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APPROACHES TO POVERTY ERADICATION AND ECONOMIC DEVELOPMENT I

Beware of the Natives!

AS THE SECOND WORLD WAR ended, the uninformed would have been justified to think that all America breathed a huge sigh of relief. After all, the great danger had passed. The establishment of the United Nations by the victorious allies, with its Charter, and the adoption of the Universal Declaration on Human Rights, marked the dawn of a new age of world peace and freedom from fear.

In any event, except for the attack at Pearl Harbour, the costly war had not touched the shores of America. The German submarines, the battleships, the new rockets, and the Luftwaffe could not cross the Atlantic to do damage to the American mainland. Neither could the Japanese war machine overcome the Pacific barrier and descend on California and the State of Washington.

And now, the Axis Powers had been routed. They had had no choice but to surrender unconditionally. The victors occupied their territories. The future of their peoples would be decided by the conquerors. They would have neither the right nor the power to threaten world peace again.

Nevertheless, as the Second World War ended, a new fear gripped the United States - the fear of Communism. Nothing would stir American passions more than the alarm call - the Russians are coming!

In this situation, Senator Joe McCarthy elected to cast himself in the role of the super-patriot. He determined that some ideas and activities, as he decreed, were communist and therefore un-American. He therefore embarked on a crusade to identify and persecute those he considered un-American Americans. Some Americans applauded or snitched on fellow-Americans, driven by the fear - the Russians are coming!

Outside the United States, a multifaceted struggle against the post-war enemy was waged, based on the three objectives of deterrence, containment and destruction.

In time the Russians were defeated. What Winston Churchill had described as the Iron Curtain came down. The Soviet Union ceased to exist. Socialism in Europe collapsed. The United States and its allies had won the Cold War.

They had defeated their Second World War ally who had turned into their post-war enemy. The communist threat was no more. When and if the Russians came, they would do so as friends and as the vanquished.

The uninformed would have been justified to think that all America breathed a huge sigh of relief, content that with the fear of communism having been banished, there would not emerge another threat that would drive all patriotic Americans back to the barricades.

And, God willing, there would not emerge a new super-patriot like Senator Joe McCarthy, to threaten the civil liberties of American patriots, pretending to respond to the alarm call - the Russians (or other enemies) are coming!

But the new-hopefuls would have been as wrong as were the hopefuls of 1945. A new fear gripped the United States because new enemies were on their way. The new alarm call was - the terrorists are coming! And then with deadly intent and results, they came on 11 September 2001.

In their wake some evil-minded people used the US Mail to spread the poisonous anthrax, which claimed a few lives. This confirmed the alarm call - the terrorists are coming, armed with weapons of mass destruction! There was now no new United Nations with a new Charter, and no new Declaration on Human Rights to convey the assurance of world peace and freedom from fear.

And neither were the Atlantic and the Pacific too wide and too deep to block the arrival of the terrorists. Those elected to take charge of the United States decided that the new enemy had to be fought at home and abroad. At home the Homeland Security system was put in place and the Patriot Act passed.

For the rest of the world, the doctrine of pre-emptive strike was adopted and implemented. This time there would be no space for the pursuit of the objectives of deterrence and containment. The enemy had to be destroyed before it could deliver its own mortal blow!

The threat of the poor

But necessarily the question had to be asked and was posed - but whence the terrorists! And so it came about that the poor of the world began to emerge as a threat to those who have much to lose.

The March/April 2002 edition of the prestigious journal 'Foreign Affairs' published an article with the menacing title, "The Reluctant Imperialist: Terrorism, Failed States, and the Case of American Empire", written by Sebastian Mallaby, a columnist of 'The Washington Post'.

He wrote about poverty producing violent disorder in poor countries, with the disorder leading to further poverty, instability and violence. To this he added the impact of high birth rates and AIDS, which he said further threatened social disintegration and government collapse, leading to the emergence of failed states. All this, he said, offers opportunities to terrorists to find sanctuaries. To save themselves, the US and its allies had to learn to love imperialism!

Thus Mallaby made the firm suggestion that in addition to destroying the terrorists through pre-emptive strikes, everything had to be done to deny them their sanctuaries. Obviously greatly disturbed, he said the chaos in the world was too threatening to ignore. The rich man could not but carry the burden of its elimination, in his own interest.

And so by this circuitous route, we arrive at a variation of the policy of containment adopted by the US and its allies in its struggle against the Soviet Union and socialism.

At that time, containment included denying the enemy, the communists, any sanctuaries. The opponents of the Soviet Union determined that poverty and failed economies would inevitably result in restlessness among the poverty-stricken masses and their seduction by the promise of a bright communist future.

What had to be done to save the United States and its capitalist allies was to rescue the poor from failed economies and poverty. Thus would they and the world be saved from communism. The collective of hungry stomachs in particular areas of the world became the rich man's burden.

As a result of this, in the period since the Second World War, the world has experienced three successful development programmes specifically and consciously aimed at the eradication of poverty and underdevelopment. The results they achieved demonstrated that it is indeed possible to eradicate these social ills.

They also demonstrated that such success required the necessary political will on the part of the rich. They also told the plain story that for the rich to part with what they have, even in their long term self-interest, they needed to be frightened virtually out of their wits. And so we all learnt the lesson that a looming perceived defeat concentrates the mind wonderfully.

To ensure that Western Europe avoided the clutches of the communists who sat in positions of power in the Soviet Union and the countries of eastern and central Europe, and had a large following within the countries of Western Europe, the US poured resources into these countries through the Marshall Plan.

A US State Department document dated 26 August 1947, entitled "Summary of Department's Position on the Content of a European Recovery Program", said of one of the fundamental objectives of the Marshall Plan: "Basic objective of program is to move entire area progressively from present condition to working economy independent of abnormal outside support, taking full account of basic changes in European conditions such as political developments in Eastern Europe, altered position of former colonial territories, and loss of overseas assets, merchant shipping and other prewar invisible exports."

And, indeed, within a relatively short period of time, the economy of the entire area was moved from its immediate post-war condition of crisis, and re-established as a working economy, independent of abnormal outside support.

The same happy fate befell the Asian Far East. Again the overriding impulse to do in the Far East what had been done in Western Europe, was fear of communism. Japan, South Korea, Chinese Taiwan and other countries of Asia were seen as likely candidates for socialist revolutions. To contain any influence from the Soviet Union, China and North Korea, they too became beneficiaries of a development programme that resulted in the "Japanese miracle" and the emergence of the "Asian tigers".

The West European and Far East Asian Economic Recovery Programmes both met their goals and proved that it was possible to carry out successful development programmes to defeat poverty and underdevelopment.

The third successful post-war development programme, a direct outgrowth of the Marshall Plan, with its political objectives, is currently being implemented. This is the European Union Regional Policy, which is focused on the eradication of the poverty and underdevelopment manifested in certain regions within the Member States of the European Union (EU).

The 15-member EU had set itself the goal to achieve this objective in one generation. The 25-member Union says it will now achieve this goal in two generations, given the greater poverty and underdevelopment of the 10 new members.

Fear is the mother of invention

History has established the fact that fear is the mother of invention. It is therefore very tempting that we too, the African natives, should drive fear into the heart of the rich, to convince them to embark on yet another successful development programme to help rid our continent of levels of poverty and underdevelopment much worse than those experienced by the 10 new members of the EU.

To do this we would have to convince them about what they suspect already, that among us, because of our poverty, lurk many terrorists that are intent on causing them grievous harm. We would have to sound the alarm bell - the Natives are coming!

We would so pound the African drum that the rich would scramble to embark on a new Africa Recovery Programme, drawing on the lessons of the West European and Far East Asian development programmes, with no need to impose on us a new American imperialism!

This time round, we would propagate the message that what has to be done to save the United States and its rich allies from the new threat, international terrorism, is to rescue the poor from failed states and poverty.

However the idea that we would ever demean ourselves by assuming the guise of terrorists is repugnant in the extreme. The fact of our poverty does not make us terrorists. Our own experience of terrorism, including genocide and racist dehumanisation, make it impossible that we should seek freedom from want by defining ourselves as savages.

And yet it is commonly agreed that Africa constitutes the biggest challenge in the global struggle against poverty and underdevelopment. Mallaby said existing methods for dealing with the chaos on our continent have been tried and found wanting. He urged the introduction of a new imperialism, when all he should have done was to call for the adoption for Africa, of the tried and tested development path represented by the Marshall Plan, the Far East Asian programme and the EU Regional Policy.

The question must be posed and answered - what was done in these instances that produced the results which, strangely, it is argued are impossible to achieve in Africa, unless she is subjected to a new Scramble for Africa!

In his article "US imperialism, Oil, and Finance", Joseph Halevi of the University of Sydney provided one of the clues as to what was done and why. He writes: "Forrestal and Byrnes were, with George Kennan, the architects of post war US globalism. They are the ones who, after the collapse of the pound sterling in 1947 and the humiliating flight of Britain to non convertibility, decided to forcefully shift the US strategy away from Britain as a junior partner focusing it, instead, on Germany in Europe and on Japan in Asia.Their strategy was aimed at creating two regional growth poles both tied to the United States.The reconstruction of the world.fell exclusively upon the United States as a provider of credit, direct investment (in Europe not in Japan), capital goods, food, and as a guarantor of the supply of raw materials, oil above all."

**** This is part one in a special series of articles about global approaches to poverty eradication and economic development. Next week: 'Rescued by the Marshall Plan'.**

APPROACHES TO POVERTY ERADICATION AND ECONOMIC DEVELOPMENT II

Rescued by the Marshall Plan

LET US consider the post-war European Recovery Programme, the Marshall Plan.

Speaking at Harvard University on 5 June 1947, US Secretary of State George C. Marshall said: "The truth of the matter is that Europe's requirements for the next three or four years of foreign food and other essential products -principally from America - are so much greater than her present ability to pay that she must have substantial additional help, or face economic, social, and political deterioration of a very grave character."

This had been preceded by President Harry Truman's 12 March 1947 address to the US Congress, when he asked for funds to help Greece and Turkey, which the U.S. government believed would fall victim to socialist revolutions. He said:

"The seeds of totalitarian regimes are nurtured by misery and want. They spread and grow in the evil soil of poverty and strife. They reach their full growth when the hope of a people for a better life has died. We must keep that hope alive. The free peoples of the world look to us for support in maintaining their freedoms. If we falter in our leadership, we may endanger the peace of the world - and we shall surely endanger the welfare of our own nation."

With regard to the Marshall Plan, the 26 August 1947 US State Department document we cited in part one said: "Program submitted for U.S. consideration must contain these elements: Concrete proposals for area-wide recovery of agriculture and basic industries - coal, steel, transport, and power - which are fundamental to viable European economy. Proposals must correlate individual national programs and individual industry programs and give priority to projects promising quickest expansion of output."

In a contemporary report, the U.S. Marshall Foundation says, "the Marshall Plan was a rational effort by the United States aimed at reducing the hunger, homelessness, sickness, unemployment, and political restlessness of the 270 million people in sixteen nations in West Europe. Marshall Plan funds were not mainly directed towards feeding individuals or building individual houses, schools, or factories, but at strengthening the economic superstructure (particularly the iron-steel and power industries.) The program cost the American taxpayers $11,820,700,000 (plus $1,505,100,000 in loans that we repaid) over four years, and worked because it was aimed at aiding a well-educated, industrialised people temporarily down but not out.

"Over its four-year life, the Marshall Plan cost the U.S. 2.5 to 5 times the percent of national income as current foreign aid programs. One would need to multiply the program's $13.3 billion cost by 10 or perhaps 20 times to have the same impact on the U.S. economy now as the Marshall Plan had between 1948 and 1952."

The report also makes the important point that, "Americans were reluctant to invest in Europe because their profits were available only in local currencies that were little desired by U.S. businesses and investors."

The May 2003 edition of the US 'Harper's Magazine' published an article by William Finnegan entitled "Economics of Empire". Finnegan wrote:

"(The) pillars of the postwar international financial order were conceived during the latter part of World War II at a conference of American, British, and European economists and civil servants held in Bretton Woods, New Hampshire, and dominated intellectually by John Maynard Keynes. The World Bank was originally intended to help finance the reconstruction of postwar Europe - a project that neither private capital nor shattered states could be expected to undertake. After the Marshall Plan made that purpose redundant, the Bank, looking for a raison d'être, began to concentrate on Asia, Africa, and Latin America, where it loaned money to poor governments, usually for specific projects."

To explain Finnegan's comments, including his reference to the World Bank, we would like to quote a portion of a 1 May 1947 Memorandum written by a State Department official, Joseph Jones, to the then Under Secretary of State, Dean Acheson. Jones wrote:

"An important omission in this outline is a discussion of why the World Bank cannot do the job, or why the American banking community cannot do it; also why the expenditures must be largely in terms of grants-in-aid rather than loans. I quote Walter Lippman, May 1, on this point: 'In acting to forestall this (West European) collapse, we can afford to have no illusions. The deficit of the western European countries cannot be met, as Mr McCloy's recent address makes clear, by the World Bank, or by the American banking community. The sums needed are too large. The transactions are abnormal and altogether outside ordinary private finance. Nor can the deficit be met by government loans because in

fact these sums cannot be paid back. They will have to be contributed as a national investment in peace and prosperity.' "

In an article in the May 1997 edition of 'Harvard Magazine', entitled "From Plan to Practice: The context and consequences of the Marshall Plan", Professor Charles S. Maier says:

"The young economists who staffed European Recovery Programme agencies had learned the new Keynesian doctrines just before the war. They appreciated large and integrated markets, but understood that sometimes government spending was required to help markets function. World War II had further demonstrated that governments could plan purposeful economic activity and mobilise productive resources.

"By 1951.Americans had supplied about $14 billion in aid, probably between 1 and 2 percent of our gross national product for the period - roughly five times the proportional share we now allocate to foreign assistance.

"In the first two years of the program, American aid provided a major share of German and Italian gross capital formation; then it fell, as in Britain and France, to a much smaller share. In quantitative terms, Europeans were soon accumulating their own capital.

"Nonetheless, Washington's assistance satisfied key needs and was targeted to eliminate critical shortages. Assistance in dollars allowed Europeans to invest without trying to remedy their balance of payments drastically through deflation and austerity. This meant that economic recovery did not have to be financed out of general wage levels. Working-class voters (at least outside France and Italy, where strong Communist political cultures still thrived) could thus be rallied by politicians who offered gradualist social-democratic alternatives and remained friendly to the West.The Marshall Plan.worked to stabilise the consensual welfare-state politics that prevailed until the 1970s."

Despite what Professor Maier says about capital inflows into the UK and France, we must however point out that in the four years 1948 to 1952, the UK and France received in grants and loans $3.2 and $2.7 billion respectively, while Germany and Italy received $1.4 and $1.5 billion.

The Marshall Plan had a number of important features.

