoring system that promotes a cross-cutting understanding of the significant inter-linkages across the various goals and targets."

UNCTAD said that the possible platforms that it could use to support member states in this process include its analytical products and policy review processes.

Another option would be the preparation, as an input to the High-level Political Forum on Sustainable Development, of an annual progress report on the implementation of the Sustainable Development Goals related to the integrated mandate of UNCTAD.

UNCTAD said re-purposing its statistical work for the needs of the 2030 Agenda for Sustainable Development would provide evidence-based support to the analysis and impact assessments.

It said: "These activities combined would alleviate the implementation and reporting burden at the national level, thereby facilitating the targeting of scarce financial and human resources to priority areas and adopting coherent national implementation strategies." *(SUNS8213)* ❐

Some ICs plan "modern trade deals" at WTO

A recent UK-convened meeting sought to explore new approaches and new issues for negotiations at the WTO.

by D. Ravi Kanth

GENEVA: Several industrial countries have begun some preliminary efforts to prepare the ground for what they call "modern trade deals" at the World Trade Organization.

If successful, such initiatives will end in fracturing the multilateral WTO, trade envoys told the *South-North Development Monitor (SUNS)*.

Some key elements of the major initiative will include graduation of "major developing countries" from special and differential treatment (S&DT), new digital trade and e-commerce, and open-ended plurilaterals in different areas, including services.

Close on the heels of notching success at the WTO's tenth Ministerial Conference (MC10) in Nairobi in December, trade envoys from Canada, Australia, Switzerland and New Zealand and former trade envoys of India and Bangladesh, among others, held a meeting convened by the United Kingdom's Foreign Office on 14-16 March to discuss a new trade agenda for addressing outstanding issues as well as new topics.

The high-profile Wilton Park Dialogue on "Unlocking the potential for the World Trade Organization to deliver modern trade deals" was convened to prepare the ground for negotiations with new approaches and new issues.

There was broad convergence at the meeting that a one-size-fits-all S&DT architecture for developing countries to address the outstanding issues in agriculture, industrial goods and services would not work, said participants familiar with the meeting.

The trade envoys discussed how to arrive at modalities that were increasingly becoming a den of hostage-taking, according to the participants who debriefed *SUNS*.

In services, there was a common understanding to pursue digital trade and e-commerce. The trade envoys also focused on how to pursue issues in a plurilateral format if they became difficult to negotiate in an open setting involving all WTO members.

The meeting sought to address how to build new trade deals based on the "successes" of the WTO's Trade Facilitation Agreement, the ministerial decision on export competition for farm products, and the Information Technology Agreement (ITA).

"However, these successes were delivered in spite of the persistent and fundamental divisions between members on the negotiating agenda of the WTO," the UK government argued in the agenda circulated for the meeting.

"For the first time," according to the agenda, "Ministers at MC10 acknowledged that the organization's membership is divided on how to progress future negotiations in the WTO.

"While recognizing the 'strong commitment of all Members to advance negotiations on the remaining Doha issues', it is clear a new approach is needed to deliver progress. Ministers also noted that some members will wish to identify and bring new issues to WTO negotiations.

"The WTO finds itself at a pivotal moment. The UK government is committed to international diplomatic engagement to ensure that the WTO re-establish itself as the driving force for global trade liberalization and the pre-eminent forum for trade negotiations. To deliver this ambition, it is clear that the flexibility, creativity and political will that has enabled these recent successes will need to be harnessed to provide a new framework for negotiations."

"Driving future progress"

In the agenda, the meeting participants were asked to deliver a set of recommendations on "how to codify best practice to drive future progress." "What has the WTO done well? Where have subject-specific negotiations and flexible approaches enabled progress?"

The chair of the WTO agriculture negotiations, Ambassador Vangelis Vitalis of New Zealand, and the Deputy Secretary-General of the United Nations Conference on Trade and Development (UNCTAD), Joakim Reiter, provided a detailed account on the outcomes of the Nairobi Ministerial Conference, particularly on what went well and what lessons could be learnt.

Canada's associate deputy foreign minister and trade envoy at the WTO, Ambassador Jonathan Fried, spoke on "Successful negotiations: what makes a good deal?" He answered several questions such as where the WTO negotiations had been successful and why.

The other questions included:

(i) What can be learnt from different approaches to negotiations in the WTO?

(ii) What are the negotiations that have enabled progress? What were the key factors in these?

(iii) Which negotiations have broken down – and what were the reasons behind these?

(iv) What enabled the conclusion of the Trade Facilitation Agreement?

(v) What has changed since 2001 and what areas of common interest can be found?

The participants, who included India's former trade envoy Ambassador Jayant Dasgupta, Bangladesh's former trade envoy Ambassador Debapriya Bhattacharya, Australia's trade envoy Hamish McCormick, Switzerland's Ambassador Remigi Winzap (who chairs the NAMA negotiating body in the WTO), senior World Bank official Anabel Gonzalez and Ricardo Melendez-Ortiz of the International Centre for Trade and Sustainable Development (ICTSD), addressed the following questions:

(i) What would a strengthened WTO that is more able to deliver modern trade deals look like?

(ii) In which policy areas or specific negotiations could new approaches be applied? Are these best pursued multilaterally or plurilaterally?

(iii) How to take forward the digital trade and e-commerce agenda?

(iv) How might the WTO use flexibilities to develop these new approaches?

(v) How can members use momentum from MC10 and Davos to build consensus in Geneva?

(vi) How to approach S&DT and allow countries at different stages of development to implement agreements at a different pace?

(vii) How to address the global goals?

(viii) How to support least developed countries to consider how their interests would be best serviced by a more open and flexible approach to WTO negotiations?

(ix) How might plurilateral negotiations help to effectively tackle the Doha and post-Doha agenda?

(x) How can plurilaterals be made more inclusive, helping developing countries like Kenya consider the benefits of joining the ITA, and making sure that new approaches do not leave much of the WTO membership behind?

(xi) In agriculture, learning from the success of delivering on the export competition pillar at MC10, can members turn their attention to domestic support and market access? Is a positive outcome on market access possible, given the proliferation of free trade agreements?

(xii) In non-agriculture market access, what has been already delivered through the plurilateral agenda and how can more countries benefit from this progress?

