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27

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GLOBALIZATION AND GLOBAL GOVERNANCE IN THE 21ST CENTURY

Project on:
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Globalization and Global Governance in the 21st Century

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Introduction

An examination of international economic relations in the six decades since World War II reveals many ways in which political factors have shaped economic outcomes. The postwar security system significantly affected the postwar economic system. The creation of a bipolar security system following the outbreak of the Cold War led to the separation of the Eastern and Western economic systems and provided a basis for the dominant role of the United States in the Western system and of the Soviet Union in the Eastern system. The end of the Cold War led in turn to the end of the East-West economic divide and to the integration of the formerly Communist countries and China into the global capitalist economy.

Domestic policymaking had a major impact on the course of international economic relations. Political concerns often outweighed economic considerations in economic policymaking. The Marshall Plan, for example, was a security policy more than it was an economic recovery program. Aid to the developing world was motivated primarily by Cold War concerns. Similarly, aid by the West to the formerly Communist countries after the end of the Cold War was motivated primarily by security concerns, such as the desire to prevent nuclear proliferation and to make a return to communism as unattractive as possible.

In addition, monetary, trade, and investment policy debates have been influenced by the mobilization of interest groups. For example, organized labor and environmental groups opposed the ratification of the North American Free Trade Agreement in 1993, despite strong support from U.S. manufacturing interests and the Executive Branch of the government, because they thought the agreement would create downward pressure on wages and environmental standards in the United States. The same groups opposed further globalization of the world economy in the late 1990s. In formerly communist countries, some government officials and the managers of state enterprises organized politically to oppose economic reforms, while others supported them. Private business interests organized effectively to influence electoral outcomes in the fledgling democracies of Russia and Eastern Europe.

Finally and most importantly, international economic relations have become a political arena where both governments and non-state actors (like multinational corporations and transnational environmental groups) try to manage conflict and seek cooperative outcomes. These actors are searching for new ways to govern the global economy. As the world economy becomes more globalized, multinational corporations and nongovernmental organizations (NGOs) are increasingly playing a role in both domestic and international politics. Economic globalization has raised the issue of global governance and with it the question of how to make global governance as democratic as possible. Thus, economic globalization has led to an internationalization of domestic politics.

The evolution of international economic governance

It is possible to divide the post-WW2 decades into three major periods: 1) the system of political control established immediately after World War II and lasting until just before the energy crises of the 1970s, or the **Bretton Woods** period (1945-1971), 2) the age of **interdependence** (1971-1989) and 3) the era of **globalization** (1989 to the present). With respect to three major issue-areas—money, trade, and investment—and in three particular subsystems—North-North, North-South, East-West—it is possible to observe important changes that have occurred over the three periods. The South is an increasingly diversified group with a major divide between the fast-growing and slow-growing countries. Since the breakup of the Soviet Union and the economic reforms in China, the East-West system is no longer defined by a global ideological struggle between capitalism and communism. Instead, capitalism is everywhere. In this paper, we will look to the future of the system as a whole to suggest some answers to the question of how it might be possible to deal with the key problem of our time: the governance of globalization.

The international regimes governing monetary affairs, trade, and investment flows evolved quite differently. Their development over time reflected the distinctive challenges of the three periods in the three different subsystems (see Table 1). After World War II, most international economic regimes were created by the United States acting either alone or jointly with Britain with the consent of the other industrialized capitalist countries. The U.S. and British governments focused on money and trade after World War II because of their shared belief that instability in monetary affairs and protectionism had played a critical role in the rise of the dictatorships after World War I. The leaders of the United States and the United Kingdom believed that a fixed currency exchange-rate regime backed by gold and a liberal trading order were the best guarantees against both fascism and communism. The exchange rate regime they established after 1945 grew weaker over time while the trade regime grew stronger. Fixed exchange rates proved unsustainable and were replaced with floating rates in 1973. The original GATT system expanded through trade liberalization and new rule making and was eventually replaced with the more ambitious WTO in 1995. No formal regime governed investment flows during the three periods. Trade-related investment measures were added to the WTO in 1995 (see Table 2) but the attempt to establish a Multilateral Agreement on Investment failed in 1998. In all three areas, there was movement away from management by the hegemonic power (the United States) toward genuine multilateral governance. However, the legitimacy of that evolution was increasingly challenged by anti-globalization forces.