- It represented a conscious, purposeful and determined response by the then most powerful country in the world to what it considered an imminent danger to its survival - developments that President Harry Truman said would "endanger the welfare of our own nation", if allowed to run their course.
- To ward off this strategic danger, the U.S. was ready to spend whatever was necessary and required.
- It understood that so big was the challenge it faced that it could not rely on "the market", the private sector, to provide the resources to meet this challenge.
- It was accordingly ready and willing to use public funds to provide the investment and other resources that would enable the West European economies to reach their "take off" point.
- Rather than argue that governments had to minimise their role in the economy, it proceeded from the positions explained by Professor Maier, that "governments could plan purposeful economic activity and mobilise productive resources."
- Accordingly, the European Recovery Programme was based on a carefully prepared plan, which took into account the immanent capacities of the West European economies, including the understanding that here the U.S. had to "aide a well-educated, industrialised people temporarily down but not out".
- It also understood and took the position that such was the level of disruption and disequilibrium of the West European economies that they could only be returned to "normality" through grants, rather than loans or dependence on foreign direct investment.
- It integrated the imperative of social cohesion and stability within the economic plan, to avoid mass rebellion by the working people, to facilitate the achievement of the economic and political goals of the Economic Recovery Programme. It therefore ensured that the economic recovery was not based on "structural adjustment" and an unsustainable debt burden, but on the avoidance of the austerity and deflation that would have made the achievement of the goal of "consensual welfare-state politics that prevailed until the 1970s" impossible.

- It achieved its objective of providing the "substantial additional help" to purchase the "food and other essential products" Western Europe needed to escape from "misery and want" and "the evil soil of poverty and strife."

- It therefore succeeded as a development programme, enabling Western Europe to develop modern economies, "independent of abnormal outside support".

The success of the Marshall Plan represented the first example in the post-war years of what could be done to achieve the objective of the defeat of the twin challenges of poverty and underdevelopment.

Given the level of development reached by many of the West European countries before World War II, it gave an indication of the larger resources that would be needed to defeat far worse poverty and underdevelopment in the larger part of the world that, even at the end of the War, constituted the colonial possessions of the countries the Marshall Plan sought to assist.

The other strategic challenge the United States faced was the future of a number of countries in the Asian Far East. Japan, the principal adversary of the US in this region, like Germany in Europe, had to be neutralised.

Similarly, it had to be rescued from the threat of socialist revolution. The same consideration applied to South Korea and Taiwan. The first had socialist North Korea as its neighbour. The second was a province of socialist China. In addition, both North Korea and China were allies of the Soviet Union.

Accordingly, the 'Truman Doctrine' had to apply both to Western Europe and the Asian Far East. Logically, the Far East had to have its own Marshall Plan.

** This is part two in a special series of articles about global approaches to poverty eradication and economic development. Next week: 'The truth & the Asian Miracle'.

APPROACHES TO POVERTY ERADICATION AND ECONOMIC DEVELOPMENT II

The Truth & the Asian Miracle

IN AN ARTICLE "From Miracle to Crash" in the 16 April 1998 edition of the 'London Review of Books', Professor Benedict Anderson writes:

"Four basic conditions made the (East Asian) 'miracle' possible, and these existed only in the long strip of coastal capitalist states stretching from South Korea to the eastern edge of the Indian Ocean.

"The first was the peculiar arc of the Cold War in the region. Nowhere else was it 'hotter' in the third quarter of the century, and perhaps nowhere else did it cool down more rapidly, thanks to the Peking-Washington rapprochement of the mid-Seventies.

"In every important country of South-East Asia, with the exception of Indonesia, there were major, sustained Communist insurrections, and Indonesia, in the early Sixties, had the largest legal Communist Party in the world outside the socialist bloc.

"The notorious domino theory was invented specifically for South-East Asia. To shore up the line of teetering dominoes, Washington made every effort to create loyal, capitalistically prosperous, authoritarian and anti-Communist regimes - typically, but not invariably, dominated by the military.Each disaster only encouraged Washington to put more muscle and money behind its remaining political allies. No world region received more 'aid'.

"On the other hand, the Washington-Peking coalition against Moscow, consolidated after the 'fall' of Indochina, meant that from the late Seventies till the collapse of the Soviet Union those countries of South-East Asia who so wished could continue to profit from Washington's Cold War largesse without facing any severe internal or external constraints (the Philippines was a partial exception, as we shall see)."

To reach their "take off" levels of development, these countries depended on this "Washington's Cold War largesse". (Here we will refer only to Japan, South Korea and Taiwan).

Here we also need to take note of Professor Anderson's remarks with regard to the other "Asian tigers". He says:

"The second, accidental condition (for the emergence of these 'tigers') was the region's propinquity to Japan.Beginning with the acquisition of Taiwan in 1895, and the annexation of Korea in 1910, Japanese ruling élites sought by economic, political and military means to create for their country, in East and South-East Asia, a zone of hegemony equivalent to that of the United States in the Western hemisphere.

"In the period of postwar recovery, the old (Japanese) ambitions did not disappear, but took an essentially economic form. Assured of its political and military dominance over Japan, and eager to make the Japanese economy a cornerstone of capitalist strength in Asia, Washington put no real obstacles in Tokyo's way.

"In those early postwar years, however, Mao's China was closed to Japanese capital, and the South Koreans' bitter memories of Japanese colonialism made them scarcely more welcoming. South-East Asia was the only real possibility, not least because Europe had now lost its colonial fortresses there.

"Beginning in the Fifties, thanks to a series of war reparations agreements whereby Japan provided substantial funds to South-East Asian countries for the purchase of its manufactures, Tokyo's economic presence rapidly increased: first in Thailand, which had been an ally in World War Two, later in other new nation-states which had had less pleasant experiences under Japanese military rule. By the early Seventies, Japan had become the single most important external investor in the region, both as extractor of natural resources (timber, oil and so on) and in industrial and infrastructural development.

"All this meant that South-East Asia was the only region in the world in which the two most powerful capitalist economies were deeply and, on the whole co-operatively, committed for four decades. Later, when South Korea and Taiwan in their turn became major exporters of capital, they followed the leading goose, reinforcing the already huge inflows of capital and technology from America and Japan."

Not models of free trade

With regard to South Korea and Taiwan, here is what World Vision, New Zealand, had to say.

"South Korea and Taiwan are often promoted as countries that have developed and reduced poverty substantially through free trade and investment, not aid. It is true that they have been spectacularly successful in reducing poverty, but otherwise this claim is wrong on all counts.

"In fact, both countries received massive amounts of aid from the United States during the Cold War, because of their role as bulwarks against communism. They also received loans from the US on very generous terms. Very little of their capital came from FDI [foreign direct investment]. Between 1951 and 1967, FDI as a percentage of total long-term capital flows was only 1% in South Korea and 8% in Taiwan. Over the same period, foreign aid and loans made up 86% and 74% of such capital flows to South Korea and Taiwan respectively.

"Far from being models of free trade and investment, South Korea and Taiwan subsidised their industries heavily and protected them with tariffs and other barriers. They also carefully controlled investment. In addition, the US opened its market to their goods, without requiring them to open their markets to US goods in return.

"More recently, South Korea and Taiwan have liberalised trade and investment. However, this happened after they had built up highly successful industries under conditions of protection. It was a case of development first, then liberalisation, rather than the model of development through liberalisation promoted by neo-liberal economists.

"South Korea and Taiwan industrialised under very specific conditions that cannot necessarily be repeated in other countries. Through much of their post-war development they were also ruled by authoritarian and repressive regimes, with little regard for human rights. For these and other reasons, they may not provide good models for other developing countries to follow. But if they are useful examples, it is certainly not as models of development through free trade rather than aid."

Chakravarthi Raghavan made the same point in a 22 May 1996 article in 'Third World Network Features', entitled "East Asia proves World Bank theory wrong". He wrote: "Some of the most successful East Asian and South-East Asian economies, during the period 1971-1980 show a small ratio of FDI to total investment. It was only 0.1% for Japan, 5% for Hong Kong, 1.2% for the Republic of Korea, 1.3% for Taiwan, and 14% for Malaysia. China, which is less integrated into the world economy than Korea, had a 10.4% ratio of FDI to total investment."

In his article published by the Nautilus Institute, "Notes From Ground Zero: Power, Equity and Postwar Reconstruction in Two Eras", Mark Selden said the following about Japan:

"The US articulated practices of postwar reconstruction in which the victor contributed to the rehabilitation of the vanquished as well as of its own allies. The result was to reverse the dominant logic of war reparations in which the defeated were customarily further bled by the victors. Nevertheless, postwar reconstruction of defeated industrialized nations became one pillar of a hegemonic strategy designed to accelerate restoration of international trade and investment while subordinating others militarily.

"Postwar reconstruction after 1945 was attuned to American strategic priorities. The US aided in the relief, rehabilitation and reconstruction of defeated enemies, notably Germany and Japan, while providing assistance to selected European allies whose recovery was central to rebuilding the world economy in line with American interests.

"The bonanza of Korean War procurements that fueled Japan's economy from 1950 was critical to reconstruction. With the US assuring Japan's security, domestic investment could be concentrated on

economic, infrastructure and social reconstruction. The occupation gave rise to a shared US-Japan vision of an economically robust and democratic Japan within the ambit of American power in a post-colonial Asia divided along Cold War lines.

"Not all Japanese occupation programs proceeded smoothly, of course. Deadlock between different sections of the occupation, and at times between the occupation and the Japanese administration, meant that programs designed to dismantle the zaibatsu, the large economic-financial combines that dominated the prewar economy and that occupation authorities initially identified as the driving force behind Japanese militarism and colonialism, were stillborn. Likewise, the occupation's reverse course of 1947, driven by mounting Cold War concerns and the anticipation of a Third World War, led to an attack on labor and progressive forces generally.

"By contrast, programs that enjoyed strong popular support including the peace constitution, land reform, the vote for women, and numerous health and welfare measures, not only were fully implemented but were sustained following the formal end of the occupation in 1952, despite US pressures to scale back some of the most far-reaching reforms."

Further to this, writing in 2002 about elements of the economic history of Japan, Toyoo Gyohten, President of the Institute for International Monetary Affairs, said:

"In the 1950s and 1960s, Japan received a great deal of benefits from international organisations, both financially and institutionally. In particular, the World Bank provided financial assistance for the post-war reconstruction of Japan, starting with a loan to the Kansai Electric Power Project in 1953, when a stable supply of electricity was a top priority. During the next 13 years, Japan received financing from the World Bank, equalling US$863 million, for 31 reconstruction projects, including dams, highways, and bullet trains.

"It should be noted that the World Bank provided not only the financial means, but also the expertise needed for the economic infrastructure, which greatly contributed to Japan's rapid economic recovery and development. Japan was able to graduate from World Bank borrowing in 1966, and finished repayment of all loans by 1990.

"Under the international monetary system of the Bretton-Woods regime, Japan benefited from the fixed rate of exchange where the yen was undervalued for a long time, at 360 yen to the dollar. This arrangement provided a foundation for the development of Japan's industries."

In addition to all this, we must take into account that the US special programme instituted to procure as much of its defence requirements from Japan as possible, provided about 30% of Japan's foreign currency receipts in the early 1950s. Like the US initiated under-valuation of the yen and the opening of the US market to Japanese textiles, this constituted a deliberate intervention to accelerate the growth of the Japanese manufacturing sector.

In a 1996 paper "Capital Accumulation Key To East Asia Miracle", Chakravarthi Raghavan discusses the important issue of savings and investment. What we have said above shows the critical role of foreign savings in helping to bring about the Japanese and East Asian "economic miracle".

It is however also true that, in time, domestic savings came to play the predominant role in terms of providing the necessary investment capital. In this regard, Raghavan says: "However important initially these (foreign capital) inflows, gross domestic savings rose to very high levels - in Japan from 24% in the early 1950s to 36% in the 1960s and 40% in the 1970s; in Singapore from 10% of GDP in 1965 to 30% in the 1970s and 42% in the 1980s. In Korea and Taiwan from about 4% and 9% during 1956-1960, it rose rapidly to an average of 32% by the 1970s in Taiwan and 22% in the 1970s and 32% in the 1980s in Korea."

However, he also makes some important observations about these savings, essentially pointing to the importance of corporate as opposed to household savings, including the role of the state in this regard. He writes:

"In all these countries corporate savings accounted for a very large share of corporate investment and in East Asian NIEs (Newly Industrialised Economies), it was not household but corporate savings.

"In most East Asian NIEs, other profit-related income also contributed to a rise in domestic savings. Personal savings and corporate profits in East Asia were linked to profits through the bonus system - tying a significant part of workers' pay to company profits.

"Government policy played an important role in growth of corporate profits and savings. Fiscal instruments were used to supplement corporate profits and encourage retention to accelerate capital accumulation. Trade, financial and competition policies raised profits above levels that would have been attained under free market conditions, thus creating rents.

"Fiscal instruments included various tax breaks and special depreciation allowances to encourage enterprises to retain and invest profits.

"But State created rents were important. These rents were created through a mix of selective protection, controls over interest rates and credit allocation, managed competition including encouragement of mergers, coordination of capacity expansion, restrictions on entry into specific

industries, screening of technology acquisition and promotion of cartels for specific purposes such as product standardization, specialization and exports.

"Credit subsidies were essential for investment in new industries, as also credit rationing which could not merely be viewed as instrument for 'picking winners', but enabling rent creation and capital accumulation.

"The rent creation through protection was linked to export performance.

"Most of the fiscal instruments and rent-creations were focused in a deliberate concerted way on specific industries at particular moments in time - they did not just reallocate given resources across various sectors, but made a significant addition to the overall rate of accumulation.

"This creation of rents.was central to the process of accelerating capital accumulation and growth and establishing new industries. It contradicted the theory of rent-seeking under inward-oriented-trade regimes developed in the 1970s and 1980s.

"The reciprocity between government support and private sector performance entailed a faster rate of capital accumulation and growth - not only because support was often provided in exchange for higher investment, but also because better export performance as a measure of quality of investment necessitated faster accumulation in order to raise competitiveness through adaptation of new technology, scale economies, learning and productivity growth."

The elements of monopoly

As we approach the conclusion of this section, we must draw attention to a particular form of corporate organisation in the three East Asian countries we are discussing.

We have already quoted Selden as saying that the US occupation authorities in Japan failed to break the economic stranglehold of the "zaibatsu", the family owned monopoly conglomerates that dominated the pre-war Japanese economy.

The 21 January 1999 'San Diego Daily Transcript' carried an article by John Patrick Ford entitled "Monopoly is not a game". He wrote:

"American-style monopolies were personified by dynamic and ruthless entrepreneurs in the late 19th century. John D Rockefeller and Andrew Carnegie come to mind with their vast empires in oil and steel being financed by the likes of JP Morgan.These tycoons forged industrial empires that made America a world power.

"The same scheme worked for free-market Asian nations. All the elements of monopoly flourish today in South Korea with cliques called chaebols and in Taiwan with similar groups named guanxiqiyes. There certainly are differences from the American example or even from the Japanese (zaibatsu) root stock.Post-war reconstruction in the former (South Korean and Taiwan) colonies retained the same (zaibatsu and post-war Japanese) keiretsu system, but with some variations to suit the local culture.

"A major change from the pre-war Japanese model was the leverage of American capitalism. With abundant US foreign aid to rebuild devastated industries, a blend of Asian monopoly with American free-trade emerged in South Korea and Taiwan. Larger Korean chaebols got their start after the country's liberation in 1945. Thoughtful entrepreneurs utilised the urgent needs of politicians to stay in power. Bribing the ranking bureaucrats gained them preferred access to government funds.

"Real growth came after the corrupt Syngman Rhee regime was discarded in 1950. Succeeding military junta regimes needed strong business connections to stabilise their administrations. Any newcomers in the monopoly game depended on government subsidies. Even the largest chaebol can be humbled by politicians who were not on the payroll.

"Validation of the chaebol structure came in 1983 as sales of the fifty top groups accounted for 94 percent of GNP. Only 10 ruling families control 30 of Korea's largest firms.