(xiii) Services: a focussed review on areas with the most potential to deliver progress in the WTO – digital trade and services bundled with goods. Do the plurilateral models of the Understanding on Financial Services or the Basic Telecoms Agreement offer alternative models for the way forward?

(xiv) Is there more space for an effective trade and development agenda and what might be the elements of that agenda?

(xv) Did Nairobi get us clear to delivering the Bali package for least developed countries and how can we make sure we do this?

(xvi) MC10 implementation: options on public stockholding by MC11 and what to do on the Special Safeguard Mechanism?

There was a common understanding, said one participant who attended the three-day meeting, that bite-sized, low-hanging fruit must be pursued given the complexities involved in the single undertaking of the WTO negotiations, which requires that nothing be agreed until everything is agreed. *(SUNS8210)* ❒

US business launches campaign against UNHLP

A UN panel which is looking at ways to promote access to medicines is in the crosshairs of US business lobbies intent on preserving strict intellectual property standards.

by D. Ravi Kanth

GENEVA: After scuttling globally beneficial obligations for sharing the latest technologies to combat climate change in the recent Paris Agreement, the powerful US industry and business lobbies have now launched a major campaign to undermine the United Nations High-Level Panel on Access to Medicines (UNHLP), according to a letter accessed by the *South-North Development Monitor (SUNS)*.

In the letter addressed to Senator Orrin Hatch, the chair of the US Senate Committee on Finance, in February, six leading American industry and business lobbies demanded an "effective inter-agency approach" – such as was adopted by the US delegation in the Paris UN climate talks in December – to other UN initiatives, particularly the UNHLP formed by the UN Development Programme (UNDP) in November 2015.

The six American lobbies were the Biotechnology Innovation Organization (BIO), National Association of Manufacturers (NAM), National Foreign Trade Council (NFTC), Pharmaceutical Research and Manufacturers of America (PhRMA), US Chamber of Commerce, and US Council for International Business (USCIB).

They cited the "effective inter-agency approach" under the leadership of the US State Department to "secure a final UNFCCC [UN Framework Convention on Climate Change] text [in Paris] that does not mention IP [intellectual property] and thus removes uncertainty that could have discouraged continued investments by US companies in clean technology."

The US lobbies maintained that "significant challenges to IP still remain in the Paris Agreement's implementation and subsequent negotiations – especially those related to the technology development and transfer chapter."

They invoked the dubious argument of safeguarding innovation and "maintaining the ability of US innovators to develop and disseminate solutions to society's great challenges," which is a euphemism for ensuring the most burdensome and onerous intellectual property commitments.

In the face of what they called proliferating challenges to IP protection within the UN system, the US lobbies wanted the administration to continue to adopt the inter-agency approach to jettison the UNHLP.

The UNHLP was set up "to review and assess proposals and recommend solutions for remedying the policy incoherence between the justifiable rights of inventors, international human rights law, trade rules and public health in the context of health technologies."

Panel membership

Coming at a time when the disease burden is multiplying in developing and poorest countries, which are unable to combat the most deadly cancer-related and other diseases because of IP provisions, the UNHLP has its task cut out.

The panel is jointly chaired by former Swiss President Ruth Dreifuss and former President of Botswana Festus Gontebanye Mogae. Dreifuss is respected all over the world for her sustained campaign against pharmaceutical giant Novartis, which refused to accept India's first compulsory licence for the cancer drug Glivec issued on public health grounds. Mogae provided leadership in tackling the HIV/AIDS problem by ensuring antiretroviral treatment to citizens in Botswana.

Along with these two eminent chairs, the UNHLP also includes several members drawn from the government, industry, public health institution and non-governmental sectors. The members include Andrew Witty, former chief executive officer of GlaxoSmithKline, Sakiko Fukuda-Parr, a development economist, Awn Al-Khasawneh, former prime minister of Jordan, Celso Amorim, former foreign minister of Brazil, Winnie Byanyima, executive director of Oxfam, Shiba Phurailatpam, an HIV patient and treatment activist, Malebona Precious Matsoso, director-general of the South African National Health Department, Yusuf Hamied, executive chairman of leading generic drug company Cipla, Michael Kiry, a retired Australian judge, Ruth Okediji, a law professor at Minnesota University Law School, Jorge Bermudez, former head of UNITAID, Kinga Goncz, a law professor from Hungary, Maria C. Freire, executive director of the US Foundation for the National Institutes of Health, and Stephen Lewis, an official of the advocacy organization AIDS-Free World.

Casting aspersions

The US business lobbies are on a warpath because the panel includes a range of people with different backgrounds and experiences and it might adopt a genuine inquiry into the policy incoherence that is responsible for denying humanitarian remedies.

"We are concerned … that the UNHLP process will not provide for an informed, balanced, and inclusive dialogue that adequately incorporates the perspectives of innovators," the lobbies claimed.

Casting aspersions on the selection process of the panel, the business lobbies raised vicious charges that the panel will not be able to assess "the complex issues impacting the development and deployment of health-related technologies."

"Based on the lack of balance evident in the background and views of Panel and advisory group members, as well as the lack of important context about the value of intellectual property in the Panel's supporting documents, it is unfortunately likely that the result of this process, while perhaps well-intentioned, will be ill-informed," the lobbies vehemently maintained.

The lobbies also downgraded work done by the World Health Organization, the UN specialized agency on health, with its Framework for Engagement with Non-State Actors (FENSA) as well as in the UN's global Technology Facilitation Mechanism.

In short, the lobbies claimed, "intergovernmental organizations that are discriminatory towards business, or that focus on a limited range of factors potentially inhibiting innovation deploy-

(continued on page 10)

Needed: revision to bond contracts, a debt workout mechanism

In the wake of Argentina's long-drawn run-in with "super holdout" bondholders, *Yuefen Li* puts forward some options for dealing with combative creditors and undertaking sovereign debt restructuring.

Argentina signed an agreement in principle on 29 February with four "super holdout" hedge funds, NML Capital, Aurelius Capital, Davidson Kempner and Bracebridge Capital.

Buenos Aires would pay them a total of about $4.65 billion, amounting to 75% of the principal and interest of all their claims on Argentina's bonds that were defaulted on during the 2001 debt crisis. This deal would allow the return of Argentina to the international capital market after 15 years of exclusion.