Table 1. Characteristics of Management and Governance in the Three Subsystems

Subsystem	**Bretton Woods (1945-1971)**	**Interdependence (1971-1989)**	**Globalization (1989 to present)**
North-North	-U.S. hegemony, Europe and Japan recover from WW2 -Creation of multilateral institutions and rules: IMF, World Bank, GATT -Numerous barriers to international economic flows gradually reduced: currency convertibility, tariff reductions	-Relative decline of the U.S., rise of Europe and Japan -Evolution of international economic regimes: IMF reform, Group of Ten, economic summits, trade rounds -Liberalization of trade and finance, economic growth -Rising international economic flows	-U.S. dominance restored, formation of EMU, Japanese economic recession -Evolution of international economic regimes: creation of WTO -Liberalization domestically and internationally -Rapidly increasing international economic flows
North-South	-End of colonialism -Superpower competition for influence in the Third World -Southern underdevelopment and dependence on the developed market economies -Isolation from the international economic institutions, import substitution strategies	-Efforts to unite and confront the North to achieve greater equity, OPEC model -Rapid growth of Newly Industrializing Countries, flows of trade, investment, capital to NICs -Continuing stagnation of Fourth World	-Spread of policies of deregulation, liberalization, privatization -Greater integration into global economy: investment and financial flows, trade -Instability arising from volatile capital flows, inadequate domestic policies and regulations -Rise of China and India -Continuing stagnation of Fourth World
East-West	-Creation of separate international economic systems for East and West -State-led domestic and international economies	-Limited reconnection with the West via Ostpolitik, détente, and Chinese economic reforms -Limits on economic growth inherent in	-End of the Cold War, Breakup of the Soviet Union -Russia joins the G-7 -In Russia and

	-Recovery from WW2 and growth	central planning	Eastern Europe: Transition from communism to capitalism and from autocracy to democracy -In China: successful economic reforms but continued political dominance of the Communist Party

Source: Joan Edelman Spero and Jeffrey A. Hart, *The Politics of International Economic Relations*, 7th edition (Boston: Wadsworth, 2009), Chapters 2-10.

Table 2. Summary of Regime Changes in the Three Periods in Monetary Affairs, Trade, and Investment Flows

Regime	**Bretton Woods (1945-1971)**	**Interdependence (1971-1989)**	**Globalization (1989 to present)**
Monetary Affairs	-Dominant role of dollar -Exchange rates fixed relative to the dollar with adjustable pegs -Movement to currency convertibility -Periodic currency crises and stress on fixed exchange rates -IMF and United States are managers of fixed exchange rate regime	-Floating exchange rates with central bank interventions -Efforts to fix exchange rates among Europeans -Increased volatility with rising international financial flows: petrodollar recycling, Third World Debt crises -IMF increased involvement in developing countries	-Financial flows increase worldwide and major financial crises become global -Creation of EU and rise of the Euro -IMF and World Bank become crisis managers
Trade	-Gradual reductions in tariffs among developed market economies through GATT negotiating rounds -Many areas excluded from	-Tokyo Round: major reductions in tariffs and increases in non-tariff barriers - Increased conflict over North-North trade	-Uruguay Round: expansion of regime to cover services, investment, and intellectual property; creation of the WTO and extension of the trade regime's scope

	GATT: defense, agriculture, services		and authority - Formerly communist countries and China join the WTO -Doha Round not completed
Investment Flows	-No regime other than preexisting international laws governing foreign investments	-Latin American and OPEC nationalizations and other challenges to MNCs	-MNCs increasingly accepted as developed, developing, and formerly communist countries seek inflows of foreign investment direct investment -TRIMs added to WTO -Failure of the MAI

Source: same as Table 1.