"Taiwan is an island of only 14,000 square miles and half the population of South Korea. Yet this 'orphan' nation ranks 15th in world trade, boasts the third-largest foreign reserves, and is one of the lowest foreign debtors.

"Taiwanese monopolies, also cloned from the Japanese model, are called guanxiqiye. It's the Chinese-language equivalent to the same Korean and Japanese words.Taiwanese monopolies bear less imprint of state and more vitality of culture and market in their design.Typical is a cluster of enterprises owned and controlled by a group bound by an ancestral network. Such a clique is called an oligopoly to distinguish it from American-style monopoly.

In the comments cited earlier, Chakravarthi Raghavan has explained the economic interaction between the East Asian monopolies, described by John Ford, and the ruling groups in these countries. In this context, we must also take particular note of the observation made by World Vision, that "through much of their post-war development, (South Korea and Taiwan) were also ruled by authoritarian and repressive regimes, with little regard for human rights."

Obviously, this short presentation on the "Asian tigers" does not and cannot cover all the details that bear on the successful development model that turned these recently poor countries into the success

stories they are. We must now, however, state some of the main conclusions drawn from this experience.

As was the case with Western Europe, the US intervention in the Asian Far East represented a conscious, purposeful and determined response by the then most powerful country in the world to what it considered an imminent Communist danger to its survival.

To ward off this strategic danger, the US was ready to spend whatever was necessary and required.

It understood that so big was the challenge it faced that it could not rely on "the market", the private sector, and especially foreign direct investment, to provide the resources to meet this challenge. In the end, this translated into aid and loans.

It was accordingly ready and willing to use public funds to provide the investment and other resources that would enable the Far East Asian economies to reach their "take off" point.

It ensured that the World Bank played the development role from which it was largely excluded in Western Europe, adding multilateral resources to the investment funds available to the East Asian economies. It was also ready and willing to open its own market, and the markets of its allies, to guarantee the Asian economies a market for their products, as well as deliberately engineer the under-valuation of the Asian currencies to encourage Asian exports and discourage imports into the targeted Asian countries, thus opening the space for an import-substitution industrial strategy.

Rather than argue that governments had to minimise their role in the economy, it proceeded from the position that these governments had a central role to play in the achievement of the goals of the East Asian Development Programme.

It accepted the entrenchment and protection of monopolies and the formation of an interdependent political and business elite that would act as its partner in driving the Development Programme, regardless of the economic distortions that would result from this arrangement.

It accepted that this elite should function in an authoritarian manner, with no respect both for democracy and human rights, to give it the possibility especially to suppress any revolt by the workers and the ordinary people, provoked by the blatantly and almost exclusively pro-business policies of the target countries.

As in Western Europe, the US accepted that in the case of Japan, it had to allow for the development of a welfare state, to ensure the quiescence especially of the working people, without having to rely predominantly on repressive methods.

Having ensured the economic recovery of Japan, the US was happy to assign to her the role of ensuring the economic development of the other "Asian tigers" in South East Asia, which coincided with Japan's own historic interest to be the dominant power in this region of the world. The dominant world power, the US, was pleased that the emerging Japanese economic powerhouse, already tied to the US, could take over the task of ensuring that this region was "saved from communism", while it attended to the same task in the rest of the world.

The Far East Asian intervention so succeeded in the context of the set development objectives of the post-war intervention by the US, that in 1993, the World Bank issued a report entitled "The East Asian Miracle: Economic Growth and Public Policy".

Contrary to what we have said about the East Asian "tigers", the August-October 1993 World Bank Policy Research Bulletin, gave a different account of "The making of the East Asia miracle". It wrote:

"What caused East Asia's success? In large measure the HPAEs (High Performing Asian Economies) achieved high growth by getting the basics right. Private domestic investment and rapidly growing human capital were the principal engines of growth. High levels of domestic financial savings sustained the HPAEs' high investment levels. Agriculture, while declining in relative importance, experienced rapid growth and productivity improvement. Population growth rates declined more rapidly in the HPAEs than in other parts of the developing world. And some of these economies also got a head start because they had a better-educated labor force and a more effective system of public administration.

"Fundamentally sound development policy was a major ingredient in achieving rapid growth. Macroeconomic management was unusually good and macroeconomic performance unusually stable, providing the essential framework for private investment. Policies to increase the integrity of the banking system and to make it more accessible to non-traditional savers raised the levels of financial savings. Education policies that focused on primary and secondary schools generated rapid increases in labor force skills. Agricultural policies stressed productivity and did not tax the rural economy excessively."

To the extent that any of this might be true, it describes a later stage of the Far East Asian development process, beyond the "take off" point achieved through the earlier post-war intervention of the US.

To come down to earth, away from the heady "market friendly" heights idealised by this World Bank presentation of the East Asian "miracle", we will next undertake a brief examination of a contemporary development process, the European Union (EU) Regional Policy.

**** This is part three in a special series of articles about global approaches to poverty eradication and economic development. Next week: 'Bridging the EU development gaps'.**

APPROACHES TO POVERTY ERADICATION AND ECONOMIC DEVELOPMENT IV

Bridging the EU development gaps

A EUROPEAN UNION (EU) document posted on its website, and last updated in May 2004, says: "Although the European Union is one of the richest parts of the world, there are striking internal disparities of income and opportunity between its regions. The entry of 10 new member countries in May 2004, whose incomes are well below the EU average, has widened these gaps. Regional policy transfers resources from affluent to poorer regions. It is both an instrument of financial solidarity and a powerful force for economic integration."

The same document says: "Inequalities have various causes. They may result from longstanding handicaps imposed by geographic remoteness or by more recent social and economic change, or a combination of both. The impact of these disadvantages is frequently evident in social deprivation, poor quality schools, higher unemployment and inadequate infrastructures."

It continues: "The EU policy to reduce regional disparities is built on four structural funds:

- the European Regional Development Fund (ERDF), (which assists regions whose development is lagging behind and those undergoing economic conversion or experiencing structural difficulties);
- the European Social Fund (ESF), (which mainly provides assistance under the European employment strategy);
- the section of the EU's common agricultural fund devoted to rural development, (to help in the development and structural adjustment of rural areas whose development is lagging behind, by improving the efficiency of their structures for producing, processing and marketing agricultural and forest products);
- financial support for fishing communities as part of the common fisheries policy (CPF), (to support restructuring in the fisheries sector.)

"The funds will pay out about 213 billion (Euros), or roughly one third of total EU spending, between 2000 and 2006.

"A further 18 billions (Euros) is allocated to the cohesion fund, set up in 1993 to finance transport and environment infrastructure in member states with a GDP less than 90% of the Union average at the time (Greece, Ireland, Spain and Portugal)."

Another EU document says: "Most structural fund assistance is granted in the form of non-repayable grants or 'direct aid', and to a lesser degree refundable aid, interest-rate subsidies, guarantees, equity participation, and participation in venture capital."

To indicate the focused attention of the EU on the challenge of development within its member states, let us quote from another EU document that discusses the ERDF. It says:

"As part of its task to promote regional development, the ERDF contributes towards financing the following measures:

- Productive investment to create and safeguard sustainable jobs;
- Investment in infrastructure which contributes, in regions covered by Objective 1, to development, structural adjustment and creation and maintenance of sustainable jobs, or, in all eligible regions, to diversification, revitalisation, improved access and regeneration of economic sites and industrial areas suffering from decline, depressed urban areas, rural areas and areas dependent on fisheries. Such investment may also target the development of trans-European networks in the areas of transport, telecommunications and energy in the regions covered by Objective 1;
- Development of the endogenous potential by measures which support local development and employment initiatives and the activities of small and medium-sized enterprises; such assistance is aimed at services for enterprises, transfer of technology, development of financing institutions, direct aid to investment, provision of local infrastructure, and aid for structures providing neighbourhood services;

- Investment in education and health (only in the context of Objective 1)."

"Objective 1 promotes the development and structural adjustment of regions whose development is lagging behind, i.e. whose average per capita GDP is less than 75% of the European Union average. These regions show a deficit in socio-economic development in that they have:

- a low level of investment;
- a higher than average unemployment rate;
- lack of services for businesses and individuals; and,
- poor basic infrastructure.

"The Structural Funds support the takeoff of economic activities in these regions by providing them with the infrastructure they lack, encouraging investment in businesses and supporting human resource developments appropriate to the region."

To illustrate the detail entailed in the implementation of the Regional Policy of the EU, we will cite only one development example, a section of Berlin, the capital of the Federal Republic of Germany. Of this section the EU says that it has not been affected by growth and development in the rest of the city. It is therefore seen as a "negative area".

"Urban waste areas and abandoned production areas or railway sidings give an impression of disunion, the unrelatedness of isolated fragments or of an insular situation within the city.

"Population is dwindling; they younger inhabitants are moving out, leaving the old people behind. Parallel to this situation, foreign immigrants and latter-day émigrés from the CIS [Commonwealth of Independent States] countries are moving in. The unemployment rate is 50% above the federal average, and one in four unemployed persons has been out of work for over two years, which is the definition of long term unemployment. There is a high degree of dependence on social aid, and the educational level is low. The eligible area is a stage for radical right-wing groups and has a high crime rate, typical of major cities.

"The economic restructuring that followed re-unification has led to massive damage in the manufacturing sector: industrial sites were abandoned, and few plans have been put forward to re-use them as yet. This economic thinning-out has had an impact on individual commerce and on service and artisan enterprises, especially since they are under pressure from competition from large-scale distribution centres."

The foregoing demonstrates the detailed meticulous preparatory work that is done to ensure that the focus on each development region is correct and effective. The comments above relate to an area of Berlin with a population of only about 30,000. This is less than 1% of the population of the city, and 2.3% of the population falling within an Objective 1 development area.

The EU developmental interventions in Berlin include overcoming labour market and economic barriers; overcoming habitat and ecological barriers; overcoming social, ethnic, cultural and communication barriers; and providing technical assistance to ensure local implementation, monitoring and assessment of the development programmes.

The US Mission to the European Union has published some documents to assist US corporations interested to do business within the EU. One of these discusses the economic programmes that result from the implementation of the Union's Regional Policy. It makes the following important points:

"Most EU funding is not paid directly by the European Commission to private beneficiaries, but via the national and regional authorities of the Member States.

"Structural Fund grants are given to national, regional and local authorities for, among others, infrastructure and industrial, projects in such areas as telecommunications, energy, tourism, environment, transport, health, education, etc.

"Projects most likely to receive (Structural Funds) money are those that contribute to EU priority objectives: development and structural adjustment of underdeveloped regions, economic and social conversion of areas facing structural difficulties, and adaptation and modernisation of policies and systems of education, training and employment.

"Most Structural Fund projects are assessed/approved by relevant local/regional authorities."

All studies indicate that the EU Regional Policy is succeeding in its objective to reduce and eradicate poverty and underdevelopment among the Member States of the Union.

The Observatory for International Library Programmes (OPIB) has this to say on this important matter: "For many years, the regional disparities in levels of development and standards of living - which existed well before the Community was created - were dealt with entirely by the Member States concerned. There have been clear improvements since the European Union started trying to reduce

these disparities: average per capita income in the three least prosperous countries (Greece, Portugal and Spain) increased from 68% of the Community average to 79% in 1999."

An August 2002 study of "The Economic Impact of EU Regional Policy in Objective 1 Regions" confirms that this improvement in the less developed regions of the EU will continue during the 2002-2006 EU development period. It says:

"The Community objective 1 interventions are expected to have the highest impact on GDP in Portugal and Greece, where the average yearly level of GDP for 2002-2006 is expected to be 3.5% and 2.4% higher than it would otherwise have been (without EU development funding).

"In Portugal and Greece the yearly average level of Gross Fixed Capital Formation throughout the period is respectively 8.9% and 8.1% higher than it would otherwise have been."

The EU interventions will also help to restructure and modernise the economies of the less developed regions, reducing their dependence on primary products. In its 2003 report, "Competitiveness, sustainable development and cohesion in Europe: from Lisbon to Gothenburg", the EU says: "The Objective 1 programmes should help the economies of the six most backward regions covered by the study to catch up and restructure. Industrial production should increase in absolute terms, with the GDP share of agriculture and the processing of agricultural products falling and the share of services increasing."

It continues: "The instruments of solidarity, the Structural Funds and the Cohesion Fund, have a major impact on the competitiveness of regions and contribute significantly to improving the living conditions of their citizens, particularly in the poorer regions. About one third of GDP increases in the worst-off regions is estimated to be attributable to transfers from structural instruments."

It then goes on to say: "The ex post evaluation of Objective 2 regions (regions affected by industrial decline, covering 16.3% of the EU population) for the period 1994-99, which was carried out in 2003, concludes that the Structural Funds and their national and private co-financing -about EUR 52.3 billion in total - contributed to the creation of 700,000 jobs (gross), assisted more than 300,000 small and medium enterprises, and provided significant support for research, technological development, innovation and the promotion of the information society. The average unemployment rate in these regions declined by 2.1% from 11 to 8.9%, which demonstrates that they performed better than regions outside Objective 2.8.15 million people (were trained) in the Objective 1 regions."

It adds: "Market forces alone will not result in balanced economic development across the Union as a whole, and eastern enlargement will double existing regional disparities in the near future."

Another EU document says: "The dynamic effects of EU membership, coupled with a vigorous and targeted regional policy, can bring results. The gap between the richest and poorest regions has narrowed over the years. The case of Ireland is particularly heartening. Its GDP, which was 64% of the EU average when it joined 30 years ago, is now one of the highest in the Union."

Correctly, the 2002 study also estimated how much of the development impact "leaks" out of the development regions in the form of import of goods, equipment and services from other EU and non-EU countries. It found that "as expected, the leakage effects are higher from the relatively small open economies of Greece, Portugal and Ireland.", with the bulk of the "leakage" being to other EU countries.

The "leakages", as a proportion of the Objective 1 interventions, were 46.4% for Greece, 41.9% for Portugal and 37.8% for Ireland. This means that to the extent of these percentages, these countries could not obtain from their own markets the goods, equipment and services occasioned by the injection of EU development funds into their economies. This was a reflection of their relatively low levels of development.

Inspired by the successes it has achieved, the EU is determined to pursue its Regional Policy despite the challenges posed by its enlargement from 15 to 25 countries.

In its January 2003 "Second progress report on economic and social cohesion", the EU says: "Once enlargement takes place, disparities are going to widen. The most up-to-date statistics show that 48 regions in the EU15 (representing 18% of the population) had a per capita income below 75% of the average Community. In the EU25, there will be 67 of these regions representing 25% of the population."

Nevertheless the report says: "When establishing the future budgetary allocations for economic and social cohesion, the Union will need to take into account the unprecedented scale of economic and social disparities in an enlarged Union highlighted in this progress report, and the intensive, long-term nature of the effort required to reduce them.

"As indicated in the first progress report, many contributions to the debate, especially at regional level, regard a figure equivalent to 0.45% of EU GDP as a minimum level for the resources to be allocated to cohesion policy for the period after 2006."

Properly to understand the EU commitment to its Regional Policy, we should contrast the 0.45% of EU GDP mentioned in the preceding paragraph with the equivalent ODA commitments to Africa.

The Summary of the 2004 "Global Development Finance" report of the World Bank says: "The European Union, the United States and other donors have announced plans that, if realised, would

increase aid to 0.29 percent of industrial countries' national income by 2006 (from 0.23 percent in 2003)."

The same report also make the two important points that, "Since 2000, the developing world has been a net exporter of capital to the advanced economies.Half of the net (increase in) official development assistance (in 2002).reflects debt relief donor agencies, rather than increased resources provided directly to developing countries."