The payment is to be made in cash before 14 April, provided that the Argentine Congress approves the repeal of the country's domestic laws, namely the Lock Law and the Sovereign Payment Law, which prohibit the country from proposing terms to the holdouts that are better than those Argentina offered to its creditors in earlier restructurings.

The reason for calling the four hedge funds "super holdouts" is that they are the largest, the most combative and the most tenacious holdout creditors.

Argentina floated exchange bonds in 2005 and then again in 2010 after it had defaulted, during the 2001 debt crisis, on its bonds that were valued at nearly $100 billion. Ninety-three percent of the holders of Argentine restructured sovereign bonds accepted the exchange proposals at a considerable "haircut" (i.e., discount rate) of about 65%. The remaining 7% of the bondholders turned down the offers.

NML Capital first sued Argentina in 2003 for repayment of 100% of the face value of the bonds it held. As a result of the suit, US District Judge Thomas Griesa issued his *pari passu* ruling which prohibited Argentina from servicing its bonds before paying the holdouts. This led Argentina to default on its debt again in 2014.

To end the stalemate, the newly elected President of Argentina, Mauricio Macri, made resolving the holdout dispute a priority and in February 2016 offered to pay $6.5 billion to the group of six hedge fund holdouts. Two of the funds accepted the offer, but not NML and three other funds which asked for better terms.

Towards orderly debt workouts

The tactics and the business model the "super holdouts" used to get a windfall out of the legal battle, as well as the legal precedents this case left behind, may have potential negative systemic impact on future sovereign debt workouts. How can the negative impact be mitigated and future debt workouts made more timely and orderly?

Current efforts have concentrated on making it more difficult for holdouts to rush to the courts, through strengthening current contract clauses. However, the financial incentives to be "super holdouts" are immense.

NML and other holdout hedge funds have done everything within the law. Purchase of sovereign bonds on the secondary market at discount rates may be legal, but one can say that the business model of specializing in purchasing hugely undervalued bonds for the purpose of resorting to litigation and other means to force the distressed governments to pay the full face value is not ethical because it is at the expense of the ordinary taxpayers and the wellbeing of a sovereign state.

Additionally, Judge Griesa's *pari passu* injunction is a strong leverage for the holdouts against the bond issuer. This injunction may still be held as a precedent and be resorted to in the future – a bet for the bond issuer to lose the case.

Three approaches may be worth considering for the purpose of reducing the likelihood of recurrence of NML-style "super holdout" cases.

One approach is to reduce incentives for holdouts. It is common business practice for goods and services bought at huge discount in retail stores or via the Internet to come with clear stipulations that they either are not refundable or cannot be changed or returned. People take it for granted that it is a lawful and correct business practice. To buy things at Christmas sales and then go back to the store to request for refund of the full original price of the products would be considered unethical.

Why then is it so unlawful to reject the request of the "super holdout" to get paid 100% when the bonds were bought at a fraction of their face value?

Because sovereign bond contracts never mention that bonds bought at very deep discount on the secondary market would be treated differently in times of debt restructuring, the issuing state becomes bound to respect the bond contract and pay it at face value.

In the absence of a multilateral legal framework on sovereign debt restructuring, reducing incentives for holdouts may be done through revising the contractual terms for the bonds. In cases when the bonds were bought at a steep discount, there could be a contractual clause to limit the margin of returns to minimize the likelihood of litigating for 100% repayment.

Consideration could be given to adding a clause to bond contracts to the effect that "in case of a debt restructuring, the bondholders would be paid back no higher than x% of the purchase price of the bond." The percentage could be a range and take into consideration past holdout cases together with haircut levels of previous incidences of debt restructuring.

The range or specific percentage should allow sufficient profit margin and avoid the possibility of moral hazard of strategic default. In this way, secondary market operations would not be disrupted and hopefully the incentives for super holdouts could be diminished.

Other ways of reducing incentives for super holdouts should also be examined. For instance, the statutory penalty interest rates of some of the bonds Elliott Management – NML Capital's parent company – holds are exorbitantly high. According to the *Wall Street Journal*, these bonds would bring 10-15-fold returns to Elliott Management. Such arrangements give insane incentives to holdout bondholders.

Another way out is to explore whether it is really beneficial for the stability of the international financial markets not to regulate hedge funds specializing in debt holdout. At a time of increased social responsibilities for institutions in the real economy, more regulations in the banking sector and more specific codes of conduct for various business sectors, should there not also be some regulations and codes of conduct with respect to these hedge funds?

Finally, there have been repeated international efforts to establish an international debt workout regime or legal framework to deal with systemic issues relating to the "too little and too late" phenomenon for debt restructurings as well as the holdout problem.

The International Monetary Fund (IMF) tried in 2003. The United Nations General Assembly set up an ad hoc committee mandated to create a multilateral legal framework for sovereign debt restructuring in September 2014. As one outcome, in 2015, the committee formulated the "Basic Principles on Sovereign Debt Restructuring" based on years of research and consensus building in the UN Conference on Trade and Development (UNCTAD).

However, political resistance from the developed countries has made it difficult for the UN to push the work to a more inclusive and substantive phase. The Argentina case has proved once again the need for a debt workout mechanism. *(IPS)* ❐

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Ebola and Zika epidemics are driven by pathologies of society, not just a virus

Combating viral threats like Ebola and Zika demands that the economic and social ills afflicting vulnerable countries be addressed, writes *David Sanders*.

The global health threats posed by recent viral epidemics, such as avian flu, H1N1, Ebola and Zika, have been happening too frequently to be dismissed as coincidental.

Unless the global public health community invests in and develops better health systems that provide for the poor, such viruses will continue to spread and have severe effects.

The mosquito-borne Zika virus was declared a global public health emergency by the World Health Organization (WHO) in February due to an increase in the number of microcephaly cases in areas where the virus was found. Microcephaly is a birth defect where babies are born with abnormally small heads. A causal link between *in utero* exposure to the Zika virus and microcephaly has not yet been proven.

This is the first time since the Ebola epidemic hit Africa in 2014 that WHO has declared a global health emergency. Although the speed with which the organization reacted has been welcomed, mounting an emergency response is not sufficient to manage the spread of viral epidemics like Zika.