Despite the uneven institutionalization of international economic regimes, the world economy grew rapidly as money, goods, and services flowed more easily across national boundaries.[1] Trade grew faster than GDP and FDI grew faster than trade, but the volume of financial flows and currency transactions grew faster than both of them, especially during the third period.

Increasing international economic interaction was driven, in part, by technological change. Transportation and communication costs declined dramatically after World War II. The combination of new computing and telecommunications technologies decreased the cost, increased the speed, and altered the possibilities of international economic production and exchange.[2] New transportation technologies increased the volume and speed of trade and the

[1] Robert O. Keohane and Joseph S. Nye, “Introduction,” in Joseph S. Nye and John D. Donahue, eds., *Governance in a Globalizing World* (Washington, D.C.: Brookings Institution Press, 2000.

[2] Jeffry A. Frieden and Ronald Rogowski, “The Impact of the International Economy on National Policies,” in Robert O. Keohane and Helen V. Milner, eds., *Internationalization and Domestic Politics* (New York: Cambridge University Press, 1996), 30.

movement of people. Average ocean freight and port charges fell from $95 per short ton of U.S. import and export cargo in 1920 to less than $20 in 2000. Small, lightweight products were increasingly shipped via wide-body jet aircraft at rates that were highly competitive with ocean freight prices. The cost of a three-minute telephone call from New York to London fell from $317 in 1930 to $.30 in 1996 (in constant 1990 dollars). Satellite television and later the Internet and the World Wide Web made the communication of text, audio, and video images about world events instantaneous. The reduction in communication and transportation costs enhanced the ability and willingness of actors to cooperate across national boundaries.[3]

Political choices also drove growing international economic interaction. The creation of the Bretton Woods regime was a critical political decision. At the time of the establishment of the Bretton Woods system**,** trade barriers, investment restrictions, and capital controls separated the industrialized economies. The common goal of the founders of Bretton Woods was to promote economic prosperity and political stability by reducing barriers to trade and financial flows through institutions, rules, and processes of liberalization. This liberalization combined with national policies of domestic compensation via the welfare state, deregulation, and privatization eventually led to greater openness to trade, financial flows, and direct investment in the world economy.[4] By the beginning of the twenty-first century, the industrialized nations were linked by a "dense network" of international flows of goods,

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[3] Taken from a presentation on globalization prepared by the staff of the World Bank. See also Matthias Busse, "Tariffs, Transport Costs, and the WTO Doha Round: The Case of Developing Countries," *The Estey Center Journal of International Law and Trade* Policy 4 (Winter 2003): 15-31; Jeffrey Frankel, "Globalization of the Economy," in Keohane and Milner, eds., *Internationalization and Domestic Politics*; and Jonathan Aronson, "Global Networks and Their Impact," in James N. Rosenau and J.P. Singh, eds., *Information Technologies and Global Politics: The Changing Scope of Power and Governance* (Albany, N.Y.: SUNY Press, 2002).

[4] John G. Ruggie, "International Regimes, Transactions, and Change: Embedded Liberalism in the Postwar Economic Order," *International Organization* 36 (Spring 1982): 379-415.

services, capital, information, ideas, and people known as globalization.[5]

Developing countries made different political choices. In the period after World War II, the developing countries found themselves in dependent relationships with the powerful, developed North. Many Southern states chose not to participate in the Bretton Woods system and pursued economic development through import-substituting industrialization policies. In the 1970s, they sought to improve their bargaining position and to gain economic benefits by uniting and using their control of raw materials such as oil. By the 1980s and 1990s, many developing countries found that isolationism and confrontation were a dead end and shifted their strategies toward deregulation, privatization, and international liberalization. They sought to benefit from integration into the global economy by increasing their share of growing trade, foreign investment, and other international capital flows. Large and faster growing developing countries such as Mexico, Brazil, China, India, Taiwan and South Korea became important regional players who also sought a seat at the table of global decision-making.