We must now state some of the main conclusions drawn from the experience of the implementation of the EU Regional Policy.

- The EU grew out of the West European system of cooperation initiated by the Marshall Plan, informed by the same strategic political and economic objectives that inspired that Plan. In addition to the task to defeat "Soviet expansionism", these included the need to ensure that contradictions among the European powers did not lead to a Third World War.
- It understood the benefits that derived from that Plan especially with regard to the irrationality of depending on loans and/or private investment to advance the underdeveloped regions within the EU to reach their takeoff point.
- It understood that these regions are too poor to generate the savings and capital they need for their development, and that their levels of poverty and underdevelopment made it impossible for them to attract significant volumes of private capital.
- Accordingly, public sector grants constitute the bulk of its development funds.
- Contrary to arguments about minimal state intervention in the economy of the underdeveloped regions, it has proceeded on the basis of the critical need for the state to be involved in the development of these regions.
- This state intervention has entailed detailed "dirigiste" planning and implementation of comprehensive development programmes, fully accepting the concept of a developmental state.
- The Regional Policy is succeeding in its central objective of reducing and eradicating poverty and underdevelopment in the least developed regions within the EU, ensuring that these regions attain the average GDP level of the EU as a whole.
- The 15-member EU aimed to achieve this objective in one generation. It estimates that given its enlargement into 25 countries, it will realise this goal in two generations.

The Marshall Plan enabled the biggest West European economies to attain their takeoff points. They were then able to develop with no need for exceptional external support. They have therefore been able to use the post-Marshall Plan wealth they are able to generate to develop the less developed EU member states.

The US and World Bank interventions enabled the Japanese economy to attain its own takeoff point. It was then able to develop with no need for exceptional external support. It has therefore been able to use the post-Western intervention wealth it has generated to sponsor the development of the economies of the South East Asian countries.

The EU also had to respond to the challenge similar to the one that confronted Japan, of developing other countries within its "sphere of influence". Largely, these were its former colonies identified as the ACP countries - the African, Caribbean and Pacific countries.

Let us therefore next week examine the ACP-EU "Cotonou Agreement" to see the extent to which the EU has drawn on the successful development model represented by the Marshall Plan and its own Regional Policy to foster the development of the ACP countries.

** This is part four in a special series of articles about global approaches to poverty eradication and economic development. Next week: 'The ACP & the philosophy of development'.

APPROACHES TO POVERTY ERADICATION AND ECONOMIC DEVELOPMENT V

The ACP and the philosophy of development

THE RELATIONS between the African, Caribbean and Pacific (ACP) countries and the European Union (EU) are governed by the 'Cotonou Agreement', which was signed in 2000.

In 1996, prior to the conclusion of this Agreement, and in an attempt to set the stage for the negotiations leading to this Agreement, the EU published a "Green Paper on relations between the European Union and the ACP countries."

Among other things this Green Paper said:

"Community aid for the ACP economies should promote their integration into the global economy.

"(The EU should adopt) a more systematic approach to the causes of low investment in most ACP countries. The EU could play a positive role by supporting administrative and institutional reforms that would encourage the mobilization of private investment, i.e. framing of competition policies, development of capital markets, modernization of business and property law, consumer protection, education, training and development of industrial cooperation.

"(It should assist in the) restructuring of public enterprises and privatisation in the wider context of the changing role of the state in the economy.

"(It should offer) greater support for an opening-up (of the ACP economies) to international trade and for regional integration.

"(The EU should help to) mobilize private-sector resources for the development of infrastructure, especially telecommunications infrastructure, and their operation in economically viable conditions.

"(It should achieve) macroeconomic and monetary cooperation (with the ACP countries). (This should) involve support for the establishment of a stable, non-inflationary and growth-generating macroeconomic framework.

"(The EU should) help reduce levels of external debt (of the ACP countries)."

Underlying all these observations was an approach to the development challenge explained in the Green Paper in the following words:

"Apart from the need to improve results (of aid), development thinking itself has moved on. Global economic changes (liberalisation, technological progress, emerging economies) and the lessons from the success stories of Asia, Latin America, or Africa, have radically modified the philosophy of development. This is especially true of perceptions about the role of the state and relations between public and private actors.

"Another factor contributing to the overhaul of cooperation is the end of the Cold War: the new political openness has allowed the emergence of a wide consensus on the principles of democracy and the market economy.

"These processes have already led to important changes in the concepts of aid and its role in development.(which include).

"A change in priorities, by reducing interventions in productive sectors.

"The creation of an instrument for structural adjustment support at macroeconomic and sectoral levels (and).

"A new conception of the economic role of the state, policies to foster private sector development, and support for trade development."

Given the strength of the EU and the relative weakness of the ACP countries, it was inevitable that these countries would have no choice but to accept the new "philosophy of development" to which the EU Green paper referred.

To prepare for the negotiations of the Cotonou Agreement, a preparatory Summit Meeting of the ACP countries was held in Libreville, Gabon in November 1997. This meeting, also attended by members of the European Commission, adopted a 'Libreville Declaration' which, inter alia, said: "We acknowledge the need to foster a culture of private enterprise and strengthen the institutions of a market economy. We therefore commit our governments to promote the development of a socially responsible private sector and encourage its participation in the development process. We intend to continue our efforts to create the kind of environment that attracts foreign direct investment including the appropriate incentive measures. To support these efforts we call on the EU to provide the necessary resources and give incentives to their private sector to ensure that investment is directed to ACP countries, especially by guaranteeing foreign investment. We further call on the EU to support the ACP initiatives to develop dynamic private sector institutions."

Developing the private sector

We should therefore not be surprised that the Cotonou Agreement includes an Article 21, which says:
"Cooperation shall support the necessary economic and institutional reforms and policies at national and/or regional level, aiming at creating a favourable environment for private investment, and the development of a dynamic, viable and competitive private sector. Cooperation shall further support:

a. the promotion of public-private sector dialogue and cooperation;
b. the development of entrepreneurial skills and business culture;
c. privatisation and enterprise reform; and
d. development and modernisation of mediation and arbitration systems."

We should, even at this early stage, also point out that subsequent to the signing of the Cotonou Agreement, in September 2000, the EU concluded its own internal agreement covering its financial obligations to the ACP countries, arising out of the Agreement. This agreement said:
"The Partnership Agreement between the African, Caribbean and Pacific States and the European Community and its Member States signed in Cotonou, Benin on 23 June 2000 (hereinafter referred to as "the ACP-EC Agreement") sets the aggregate amount of Community aid to the ACP States for the five-year period 2000-2005 at EUR 15 200 million.
"This amount is comprised of, on the one hand, EUR 13 500 million from the 9th European Development Fund (9th EDF) contributed by Member States and, on the other hand, EUR 1 700 million from the European Investment Bank (hereinafter referred to as "the Bank").
"In addition, any balances from previous European Development Funds as of the day of entry into force of the Financial Protocol to the ACP-EC Agreement will be transferred to the 9th EDF and used in accordance with the conditions laid down in the ACP-EC Agreement. The total amount foreseen will cover the period 2000-2007. This period comprises the period of approximately two years required for ratification of the 9th EDF and the two years following the expiry of the 9th EDF."
Properly to understand what the foregoing means, we should recall the amounts budgeted for the 2002-2006 EU Regional Policy. The following is the allocation picture we get:

- ACP (2000-2005): EUR 15.2 billion.
- EU Regional Policy (2000-2006): EUR 213 billion.

The top five EU recipient member states will each receive the following amounts, each exceeding the amount allocated to all the ACP countries combined:

- Spain: EUR 38 billion.
- Italy: EUR 22 billion.
- Greece: EUR 20.9 billion.
- Germany: EUR 19.9 billion.
- Portugal: EUR 19 billion.

We should also compare these sums with the resource transfers from West to East Germany after unification in 1990. These amounted to about EUR 750 billion during the first decade of unification, responding to the needs of 16 million people.
Figures published by the OECD of Gross Bilateral ODA for 2001-2002 also confirm the less advantaged position of the ACP countries. (Please note that in 2001, bilateral aid constituted 67% of total ODA, rising to 70% in 2002). The top ten ODA recipients were:

- China: $1,847 million.
- India: $1,642 million.
- Indonesia: $1,443 million.
- Egypt: $1,397 million.
- Serbia & Montenegro: $1,277 million.
- Mozambique: $1,244 million.

- Russia: (net OA): $1,062 million.
- Pakistan: $960 million.
- Tanzania: $939 million.
- Philippines: $914 million.

Of these, only Mozambique and Tanzania belong to the ACP group, which together present the biggest global development challenge.

ODA transfers should, of course, also be compared with the international debt burden of the ODA recipient countries. In this regard, the OECD said that in 2002, these countries had "Total Identified External Debt" amounting to $2,485 trillion. As opposed to the $60 billion in ODA available for the year, these countries had debt due within a year and payable to official donors amounting to $209 billion.

We should now give an indication of how some of the EUR 15.2 billion allocated to the ACP countries will be used. The internal EU document to which we have referred says:

"Up to EUR 10 000 million (will by given to the ACP countries) in the form of grants (reserved for an envelope for support of long-term development) comprising up to:

"EUR 9 836 million (will be) reserved for support for long-term development to be programmed in accordance with Articles 1 to 5 of Annex IV to the ACP-EC Agreement. These resources may be used to finance short-term emergency actions in accordance with Article 72(3) of the ACP-EC Agreement;" (these Articles refer to equity and loan participation in private and public sector enterprises as well as humanitarian & emergency assistance).

"Up to EUR 1 300 million (will be) reserved for the financing of support for regional cooperation and integration of the ACP States in accordance with Articles 6 to 14 of Annex IV to the ACP-EC Agreement." (these Articles refer to social infrastructure, export earning fluctuations, regulatory matters to protect private companies, financing SMMEs, facilitating private sector growth, foreign currency allocations).

"Up to EUR 2 200 million shall be allocated to finance the Investment Facility in accordance with the terms and conditions set out in Annex II ("Terms and conditions of financing") to the ACP-EC Agreement, without prejudice to the financing of the interest rate subsidies provided for in Articles 2 and 4 of Annex II to the Agreement funded from the resources mentioned in Article 3(a) of Annex I thereto." (this refers to European Investment Bank loans, equity participation to eligible enterprises, quasi-capital assistance, interest subsidies, guarantees, and catalysing foreign private investors and lenders)."

From all this we can see that the bulk of the EUR 15.2 billion has, indeed, been allocated to actual economic development. Understanding the complexity of the Financing Agreement for the developing ACP countries, which face capacity constraints, the EU decided that some of the EUR 15.2 billion would only be distributed after reports had been submitted indicating proper management of earlier disbursements.

The internal EU financing agreement therefore includes a provision which says:

"Out of the EUR 13 500 million referred to in paragraph 1, an amount of EUR 1 000 million may be released only following a performance review undertaken by the Council in 2004, on the basis of a proposal from the Commission. These resources shall, if released, be distributed as appropriate to the envelopes referred to in paragraphs 1(a), (b) and (c)."

Negative view of aid

The Cotonou Agreement was concluded within the context of a negative climate towards aid or foreign development assistance in the EU and other developed countries. The 1996 EU Green Paper explained this in the following terms:

"During the 1980s various factors contributed to a general feeling of disillusionment with the actual results of development aid: the budgetary constraints of donor countries; rising unemployment and the worsening of social problems in industrialised countries, with the consequent tendency to turn inwards; the perception that, in comparison to trade and investment, aid had played a marginal role in the economic success of certain Asian and Latin American countries."

With regard to this "disillusionment" and other problems, we should perhaps cite some facts mentioned by a 2002 report of the French Ministry for Employment and Solidarity, entitled "Fighting the New Poverty". One partial summary of the report says: "According to the report, the government spends 28 billion euros per month to support the lowest income families, which comprise approximately six million people. In addition, special payments go to nearly 500,000 unemployed who are no longer eligible for regular assistance. Further financial support goes to 2.8 million workers who are employed either part-time, by temporary employment agencies, or on fixed-term contracts, and who receive less than the legal minimum wage (a net sum of 5.27 euros per hour)."

These are large financial commitments that the French state has to honour before it commits additional resources to the eradication of poverty and underdevelopment in the rest of the world.

The then European Commissioner for Development Cooperation and Humanitarian Aid, Poul Nielson, spoke at the signing ceremony in Cotonou, Benin, which concluded the negotiations leading to the adoption of the Cotonou Agreement. Among other things, he said:

"Under the Lomé Convention, trade co-operation largely took the form of preferential tariffs. In future, our economic and trade co-operation will consist of a more comprehensive set of arrangements. The new process approach aiming at establishing new trading arrangements is crucial to improving the ACP countries' capacity to trade and to attract international private investment. It will be accompanied by appropriate support with a view to easing the transition and to prepare for a more dynamic and equitable participation in the international economic system.

"There are many sceptics watching what we are doing. The short version is that it simply doesn't work. This is wrong. I came to Benin a few days early for this meeting in order to see for myself what we are doing here with our partner. I saw road construction in progress, hospitals, new born babies in small clinics, people giving blood in safe and controlled operations and I saw a local market where 47 women are now in control of their own business -and prospering. I am confident that this is also what I could see in other ACP countries. Our partnership works, even if we all know it can be improved and will be improved.

"We must show to the rest of the world that we have a shared vision of the future of this relationship and that we will deliver. One of the necessary conditions to do this is to work in an environment which is politically stable and respectful of human rights, democratic principles, the rule of law and good governance. The Community will be behind you, and together with you, to achieve this objective."

Poul Nielson was right in many respects.

Through the Cotonou Agreement, the developed North, represented by the EU, has tied the developing South to a development model based on the integration of the South in the global economy, which would be achieved through free trade and private foreign direct investment in the countries of the South.

The developed North is determined to make political stability, respect for human rights and democratic principles, the rule of law and good governance necessary conditions for any capital transfers to, and economic cooperation with the countries of the South.

In Cotonou he saw practical examples of successful development projects, funded by the EU, that are helping to address the challenge of poverty and underdevelopment in the countries of the South.

The question to ask is whether he was right when he said "our partnership works", when its effectiveness is measured against the strategic objective of achieving the development that was achieved in post-War Western Europe and the Asian Far East, and is currently being realised through the EU Regional Policy!

In its 1996 Green Paper discussing EU-ACP cooperation, the EU said: "Europe cannot claim to be a player on the world stage without a responsible strategy towards the different regions of the South, and in particular those most at risk of poverty and marginalisation. It cannot pride itself on its solidarity with Eastern Europe's fledgling democracies without confirming a partnership with countries feeling their way towards a just society founded on fundamental human rights."

Trade and development

That "responsible strategy" will find expression in the detailed Economic Partnership Agreements (EPAs) that must be concluded between the EU and various ACP regions in terms of the Cotonou Agreement. Of these EPAs, in an April 2004 paper entitled "Why the EU approach to regional trade negotiations with developing countries is bad for development", the non-governmental Concord Cotonou Working Group said:

"According to the Cotonou Agreement EPAs would contain, 'new WTO compatible trading arrangements, removing progressively barriers to trade between EU and ACP countries' building on 'the regional integration initiatives of ACP states'. The negotiations are to be concluded by the end of 2007 and then gradually implemented between 2008 and 2020.

"EPAs would not only bring an end to the unilateral trade preferences enjoyed by the ACP countries but would establish a trade regime between the EU and the ACP countries that would be 'WTO-plus' in two respects.