In the case of the Ebola outbreak, after a long delay, WHO called for an urgent change in three main areas. These included:

- rebuilding and strengthening national and international emergency preparedness and response;
- addressing the way new medical products are brought to market; and
- strengthening the way in which WHO operates during emergencies.

But the response has not been far-reaching enough to prevent similar viral outbreaks. The Zika virus is proof of this. Environmental, social and economic factors cause populations not previously affected by a particular disease to be exposed to its virus. To tackle such outbreaks in future, these factors must be addressed.

Containing the spread of a virus

Outbreaks happen for two reasons: the daily conditions that negatively affect the health of a country's inhabitants have not been addressed; and there are weak national health systems in place. There are several structural drivers that influence these, resulting in outbreaks and determining their severity. These include:

- the way populations move and migrate. This is compounded by generally poor access to (weak) healthcare services, especially for migrant populations.
- hybrid viruses that appear in food processing factories and increase the chances of human-animal interactions.
- increased interaction between humans and forest animals. This happens as indigent populations are forced deeper into forested areas to look for food.

This increased interaction is thought to be behind the spread of Ebola. Human beings were never the primary target of the virus. It is believed the virus was primarily found in a few species of fruit bats, which live in the tropical rainforests of central Africa.

Although central Africa has been the site of all earlier major Ebola outbreaks, it is hundreds of kilometres from the epicentre of the latest epidemic, which took place in West Africa. The geographic spread may be explained by poverty forcing people deeper into the forests in search of food, where they came into contact with the fruit bats or other animals infected by the bats.

How is the recent explosive Ebola outbreak explained? The answer lies not in the pathology of the disease but in the pathology of society, and the global political and economic architecture.

Economic exploitation is partly to blame

The spread of the Ebola epidemic was the result of poverty and the ruthless exploitation of the region's natural resources. Those afflicted, at least initially, were typically the poorest – those forced, by scarcity, to look for food in the forests, where they came into contact with animals harbouring the virus.

Economic exploitation also resulted in under-resourced and weak health systems that could not contain the spread of the virus.

Take Sierra Leone, for instance. Its iron ore mining industry has rapidly expanded, fuelling economic growth in the country of 20% in 2013, according to the International Monetary Fund. Interest in its largely untapped mineral resources sparked a flood of investment a decade after the end of the devastating 1991-2002 civil war. The country's economic growth rate is ranked among the highest in the world.

Yet in 2010 the country's mining industry contributed almost 60% of exports but only 8% of government revenue. In 2011, only one of the major mining firms in the country was paying corporate income tax, while none of the top five was reporting profits despite a boom in mineral exports.

Similarly, both Liberia and Guinea

have been heavily targeted by foreign companies. Liberia currently has the highest ratio of foreign direct investment to gross domestic product in the world. This largely is the result of foreign ownership of rubber production companies.

In Guinea, the area affected by Ebola attracted agribusiness shortly before the outbreak. In 2010, the British-backed Farm Land of Guinea Limited bought huge tracts of land for maize and soybean cultivation. And an Italian energy company has bought more than 700,000 hectares for biofuel crops.

These countries' dependence on extractive industries such as mining and logging, and financial losses due to tax evasion have left them impoverished and contributed to under-investment in – and the severe weakness of – their health systems.

It is no accident that the Ebola epidemic affected three of the poorest countries in the world.

Liberia, Guinea and Sierra Leone number 175, 179 and 183, respectively, out of 187 countries on the United Nations' Human Development Index. Their health systems are ineffective and almost nonexistent in many regions, affecting management of diseases.

In Sierra Leone, for example, in the four months following the outbreak of Ebola, 848 people were infected by the virus and 365 died. And in an average four months, the country sees about 650 deaths from meningitis, 670 from tuberculosis, 790 from HIV/AIDS, 845 from diarrhoea and more than 3,000 from malaria.

Such deaths have been occurring for decades, but with no previous focus on these countries.

Furthermore, in these three countries there is a persistent crisis of human resources, with a serious deficit of health workers, especially in rural areas. This is a result of long-term underproduction and continuing migration. More Liberian and Sierra Leonean medical doctors work in the US and the UK than in their home countries.

How to solve the problem

As a start, it is important to focus on crisis response. WHO had a feeble initial response to Ebola, in part because of cuts of more than 50% in its outbreak and response budget – the very budget line needed to respond to Ebola. This dropped from $469 million in 2012/2013 to $228 million in 2014/2015, mainly because member states, particularly rich ones, failed to pay their financial contributions.

But managing viral epidemics requires that authorities look beyond the immediate crisis response. A major and sustained investment in human resources is required. Initially, this will require greatly increased donor assistance.

In the medium term, there is an urgent need to strengthen health systems in the region. Although talk of "health systems strengthening" has become commonplace, there is little evidence of this in several African countries.

But the most sustainable solution requires fundamental changes to economic and power relations between these countries and the capitalist economies and enterprises that continue to bleed them dry, often with the collusion of local officials and elites. ❒

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ment, undermine evidence-based policy-making and hobble the delivery of solutions to healthcare and other sustainability challenges".

The continued crusade against "inter-governmental organizations" by the US lobbies is not something new. Whenever any panel is formed at an inter-governmental organization, the US business lobbies go into overkill to ensure that the panel members are tainted if they adopt genuinely people- and development-centred positions.

Time and again US negotiators have ensured that the country's heavily subsidized "innovators" continue to reap monopoly profits through IP protection at the cost of worsening global epidemics and climate change problems.

The US administration has also adopted similar tactics in the global trade negotiations, in which it has aggressively ensured that the developmental concerns of the developing countries are trumped by the concerns of its egregiously subsidized farm groups.

The US led the efforts to try to dismantle the Doha Development Agenda (DDA) trade negotiations in Nairobi over three months ago. It is an open secret that the DDA negotiations stood in the way of Washington's pursuit of perpetuating inequities and distortions stemming from the previous Uruguay Round of trade negotiations.

Unless the developing and poorest countries adopt common positions to secure credible and developmental outcomes for addressing global challenges, they will continue to face defeat after defeat in crafting major international agreements. Invariably, according to several developing-country envoys, it is a battle between the profit-centred American positions on the one side, and life-and-death survival concerns of poor countries on the other. *(SUNS8215)* ❒

Development through industrialization

The following extract from a report by international development NGO ActionAid considers how developing countries can engage in higher-value-added manufacturing by learning from success stories of the past and overcoming present-day barriers to industrialization.

