Lecture 15

Relative Role of Actors in Shaping the Global Economy (III): Multilateral Institutions

KEY QUESTION:

Can multilateral institutions influence economic activities?

With the completion of this lecture, attached readings and tutorial, you should be able to discuss the influence of multilateral institutions on TNCs and states:

– Association of Southeast Asian Nations (ASEAN)
– World Trade Organisation (WTO)
– World Bank

Lecture Outline

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15.5 Conclusion

The World Trade Organization (WTO) sets out trading standards for much of the world to follow. But the relevance of such standards has been called into question in today's economy which has grown more complicated compared to the time when it was formed.

The WTO is an example of a multilateral institution, accorded with powers that can influence the global economy. Which other institutions operate above the scale of the state?

How effective have these multilateral institutions been in influencing TNCs and states?

15.1 Introduction: Multilateral Institutions

- Multilateral institutions (MIs) are **international institutions created by states**, usually as a means of **achieving collective objectives, usually of global priority, that could not be accomplished by acting individually**.
- Some multilateral institutions have a **truly global mandate**, such as the World Bank and the World Trade Organisation (WTO). They play a powerful role in **global development**, including **promoting economic and social development in specific countries or regions**.
- Other multilateral institutions operate at a **macro-regional** scale, such as the Association of Southeast Asian Nations (ASEAN).
- In this chapter, we will examine how MIs **shape the global economy**. In other words, we want to be able to explain how MIs promote flows of trade, capital and labour within the global economy, thereby affecting connectedness and interdependence in the global economy. We also want to understand how MIs contribute to changes in the economic structures of countries. Finally, we should be able to explain how MIs contribute to variations in levels of development in the global economy. Many of these impacts will involve TNCs responding to the policies and measures implemented/recommended by MIs.
- In addition, we learnt in **Lect 13** that states regulate and manage the flows of economic activities across their borders. But when multilateral institutions are involved, the state's role in governing its economy may arguably be compromised.
- However, most of these multilateral institutions represent an **upscaling** of economic governance by states. They upscale from their national regimes of regulation to the **international** and **macro-regional** scale.
- Nevertheless, while some states might have given up part of their capacity for economic governance to these multilateral institutions, it is important to remember that the **world's most powerful states today** (e.g. the United States, Germany, and China) have **remained the key movers behind these institutions**.
- Note that our syllabus requires us to be familiar with the:
  - ASEAN Free Trade Area (see **Section 15.2**)
  - World Trade Organisation (see **Section 15.3**), and
  - World Bank (see **Section 15.4**)

15.2 Influence of Association of Southeast Asian Nations (ASEAN) on TNCs and States

- The Association of Southeast Asian Nations (ASEAN) was established on 8 August 1967 in Bangkok, Thailand, with the signing of the **ASEAN Declaration (Bangkok Declaration)** by the Founding Fathers of ASEAN: Indonesia, Malaysia, Philippines, Singapore and Thailand. Brunei Darussalam joined ASEAN on 7 January 1984, followed by Viet Nam on 28 July 1995, Lao PDR and Myanmar on 23 July 1997, and Cambodia on 30 April 1999, making up what is today the **ten Member States** of ASEAN.

- ASEAN operates at the macro-regional scale. A **macro-region** is a geopolitical subdivision that encompasses several traditionally or politically defined regions or countries.
- As we saw in **Lect 13**, states – like firms – are competitors in the global economy. But they are also – again like firms – often *collaborators*: involved in trade agreements with other states.
- One way that states collaborate with each other is by forming regional MIs, like **ASEAN**.
- Regional MIs like ASEAN have become a pervasive feature of the global economy. At least one-third of total world trade occurs within such agreements. These have a two-sided quality: they liberalise trade between members while, at the same time, discriminating against third parties.
- There has been an especially marked acceleration in formation of regional organisations since the early 1990s (see **Fig. 1**).

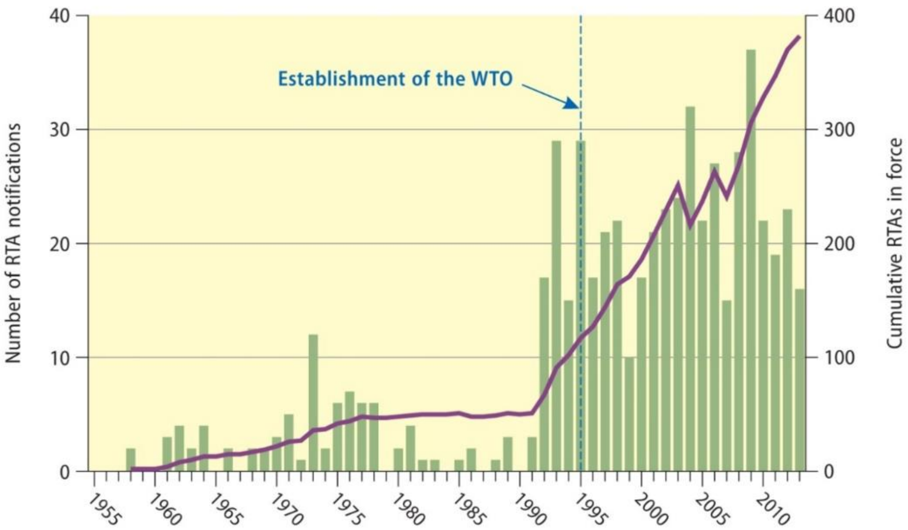


Fig. 1 The Acceleration in Trade or Regional Bloc Formation

- Although no regional MIs has yet adopted rules contrary to those of the WTO, there are some concerns about the impact of regional MIs on states and TNCs:
  - Regional MIs can <u>divert trade</u>, inducing a country to import from a country rather than from a cheaper supplier elsewhere;
    - There is a growing consensus that regional multilateralism is an important force that shapes the global economy. The EU, NAFTA and ASEAN+ (associated arrangements with other countries) triad of regional trading arrangements dominate the world economy, accounting for about 70% of all world trade.
  - Regional MIsmight <u>raise barriers against each other</u>, creating protectionist blocks;
  - Regional trade rules may <u>complicate the establishment of new global regulations</u>.
  - In addition, regional MIs have a **major influence on flows on investment by TNCs**. The removal of internal trade (and other) barriers may lead firms to realign their organisational structures and value-adding activities to reflect a regional rather than a strictly national market. This, by definition, 'diverts' investment from some location in favour of others.

- ASEAN'S **aims** are to:
  - **Accelerate economic growth, social progress and cultural development** in the region**.**
  - **Promote peace and stability** in the region.
  - **Promote mutual assistance and active collaboration** based on common interest in various fields such as economic, social, and cultural.
  - **Provide assistance** to each other in areas such as research in education.
  - **Collaborate** effectively to facilitate continuous growth in the agriculture, industry, and trade sectors to increase the standards of living for ASEAN people.
  - Promote Southeast Asian studies**.**
  - **Maintain** close and beneficial cooperation with existing international and regional organisations.
- The leaders of ASEAN view it as a community with enhanced capacity and capabilities to both respond effectively to challenges and to seize opportunities. To achieve the aims of ASEAN, ASEAN's operations are divided into three communities; political-security, economic and socio-cultural. In line with the syllabus, we will examine the **ASEAN Economic Community** in detail.

15.2.1 The ASEAN Economic Community (AEC)

(a) Background

- The AEC is the realization of the region's end goal of economic integration. It envisions ASEAN as a single market and product base, a highly competitive region, with equitable economic development, and fully integrated into the global economy.
- The history of AEC can be traced back as far as 1992 when the ASEAN Leaders mandated the creation of the ASEAN Free Trade Area (AFTA). Since then, efforts were intensified to broaden the region's economic potentials.
- The adoption of ASEAN Vision 2020 by the Leaders in 1997 has further envisaged ASEAN as a highly competitive region with free flow of goods, services, investments, a freer flow of capital, equitable economic development and reduced poverty and socio-economic disparities.
- The AEC Blueprint 2015 was adopted in 2007 as a coherent master plan guiding the establishment of the AEC in 2015. Immediately after that, a new AEC Blueprint 2025 was developed to set the strategic directions for the next phase of ASEAN's economic integration agenda. The AEC Blueprint 2025 is envisaged to further deepen economic integration and achieve a more integrated economic community with the following characteristics:
  - **A Highly Integrated and Cohesive Economy**: The ASEAN Economic Community envisions ASEAN as a single market and production base. Free flow of goods, services, investments, capital, and labor will allow the development of production networks in the region and enhance ASEAN's capacity as the global supply chain.
  - **A Competitive, Innovative and Dynamic ASEAN**

- The goal of ASEAN economic integration is to create a stable, prosperous, and highly competitive economic region. Three core elements under the competitive region are:
  - Competition policy
  - Consumer Protection
  - Intellectual Property Rights (IPR)
- ASEAN Member States are committed to introduce nation-wide competition policies and laws (CPL) to ensure a level playing field and incubate a culture of fair business competition to enhance regional economic performance.