"First, for the European Union EPAs can only be based on Free Trade Areas (FTAs) as defined by the WTO, namely by Art.XXIV of GATT. Free Trade Areas imply the elimination (not the reduction, but the elimination) of duties and other restrictive regulations of commerce on essentially all trade within a period of 10 years (which can only be extended in exceptional cases). In addition the EU sticks to a narrow interpretation of this WTO rule insisting that 'essentially all' eventually would mean more than 90% and that extensions would be limited. In other words EPAs would require the ACP countries to almost completely open their markets to EU imports within a short period of time.

"Second, for the EU EPA negotiations should also include investment, competition, government procurement, trade facilitation and data protection. The first four belong to the so-called Singapore issues that many developing countries, including the ACP countries, resisted so much at the WTO-level. Only an investment protection agreement and cooperation on competition policies is foreseen in the Cotonou Agreement. The EU therefore does not only want to go beyond the consensus at WTO level, but also outside the scope of Cotonou. The latter is also the case with regard to trade in services, where the EU pushes for expeditious and ambitious negotiations.

"While EU and the ACP countries agree that EPAs must become 'instruments for development', the EU approach to the EPA negotiations puts this development goal in jeopardy."

In 2003, Teresa Thorp delivered a paper at a Conference of the African Studies Association of Australasia and the Pacific entitled "Regional Implications for the ACP-EU: Economic Partnership Agreements". She set the stage for an informed and rational discussion of the EPAs. Commenting on what had preceded the Cotonou Agreement, she said:

"All in all the results have not lived up to expectations: trade preferences have not prevented the ACP from being increasingly marginalized in world trade; they have not prevented the continued decrease in the ACP's share in total EU imports nor have they overcome the high dependence of the ACP on a few commodities.

"The ebb and flow of multilateralism and universalism of trade has meant, for the most part, that the poorest ACP countries continue to be marginalized, enduring only as spectators to the global stage. This backdrop leads one to ask whether the EPA's will be successful where preceding negotiations and Conventions, principally economic structural reforms, have failed to integrate the ACP states into the global economy.

"Closer economic relationships between the African, Caribbean and Pacific States and the European Union have evolved over a fifty-year period. They were incorporated into the Treaty of Rome in 1957 (Article 131), and cemented by a series of other conventions: Yaounde I & II (1963 and 1969 respectively), and the Lomé Conventions (1975-1995). The conventions enlarged the ACP pact and focused on progressive market liberalization initiatives. Today, 79 ACP countries are signatories to the ACP-EU Partnership Agreement. Yet, the majority continue to linger on the fringe of global trade."

However, and presumably to move the ACP countries out of the "fringe of global trade", according to the Concord Cotonou Working Group, the EPAs are intended to oblige the ACP countries to conform to a "free market" model of development that was never imposed on both Western Europe and the Asian Far East after the Second World War. This was precisely because, at that time, the US understood that this would negate the possibility for these regions to overcome their condition of underdevelopment.

The Concord Working Group Report we have cited went on to say that because of this "free market" model of development: "There will also be little incentive for ACP producers to diversify into more 'value-added' products, or for investors to put money in to developing new capacity, given uncertain domestic and regional markets for products competing with EU imports. This could lead to a 'glass-ceiling' being placed on ACP countries' development, an increased dependence on the production and export of primary products and possible deindustrialisation with associated job losses."

Contrary to this perspective, when he addressed the meeting in Windhoek, Namibia, in July 2004, to begin the SADC-EU EPA negotiations, the EU Development Commissioner, Poul Nielson, said: "I would like to explain what we mean by 'integrating the ACP in the world economy'. They have always been there but in a role that is not satisfactory, mainly as providers of raw materials and commodities. What we wish to do is to assist you in playing a more interesting and equitable role in the global economy, to increase the added value, to diversify your economies and, by leaving the long hangover of colonial economic relationships, to become fully equal partners.We are trying to do something new."

Speaking at the 1997 Libreville ACP Summit meeting, Poul Nielson's Portuguese predecessor as EU Development Commissioner had also spoken about the ACP countries "leaving the long hangover of colonial economic relationships, to become fully equal partners". He said that "the post-colonial period is over", and that the new (Cotonou) agreement would have to be based on reciprocal and mutually beneficial arrangements between the ACP and EU countries.

Feeling no obligation to be as diplomatic as the Danish Poul Nielson, he communicated the unequivocal message that the former European colonial powers felt that they had paid their debt to their former colonies. In future, the former colonies had to relate to their erstwhile colonisers as more or least equal economic partners and competitors. The colonial debt had been paid, in full!

In this regard, a 2003 report prepared for the EU entitled "Sustainability Impact Assessment (SIA) of trade negotiations of the EU-ACP Economic Partnership Agreements" said: "To the extent that the EPAs can encourage enhanced processing, and to the extent that West African countries can improve their own competitiveness and productivity, they may be able to compete effectively in some areas including, inter alia: fruit juices, fruit extracts, prepackaged fresh fruits, pre-cooked vegetables and fish. However, in order to develop potential in nascent processing industries, the countries of the region will

have to be able to meet the standards imposed by its trading partners. A failure to make these fundamental gains could lead to the collapse of much of the manufacturing sector, which at the moment constitutes the backbone of the modern economy in the region and is an important employer in urban centres which is a refuge for unemployed populations but does not have the capacity to support viable small and medium-sized enterprises."

So much for the assertion that the EPAs would serve as "instruments for development"!

Recognising the problems posed by the EPAs, at its February 2004 meeting in Addis Ababa, the ACP-EU Joint Parliamentary Assembly adopted a resolution on "Economic Partnership Agreements (EPA): problems and prospects". Among other things, this Resolution:

"(Called) upon the European Commission to support, in a transitional period, the principle of commercial non-reciprocity which must govern relations between the industrialised and developing countries, and to develop flexibility towards ACP countries during the EPA negotiations in view of their level of development, of the relatively small size of their economies, and of their financial, development and trade needs, and to ensure that, in reality, EPAs become instruments for sustainable development in the ACP countries; calls on the Commission, in this connection, with a view to promoting sustained economic growth in ACP countries and regions, to improve ACP export opportunities to the EU market, inter alia through:

- widening the scope of products, both semi-finished and finished, of interest to them under the EPAs,
- addressing both tariff and non-tariff measures, and
- wherever possible, improving and injecting flexibility into the Cotonou rules of origin, including the acceptance of asymmetric rules of origin to take into account the differences in the level of industrial development between the EU and ACP countries."

The Assembly went on to "(stress) that major investment must be made before the economies of these (ACP) countries enter into competition with EU undertakings; (and observed) that this financial effort must be better evaluated and calls on the EU to explore appropriate measures to address the funding requirements in this regard."

From the foregoing we can draw the following conclusions:

- In the post-Cold War period, the developed countries are ready to respond to the challenge of poverty and underdevelopment in the countries of the South as a moral rather than a strategic imperative that is necessitated by a threat to their survival;
- They believe that the development of these countries should be financed through private capital, rather than public sector funds;
- They work to ensure minimal state intervention in the economies of the South and therefore reliance on "the market" and the private sector to achieve the development goals of these countries;
- They believe that these developing countries must be fully integrated within the global economy, interacting with all other countries through free trade and reliance on the global capital markets and global investors for the investment funds they need;
- Critically, they believe that the developing countries should be obliged to participate in reciprocal "free trade" arrangements, insisting that it is such "free trade" rather than "aid" that will catapult the developing countries to reach their "take off" levels of development;
- They are convinced that such economic assistance as they extend to the developing countries should act as a catalyst towards the achievement of the central goal of creating "investor friendly" conditions that would enable the developing countries to attract the requisite volumes of domestic and foreign private investment, creating the capacity for recipient countries of this investment to expand the space for these investors freely to trade their products;
- They are determined to ensure that except for developing countries with domestic economies so large that their investors cannot ignore them, all others must meet such political and governance standards as they set, to reassure especially the foreign investors;

- They are unwilling to provide sufficient public sector funds to enable the developing countries to reach their takeoff point, and do not pursue this objective, leaving it to the private sector;

- This development model has not produced any success with regard to sustained development that does not require exceptional external intervention, despite all efforts by the developing countries to create the political, policy and other conditions the developed countries set as pre-conditions for the sustained development of the countries of the South.

None of these are natural, God-given results. They reflect the ideological dominance of a development paradigm described as "the Washington Consensus" that represents what has been described as "market fundamentalism".

This paradigm reflects a number of global developments to which there has as yet been no successful concerted response of benefit to the poor of the world.

These are:

- the collapse of the Soviet Union and the prospect of the emergence of socialism as a world socio-economic system, leading to the capitalist system establishing itself as the only viable condition for human existence;

- the elimination of all fears within the capitalist world that failure to reform itself to become responsive to the needs of the ordinary people, it would be replaced by an alternative socio-economic system;

- the growth of the global transnational corporations and financial capital, creating the need for them to operate in global conditions that allow them to operate as freely as possible within the context of a liberalised and deregulated global economy; and,

- the elimination of the fear by the developed capitalist countries that any rebellion by the poor of the world would threaten their stability, growth and continued prosperity.

Responding to all this, the dominant ruling groups in the developed capitalist countries have adopted a development model driven by the imperatives of capitalist development in the post-Cold War period.
** This is part five in a special series of articles about global approaches to poverty eradication and economic development. Next week: 'Despair and the Washington Consensus '.

APPROACHES TO POVERTY ERADICATION AND ECONOMIC DEVELOPMENT VI

Despair and the Washington Consensus

THE 2003 UNDP Human Development Report said: "For many countries the 1990s were a decade of despair.In the 1990s average per capita growth was less than 3% in 125 developing and transition countries, and in 54 of them average per capita income fell. These include many priority countries but also some countries with medium human development."

Susan George, then associate director of the Transnational Institute, gave one of the reasons for this despair as what had happened during the 1980s. In an article, "How the Poor Develop the Rich", she said: "According to the OECD, between 1982 and 1990 total resource flows to developing countries amounted to $927 billion. During the same 1982-90 period, developing countries remitted in debt service alone $1,345 billion (interest and principal) to the creditor countries.In spite of total debt service, including amortisation, of more than $1.3 trillion from 1982 to 1990, the debtor countries as a group began the 1990s fully 61 percent more in debt than they were in 1982."

In a background paper to the 2003 UNDP Report, the economist Richard Jolly wrote: "The Bretton Woods Institutions, BWI, (the IMF and the World Bank) have been keen to negotiate with individual countries time dated, quantitative economic targets as part of the conditionalities of adjustment programmes. These targets have typically focused on such variables as the public sector deficit, the balance of payments and the inflation rate - each of which are, of course, means to improving economic performance rather than ends of development, let alone goals of human development. More serious, the single-minded focus of the BWI on economic variables has been driven by a narrow view of structural adjustment which in turn has led, especially in the 1980s, to policies and actions which often diverted attention from the social dimensions of adjustment, set back progress in the social sectors, and worked against the achievement of global goals in education, health and nutrition."

What Jolly was referring to as "a narrow view of structural adjustment" is what is called "the Washington Consensus". The former Chief Economist of the World Bank and Nobel Prize winner, Joseph Stiglitz, has described this "consensus" as "consensus between the IMF, the World Bank, and the U.S. Treasury about the 'right' policies for developing countries - that signalled a radically different approach to economic development and stabilisation."

Confronted by the fact of the further impoverishment of the poor as a result of these policies, the Administrator of the UNDP, Mark Malloch-Brown, spoke out at the launch of the 2003 Human Development Report (HDR) and said there was need to launch a "guerrilla assault" against the "Washington Consensus."

He added: "The IMF and the World Bank should no longer set these kinds of ceilings on spending. These measures were introduced at a time when finances were leaking red ink all over the place and there was an urgent need to stabilize. The strategy had its time and place. The Washington Consensus did some good things, but people stuck with it too long - and it wasn't enough."

Obviously conscious of the successful development interventions to which we have referred, the principal author of the 2003 HDR, Sakiko Fukuda-Parr, said, "Public interventions are necessary to set the preconditions for market-led economic growth."

Accordingly, as we would expect, the 2003 HDR argues for bigger volumes of development assistance, as promised at the UN Monterrey Summit on Financing for Development, to enable the "public interventions" that Fukuda-Parr was talking about to take place.

In this context, in April 2004, Peter McCawley, Dean of the Asian Development Bank Institute said:

More Information:

- Part One: Beware of the Natives!
- Part Two: Rescued by the Marshall Plan
- Part Three: The Truth & the Asian Miracle
- Part Four: Bridging the EU development gap
- Part Five: The ACP and the philosophy of development

"Global ODA [Overseas Development Assistance] is roughly $60 billion. It sounds like a large amount but there has been a question emerging in the last four to five years of why has aid failed and why are so many countries still in a terrible mess. This problem is particularly acute in the case of Africa and it has led to a very large concern in the international community over the effectiveness of aid.

"Concerning the $60 billion, there is a misunderstanding about the magnitude. What is interesting about this figure is how small it is. The $60 billion goes to four billion people, including those in India and China. That equals $15 per person per year, or roughly $1 per person per month in developing countries. Hence, I suggest to you that one of the reasons aid has been ineffective is that it has barely ever been tried. A transfer of $1 per person per month is hardly a significant transfer and it is a tiny transfer compared to those that we are used to inside rich countries. When we have a problem with the agriculture sector, it is not at all unusual for governments in rich countries to provide transfers of $20,000 or $30,000, or even $100,000, per farm.

"Twenty or 30 years ago, multilateral development banks (MDBs) talked much about investment and focused to a considerable degree on projects like infrastructure. We do not hear as much about the accumulation of capital, the levels of investment. The topic has tended to move aside and now we hear much more about the need for good governance and anti-corruption programs than the investment/GDP ratio. It is said that, to some extent, developing countries themselves are responsible for the levels of investment and they need to do more to improve the domestic investment climate.

"The views of poor countries tend to be somewhat different. On economic growth, poor countries tend to place more emphasis on the quantity of economic growth."

Wisely, Peter McCawley also said: "The philosophy of development changes as time goes by, partly as a result of facts and new experiences as well as events."

The "Washington Consensus" represented such a change in the philosophy of development, resulting in the "narrow view of structural adjustment" that Richard Jolly complained about.

The first person to spell out the goals of the "Washington Consensus" was the economist John Williamson. In remarks at the U.S. Centre for Strategic and International Studies in November 2002, thirteen years after he first announced the programme of the "Washington Consensus", he said:

"Let me remind you of the ten reforms that I originally presented as a summary of what most people in Washington believed Latin America (not all countries) ought to be undertaking as of 1989 (not at all times):

1. " Fiscal Discipline. This was in the context of a region where almost all the countries had run large deficits that led to balance of payments crises and high inflation that hit mainly the poor because the rich could park their money abroad.

2. " Reordering Public Expenditure Priorities. This suggested switching expenditure in a pro-poor way, from things like indiscriminate subsidies to basic health and education.

3. " Tax reform. Constructing a tax system that would combine a broad tax base with moderate marginal tax rates.

4. " Liberalizing Interest Rates. In retrospect I wish I had formulated this in a broader way as financial liberalization, and stressed that views differed on how fast it should be achieved.

5. " A Competitive Exchange Rate. I fear I indulged in wishful thinking in asserting that there was a consensus in favor of ensuring that the exchange rate would be competitive, which implies an intermediate regime; in fact Washington was already beginning to subscribe to the

two-corner doctrine.

6. " Trade Liberalization. I stated that there was a difference of view about how fast trade should be liberalized.