Political decisions also shaped the interaction of the USSR, China, and the communist states of Eastern Europe with the world economy. After World War II, with the onset of the Cold War, the East isolated itself from the Western international economic system by establishing state-managed economies and creating a separate, independent international economic system. Politically motivated barriers created by Western states accentuated their isolation. At the end of the twentieth century, interaction between East and West increased significantly when the communist regimes in the USSR and Eastern Europe collapsed, China and Vietnam adopted market-oriented economic policies, and the West eliminated its economic sanctions. Integration of the formerly communist countries into the international

[5] Robert Keohane and Joseph Nye, "Introduction."

economic system became a key political challenge for the West. Its efforts in Eastern Europe and Russia focused on supporting the consolidation of their new democratic systems. In China, which had successfully integrated itself into the world economy without abandoning authoritarianism and communism, the challenge was figuring out how to accommodate growing Chinese economic power while encouraging and supporting political liberalization.

Challenges for Global Governance

Globalization has significantly altered the conditions for achieving cooperation and managing conflict in international economic relations. It has changed the nature of the state, the major player in international relations. National sovereignty, national decision making, and national boundaries have not disappeared and states remain the principal actors in international economic relations. However, states are increasingly open and subject to external influences. For example, the Mexican peso and Asian crises reverberated around the globe, disrupting national financial markets and national economies in both developed and developing countries. The slowing of growth in the United States in 2001 profoundly affected economic performance in Asia, Europe, and the Americas. The financial crisis in the United States in 2008 quickly spread to other nations before it could be contained. As a result, states are restructuring to reduce their vulnerability to international economic changes and to adapt quickly to those changes to which they remain exposed.[6]

Another challenge centers on the continuing need for leadership within the system. Throughout the second half of the twentieth century, the United States acted in concert with other developed market economies to lead the global economic system. In the twentieth

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[6] Jeffrey A. Hart and Aseem Prakash, "Globalization, Governance, and Strategic Trade and Investment Policies," in Aseem Prakash and Jeffrey A. Hart, eds., *Globalization and Governance* (New York: Routledge, 1999).

century, the United States was the principal beneficiary of globalization and emerged as the world's superpower both after World War II and after 1989. United States leadership in the 21st century was still essential but also problematic.

Part of the problem with U.S. leadership lay in resistance to globalization. Debate and conflict over globalization and the U.S. role in international economic management intensified at the dawn of the twenty-first century. American advocates of globalization, much like policy makers at Bretton Woods, pointed to the economic and political benefits of greater trade and financial flows and supported the continued liberalization of national economies and the removal of barriers to international economic flows. Recognizing that globalization undermined the ability of national governments to manage their economies, these advocates supported the creation of multilateral regimes to govern global economic interaction.[7]

American critics of globalization included labor unions fearing the loss of jobs to foreign competition, environmentalists concerned that globalization would undermine national environmental laws and policies, and isolationists and neo-imperialists who opposed foreign influence and multilateral decision making. Critics on the left pointed to the instabilities and inequities of globalization. Much like the structuralists and Marxists of an earlier era, they argued that international trade, investment and finance favored the developed countries and harmed developing countries who suffered from financial crises and from the harsh policies of international financial institutions, especially the IMF. Critics on the right focused on the impact of globalization on national sovereignty and independence. They wanted to erect new barriers to trade, capital, and labor flows, claiming that existing flows

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[7] See, for example, Jagdish Bhagwati, *Free Trade Today* (Princeton, N.J.: Princeton University Press, 2002); Sylvia Ostry, "Convergence and sovereignty: policy scope for compromise?", in Aseem Prakash and Jeffrey A. Hart (eds.), *Coping with Globalization*, (New York, NY, 2000); and Douglas Irwin, *Free Trade Under Fire* (Princeton, N.J.: Princeton University Press, 2002).

threatened national security. Opponents of globalization on both the left and the right mobilized politically against U.S. leadership in liberalizing the international economy and expanding multilateral economic institutions and rules.[8]

In Europe and Japan, traditional allies in strengthening international economic governance, the debate over globalization mirrored that in the United States and was reinforced by the fear that globalization was a vehicle for U.S. dominance. European, Latin American, African, and Asian governments formed regional economic regimes, which also played a role in global governance. Some of those regional organizations, especially the European Union and Mercosur, were formed in part to offset U.S. predominance and enhance the role of their member-states in international economic decision-making.