- **Enhanced Connectivity and Sectoral Cooperation**: Regional economic integration under the AEC necessarily demands greater connectivity between ASEAN Member States as well as within the countries. Transport, ICT, energy connectivity and tourism are key elements of physical and people-to-people connectivity in the region. Additionally, other sectors such as agriculture, forestry, fisheries, science and technology all play an important and complementary role to achieve an integrated market under the AEC.
- **A Resilient, Inclusive, People Oriented and People-Centered ASEAN**: Key initiatives in the development of a resilient and inclusive ASEAN focus on the development of micro, small and medium enterprises (MSMEs) and promotion of ASEAN integration among the developing members of ASEAN. These initiatives move towards bridging the development divide both at the SME level and enhance economic integration of Cambodia, Lao PDR, Myanmar, and Vietnam to enable all Member States to move forward in a unified manner. All of which will enhance ASEAN's competitiveness as a region as well as to ensure the benefits of the integration process for all. The ASEAN Economic Community also supports private sector engagement by facilitating work with ASEAN Business Advisory Council and other business councils in the region.
- **A Global ASEAN:** ASEAN operates in an increasingly inter-connected and highly networked global environment, with interdependent markets and globalized industries. Establishing ASEAN as a dynamic region with businesses that can compete internationally means looking beyond the border of ASEAN Economic Community (AEC). Through **Free Trade Agreements (FTA)** and **Closer Economic Partnership (CEP)** as well as enhanced participation in global supply networks, ASEAN is both integrating into the global economy as well as enhancing the attractiveness of its internal market for foreign investment.

(b) Influence of ASEAN on TNCs

- The benefits to importers illustrate the impact that AEC could have on TNCs (see **Fig. 2)**.

TOPICS	FACTS	BENEFITS TO IMPORTERS
Goods Coverage	Tariff reduction/ elimination for 98% of all tariff lines	Tariff-free importing for most products
Tariff Elimination Schedule	Gradual tariff reduction/ elimination started in 1993 ASEAN-6 countries will eliminate all tariffs for products in Schedule A by 2010 CLMV will eliminate all tariffs for products in Schedule A by 2015, with flexibility up to 2018	Almost all imports from Singapore into Brunei, Indonesia, Malaysia, Philippines and Thailand will be duty-free by 2010 Almost all imports from Singapore into Cambodia, Lao PDR, Myanmar and Vietnam should be duty-free by 2015
Rules of Origin	40% local/ regional value-add required, based on FOB price, or change in tariff heading (4-digit level); or Product-specific rules may apply	Access to a wide range of products eligible for preferential tariff treatment
Mutual Recognition Agreements	Concluded MRAs: • cosmetic products • electrical and electronic equipment • pharmaceutical products	Avoids duplication of testing Reduces the cost to importers Cuts down the time to market
Customs Procedures	ASEAN members have committed to improving customs clearance of goods through: • green lane system for products under ATIGA • adoption of WTO agreement on customs valuation • service commitment • single-window approach (including electronic processing of trade documents) • Back-to-back certificate of origin • Third Party Invoicing	Time and cost savings Standardisation of procedures (less complicated)

Fig. 2 AEC at a Glance

- The **AEC has influenced TNCs in their locational decisions**. 2019 and 2020 were exceptional for ASEAN in terms of foreign direct investment (FDI): 2019 saw the region's highest-ever inflows, at $182 billion – making ASEAN the largest recipient of FDI in the developing world.
- 2020 saw the unprecedented impact of the COVID-19 pandemic, with a 25% fall in FDI, to $137 billion (see **Fig. 5**). The decline followed lockdown measures, supply chain disruptions, falling corporate earnings, successive waves of the pandemic, economic uncertainty and postponement of investment by TNCs.
    - Investment activity in the region shrank across all types. Announced greenfield investment declined by 17% to $68 billion, international project finance fell by 21% to $53 billion, and cross-border mergers and acquisitions (M&As) recorded a precipitous dive from $9.8 billion in 2019 to -$4.7 billion.
- Despite the decline, ASEAN remained an attractive investment destination; the region's share of global FDI rose from 11.9% in 2019 to 13.7%. FDI inflows remained more than twice the amount seen during the 2007–2008 global financial crisis and nearly five times more than the annual average during the 2002–2004 outbreak of SARS (severe acute respiratory syndrome) (see **Fig. 3**).

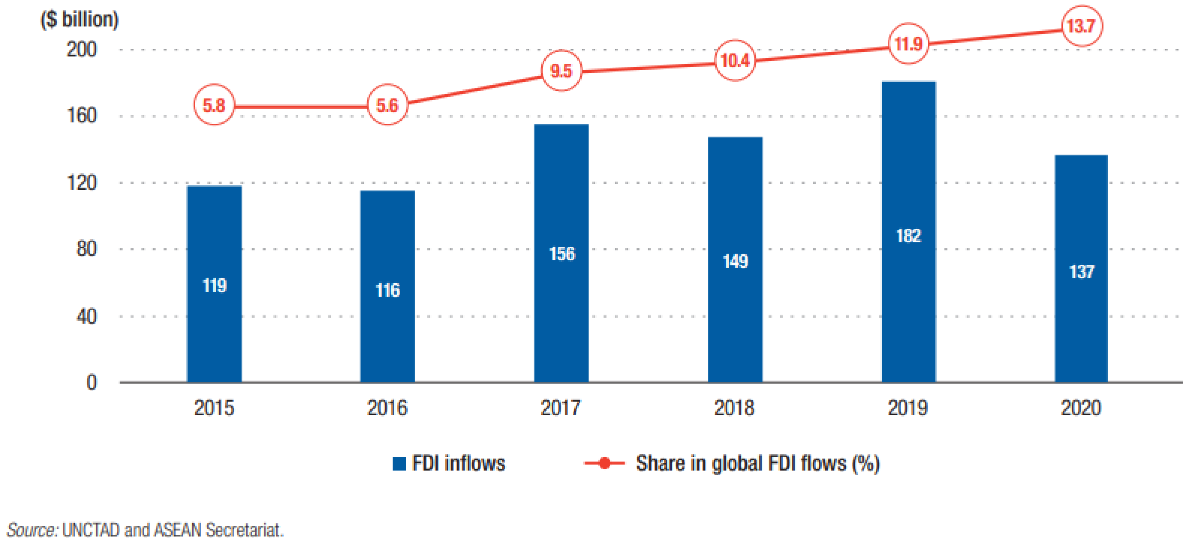


Fig. 3 FDI Inflows into ASEAN and Share in World Total, 2015 to 2020 (Billions of Dollars and Per Cent)

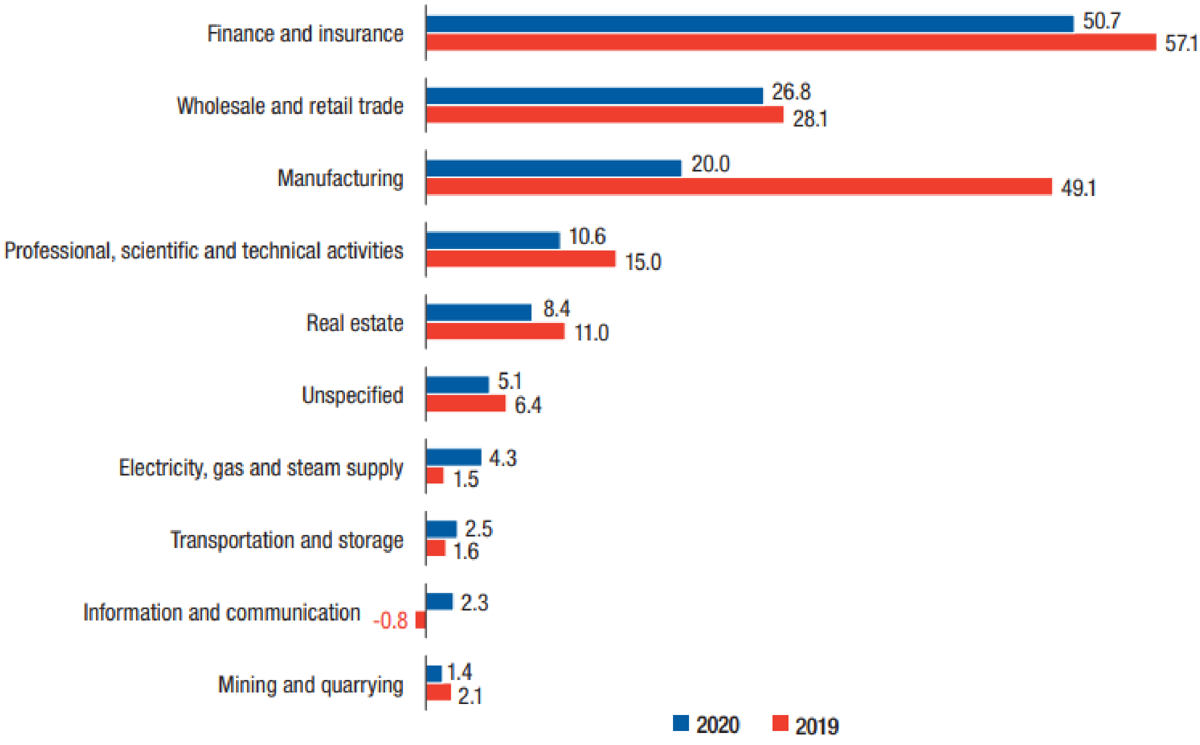
- Apart from the attraction of a large market, some TNCs choose to locate in ASEAN to reduce the cost of production, circumvent trade tensions or to diversify their supply chains (see **Table 1**).