Industrialization in the past: factors for success

In the 1960s and 1970s, many governments around the world actively intervened in the economy to encourage industrialization. Rather than relying exclusively on their static comparative advantage, or what they already had, successful industrializers exploited their dynamic comparative advantage, or what they could develop. Like with some of the best entrepreneurs, many of the strategies they tried out failed, but those that succeeded propelled rapid economic transformation.

Implementing successful industrial policies is a learning process. Governments worked with a range of experts – engineers, managers, business owners, investors – to identify and respond to blockages and obstacles to the emergence of new sectors. They balanced high-risk investment in emerging and capital-intensive manufacturing with support for industries and sectors that can be relied on to provide employment or export earnings.

Critics are right to point out that some of these efforts were less successful than others, pointing to the legacy of industrial policy in some countries in South America and sub-Saharan Africa. Import substitution policies come in for particular criticism; that is, where measures are put in place to prevent imports of products governments were encouraging firms to produce at home. But the wholesale rejection of import substitution as a strategy misses the point. Almost all industrialized countries, including some of the most successful, started out by restricting imports of manufactured goods and by allocating subsidies to emerging sectors.

Even those that are the greatest proponents of liberalization and deregulation today protected and supported emerging sectors in the past. Britain maintained high tariffs on manufacturing until as late as the 1820s. Between 1816 and the end of World War II, the US had one of the world's highest average tariff rates on manufacturing imports. Other European countries provided emerging industries with subsidies, financing and monopoly rights, and invested in research and technology. The US government continues to invest heavily in specific firms and products as well as upstream research and development.

So what distinguished successful industrializers from those who were less successful?

Discipline firms as well as protecting them

Economist Alice Amsden spent decades combining theory, quantitative analysis and careful fieldwork in East Asia: she argued that the successful industrializers used import substitution policies, but made support conditional on firms meeting certain results-oriented performance standards. She called this the "reciprocal control mechanism" and argued that it was the key factor in successful industrialization in East Asia.

Firms receiving support were compelled to improve their production processes. Performance standards included export targets, local content requirements, debt-equity ratios and others. If firms failed to fulfil the performance requirements, they lost the subsidies.

Tackling inequality was a key factor in whether or not government had the leverage over domestic elites needed to bring about industrialization. In Asia, a relatively equal distribution of land ownership drove wealthy individuals to invest in new productive industries rather than in land. But in South America, elites were able to generate rents through their ownership of large tracts of land; as a result, they avoided more risky investments in industry. Where there are high levels of inequality, governments are prone to using subsidies as a way of preventing social unrest, rather than targeting them carefully to well-performing industries. Both of these forms of inequality make it very difficult for government to impose performance requirements on investors.

Looking at the successful industrialization strategies of South Korea and Taiwan can show us how these reciprocal control mechanisms worked in practice. The industrialization path of these countries had a dark side, involving suppression of unions, low wages and environmental damage. Nonetheless, lessons can still be drawn from what they managed to achieve.

South Korea's industrialization was led by "national leaders", or large firms with quasi-monopolistic rights. From the 1960s on, Korea protected textiles and later heavy industries from competition by putting in place tariffs, quotas, export subsidies, credit and other measures. Price controls were used to curb monopoly power and harsh capital controls played a role in preventing capital flight. Subsidies were subject to performance, notably against export targets.

Export targets were agreed at monthly meetings between government and business, which the president attended – these meetings helped bureaucrats learn about and address the problems that prevented businesses from exporting more. Representatives of Korean development banks visited firms and engaged with engineers on the shop floor, helping and encouraging them to improve the quality and efficiency of their production. Firms that responded to performance-based incentives received further support. In contrast, if a targeted firm was a poor performer, it ceased being subsidized. If a firm went bankrupt, the state simply refused to bail it out.

Taiwan's manufacturing sector is made up of lots of smaller firms working together and with foreign investors. Success was built on strong linkages between domestic firms and foreign investors, who were able to take advantage of the export opportunities offered by international trade. The 150 engineers in Taiwan's Industrial Development Bureau worked closely with domestic firms to help them improve the quality and reduce the price of their products. But they also worked to encourage investors to source inputs from Taiwan.

For example, the Bureau worked with the foreign investment board to ensure that applications by Phillips' Taiwanese subsidiary to import glass for television sets were subject to significant delays. This was sufficiently inconvenient to prompt Phillips to explore the potential of sourcing from local suppliers, which gave Taiwanese firms enough confidence to invest in improving production. After two Taiwanese glassmakers demonstrated that they were able to produce high-quality glass at competitive prices, Phillips stopped importing and sourced from these firms instead.

Build on existing technology

Of course, in order to improve the efficiency and quality of their production, firms need access to technology and know-how. In some cases, whether by accident or design, technology is developed based on a genuinely new discovery – usually involving significant state investment. But in most cases, firms use and adapt existing technology, building on what was already available to create something new. One of the key markers of the success of industrial policy was whether or not firms were able to learn from and innovate using existing technology.

Argentina and Mexico had historically high levels of foreign investment. In theory, these investors could have played an important role in sharing skills and new technology with domestic firms. However, in practice foreign firms spent virtually nothing on science and technology. Instead, investors "crowded out" the domestic firms that may have made such investments, putting these less competitive companies out of business. Research on the textile industry in Mauritius and Bangladesh in the 1980s found similar results: "only a few of the 15 multinationals surveyed helped domestic firms acquire new technology."

In contrast, successful East Asian economies chose to invest directly in new, risky ventures, learning from and building upon existing technology to establish modern industries. Instead of relying on foreign investors, firms bought technology or tried to figure out how it worked and copied it – this is known as "reverse engineering". Accessing the technology was only part of the equation – firms also needed to learn how to use it. The more advanced technology became, the more skill was required. So investment in skills, including project planning and management as well as engineering skills, was crucial. In China, India, Korea and Taiwan, the governments catalyzed the development of new technology by putting in place requirements and incentives for nationally owned or financed firms to invest in research and development.