Furthermore, states were no longer the only actors in international economic relations. A variety of non-state players that worked across national boundaries emerged. Besides MNCs, labor unions, NGOs, and other nongovernmental transnational actors played a growing role in global governance. These actors argued that they were similar to interest groups in domestic polities by asserting their independence from governments and their ability better to represent the interests of citizens in specific policy areas. Unlike domestic interest groups, however, they attempted to influence decision making at both the domestic and international levels. They sought to reform international regimes to make them more responsive to non-governmental actors. To do this effectively, they had to communicate and coordinate policies transnationally and to form alliances with other non-governmental actors.[9]

[8] Kevin Philips, *Bad Money: Reckless Finance, Failed Politics, and the Global Crisis of American Capitalism* (New York: Viking, 2008); Evan Osborne, *The Rise of the Anti-Corporate Movement: Corporations and the People Who Hate Them* (Westport, Conn.: Praeger, 2007); Sidney Tarrow, *The New Transnational Activism* (New York: Cambridge University Press, 2005); and Dani Rodrik, *Has Globalization Gone Too Far?* (Washington, D.C.: Institute for International Economics, 1997).

[9] See Ann Florini, *The Coming Democracy: New Rules for Running a New World* (Washington, D.C.: Brookings Institution, 2005); and Ann Florini, *The Third Force: The Rise of Transnational Civil Society* (Washington, D.C.: Carnegie Endowment for International Peace, 2000).

While national political systems have devised a wide variety of ways to provide access for domestic interest groups, international institutions have been largely closed to such groups. Decision processes of most international economic institutions are based on the idea of **intergovernmentalism**, participation by government officials only, and are not always transparent. Thus, another challenge for global governance was whether and how to provide access for non-state actors. In the long term, the ability of the system to provide the right amount of access and transparency would be critical to enhancing the legitimacy and effectiveness of the global governance.[10]

Because of globalization, there was also a need to manage interaction in many arenas that traditionally had been in the purview of states and that were deeply imbedded in national policies and practices. A level playing field in international trade was shaped by national competition policies. The stability of the international financial system had become dependent on the safety and soundness of national financial systems. The effective transition from communism to capitalism in Russia and Eastern Europe was an international as well as a national concern.

In addition, social goals were becoming linked to global governance. Environmentalists wanted the WTO to incorporate rules to protect the environment while also promoting the liberalization of trade. The NAFTA agreement included separate codicils on labor standards and environmental protection. The G-8 considered methods to deal with the global problems created by the AIDS pandemic, including the problem of getting expensive AIDS medicines to low-income individuals at reasonable prices while maintaining incentives for drug companies to develop new treatments and possible cures. Policies designed to deal with the threat of climate change were discussed in the United Nations, the G-8, and other

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[10] Keohane and Nye, “Introduction.”

global forums.

These linkages between the global economy and traditionally national areas of decision-making led to significant tension between state and international decision-making. The WTO, for example, found in several rulings that national social policies designed to control use of alcohol or gambling violated international trade agreements. Similarly, as financial markets grew exponentially in the era of globalization, national bank supervisory and regulatory structures became increasingly inadequate to assure safety and soundness of the global markets. However, national authorities were not ready or able to create a global financial regulatory structure. The challenge was to develop an economic order that preserved the sovereignty of nation-states while also addressing the need for global governance.

Characteristics of a new system of governance

The future order will continue to rely on political management by a core of powerful, developed countries. The developed economies and especially the “big five”—the United States, Japan, Germany, France, and the United Kingdom—will remain key actors in the system. The size and vitality of their economies will ensure their continuing leadership. Their growing interdependence will be a force for cooperation. Nevertheless, power relationships among the big five and between them and the rest of the world are changing, thus affecting governance arrangements.