7. " Liberalization of Inward Foreign Direct Investment. I specifically did not include comprehensive capital account liberalization, because that did not command a consensus in Washington.

8. " Privatization. This was the one area in which what originated as a neoliberal idea had won broad acceptance. We have since been made very conscious that it matters a lot how privatization is done: it can be a highly corrupt process that transfers assets to a privileged elite for a fraction of their true value, but the evidence is that it brings benefits when done properly.

9. " Deregulation. This focused specifically on easing barriers to entry and exit, not on abolishing regulations designed for safety or environmental reasons.

10. " Property Rights. This was primarily about providing the informal sector with the ability to gain property rights at acceptable cost.

"The three big ideas here are macroeconomic discipline, a market economy, and openness to the world (at least in respect of trade and FDI [Foreign Direct Investment]). These are ideas that had long been regarded as orthodox so far as OECD countries are concerned, but there used to be a sort of global apartheid which claimed that developing countries came from a different universe which enabled them to benefit from (a) inflation (so as to reap the inflation tax and boost investment); (b) a leading role for the state in initiating industrialization; and (c) import substitution. The Washington Consensus said that this era of apartheid was over."

Regardless of what John Williamson's intentions were in 1989, the fact of the matter is that the Bretton Woods institutions and the developed world began using the prescriptions contained in the "Washington Consensus" as the alpha and the omega of a development model that all developing countries had to implement.

In February 2003, the U.S. Global Policy Forum published an article written by Xavier Cano Tamayo entitled "Burying the 'Washington Consensus".

To explain the real origins and effects of this Consensus as he understood it, he said:

"Communism, having been disarmed and extinguished in combat; capitalism put on a brave face and in the death throws of the eighties formulated economic policy directives with mandatory effect; a process leading towards the final consequences of economic liberalism as formulated at the end of the eighteenth century and the beginning of the nineteenth.

"The 'Consensus' prescribed budgetary discipline (a passion for eliminating deficits), fiscal reform (favouring those who own most), trade liberalisation (removal of tariff barriers by less developed countries without any compensation from the rich), opening up to foreign investment (without rules or controls), privatisation (public patrimony within the grasp of the powerful), deregulation (weakening or removal of labour guarantees, social and environmental controls), absolute guarantee of right to property and management of lesser affairs (excepting police involvement)."

He went further to report that: "Latin America, the principal victim of this 'Consensus', is a prime example of the disaster it has caused. In 1980 there were 120 million poor; in 1999 the number had increased to 220 million, 45% of the population; the richest 20% is almost 19 times richer than the poorest 20%, when the world average is that the rich are only 7 times richer than the poorest. After a decade of blindly devoted application of the Washington Consensus guidelines, Latin America stands on the edge of a precipice. Debt grew from US$492,000 million in 1991 to US$787,000 million in 2001. Railways,

telecommunications, airlines, drinking water supplies and energy supplies were virtually wound up and handed over to giant US and European corporations. Public spending on education, health, housing and social benefits was reduced, price control was abolished, wages were frozen and millions of workers were dismissed by the new masters of the now-privatised public undertakings."

He reported that in the light of all these negative outcomes of the "Washington Consensus" policies, "James Wolfensohn, President of the World Bank, declared in November 2002 at a Latin American Meeting in preparation for the Davos World Economic Forum; 'the Washington Consensus is dead'."

The World Bank also issued a statement on the results of a seminar it had convened in Paris to discuss the "Washington Consensus". It said: "The so-called Washington Consensus on market-oriented policy measures and macro economic balance either failed to achieve expected results in terms of growth and poverty reduction or was interpreted from an ideological point of view in many developing countries, a group of experts and analysts agreed at an international roundtable hosted by the World Bank last week in Paris. The gathered experts sought a new approach that would include investment in social development, environmental responsibility, and a strong regulatory role for the state, as well as international cooperation through multi- and bilateral development institutions. They also agreed that people's needs must be at the center, when formulating an economic policy."

It has also been reported that when he addressed the Foreign Correspondents Club in Tokyo in January 1999, in the aftermath of 1997-98 Asian crisis, Japan's vice-finance minister for international affairs, Eisuke Sakakibara, criticised the IMF's handling of the Asian crisis, and said the Fund's philosophy reflected the "Washington consensus" of "free markets and sound money", which had been blindly applied as a universal model on emerging economies.

He went on to say: "Since I was personally involved in the process and agreed, although reluctantly, in the end to what was recommended, I am in no position to criticise others for what has happened. But unlike the (IMF) managing director Michel Camdessus I can only say that if I am confronted with similar situations in the future I will probably handle them differently."

At the time still the Managing Director of the IMF, Michel Camdessus participated in UNCTAD X in Bangkok, Thailand in 2000. During an interactive session with the public, among other things he said:

"It is recognised that the market can have major failures, that growth alone is not enough or can even be destructive of the natural environment or precious social goods and cultural values. Only the pursuit of high quality growth is worth the effort - growth that can be sustained over time... growth that has the human person at its centre.... growth based on continuous effort for more equity, poverty alleviation, and empowerment of poor people.

"Systematically dismantling the state is not the way to respond to the problems of modern economies; rather, we must aim for a slimmer yet more effective state.

"The new emerging paradigm, rooted in fundamental human values, taken together with a better ability to prevent and manage the crises, is a distinct and positive chance of our times... A new perception of globalisation is emerging a call for common action to transform globalisation into an effective instrument for development."

The Managing Director of the IMF also made the comment, "I don't know what the Washington Consensus was. I never signed it."

In 2001, Mark Weisbrot delivered a paper entitled "The Need to Rethink Development Economics", at a conference in Cape Town organised by the United Nations Research Institute for Social Development. Among other things he said:

"Most of the neo-liberal principles that have replaced the discipline of development economics - most importantly, the idea that simply opening up to international trade and investment constitutes a development strategy -enjoy widespread acceptance in educated circles.

"This is true in spite of the fact that the last 20 years of the experiment in applying these principles, during which most low and middle income countries significantly opened their economies and followed Washington's economic advice, have been an unquestionable economic failure. In Latin America, GDP per capita has grown by about 7 percent over the last two decades; from 1960-1980 it grew by 75 percent. In Africa, income per capita grew by about 34 percent from 1960-80; it has since declined by more than 15 percent. This decline in growth has occurred throughout the vast majority of developing countries. The major exceptions are China and India, but neither can be pointed to as an example of success in adopting neo-liberal policies. China, which recorded some the highest growth rates in world history over the last 20 years, maintains strict currency controls, considerable protection of its domestic consumer markets, and its financial system is dominated by state-owned banks.

"If we group countries by their starting level of per capita income, rather than by region, the growth slowdown is very pronounced. The lowest quintile went from a per capita GDP growth rate of 1.9 percent annually in 1960-80, to a decline of 0.5 percent per year (1980-2000). For the middle quintile (which includes mostly poor countries), there was a sharp decline from an annual per capita growth rate of 3.6 percent to just less than 1 percent. These declines in growth represent an enormous difference in living standards as compared to what was considered normal and feasible in the past, and there were declines across all groups of countries.

"The failure of the last two decades also shows up in a substantial decline in the major social indicators (again dividing the countries into quintiles according to their initial level at the beginning of the period). For almost all groups of countries, there was considerably reduced progress in life expectancy, infant and child mortality, measures of education, and literacy in the past two decades, as compared with the period from 1960-1980.

"If these basic facts were well known - especially the failure regarding economic growth - there would be a much different public debate about the last 20 years. The main question would be: what has gone wrong? What are the structural and policy changes that have led to this wide-ranging failure?

"A change in the debate of this nature would help to create political space for a renewed practice of development economics. There are many paths to development, as Keith Griffin has argued, but the problem is that almost all of them are currently blocked by the reigning neo-liberal orthodoxy. And now we have the WTO [World Trade Organisation] throwing further obstacles in the way, for example, through its TRIPS (Trade Related Aspects of Intellectual Property Rights).

"By tightening the enforcement of patents and copyrights, the TRIPS agreement will make it much more difficult, if not impossible, for developing countries to industrialize in the way that countries such as South Korea and Taiwan did, on the basis of borrowed technology; while at the same time draining tens of billions of dollars of scarce capital from South to North, for royalties and other intellectual property payments.

"Economists and policy analysts from throughout the world can play an important role in changing the public debate, and making it more honest. In the last year or two the World Bank has for the first time begun to respond to its critics on the economic arguments."

We should draw a few conclusions from the foregoing:

- The "Washington Consensus" constitutes a development model based on the ideology of "market fundamentalism".

- It has obliged the developing countries to depend on "the market" for the investment and other interventions that would enable them to reach their takeoff point, contrary to what happened to post-war Western Europe and the Asian Far East, and is happening within the EU.

- Private capital, however, is inherently driven by the profit motive and is incapable, on its own, of addressing the challenge of poverty and

underdevelopment.

- Consequently, with regard to the majority of developing countries, in the context of weak supportive intervention by the governments of the developed countries because they do not feel threatened by the poverty in these countries, the pursuit of profit by global private capital has worked against the goal of people centred development.

- Contrary to its own development experience with regard to the Marshall Plan and its Regional Policy, the EU persuaded the ACP countries to adopt the Cotonou Agreement, which is based on the precepts of the "Washington Consensus", to which the EU Green Paper on its cooperation with the ACP countries referred when it said, "development thinking itself has moved on".

- The members of the OECD and the multilateral development institutions have taken the same position, in favour of the "Washington Consensus" positions. Accordingly, with regard to the developing countries, they are unwilling to adopt the position of the EU with respect to its Regional Policy, that this must entail the necessarily substantial resource transfers from the rich to the poor.

- Globally, the vast bulk of capital is in the hands of the private sector. The strategic posture represented by the "Washington Consensus", to rely on this sector to achieve development, means that the governments of the developed countries will resist all efforts to transfer a portion of global private capital to the public sector, which would give this sector the possibility to make the "public interventions" mentioned by Fukuda-Parr.

- Whereas, today, the "Washington Consensus" has few overt supporters among the global decision makers, it has not been replaced by any serious programmes that seek to replicate the successful Marshall Plan and the related development models.

- Freed of any challenge equivalent to the perceived threat posed by "communism", the developed capitalist countries will devote only such resources to meet the needs of the poor billions in the world as would ensure that these billions do not act in a manner that threatens their survival as prosperous capitalist countries.

- Conscious of the absence of such a threat, these countries are ready to argue against substantial resource transfers to the poor, on the basis that their constituencies suffer from "donor fatigue". In any case, they have a responsibility to address the serious challenge of poverty within their own societies.

- These positions have become the dominant ideology of contemporary society, and are therefore sustained by a veritable army of prophets in academia, the media and decision makers in many countries, regions and the multilateral organisations.

- The infinitely elastic determinations of this dominant ideology of what constitutes the basis for successful social and economic development inevitably lead to the realisation of the self-fulfilling prophecies of these prophets - there will be failure until success is achieved, in circumstances in which the pursuit of success prescribes continuing failure!

South Africa is fully integrated within the global economy. It is therefore open to the pressures imposed on all medium-sized middle-income countries of the South by the objective process of globalisation and the attendant subjective

ideology of market fundamentalism. At the same time, a large part of our population is caught in an underdeveloped sector, the Second Economy, which cannot escape the trap of poverty and underdevelopment through reliance on "the market".

The question that arises is whether we have an autonomous domestic possibility to achieve what Sakiko Fukuda-Parr spoke about with regard to "public interventions (that are) are necessary to set the preconditions for market-led economic growth".

** This is part six in a special series of articles about global approaches to poverty eradication and economic development. Next week: 'Transform the Second Economy'.

APPROACHES TO POVERTY ERADICATION AND ECONOMIC DEVELOPMENT VII

Transform the Second Economy

IN 2003, to prepare for our First Decade of Democracy in 2004, our government published the major study, 'Towards a Ten Year Review'. Among other things, the Review said: "One of the major consequences of the change in the structure of the (South African) economy is that 'two economies' persist in one country. The first is an advanced, sophisticated economy, based on skilled labour, which is becoming more globally competitive. The second is a mainly informal, marginalised, unskilled economy, populated by the unemployed and those unemployable in the formal sector. Despite the impressive gains made in the first economy, the benefits of growth have yet to reach the second economy, and with the enormity of the challenges arising from the social transition, the second economy risks falling further behind, if there is no decisive government intervention."

In his well known book, 'Development as Freedom', the Nobel Prize winner in economics, Amartya Sen says: "Development requires the removal of major sources of unfreedom: poverty as well as tyranny, poor economic opportunities as well as systematic social deprivation, neglect of public facilities as well as intolerance or overactivity of repressive states. Despite unprecedented increase in overall opulence, the contemporary world denies elementary freedoms to vast numbers - perhaps even the majority - of people. Sometimes the lack of substantive freedoms relates directly to economic poverty, which robs people of the freedom to satisfy hunger, or to achieve sufficient nutrition, or to obtain remedies for treatable illnesses, or the opportunity to be adequately clothed or sheltered, or to enjoy clean water or sanitary facilities. In other cases, the unfreedom links closely to the lack of public facilities and social care, such as the absence of epidemiological programmes, or of organised arrangements for health care or educational facilities, or of effective institutions for the maintenance of local peace and order. In still other cases, the violation of freedom results directly from a denial of political and civil liberties by authoritarian regimes and from imposed restrictions on the freedom to participate in the social, political and economic life of the community."

He contrasts what he calls "growth mediated" with "support-led" development, expressing preference for the latter. He writes: "In contrast with the growth-mediated mechanism, the support-led process does not operate through fast economic growth, but works through a programme of skilful social support of health care, education and other relevant social arrangements."

In this context he argues that "Despite their very low levels of income, the people of Kerala (in India), or China, or Sri Lanka enjoy enormously higher levels of life expectancy than do much richer populations of Brazil, South Africa and Namibia, not to mention Gabon (with wealth measured by GNP per capita).An income-centred (GNP) view is in serious need of supplementation, in order to have a fuller understanding of the process of development."

Everything Sen says indicates the challenge we face as we work to transform the Second Economy. Fortunately we no longer have the burden of the "unfreedom" imposed by tyranny and the denial of political and civil liberties by an authoritarian regime. Nevertheless the Second Economy in our country is characterised by many of the "unfreedoms" that Sen wrote about.

Contrary to what was stated in the 'Ten Year Review' the challenge we face extends beyond "(economic) growth" and relates to the complex of "unfreedoms" mentioned by Sen. The very fact of the existence of the Second Economy side by side with the First argues against a simple focus on growth.

In his article "Paradoxical Growth" in the book, 'The Post-Development Reader', Serge Latouche, Professor of Economics at the University of Paris XI, wrote: "In a World Bank report of 1991, we read: 'During its first two decades of existence, the World Bank tended to identify development with economic growth. The benefits of growth were assumed to trickle down, the poor automatically benefiting from the creation of jobs and the increase in goods and services.'"

The famous trickle-down effect

He continues: "The claim of economic growth to be the basic objective of human society is therefore mainly based on the famous trickle-down effect, magnified by the euphoria of the myths of modernity. However, this seductive formulation cannot stand up to a serious examination. So many paradoxes beset the reasoning that the miracle effect, in fact, turns out to be the mirage effect.What invalidates the whole ideology of growth is the fact that the trickle-down effect is an imposture.At the planetary level, the mechanism never functioned anyway. Between 1950 and 1987, according to the World Bank's own statistics, while the world's revenues multiplied by 2.5, the gap between the richest and the poorest fifths of the population grew from 30:1 to 60:1." ('The Post-Development Reader', compiled by Majid Ranhema & Victoria Bawtree: David Philip, Cape Town, 1997).