Company	Nationality	Industry/activity	Host Country	Year	Remarks
Foxconn	Taiwan Province of China	Electric Components	Vietnam	2020	Major supplier of Apple; moved manufacturing of some iPads and Macbooks from China to mitigate the risk of the trade tensions
Irobot	United States	Home and office electronic products	Malaysia	2019	Diversifying supply chain

Table 1 Diversification of Production from China to ASEAN due to United-States-China Trade Tensions and Other Reasons (Selected Cases)

(Source: ASEAN Investment Report 2020–2021 – Investing in Industry 4.0)

- The top 10 industry recipients accounted for 95% of FDI in 2019 and 2020, with the traditional top 3 (finance, wholesale and retail, and manufacturing) accounting for more than 70 per cent (see **Fig. 4**). This shows **the types of TNCs whose locational decisions have been influenced by AFTA**.



Source: ASEAN Secretariat, ASEAN FDI database.

Fig. 4 Top 10 Industry FDI Recipients, 2019 and 2020 (Billions of Dollars)

- A few ASEAN Member States tend to attract investment in regional headquarters. In 2019–2020, Kargo Global and iiPay (both United States), Total Group (France), Deutsche Messe (Germany), Mitsubishi Chemical and Mitsui Knowledge Industry (both Japan) opened regional headquarters in **Singapore** to coordinate their Asia-Pacific and ASEAN operations. In **Malaysia**, OPPO (China) established its fourth regional operations centre in 2019 to support its regional expansion. In 2020, Volvo (Sweden) launched a $32 million warehouse in **Thailand** as a one-stop hub in ASEAN and Yamaha Motors (Japan) opened an office to serve as its regional headquarters to strengthen the robotics business in the region (e.g. semiconductor manufacturing equipment and industrial robots).
- TNCs tend to adopt transnational production strategies that tap the complementarity in resource endowments among countries in the region, i.e., based on the strengths of different countries. For example, BMW's IT Technology Office is in Singapore while it maintains production plants in Thailand, Indonesia and Vietnam (see **Fig. 5)**.

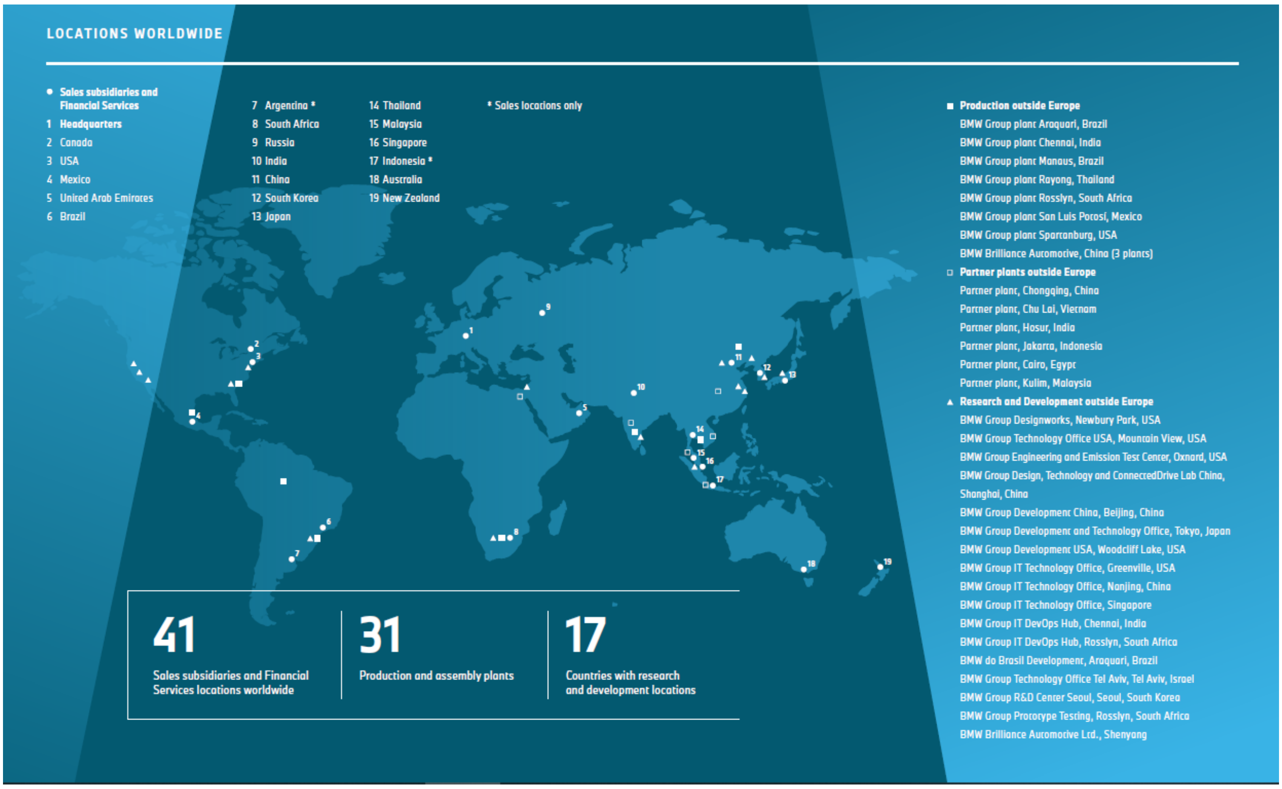


Fig. 5 BMW's GPN

(c) Influence of ASEAN on States

- Overall, the AEC encourages higher market competition. The export and investment sectors will generate higher potential in the long term.
- The AEC will help ASEAN countries' products gain access to a regional market that incorporates many substantial advantages:
  - a population of more than 600 million (i.e. larger than the EU or North America; next to China and India, ASEAN has the world's third largest labour force that remains relatively young),
  - $2.4 trillion gross domestic product (seventh largest in the world in 2013),
  - huge international trade (with total merchandise exports of over $1.2 trillion a year, nearly 54% of total ASEAN GDP and 7% of global exports), and
  - The group of Indonesia, Malaysia, the Philippines, Singapore, and Thailand collectively attracted more foreign direct investment than China ($128 billion versus $117 billion) in 2013
- The elimination of tariff and non-tariff barriers has also **facilitated trade in goods** between the countries involved.
  - As a result, trade among ASEAN countries has grown from US $ 44.2 billion in 1993 to US $ 73.4 billion in 1998, representing an average increase of 13.2%. Before the financial and economic crisis struck in mid-1997, intra-ASEAN exports had been increasing by 29.6%. This is significantly higher than the rate of increase of total ASEAN exports at 18.8%.

- But the advent of the financial and economic crisis (i.e. 1997 Asian Financial Crisis) has adversely affected intra-regional trade more than trade with the rest of the world. Intra-ASEAN trade contracted by 15.9% in 1998 compared to the 5.8% reduction in total ASEAN exports. This trade decline suggests that economic integration/interdependence can also heighten economic vulnerability of member states.

- But member states of ASEAN have been said to **benefit unequally** from this economic arrangement (see **Fig. 6**).

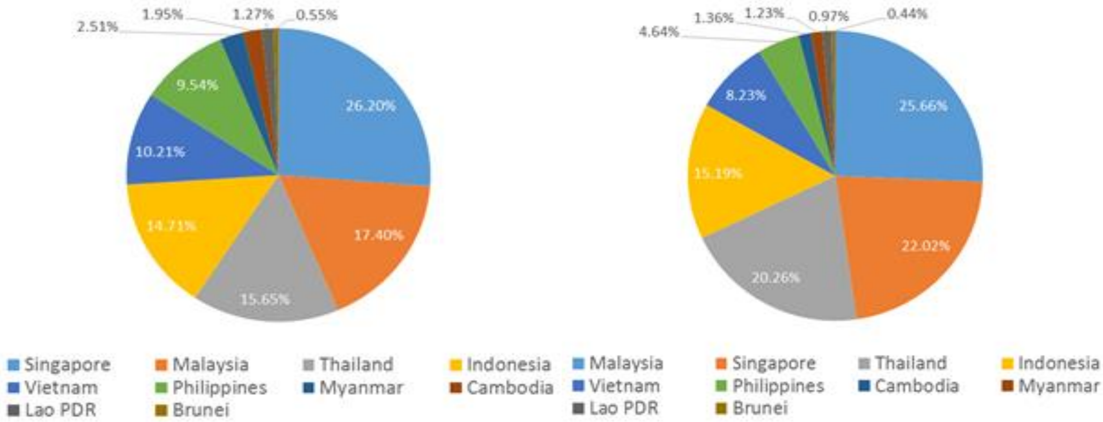


Fig. 6 Intra ASEAN import value share (left) and export value share (right) in 2016

- Today, intra-ASEAN trade is mainly driven by Indonesia, Malaysia, Thailand and Singapore. These four countries' combined export share and import share of intra-ASEAN trade were 83.1% and 74.0% respectively in 2016.