Japan, as the second largest developed market economy after the United States, has sought over time to play a more important role. Japan has already staked out a greater role in a wide variety of global economic regimes, including the World Bank and the IMF. Japan is one of the leading users of the dispute settlement machinery of the WTO.[11] The Japanese played a key role in pushing for the Doha Development Round. The ability of Japan to restructure and revitalize its economy will shape its ability to increase its influence. At the same time, the big three countries of Western Europe—France, Germany, and the United Kingdom—continue to enhance their global economic power primarily through European integration and expansion of the EU. The ability of the EU to achieve its goal of a common economic system with a free flow of goods, services, money, and people will shape the role of its member states in the new systems of global governance.

Governance institutions will have to be broadened in some cases and some areas to reflect the rise of new centers of power. In particular, China's new economic power will have to be taken into account in overall governance mechanisms including the economic summits. As a major factor in international trade as well as a financial power due to its large financial surpluses, China must increasingly take on responsibility in its domestic and international economic policies for the entire system.

Members of OPEC and other major oil and natural gas exporters such as Russia, for example, will continue to have a major say regarding energy issues. In the area of trade and foreign investment, the fast-growing developing countries will play a greater role. Brazil, China, India, Mexico, and South Korea, whose trade and investment flows are of great importance to the world economy will be in a position to demand and receive greater access to global governance institutions. Their views will have to be taken into account especially in future negotiations about the trade and investment regimes.

Whereas the governments of some developing countries will be involved to a greater extent than they are now in global governance, the role of other governments in the South is

[11] Saadia Pekkanen, *Japan's Aggressive Legalism: Law and Foreign Trade Politics beyond the WTO* (Stanford: Stanford University Press, 2008).

unlikely to change. The poorer and slower growing developing countries are not likely to play a significant role in global governance institutions beyond the United Nations system, but they can expect to receive greater attention from the powers that be in the years to come. The Fourth World will be helped by allies in the South and by non-governmental organizations in the North who have mobilized against the inequities of the international economic system. The rich countries of the North are paying more attention to the Fourth World because they see that as part of a necessary response to the challenges posed by global terrorism, the AIDS pandemic, and global warming.

Finally, the new system of governance will need to continue to promote the economic and political restructuring of Russia and Eastern Europe to integrate these countries into the system of global governance. Russia has joined the IMF, the World Bank, and the economic summits, and should eventually become a member of the WTO. Eastern European countries have been brought into the system through the EU, the OECD, the WTO, World Bank, and IMF as well as through membership in NATO.

Among the powerful core, there remains a recognized cluster of common interests. Despite conflicts raised by economic change and in particular by globalization, the developed market economies continued to support a liberal, capitalist global economy. The postwar experience reinforced their belief in the need to cooperate to achieve a stable and prosperous economic system. The persistence of the shared goal of cooperation was demonstrated by the behavior of the industrialized nations during the crises of the 1990s as well as the successful conclusion of the Uruguay Round and the formation of the World Trade Organization. In the early 21st century, the ability of the powerful core to continue to support a liberal, capitalist global economy will be tested again, particularly by the new challenges of trade (completing the Doha Round) and finance (addressing the global financial crisis of 2008).

There were signs that the second tier of states—some members of OPEC, the Asian tigers, and the BRICs, among others—shared at least some of the norms of cooperation currently held by the industrialized countries. Adoption by many developing countries of more pragmatic policies toward trade and foreign investment in the 1980s and beyond represented significant movement toward greater global consensus. The Asian tigers and the BRICs were more receptive to supporting effective global economic governance than the rest of the South because they had a greater stake in the system. They sought to preserve liberal trade and investment regimes because these regimes were vital to the continued success of their export-led development strategies.