The First and Second Economies in our country are separated from each other by a structural fault. The Second Economy emerged during the long period of colonialism and apartheid as a result of the deliberate imposition of the "unfreedoms" described by Sen. This process aimed to achieve the enrichment of the white minority at the cost of the impoverishment of the black majority.

That process of impoverishment included ensuring that the white economy had access to unlimited supplies of cheap unskilled black labour, and that this economy did not waste any money on the development of the localities in which the black workers lived. This did not even allow for the possibility of improving the lives of the oppressed majority through the "trickle-down effect".

Accordingly, what we now have is the reality described in the 'Ten Year Review', of a "mainly informal, marginalised, unskilled economy, populated by the unemployed and those unemployable in the formal sector".

The Second Economy is caught in a "poverty trap". It is therefore unable to generate the internal savings that would enable it to achieve the high rates of investment it needs. Accordingly, on its own, it is unable to attain rates of growth that would ultimately end its condition of underdevelopment.

It does not have the internal means to effect the "support-led" development Amartya Sen spoke about, resulting in targeted improvements in the health, education, training and social development of those imprisoned within the Second Economy, despite its low level of economic development as measured by per capita GDP.

It is linked to the First Economy by the extent to which it can still supply the cheap, unskilled labour this economy may require. It survives on money transfers sent by family members who have been able to secure regular or occasional employment within the First Economy, as well as social grants and elements of the social wage provided by the democratic state.

It is also linked to the First Economy by the goods, equipment and services it purchases with the meagre resources at its disposal. Those resources also make it possible for the Second Economy to maintain an informal economic sector of small traders, artisans and service providers.

Such positive trickle-down effects as would result from the higher earnings of family members who would benefit from higher incomes in the First Economy, as well as individual and social transfers by the state, would not be sufficient significantly to raise the standard of living in the Second Economy, or close the ever-widening wealth and development gap between the two economies.

The market economy, which encompasses both the First and the Second economies, is unable to solve the problem of poverty and underdevelopment that characterises the Second Economy. Neither can welfare grants and increases in the social wage. The level of underdevelopment of the Second Economy also makes it structurally inevitable that the bulk of such resources as flow into the Second Economy will inevitably "leak" back into the First Economy.

Such public and private interventions as may be made producing a positive outcome in the First Economy cannot have any strategic impact on the Second Economy because it constitutes the structural periphery of the former, inherently positioned to remain on the periphery. Its internal objective reality in terms of the forces of production and their interaction makes it impossible for it to respond to the impulses that drive the growth and development of the First Economy.

All this makes decisive government intervention imperative, as the 'Ten Year Review' said, which would "set the preconditions for market-led economic growth". Fortunately, in this regard, we have the possibility to draw on the positive examples and lessons of the Marshall Plan, the post-war development of the Asian Far East, and the EU Regional Policy. We can also learn from the negative examples of the ACP-EU Lome and Cotonou Agreements and the implementation of the policies of the "Washington Consensus".

Reliance on domestic resources

One of the lessons from these experiences is that we should, to the greater extent, finance the transformation of the Second Economy relying on domestic resources. These should be made available through the state in the form of grants. This does not rule out accessing commercial loans by the state, or equity participation funds, to finance economically viable projects that have the possibility to generate profits that would be used to finance debt.

Necessarily, therefore, decisive government intervention in the Second Economy requires that the government should have the resources to make this intervention.

The successful management of the macro-economy, coupled with policies that have resulted in the growth of the First Economy, have enabled the government to generate these resources. These results must therefore rank among our most important achievements during the First Decade of Freedom, precisely because they create the possibility for our country seriously to confront the challenge of the Second Economy.

The 2004 Budget Review of our National Treasury makes a number of important observations in this regard. It says:

"Greater impetus to economic restructuring began in 1996, with a macroeconomic strategy (GEAR) that emphasised improved industrial competitiveness, inflation reduction, gradual relaxation of exchange controls, strengthened funding of training, tax incentives to stimulate investment, deficit reduction and budget reform focused on the redistributive thrust of expenditure. Having laid these secure foundations, a more expansionary fiscal policy stance could be adopted in 2001.

"Against the background of the fiscal consolidation achieved over the past decade - expenditure reprioritisation, a lower budget deficit, improved management of the public debt, lower interest rates and a buoyant tax structure - the 2004 Budget aims to invigorate the recovery evident in the last quarter of 2003 while continuing to build firm foundations for long-run growth and development.

"Prudent fiscal management has resulted in public debt levels falling within manageable limits, lowering debt service costs and freeing resources for more important socio-economic programmes, including infrastructure development, job creation and social security. Enhanced management and governance, together with improving delivery capacity, ensure that this expenditure contributes meaningfully to economic growth and development."

In the context of the success of the post-1996 macro-economic policies resulting in "freeing resources for more important socio-economic programmes", various policies and programmes have already been decided. The Integrated and Sustainable Rural Development and Urban Renewal Programmes are central to the success of our response to the Second Economy. They must focus on addressing the "unfreedoms" mentioned by Sen, and not just the goal of economic growth.

Similarly, we also have to ensure the success of our Expanded Public Works, the Human Resource Strategy, and Comprehensive Agricultural Support Programmes, all of which relate directly to the transformation of the Second Economy.

Other interventions in other areas, ranging from the Municipal Infrastructure Grant to the development of e-government through the use of modern information and communication technologies, must, in part, be geared towards ensuring the success of the major programmes we have mentioned, specifically directed at the transformation of the Second Economy.

With regard to all these interventions in both the First and Second economies, on 26 October this year, Minister of Finance Trevor Manuel said:

"Our policy agenda focuses on both growing the formal economy and expanding the economic opportunities of those who are marginalised, those who, without direct policy interventions, will not benefit from the fruits of a growing economy. Reducing this social exclusion through drawing in the millions who find themselves trapped in the second economy is a fundamental principle of our policy stance. To achieve this objective, we will have to intervene directly in the way in which the fruits of economic growth are shared, in the way in which economic opportunities are parcelled out.

"South Africa's development challenge is to build a single and integrated economy that benefits all, encompassing both growing, competitive relations with the global economy and a caring, inclusive network of social services and support for the disadvantaged. This is, on a larger scale, the central challenge also of international relations - the struggle for modernisation and solidarity against deeply embedded inequalities, conflict and prejudice."

As with the European Union (EU) Regional Policy, we must aim to achieve:

- productive investment to create and safeguard sustainable jobs;
- investment in infrastructure which contributes to development, structural adjustment and creation and maintenance of sustainable jobs, or, in all eligible regions, to diversification, revitalisation, improved access and regeneration of economic sites and industrial areas suffering from decline, depressed urban areas, and rural areas;
- development of the endogenous potential by measures which support local development and employment initiatives and the activities of small and medium-sized enterprises; such assistance should be aimed at services for enterprises and cooperatives, transfer of technology, development of financing institutions, direct aid to investment, provision of local infrastructure, and aid for structures providing neighbourhood services;
- Investment in education and training and health.

We must also take note of the observation made by the EU that "the dynamic effects of EU membership, coupled with a vigorous and targeted regional policy, can bring results".

Success in the First Economy

We must fully understand that the success of our own vigorous and targeted interventions in the Second Economy is also dependent on the success of the First Economy and building the structural links between these two economies. In the end, as was the objective of the Marshall Plan, those

currently caught within the Second Economy should ultimately be able to grow and develop without the need for exceptional outside interventions.

This means that even as we pay concentrated attention to the Second Economy, we must not reduce our focus on the growth and development of the First Economy.

Even as we do so, given the continuing imperative for our economy to create jobs, we should pay attention to an empirical observation made by the German Bundesbank. Commenting on the impact on growth of foreign direct investment (FDI), on 24 February 2003 its International Relations Department said: "FDI can act as a significant impetus to growth but only if the level of human capital has crossed a certain threshold. The intuition behind this result is that the more advanced technologies can be fruitfully put to use only after the required human capital has been acquired. Should the technology, however, exceed the absorptive capability of the host country, no trickle-down effects will ensue. Similarly, it can be argued that the products of MNEs (multinational enterprises) may often be too capital intensive for the needs of the host country. The effect may then be to create 'dual economies', with one modern sector and distinct from it a backward domestic sector with only limited overlap. FDI of this kind might consequently result in an excessively capital-intensive production process, leading to a less favourable development of the overall employment situation."

This emphasises the need for us to pay very close and sustained attention to the success of our Human Resource Development Programme to prepare our people to have the vocational and professional skills required by the modern global economy, which includes our First Economy.

In this regard, we have to be aware of the increased global mobility of skills, which results in skilled people being drawn to other countries because of higher pay and opportunities for professional development. This also gives us the possibility to meet our skills shortages by improving immigration of the right people into our country.

We must also ensure the success of the interventions to gain access to private capital for targeted investments, as visualised by the Growth and Development Summit, and properly to utilise the capital available to the government and the public sector Development Finance Institutions.

Given the responsibilities that fall on the democratic state with regard to the development and transformation of both the First and Second Economies, we have to ensure that the state machinery is so organised, empowered and motivated that it can discharge its responsibilities effectively. We must also mobilise the people to participate in the eradication of the "unfreedoms" imposed on them by a long history of colonialism and apartheid.

Simultaneously, we have to maintain the social expenditures targeted at providing a social security net for the poor and disadvantaged, as well as social development to achieve higher levels of education, better health and nutrition, and other outcomes to improve the quality of life and empowerment of all our people, including the women and the youth in both urban and rural areas.

However, the democratic state will have to take great care to ensure that expenditure on social security does not lead to such misallocation of public resources that there is nothing to direct to the fundamental task of the transformation of the Second Economy. In this regard, on 26 October this year, Minister of Finance Trevor Manuel, said: "We need to acknowledge that our social security net is under severe strain. Rapid growth in disability and foster care grant applications indicate both rising income support needs and apparent deficiencies in administrative systems. A sustainable social security system must balance bringing in everyone who is entitled to grants and keeping out everyone who is not entitled to them."

From all this we can draw the following conclusions:

- We must understand the irrationality of depending on "market mechanisms" and/or private investment to advance the Second Economy to reach its takeoff point.
- The Second Economy is too poor to generate the savings and capital it needs for its development. Its levels of poverty and underdevelopment make it impossible for it to attract significant volumes of private capital.
- Accordingly, public sector transfers must constitute the bulk of its development funds.
- However, it will also be possible to use private sector capital to finance profit making ventures within the Second Economy. Some public sector funds should also be devoted to the development of such ventures on a recoverable basis.
- Contrary to arguments about minimal state intervention in the economy, we must proceed on the basis of the critical need for the state to be involved in the transformation of the Second Economy.

- This state intervention must entail detailed planning and implementation of comprehensive development programmes, fully accepting the concept of a developmental state.

- The government must commit the necessary human and material resources to ensure that the state machinery is able to discharge its development responsibilities. Among other things, this must entail the necessary progress with regard to the government's efforts to achieve an integrated system of government, affecting all the national departments and the three spheres of government.

- The government must ensure the success of its interventions with regard to the development of small, medium and micro business within the Second Economy.

- As part of the process of monitoring and evaluating its interventions in the Second Economy, the government should set some benchmarks against which to measure the success of these interventions. These could include the reduction in the relative share of social welfare spending within the national budget, caused by the increase in numbers of people dependent for their income on productive employment.

Taken together, the interventions in the Second Economy should, as Sen said, ensure "the removal of major sources of unfreedom: poverty.poor economic opportunities as well as systematic social deprivation, neglect of public facilities.", responding to a view of development that goes beyond a narrow "income-centred (GNP) view" of development.
** This is part seven in a special series of articles about global approaches to poverty eradication and economic development. Next week, in the final part of the series: 'Empty bellies have no ears'.

APPROACHES TO POVERTY ERADICATION AND ECONOMIC DEVELOPMENT VIII

Empty bellies have no ears

THE GLOBAL contest between the different development models also entails a dispute about the overall impact of the process of globalisation. There are many who argue that in general, this process has expanded human welfare throughout the globe. These advance the view that the hopes of the poor and underdeveloped countries of the world for a better life lie in their integration within the global economy.

In an article published in the 'Financial Times' on 24 January 2001, entitled "Growth makes the poor richer", its well known columnist, Martin Wolf, says "One thing, above all, is quite clear: if the world is to become less unequal through raising the bottom, rather than collapsing the top, and still more if mass poverty is to be eliminated, it can only be via successful integration, not its opposite."

We must however counterbalance this prayer to the future with global experience to date. For an account of this experience, we shall rely extensively on a May 2001 paper written by Professor Robert Hunter Wade of the London School of Economics, entitled "Is Globalisation Making World Income Distribution More Equal?" He writes:

"If we are interested in world income distribution from the point of view of most of the issues that concern the world at large.the conclusion is unambiguous: world income distribution became much more unequal over the past quarter century, whether we use decile distributions or an average coefficient like the Gini and whether we weight individuals or countries equally.

"Moreover, the gaps in 'real' well-being are probably bigger than the income figures suggest.Those in the bottom half of the world income distribution have incomes that are not only lower but also more insecure, and they have probably faced rising insecurity over the 1990s (much of the new employment in low income areas is in jobs subject to short-term contracts and immediate dismissal.).

"Most of the increase in inequality reflects the increase in the proportion of the world's households located at the extreme rich end and the extreme poor end of the world income distribution. On the one hand, population growth adds disproportionately to numbers at the poor end. On the other hand, technological change results in disproportionately fast increase in the numbers of households at the rich end, without shrinking the distribution at the poor end.

"The prices of the industrial goods and services exported from high-income countries are increasing relatively faster than the prices of goods and services produced in low-income countries that do not enter into international trade. These price trends mean that the majority of the population of poor countries are able to buy fewer and fewer goods and services that enter into the consumption patterns of high-income country populations.

"The poorer countries and the poorer two thirds of the world's population suffer a double marginalisation: once through slower growing output, again through falling relative prices.

"The capital inflows tend to occur when economic growth is relatively fast, and the combination of fast growth and capital inflows together tends to boost asset prices, which benefits mainly the rich (asset owners). The benefits to the poor take much longer to accrue through higher employment and government spending on services. So the capital inflows tend to widen national income inequality.

"When a shock hits (as a result of financial crisis in a situation of financial liberalisation).the crisis ricochets around the economy, causing layoffs, falls in demand, rises in inventories, bankruptcies, cuts in government services, unrest. While the benefits of the capital inflows are shared 'oligarchically', the costs of the crisis are shared 'democratically', with immediate impacts on the poor and on the middle class which had taken on lots of debt during good times.

"The crises cause not only instability of developing country growth rates; they also cause a tendency to lurch towards another set of economic policies - even though there may be no good evidence that the previous policies caused the crisis. The most dramatic case in point is the wholesale revulsion towards 'import substitution' in Latin America in the wake of the 1980s debt crisis, and the embrace of neo-liberalism. The crisis was due largely to mismanagement of the capital structure (the debt structure) - the governments borrowed too much and the lending banks, mostly American, lent too much relative to the countries' capacity to pay.

"But instead of seeing this as the cause of the crisis, the governments, encouraged by the IMF and the World Bank and the US Treasury, abandoned a set of economic policies that had in fact generated high growth in the 1960s and 1970s, and put in place a standard package of neo-liberal market opening measures. These have not delivered high growth, and they have resulted in high levels of (corporate, household and sovereign) indebtedness.Even 'The Economist', no foe of income inequality, agrees that rapid market liberalisation is likely to widen income inequalities.(5 November 1994).