Keep going long enough to get results

For successful industrialization, governments and firms need an environment conducive to learning – where they can try things out and make mistakes. Some countries will have more learning to do than others. Successful industrializers in East Asia had a strong base of manufacturing experience to build on and a long history of regional trade in manufactured goods. In contrast, Africa's colonial history left the continent largely without manufacturing experience.

In the 1960s and 1970s, newly independent African states made significant efforts to make up for lost time. It was obvious that their newly formed bureaucracies were still learning. Nonetheless, despite the lack of manufacturing and planning experience and the dire state of infrastructure on the continent, nascent manufacturing industries started to emerge.

This industry was still relatively weak and required significant levels of support. In many countries, periods of industrialization were interrupted by political instability and conflict. Nonetheless, with more time for officials to build expertise and to try out different policies and more time for nascent industries to improve their production processes, a relatively healthy manufacturing sector could have developed.

But the imposition of structural adjustment policies in the 1980s meant that support was suddenly withdrawn; many domestic businesses did not survive strong competition from foreign competitors with more experience and better access to finance. Developed-country tariffs on manufactured goods were much higher than those on raw materials, discouraging African exporters from entering into higher-value-added activities.

This has had serious consequences for working people. In the past decade, sub-Saharan Africa has seen rapid growth rates, but these were largely due to high commodity prices. Wealthy elites have seen the benefits of growth, but these benefits haven't trickled down to the rest of the population. In many countries, large proportions of the labour force have been forced into very-low-productivity agriculture and informal activities, which arguably does more to disguise unemployment than it does to create jobs.

In spite of the continent's deindustrialization, there is still a base of experience to build on. In Kenya, between 1990 and 2007, virtually no new jobs were created in the formal manufacturing sector. But over this same period, the number of jobs in informal manufacturing increased from just over 300,000 to almost 1.6 million. Kenya is not unique: statistics from Nigeria indicate that half of the 11% of the population engaged in manufacturing work in the informal sector.

The importance of agriculture

No country has managed to industrialize successfully without investing in agricultural productivity. Increasing productivity in agriculture reduces the number of people required to work on farms, freeing them up to work in newly established factories. Agriculture plays an important role in providing food for urban populations and raw materials for industry. Agricultural surpluses increase rural incomes, driving consumer demand for new products.

Developing an agricultural processing sector is often the first rung on the industrialization ladder, increasing value-added significantly as compared to exporting raw commodities. It has the potential to contribute to the growth of the rural non-farm economy, creating jobs closer to where people in poverty are living. By keeping food prices in check, it limits inflation, allowing wages in factories to be relatively low. It also links the rural economy into the industrial economy, facilitating more equal distribution of the benefits of industrialization.

Investment in agriculture also ensures that industrialization is equitable: pursuing industrial development without investment in agriculture risks trapping people in poverty. About two-thirds of those living in poverty live in rural areas, and agriculture provides work for an estimated 1.3 billion smallholders and landless workers. Agricultural growth is associated with two to five times greater poverty reduction compared to growth in manufacturing or services. Broad-based rural industrialization in Taiwan and China is strongly associated with redistributive land reform.

Unfortunately, neglect of agriculture has characterized economic development in many parts of South Asia and South America as well as sub-Saharan Africa.

New realities for industrialization

While there is growing recognition of the role of industrial policies in the success stories of the 1980s, there is also a growing concern that the global economy has changed so fundamentally in the past few decades that these lessons may no longer be relevant.

Unable to break into high-value segments of the value chain, or to generate substantial levels of employment in the small niches of the chain they occupy, countries with small manufacturing sectors are moving into services much more quickly than happened in the past. Developing countries without an established manufacturing sector are finding it hard to compete with established suppliers, who have the infrastructure and economies of scale that allow them to supply at much lower prices than new entrants can manage.

In light of the challenges associated with upgrading within global value chains, some argue that the industrialization path pursued by now-industrialized countries is no longer available to developing countries.

Will services replace manufacturing?

In countries with small or non-existent manufacturing sectors, the services sector often provides work for a large proportion of the population and contributes a significant proportion to GDP. Some analysts suggest that modern services like transport, finance and telecommunications can foster economic transformation just as manufacturing did in the past.

Unfortunately only a handful of services are productive and tradable, like manufacturing. The vast majority of services can't be traded on international markets. They are the bread and butter of our societies, but the wages that retail and care services attract depend on how much other people in the society earn and how able they are to pay well for services they value highly. The only ways to increase productivity in these non-tradable services are to push down wages or to cut corners.

Well-paid jobs in the service sector are few and far between. In India, high-value services in finance, insurance, real estate, IT and telecommunications account for nearly 20% of GDP. But those sectors only employ 2% of the workforce. In the US, total employment in six of the most innovative firms – Apple, Microsoft, Facebook, Cisco, Google and Amazon – was 291,391 in 2012. This is about an eighth of Walmart's 2.2 million employees in 2011.

Even in the world's richest economies, the jobs market is hollowing out in the middle, dividing between low-paid jobs in care, retail and hospitality for the majority and highly-paid jobs in finance, law and IT for the lucky few. This trend goes to the extreme in developing countries where the absence of alternatives drives the vast majority into precarious and underpaid jobs in the informal sector, while elites and a small middle class secure well-paid jobs in global service industries.

In a recent study of 21 low- and middle-income countries, the Hay Group found that wage disparities between skilled workers and senior managers increased by 12% between 2008 and 2014. It's notable that they didn't study the gap between the highest-paid and lowest-paid workers, but used a more conservative estimate of the gap between two increasingly polarized groups of employees.

International Monetary Fund (IMF) analysis shows that if the share of global income going to the bottom 20% increases, GDP increases over the medium term. GDP growth is also associated with an increasing share of income going to the middle classes. In contrast, an increase in the share of income going to the top 20% is associated with falling GDP.

The services sector is unlikely to replace manufacturing as a driver of growth. In fact, a key factor in determining whether the service sector can create and sustain high levels of employment is the linkages between services and manufacturing. A key factor in determining whether countries can capture the profit associated with manufacturing is whether they have managed to diversify into the service segments of the production chain, like design and marketing.

Opportunities and challenges with global value chains

Global value chains have existed for a long time, and countries like Taiwan and South Korea participated in these production networks as part of their industrialization strategy. But these networks have become dramatically more fragmented than they were in the past.