Still, it seems quite likely that North-South tensions will persist. Despite the growing differentiation between the more-advanced and the least-developed countries, the wealthier Southern states continue to support greater emphasis on poverty alleviation and the reduction of global inequality. They now have important political allies in the form of NGOs based in the developed world. Although the industrial core does not reject the Millennium Development Goals, they are still not seen as a primary goal of global economic governance or as a responsibility of the developed market economies. Even though the NGOs and the South have succeeded in putting reducing global poverty and inequity on the agenda and the developed countries are willing to support some aid programs (especially in the case of humanitarian emergencies), the North so far has been unwilling to alter noticeably the established system's operation in the direction of redistribution.

Furthermore, many northern critics have questioned whether equity, as demanded by the less-developed countries, is a legitimate goal. Some charge that redistribution as now conceived will benefit only a few or only a small stratum of the population of the less-developed countries and not the poorest in the poor countries. Without extensive internal political, social, and economic reform in the less-developed countries, international efforts at redistribution and development will be useless, according to many in both the North and the South. Conflict over equity and redistribution therefore is likely to continue to be a political dynamic in the new international system.

Finally, the new international economic regime will be a system of multilateral governance. In the past, a single leader to a great extent carried out the management of conflict and cooperation. In the nineteenth century, Great Britain was this leader, and in the postwar era, the United States took the part. The more even distribution of power in the future, however, will require the active participation of a coalition of powerful states—that is, it will require collective governance.

Collective governance is difficult. Throughout history, agreement among sovereign powers in the absence of world government has proved to be a difficult and often an impossible task. Several factors, however, enhance the possible success of collective governance. The basic consensus among the powerful will be an important factor; so, too, will be the experience in cooperation since World War II. Collective governance will be facilitated by a variety of formal and informal methods developed over the last four decades. A relatively sophisticated and complex structure of cooperative mechanisms has unfolded in the postwar era, and experience in using these mechanisms has grown. Yet, as evidenced by the financial and economic crisis of 2008, those mechanisms may prove inadequate to the demands of a global economy.

Even within a collective governance system, however, leadership will be important. Existing institutions are insufficiently developed to govern the system without supplementary action on the part of leading nation-states. Most often, that leadership will have to come from the United States. Unless and until the European Union becomes politically unified, and the

EU or Japan assumes a more assertive posture in world affairs, the United States, by the very size of its economy, will continue to be the most important single international economic actor. Although the United States will be unable to govern the system by itself, management and reform will be impossible without U.S. approval, and U.S. initiatives and support for reforming global governance will be crucial to success.

Because of the political setting and the nature of the task, the process of international economic reform will be piecemeal and evolutionary. Reform will result, in part, from international negotiations such as multilateral trade negotiations. It will arise from the evolution by negotiation of international institutions such as the International Monetary Fund, the World Bank, and the World Trade Organization. Reform will also grow out of common law, the establishment of rules and procedures through trial and error and through ad hoc responses to problems and crises. International monetary management through consultations among central bankers and finance ministers of the G-7 will most likely evolve through such a process. Reform will come not only from such international agreement and managed change but also from sporadic crises. It was the currency crises of the 1960s and 1970s, not international agreement, that led to the floating exchange rate system. The debt crises in Venezuela and Mexico led to a new approach to the debt problem; the Mexican peso crisis of 1994–1995, the Asian financial crisis of 1997-1998, and the Russian crisis of 1998 led to IMF reform. In the absence of agreed-upon rules, structures, and processes, such disturbances may multiply.

Finally, there is no assurance that multilateral cooperation among the major industrialized countries will continue or that it will be successful. The evolutionary process of reform is in many ways precarious, for it relies on mutual restraint and cooperation by the major powers until reform is achieved. Without agreed-upon rules, institutions, and procedures, a major economic shock could undermine cooperation and lead to economic warfare, as occurred in the 1930s. Without strong multilateral institutions such as the G-8, the WTO, the IMF, and the World Bank, the world could gradually evolve into a series of economic blocs: a Western hemisphere block centered on the United States, Canada, and Mexico; a European-African block based on the EU; and a Pacific block built around Japan. If the multilateral system is weakened, regional management could become a hedge against the possibility of a breakdown in global multilateralism. Nevertheless, recent experience suggests that the will and ability to find mutual solutions persists and that cooperation among the powerful will continue.

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