- Within these four countries, Malaysia exported the most to other ASEAN countries in 2016 at USD 60.5 billion or 25.7% of total intra-ASEAN export. On the importing side, Singapore imported the most from other ASEAN members in 2016 at nearly USD 71.0 billion or 26.2% of total intra-ASEAN import value.

- ASEAN's combined population size has provided a large consumer market for Malaysia to fuel export-oriented growth.

- While ASEAN as a regional hinterland has allowed resource-scarce Singapore to take advantage of geographical differences - obtaining resources at a cheap cost.

- However, it must be recognised that the dominance of these four countries is on the decline as other members including Laos and Myanmar have more recently opened their economies to participate more actively in regional and global trade activities.

- Within AFTA, TNCs may also **<u>re</u>organise** their GPN to reduce their cost of production. Since the 2010s, within ASEAN, TNCs have relocated from higher-cost Member States to Cambodia, Lao, Myanmar and Vietnam.

- Given the large number of ASEAN members and the different types and volumes of FDI inflows that each member attracts, it is worthwhile to examine the case of specific member countries – the Philippines (see **Box 1**) and Indonesia (see **Box 2**).

<u>Box 1</u>: The Impacts of AFTA on the Philippines

A publication by the Southeast Asian Council for Food Security and Fair Trade (SEACON) in the early 2000s revealed the following in its research on AFTA's impacts on the Philippine economy and small-scale producers:

1. Using ASEAN import-export figures from 1993 to 2001, the share of the ASEAN market in the Philippines' total exports more than doubled from seven to 15.7 percent. Despite the significant growth, the Philippines still registered PhP 6,528,213.30 in losses from the intra-ASEAN trade transactions within the same period.

2. The business sector reported in July 2004, that the impacts of AFTA from 1993 was truly lamentable. That Philippine industries suffered from more competitive imports from ASEAN and from other Asian countries, particularly China, Taiwan and South Korea. The business sector reported closing down or the cutting of outputs because of cheaper or better imports from ASEAN and other markets:
   - Industries severely injured include the appliance industry; shoe industry; car battery industry; car parts industry; chemicals industry; plastic industry; textile industry; match industry, aluminium industry; rubber industry; cordage industry; tire industry; steel industry; pulp and paper industry; cement industry; ceramic tile industry, among others.
   - As to agriculture, most affected industries include the following: garlic; onion; sugar; fruit; corn; potato; coffee; vegetable; wood industry. By the mid-1990s the country had turned from a net agricultural exporter to a net importer.

3. In the local research, the following situation describes the Filipino farmers and fishers during AFTA implementation:
   a. The situation of small Filipino rice and corn farmers have not improved.
   Tenancy, monocropping and chemical intensive farming, high cost of production, high post-harvest losses, low income levels. This indicates that Philippine rice and corn is not competitive to world markets. Backward fishing modes also describes the marginal fishers especially in comparison to commercial fishing vessels
   b. Although rice is not yet in the Inclusion List, and that tariff rate is still high at 50% but nevertheless, Philippine rice is still not competitive. What tragedy shall befall the Philippine rice industry and the millions of rice farmers once the rice market is fully liberalized!

4. A thorough evaluation at the local, national and regional levels would reveal that AFTA's scheme of the lowering of tariffs, removal of trade barriers contributed to Philippine agriculture and industries suffering massive and crushing defeat in the hands of the stronger ASEAN and global economies.

***Box 2*: The Impacts of AFTA on Indonesia**

- The purpose of AFTA is to help products produced within ASEAN compete in the global market, attract more Foreign Direct Investment to the region, and increase intra-ASEAN trade.
- According to Indonesia's Center of State Revenue Policy – Fiscal Policy Agency, there are several benefits of AFTA for Indonesia, that is,
  - greater and wider market opportunity for Indonesian products,
  - lower production costs for Indonesian businesses that require capital goods and raw/auxiliary materials from other ASEAN member countries,
  - more diverse product options in the domestic market for consumers, and
  - greater opportunity to enter into alliances with business actors from other ASEAN member countries
- The more specific impacts of AFTA on selected industries in Indonesia are described below.

(i) Trade

- ***Export***

It is argued that economic integration has largely benefitted Indonesia considering the number of transnational companies like Unilever relocating their factories to Indonesia for the reason of cheaper labour costs. Transnational companies like Unilever can export goods to ASEAN countries, which in turn will increase the value of Indonesia's exports.

- ***Import***

Indonesia, through its Ministry of Finance, has implemented its AFTA commitment by imposing certain tariff rates on imported goods based on the ASEAN Trade in Goods Agreement. Most of the tariffs on the goods are 0%, except for cane or beet sugar and chemically pure sucrose, in solid form.

(ii) Financial Sector (Banking, Insurance, and Investment)

Indonesia's banking sector had to gear up to compete with banks in other ASEAN countries. AFTA requires the Indonesian banking sector to step up efforts to compete with other banks in the region. One issue concerns interest rates on loans employed by Singaporean, Malaysian, and Thai banks, which are lower than those of Indonesian banks.

With the implementation of AFTA, the Indonesian banking sector have more responsibility in helping small and medium enterprises. Bank Indonesia, the central bank, had drawn up four main policies when preparing for AFTA, i.e., improving banking system durability, increasing banking intermediation, increasing the role of Shariah banking, and increasing the role of rural banks in providing micro- financing.

For the insurance sector, more foreign insurance companies, especially from ASEAN countries, entered Indonesia. The consequences with the implementation of AFTA are:

1. An influx of foreign capital and technical skills;
2. Globalisation may accelerate product innovation and marketing diversification;
3. The presence of new capital will increase competition in the domestic market; and
4. Globalisation will open opportunities for insurance companies to go international.

In the investment sector, AFTA, as a free-trade system in Southeast Asia, results in an interdependency and integration of investment and will impact investment and economic management, including in Indonesia, by making trade free of tariff and non-tariff barriers; meaning that goods produced by ASEAN countries are free to enter each ASEAN member country.

This was not the case before AFTA, as foreign investment in Indonesia is regulated and limited under Indonesia's Negative Investment List. Loosening of this regulation was necessary to accommodate ASEAN economic integration to allow the free flow of investment.

(iii) Agriculture

The implementation of AFTA affected the export and import of Indonesian agricultural commodities. The net export of Indonesian agricultural products has increased since the implementation of AFTA in 2003. It might be advisable for

Indonesia to focus on the production and export of rice, corn and soybeans, commodities for which it has the advantage of plentiful land and low production costs. Indonesia was the top rice-producing country in ASEAN from 1990 to 2008. (According to the theory of comparative advantage, countries with low production costs may want to specialise in a few products and increase their exports of these products. Countries can import those goods for which high production costs mean it does not make economic sense to produce the goods domestically.)

(iv) Construction and Infrastructure

In a report prepared by the ASEAN Constructors Federation (ACF), ASEAN countries in general are seen experiencing robust growth in the construction industry. Indonesia had the largest construction industry among ACF member countries in 2002, valued at US$9.92 billion. The adoption of AFTA benefits the region in terms of better procurement of construction materials, allowing the materials to move through the region more freely than before. The abundance of land outside Java that remains undeveloped makes Indonesia an attractive destination for foreign investment.

Further, the need for infrastructure development and cheaper land present a tempting opportunity for foreigners entering the Indonesian construction industry. Expansion of infrastructure, particularly the construction of highways, also provides opportunities to contractors from ACF member countries. In addition, the Indonesian government has worked to open up its market to foreign firms to form joint ventures with local construction firms for such projects. These foreign firms are issued a three-year construction license.

With AFTA, the reduction in import duties could facilitate the expansion of the regional steel market, lowering the price of steel products and enhancing the pace of construction projects.

(v) Manufacturing

While AFTA promotes the liberalisation of trade, for Indonesia, which has adhered to its commitments, some manufacturing sectors faced difficulties as a result of AFTA implementation. One of the biggest and most prominent regards the impact on workers.

Most manufacturing sectors in Indonesia still use less advanced technology and are labour intensive. This is to say that many manufacturing sectors in Indonesia, particularly textiles and wood products, depend on low-cost labour. The implementation of AFTA requires manufacturers to ensure the sustainability of their businesses by moving away from low-cost labour and improving the quality of their goods or finding some other advantage. This will allow Indonesian products to stand alongside products from other ASEAN countries.

(vi) Labour

In an ILO/ASEAN Joint Study on the Social Implications of AFTA on Labour and Employment, free trade is seen leading to greater efficiency and cheaper products. The idea is that removing trade barriers would bring huge benefits to the people of ASEAN, lead to greater specialisation and division of labour as each country concentrates on producing goods and services in which it has a competitive advantage.

On the downside, however, the greater levels of competition unleashed by AFTA will lead to the collapse of inefficient companies that have been operating behind protectionist barriers. Therefore, for countries, the key to taking advantage of trade liberalisation is very much determined by the competitiveness, or quality, of its labour force.