"(Another cause of the growing income inequality is) the continuing redistribution of income in the OECD countries through the tax system and the welfare state, which in the case of the UK in 1992 reduced the ratio of the income of the top 20 percent of Britons to the poorest 20 percent from 25:1 before taxes and transfers to 7:1 afterwards. This welfare state system prevents anyone living in the OECD countries from falling very far down the world income distribution. And of course it gives a huge incentive for people living elsewhere to try to enter the OECD world by whatever means possible.

"The richest 10 percent of the world's population is pulling up from the median, and the poorest 10 percent is falling away from the median; the world middle class, so to speak, remains tiny, while the gulf between the 15 percent of the world's population living in the richest countries and the three quarters living in the poorest countries remains huge.

"Income divergence helps to explain another kind of polarisation taking place in the world system, between a zone of peace and a zone of turmoil.At least for those in the top half of rich country income distributions, this is a blissful time to be alive. On the other hand, the regions of the lower and middle income pole contain many states whose capacity to govern is stagnant or eroding, mainly in Africa, the Middle East, Central Asia, Russia, and parts of East Asia. Here a rising proportion of the people find access to basic necessities restricted at the same time as they see people driving Mercedes - on television if not outside their own windows.

"World inequality matters as an indicator of global political strain. But it also matters for more directly economic reasons, as an indicator of the limits of growth of the rich countries. Marginalisation of poor country populations robs rich country producers of customers.

"The US after World War Two realised that its own growth would be imperilled if it did not redistribute massively to Europe, including the defeated states. The Marshall Plan redistributed around 4 percent of US GDP for several years in order to generate in Europe the purchasing power needed to buy US goods, as well as to keep communist movements from state power.

"Today, resource transfers from rich countries to poor, and downwards redistribution within poor countries (including via the mechanisms used in the West, such as collective action by the poor and slowly rising legal minimum wages or earned-income credits), are in the collective interests of the rich countries as the Marshall Plan was to the United States. Those who respond to evidence of rising world inequality by saying, 'pulling up the poor still remains a nobler calling than pulling down the rich', overlook this. Without downwards redistribution, the rich may not remain rich.

"It might be argued (as did Martin Wolf), that since the biggest increase in poverty came in Africa, central Asia, rural India and rural China - places not connected to the global economy - this shows that globalisation works to reduce poverty. The solution for these areas is fuller integration into the world economy - more globalisation rather than less. (This position) begs the question of the conditions for 'successful integration'.

"People in the bottom deciles suffer from the weakness of capitalist development in the regions where they live. The question of development policy is whether this weakness can be cured mainly by opening up their markets, investing in infrastructure, removing price distortions, and strengthening the rule of law. Many economists say that the positive correlation between average incomes and countries' integration into the world economy (high trade to GDP, for example) supports the case for a development strategy based on maximum integration.

"But this argument obscures the distinction between the policies that the richer countries followed while they were getting rich and those they followed once rich. The East Asian states achieved great economic success.by creating national economic space that was partially separate from the world economy, within which resources could be combined and made to produce nationally-marketable products even when those products would not have been able to compete against import substitutes; at the same time as they gave strong incentives for producers to export to world markets.

"They recognised - as did the World Bank and even the US government in those days - that if they just concentrated on 'levelling the playing field', the players might not show up and those who did might include few of their nationals. Their strategy for creating self-generating development and integrating into the world economy in a strategic way fits neither of the two alternatives - full-scale integration or isolation - that Martin Wolf, among others, pose.

"In particular, they were careful about the terms on which they allowed foreign capital to enter (whether in the form of direct foreign investment or loans), and about the liberalisation and opening of the financial system. In the 1990s Korea abandoned its earlier caution as it came under heavy US

pressure to open its financial markets in return for US support of its OECD membership. It was rewarded by being far more adversely affected by the Asian crisis of 1997-98 than nearby Taiwan, which remained more cautious about financial liberalisation and opening.

"In African conditions today, what possibility is there of national populations which are 50 percent functionally illiterate and innumerate getting access to the productivity gains of new technologies? In open competition with labour forces and infrastructures elsewhere, they will always lose, however low the exchange rate (except where high transport costs give natural protection).

"They should put up partial barriers as the East Asians did, behind which partly different rules apply, so as to balance (a) the benefits of comparative advantage and competitive discipline, against (b) the benefits of putting resources to work that could not be profitably put to work in a fully open economy. They should have a partly closed capital account, and should take care to minimise the 'inverse correlation' in their capital structure (minimise the extent to which repayment obligations are lower than capacity when capacity to repay is higher and higher when capacity to repay is lower). Hence they should pay more for foreign loans during good times, by hedging or by indexing them to the price of their main exports or by denominating them in domestic currency; and they should also hedge the price of their main commodity products.

"China is in the midst of perhaps the fastest and most far-reaching transformations seen anywhere in the past two hundred years - but doing so in a 'gradualist' way in line with the broadly dirigiste strategy of pre-1970 Japan and pre-1990 South Korea and Taiwan; and thereby violating many current World Bank precepts about how countries should develop. Russia and most of the Soviet empire have followed a Big Bang strategy of full-scale integration and privatisation (with Harvard-based American advisers and the World Bank playing the leading role in devising and implementing the Big Bang). The result? Large parts of the former Soviet Union are more impoverished than they were in 1989, and the most profitable assets have fallen into the hands of economic gangsters. In the comparison, China easily wins.

"The great danger of the state governing the market is wholesale corruption and incompetence.A development strategy focused on building up the institutional infrastructure of markets, investing in infrastructure on roads, schools, health systems, and promoting the rule of law, may be about the best that can be hoped for.

"In the longer run, building up organisational capacity outside the state is important. 'Non-governmental organisations' can constitute a form of social mobilisation through which governments can be made more accountable.But NGOs tend to be single-interest and therefore politically divisive. They have to be balanced by political parties and the state itself, organisations where different interests can be aggregated, brought to a point of convergence, compromises struck, priorities established.

"By and large, stronger markets need stronger states, and stronger states need both stronger markets and stronger civil societies.The Marshall Plan's programmes in post-war Europe recognised that redistributive flows had to be accompanied by measures to build state capacity to manage the national economy and regulate markets, financial markets especially.

"Concerted strategies to strengthen states, industries, and civil societies in low income parts of the world have to be complemented by more open markets in Europe, North America and Japan for exports from these areas; and by increases in the flows of cheap, low cost resources from rich countries to poor, to be invested in many sectors (like water treatment, universities) where private financiers have no interest. Without a big push, we can expect world income distribution to continue widening, especially between Subsaharan Africa and parts of South Asia, on the one hand, and the rest of the world. This will generate more global political turbulence and more economic crises - not only in the low income world but in the rich world as well.

"It is remarkable how unconcerned are the World Bank, the IMF, and other agenda-setting global organisations about world income inequality. The Bank' s World Development Report for 2000 even said that rising income inequality 'should not be seen as a negative' provided that the incomes at the bottom do not fall and the number of people in poverty falls.

"It is striking that most of the organised opposition, as well as much of the support, for more globalisation comes from North America, western Europe and Oceania. Why have elites from developing countries for the most part subscribed to the globalisation agenda that western states, businesses, and multilateral organisations have been promoting, if a plausible case can be made that the gains of free markets for goods and capital tend to be concentrated in the top levels of the income distributions of their countries?...

"Part of the reason may be that elites in developing countries, like their counterparts in the rich world, are content to believe either that world inequality is falling, or that inequality is good because it is the source of incentives. They, like the intergovernmental economic organisations, worry about poverty. But they see no link between widening world income distribution and poverty; and they think that

poverty can be fixed by providing the poor with welfare and opportunities without changing income and asset distributions or mounting an active state industrial policy.

"The growing inequality in world income distribution is like global warming. Its effects are diffuse and long term, and there is always something more pressing to deal with. We don't seem to be able to rely on leadership and appeals to humanity to generate action.

"The question is how much more unequal world income distribution can become before the resulting political instabilities, migration flows and social disruption reach the point of harming the rich world enough to move it to action.

"If today's inequalities continue to increase, if social policy continues to move in the direction of 'risk is an opportunity for individuals to profit from' and away from 'society has a responsibility to protect individuals from certain kinds of risks', if the operational norm of world elites continues to shift towards 'grab what you can and the devil take the hindmost as quickly as he can', opposition to the things called 'globalisation' will continue to spread.

"We in the rich world should mobilise our governments, the multilateral organisations, and international NGOs - the actors who have the power to change the norms and rules of the world economy - to establish as an overarching priority a more equal world economic distribution, and not just, as now, fewer people in poverty."

The realisation of the goal of a more equal world economic distribution requires that both domestically and internationally, countries and human society as a whole must implement comprehensive and integrated development programmes informed by the objective mentioned by Professor Wade, in favour of the "protection of the individual from certain kinds of risks", away from the concept "grab what you can and the devil take the hindmost as quickly as he can".

Without this protection from the risks that Amartya Sen described as "unfreedoms", it will be impossible for South Africa, Africa and the rest of the developing world to succeed in the struggle against poverty and underdevelopment. That protection requires a conscious, determined and sustained transfer of development resources from the rich to the poor as well as a focused and effective use of such transferred resources to extricate the poor from the condition of dehumanising human backwardness.

And as Professor Wade has said, "Today, resource transfers from rich countries to poor, and downwards redistribution within poor countries (including via the mechanisms used in the West, such as collective action by the poor and slowly rising legal minimum wages or earned-income credits), are in the collective interests of the rich countries as the Marshall Plan was to the United States."

Overwhelmingly, the bulk of the resources to which he refers are in the rich countries that constitute 15 percent of the world population. Within these countries, the development resources we are talking about, including the all important capital, are in private hands.

Consistent with a fundamental law of the capitalist mode of production, the capitalists who own or control these resources put them to such uses as provide them with profit. However, the pursuit of this objective may not be consistent with the global goal of the defeat of poverty and underdevelopment, and the achievement of the objective of a more equitable distribution of income and wealth.

Objectively, as we respond to the development challenge, we are obliged to focus on two critical matters. One of these is the role of the state in development. The other is access to the enormous resources in private hands, without which successful development will not take place.

In its 1999/2000 World Development Report, the World Bank said: "Mutual funds, hedge funds, pension funds, insurance companies, and other investment and asset managers now compete with banks for national savings.Institutional investors have taken advantage of the easing of restrictions in many industrial countries to diversify their portfolios internationally, enlarging the pool of financial capital potentially available to developing and transition economies. In 1995 these investors controlled $20 trillion, 20 percent of it invested abroad."

At the same time, we must bear in mind that the bulk of foreign investment flows among the developed countries. The same World Bank Report said: "In 1997 developing countries accounted for 30 percent of the foreign direct investment stock, or $1.04 trillion, 90 percent of which originated in industrial countries. Five countries - Argentina, Brazil, China, Mexico, and Poland - received half the total for developing countries."

These World Bank observations highlight three important matters:

- there are huge volumes of capital in the developed countries which the developing countries need to access to achieve their development goals;
- this capital is in private hands and responds to market developments to seek the most profitable opportunities; and,

- these market possibilities draw this capital to a limited number of developing countries, partly drawn to these countries by the size of the domestic population.

This leads to the inevitable conclusion that the majority of the developing countries cannot rely on the market to gain adequate access to the capital available within the world economy. Other interventions must therefore be made to increase such access - hence the relevance of the correct call made by Professor Wade, that "We in the rich world should mobilise our governments, the multilateral organisations, and international NGOs - the actors who have the power to change the norms and rules of the world economy." to effect the resource transfers from the rich to the poor.

Consistent with this, the 1999 UNDP Human Development Report said "Pro-poor growth is needed.An important step would be to establish an international transfer mechanism to encourage resource flows to poor countries - through private investment and through purposeful allocation of global revenues derived from taxing pollution or charging for use of the global commons."

The observations made by Professor Wade and the UNDP draw attention to the critical importance of the role of government in the struggle against poverty and underdevelopment. In this regard, the 1997 World Development Report of the World Bank said:

"The collapse of the Soviet Union - by then no longer an attractive model -sounded the death knell for a developmental era. Suddenly, government failure, including the failure of publicly owned firms, seemed everywhere glaringly evident. Governments began to adopt policies designed to reduce the scope of the state's intervention in the economy. States curbed their involvement in production, prices, and trade. Market-friendly strategies took hold in large parts of the world. The pendulum had swung from the state-dominated development model of the 1960s and 1970s to the minimalist state of the 1980s.

"The consequences of an overzealous rejection of government have shifted attention from the sterile debate of state versus market, to a more fundamental crisis in state effectiveness. In some countries the crisis has led to outright collapse of the state. In others the erosion of the state's capability has led nongovernmental and people's organisations - civil society more broadly - to try to take its place. In their embrace of markets and rejection of state activism, many have wondered whether the market and civil society could ultimately supplant the state. But the lesson of a half-century's thinking and rethinking of the state's role in development is more nuanced. State-dominated development has failed, but so will stateless development. Development without an effective state is impossible."

All successful development initiatives since the Second World War confirm the conclusion of the World Bank - that development without an effective state is impossible. For the poor of the world, including our own, the importance of this observation is underlined by the fact that, despite its importance, the state does not own or control the huge volumes of capital available within the global economy.

The "resource transfers from rich countries to poor, and downwards redistribution within poor countries" of which Professor Wade spoke cannot and will not happen without the intervention of the state. If the state does not intervene, neither we nor the rest of the developing world will succeed to achieve the objectives of the eradication of poverty, underdevelopment and the inequitable distribution of income and wealth.

Global poverty constitutes one of the greatest challenges facing humanity. To confront it will require the development of a strong world movement mobilised to oblige "the governments (of the developed countries), the multilateral organisations, and international NGOs - the actors who have the power to change the norms and rules of the world economy - to establish as an overarching priority a more equal world economic distribution, and not just, as now, fewer people in poverty."

It also requires that the state everywhere, including in our country and the rest of Africa, should discharge its responsibilities to the people, fully understanding the observation made by the World Bank, that development without an effective state is impossible.

Professor Wade expressed amazement that "elites from developing countries for the most part subscribed to the globalisation agenda that western states, businesses, and multilateral organisations have been promoting". Perhaps he should keep in mind the Turkish proverb - he who has no bread has no authority.

Perhaps the elites that lead peoples who do not have bread believe that they stand the greatest chance to persuade those who have authority to come to their aid by repeating the injunctions propagated by those who have. Perhaps they believe that, in any case, the age of revolutions is over, and that therefore they have no choice but accommodate themselves within the globalisation agenda set by the dominant voices in world politics and the world economy.

But a Greek proverb says - you cannot reason with a hungry belly; it has no ears! Billions across the globe live with the reality of hungry bellies. Those who live in the comfort of wealth and prosperity may issue appeals to the poor to be patient because, in time, they too will enjoy lives of wealth and

prosperity. They may go beyond this to close the doors to their countries to tell the poor of the world they should stay at home to await the arrival of a better life for themselves.

They will have to pay attention to what Professor Wade said, that "Without a big push, we can expect world income distribution to continue widening, especially between Subsaharan Africa and parts of South Asia, on the one hand, and the rest of the world. This will generate more global political turbulence and more economic crises - not only in the low income world but in the rich world as well."

The rich world will need to remember that it cannot reason with a hungry belly; it has no ears! It will need to beware of the natives, whose only possession is hungry bellies without ears! In the era of globalisation, no country is an island.