Production of a final product or service has been divided and subdivided into a long sequence of separate tasks. Revolutions in transport and communications mean that each of these tasks can be carried out in a different location, often in a completely different part of the world. Global trade in intermediaries, or inputs and unfinished products, has exploded.

The fragmentation of global value chains presents an opportunity insofar as countries with limited or no manufacturing experience may find it easier to develop a manufacturing sector. Rather than having to put in place the network of different industries necessary to develop a final product, they can specialize in one segment of the value chain, importing inputs and exporting components of products that will be finalized elsewhere. Foreign investors have the capital, technology and know-how to establish higher-value-added activities more quickly than domestic firms could. Parent firms or global buyers can push domestic firms to improve their supply-side capacity through the quality standards they demand, just as some governments have done in the past, for example in Taiwan.

But these changes also limit the potential for industrialization. Many developing countries that are integrated into global supply chains are stuck in low-value-added segments of production and struggle to move into more profitable activities. They may struggle to meet quality standards associated with higher-value products, whether these are set by parent firms in a multinational group, by independent buyers or by importing governments.

Even if they can break into higher-value-added production, their position within the global supply chain means that firms don't have enough control over where different tasks are carried out to source goods and services from other domestic firms. The success of a firm that is linked into a global value chain may not spill over into the rest of the economy by generating work for employees of other businesses. This can make such firms highly vulnerable to financial or economic crisis, or falling demand in key export markets.

As production has fragmented, low-value activities have become less and less profitable. In the early 1980s, producing countries received about half of the total income from the sale of coffee. Today, 90% of the income goes to the country where a multinational's headquarters is located or buyers are based. The price of low-technology products that developing countries tend to specialize in – like garments, footwear, furniture and toys – dropped by approximately 40%, relative to US consumer prices, between 1986 and 2006. Part of this price drop reflects lower costs of trade and transport, but part of it reflects the competition among suppliers to provide goods at lower and lower prices. In low-technology manufacturing, the easiest way to reduce costs is to reduce wages.

As low-value activities become less profitable, more and more profit is associated with intangible activities and manufacturing-related services like design and marketing. These activities tend to be located in countries where parent firms and buyers are based or in low-tax jurisdictions.

ActionAid calculations show that a single fashion designer in the US, paid $6,133 a month on average, earns more than the combined monthly wages of 27 garment workers in Asia.

These changes aren't just due to increased competition among all firms. Rather, they are a result of the degree to which multinationals or buyers in global value chains control the market – and the degree to which society is willing to subsidize their profit margins.

There are relatively few global players; in many industries, global oligopolies consolidate their market power through product differentiation and brand, making it more difficult for new players to enter the market. In contrast, the market is saturated with many suppliers doing more or less the same thing. Buyers are able to play suppliers against each other to source products at lower and lower prices. This allows multinationals to maintain and increase their profit margins even as prices fall – US firms have increased profits as a proportion of value created in the US from approximately 24% in 1986 to approximately 32% in 2006.

Global rules limit the range of industrial policy tools available

Changes in global economic regulations have made it much easier for powerful multinationals to move goods, services and profits around the world. Investment treaties and clauses in investment contracts protect investors from changes in domestic regulations that might have an impact on their profits. The global network of tax treaties facilitates transfer of profits into low-tax jurisdictions.

While today's industrialized countries used a range of policies to protect and promote emerging industries, including a combination of import substitution and export orientation, many of these policies are now unavailable to developing-country governments. In some cases they are prohibited under trade and investment rules, in other cases use of these policies puts aid receipts at threat.

Despite the lessons of the recent global economic crisis, deregulation, privatization and liberalization remain ubiquitous in the advice that the World Bank group and other donors give to developing-country governments. The weakness of states in sub-Saharan Africa is due at least in part to privatization and liberalization policies promoted by donors like the World Bank. The "good governance" agenda, while it sounds like a good thing, continues to push developing-country governments to become more "efficient" rather than promoting institutions and policies that promote learning, which are crucial for structural transformation.

World Trade Organization (WTO) negotiations have stalled for many years, but trade liberalization and negotiations on non-trade matters continue apace through bilateral, mega-regional and plurilateral agreements, with the intention that these approaches will be "multilateralized" or incorporated into WTO rules in the near future. Since the 1980s, global rules have become more and more restrictive, outlawing many of the strategies followed by countries that have already industrialized successfully.

Crucially, the export performance requirements that were a core part of the reciprocal control mechanism in East Asia are no longer easy to apply. Subsidies contingent on domestic sourcing or export performance are prohibited under WTO rules.

WTO rules and bilateral trade and investment agreements prevent governments from getting the best out of foreign investment: requirements for investors to share technology and know-how and to source from local suppliers are increasingly difficult to apply. New-generation trade and investment agreements cover an even wider range of issues, including competition policy, government procurement and other policy tools to promote industrialization.

In the past, governments could take the risk of bending the rules; if another government challenged them and they lost a dispute at the WTO, they would be asked to stop or, if they weren't prepared to do so, to pay compensation. Trade disputes might take several years – in the meantime the policy could continue to be applied. Under investor-state dispute provisions in new trade and investment agreements, foreign investors are able to sue governments directly in international arbitration for implementing policies that discriminate in favour of domestic firms or that threaten investors' future profits. If governments lose, they could be liable to pay the investor millions of dollars in compensation. Even if they win, the costs of defending an investment dispute far exceed those of defending a WTO dispute.

In the light of these restrictions, governments may choose to turn to other tools like competition policy and monetary policy to catalyze industrialization. But using these tools usually requires a better-financed bureaucracy than most developing countries can afford.

Global rules protect powerful players, not workers

Proponents of industrial policy often focus on how international economic regulations limit the policy space of developing-country governments. But they shouldn't forget the other ways that global rules reinforce the status quo. Global rules consolidate the power of firms from already industrialized countries, making it difficult for new firms to enter the market. At the same time, they undermine the power of workers.

Once their manufacturing sectors were competitive, European and North American governments used a range of policies to reinforce the competitive advantage of those industries, attempting to stifle industrialization elsewhere and forcing developing countries to open their markets. Britain also put in place policies to prevent industrialization in its colonies. This had long-term consequences for new firms trying to enter the market: "the same multinational companies whose innovations had secured them market power in the late nineteenth century were still exercising that power over nascent companies in 'the rest' in the late twentieth century."