Unfortunately, a low-quality labour force is still a problem for Indonesia. This is reflected by the relative lack of education of Indonesian workers compared to other Asian countries. This hinders the process of industrial transformation that would otherwise take place at a faster pace due to trade liberalisation, because workers are not flexible enough to change jobs and move into more advanced sectors. Indonesia also has a relatively high unemployment rate, which will prevent it from reaping the full benefits of trade liberalisation. As the economy opens up, Indonesian workers could find it difficult to compete with workers from neighbouring countries.

Conclusion

There are positive and negative impacts from the implementation of AFTA in Indonesia. While businesses benefitted from the highly competitive market as a venue to expand their production and networks, small enterprises and poorly educated labourers may have found it difficult to compete with the free flow of goods, services, and skilled workers. The Indonesian government will have to continue playing a pivotal role in reconciling this gap.

15.3 The Influence of the World Trade Organisation (WTO) on TNCs and States

(a) Background of WTO

- Trade is the most vital element in the growth of the global economy. However, as we have learnt in **Lect 13**, states have the power, for various reasons, to put up obstacles such as tariffs (see **Section 13.2.2**) that might impede trade.
- In 1947 a group of 23 nations agreed to reduce tariffs on each other's exports under the General Agreement on Tariffs and Trade (GATT). Since the GATT was established, there have been nine 'rounds' of global trade talks. The most recent, the Doha (Qatar) round, began in 2001. A total of 142 member countries were represented at the talks of Doha. Its aim was to achieve major reform of the international trading system through the introduction of **lowered trade barriers** and **revised trade rules**.
- The most recent important development has been the creation of the **World Trade Organisation (WTO)** in 1995. Unlike its predecessor, the loosely organised GATT, the WTO was set up as a permanent organisation with far greater powers **to arbitrate trade disputes**.

(b) Key functions

- The WTO hence exists **to promote and regulate global trade**. The majority of world trade takes place according to **a set of rules administered by the WTO**. These rules are binding on members (see **Fig. 7**) and the WTO has a dispute settlement body to enforce these rules and principles.
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(c) WTO's Benefits to States

- Currently, the WTO has 164 members, accounting for 98% of world trade. A total of 22 countries are negotiating membership.

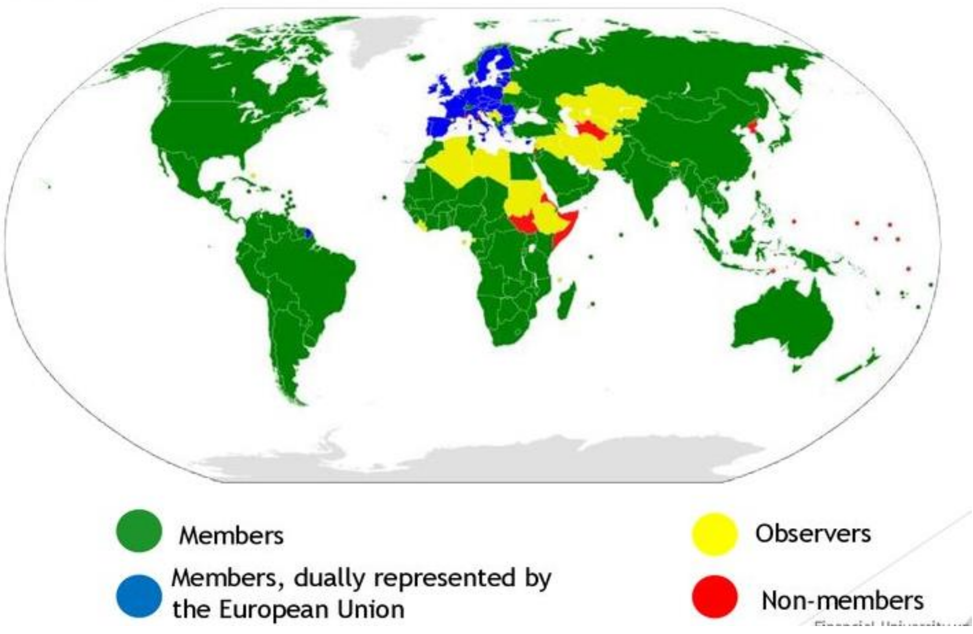

Fig. 7 Members and Observers of the WTO

- According to the WTO, the benefits of its work can be categorised as follows.

Main Benefits	**Explanation**
1. Minimise trade disagreements	• The system contributes to assurance and stability, and therein international peace. Decisions in WTO are typically taken by **consensus** among members and they are ratified by members' parliaments. This allows for a more prosperous and peaceful global economy. • The agreements that are negotiated and signed by the member states are legal foundations for global trade. o Essentially, they are contracts, guaranteeing WTO members important trade rights. o They also bind governments to keep their trade policies transparent and predictable which is to everybody's benefit. These agreements provide a stable and transparent framework to help producers of goods and services, exporters and importers conduct their business. o The WTO cannot claim to make all countries equal. But it does reduce some inequalities, giving smaller countries more voice, and at the same time freeing the major powers from the complexity of having to negotiate trade agreements with each of their numerous trading partners.
2. Disputes are handled constructively	• As trade expands in volume, in the number of products traded, and in the numbers of countries and companies trading, there is a greater chance that disputes will arise. • Trade frictions are channelled into the WTO's dispute settlement process, where the focus on interpreting agreements and commitments and how to ensure that members' trade policies conform with them. That way, the risk of disputes spilling over into political or military conflict is reduced. The WTO system helps resolve these disputes peacefully and constructively.
3. Stimulates economic growth and addresses poverty	• Trade clearly has the potential to create jobs. In practice there is often factual evidence that lower trade barriers have been good for employment. • A WTO Committee on Trade and Development looks at developing economies' special needs. Its responsibility includes implementation of the WTO agreements, technical cooperation, and the increased participation of developing economies in the global trading system. • But the picture is complicated by several factors. Nevertheless, the alternative — protectionism — is not the way to tackle employment problems. • Lowering trade barriers allows trade to increase, which adds to incomes — national incomes and personal incomes. • The WTO global system reduce trade barriers through negotiation and applies the principle of non-discrimination. Results are lower costs of production (because imports in production are cheaper) and reduced prices of finished goods and services, and ultimately a lower cost of living.
4. Provides more choice of products and qualities	• Think of all the things we can now have because we can import them: fruits and vegetables out of season, foods, clothing and other products that used to be considered exotic, cut flowers from any part of the world, all sorts of household goods, books, music, movies, and so on.

5. Good governance is encouraged	• Under WTO rules, once a commitment has been made to liberalise a sector of trade, it is difficult to reverse. • The rules also discourage a range of unwise policies. For instance, protectionism is generally, unwise because of the damage it causes domestically and internationally. For businesses, that means greater certainty and clarity about trading conditions. For governments it can often mean good discipline.

Table 2 The Benefits of WTO, according to WTO

- Although agreements have been difficult to broker at times, the overall success of GATT/WTO is undeniable: today average tariffs are only a tenth of what they were when GATT came into force and world trade has been increasing at a much faster rate than GDP. In addition, the average share of exports and imports of goods and commercial services in world GDP increased significantly by 10% from 1995 to 2014.
- Furthermore, over the 1985-2000 period, global inequality as measured by the Gini coefficient seems to have declined significantly (see **Fig. 8**). The main reason has been the rise in living standards in China (See **Box 1**) and India. But what about the poor countries of Africa and elsewhere in the world? In fact, the WTO faces several more criticisms (see **part (d)** below)

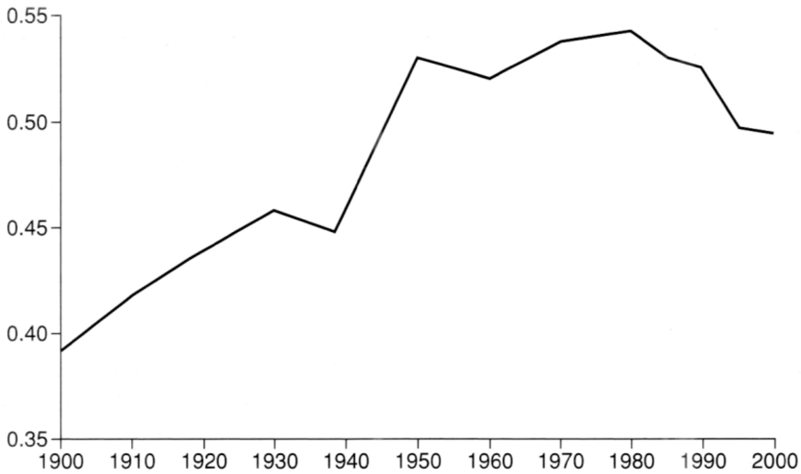

Fig. 8
Gini Coefficients of Worldwide Income Distribution

Box 3: China Joins the WTO
Extract from GeoFile Online 463, published in ***2004***

The most significant recent event in the history of the WTO has been China's entry into the organisation, in October 2001. For the DCs in particular the main benefits of Chinese entry are:

- Its huge market potential. For example, car sales are taking off, exceeding 1 million in 2002 for the first time. China is now VW's biggest market outside Germany. China now imports more from the rest of Asia than does Japan. As WTO membership opens China's markets to competition, its importance as a source of demand will grow.
- That China would be bound by WTO rules on a range of issues concerning production and trade. Before WTO membership, many countries were concerned that China was 'breaking the rules' in various ways.
- Before WTO membership, TNCs were not allowed to set up wholesale, retail, distribution and after-sales networks. The changes brought about in 2001 explain why Wal-Mart, the US supermarket chain, has invested heavily in China over the last two years in copying its American model in another vast market.

The main concerns *for* China in the WTO are the problems caused by the new rules that China had signed up to as the country struggled to identify and specialise in fields of comparative advantage. In 1999 the World Bank estimated that up to a third of the 140 million workers employed in China's state-owned industries, many of which were considered to be very inefficient, may be surplus to requirements.

Foreign direct investment
China attracted a record $52.7 billion in foreign direct investment in 2002, taking over from the USA as the world's biggest net recipient of FDI. The Chinese government expects to attract about $100 billion in FDI a year between 2006 and 2010. The major attraction to manufacturers is the cheap labour market where wages are less than 5% of those in the USA.

Infrastructural improvements
Such a high rate of economic growth has demanded equally rapid improvements in infrastructure. China's rail network is expanding rapidly. A $24 billion high-speed rail link between Beijing and Guangzhou is being planned which would reduce train travel time between the two cities from 23 hours to 10. A multitude of new road schemes have either been completed or are in progress. The Three Gorges Dam on the Yangtze River is the most spectacular feature of China's changing infrastructure.

(d) WTO's Drawbacks for States

Favoring DCs, Being Unfair to LDCs

- Most critics of free trade accept that it does generate wealth but they **deny that all countries benefit from it**.
  - For example, The Fairtrade Foundation revealed in 2010 how the $47bn in subsidies paid to rich-country producers in the previous 10 years has created barriers for the 15 million cotton farmers across west Africa trying to trade their way out of poverty, and how 5 million of world's poorest farming families have been forced out of business and into deeper poverty because of those subsidies.
- On the persistent poverty seen in several African countries, supporters of the WTO say that it is scarcely credible to argue that this is the result of globalisation since they are all outside the mainstream of free trade and economic globalisation. However, critics say that the WTO and other international organisations should be paying more attention to the needs of the countries, making it easier for them to become more involved in, and gain tangible benefits from, the global economic system.
- Critics also ask why it is that DCs have been given decades to adjust their economies to imports of textiles and agricultural products from LDCs, when the latter are pressurised to open their borders immediately to banks, telecommunications companies and other components of the service sector in DCs. The removal of tariffs can have a significant impact on a nation's domestic industries. For example, India has been very concerned about the impact of opening its markets to foreign imports (see **Box 4**).

Box 4: India – The impact of the removal of agricultural tariffs

In the late 1990s, since India was forced by a WTO ruling to accelerate the opening up of its markets, food imports have quadrupled. Large volumes of cheap, subsidised imports have flooded in from countries such as the USA, Malaysia and Thailand. The adverse impact has been considerable and includes the following:

- Prices and rural incomes have fallen sharply. The price paid for coconuts has dropped 80%, for coffee 60% and pepper 45%.
- Foreign imports, mainly subsidised soya and palm oil from Malaysia, have undercut local producers and have virtually wiped out the production of edible oil.

Farmers, trade unionists and many others are against these trends, or at least the speed at which they are taking place. They are calling for the reintroduction of import controls, thus challenging the basic principle of the globalisation process – the lowering of trade barriers.

Protectionism still exists

- While WTO claims to promote free trade, in some areas **protectionism** is still an issue, particularly in the sectors of clothing, textiles and agriculture.
- In principle, every nation has an equal vote in the WTO. ***In practice, the rich world shuts out the poor world from key negotiations***. The WTO has failed to curb the speedy increase in the number of protectionist measures. In recent years, agreements have become more and more difficult to reach, with some economists forecasting the stagnation or even the break-up of the WTO. In fact, many LDCs have criticised the WTO for being too heavily influenced by the interests of the USA and the EU.
- This has to do with the difference in representation in WTO missions in Geneva.
  - While 65 developing countries maintain WTO missions in Geneva, 26 continue to be represented by missions or embassies elsewhere in Europe, and 7 more list as their representatives people located in their own capitals. In 2000, 24 countries had no permanent presence in Geneva.
  - These countries cannot object to the so-called consensus that various bodies of the WTO arrive at in their everyday workings.
  - Even among the countries that enjoy diplomatic representation in Geneva, the size of their delegations is small. The average size of the developed country delegation is 7.38 delegates per country. In contrast, the average size of the developing country delegation is 3.51.
  - This can be a major problem in an MI like the WTO where there are about 1200 events through the year, often resulting in overlaps of meetings. Many developing countries find it difficult to attend the meetings of the WTO, especially if they must also cover all the other international organisations in Geneva with the same small delegation.
  - The difference in representation between the developed and developing countries works to greatly disadvantage the latter.
  - To make things worse, if a country wishes to reject a proposal, it must do so openly and clearly in front of other members present. Many developing countries point out that they often fear the consequences of expressing their objections publicly, and hence choose the alternative option of remaining silent.
  - As the absence of objection is seen as consensus, developing countries end up giving in to decisions that they have problems with.

An outdated agenda

- Critics have pointed that the WTO continues to pursue what is essentially a 20th century agenda. The WTO was set up at a time when the trade system was primarily selling already-made goods. But the nature of global trade has changed.

- Most trade today is not about making goods in one nation and selling them to consumers in other nations. About 70 per cent of global trade is now in intermediate and capital goods and services, through supply chains.
  - The iPhone is a classic example. It is designed in California and assembled in China, but its components come from more than 200 suppliers from all over the world. Thousands of products are "made in the world" in this way.
  - To operate efficiently and fairly, supply chains need quite different rules from those addressed by the WTO.
- Trade is now also not just about goods, but services as well. Services such as design, engineering, logistics, telecoms and finance play a vital role in supply chains, like the one needed to assembly an iPhone.
  - In the case of the iPhone, for example, the merchandise components account for less than one-third of the value of the final product. Most of the value is derived from services, such as research and development, design, software development, engineering and marketing. Apple's App store, which hugely enhances the value of the iPhone, is a service.
  - Barriers to cross-border movement of services are now barriers to trade. By not focusing on such issues, the WTO rules fail to address the realities of business.

Low priority given to the environment

- Critics have also argued that the **environmental impact** of a major increase in world food trade is also being felt around the world.
- For example, trade-related transportation is one of the fastest growing sources of greenhouse emissions. The distance food travels is expressed in terms of food miles. As well as distance, the mode of transport (e.g. air freight vs. sea freight) is also an equally important, but sometimes a forgotten variable.
  - Milk provides a useful example of unnecessary food trade facilitated by the WTO. Until the 1960s, most people consumed milk produced locally, but the WTO has facilitated an increase in milk exports, with many countries importing and exporting large quantities, resulting in millions of extra food miles.

(e) WTO's Impact on TNCs

Siding with TNCs

The WTO's decisions have sometimes also sided with TNCs. Bananas are crucial to the Caribbean economy. Half the population of the Caribbean rely on the banana industry to supply their basic needs such as food, shelter and education. Traditionally, the European Union (EU) has given preferential terms and treatment for banana imports from the Caribbean. This has protected banana farmers in the Caribbean from competition from Latin America, whose bananas are cheaper because they are grown on large-scale, mechanised plantations run by giant US-based transnational corporations (e.g. Dole. Chiquita).

The economic practice is supported by the Lomé Convention - an agreement created in the 1970s which commits the EU to promoting trade with its former colonies. The Lomé Convention has protected postcolonial developing countries, including those of the Caribbean islands, to the full force and impacts of the free market economy.

The 1990s "banana trade wars" is the culmination of a dispute between the US and the EU. The US government filed a complaint to WTO that EU's preferential terms for banana imports from the Caribbean has flouted free trade rules. It (the US government) was pressurized by powerful US-based transnational corporations, which control the Latin American banana crop. This happened even as a mere seven per cent of Europe's bananas came from the Caribbean in the 1990s.

In the end, US emerged victorious in the dispute. The EU was instructed subsequently to alter its economic rule.

15.4 Influence of the World Bank (WB) on TNCs and States

- The WB (an UN agency) was brought into being at a conference designed to plan a new economic structure for the post-war period, held at Bretton Woods, New Hampshire in 1944. The WB is based in Washington, DC.
- The initial role of the WB was to assist in the funding of reconstruction in the countries decimated by the war. The key features of the WB are shown in **Table 3**.

Features	**World Bank (WB)**
Objectives	Promote long-term economic development and poverty reduction by providing technical and financial support to help countries reform certain sectors or implement specific projects.
Functions	By giving out loans to reform certain sectors or implement specific projects – such as building schools and health centers, providing water and electricity, fighting disease etc.
Funding	Generally long-term and is funded by member country contributions and through bond issuance.
Specialisation	Staff are often specialists on particular issues (e.g. Climate Change mitigation), sectors E.g. Education, Social protection) or techniques.