The skills, technology and brands of dominant firms are protected by what is arguably the only effective international regulatory regime, the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). Proponents of such protectionism argue that firms would not invest in innovation if they couldn't guarantee that they would profit from its exploitation. But the reality is that rather than incentivizing and rewarding research and innovation, intellectual property is increasingly used to shore up the competitive advantage of dominant multinationals.

This system is exacerbated by the global tax system. It is almost impossible to say what intangible assets like brands and patents are worth, and so it is easy to claim that they generate a very high proportion of the profit realized from the sale of a product. Because they are intangible, these assets are easily moved into tax havens and low-tax regimes, many of which are controlled by the world's richest economies.

Mariana Mazzucato – one of the three most important thinkers about innovation, according to the *New Republic* – argues that these tax breaks are not even effective in terms of catalyzing innovation in the OECD. By offering tax breaks on income associated with patents rather than the research itself, governments further inflate profits already protected by intellectual property law. All this does is reduce government revenue, while failing to make research happen that would not have happened anyway.

Intellectual property laws protect profits associated with intangible assets like brand, but there is no international legal regime to ensure that workers in the retail sector selling those branded goods are paid a living wage. In fact, at the same time as intellectual property law has got stronger, regulations to protect workers have got weaker.

The past 30 years have seen an erosion of labour rights, increasing economic insecurity for workers. Foreign investors can threaten to move their operations to another country, giving them more bargaining power with governments than workers have. Countries have been engaged in a race to the bottom to attract investment and to provide ever-cheaper products to international buyers. Labour market flexibility – where it is easier to fire workers and employ them on precarious contracts – reduces the bargaining power of lower-income workers.

The World Bank and others have claimed that labour rights contribute to unemployment by increasing the cost of labour and pushing more workers out of the formal sector into vulnerable, informal employment. But empirical studies show that they have at most a modest impact on the number of jobs available. On the plus side, labour rights are associated with increases in the total income of low-paid workers and have been critical when countries faced dramatic changes, whether rapid growth or economic collapse.

New strategies and signs of change

Opportunities to change global rules

Recently, some developing countries have begun pushing back against restrictive global rules to get more out of their negotiations with foreign investors. For example, in 2010 South Africa carried out a detailed assessment, in collaboration with the domestic private sector, of the costs and benefits of the international investment agreements they had signed. They found that these agreements had no impact on the decision of an investor to locate in South Africa. Rather, the provisions of these agreements prevented the country from putting in place public policy measures to tackle inequality.

In response, South Africa began to unilaterally revoke its bilateral investment agreements or to let them lapse, replacing them with a domestic investment strategy. For example, South Africa has made support to the car industry conditional on export performance: "the way the programme was structured was if [a manufacturer] exported, [the firm] could reap the export duty but only if its exports were at the competitive price and if it had improved its efficiencies."

South Africa joins Brazil, Argentina, Bolivia, Ecuador and Indonesia in rejecting or renegotiating investment agreements. In the next few years it will be possible to unilaterally revoke almost half of all bilateral investment agreements. Momentum is building.

At the same time, developed countries are ignoring many of the global rules that prohibit industrial policies, undermining their credibility and reinforcing the need for change. For example, direct support to the automobile industry and policies to encourage car sales were common responses to the 2008-09 crisis: the US bailout of General Motors and Chrysler received extensive attention, but other countries adopted similar strategies, including Canada, China, Estonia, France, Israel, Japan, the Netherlands, Norway, Portugal, South Korea, Spain and the UK. In another well-publicized example, the WTO has ruled that subsidies to Boeing and Airbus are illegal, but the EU and the US continue to support their respective airline companies.

New strategies for fragmented value chains

But even with more policy space, developing countries are faced with changes in the reality of global trade. More fragmented value chains mean that governments have much less leverage over production choices and that multinationals have much more power. Governments need to get better at negotiating with multinationals and getting the best out of foreign investment.

Key policies to get the best out of participation in value chains include local content rules and technology transfer requirements. Governments need to make a greater effort to support the growth of high-value segments like design and marketing that might have been more closely integrated with physical production in the past.

Local content rules are widely used in the oil and gas sectors, as well as being key in the development of the motorcycle industry in Vietnam, for example. These policies try to prevent the development of enclave investments with few links to the local economy. Of course, local content rules are not enough by themselves: as above, governments will need to support and compel domestic firms to improve the quality of their production.

In China, the government required foreign investors to form joint ventures with Chinese companies, most of which were state-owned or closely linked to the state. The government also acquired foreign companies with more advanced technology and put in place incentives for foreign firms to carry out research and development in China. Performance requirements in Singapore have led foreign investors to locate research and development activities in the state, resulting in innovation in production processes.

Governments should take advantage of the potential for technology transfer to spur further innovation. State investment in cutting-edge, green industries is a good direction, not just because it is part of the response to climate change, but also because it is a relatively new sector, with more potential for developing countries to get involved in the high-value innovative segments of the chain before these become dominated by powerful global oligopolies. This is crucial in order to maximize the potential of manufacturing to generate profits and well-paid jobs and to spur innovation in the rest of the economy.

Commercial pressures on workers' rights in global value chains make it all the more urgent to ensure that workers' rights are protected. In the past, governments and firms colluded in keeping wages low in the manufacturing sector in order to keep their exports competitive. This has had horrific consequences for women's economic inequality. However, if governments stop competing with their regional neighbours and instead cooperate to implement and enforce a living wage and other labour rights, this could catalyze a race to the top, helping them escape the threat of companies taking their business elsewhere.

To support their efforts, governments may want to tap into the pressure that campaigners in developed countries can put on multinationals to improve working conditions in their supply chain. Governments could supplement these efforts by requiring investors to employ local people and invest in training and skills development.

Far from undermining growth, these efforts can reinforce industrial policies. Higher wages across an entire region would stimulate regional demand, offering an alternative to traditional export markets in the developed countries, where consumer demand is stagnating. ❐

The above is extracted from "What a way to make a living: Using industrial policy to create more and better jobs", a report written by Ruth Kelly and published by ActionAid (March 2016). The full report with references is available on www.actionaid.org.uk.