Table 3 Key Features of the WB

15.4.1 The World Bank

(a) Role of the World Bank

- The WB borrows about USD 20 to 30 billion a year in a variety of currencies. This money has provided financing for more than 12,000 projects in more than 170 countries since 1947.
- When the reconstruction of Europe was complete (this was its initial purpose), the WB increasingly turned its attention to developing countries. In fact, the WB positions itself as **a vital source of financial and technical assistance to developing countries** around the world by partnering them to **reduce poverty and support development**. It comprises:

- *International Bank for Reconstruction and Development* (IBRD), which lends to governments of middle-income and creditworthy low-income countries.
- *International Development Association* (IDA), which lends only to nations with a very low per capita income. For such countries loans are interest free and allow long repayment periods.
- *International Finance Corportaion* (IFC), which offers investment, advisory, and asset-management services to encourage private-sector development in less developed countries.
- *Multilateral Investment Guarantee Agency* (MIGA), which offers political risk insurance and credit enhancement guarantees. These guarantees help investors protect foreign direct investments against political and non-commercial risks in developing countries.
- *International Centre for Settlement of Investment Disputes* (ICSID), which is an international arbitration institution established in 1966 for legal dispute resolution and conciliation between international investors and States.

- Some of the projects are co-financed with governments, other multilateral institutions, commercial banks, export credit agencies, and private sector investors.
- World Bank policies evolve along with main objectives of the era and more pertinent issues accordingly. For instance, in the 1970s, objective was to alleviate poverty whereas from the 1990s onwards, the World Bank began to promote sustainable development with most funding going to small-scale projects.
- The World Bank is responsible for offering development assistance to correct long-term issues. Like any other banks, the World Bank pursues profit and returns on its investments. But unlike commercial banks, however, the World Bank takes no financial risks since its loans are to governments, who will pay off their debts from their country's future revenue or through taking up new loans.
- Loans come with conditions of economic reforms thereby affecting states (see **15.4.1(c)**). These conditions often promote **neo-liberalism**, i.e., prioritising the private sector and favoring economic open-ness. Frequently, states are required to make the following changes in exchange for loan approval.

(b) Benefits of the World Bank to States

- The WB operates under their slogan "Working for a World Free of Poverty". **It gives particular attention to projects that can directly benefit the poorest people in developing countries.** The direct involvement of the poorest in economic activity is being promoted through lending for agriculture and rural development, small-scale enterprises, and urban development.
  - The WB is helping the poor to be more productive and to gain access to such necessities as safe water and waste-disposal facilities, health care, family-planning assistance, nutrition, education, and housing.
  - Within infrastructure projects there have also been changes. In transportation projects, greater attention is given to constructing farm-to-market roads. Rather than concentrating

exclusively on cities, power projects increasingly provide lighting and power for villages and small farms.

  - Industrial projects place greater emphasis on creating jobs in small enterprises. Labor-intensive construction is used where practical.
  - In addition to electric power, the WB is supporting development of oil, gas, coal, fuelwood, and biomass as alternative sources of energy.

- The WB provides most of its financial and technical assistance to developing countries by supporting specific projects. Although IBRD loans and IDA credits are made on different financial terms, the two institutions use the same standards in assessing the soundness of projects. The decision whether a project will receive IBRD or IDA financing depends on the economic condition of the country and not on the characteristics of the project. (See **Box 5** for an example of WB's efforts in improving education in Egypt, and **Box 6** for an example of WB's rejection of India's proposal for coal-related projects).
- In making loans to developing countries, the WB does not compete with other sources of finance. It assists only those projects for which the required capital is not available from other sources on reasonable terms. Through its work, the Bank seeks to strengthen the economies of borrowing nations so that they can graduate from reliance on Bank resources and meet their financial needs, on terms they can afford directly from conventional sources of capital.
- "Graduation" from the IBRD and IDA has occurred for many years. Of the 35 very poor countries that borrowed money from IDA during the earliest years, more than two dozens have made enough progress for them no longer to need IDA money, leaving that money available to other countries that joined the WB more recently. Similarly, about 20 countries that formerly borrowed money from the IBRD no longer have to do so. An outstanding example is Japan. For a period of 14 years, it borrowed from the IBRD. Now, the IBRD borrows large sums in Japan.

Box 5: Closing the human capital gap in Egypt

World Bank, Annual Report 2020

Middle East and North African (MENA) is facing a human capital gap. While there are many factors holding back the region's outcomes, employment, and productivity, chief among them are the poor learning outcomes. MENA's children are expected to receive 11.4 years of schooling by age 18 yet they only obtain 7.6 years of actual learning, with boys underperforming girls. Closing the learning gap is an urgent priority for the region.

Challenge

Investment in school facilities has not kept pace with the rapid increase in the number of students, resulting from high rates of population growth and rising enrolment rates. Overcrowding – with classes regularly containing between 40 and 50 children – and poor facilities do not create an environment conducive to learning. The teaching profession tends to also be associated with a low social and economic status. The notion is reinforced by the meagre salaries—rarely amounting to about US$281 a month—and the poor quality of training.

Solution

The $500 million *Supporting Egypt Education Reform Project* aims to improve teaching and learning conditions in schools. It is helping increase access to quality kindergarten education, enhance the capacity of teachers and education leaders, develop a reliable student assessment system, and expand the use of modern technology and digital learning resources in teaching and learning. The project's goal is to have 500,000 new students enrolled in kindergarten, with 50 percent from the poorest districts; teachers applying better practices; 2 million students benefiting from the new assessment system; and a reformed secondary school graduation system focused on building skills.

Meanwhile, IBRD provided additional financing of $500 million for a second phase of the *Strengthening Social Safety Nets Project*, which supports Egypt's national cash transfer program. This program is the largest cash transfer operation in the Middle East and North Africa and among Egypt's most significant investments in promoting human capital. It has reached over 3 million households to date, representing more than 8 million individuals, with over 67 percent of the cash directed to the poor and vulnerable and 74 percent of program cardholders being women. As part of these efforts, the Takaful program provides conditional, monthly family income support to protect poor households from the short-term negative impacts of economic reforms and shocks. It also encourages families to keep children in school and provides health care, including pre- and postnatal health services and the monitoring of children's growth. The complementary Karama program provides monthly unconditional cash assistance to poor elderly citizens, people with severe disabilities and diseases, and orphans. Under the latest round of financing, the government is also preparing an initiative that will help promote livelihoods and boost economic inclusion across eight governorates.

In March 2020, the Bank activated $8 million from the contingency emergency response component of this project to fund emergency response to the COVID-19 outbreak in Egypt, including implementation of a preventive plan to confront the pandemic. This comes in addition to a $50 million project that was launched under the Bank Group's Fast-Track Facility for COVID-19, which aims to strengthen the prevention, detection, and response to the pandemic.

Box 6: World Bank won't fund coal-related projects in India

The Economic Times, 31 July 2015

The World Bank has made a U-turn on its stance that coal is the backbone of the India's energy economy 17 years after it agreed to lend $1.03 billion to Coal India along with a Japanese lending agency. The international lender has now decided not to invest in any coal-related project, be it a coal mine or a thermal power plant.

"The World Bank Group will only in 'rare circumstances' provide financial support for new greenfield coal power generation projects; these 'rare circumstances' refer to considerations such as the country in question having no other feasible alternatives to meet the basic energy needs of its people," a World Bank spokesperson told ET.

Coal continues to fuel 70 per cent of India's power requirements. In 1998, World Bank and Japan Bank for International Cooperation (now part of Japan International Cooperation Agency) had agreed to lend $1.03 billion to Coal India for taking up 24 coal mining projects under its subsidiary Northern Coalfields, with global sourcing of equipment.

Coal India took $484.4 million loan between 1998 and 2004, which have since been repaid. At that time World Bank believed that indigenous coal will remain the most stable and least-cost option for the bulk of India's energy needs since the country's coal reserves are deemed large enough to meet its demand for 250 years, while its crude reserve can meet the country's energy requirement for only 15 years and that of natural gas for 18 years. While coal still remains the least costly energy option for India, the World Bank now believes coal is no cure for global poverty.

(c) Drawbacks of the World Bank on States

- However, the WB has many critics. The US-based Heritage Foundation examined economic growth rates in 85 countries that received IDA loans in the 1980s and 1990s, and found that:
  - Rather than helping the recipient countries, the loans pushed many into further debt, with new loans often being used to pay off old ones, the classic vicious cycle.
  - Recipient countries were more likely to experience a drop in per capita wealth than to achieve significant growth.

- Frequently, states are required to make the following changes in exchange for loan approval:
  - **Fiscal austerity**
    In the cases of Lao People's Democratic Republic, Colombia and Serbia, loan conditionality was very specific in terms of putting ceilings in place for public sector hiring. In Serbia loan conditionality called for reducing staff of the public railway and the electricity company as part of the downsizing operation for these state-owned companies. This may undermine the role of the state as the primary provider of essential goods and services, such as healthcare and education, resulting in the shortfall of such services in countries badly in need of them. In addition, this would depress employment levels when the economic situation is already dire (a negative impact on the state).

  - **Increased private sector participation**
    In Egypt, the energy sector reform agenda is centred around two axes: the oil and gas sector on the one hand and the electricity and renewable energy sector on the other. The conditions on electricity and renewables include: sector reform, better energy efficiency and tariff recovery. The loan also included a prior action supporting the

modernisation of the petroleum sector in order to make Egypt into a regional oil and gas hub. The World Bank provides advisory services to assist Egypt in the modernisation of the oil sector, which has the objective of improving the fiscal situation and attracting more foreign investment in the petroleum and gas sector. This would inevitably benefit TNCs, while prejudicing local firms (a negative impact for the state).

- **Adopt international competitive bidding for "complex, high-risk, and/or high-value contracts"**
  Public procurement is an important branch of government spending, broadly representing between 12-14% of Gross Domestic Product (GDP). This is at the highest level for low-income countries, where public procurement represents 14.4% of GDP. Procurement systems are important, as they determine how a country uses Official Development Assistance (ODA) and project loans. In addition, pro-poor procurement practices have the potential to deliver a double development dividend, through purchasing goods and services locally that deliver benefits both to the domestic private sector and to the beneficiaries of those goods and services. However, the mandatory adoption of international competitive bidding would put local firms in direct competition with powerful TNCs. More often than not, local firms lose out. This results in the loss of the double development dividend as contracts are awarded to TNCs who are able to offer higher quality/service standards or more competitive rates. The loan conditionalities that come with WB loans hence benefits TNCs while delivering a blow to a country's poverty alleviation efforts.

- It has been argued that the conditions attached to WB loans have, contrary to its aims:
  - Crippled economic growth in recipient countries,
  - Hindered development,
  - Promoted dependency, and
  - Increased poverty.

- One such critic is Naomi Klein, a columnist in *The Guardian* (27 April 2007), who wrote:

  The truth is that the bank's credibility was fatally compromised when it forced school fees on students in Ghana in exchange for a loan; when it demanded that Tanzania privatise its water system; when it made telecom privatisation a condition of aid for Hurricane Mitch; when it demanded labour "flexibility" in Sri Lanka in the aftermath of the Asian tsunami; when it pushed for eliminating food subsidies in post-invasion Iraq. Ecuadoreans care little about Wolfowitz's girlfriend; more pressing is that in 2005 the World Bank withheld a promised $100m after the country dared to spend a portion of its oil revenues on health and education. Some anti-poverty organisation.

- There are also concerns about the types of development projects funded. Many infrastructure projects financed by the World Bank have social and environmental implications for the populations in the affected areas, and criticism has centred on the ethical issues of funding such projects. For example, World Bank-funded construction of hydroelectric dams in various countries has resulted in the displacement of indigenous peoples of the area.

- Industrialised countries dominate the WB's governance structure. Decisions are made and policies implemented by leading industrialised countries—the G7—because they represent the largest donors without much consultation with poor and developing countries. Votes are made by member countries on the allocation of World Bank funds accordingly to the financial contribution of that nation to the WB ('one dollar one vote'). On this basis, industrialised countries have over 45% of voting rights, with the US having about 16.38%., while the remaining 175 countries share the rest. Typically, most of the poorest countries have less than 0.1% of the votes.

(d) Impact on TNCs

- Through its investments in the private sector in developing countries, the IFC shapes the global economy by **channelling investments to developing countries**, as well as **influencing how TNCs are run (**see **Box 7)**.

***Box 7*: IFC Invests in Pakistan's Key Fashion Retail Sector to Help Create Jobs, Support Women**

Karachi, Pakistan, May 27, 2022—IFC is investing in Pakistan's top fashion retailer to create jobs, promote gender equality, and support the country's crucial textiles sector post-pandemic.

IFC will invest the equivalent of $25 million in Pakistani rupees for a minority stake in Khaadi Corporation, which has 57 retail outlets spread across Pakistan and presence in UK and GCC countries. The funding will help the company accelerate its growth by expanding its retail footprint and online global sales. It will also indirectly support the retailer's suppliers in Pakistan, many of whom are smaller businesses.

"We are excited to begin the next chapter of our growth transformation with IFC's first investment in the Pakistan fashion retail sector. We envisage this investment will help us set new benchmarks in organizing the retail sector in Pakistan and beyond, through strategic initiatives to drive growth, corporate governance, and diversity," said Shamoon Sultan, founder and CEO of Khaadi Corporation.

IFC's investment is designed to support the development of Pakistan's retail and textiles sectors, which provide 40 percent of employment and account for about 9 percent of the country's gross domestic product. About 30 percent of those who work in the textiles sector are women and supporting the industry will help promote gender equality in Pakistan.

"The textiles and retail industry is a core part of Pakistan's economy and a major employer of women, especially in the garment sector," said Zeeshan Sheikh, IFC Country Manager for Pakistan and Afghanistan. "By channeling financing and advisory support into the industry and partnering with innovative companies like Khaadi we can help the sector grow, formalize, become more sustainable, and create greater economic employment opportunities for women."

Along with the investment, IFC will advise Khaadi Corporation on enhancing its corporate governance structures, sustainability, and gender diversification programs.

This investment is part of a broader effort by IFC to support the development of Pakistan's private sector, which is key to creating opportunities and combating poverty in the country. Since 1956, IFC has invested over $1.2 billion in Pakistan, helping to support smaller businesses and spur the development of renewable energy, hydro, and wind energy projects.

- At the same time, some have argued that the **neoliberalistic loan conditions** (trade liberalisation, privatisation and deregulation) allow transnational corporations headquartered in the developed world to capitalise on resources in untapped and unexploited economic markets (see **Box 8**).

Box 8: Singapore firm awarded urban water project in Ghana

SMEC, a unit of the Singapore-based urban planning and development group Surbana Jurong, has been selected as the contract manager and supervisor of a major project aimed at enhancing water delivery in the Ghanian capital Accra. Surbana Jurong is part of Jurong International Holding, Singapore's leading international consultancy service provider, with a special emphasis on industrial developments.

Over half of Ghana's water produced is lost before it reaches consumers, leading to significant financial losses for the state-operated Ghana Water Company Ltd. (GWCL). In response, GWCL is aiming to reduce non-revenue water – water that, although distributed, fails to generate revenue, predominantly due to leaks, inaccurate metering, and unauthorised consumption.

The Accra East Water Loss Reduction project aims to lower non-revenue water to 25% through performance-based contracts. Under these contracts, payments, and incentives for the service provider hinge directly on achieving specific outcomes, like tangible reductions in water losses. SMEC will assist GWCL with the performance-based contract procurement, and then act as the client representative, overseeing the contractor's performance throughout each phase of the project.

The project is sponsored by the Ghana Ministry of Sanitation and Water Resources, which has recently secured additional financing from the International Development Association, part of the World Bank Group. This funding is part of the Greater Accra Metropolitan Area Sanitation and Water Project.

The involvement of TNCs in Ghana's water industry is not new. In 2011, the World Bank, through its private sector arm, the International Financial Corporation, invested in WaterHeath International (WHI). WHI's business model involves constructing small micro-utilities that disinfect local water and sell it to the rural and semi-urban poor in developing countries. Communities are loaned start up costs, and revenue from selling the water is used to pay this back and cover operating costs, with communities eventually taking ownership of the facility. The extent to which this model is driven by massive water-using corporations should not be underestimated. WHI boasts of corporate partnerships with the Coca-Cola Company and UK drinks giant Diageo. WHI's scheme in Ghana was initiated by NGO the Safe Water Network, of whom Pepsi Co is a major funder. WHI was perceived as an "excuse" to introduce "market solutions" as the "miracle solution" for the water crisis in developing countries.

There was a concern that after handing over to the community, the infrastructure's maintenance needs would vastly increase. Usually the amount required for repairs and maintenance is larger than the revenue generated from the system. Communities at this stage will be at the mercy of market forces who will exploit their misery. The danger of such a move is to open the floodgates for greedy speculators to begin the race of exploiting unserved rural and urban populations. In addition, these stand-alone initiatives end up increasing the costs to governmental departments, who are called upon to rectify the defects when the project sponsors have left.

15.5 Conclusion

- In this lecture, we learnt that multilateral institutions represent an upscaling of economic governance by states. This provides a new angle on the influence that states have in shaping the global economy.
- We have also learnt that while multilateral institutions can **directly** and **indirectly** influence TNCs.
    - Some multilateral institutions may invest in TNCs to achieve their mission,
    - By striving hard to establish its own set of rules in reducing barriers in order to promote free trade and investment environment at various scales, multilateral institutions can indirectly influence the locational decisions of TNCs.
- At the same time, some challenges exist and awaits the institutions as they work towards sustainable development in the global economy.
- Despite the challenges, the rise of multilateral institutions since the 1950s has meant that they have become influential actors, alongside states and TNCs, in shaping the global economy.